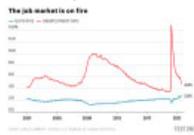


Most Popular



The Great Resignation is no joke



Stock futures slip after the S&P 500 hits a new record — Bitcoin sputters

FINANCE • EYE ON INVESTING

Is this a Bitcoin bubble? The debate is roiling some of Wall Street's most seasoned investors

BY **SHAWN TULLY**

October 21, 2021 8:30 PM EDT



Subscribe to *Fortune Daily* to get essential business stories delivered straight to your inbox each morning.

It's hard to think of a case when two opposing camps, both comprising leading CEOs and money managers, held such wildly divergent views of a major asset. The critics contend that the world's hottest, most media-obsessing pick is practically worth zero, while its fans swear that their favorite's recent leap is just the first leg in a moonshot. As Bitcoin hits an all-time record, investors are trying

to sort through the outright derision on one side and cultlike belief on the other and get a rational answer to the market's leading puzzle, "Is Bitcoin in a bubble?"

Surprisingly, neither extreme gives an accurate guide to Bitcoin's future. The answer: Sure, Bitcoin has almost no [practical uses](#), but folks love it as a vehicle for speculation that, despite the bumps, has proved immensely rewarding, and that romance is likely to endure. If stocks and housing keep doing great, Bitcoin could do even better. But if times get tough, watch out for losses that will dwarf the hit to stocks, bonds, or real estate.

At midafternoon on Oct. 20, Bitcoin was hovering at \$66,000, beating the all-time, intraday record set on April 13 of \$64,863 by two percentage points. It's jumped, capping a rise of 89% in the past 90 days, adding nearly \$600 billion in market cap. The leading cryptocurrency's amazing run—it's quintupled in the past 12 months—has stirred an array of prestigious investors to claim that it's crazily overvalued and headed for disaster. Earlier this year, famed hedge fund manager Michael Burry claimed Bitcoin was heading for "the mother of all crashes" when its price was far lower. Its new surge stirred Burry to take aim again on Oct. 15, tweeting that the signature coin is "driven by speculative fever to insane heights from which the fall will be dramatic and painful." Burry's view got lots of press, since he's a veteran at calling frenzies that end in tears; he profited richly by betting against the housing market during the 2006 frenzy, as chronicled in Michael Lewis's bestseller *The Big Short*.

Two other celebrated money managers who made billions calling the subprime meltdown joined the chorus of doom. In August, John Paulson branded cryptocurrencies "a bubble," predicting that once it pops, Bitcoin and the others will prove "worthless." Paul Singer, founder of \$48 billion hedge fund Elliott Management, charged earlier this year that cryptocurrency investors are deluded in "thinking they're rational" and that he is waiting for the debacle to end, "when we can say, 'I told you so.'"

In opposition stands a prestigious roster of Bitcoin champions. Among the leaders are ARK Invest founder Cathie Wood, who predicts that Bitcoin will leap eightfold from its current summit to \$500,000. She's joined by a trio of CEOs who've piled Bitcoin on their balance sheets: Elon Musk of [Tesla](#), Jack Dorsey of Square, and Michael Saylor of MicroStrategy. So let's examine the bulls' reasons for wagering that Bitcoin will keep climbing from here, and contrast them with the naysayers' position that it's on the cusp of a free fall that could erase its

champions' entire stakes.

The pro-Bitcoin group believe the coins will prove increasingly valuable because they have real, tangible uses. Those roles fall into four categories: Bitcoin as a currency, as a place to park corporate cash, as an inflation hedge, and as a “store of value” that’s better than gold. Wood sees Bitcoin as gaining wide acceptance for sales and purchases, the anchor of “an internet payment ecosystem” made possible by advances in technology that its critics don’t appreciate. Musk has also spoken approvingly of Bitcoin’s future as a coin of the realm, promising to accept it for purchasing his EVs if its [environmental footprint improves](#). All three CEOs think Bitcoin’s a great vehicle for getting much bigger returns from the billions sitting in their war chests, which would otherwise earn puny rates of interest. [Square CFO Amrita Ahuja recently advised others to take Square’s lead](#): “There’s absolutely a case for every balance sheet to have Bitcoin on it. We see Bitcoin and cryptocurrencies as expanding access to financial services,” she told *Fortune’s* Sheryl Estrada this summer.

Now that inflation is roaring, Bitcoin’s fans are reprising their claim that it offers long-term protection versus fast-rising prices—chiefly because its supply is fixed and can’t be manipulated by a central bank. Saylor maintains that Bitcoin is a much better shield than that traditional haven, gold. The “better than gold” argument advanced by Saylor and Wood holds that Bitcoin should appreciate faster than the precious metal because, as Saylor argues, Bitcoin can be distributed digitally, in small dollar quantities, giving it tremendous reach to potential investors. And the quantity that can be unearthed can never increase, whereas a jump in gold prices gets the mines running faster, or in a great market leads people to sell their family heirlooms.

The Bitcoin bears

By contrast, the anti-Bitcoin contingent holds that Bitcoin fails on all four counts. And for the most part, they’re correct. Other than outliers Tesla, MicroStrategy, and Square, Bitcoin has failed to get CFOs to take a flier with their corporate cash. “Bitcoin has 90% annual volatility, so that takes its use on balance sheets off the table,” says Cam Harvey, a professor at Duke University who’s an expert in decentralized finance. Companies instead value liquidity and safety above all, the opposite of the bumpy ride offered by Bitcoin. It has also gained virtually no traction in buying and selling everyday (or even expensive) consumer items. That’s because Bitcoin transactions that run over the public blockchain are far too

slow and expensive to compete with the likes of credit card platforms. “It’s not a transaction mechanism, given the cost,” says Harvey. Even Saylor, contrary to Wood, admits that Bitcoin will never be a medium of exchange. It’s also ineffective in protecting purchasing power during periods of rising prices. “There’s no evidence it’s a hedge against inflation,” says Harvey. “If next month’s inflation print shows a big increase, it’s likely that stock and bond prices would plummet, and given what we’ve seen in the past, Bitcoin would plummet even more.”

As for the “better than gold” assertion, Bitcoin lacks the fundamentals that support gold’s price and cushion the swings in its value. “Gold has real world, tangible uses,” says Harvey. “Seventy percent of gold is used in jewelry as well as for electronics, and in some countries, for dental work.”

Harvey highlights the problem with valuing Bitcoin. “It has no fundamental, tangible value,” he notes. “Unlike stocks or bonds, this is an asset with no future cash flows.” Investors can make estimates of whether Tesla or [Apple](#) is over- or undervalued based on projections of their earnings versus their current price. Likewise, the ratio of home prices to rents on apartments of comparable size, versus the historical norms, gives strong insight into whether houses are rich or cheap. But folks and funds can’t run similar analyses for Bitcoin.

Hence, Bitcoin is different from gold. It’s strictly an intangible, speculative asset. Since it’s impossible to value, the dispersion of views on what it’s really “worth” is gigantic, as shown by the distance between the boosters and foes. So where is the Bitcoin price headed from the new peak? “We’ve seen this movie before,” says Harvey. “What moves Bitcoin is the ebb and flow of speculators.” He foresees that Bitcoin will endure multiple crashes and spikes going forward. “The closest crash was late 2017 to late 2018, when Bitcoin went from over \$20,000 to under \$4,000, losing more than 80% of its value,” he says.

For Harvey, Bitcoin is the ultimate “risk on” asset that mostly follows the jumps and drops in stocks. The difference is that Bitcoin appears “leveraged” to those market moves. When equities surge, Bitcoin outpaces the rise; when the S&P 500 falls, Bitcoin’s fall is steeper. It’s possible that the factor causing those lurching moves is a mostly overlooked weakness that could prove extremely dangerous. It’s the large proportion of Bitcoin trading conducted using futures options, mainly on unregulated exchanges. That results in highly leveraged trades where betting or withdrawing small amounts of cash can cause big swings, and a strong

downdraft could force investors to liquidate their positions, accelerating the descent. Warns Burry: “If you don’t know how much leverage is involved in the run-up, you may not know enough to own it. If you don’t know how much leverage is in crypto, you don’t know anything about crypto.”

So what are the chances that Bitcoin can keep waxing from here? It all depends on whether investors’ animal spirits, which keep driving U.S. stock prices ever higher, remain as vibrant as they are today. Optimism about stocks fuels optimism on steroids for Bitcoin, and when the mood darkens for equities, it can go black for Bitcoin. In March of last year, the S&P 500 fell 35%, and Bitcoin dropped 55%. When stocks rebounded in the current rally, Bitcoin rallied even more. Right now, the stock market and the economy are enjoying a frothy, euphoric state: P/E multiples are at a premium, in the mid-20s, on top of earnings that are one-third higher than their record at the end of 2019. If rates stay extremely low, the consumer keeps spending freely, and the new government stimulus programs put even more cash in families’ wallets, stocks could keep chugging, and Bitcoin could chug faster. But if we’ve hit peak profits and rates rise, stocks will go flat or decline, and Bitcoin will take a big hit.

Will Bitcoin disappear or go to nil as its detractors predict? “I think it has a future,” says Harvey. “It’s a computer program; by definition it won’t be turned off. It will remain.” He notes Bitcoin can be useful for very large transactions where cost isn’t a problem. “We saw a \$5.4 billion transaction go over the blockchain,” he says. Of course, that’s a niche use that won’t bolster Bitcoin’s price. Bitcoin isn’t an automatic escalator powered by its appeal as a currency or as a harbor for corporate cash or by earnings that will grow going forward. It takes its cue from other “risk assets” only careens far more. In good times, you could do better holding Bitcoin. But when times are tough, you get the worst of all worlds, bigger drops than for stocks, and none of the protection of gold. Whether Bitcoin will deliver in the years to come is an open question. But if you’re a believer, fasten your seat belt for the wildest of rides.

More [finance coverage](#) from Fortune:

- 4 things to know about [stimulus checks in 2022](#) and beyond
- [GameStop report from SEC](#) sheds new light on meme stock mania—conspiracies and all