

Cryptocurrency Trading - Way to Invest in the Short Term

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Abstract

This paper, entitled "Cryptocurrency Trading", is a research study covering theoretical and practical notions about cryptocurrencies and their trading in financial markets.

We chose this topic because cryptocurrencies and the technology behind them have revolutionised the financial sector and even now, after a period of time since their emergence and a period of time in which they have been used, cryptocurrencies raise some questions.

The main objective of this paper is to show that, in the financial markets, cryptocurrencies are assets that promise a high return, i.e. a good short-term investment. The specific objectives have been highlighted by elaborating a study presenting the ways in which cryptocurrencies are traded in the financial markets and by conducting an analysis on them.

The aim of this paper is to show that cryptocurrencies Bitcoin, Ethereum and ADA are the most popular and show functionality and market capitalization.

Key words: cryptocurrencies, financial markets, financial assets and investment

J.E.L. classification: E2, E22

1. Introduction

Given that the world wants a more digitalised life, it is no surprise that the financial system has followed suit. The transition that banks have made from an exclusively cash-based system to electronic banking using cards has served as a basis, but has been limited by the impossibility of securing a fully online banking system.

The innovative development of cryptocurrencies based on blockchain technology has given society the ability to transact directly and securely without the need for a trusted third party (Goodman, 2019).

The advantages of cryptocurrencies include (John and Law, 2021):

1. Protection against payment fraud. Bitcoins are digital currencies. They use a cryptographic algorithm and protocols. This makes them impossible to counterfeit (Keenan, 2018).

2. Reduced possibility of identity theft. Bitcoin transactions are completely anonymous. Bitcoin transactions require no personal details or sensitive information from the sender or receiver.

3. Direct Transfer. Transactions take place directly between users, i.e. sender and receiver. No third party is involved. This eliminates fees for involving an intermediary.

4. Higher liquidity. While converting to other real currencies, bitcoin retains most of its value, while other currencies have lost value.

5. International transactions. Bitcoin is the easiest way to initiate an international transaction. It charges no additional fees and is paid immediately to a recipient.

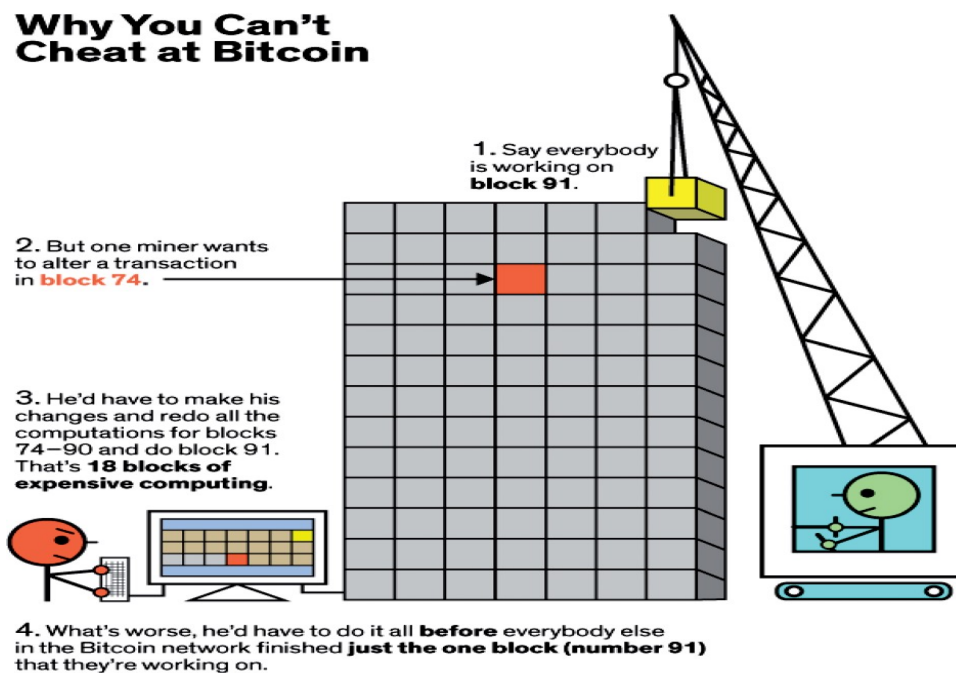
6. Blockchain. Bitcoin transactions are tamper-proof thanks to the Blockchain.

2. Literature review

It is worth noting that Bitcoin (and all other cryptocurrencies) could not exist without blockchain technology, which in the simplest way involves creating unalterable data structures (Kratter, 2019).

Blockchain is the technology that secures the storage of cryptocurrencies, their transactions and the information relationships between them (Linton, 2020).

Figure no. 1 How the Blockchain technology behind cryptocurrencies works



Source: Own processing based on information from (Yermack, 2015, p. 46)

According to Figure no. 1, once new blocks are attached to previous ones, transaction information within them can be traced back to the first block created, making the system "incorruptible" due to the fact that all previous blocks must be modified to make a change in the registry, limiting attempts by malicious people to attack the system (Mishkin F., 2018).

This first block (which resulted in the mining of 50 bitcoins) is now referred to as the Genesis Block. Bitcoin had virtually no value at this point, as well as in its first few months of existence. Six months after bitcoin became tradable, in April 2010, the value of a BTC was just under 14 cents. In early November, the price rose to 36 cents.

3. Research methodology

As with any financial instrument traded in the financial market and with cryptocurrencies, short, medium and long term trends can be found in any technical analysis study, i.e. chart analysis of the evolution of the financial instrument to be traded (Snow, 2018).

The first step in cryptocurrency trading is to determine the trend, which can be upward, downward or sideways. A market trend can be identified by drawing a support line (the bottom one) and a resistance line (the top one) on the chart, forming a trend channel.

Investors and analysts use a variety of technical indicators to identify trends in the market, anticipate potential changes in trading and ultimately either trade successfully themselves or provide advice to clients so they can trade successfully.

In the case of trade management, its purpose is to ensure that with a winning trade you always allow yourself to lose 3. You can do this by setting stop loss (the trade stops automatically when a certain amount is lost) and take profit (the trade stops automatically when a certain amount is won).

4. Findings

According to Figure 2, the Ethereum cryptocurrency has followed the same market movement as the Bitcoin cryptocurrency and is currently in a downtrend position as well.

The historical high of Ethereum cryptocurrency was recorded in November 2021 when it registered around 4800 USD and currently, on 29.08.2022, the buying price is 1479 USD.

Figure no. 2 Ethereum cryptocurrency trend today



Source: Own processing based on information from etoro.com

Figure no. 3 Using the MACD oscillator on the chart of bitcoin evolution from the present



Source: Own processing based on information from etoro.com

Figure no. 3 shows a week-by-week chart of the evolution of the Bitcoin cryptocurrency at present and the MACD oscillator at the bottom.

According to the chart the bitcoin price has formed a downtrend but according to the MACD oscillator, due to the fact that the black line intersects the red one from bottom to top and both lines are positioned below the center line (0 line), the price is expected to rise to the resistance line.

In this context, in this case study we can make a Bitcoin cryptocurrency purchase trade.

Figure no. 4 Transaction management in case of ADA cryptocurrency



Source: Own processing based on information from etoro.com

In Figure no. 4, a purchase transaction of ADA at the current value of USD 0.4 was proposed, setting the stop loss at USD 0.15 (respectively 62.5%) and the take profit at USD 1.7 (respectively 325%). Thus, for 1.3 USD profit, 0.25 USD is risked, so a winning trade allows the loss of at least four trades.

5. Conclusions

The innovative development of cryptocurrencies based on blockchain technology has given society the ability to transact directly and securely without the need for a trusted third party.

Bitcoin is the leader of the crypto sector. It is also the first cryptocurrency to appear and was created and launched in the year 2009 by a person (or possibly a group) who goes by the pseudonym Satoshi Nakamoto. Almost a thousand new bitcoins are mined (digitally mined) every day, bringing Bitcoin closer and closer to its finite maximum number.

Ethereum (ETH) is the second most popular cryptocurrency after Bitcoin. Founded by Vitalik Buterin and Gavin Wood in 2015.

The Cardano platform can handle all types of transactions, but the real goal is to create an ecosystem that enables seamless interchangeability between different blockchains.

6. References

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