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April 13, 2018

Focus on Funds: Understanding Cryptocurrencies and Investing

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There's a lot of talk about investment in cryptocurrencies—but do they actually affect the average investor? In the April 13, 2018, edition of *Focus on Funds*, ICI Chief Industry Operations Officer Marty Burns details the barriers to fund investment in such currencies, and what protections will need to be in place before the time is right.

Transcript

Stephanie Ortbals-Tibbs, ICI director of media relations: You've probably been hearing quite a bit about Bitcoin. So, is it in your 401(k), your ETF, your mutual fund? Well, not quite yet. I learned a lot about the investment issues around cryptocurrency speaking with Chief Industry Operations Officer Marty Burns.

Marty Burns, ICI chief industry operations officer: The Bitcoin today, and cryptocurrencies generally, are not regulated. So, they are not issued by any government; they don't have any legal standing. They are really a consensus product, which means the buyer who is willing to pay for it and the seller who is willing to take what the buyer will take, that's what establishes the transaction for cryptocurrency. No regulation: no 401(k).

Ortbals-Tibbs: So if they're not going into mutual funds or ETFs yet, what would need to happen in order for mutual funds and ETFs to start considering these cryptocurrencies, and are there other ways we might start to see them work their way into our portfolio?

Burns: Until there is more regulation around it, and there's some real structure and direction from the regulators—as to whether they're an investment, whether they're a currency, whether they're an asset—it's not possible for the '40 Act funds to draw that in, because they don't really fit as a potential for the portfolio investment.

Ortbals-Tibbs: As you look in the crystal ball, what else would you have mutual fund and ETF investors, and those in the industry, be watching over the next six months to a year?

Burns: The biggest key for cryptocurrencies as an investment is, really, valuation. As we sit here today, it really resembles more of a barter system—again, what one person is willing to sell for, and what the other person is willing to pay. So it's very difficult for a mutual fund to create any notion of a consistent valuation. And remember, the boards have to approve valuation processes, so it has to have some structure to it.

That valuation is key, and that's really the first step forward that will have to occur before the mutual funds will really be able to use cryptocurrencies in their portfolios as an investment.

Ortbals-Tibbs: So I guess, depending on the day, you could almost call that the $64,000 question, or the $6,400 question, or the $64 question?

Burns: That sort of fluctuation and volatility is very difficult for a '40 Act fund to manage in its portfolio. Not impossible—there are other investments that do fluctuate—but it's very difficult. And without that regulatory structure, and without that structure for valuation, it's not an opportunity, as we sit here today, for funds to use.

Ortbals-Tibbs: That's true on this side of the ledger. What your folks are looking at a lot are the operational possibilities.

Burns: Correct. There's efficiencies that can be gained from the use of cryptocurrencies, and that's really a conversation that is beyond the investment. That really gets into the enhancements and efficiencies and technical aspects of the cryptocurrencies that can benefit mutual funds once they become a regulated entity that can be used for settlement.

Additional Resources

- From the *Investment Company Fact Book*: Core Principles of Mutual Fund Regulation
- FAQs: The Differences Between Mutual Funds and Hedge Funds
