FINANCIAL FOCUS

Bitcoin: Investing or speculating?

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Many people have decided that bitcoin is the next big thing – and they are backing up their enthusiasm with dollars. Should you, too, consider putting money into bitcoin or other cryptocurrencies?

First of all, keep in mind an essential piece of financial advice: *Don’t invest in something you don’t understand*. And bitcoin is not easily understandable. There’s no physical bitcoin, nor is it backed by a bank or government. It’s a digital currency, used for transactions on a decentralized network of computers. The market’s demand for bitcoin largely determines its price, though other factors are also involved.

And this price can vary widely. Since bitcoin was introduced in 2009, it has gone through periods of enormous gains and precipitous declines. Its short history has reminded market watchers of the bursting of the “dot.com” bubble in 2000 and the housing market bubble in 2007. These results have raised the following question about purchasing bitcoin: Is it investing or speculating?

There’s a big difference between the two. Speculators engage in risky transactions with the hope of profiting from short-term price fluctuations in various financial vehicles. Investors, on the other hand, stick with these practices:

• **They follow a long-term strategy**. Real investors follow a long-term strategy based on their goals, risk tolerance and time horizon. Generally speaking, long-term investors don’t do a lot of buying and selling, saving on fees and potential taxes. But this “buy and hold” approach doesn’t mean investors put their portfolios on autopilot. Instead, they review their portfolios at least once a year to make sure their investment mix is still appropriate for their needs.

• **They focus on quality**. Long-term investors stay away from the flashier – and riskier – financial instruments. Instead, these investors seek *quality*. When they’re considering stocks, for example, they look for companies with solid fundamentals, including strong management teams, competitive products and services and business plans that bode well for the future. When they buy bonds, they seek those with high credit ratings issued by the independent rating agencies. Focusing on quality doesn’t yield quick results, but it can instill confidence in one’s investment choices.

• **They diversify their holdings.** If a downturn in the financial markets affects one type of asset particularly hard, and your portfolio contains a high concentration of that asset, your financial strategy could be jeopardized. Long-term investors reduce this risk by owning a variety of investments. While diversification can’t guarantee profits or protect against all losses, it can help reduce the impact of market volatility on your portfolio.

And here’s one more difference between investors and speculators: *track record.* Investors put their money into companies that provide tangible goods and services, and these companies have historically grown with the overall economy. Stocks and bonds are established investment vehicles with well-defined and regulated markets. Consequently, investors can assume a certain degree of predictability, though, of course, stock prices will always fluctuate in the short term and there are no guarantees against loss of principal. Cryptocurrencies, on the other hand, are relatively new, largely unpredictable and will likely face increased regulation in the future, with the ultimate risk being an outright ban by some governments.

You work hard for your money – so think carefully about how you can best put it to use to help you reach your lifetime goals.

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*This article was written by Edward Jones for use by your local Edward Jones Financial Advisor.*