

# What is Bitcoin? Understanding Cryptocurrency

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At Financial Harvest Wealth Advisors, we sometimes get questions from our clients who are curious about Bitcoin and want to better understand cryptocurrency. Should they be investing in it? Is it safe? And the question we're asked most often, "What is Bitcoin and how do Bitcoin and other cryptocurrencies even work?"

Let's start with the basics.

## What is Cryptocurrency? What is Bitcoin?

Conceptualized as far back as 1996 by the National Security Agency, cryptocurrency was first created in 2009 in the form of Bitcoin. In the next few years, Litecoin and Peercoin followed and since then, distinctive cryptocurrencies have streamed forward, now totaling more than 6,000 unique currencies, with new cryptocurrencies being added all the time.

**"CRYPTOCURRENCY"  
IS A COMBINATION OF  
THE WORDS  
ENCRYPTION AND  
CURRENCY.**

Systems of cryptocurrency are defined by a set of conditions that generally include that it does not require a central authority, that it follow its own uniquely pre-established guidelines, and that it can be owned, and the ownership can be changed transactionally. Bitcoin, as an example, is entirely decentralized, with no person, bank, or government backing it.

*More importantly, cryptocurrencies are never physical. They exist only as computer code—a chain of code that lives on a computer.*

The process of decryption of the blockchain of code to earn a Bitcoin requires both an enormous investment of time and mental resources, as well as the use of hundreds or thousands of hours of computer time, all processed through massive computer grids.



Bitcoin specifically has a threshold of 21 million “coins”. Bitcoin “miners” compete, pursuing these coins using thousands of computers computing complex math equations to solve a blockchain. Once solved, the miner, which is typically a corporate organization that has the capital to front the costs of mining, is then rewarded with one of the 21 million Bitcoins. The coin can then be held by the mining organization or sold in the marketplace.

## Deeper Dive on the Challenges of Bitcoin and Other Cryptocurrencies

Bitcoin, and all cryptocurrencies, have inherent challenges. The first hurdle with Bitcoin investing comes with achieving decision making confidence in an investment vehicle that is both abstract and complex.

Other measurable challenges include:

### 1 - Competition.

With thousands of cryptocurrencies in existence, and more becoming available all the time, the competition to be the most popular and thereby the most valuable is tremendous and constantly in flux. Although Bitcoin, primarily by virtue of being the first cryptocurrency, currently dominates the field, that positioning could change at any time.

### 2 - Theft and Loss.

Estimates show that approximately 20 percent of cryptocurrency owners have lost access to their computer-based currency through the loss of a password, username or other user-error challenge. Likewise, ownership of cryptocurrency puts your computer at higher risk of being hacked, and your currency stolen.

A [New York Times](#) article published earlier this year, stated: “Bitcoin owners who are locked out of their wallets speak of endless days and nights of frustration as they have tried to get access to their fortunes.”

The article goes on to add, “The quandary is a stark reminder of Bitcoin’s unusual technological underpinnings, which set it apart from normal money and give it some of its most vaunted — and riskiest — qualities.”

## 3 - Energy Consumption / Practicality.

Envision warehouse-sized facilities stacked wall-to-wall, floor-to-ceiling with computer processors that all demand energy to run, plus constant cooling and temperature control. A May 2021 [Fortune](#) magazine article cites a Bank of America study that reported, “Mining the currency emits more CO2 than the whole of Greece. And that could worsen. If the price of Bitcoin were to rise to \$1 million, BofA calculates, the digital currency could turn into the fifth largest CO2 emitter in the world, surpassing Japan.” For further perspective, consider that the energy consumption of Bitcoin alone is rapidly escalating, growing over 200% between 2018 and 2020.

## 4 - High Transaction Costs to Convert to Currency.

If you own a Bitcoin you want to convert to U.S. dollars, or want to sell your Bitcoin to someone else, you’ll face transaction fees in the forms of commissions, transfer of funds fees, and a bid-ask spread. Even using your Bitcoin can be challenging. Only a narrow selection of companies accepts Bitcoin as payment and those that do usually confine it to online transactions only. Even when you hear headlines, such as, “Burger King accepts Bitcoin,” a little research reveals that it is only for a specific chain of Burger King restaurants in Venezuela, and likely done as a way to garner publicity.

# 5 - Volatility

This is the big one. The chart below shows the value of Bitcoin in April at around \$60,000, dropping down to around \$30,000 a month later, and as of earlier this month sitting at about \$45,000.

## PRICES CHANGE BY THE SECOND.



Cryptocurrency volatility as shown in 2021 year-to-date bitcoin price chart.

# 6 - Government Regulation.

Currently, only El Salvador accepts Bitcoin, and there are multiple concerns internally and externally of the country of its recent acceptance as legal tender. No other government in the world backs any cryptocurrency at all. Until that changes, Bitcoin and all other cryptocurrencies will suffer from a lack of regulation. China, is taking an aggressive position to discourage cryptocurrencies, having earlier this summer banned all crypto mining within the country,

Only weeks ago, US Securities and Exchange Commission (SEC) [Chairman Gary Gensler](#) described the cryptocurrency marketplace as a “Wild West” and stated, “This asset class is rife with fraud, scams and abuse in certain applications.” Addressing a global conference, Gensler added, “We need additional congressional authorities to prevent transactions, products and platforms from falling between regulatory cracks.”

Worth noting: gains from the sale of cryptocurrency are considered, by the IRS, like any capital gains from other assets, and as a result are typically taxable



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# Bitcoin as an Investment

When considering cryptocurrencies as an investment, you will want to evaluate them as you would any other investment, looking at your expected return. For example, your expected revenue from stocks, real estate, or bonds are your anticipated future profits, dividends, rent, interest cashflows or other income stream potentially created by these assets.

Instead, Bitcoin is more comparable to a baseball card. The card has a value only if, and for as long as, there is someone else willing to purchase it. What that value may be is controlled entirely by the purchaser. But the card itself does not produce any cash flow or utility, nor can anyone reliably project the card's value in the future.

**ARE THERE ANY  
FUTURE CASHFLOWS  
OR INCOME STREAMS  
WITH BITCOIN? NOT  
REALLY.**



# Your Team at Financial Harvest Wealth Advisors



Ten years ago, no one knew anything about Bitcoin. Ten years from now, the positioning of cryptocurrency may have evolved dramatically. But you are an investor today, and our goal at Financial Harvest Wealth Advisors is to equip you with sound, reliable information to help you make optimal decisions about your finances now and for your secure and thriving future.

As always, [we are here for you](#), as our client, should you want to explore your investment options and strategies in more detail.

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