# Cryptocurrencies: The Volatility Continues

## Description

This past week, the price of Bitcoin, often used as the benchmark for the broader cryptocurrency market, slumped significantly amid concerns that large investors holding significant amount of digital currency (often referred to as “whales”) had begun liquidating positions. It is widely known that a small percentage of Bitcoin owners hold the vast majority of the outstanding float of the digital coins, leading many to believe that the recent sale of US$400 million worth of Bitcoin by the bankruptcy trustee for Mt. Gox is only the beginning of what is to come among whales holding in excess of US$1 billion worth of Bitcoin.



Regulatory scrutiny in countries such as Japan and the U.S. has also heightened worries that trading may become more difficult, and demand may be hampered by regulatory oversight in a “dark” sector which is often looked to for grey or black market activities. Concerns about such activities from regulators has led to a significant amount of bearish talk in countries such as South Korea and Japan, two of the largest markets for cryptocurrencies overall.

I would like to quote specific wording from a report issued by Mark Carney (current governor of the Bank of England), which was highlighted in a recent piece from fellow fool contributor Jason Phillips; Mr. Carney spoke of some of the risks related to Bitcoin and cryptocurrencies, highlighting some of the high-level concerns central banks are beginning to have with this sector:

Mr. Carney spoke of “paradigm justifications, broadening retail enthusiasm, and extrapolative price expectations” as key driving factors underpinning the rise in prices related to cryptocurrencies, leading to bubble-like environment. I tend to agree and would caution investors to be extremely careful with putting any money toward this sector currently.

On Sunday, the price of a single Bitcoin rallied in the double-digit range intra-day, as investors continued to weigh the risk/reward relationship for this novel sector. With prices bouncing up and down regularly in the double-digit range on a daily basis, attempting to time this market appears to be a very difficult thing for speculators to do.

For investors looking for out-of-this-world returns in a short amount of time, such is the reality when investing in highly speculative instruments such as cryptocurrencies. Volatility, which leads to the sharp short-term price increases in cryptocurrencies, carries with it a downside; volatility can be an investor's worse enemy when the need for fiat currency outweighs the potential gain from an investment (i.e., a bear market).

While some pundits believe that cryptocurrencies act as a hedge against a bear market (akin to commodities such as gold), I would argue the exact opposite. I believe it is the availability of cheap liquidity with few places to flow to gain a decent return which has resulted in some investors wading into the waters of "investing" in "assets" such as Bitcoin or other cryptocurrencies.

My thesis is that when the time comes for investors to cash out (either voluntarily or involuntarily via a market correction or bear market), the downward momentum that will drag the value of such speculative instruments down will do so in a violent and unforgiving way.

To truly add some alternative investments to your portfolio, which should act as buffers to equity markets in the event of a downturn, I suggest investors look at defensive strategies, such as acquiring stakes in time-tested alternative investments such as real estate investment trusts, like **Killam Apartment REIT** (TSX:KMP.UN), bonds, or in commodities — asset classes that are less correlated to broader equity markets.

Stay Foolish, my friends.



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