

The sharp rise and subsequent fall in Bitcoin's value places it among the greatest market bubbles in history. It has outpaced the 17th-century tulip mania, the South Sea bubble of 1720, and the more recent Japanese asset price and dot-com bubbles.

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The rapid price rise garnered attention from an increasing number of academics and investment advisers. Some have suggested that Bitcoin improves portfolio performance and can even be used as a potential “safe haven” asset in [place of gold](#).

Our work finds that much of this research is [flawed](#) and overlooks some [important attributes](#) that any investor should consider before allocating funds to such a speculative investment.

This is particularly relevant if investing in Bitcoin is rationalised as a prospective [safe haven](#) in times of market turmoil.

## Hard to value

The first attribute investors consider is how to value Bitcoin. Typically, assets are valued based on the cash flows they produce. Bitcoin lacks this property.

This leads to ongoing debate as to the true value of Bitcoin and other cryptocurrencies. Some, such as the Winklevoss twins and other [Bitcoin entrepreneurs](#), believe the price will soar far higher. Others, including Nobel prize winner

[Eugene Fama](#)

and esteemed investor Warren Buffett, believe the real value is closer to zero. Another Nobel winner,

[Robert Shiller](#)

, suggests the correct answer is “ambiguous”.

There is even wide variation in price across the various Bitcoin exchanges. This is common in fragmented markets and makes it difficult for an investor to find the best market price at any point in time – a process called price discovery.

### **High price volatility**

Bitcoin prices also have a high level of variation (volatility) when compared to other possible investments including bonds, stocks and gold. Even tech stocks such as Twitter, which are considered relatively volatile, are found to have less price variation. This adds to the difficulty investors face when trying to value Bitcoin and any portfolios that contain it.

This is of particular concern given the large daily losses that Bitcoin has experienced in its relatively short life. The largest one-day decline experienced by the popular S&P500 index since 2011 is 4.2%. Bitcoin has had nearly 200 days that were worse (and over 60 days worse than the biggest decline in the gold price of 10.2%).

Put another way, Bitcoin has had 200 days worse than the worst day on the stock market. This hardly seems like an enticing investment for most.

### **Low liquidity**

Investors should also consider the ease with which they are able to buy and sell any assets in which they invest. One method used to measure this liquidity attribute is the bid-ask spread – the difference in the price at which one is able to buy and sell the asset.

More liquid assets have a narrow bid-ask spread. Bitcoin's bid-ask spread varies from one exchange to another, but in general it is much larger than for other assets.

While bid-ask spreads provide one measure of implicit trading costs, investors also consider the explicit transaction fees they are charged when trading. Transaction fees for trading traditional investments are typically well known and have trended down over time.

While Bitcoin fees have recently declined, they have proven to be highly variable, ranging from

over \$30 to under \$1. The time taken to process a transaction can also be greater than 78 minutes. This is much longer than for stocks or bonds and creates another layer of uncertainty for investors.

### Only for the most risk-loving

Bitcoin is harder to value, more volatile, less liquid, and costlier to transact than other assets in normal market conditions. Potential investors should be wary and carefully consider whether such highly speculative assets are appropriate additions to any portfolio.

Given safe havens are typically in demand during financial crisis, when markets are more volatile and less liquid, it is highly unlikely that Bitcoin is even worth considering as a safe-haven asset.

*Lee Smales does not work for, consult, own shares in or receive funding from any company or organization that would benefit from this article, and has disclosed no relevant affiliations beyond their academic appointment.*

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