



The Bitcoin Futures ETF Launch: What This Means for Crypto

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IN THIS ISSUE, WE DISCUSS:

- >> Why the new ProShares Bitcoin Strategy ETF is an imperfect product ... but still a huge milestone for the crypto industry
- >> What the new ETF will mean for bitcoin ... and other cryptoassets
- >> What to expect in the next 12-36 months on the ETF front

Earlier today, the first U.S. bitcoin ETF — the ProShares Bitcoin Strategy ETF (ticker: BITO) — began trading on the New York Stock Exchange.

All signs suggest the launch will be a big success. As of 2:00pm ET, BITO had already traded more than \$700 million, putting it on pace to have one of the highest first-day trading volumes of any ETF in history.

But how does the product work? What does it mean for the crypto market? And what should investors expect going forward?

WHAT IS THE PROSHARES BITCOIN STRATEGY ETF?

For the past 8.5 years, investors have been waiting to see a bitcoin ETF launch in the U.S. That wait ended today with the debut of BITO on the New York Stock Exchange.

The new ProShares Bitcoin Strategy ETF is not *quite* the bitcoin ETF everyone has been hoping for. Most investors have been dreaming of a “spot” bitcoin ETF, which would hold bitcoin directly. Instead, BITO invests in bitcoin futures contracts traded on the Chicago Mercantile Exchange.

From one perspective, this is disappointing. A futures-based ETF is not as good for investors as a spot-based ETF, for multiple reasons:

1. **Cost:** The bitcoin futures market tends to trade “in contango,” which means the futures price is higher than the spot price. Over time, this can create a major headwind. History suggests this “roll cost” will amount to 5-10% a year for futures-based products, beyond the direct expense ratio of the ETF (~1%).

¹ The first filing for a bitcoin ETF in the U.S. took place on July 1, 2013. At the time, bitcoin was trading at roughly \$90.



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2. Dilution: For tax-related reasons, ETFs cannot actually hold a 100% position in bitcoin futures. Most likely, they'll target about 85% futures exposure, with the rest allocated to other things. This wrinkle could cause the ETF to track the price of bitcoin imperfectly over time.

3. Tail Risk: The futures market is complex. There are position limits, for instance, that cap the amount of futures a fund like BITO can hold. There may be some risk that the fund runs into these and other issues in the future.

Despite these challenges, however, investors are flocking to BITO. This tells you something very important: Investors are eager to access bitcoin through their brokerage accounts.

And this, actually, is a *very* big deal.

For the past few years, a vocal minority in the crypto market has argued that we do not need an ETF. These ETF skeptics have argued that investors can already access bitcoin through other means: apps like Coinbase, custodians like Fidelity, and so on.

Others have argued that these alternative approaches do not work for professional investors, who prefer traditional solutions like an ETF and have been shut out of the crypto markets to date.

The market's early response to BITO suggests that the ETF optimists were right, as investors are using the fund despite its shortcomings. This suggests that there is a wave of capital sitting on the sidelines of the crypto market. It may now find its way in.

If true, this could be one of the defining stories for crypto over the next few years.



Investors are eager to access bitcoin through their brokerage accounts.

WHAT DOES THIS MEAN FOR BITCOIN ... AND OTHER CRYPTOASSETS?

It is difficult to attribute price changes in the crypto market to any one thing. The market is impacted by many forces, from regulatory developments to technological progress to the passage of time.

But it's hard to look at bitcoin's recent price movement and not conclude that the news about the ETF has had a significant impact. The price of bitcoin is up 27% in October and is trading near all-time highs.

As for other cryptoassets?

So far, they have not played along: The Bitwise 10 ex Bitcoin Crypto Index, which comprises the nine largest cryptoassets by market cap excluding bitcoin, is up just 3.9% over the same time frame.

The question is whether investors in the new bitcoin futures ETF will follow the well-worn path of other crypto investors.

Historically, investors tiptoe into the crypto markets via bitcoin, the largest, best-known, and most regulated cryptoasset. But over time, they tend to develop interests in other cryptoassets: Ethereum, Solana, Uniswap, and so on. In our experience, this transition tends to take 3-6 months, as investors learn more about the nuances behind different cryptoassets and their underlying technologies.



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WHAT SHOULD WE EXPECT GOING FORWARD?

BITO was the first crypto ETF, but it's unlikely to be the last. Now that the door is open a crack, you can expect Bitwise and other cryptoasset managers to try to pry it open further.

You're already seeing it: Here at Bitwise, last week we filed with the Securities and Exchange Commission for approval to launch a physical bitcoin ETF. We submitted more than 150 pages of research in support of our application — research we conducted to respond specifically to the questions and concerns the SEC posed to us about approving a physical bitcoin ETF.

The SEC has up to 240 days to review our application, and there is of course no guarantee it will gain approval.

Long term, however, the industry will get there. For the past decade, crypto has been on a journey from the fringes of finance to the mainstream. BITO is a major milestone in that journey, but it's not the end point. A large majority of investors still have zero exposure to crypto.

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ABOUT BITWISE

Based in San Francisco, Bitwise is one of the largest and fastest-growing cryptoasset managers. As of October 15, 2021, Bitwise managed over \$1.5 billion across an expanding suite of investment solutions. The firm is known for managing the world's largest crypto index fund (OTCQX: BITW) and pioneering products spanning bitcoin, ethereum, DeFi, and crypto-focused equity indexes. Bitwise focuses on partnering with financial advisors and investment professionals to provide quality education and research. The team at Bitwise combines expertise in technology with decades of experience in traditional asset management and indexing, coming from firms including BlackRock, Blackstone, Facebook and Google, as well as the U.S. Attorney's Office. Bitwise is backed by leading institutional investors and asset management executives and has been profiled in Institutional Investor, CNBC, Barron's, Bloomberg, and The Wall Street Journal. For more about Bitwise, visit www.bitwiseinvestments.com.

ABOUT MATT HOUGAN

Matt Hougan is one of the world's leading experts on crypto, ETFs, and financial technology. He is the Chief Investment Officer for Bitwise Asset Management, the world's largest provider of cryptocurrency index funds. He was previously CEO of ETF.com and Inside ETFs, where he helped build the world's first ETF data and analytics system, the leading ETF media site, and the world's largest ETF conference. Matt is co-author of two publications for the CFA Institute Research Foundation: "A Comprehensive Guide to Exchange-Traded Funds" and "Cryptoassets: The Guide to Bitcoin, Blockchain and Cryptocurrencies for Professional Investors." He is a crypto columnist for Forbes, a three-time member of the Barron's ETF Roundtable, a member of ETFdb's ETF Hall of Fame, and the eighth person to receive a Lifetime Achievement Award from ETF.com for contributions to the ETF industry.

