A deeper dive beyond crypto

Still waters run deep, but what about tumultuous waters? Few traditional assets can rival cryptocurrencies in terms of the splash they have caused, both with respect to the strong views by supporters and opponents, as well as the price swings they have seen. One of the main cryptocurrencies, the most prominent example, rose massively between September 2020 and March 2021, making the 20% rise in global equity markets over the same period look small.

Cryptocurrencies are just the surface of the deeper ocean though. Diving deeper, it becomes clear that cryptocurrencies are just one example of a digital asset. A digital asset is just one use case for a blockchain, which in itself is only one application arising from distributed ledger technology (DLT). Distributed ledgers are decentralized databases that make use of various technologies to provide alternative solutions to make transactions more efficient, secure and transparent.

DLT opens the door to contracts that automatically trigger payments based on certain conditions, and can speed up and lower the costs of services such as settlement and collateral management. Applications in other areas are possible as well, such as anonymizing medical history in healthcare, product history information for consumer and luxury goods, and intellectual property licensing. Disruption from DLT is therefore likely not just in the financial services industry, but across much of the economy and in our private lives.

We think that long-term value creation potential lies with those companies that either support the evolution of the DLT ecosphere—enablers who provide the hardware and software to keep data centers running—or, in particular, those that serve as platform companies. These companies provide innovative products and services based on DLT, helping to improve efficiency and lowering costs in various business processes. Investing in such companies means swimming with the current, rather than trying to capture the splashes on the surface. To explore the opportunities and risks involved further, we recommend having a look at our recent publication: “Distributed ledgers and digital assets.”

So is there a place for crypto coins in investors’ portfolios? From a strategical point of view, our answer is no. We think it is difficult to have sufficient confidence in valuation frameworks and to properly assess all the regulatory, legal, and technology risks. In addition, several cryptocurrencies score very poorly when it comes to their environmental footprint. Therefore, we don’t see cryptocurrencies as a regular portfolio component. That said, for highly risk tolerant investors who are naturally drawn by the high volatility and large price swings, cryptocurrencies may serve as a highly speculative investment, if they accept the potential permanent loss in wealth while aiming for outsized gains.

Ultimately, buying crypto coins is a very personal decision: What are investors’ return expectations and needs? What is the investment horizon? How much risk are investors willing and able to take? It is by far not the only personalized decision that investors can and should take. Managing financial interests can mean entering deep waters, but UBS is happy to support to help investors’ wealth voyage run smoothly.

Author: Michael Bolliger, Chief Investment Officer Global Emerging Markets