Should Bitcoin Really Be Part of Your Retirement Portfolio?

Description

Bitcoin's incredible 95% bull run year to date captured the attention of investors across the world. Since its inception in January 2009, the dominant cryptocurrency has returned an astonishing 16,646%. However, this rally has been accompanied by gut-wrenching volatility. Intraday drops of 5% or more are common, and multi-year bear markets with losses of up to 80% can shake even the most risk-tolerant of investors.

Despite this, the evidence so far has shown that the investors who "HODL" Bitcoin for a sufficient length of time to ride out the volatility almost always enjoy juicy returns. With a long time horizon and good appetite for risk, Bitcoin (and other cryptocurrencies) could be an excellent addition to your retirement portfolio.

Diversifying your portfolio

According to a study by Yale University economist Aleh Tsyvinski, portfolios should have anywhere from a 4% to 6% Bitcoin allocation for diversification purposes. Because Bitcoin (and other cryptocurrencies) are an entirely different asset class compared to stocks, bonds, commodities, and gold, allocating part of your portfolio to it can actually reduce risk.

By adding Bitcoin, we limit our exposure to any single asset and its risk. For example, as the U.S. dollar and stock market drop, Bitcoin tends to gain in value, which can help your portfolio mitigate this loss. A 4-6% allocation to Bitcoin will not make your portfolio that much more volatile but could, in fact, offset risks from other assets you hold.

Boosting portfolio returns

Bitcoin has been one of the best-performing assets of the 21st century, handily beating most indexes, actively managed funds, and even leveraged assets on a risk-adjusted basis over the long term. Despite its higher volatility, investors who hold it for the long term over a period of several yearswithout selling enjoy greater returns and gains.

We can look at how Bitcoin did compared to traditional stock market indexes during the bull run of the last five years, where stocks benefited greatly. Whereas the tech-heavy **NASDAQ 100** returned 235%, Bitcoin returned 7,066% during that same period. However, keep in mind that this outperformance is only attainable if you have an iron risk tolerance and can avoid panic selling during periods of high volatility.

Getting exposure in your retirement account

Holding Bitcoin in a Tax-Free Savings Account (TFSA) or Registered Retirement Savings Plan (RRSP) is now possible thanks to the creation of Bitcoin exchange-traded funds (ETFs) by fund managers such as **Purpose Investments, Evolve ETFs**, and **CI Global Asset Management**. These ETF providers buy Bitcoin and put it in a “basket” of sorts. When you buy shares of the ETF, you receive “slices” of this basket, which holds a portion of the underlying Bitcoin.

The price of the ETF is dependent on the movement of Bitcoin and will track it closely minus fees, expenses, and currency fluctuations. However, keep in mind that although Bitcoin trades 24/7 and on weekends, the ETF only trades during regular exchange hours. Hence, large after-hour price movements may not be reflected until the next trading day, and you will not be able to buy or sell after hours.

The Foolish takeaway

Canadian investors should strongly consider diversifying their portfolio with a small allocation in Bitcoin. You can do so in a TFSA or RRSP via various Bitcoin ETFs. Doing so may increase your portfolio returns over the long run. However, it is important that you fully research how Bitcoin works, its fundamentals, and what the future outlook is. Bitcoin can be highly volatile, and thus, investors looking to incorporate it into their portfolios should assess their risk tolerance accordingly.

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