

Are Hedge Funds Playing Greater Fool?

Stockholm (HedgeNordic) - The price of bitcoin has surged more than 600% year-to-date, with the world's largest cryptocurrency regularly setting new all-time highs in recent weeks (a fresh all-time in the \$7,800s was reached earlier this week). Market observers say institutionalised money movers, many of the hedge funds, helped fuel the surge in the digital currency's price.

Bitcoin has outperformed all traditional currencies each year since 2011, except for 2014, which has fed an insatiable appetite for bitcoin from the traditional financial industry. Institutional investors are increasingly looking to hedge funds and investment firms to capitalise on the ever-increasing bitcoin price.

Bobby Cho, the head trader at large liquidity provider in cryptocurrency markets Cumberland Mining, was recently quoted in a New York Times article as saying that institutional investors accounted for most of their business after years of hesitation on the part of big-money investors. "The vast majority of the trading we do is with institutions," Cho said. "The education and research have turned into real-life activity," he added.

Fintech analytics firm Autonomous NEXT counts around 130 hedge funds that trade cryptocurrencies, with most of these funds having been set up over the last year alone. Even traditional hedge fund vehicles have been stocking bitcoins in their portfolios. For instance, fund manager Bill Miller, a former manager of the Legg Mason Value Trust mutual fund, has approximately 30% of a \$154-million-hedge fund's assets in bitcoin.

However, the entrance of big-money investors into the cryptocurrency space are creating new risks for bitcoin, according to market observers. Kevin Zhou, co-founder of crypto trading fund Galois Capital, said a single fund's cashing out could trigger a sharp drop in bitcoin price due to the relatively small size of the market. "You could get a possible run on the bank if one large investor withdraws and that causes the price to tank," said Zhou. "That could cause a cascade of withdrawals."

Could it be that new crypto-focused hedge funds and other vehicles are playing the greater fool game? Investors could be buying bitcoins on the assumption that they will sell later to a more unsuspecting investor at a higher price. Bitcoins may have a future still; they actually could end up trading up much further. But unless the fundamental underlying demand grows (with people using the currency to transact for other reasons than speculation) there are reasons to believe a lot of hedge fund players, large-scale investors, and individual investors alike will be disappointed.