

University

IS THERE A FUTURE FOR CRYPTOCURRENCY?

Student's Name and Surname

Course

Professor

Due Date

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The first release of an open-source cryptocurrency, which has shortly become a self-sufficient alternative to traditional currencies, is fairly considered to be one of the most important events on the global financial market during the 2000s. Today, when almost a decade has passed since Bitcoin was introduced to the general public, the first wave of excitement appears to have changed with the increasing skepticism over cryptocurrency's future. Undoubtedly, many expectations of cryptocurrency enthusiasts have failed, yet some crypto-based technologies, like Blockchain, still appear to be remarkably promising. Subsequently, to understand the prospects of cryptocurrency comprehensively, it is necessary to track its history and outline the potential scenarios for the cryptocurrency market's development in the upcoming decades.

To start, it is necessary to define the terms and designate the landmark points underlying the history of cryptocurrency. The term "cryptocurrency" is used to mark "a digital or virtual currency that uses cryptography for security."¹ One of the most decisive features characterizing cryptocurrency stems from its organic nature, as it is not issued by a centralized financial authority. This means that government interferences and manipulations are not likely to threaten cryptocurrencies. In contrast, the concept's critics argue that the availability of crypto-mining for private organizations and individuals is even more dangerous compared to potential governmental interferences. The high volatility of the demand for Bitcoin is supportive of the latter statement.

Bitcoin, which remains the largest cryptocurrency in the world, was mentioned for the first time in a white paper published in 2008 under the pseudonym "Satoshi Nakamoto."²

¹ Flamur Bunjaku, Olivera Gorgieva-Trajkovska, and Emilija Miteva-Kacarski. "Cryptocurrencies—advantages and disadvantages", *Journal of Economics* 2, no. 1, 2017.

² Aleksander Berentsen and Fabian Schar. "A short introduction to the world of cryptocurrencies", *Federal Reserve Bank of St. Louis Review*, First Quarter 100, no. 1, 2018.

Initially, Bitcoin was released to create an alternative payment system that would allow electronic transactions without a peg to physical cash. Shortly after Bitcoin was released, many alternative cryptocurrencies were introduced. Among others, Namecoin and Litecoin were released in 2011. Today, there are more than 1,000 cryptocurrencies circulating around the globe, and dozens of new ones are released regularly. In 2013, Bitcoin faced its first substantial drop in price. Despite the fact that the demand and price for Bitcoin were shortly reinforced, the crisis indicated that the future of cryptocurrency could be overshadowed by its drawbacks and limitations.

In this regard, it is necessary to discuss the drawbacks of Bitcoin more thoroughly, as they are linked directly to the future of cryptocurrency. As of August 2018, the cost of one Bitcoin was a little more than \$7,600. To compare, in December 2017, the price per Bitcoin has reached the point of \$16,000. No doubt, in the next few months, the price of Bitcoin could once again increase drastically, yet it will only prove the most capitalized virtual currency to be also an extremely volatile store of value. Today, the only effective application of Bitcoin implies low-costs transfers of value over geographically distanced locations. At the same time, Bitcoin remains largely inapplicable to traditional financial operations, as its price could drop at any moment.

If there is a future for cryptocurrency, these are altcoins that give promise. Even though similar technologies are behind all cryptocurrencies, some of them are more sustainable and reliable compared to Bitcoin. As an illustration, with the use of Litecoin, new blocks to the chain can be added more easily and smoothly. Ethereum, another popular altcoin, is commonly used to make secure contracts based on payments that proceed exceptionally when a specific task is completed. Interestingly, it is the technology of Blockchain that is behind most cryptocurrencies,

and industry optimists pin remarkable hopes on Blockchain.

Blockchain represents a public database of all transactions that network users do. Before the particular transaction is allowed, the users' majority should verify it. The need for consensus, transparency, as well as the fact that no changes could be done to the chain after a transaction is completed proves Blockchain to be one of the most promising financial technologies. Global Internet giants, including Google and Facebook, have already expressed their interest in Blockchain as a means of ensuring the security of online payments and other transactions. In addition, the Bank of England has recently announced its plans to introduce an official cryptocurrency based on Blockchain.³ Undoubtedly, this news marks that cryptocurrencies are not likely to disappear with the decay of Bitcoin.

Speaking of cryptocurrency's future, some specific scenarios are worth being presented. The first scenario is based on the prediction that cryptocurrencies will receive more support from institutional investors. The already mentioned case of the Bank of England may serve as a real-life illustration of this trend. The increasing interest of institutionalized investors, including traditional banks, would also mean that the cryptocurrency market will become more regulated. To put it simply, the mining, demand, and supply will become more stable, which means that extreme volatility, like in the case of Bitcoin, will no longer challenge the industry's development.

The second scenario implies the reinforcement of efforts on the international level to increase the cybersecurity of cryptocurrencies and impose corresponding regulations. Interestingly, the lack of regulations could be treated as both an advantage and disadvantage of

³ Robert Mendick, "Bank of England Plots Its Own Bitcoin-style Digital Currency," *The Telegraph*, 2017, accessed August 02, 2018, <https://www.telegraph.co.uk/news/2017/12/30/bank-england-plots-bitcoin-style-digital-currency/>.

cryptocurrency. On one hand, the lack of governmental involvement ensures the organic development of the market while, on the other hand, the market players cannot receive the protection of national agencies in the case of fraud. Subsequently, the introduction of universal basic regulations is likely to reinforce the security and popularity of cryptocurrency as a means of financial transactions.

Finally, the third scenario implies that the cryptocurrency's volatility will remain substantially high. This scenario is likely to become a reality in case crypto-mining will remain uncontrolled. Institutional investors will not invest in cryptocurrencies, and no international regulations will be introduced. In such a case, most altcoins will have to replicate the notorious fate of Bitcoin. If cryptocurrencies remain highly volatile, their use will also remain restricted to low-cost transactions of financial value.

To sum up, the decade after Bitcoin's release showed that the concept of cryptocurrency as an alternative to traditional storages of value implies both advantages and drawbacks. Today, high volatility, uncontrolled mining, and demand-related speculations remain the major challenges for cryptocurrency's future. Subsequently, positive scenarios are based on the increased involvement of institutionalized investors, the further development of Blockchain technology, and an introduction of productive regulations on the international level. In contrast, in case cryptocurrencies will remain highly volatile, most of the altcoins will have to share the fate of Bitcoin—which remains effective only for low-cost transactions of value.

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