Cryptocurrency: An Introduction – Video Transcript

You’ve probably heard of Bitcoin. Launched in 2009, Bitcoin was the first cryptocurrency and remains the best-known. But there are thousands of cryptocurrencies today.

So, what is a cryptocurrency?

Cryptocurrency is a digital asset generally intended to support financial transactions. It's generally acquired and used online.

A central authority, like a government, does not control it. Instead, digital assets like cryptocurrency are built on a decentralized ledger technology called “blockchain.”

The blocks that make up a blockchain contain the transactional data associated with the cryptocurrency. Each block, as well as the overall chain, have built-in safeguards to prevent tampering.

Many cryptocurrencies, like Bitcoin, were created to operate like traditional currencies — just without any central governing authority.

Other cryptocurrencies were created, at least in part, to support the blockchain platform they are associated with. For example, the cryptocurrency Ether supports Ethereum’s blockchain platform — a platform that enables many other decentralized applications.

Unlike the U.S. or Canadian dollar, cryptocurrencies are not issued or backed by a government. In fact, cryptocurrency generally has no real intrinsic value, other than its use as an asset. Instead, its value is almost entirely based on the perceptions and expectations of those who use it. As a result, cryptocurrencies can be highly volatile, with sometimes dramatic price fluctuations.

Some cryptocurrencies called stablecoins try to reduce price fluctuations by attempting to peg their value to a government-backed currency or to some other benchmark, or by using algorithms to control the supply of the cryptocurrency.

Cryptocurrency can be a high-risk, highly volatile asset. So should you even consider including cryptocurrency in your portfolio?

It depends not only on your timeframe, personal goals, and risk tolerance but also on your personal opinion of the future of cryptocurrency and the role it might play in the global financial system. It is definitely not appropriate for all investors.

Cryptocurrencies are not a traditional investment, are highly speculative, and carry higher risk and volatility. Cryptocurrencies are not typically subject to the same reporting and data integrity requirements that apply to more traditional investment products. The IRS is treating cryptocurrency as an asset subject to capital gains taxation rather than as a currency. The reserves of stablecoins may not be subject to rigorous audits, and the quality and quantity of collateral may not, in some cases, correspond to the issuer's claims. Stablecoins that maintain their value through algorithmic mechanisms are potentially subject to failure due to market pressures, operational failures, and other risks.

Centralized cryptocurrency exchanges are not currently regulated by any government agency, such as the Securities and Exchange Commission (SEC) or Commodity Futures Trading Commission (CFTC). They rely on a third party or intermediary account to monitor and confirm that all transactions are secure. With a centralized exchange, traders deposit their funds into an intermediary account for a specified period. Centralized cryptocurrency exchanges give their platforms greater control over their users, and could be susceptible to fraud or compromise. Decentralized cryptocurrency exchanges, on the other hand, use peer-to-peer systems that give users full control of their accounts.

All investing involves risk, including the possible loss of principal, but new technology ventures are especially risky. Some of the blockchain projects in development may turn out to be viable and profitable, but many others could fail. It is important to be skeptical when evaluating a claim made by a company about its entry into this arena. Steer clear of unsolicited and Internet-based investment offers — and never wire money to pay for an offer or service.