Understanding Crypto ETPs: a 1% fee differential may lead to exponential underperformance

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Key Takeaways

- Fees are not the whole cost of an investment. The future returns on the fees are.
- The opportunity cost created by the compounding fees for high performance assets can grow exponentially.
- The difference in performance for two investors investing US$100 in bitcoin over the last five years could amount to US$115 at the end of the period. More than their initial investment!

- Related Products WisdomTree Physical Bitcoin, WisdomTree Physical Ethereum, WisdomTree Physical Cardano, WisdomTree Physical Polkadot, WisdomTree Physical Crypto Altcoins, WisdomTree Physical Crypto Mega Cap, WisdomTree Physical Crypto Mega Cap Equal Weight Find out more

John C. Bogle is often credited with being the father of passive investing. His philosophy was to concentrate on investing strategically and being mindful of cost. He once summarised those principles when he said, “Investors need to understand not only the magic of compounding long-term returns but the tyranny of compounding costs; costs that ultimately overwhelm that magic”1.

The fees are not the whole cost. The future returns on the fees are.

The compounding of cost is particularly interesting. Taking a simple example of a US$100 investment in equities over a period of 10 years and assuming a yearly return of 6%, an investor that pays no cost would end up with US$179. The same investor that pays 1% per annum of fees would end up with US$163 – US$16 less. The total opportunity cost for the investor over the period is US$16, or 1.6% of the initial investment every year, not the US$10 that we could expect from simple calculations.

The reason for this big difference is the compounding or, in other words, the fact that investors do not benefit from the growth of the money they paid in fees early in the investment. Keeping with the same example, the asset grew 69% in the last nine years of the investment (again assuming 6% per annum). In year one, the investor paid US$1 of fees. Had they not paid that US$1 in year one – nine years later (ie at the end of the investment period), this US$1 would have turned into US$1.69. So, the US$1 of fees ended up costing US$1.69 to the investor. Assuming a 20-year investment period, it would have been US$3. The cost of opportunity of the fees paid can grow quite astonishingly over time.

But what happens if the assets the investor invests in are not run-of-the-mill equities but something with higher volatility and higher growth potential?

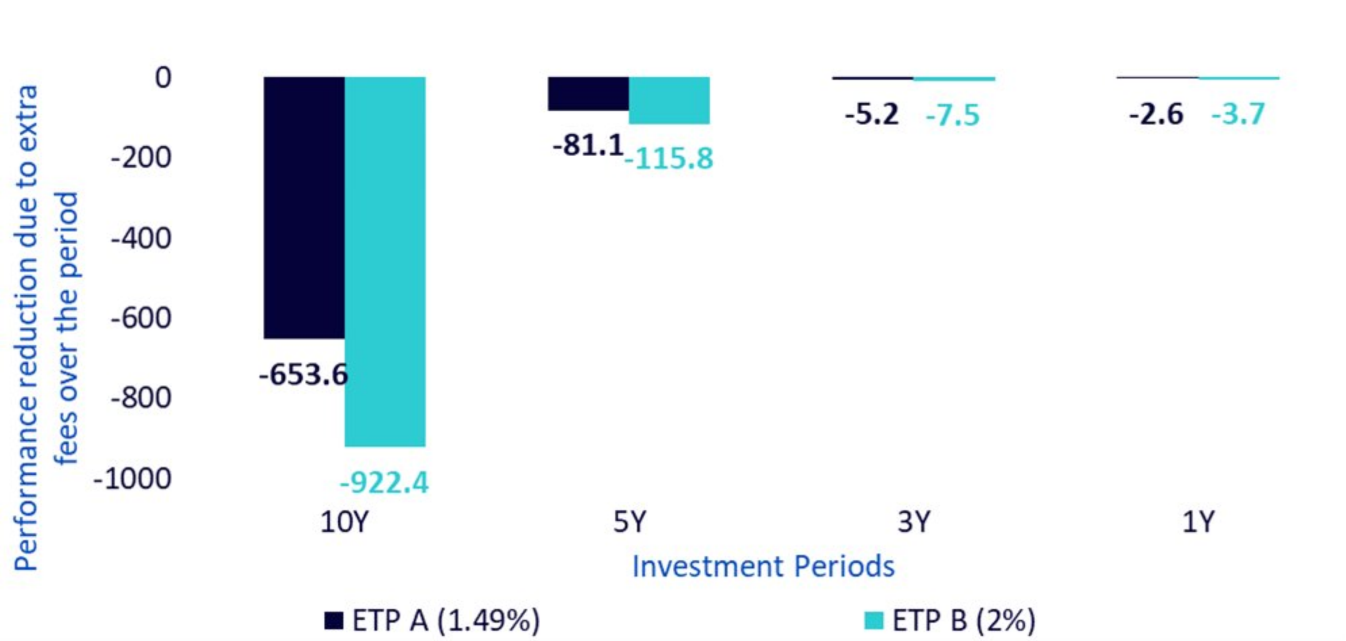
The impact of fees on high growth assets like bitcoin

In this example, we assume at investment of US$100 at different point in time in the following three bitcoin Exchange Traded Products (ETPs):

- **WisdomTree Physical Bitcoin** with a MER of 0.35%
- **ETP A** with a MER of 1.49%
- **ETP B** with a MER of 2%

Figure 1 illustrates the end result for the investor, depending on the period of investment. If the investor invested in an ETP with 0.35% of fees, such as the WisdomTree Physical Bitcoin, on 31 January 2013, 10 years later the US$100 would have turned into US$5968. If the same investor had invested in a more expensive product, the results would have been very different. An investor in ETP A would have received US$5314, US$654 less, and an investor in ETP B would have missed out on US$922. Clearly, the fee impact has not been US$11.40 or US$16.50, but hundreds of dollars.

Figure 1: Difference in performance because of fees in Bitcoin ETP depending on time periods compared to the cheapest one.



Source: Bloomberg, WisdomTree. From 31 January 2014 to 31 January 2024. In US$. The graph shows the difference in investment value at the end of the period between ETP A or B and WisdomTree Physical Bitcoin (assuming a 0.35% MER over the full period). **For illustrative purposes only.**

Even on small periods, the impact is significant. Over five years of investment, investors would have lost US$81 or US$116. Looking only at the last 12 months, the impact is already visible. An investor in the cheapest ETP would have turned US$100 into US$216.60 when the investor in ETP B would have received almost US$4 less.

Conclusion

Compounding costs are a real drag for long-term investors in most assets. But in cryptocurrencies, it is also a drag for even short to medium-term investors. When it comes to selecting a crypto ETP, there are many aspects to consider, such as the structure, the issuer or the storage conditions, but overall costs may be one of the most important aspects of the final result.

WisdomTree crypto ETPs: Institutional grade structure at a low price point

Since its establishment in 2006, WisdomTree has been at the forefront of providing liquid, transparent, and efficient ETPs to its clients across the globe. In 2019, launched our inaugural bitcoin ETP in Europe, the WisdomTree Physical Bitcoin, becoming the first established ETP issuer to provide investors with an institutional-grade physically backed crypto ETP in Europe.

We currently oversee more than US$500 million in assets under management across our crypto ETP range. Recently reinforced our commitment to investors by reducing fees across our entire range of physically-backed crypto ETPs, which is already amongst the lowest priced in Europe. This move also means that WisdomTree Physical Bitcoin has the lowest fee level of any physically backed bitcoin ETPs in Europe that dont participate in crypto lending – 0.35%.

Our crypto ETPs provide investors with a simple, secure and a low-cost way to gain exposure to a range of cryptocurrencies including Bitcoin, Ether, Solana, Cardano, Polkadot and a selection of diversified crypto baskets.

Sources

1 John C. Bogle, The Clash of the Cultures: Investment vs. Speculation

Important Risks Related to this Article

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