



## The Nature of Bitcoin: Can It Be Money, an Asset, or neither?

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### Introduction

In January of 2021, the world witnessed a boom in the cryptocurrency markets. Blockchain and distributed-ledger technology were the hot topics of the financial markets with Bitcoin (BTC), the first and most widely used cryptocurrency in the world, taking center stage. In fact, has been said that Bitcoin has the potential to serve as “digital gold,” with some institutions like J.P. Morgan believing Bitcoin could reach even higher, rivaling the market value of the precious metal gold itself.<sup>i</sup> That said, Bitcoin still has a long way to go if it is to be adopted on such a scale. In this article, we will discuss the nature of bitcoin, and whether it can serve as a digital form of gold, an asset, or even of money itself.

### The Essence of Bitcoin

Perhaps the greatest driver of Bitcoin’s initial boom was the idea that this digital token was going to change the world forever. Bitcoin was created through the utilization of distributed-ledger technology, a newfound tool capable of maintaining an official database without the need of a centralized authority. In other words, the creation of Bitcoin made decentralized transactions possible in the modern world. This idea was spread by Bitcoin’s original supporters as not only an alternative medium of exchange, but as an alternative to money itself. Knowing this, it begs the question of whether or not Bitcoin could, with the help of blockchain technology, **be the next form of money?**



- Although Bitcoin is often depicted as a physical coin like the one shown above, there is no tangible form of Bitcoin in circulation.<sup>ii</sup>

### The Nature of Money

If we are to determine Bitcoin’s likelihood of becoming the next form of money, we must first understand the nature of money itself. By definition, money must meet three distinct requirements:<sup>iii</sup>

1. Money must be **liquid** and easily transferred between parties.
2. Money must be **uniform**, meaning that each unit of money has the same worth as the next, and thus can serve as a **unit of account** for business affairs.
3. Money must serve as a consistent **store of value**.

By recognizing the essential properties of money, we can better understand where Bitcoin stands in becoming future money.

## Uniform and Liquid

It can be fairly stated that Bitcoin, by its nature, is a **highly liquid asset** due to its electronic presence in the global market. As of the 3<sup>rd</sup> Quarter of 2020, it is estimated that over 350,000 Bitcoin transactions are conducted on a daily basis worldwide.<sup>iv</sup> Unlike credit and debit card transactions (which have similar electronic properties), purchases and transfers of Bitcoin are virtually untraceable by government regulators.

It can also be said that Bitcoin can serve as a **unit of account**, meaning that individuals and businesses can easily understand how much Bitcoin (or what fraction of a Bitcoin) they have whenever necessary. In addition, two equivalent units of Bitcoin are confirmed to have identical value relative to the U.S. Dollar or other world currencies at any given time. However, the value each unit or fraction of Bitcoin itself in relation to these government currencies **does not** remain the same. In fact, perhaps one of Bitcoin's most defining traits to mainstream investors is its extreme price volatility. This trait, perhaps the greatest shortfall of Bitcoin and many other cryptocurrencies, is the **fatal obstacle** standing in the way of Bitcoin becoming future money.

## Store of Value

Some proponents of Bitcoin point to its price as evidence of its widespread adoption as money. However, this argument is precisely why it cannot serve as money. If you were to purchase Bitcoin at \$30,000 and the value of your Bitcoin doubles to \$60,000 in one month, holders of Bitcoin have a strong incentive to keep it in their possession and not spend it. When taking this rationale to its logical extreme, we see that if everyone were to stop spending their money all at once from following this incentive structure, it is clear that our entire economic system would collapse because businesses would have no revenue to work with to pay employees, debt obligations, or shareholders.

In addition, having money be a stable store of value is not important only for savers, but for borrowers as well.

Suppose you receive a \$1,000 loan from your bank. When paying back that loan, you expect the cost of paying back that loan to be the same as the benefit received from the capital acquired from the loan. Now let us say you apply for a one-year loan of exactly one Bitcoin. If that one Bitcoin is worth \$50,000 today, but then skyrockets to \$95,000 when repayment of that one Bitcoin is due, this newfound debt burden will far outweigh the temporary benefit of the loan.

Because of this, companies looking for cash are unable to take the risk of borrowing in Bitcoin. In other words, companies need to know the "value" of the debt they are taking on. The advantage for companies borrowing in U.S. dollars and other world currencies is that the average annual 2% inflation rate allows companies to pay back the fixed loan amount in "cheaper" dollars, therefore providing an incentive for companies to borrow additional capital to grow in the long-term. That said, a 2% inflation rate still implies a slow, yet steady depreciation of this conventional store of value, which indicates that no currency in existence has been a perfect store of value, but that some currencies may be better than others.

## Conclusion

Through understanding these concepts, we can say that although Bitcoin may not be able to serve as money in today's world, it has been able to serve as a digital asset for buyers in the free market where the value of the asset itself is determined by those buyers. It is unique in the sense that it does not behave the same as other assets like stocks, bonds, or real estate, and so risks related to price fluctuations should always be considered when owning this digital asset. That said, there could be a world where Bitcoin may not be used as money per say, but the underlying distributed-ledger technology within these cryptocurrencies could be used to provide solutions for industries not necessarily related to finance or payment systems. These other solutions, while very exciting and worth discussing, will be further explored in future articles to come.

<sup>i</sup> Bitcoin: J.P. Morgan says value could triple, challenge gold | Fortune

<sup>ii</sup> [https://specials-](https://specials-images.forbesimg.com/dam/imageserve/1067593436/960x0.jpg?fit=scale)

[images.forbesimg.com/dam/imageserve/1067593436/960x0.jpg?fit=scale](https://specials-images.forbesimg.com/dam/imageserve/1067593436/960x0.jpg?fit=scale)

<sup>iii</sup> Money | Definition of Money by Merriam-Webster ([merriam-webster.com](https://www.merriam-webster.com/dictionary/money))

<sup>iv</sup> Daily Bitcoin transactions 2017-2021 | Statista