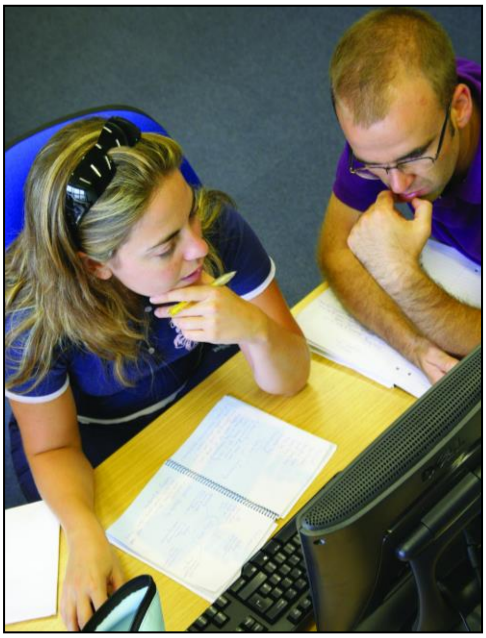
"Bitcoin: Currency or Commodity? Is there a future for virtual currencies?"

By Jack Whybrow

What's all this hype about the Bitcoin I have been hearing?

Bitcoins have been around since 2009 but unlike the pound sterling do not rely on a central authority for either creation or management. It relies instead on cryptography. Bitcoins can be mined by employing computing power to solve complex algorithms. Users then store these in a bitcoin wallet. These can then be transferred from users to user to purchase some types of goods and services or exchanged for traditional money. The exchange rate for a bitcoin has been a rocky one starting in 2009 where one bitcoin was essentially worth nothing to a peak of $1,250 (£750) in November 2013.



Okay, but what determines how much a bitcoin is worth?

This depends upon supply and demand. Supply with respect to how many bitcoins are being traded at any particular time and the total number in existence. Demand by how much people are prepared to pay. The latter depends on a number of features such as how many sellers accept bitcoins. Clearly though one of the main advantages of using bitcoins over traditional money is that transactions are harder to trace and have been associated with illicit sites such as 'Silk Road'.

Fair enough, so which is it, a currency or commodity?

Currently, I would say it is more of a commodity that can be bought and sold rather than a generally accepted form of payment. One of the main stumbling blocks bitcoins and other virtual currencies face is their volatility. After all economic theory tells us these have to be a good store of value. If this can be overcome a future currency may be on the cards for the humble bitcoin.