

Transcript

The Ideas Exchange

Episode 43: An introduction to Bitcoin ETFs

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**Rory Cunningham (00:00):**

Welcome to The Ideas Exchange by ASX, connecting you with investment experts, market updates and ideas. I'm Rory Cunningham, senior manager of investment products at ASX, and this is our regular podcast covering everything from investment trends through to different ways to invest using a variety of products.

**DISCLAIMER(00:19):**

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**Rory Cunningham (00:47):**

Welcome to The Ideas Exchange, I'm your host, Rory Cunningham, from ASX. Today, we welcome Jamie Hannah, who is deputy head of investments and capital markets at VanEck. Jamie has a wealth of experience in financial markets, and I'm looking forward to our discussion today. Jamie, thank you for joining us.

**Jamie Hannah (01:05):**

You're welcome.

**Rory Cunningham (01:06):**

Today, we're going to be discussing Bitcoin. I'm very excited for this discussion. Before we get into it though, and to provide some context for our listeners, I thought I'd just mention a couple of things. Firstly, VanEck recently launched a Bitcoin Exchange Traded Fund, or ETF, on the ASX. Their launch on ASX follows similar ETF listings from VanEck and other investment firms on exchanges around the world over the last few years providing investors seeking exposure to Bitcoin and other cryptocurrencies with convenient access point via ETFs. As we sit here today, the price of Bitcoin is currently trading around 60,000 US dollars and has a market cap of around 1.2 trillion US dollars. Now, Bitcoin's price is renowned for being highly volatile, but despite that, over the last decade, it has become the top performing asset of any class, including stocks, commodities and bonds. 10 years ago, just for

reference, its price was around 500 US dollars. With that as the backdrop, and before we get into the details of Bitcoin, Jamie, maybe just for our audience, could you briefly introduce yourself and also share how you got involved with VanEck?

**Jamie Hannah (02:30):**

Definitely. Well, thank you for having me today. I guess I've been in the industry now for more than 20 years, and I'm talking the finance industry. I originally started as a stockbroker back in the late 90s in Australia where I was selling shares on the ASX through mom and dad investors, but I decided I wanted to move into the institutional space. I packed up the bags and moved to London and spent the next decade working in investment banks in London and New York on the large trading floors, primarily working in equities, so working a lot among all the global share markets around the world. An opportunity came up to join in Europe, a start-up firm, which was launching ETFs.

**(03:14):**

These were new, 12 years ago, 15 years ago. They were very much a start-up. I was part of a company called Source, and we launched over a hundred ETFs in Europe, but I'm Australian and I was getting a little bit sick of being in dreary London, so I packed up the bags and moved back to Australia, and VanEck had just set up here in Australia. They just launched their first fund. They had \$6 million under management. They were after some experienced people and I was obviously, experienced in the ETF market. Since I started there in 2014, we've now gone from \$6 million to over \$18 billion in Australia and more than 40 ETFs, but by and large, I'm a traditional asset manager, so I've always managed shares, bonds, and commodities. Crypto assets are a completely new asset class for us.

**Rory Cunningham (04:05):**

Incredible timing. Actually, 10 years ago, the ETF market in Australia was quite small, and as we sit here today, 10 years later, we're now at just over \$200 billion in the entire Australian ETF market. You've seen an incredible rise over that period, Jamie. Now, taking us into crypto assets, maybe firstly, do you want to just give us a bit of a brief history of VanEck's experience in crypto assets?

**Jamie Hannah (04:32):**

Yeah, look, VanEck had been operating in the US since the 1960s, in traditional assets, especially in equities. Around 2017, Jan VanEck, the owner of VanEck, really got involved in the crypto-sphere and saw opportunities there. We were one of the first, well, we were the first in the US to apply to the SEC in the US for a spot Bitcoin ETF to be listed and we first started managing crypto assets in 2017. Fast forward to where we are today, we have over 20 crypto funds around the world, in US, and in Europe, managing over \$2 billion in crypto assets. As a firm though globally, we're managing

over \$100 billion. Whilst it is only a small part, we're certainly leaders in that sphere and Jan VanEck has been potentially one of the leading advocates for the industry globally.

**Rory Cunningham (05:23):**

Okay, excellent. All right, well let's get into Bitcoin because you have recently launched a Bitcoin ETF on the ASX. Now, for beginners, I'm sure all of our listeners have heard of Bitcoin, but from your perspective, do you want to describe what is Bitcoin for our listeners?

**Jamie Hannah (05:39):**

Yeah, look, I mean Bitcoin is one of the most talked about things in the world, I should say. It was originally set up in 2009 by an unknown pseudonym known as Satoshi Nakamoto, and it was essentially set up as a cryptocurrency for peer-to-peer electronic cash that could be used over internet to pay for goods and services over the internet. The key part of Bitcoin was that it wasn't controlled by an individual country. Look, where it is now is that Bitcoin is synonymous with not necessarily purchasing goods around the world, but it is known as a potential new asset class. The thing with Bitcoin is that every transaction is recorded on a blockchain and we don't have to go into that, but every transaction is recorded and everyone can see the transactions. It's completely transparent, it's not run by any country and it's essentially meant to replace physical cash.

**Rory Cunningham (06:33):**

Thanks for that description. Now, as I mentioned, Bitcoin can be volatile in terms of its price movement, however, it has shown strong historical performance. Why is it that you think investors purchased Bitcoin?

**Jamie Hannah (06:48):**

Yeah, look, I mean, you're right, it has shown extremely strong performance since it launched in 2009, and you did mention the volatility. I need to point out that it is extraordinarily volatile. It's generally been seen as a momentum asset if you really want to break it down. That basically means that the price moves because there's a demand for the asset. With high demand, more people are wanting to buy it, more people are thinking about it. It's become quite just a thing talked about in the general public. What you're seeing is as more and more people hear about it and want to get some, the momentum builds up and people tend to buy it. It's generally just been driven by momentum as more and more people hear about it and buy it. Now, the momentum is no doubt the strongest driver, but it was, as I said, originally set up as a substitute for fiat currency.

**(07:38):**

There is still some people who can buy and sell things using Bitcoin. One of the other things is it offers excellent diversification. As an asset class, it's highly uncorrelated to other assets, so it doesn't move as equities or shares

go up or bonds go up and down, it doesn't move in the same direction. It's a very good diversifier for a portfolio and it's extremely liquid. The turnover numbers in terms of Bitcoin are astronomical, certainly higher than most shares around the world. Let's be honest, if you held Bitcoin from inception, you're probably sitting on a beach somewhere with your feet up enjoying life, but the volatility would've killed most people long before then and they would've sold, so very few people have held since inception.

**Rory Cunningham (08:22):**

A few key takeaways there. First of all, some investors are buying Bitcoin for that swinging volatility or to get in during periods of momentum, be that momentum up or momentum down. It's a liquid asset class, it's a liquid currency, which means that for investors, they can feel confident that they're going to get in and out without changing the price intraday. Also, not to mention, it can be used for currency for transactions of goods and services, though I suppose we've seen a little bit less of that relative to the original stated use case of Bitcoin, which we'll touch on in a little bit. All that talks to, I suppose, the demand side for Bitcoin. Let's talk about the supply side and the limited supply of Bitcoin. Can you elaborate on the limited supply side for Bitcoin?

**Jamie Hannah (09:16):**

Yeah, look, I mean, there will only ever be 21 million Bitcoins in circulation. At the moment, there's somewhere around 19.8 million Bitcoins currently available to purchase and buy. What this does, it creates I guess scarcity, and anything that's scarce and is in demand will potentially have its price driven up and that's what we've seen. However, we've seen extreme volatility at the same time. The fact that there's only a limited supply of Bitcoin means that everyone can't have as much as they want. To be fair, there's over a trillion dollars' worth of value in it, but potentially no one can control the complete supply of Bitcoin. Now, things can move it though. Let's use an analogy from the last couple of weeks. The Republican party have come out and said that they intend to buy if they get into power 1 million Bitcoins.

**(10:08):**

Now, that's 5% of the outstanding amount of Bitcoin. Now, it opens up many questions. One, how do they get a million Bitcoins and what are they willing to pay for it? Two, what are they going to do with it? Presumably, they just sit on it, which means it removes 5% of the Bitcoin flow from circulation. Then if the US are doing it, would other central banks around the world also want to hold something like this? It opens up plenty of questions that if there's only 21 million of them out there, what is the demand and how much are people willing to pay for something that is somewhat scarce?

**Rory Cunningham (10:42):**

When you read about the investment case for Bitcoin from commentators generally in the market, some of the comments that come back are around

that Bitcoin can serve as a potential hedge against inflation. Do you have any comments on that position?

**Jamie Hannah (10:58):**

Yeah, look, Bitcoin is decentralized, meaning it's not controlled by a country, and that generally means that it's not being controlled by the central banks that set the underlying monetary policy or the interest rates. Therefore, it would mean it's not subject to inflation, but I don't agree with that, to be fair. I think that it doesn't warrant that Bitcoin and inflation are inherently linked. I think there is no links. I think that Bitcoin has only been around since 2009. It's been highly volatile, and yes, it's been going up as inflation has been going up, but I don't believe there's any real research or long-term history that can be relied upon to say that it is an inflationary hedge. There's certain research papers that are out recently and one of them highlighted that actually, central bank policy, the movement of interest rates by central banks does impact the price of Bitcoin. A lot of the thesis behind what they're saying, I'm not sure is necessarily true. I would say the jury is out if that's actually true. I tend to say that it's a very weak case at the moment.

**Rory Cunningham (12:06):**

Okay, no problem. Now, as I mentioned, one of the original use cases for Bitcoin was to use it for payments. Now, before coming here, I bought a coffee and I don't know, a coffee shop in Sydney that will accept Bitcoin as payment for a coffee. I was recently over in the US and Canada and I would have similar problems trying to pay for any goods and services over their physical goods and services, maybe not digital goods and services. In relation to payments, I mean to what extent is that payment use case for Bitcoin occurring in society?

**Jamie Hannah (12:42):**

Look, you've already identified it, it is very low. It can be used for goods and services. There are people who will accept it. There are people who have been actively trying to promote the use of Bitcoin in society, but I think it's extremely limited in most countries around the world. Some countries, and I won't name them, you don't have to look on the internet, but some countries with unstable currencies where they don't trust their central banks and they're unhappy with how their currency moves against US dollar, for example, they have tended to use Bitcoin a little bit more for day-to-day purchasing.

**(13:19):**

Certainly, the developed world doesn't use it a lot, but if you're under a currency which is more volatile than Bitcoin, then it's highly likely that you can probably use something like Bitcoin because it offers a little bit more stability and also a way to get out of your local currency. One thing with Bitcoin, it's divisible by eight decimal places, which means that it can go down a fraction of a cent. It is highly divisible, it's just not widespread. I don't know

when it will ever become widespread or if it even will. I think we just need to watch and wait, but I'm certainly not spending Bitcoin for any purchases at the moment either.

**Rory Cunningham (13:54):**

Let's talk a little bit about risk, the risk of investing in Bitcoin. From your perspective, what do you think investors should know about the risks of investing in Bitcoin?

**Jamie Hannah (14:03):**

Look, I mean, it's imperative to understand that the volatility of Bitcoin is extraordinarily high and that you can actually lose money on Bitcoin. If you take a bond or an equity, there's at least a company behind the asset. The company can go bust through poor operations, but there's at least some activity behind it. We talk about the performance of Bitcoin a lot, but let's put it in context. Over the last 11 years, if you compare Bitcoin to every single other asset class, we're talking gold, we're talking the ASX 200, we're talking the S&P 500, we're talking bonds, we're talking houses. Over the last 11 years, it has been the top asset performer eight of those years.

**(14:42):**

On the three years when it wasn't the top performer, it was the worst performer out of all of them. On those three years, it fell more than 60% each year. This is extraordinarily big volatility, and that's only just the tip of the iceberg, really. Because there are just a lot of risks and things like there isn't a centralized exchange for Bitcoin like the ASX, there's regulatory risks. For example, Bitcoin is illegal in China. There's also safekeeping risks, how do you safe-keep your private key and your assets? It keeps going, and so what I'm really highlighting here is that Bitcoin as an investment is about as risky as you can get.

**Rory Cunningham (15:23):**

All right, heard loud and clear. Thanks, Jamie. Let's talk about how to access Bitcoin. As I mentioned in the beginning of this discussion, we've seen an increase in the number of ETFs that offer access to Bitcoin and other cryptocurrencies, which is improving accessibility. Let's spend a bit of time delving into the different ways in which investors can access Bitcoin. Now, I suppose in relation to that, if buying Bitcoin directly, there's challenges associated with storing that Bitcoin. Can you just talk us through that?

**Jamie Hannah (16:03):**

Look, let's take a step back. There's two main issues here. One, is that there is no standard exchange, and I touched on that before. When you're buying and selling Bitcoin, there's nothing like the ASX. In fact, each Bitcoin exchange that you go to, and I won't name some, but they're all independent and many of them are not regulated. Hence, you can't ever guarantee a fair price or your cost or your safekeeping. A lot of that really depends on your own

investigation into it. Then that's just the execution part, then there's the storing of the Bitcoin. It'll basically involve you either keeping the private key yourself, and if you lose that or it gets stolen, it's essentially unrecoverable. It's gone forever. Now, if you then decide to rely on the exchange that you use to store your Bitcoin for you, then you have some counterparty risk against that individual exchange, and you also still need to maintain passwords. For all intents and purposes, it can still be hacked because it's still connected and online in what's called a hot wallet.

**Rory Cunningham (17:05):**

Do you just want to touch on what counterparty risk means just for the benefit of beginner investors?

**Jamie Hannah (17:10):**

Depending on how the exchange is structured, if they hold your Bitcoin, there's a chance that if they went under or they were unscrupulous, there is a potential that you could lose your assets, that they could either be stolen, hacked, or otherwise, lost.

**Rory Cunningham (17:29):**

Now, how do Bitcoin ETFs simplify the process of investing in Bitcoin?

**Jamie Hannah (17:33):**

The Bitcoin ETF essentially brings institutional-grade security execution and management to the Bitcoin holding. For example, when the Bitcoin is traded, normally, if you were doing it through an individual exchange, you would do the execution yourself and the spreads that you pay on the spot price of Bitcoin are one to 2%. Some of them are extraordinarily high. When we execute, we don't execute through one exchange. When VanEck goes and buys the Bitcoin, we will go out to a whole entire panel of Bitcoin exchanges, we call them liquidity providers, and we ask them for a set rate at a set time of the day. We're paying against the price of Bitcoin a price, which is about 0.05 of a percent. Our execution costs are minimal compared to what any individual would pay. Then if we look at it, secondly, we're able to store the Bitcoin considerably more securely in what's known as cold storage.

**Rory Cunningham (18:33):**

You want to touch on what cold storage is? You also mentioned what hot storage is, so maybe compare and contrast the two.

**Jamie Hannah (18:39):**

Yeah, definitely. Cold storage is where the Bitcoin private key, which is the ownership of the asset and the password I sent essentially for storing your holding is in a secure location, which is not connected to the internet, which means that nobody can hack your underlying Bitcoin holding because it's in a physical location and it requires multiple access security obligations to

actually get into it. Now, obviously, it's in a physical location, so worst-case scenario, someone could actually access that location, but they would be unable to assemble the private key because nobody has the private keys. Without getting too technical, it's all encoded through this, I guess a thing known as the hardware security modules and nobody has an individual hardware security module which has the entire key. It needs to be put together and someone needs to access the location to actually draw your Bitcoin out of cold storage.

**(19:40):**

Now, it's essentially about, it's similar to way they keep nuclear codes in the US, so it's about as safe as we can make it. To move it from cold storage is where the vast majority of our Bitcoin is stored. It's as secure, as I said, we can make it, but when we transact, we need to move it out of cold storage into a hot wallet. Now, hot wallet means it's connected to the internet so that you can settle your transaction and sell or buy new Bitcoin. Most individuals, when they buy Bitcoin, it will still be in a hot wallet. Most, if not, nearly all the retail products will keep it in a hot wallet, which means it's connected to the internet at all times and it's not in cold storage.

**Rory Cunningham (20:28):**

How do Bitcoin ETFs address concerns about security, which you've touched on already, but then also regulatory oversight compared to direct ownership?

**Jamie Hannah (20:40):**

I mean, look, the main point here is that everything to do with ETFs is regulated, which adds extra layer of protection. VanEck, we're regulated. The ASX, they're regulated. Our custodian, in this case, is Gemini. They're regulated in the US. It means that there's strong governance and controls in place, and more importantly, there's accountability. It's important to note that some exchanges that you buy Bitcoin on are regulated, but there's more than a hundred exchanges out there. Some of them are frankly dodgy and a terrible way to invest money. Some of them are obviously legitimate and regulated, but they still don't offer the same protections and levels of regulation that we're able to offer through the ETF. Not to mention, we also have insurance in place, both at VanEck and Gemini, the custodian, who hold the Bitcoin. It's just, I guess more secure for any investor looking to enter the Bitcoin space. We, as already existing custodians and money managers across traditional assets, we have knowledge of this type of safekeeping and how the regulatory environment works, so we're bringing institutional knowledge and experience to the Bitcoin space.

**Rory Cunningham (21:59):**

Thanks for that deep dive on the differences between accessing directly versus the ETF. Let's touch a little bit more on VanEck's role in the Bitcoin ETF market. Could you share more about VanEck's Bitcoin ETF offering and what you think makes it unique versus other offerings in the marketplace?



**Jamie Hannah (22:18):**

Look, it was the first Bitcoin ETF listed on the ASX, and it's certainly the most cost-effective. We charge 0.49% per year. It has all the benefits which I've already outlined, which is institutional-grade custody and a lot of everything that we've just addressed. What it really does is it just allows ordinary ASX investors who already have a broken account to be able to purchase them like they would any normal share. You can get access to Bitcoin now through just buying VBTC on the ASX, and it will then go on your HIN, so you can see it on your CHESS statements.

**(22:55):**

What we also focus on, like any ETF, is we focus on the bid-ask spread, which is the price you're paying on screen compared to the price of Bitcoin. We're monitoring that live. We're ensuring that the price of Bitcoin that you are purchasing at on the ASX is comparable to the price of Bitcoin that you would be getting if you'd purchase at the spot rate. We're also making sure that the difference between the bid and the ask is tight. On the last ASX report, it was under 0.2 of a percent. You're essentially, in our opinion anyway, getting the cheapest option to buy Bitcoin through your normal broken channels with institutional-grade safekeeping and management.

**Rory Cunningham (23:35):**

Now, it's not an easy process bringing an ETF to market, and it's definitely not an easy process in bringing a Bitcoin ETF to market. Do you want to talk about some of the challenges that you faced as an organization and maybe even in your role in doing that?

**Jamie Hannah (23:51):**

Look, definitely. As I said, we manage over 40 ETFs in Australia, and I've launched over a hundred in Europe, but this was far and away the most difficult product I've ever been involved in, essentially because it is a new asset class, and that was debatable. Is it an asset class? Essentially, the initial bit was ASIC creating some policy framework in regard to this. We had meetings with ASIC to help them on the education front and how spot ETF might work, they then went away and created some policy. It was then up to the ASX to then develop their own internal framework requirements after ASIC gave INFO 225 and information on how this could work. ASX then went away to develop their own framework, and then we then had to go away and work out our ability to structure a product, which met all of the requirements.

**(24:50):**

It was a big work in progress over many years, and a lot unfolded in the crypto space over those years when we first started. There was FTX, there was Terra Luna. There was a lot of different, I guess, headwinds to actually getting anything started, but there's no doubt that in January this year when

the US SEC allowed a Bitcoin ETF to be launched, that was kind of the catalyst. I think that was enough to get the regulatory framework in Australia over the line. After the US happened, things continued at quite a fast pace for six months, and we eventually launched this Bitcoin ETF in June this year.

**Rory Cunningham (25:28):**

Being a new product investor, education is key and financial advisor education, how does VanEck help ensure that these ETFs are accessible and understandable for investors?

**Jamie Hannah (25:40):**

Look, I mean, we try to educate as much as possible. Things like this podcast, for example, we do webinars. Obviously, our online website as well, but we're also open to face-to-face discussions. You can always call up. There's a lot of information out there, let's be honest, on the internet, but we as a regulated institution, we're bound by tight regulations and what we can and can't say. Everything that we have and all the information that we provide, we have to be able to substantiate our information. We can't just sprout random information out there, otherwise it goes against all of our compliance obligations. Like all other ETFs, education is key, and we try to produce as much educational material as we can to inform investors.

**Rory Cunningham (26:24):**

Let's talk a little bit about the future of the Bitcoin ETFs. How do you see the Bitcoin ETF market evolving over the coming years?

**Jamie Hannah (26:31):**

Look, I think it's just becoming more institutional. If anyone asks where the price of Bitcoin goes, look, I don't really have a comment on that. We know it's volatile. My biggest observation, bearing in mind for more than 20 years, I've been working in shares and bonds and commodities. What would normally be considered traditional assets? One of the things I've noticed over the last four to five years that I've been involved in the crypto space and really helped this product come along is that I've met with, I guess, some of the top people in the crypto industry, from custodians to exchanges to regulators. The one thing that I have noticed is that nearly everyone involved on the exchange side, on the safekeeping and custody side, most of them, you can take this however you want, but most of them are ex-investment bankers. A lot of them have jumped over from investment banking roles and brought their institutional knowledge and experience, control environment, compliance frameworks, to the crypto industry.

**(27:33):**

The only reason why we're sitting here talking about this now is because it was originally just a FinTech, quite a niche asset crypto in particular. The reason why we're all talking about it is because a lot of these investment bankers and experienced financial professionals have made it more popular.

We started talking about it from 2016 onwards, '17 onwards, and that's because these people made the jump, institutionalized it, brought in their marketing, brought in their salespeople, brought in the backend operations. From that perspective, it's institutionalized way faster than anyone imagines. A lot of people have generally thought of Bitcoin as getting away from the governments and getting away from the regulators and all that type of stuff. I have to be honest, the people behind the exchanges and behind the Bitcoin industry are the same people who are behind financial products in the big investment banks in the past. For good or bad, however you see that, it's certainly one of the observations I've known, and I think that's probably going to continue.

**Rory Cunningham (28:38):**

Any final thoughts for investors that are interested in Bitcoin ETFs?

**Jamie Hannah (28:42):**

I think it's vitally important that you understand the risks, that you don't put too much of your money in any single Bitcoin investment, and that goes for any form of investment and really to have a well-diversified portfolio. Because certainly, there are risks in the market and you don't want to put too many eggs into one basket.

**Rory Cunningham (29:00):**

Excellent. Jamie, thank you very much for joining us today.

**Jamie Hannah (29:03):**

Thank you very much.

**Rory Cunningham (29:04):**

If you'd like to know more about VanEck, head to their website where you will find a lot of education material. Thank you to all of our listeners for joining today, and we look forward to tuning in next month on The Ideas Exchange.

**Blog(29:16):**

Are you keen to learn more? Why not visit the ASX blog? [asx.com.au/blog](http://asx.com.au/blog), for a wide range of articles, videos and insights from ASX experts, listed companies, and investment professionals.