

Why there's no future in cryptocurrencies

Richard Firth, CEO,
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FTX, a major cryptocurrency exchange, and FTX.US, its American branch, filed for Chapter 11 bankruptcy on 11 November 2022. This is not the only disturbance to hit the extremely volatile cryptocurrency market – a market that has repeatedly avoided all efforts at regulation and integration into traditional financial systems.

Since the first cryptocurrency made its appearance in 2008, proponents have hyped the value of a decentralised alternative to fiat currencies. This is, in part, why cryptocurrency values are so unstable – hype cycles have led to massive over-inflation of the worth of digital currencies, leading to price extremes that are hard to predict.

Last year, for example, more than \$300 billion was wiped out by a crash in cryptocurrency in just a week. The price of Bitcoin plunged to its lowest point since 2020. Coinbase, another large cryptocurrency exchange, also tanked in value.

Building on hype cycles

The FTX crash was the direct result of a lack of liquidity and mismanagement of funds, followed by a large volume of withdrawals from rattled investors. But this is merely a symptom of a larger problem. Despite the fact that the world has largely moved away from the gold standard, fiat currency values are wrapped up in very real dynamics. From a country's GDP, to its credit rating, the worth of a traditional currency is impacted by quantifiable factors. Cryptocurrencies, on the other hand, rise and fall on the basis of investor interest, which is largely based on perceived value.

“The value of cryptocurrencies has been propped up by hundreds of millions of dollars being injected into the market to secure a higher price. From the earliest days of digital currencies, investors have been capitalising on extreme value spikes to make massive profits, and these have correlated closely to media reports promoting the hype. Many of the journalists reporting on the rise and fall of crypto values were early investors themselves, creating the cycles that have seen some people become overnight crypto billionaires,” says Richard Firth, CEO of MIP Holdings.

Rowan Williams, Chief Investment Officer at Nitrogen Fund Managers agrees, adding that in addition to the journalists being complicit in the hype, the large venture capital firms carry their own share of the blame through overinflated values of exchanges like FTX. “These firms placed outrageous valuations on FTX with very little due diligence and squandered investor funds on what turned out to be a very speculative investment,” he points out.

In fact, a lack of due diligence and regulatory oversight is the most common theme when it comes to wider use of cryptocurrencies. The collapse of FTX is just one more failure of oversight and regulation in an industry that operates outside conventional banking rules.

The regulatory dilemma

According to Williams, regulation remains an existential dilemma for crypto as any form of centralised regulation negates many of the benefits and utility of decentralised currencies. “Does this mean that crypto is sown with the seeds of its own destruction or alternatively will remain at best a fringe technology and not achieve widespread adoption due to its inherent risk of fraud and misappropriation? This remains a major hurdle for the technology to overcome,” he says.

“The fact is that if the world regulates crypto then these technology platforms become just another banking system or platform where currencies, transactions and consumers are tracked and traced. If we regulate crypto, then how does the cyber underworld collect revenues through their massive and lucrative scams? There is a one-to-one correlation between the increase in cybercrime and the increase in crypto usage,” says Firth.

Williams adds that the volatility of the various tokens is a further barrier to their mainstream adoption for more commonplace transactions. “If the challenges of regulation and transparency can be addressed and tokens such as Ether become more mainstream, I anticipate that, ironically, the tokens will drop in value as they transition from being a speculative investment opportunity to a more mainstream currency that is less volatile and more widely accepted. This is another reason to sit out of the crypto investment hype,” he says.

Firth points out that while many may argue that Blockchain technology still holds value, there is no value in ripping and replacing current administrative platforms. These give the consumer direct access to all their transactions taking place in an ecosystem, with regulatory oversight ensuring transparency – and more importantly – trust.

No mainstream crypto on the horizon

The FTX crash has predictably resulted in calls for more oversight, but this will do very little to solve the inherent problems cryptocurrencies carry with them. “U.S. exchanges are subject to more regulation and reserve bank requirements than international exchanges, and we are still seeing these types of bubbles burst. In a real world scenario, not only are these ups and downs the equivalent of bank runs, the hype cycles are ensuring that there is no real hope for the kind of stability cryptocurrencies would need to become more mainstream,” Firth says.

“How would retailers like Pick 'n Pay or Woolworths get value for merchandise sold in a cryptocurrency that has lost more than 30% of its value in a single year? The FTX crash proves that digital currencies are nowhere close to being a real alternative for the financial industry. Investors and FTX customers have lost billions, and not all of it will be recovered. Without trust and stability, cryptocurrencies are going to remain a tool for scammers and cybercriminals, with limited applications in any other market,” he concludes.

