Why the Bitcoin ETF approval by the SEC is a big deal!

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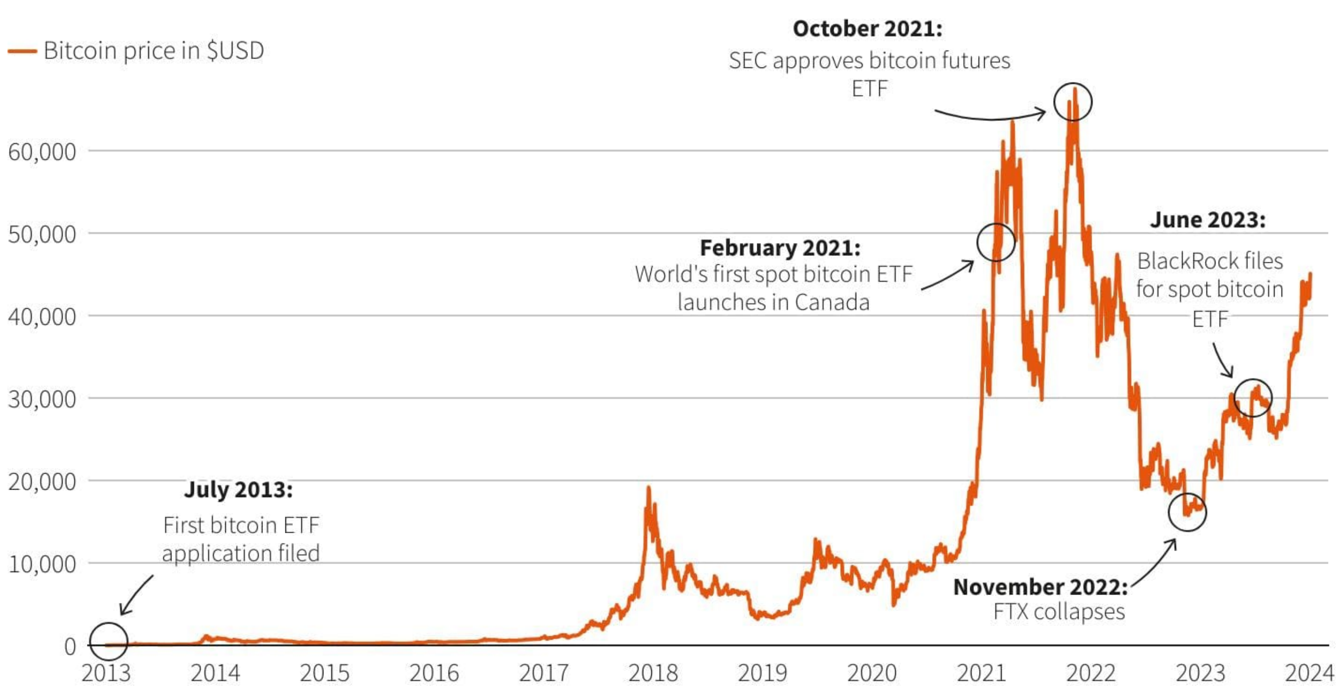
Introduction

An exchange-traded fund (ETF) is a type of financial instrument that can be bought and sold much like an individual security and aims to track or mimic the price of an underlying asset e.g an individual commodity, an individual security or a diverse collection of securities as contained in a securities index, say the S&P 500. Unlike the typical mutual fund or even an index fund, which only trades once a day at market close, an ETF can be bought and sold throughout the trading day.

Traditional ETFs have a long history tracing back decades with the first having been issued in 1993.

The first Bitcoin ETF application was only made in July 2013, but it is the latest action by the SEC to approve a Bitcoin ETF that has created the most media and investor hype.

This report outlines the reasons behind this media and market hype.



Source: London Stock Exchange Group (2024)

Registration

Being registered with the financial markets' regulator e.g the SEC requires the financial instrument-issuer (here the BTC ETF-issuer) to provide detailed information about their business and financial operations to enable investors make informed investment decisions. This requirement means that investors are able to take a deep-dive into the nature and scope of their investment and make an informed assessment of the related risk-return profile.

Further, registering securities with the SEC means that these securities remain in strict compliance with securities laws thereby increasing their transparency, the protection of investor interests and indeed their valuation.

Listing

Listing on a securities exchange, that typically follows registration with the regulator (though not always), helps boost the attractiveness of the financial instrument to investors through enhanced profile while improving its liquidity. Greater liquidity and both the increased investor and analyst attention following a listing, further provide for better price discovery of the traded Bitcoin ETF.

Examples of Bitcoin ETFs now listed on exchanges include the Grayscale Bitcoin Trust (GBTC), BlackRock's iShares Bitcoin Trust (IBIT), ARK 21Shares Bitcoin ETF (ARKB), Bitwise Bitcoin ETF (BITB), Invesco Galaxy Bitcoin ETF (BTCO) and Fidelity Wise Origin Bitcoin Trust (FBTC), having made their debuts on securities exchanges like the Chicago Board Options Exchange (CBOE), the New York Stock Exchange (NYSE) and Nasdaq.

Intraday trading

Intraday trading involves buying and selling securities within the same trading day, aiming to profit from short-term price moves and volatility. Bitcoin ETFs will enable both retail and institutional investors optimise trade entry and exit rules that fit their styles and maximise on profit-taking where opportunities present themselves.

With the introduction of Bitcoin ETFs, all investor types will be able to employ a whole host of investment strategies to take advantage of intraday trades from algorithmic trading down to employment of such trading tools as limit orders, stop-loss orders and margins.

Volatility

The volatility inherent in the crypto space, including in Bitcoin, with wide intraday price swings provides opportunities for return for all investor types from those hunting for value to those actively looking for price anomalies brought about by FOMO and FUD.

The opening hour of trade, in particular, tends to see significant volatility as traders react to overnight news and events, while the last hour before close also exhibits trading opportunities around the closing price range. Unlike with index funds and other mutual funds which only trade at close of business, this volatility provides Bitcoin ETFs with numerous opportunities for profit-taking throughout the trading day.

Bull market

The approval of a BTC ETF could not have come at a better time, right on the cusp of the end of the crypto winter and start of what appears to be a renewed bull market partly instigated by the upcoming Bitcoin-halving in April 2024. Bitcoin has topped its ATH multiple times and in quick succession since the beginning of the year.

Approval of the BTC ETF by the SEC is clearly the icing on the cake in a market that is set to continue to see more all-time highs as there appears to be little sign of a slowdown in USD printing- the default currency BTC is priced in.

Bitcoin is seen by many as a deflationary asset.

Liquidity

Drawing in institutional investors, (due to the reassurance served them through SEC registration of a BTC ETF), will greatly increase trading volumes, reduce bid-ask spreads and lead to better price discovery. Greater liquidity makes it quick and efficient for buyers and sellers to trade in and out of securities with tight spreads and also lowers transaction costs.

Deep and liquid financial markets are also key to financial stability. Market participants require liquid markets in order to effectively manage risks. Market depth and liquidity work in a symbiotic manner to help reduce overall market risk.

Legitimacy

Approval of the Bitcoin ETF by the SEC provides legitimacy to the underlying asset- BTC and acts as a seal of approval helping to improve BTC's investment profile and its inclusion in a wide array of portfolio types.

Since its inception, Bitcoin has received much negative press with even notable leaders in the financial world – most notably chairman and chief executive officer of JPMorgan Chase & Co.- Jamie Dimon and no lesser personality than the 'Oracle of Omaha'- Warren Buffett referring to it as a scam.

The SEC approval helps to allay these fears.

Last word!

The advantages that a bitcoin ETF brings to investors, both retail and especially institutional, are rooted in the credibility accorded the relevant financial instrument through registration with the regulator and subsequent listing where this also takes place. Increased investor confidence brought about by such registration inadvertently leads to greater investor participation, higher trading volumes and pursuant improved liquidity.

An added advantage is that, while index funds that track the price of Bitcoin may offer similar advantages to that offered by ETFs, it is the ability of ETFs to allow for intraday trading that makes ETFs especially attractive. Given the volatility inherent in Bitcoin and significant intraday price swings that can occur within hours in the cryptoasset space, the opportunities to make huge profits in a relatively short period of time by employing superior analytical and proprietary tools (as would be available to institutional investors in particular) act as a draw to both large and small players in the market.

As the crypto market continues to deepen, investors both large and small should expect the introduction and approval by various regulators of more financial instruments based on cryptoassets.

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