

This copy is for your personal, non-commercial use only. Distribution and use of this material are governed by our Subscriber Agreement and by copyright law. For non-personal use or to order multiple copies, please contact Dow Jones Reprints at 1-800-843-0008 or visit www.djreprints.com.

<https://www.wsj.com/finance/currencies/bitcoin-inflation-hedge-84f6b840>

FINANCE | CURRENCIES

Is Bitcoin an Inflation Hedge? Here Are the Arguments on Both Sides

Two experts, Zach Pandl of Grayscale Investments and Eswar Prasad of Cornell, make their cases on whether bitcoin is protected from inflationary pressures, or is more of a speculative investment

By Dan Weil

Oct. 8, 2023 11:00 am ET



Bitcoin is scarce, that much is not in doubt. But whether that makes it a good inflation hedge is debatable. Here, a crypto automated-teller machine in Barcelona. PHOTO: ANGEL GARCIA/BLOOMBERG NEWS

Bitcoin advocates have talked up a number of selling points over the cryptocurrency's 14-year history. It is anonymous. It lets you make secure transactions without getting a bank involved.

And then there is one particularly contentious argument: Bitcoin is a hedge against inflation, much like gold.

Why? There is a limited supply of bitcoins. Only 21 million can be mined—a limit set by the currency's founder, who has the pseudonym Satoshi Nakamoto—and there already are about 19.5 million in existence. That constraint, advocates say, means bitcoin is protected from the inflationary pressures that can afflict other currencies.

But bitcoin's record as an inflation hedge has been mixed. For example, when inflation surged from late 2020 until June 2022, bitcoin's value did rise, but with big moves up and down along the way. And as inflation has slid since June 2022, bitcoin has continued to bounce around, now standing little changed from early that month.

Given this volatility, bitcoin naysayers say, the cryptocurrency is more a vehicle for speculation than a hedge against inflation. Also, they say, there is no reliable method for valuing bitcoin, and its lack of central-bank backing makes it even riskier.

So, is bitcoin an inflation hedge? Does it have the potential to serve as a store of value? We asked two experts on opposing sides of the issue.

On the "yes" side is Zach Pandl, managing director of research for digital-currency asset manager Grayscale Investments. On the other side is Cornell University professor of trade policy Eswar Prasad.

Here is a closer look at their arguments.

YES: Scarcity makes bitcoin valuable

Bitcoin has some of the same characteristics as assets that have historically outperformed during inflationary periods, such as gold, Pandl says. And it offers unique features that make it better suited as an inflation hedge down the road.



Zach Pandl

The biggest element it has in common with traditional hedges: scarcity. But unlike those other assets, bitcoin's scarcity is guaranteed. Take gold, for instance. "While estimates exist, the absolute amount of gold that will ever exist is unknown," he says.

True, bitcoin isn't backed by anything tangible in the real world. But consider this, Pandl says: According to the World Gold Council, he says, 85% of the aboveground gold stock is used for jewelry or investment purposes (in which he includes official holdings in central banks). So gold, too, is largely a speculative vehicle, not an asset with widespread uses. Gold "has value because of social agreement," even if it has ancient roots, he says.

Meanwhile, bitcoin's value isn't just guaranteed by scarcity. The cryptocurrency is entirely digital, which gives it advantages that concrete investments don't have, such as portability for all investors, Pandl says. Cryptocurrency holders "can access their bitcoin anywhere in the world as long as they can connect to the internet and have their private key," he says.

Bitcoin is also divisible into smaller units for transactions, which gold isn't. That means investors can buy and sell smaller denominations of bitcoin than, say, physical gold or gold ETFs, which gives buyers and sellers the freedom to make transactions that suit their needs more closely.

More broadly, Pandl says, bitcoin is built on technologies that will become widespread in the future—public blockchains, which can handle financial transactions securely without the need for a central authority. As our lives blend the digital and physical with technologies such as artificial intelligence, he says, bitcoin will be viewed as a more natural store of value than an asset like physical gold.

"Bitcoin will continue to capture market share from gold as an inflation-hedging asset better suited for our globalized and digitized age,"

Pandl says.

In fact, he thinks bitcoin's movement over the past 3½ years already has shown it to be an inflation hedge. Bitcoin began a 20-month surge in March 2020, shortly after the initial Covid outbreak in the U.S., rising by more than 1,100% at its peak on Nov. 7, 2021. Gold rose 9% over the same period.

That gain came “as the economy recovered and the Federal Reserve overstimulated the economy,” Pandl says. And the digital currency’s high arrived as the central bank said it would start to tighten monetary policy.

“This is exactly what we would expect from an inflation-hedge asset,” he says. “Outperformance when the central bank is too dovish and causing inflation, and underperformance when the central bank turns hawkish in an effort to bring inflation back down.”

NO: Bitcoin is speculative and volatile

The fundamental issue for bitcoin is what gives it value, Prasad says, and its only value is scarcity. In contrast to the dollar, which the Fed can create in infinite amounts, bitcoin has its 21 million cap.



Eswar Prasad

The idea is that something scarce will preserve its value better if the money supply increases, Prasad says. “But there is no intrinsic value for bitcoin, because it’s a purely speculative financial asset. There’s no valuation model,” he says.

True, he says, bitcoin is scarcer than gold—but bitcoin isn’t being used for much outside of speculative transactions, while “gold has some intrinsic value for industrial and jewelry usage.”

There are other issues that limit bitcoin’s value as a hedge, Prasad says. For one thing, the technology isn’t as reliable as it looks. “It’s supposedly a medium of exchange without a traditional intermediary like a bank,” he says. But “it’s volatile and inefficient in transactions. The blockchain system can’t handle a lot of bitcoin transactions at once.”

Swings in price are a big issue. “Bitcoin provides a pretty good return sometimes, but there’s the large volatility,” he says. “Given that it is a speculative asset, we have seen it behave like other risky assets. It can be much more volatile than stocks.”

Measured daily over the past three years, bitcoin put up a standard deviation of 3.4 from its average price—a measure of volatility, with higher being more volatile—while stocks were at 1.1 and gold just 0.9, Prasad says.

Consider bitcoin’s price swings since 2020. On March 8 of that year, bitcoin was trading at \$5,392. A little over a year later, on April 4, 2021, it had soared to \$60,205. Within three months, the price had dropped by almost half, then more than doubled about four months later. After more swings in between, on Oct. 3 of this year, the price stood at \$27,468.

“Bitcoin’s price fluctuations over the past year hardly lend credence to the view that it is an effective hedge against inflation,” Prasad says. “Rather, much like other risky assets, its prices seem to be influenced by macro factors, such as policy interest rates and liquidity conditions. But it is subject to much larger speculative swings in prices than many traditional asset classes.”

Those who bought bitcoin in the early years of its existence have made a fortune, Prasad acknowledges. But that has nothing to do with bitcoin being an inflation hedge. And “if you have timed your purchases badly over the past few years, you have lost,” he says.

Dan Weil is a writer in West Palm Beach, Fla. He can be reached at reports@wsj.com.

The Sam Bankman-Fried Trial

Coverage of the crypto exchange’s collapse and the trial of the FTX founder

SIGN UP FOR THE WSJ CRYPTO NEWSLETTER



What’s Happening at the Bankman-Fried Trial



Can Someone Lose Track of Billions of Dollars?



The SBF Trial: How We Got Here



Meet the Star Witness at the SBF Trial



Crypto Could Be a Mystery to Jurors in SBF Case



It’s Their Job to Put Sam Bankman-Fried in Prison



FTX Employees Found Alameda Backdoor Before Collapse



Podcast: The Trial of Crypto’s Golden Boy

Appeared in the October 9, 2023, print edition as ‘Is Bitcoin an Inflation Hedge? Here Are the Arguments on Both Sides’.

Next in Journal Reports: Investing Monthly