International Journal of Cryptocurrency and Blockchain Theories ISSN PENDING
Vol. 1 No 1 | 20-24

Exploring the Differences Between Cryptocurrency and the Nigerian Capital Market

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Abstract

The rise of cryptocurrency has introduced a dynamic shift in global financial systems, challenging traditional markets such as the Nigerian capital market. This study investigates the prevalence and growth of cryptocurrencies compared to the established capital market in Nigeria. By exploring the operational mechanics, market value determination, and investor participation in both systems, the research highlights key similarities and differences. While both markets derive their value from underlying ideas and are influenced by demand, cryptocurrency offers unique advantages such as decentralized control, 24/7 trading, and minimal transaction costs. However, it also faces challenges such as high volatility, manipulation, and ambiguous legal status in Nigeria. In contrast, the capital market, with its structured institutional backing, offers more stability but is constrained by regulatory oversight and operational timelines. The study provides a comprehensive evaluation of both financial instruments, guiding investors toward informed decisions about the opportunities and risks each market presents.

Introduction

The pursuit of wealth is a natural phenomenon for every individual, this is required in order to guarantee a better future and ensures the provision of basic necessities. When placed on a larger scale, this facilitates the growth of a country's economy, hence the need for a good financial system in an economy. The fundamental role of the financial system is to expedite the exchange of goods and services, possibly through time. There are diverse institutions and mechanisms contained in a financial system. Proper financial knowledge is necessary in order to guide the investor on the right investments to make so as to get maximum returns and also to avoid hazardous risks thereby minimizing losses. Although there are quite a number of financial instruments belonging to the asset class, the two most commonly used in recent times are the stock market and cryptocurrencies.

This study seeks to evaluates the increasing prevalence of the Cryptocurrency market and alongside the already existing Capital market considering the various growth levels and adoption so far.

Cryptocurrency

Cryptocurrency can be described as a system that makes use of cryptography in order to allow secure transfer and exchange of digital tokens in a distributed and decentralized way. Cryptocurrencies have no physical existence, instead they are seen as electronic accounting systems that keep track of people's transactions thereby retaining purchasing power. These tokens are traded at market rates and valued in fiat currencies (Ali, Barrdear, & R Clews, 2014). Crypto-currencies depend on cryptography to facilitate and keep track of transactions on electronic ledgers or databases of financial transactions. Due to their electronic depiction, crypto-currencies are therefore referred to as digital currencies (ECB, 2012). Also, cryptocurrencies are decentralized, having no central authority accountable for maintaining the ledger or the code used for its implementation unlike those of commercial banks.

The first cryptocurrency was Bitcoin, which began trading in January 2009. Since then, many other cryptocurrencies have been created employing the same innovations that Bitcoin introduced, but changing some of the specific parameters of their governing algorithms. The two major innovations that Bitcoin introduced, and which made cryptocurrencies possible, were solutions to two long-standing problems in computer science: the double-spending problem and the Byzantine Generals Problem.

In spite of Bitcoin being a decentralized payment protocol, governments around the world have always tried to ban it. In some countries like Morocco and Bolivia, trading Bitcoins attracts a hefty fine or jail term. In Nigeria, Bitcoin's legal status is largely ambiguous. As crypto-currencies are denominated in their own unit of account, they are like foreign currencies relative to traditional fiat currencies, such as dollars and pounds.

Like traditional currencies, such as dollar notes or gold coins, crypto-currencies can be used to facilitate 'peer-to-peer' transactions between individuals without the services of a specific financial intermediary. While commodity currencies such as gold have tangible alternative uses, fiat currencies, bank deposits, and crypto-currencies have no secondary, non-monetary purpose. People transacting using these modern currencies believe that other people will accept them for future transactions and that such currencies will therefore be useful as a temporary store of value. Although crypto-currencies often have no centralized issuer, they are predominantly fiduciary in the sense that they are not backed by precious metal and require trust.

Capital Market

The capital market is a market for financial investments that are direct or indirect claims to capital (Gart, 1988). The capital market comprises of complex of institutions and mechanism through which intermediate term funds and long term funds are pooled and made available to business, government and individuals.

The Financial Market can also be referred to as a market where securities such as stocks and bonds are traded (Buying and Selling). Financial markets are divided into several categories of which stock markets and bond markets are the major ones. Simply put, stocks are ownership instruments to a part of the issuer's capital, while bonds are seen as debt instruments on its issuer. When a stock is purchased, it avails the buyer the privilege of becoming a shareholder in the company. On the other hand, the purchase of a bond makes the purchaser a creditor to the company (Dougall & Gauminitz, 1986). The Capital market enables utilization of savings from individuals and converts them into a pool of capital which can be utilized for the economic development of a country. Efficiency is essential in the capital market for raising capital by the corporate sector of the economy and also vital for the protection of investors' interests in corporate securities.

The Nigerian Capital Market traces its origin back to colonial times during the British era of government who at that time required funds for running the local administration. Most of the funds were derived from the marketing of agricultural produce and solid mineral mining. Realizing that these sources were insufficient to cater for the growing financial obligations, the colonial administration decided to increase its revenue base by restructuring the method of revenue mobilization and taxation. It also needed to raise funds from public sector so as to make up for the shortfalls in the availability of funds. Therefore, the necessity to institute a financial system by setting up the basic infrastructure for its takeoff awaiting the development of a well-structured private sector.

A Brief Timeline of Cryptocurrency

2008 recorded the first milestone in crypto currency existence as the domain name bitcoin.org was registered on the18th August, 2008 and on 31st October, 2018 Satoshi Nakamoto who was the designer of bitcoin, made a paper publication captioned "Bitcoin: A peer-to-peer Electronic Cash System" which premiered the bitcoin enterprise. (Satoshi, 2008). 2009 witnessed the first bitcoin transaction as Nakamoto transferred 10 bitcoin (BTC) to Hal Finney, a computer programmer, on the 12th of January, 2009. In 2010, the inaugural bitcoin sale takes place, allowing a monetary value to be attached to cryptocurrency for the very first time. Two pizzas were swapped 10,000 coins by a bitcoin user. In 2011, witnessed the emergence of other cryptocurrencies like Litecoin, Swiftcoin and Namecoin. Meanwhile, bitcoin is condemned based on claims that it was being used for illicit and illegal activities on the "dark web", especially on sites like Silk Road. Despite the bad publicity, the value of bitcoin skyrocketed that same year before experiencing a crash. In 2012 cryptocurrencies continued to gain popularity, while in 2013, various countries began attempting to work out the ways of dealing with cryptocurrencies. In 2014, Microsoft allowed its users to purchase games with the bitcoins. 2015, saw the emergence of new cryptocurrencies, which included ethereum and coinbase. In 2016, Cryptocurrencies continue to gain popularity and prominence. More bitcoin bitcoin ATMs are launched as the number rises from around 500 to 900 by the end of the 2016. In Argentina, Uber adopts the use of bitcoin payments as well as Swiss national railway and software websites. In 2017, cryptocurrencies experienced a great boom. After starting the year with acumulative market valuation of just $17.7 billion, digital currencies ascended till the end of the year with a collective market capitalization of $613 billion (Rosemary, 2018).

Similarities and Differences between Crypto Market and Stock Market

There has been a lot of debate concerning the Stock market and Crypto Market in terms of similarities and differences. Many argue that the crypto and stock markets vary in prospects and are vastly different in many aspects while some others argue otherwise.

In comparison, it is evident that the two markets function the same way. On the basics, the price of both markets are determined based on demand. This means that the value of the market is dependent on how much people are willing to pay for a share or a currency which implies that the highest bidder determines the price of the stock or currency. It also implies that when investors are only willing to pay less than a current price value, the price of the stock or currency goes down.

Also, the two markets are thus far valued in fiat currencies. This might not be the case if the goal of cryptocurrency becoming a legalized medium of exchange is actualized. But for the meantime, the value of the both markets are in fiat currencies like the USD etc. Similarly, both markets obtain their value from the idea behind them. For instance, a stock is valued based on the business idea behind it, likewise a currency's value is based on the idea, this makes them similar in this context.

In contrast, regardless of the fact that both markets obtain their value from the underlying idea behind them, investors in the stock market actually invest in the company, while those investing in cryptocurrency invest in the underlying technology or the currency, therefore unlike the stock market, cryptocurrency investors however, do not own any part of the company. This in turn affects the total assessment of the crypto market, because the total market capitalization for cryptocurrencies is uncertain. Also the cryptocurrency market is much faster than the stock market in terms of price fluctuations. There is fast rise in prices likewise a fast fall and the magnitude of price changes is larger in the crypto market than in the stock market. In the stock market, there is nothing like market manipulation. On the other hand, in the cryptocurrency market, there is a lot of manipulation going on. This might be advantageous for the wider adoption, because more people are involved.

When it comes to Cryptocurrency trading, there is no time limit, unlike in traditional stock markets where trading activities are not carried out during weekends. The cryptocurrency market is always open all year round and cryptocurrency trading can be done from anywhere, through a reliable trading platform, which makes it more convenient than the stock market. Money transfer in cryptocurrency trading is easier, cheaper and faster than stock trading. Most times it costs nothing to make transfers in cryptocurrency and all deposits and withdrawals are performed directly. The cryptocurrency market is not dependent on banks and are not controlled by any central authority with authority to reject or limit transactions. Starting cryptocurrency trading, unlike conventional stock trading, is much easier as there is no need to employ the services of a professional stock broker and the long and strenuous processes are not required.

Trends in Cryptocurrency

In 2017, cryptocurrencies experienced a great boom. After beginning the year with an aggregate market valuation of just $17.7 billion, digital currencies soared to end the year with a combined market cap of $613 billion. That's a gain of more than 3,300%, for those of you keeping score at home, and very likely represents the single greatest year on record for any asset class. Although this momentum continued until Jan. 7, 2018, with the aggregate market cap hitting an all-time high of $835 billion, the past roughly six months haven't been pretty. Led by bitcoin, Ethereum, and Ripple, cryptocurrencies have mostly been throttled across the board. Last week, the aggregate cryptocurrency market cap hit an intraday low of $232 billion, which is its lowest level in seven months, and representative of a 62% peak-to-trough decline since the year began (Williams, 2018).

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