Cryptocurrency

A quick guide to usage and risks

The tremendous surge in the price of certain cryptocurrencies such as bitcoin have attracted the attention of the news media and many investors, including some Vanguard clients. Need a primer on bitcoin and other cryptocurrencies? Read on for quick answers to your questions.

What are cryptocurrencies?

Cryptocurrencies, invented in 2008, are a digital (or virtual) means of facilitating online, peer-to-peer transactions.

How many cryptocurrencies are there currently?

6,700 Today, there are more than 6,700 cryptocurrencies (as of January 2021).

Among the largest are bitcoin, Ethereum, XRP, Tether, and Litecoin.

How are cryptocurrencies used?

A cryptocurrency is not a commodity, asset class, or currency, but shares some characteristics with them. Individuals can use cryptocurrencies to buy goods and services.

What is the technology behind it?

Blockchain is the technology underlying cryptocurrencies. It is a database or ledger distributed across a peer-to-peer network that supports all types of transactions.

Where are cryptocurrencies stored?

Cryptocurrencies are stored in a "digital wallet" on a holder's computer or phone, or in the cloud. The wallet serves as a virtual bank account.

How do you buy and sell cryptocurrencies?

Cryptocurrencies can be bought and sold directly on crypto exchanges, crypto brokerage platforms, and crypto kiosks.

How do cryptocurrencies compare to regular money?

1. They are not a universally accepted medium of exchange.
2. Their price volatility makes them impractical for many transactions.
3. They have no central authority to manage them.
4. Bitcoin's supply limit is set to 21 million.

(Read on for investment considerations.)

Is there a role for cryptocurrencies in a well-balanced investment portfolio?

For investors, adding cryptocurrency exposure to their portfolio would mean reducing their allocation to traditional asset classes, such as stocks, bonds, and cash—the building blocks of a prudent, well-balanced investment program.

What are the five biggest risks of investing in cryptocurrencies?

1. **Volatility.** Cryptocurrency prices are subject to wide fluctuations.
2. **Liquidity risk.** Cryptocurrencies may be difficult to liquidate quickly at a reasonable price.
3. **Lack of regulation.** Cryptocurrencies are not overseen by any government or central bank.
4. **Pricing variability.** There is no central market for pricing.
5. **Cybersecurity risks.** Exchanges and platforms are subject to breaches.

Cryptocurrencies: The bottom line

Vanguard cautions against speculating in bitcoin and other cryptocurrencies. Unlike stocks and bonds, cryptocurrencies lack intrinsic economic value and generate no cash flows, such as interest payments or dividends.

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All investing is subject to risk, including the possible loss of the money you invest.

FAVBITO 032021