

Cryptocurrencies: revolution or speculation?

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On 11 December last, Bitcoin started trading on the Chicago futures market (CBOE), and its value rose to more than US\$15,000 in the first few days. These events have fuelled the debate about cryptocurrencies. Are we dealing with a revolution with firm foundations or a passing fever?

But first we need to distinguish between cryptocurrencies and virtual currencies. While both are digital means of exchange, cryptocurrencies are based on the encryption of information, protecting the identity of users of the cryptocurrency by means of a system that is very difficult to crack with current computing capabilities. Virtual currencies do not per se ensure decentralisation of their control or encryption.

Supporters of cryptocurrencies base their value on privacy (i.e. the fact that the information is encrypted) and on the reduction in the number of intermediaries involved in executing a transaction, making the existence of a central body impracticable. Barack Obama defined them in 2016 as a “Swiss bank account in [your] pocket”.

Others point to technological advantages. For example the added value of cryptocurrencies is said to come from their efficiency. In the traditional system, sending and receiving large sums of money becomes a difficult task, whereas with cryptocurrencies it can be done quickly, cheaply, with fewer intermediaries and while also protecting one’s identity. Although these advantages are partly offset by the excessive consumption of energy involved and the long settlement times.

There could also be so-called “financial advantages”. While the money supply in conventional currencies grows, Bitcoin for example is limited by means of its algorithm to 21 million Bitcoins in circulation, avoiding monetary inflation and loss of purchasing power. It could even be a deflationary currency, since the money supply base could be reduced due to the possibility of losing access to cryptocurrencies (because of the strength of encryption).

These advantages relate to one of the main criticisms: the difficulty of regulating them, precisely due to their decentralisation. Although cryptocurrencies protect identity, they also allow illicit trading. This is a challenge for governments and the current financial system, since it would involve the emergence of a financial system based on decentralised individual transactions, with consequences that are difficult to foresee and with tax implications too (regarding money laundering, among other things).

But if this technology has been available since 2009, why is it only now that cryptocurrency fever has broken out? There are two answers: the first, that it is a speculative bubble; the second, that society has entered the next phase of adaptation.

The bubble interpretation asserts that the main attraction of cryptocurrencies is speculative, since their profitability depends solely on more people acquiring them. Furthermore, it is argued that these are not currencies but commodities, since they do not perform the functions of money: deposit of value, means of exchange and unit of account. Due to the low level of adoption of cryptocurrencies in the real economy and

their high degree of volatility, it seems that they are still far from being institutionalised as money, or at least in accordance with the traditional definition of money.

Others argue that cryptocurrencies are reaching the next stage in their adoption by society and that this speculative behaviour forms part of a first phase prior to their institutionalisation. The fever could be reflecting rising expectations that cryptocurrencies will be widely used in the future as the world becomes more globalised and digitised.

This is what occurred with the invention of the light bulb: in order for its use to spread it was necessary to develop an industry, a network of engineers familiar with it, electricity and knowledge of its advantages among society. In the same way, cryptocurrencies are currently in the adoption phase. If this interpretation is correct, regulation will assume a fundamental role, since the fact that these are still unregulated assets increases mistrust among users. In this regard, the listing of Bitcoin futures on the CBOE represents a major step in the process.

In any case, there seems to be a certain consensus that cryptocurrencies are still far removed from the standardisation of conventional regulation, in an embryonic phase, and that they remain highly volatile. For this reason, in the wake of Bitcoin, various other rival cryptocurrencies have arisen, aiming to improve their functioning. Alternatives to decentralised cryptocurrencies include private cryptocurrencies for certain transactions and cryptocurrencies issued by central banks.

The success of cryptocurrencies will depend largely on whether they can demonstrably improve people's lives and be accepted by the population. Meanwhile, their price will continue to be based on expectations and speculation about the future. Will personal encryption of our money end up forming part of our daily life?

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