

Defiance's IBIT Enables Investors to Participate in or Hedge Crypto Downside Risk

Defiance ETFs is creating unique, transparent, portfolio-based products linked to disruptive technologies – including 5G, quantum computing and hydrogen – that will change the way we live, work, play and operate. Among its offerings is the Defiance Digital Revolution ETF (NFTZ), which provides long exposure to the blockchain and digital asset ecosystem. Recently, the firm also launched the Defiance Daily Short Digitizing the Economy ETF (IBIT), which can be used as a tool to express a bearish view on the cryptocurrency ecosystem or hedge downside risk.

Some investors see cryptocurrencies, blockchain technology and digital assets as the wave of the future; others see them as a fad. Ultimately, differing viewpoints are what makes a market. But one cannot ignore the fact that bitcoin has lost about 70% of its value in 2022, and a host of companies that operate in the crypto space have seen their stocks plummet as well. Many long investors who have not sold their positions are facing huge losses in their portfolios.

IBIT is an actively managed ETF with a management fee of 0.95% that aims to track the inverse daily price and yield performance of the Amplify Transformational Data ETF (BLOK), calculated as gross total return. BLOK invests at least 80% of its net assets in equity securities of companies actively involved in the development and utilization of blockchain technologies. IBIT seeks to provide the -1x daily return of the underlying benchmark.

"IBIT is an investment portfolio or hedging tool, and it's not necessarily an opinion of ours," notes Sylvia Jablonski, CEO and CIO of Defiance ETFs. "Currently, no other ETF strategy competes with it. The ProShares Short Bitcoin Strategy ETF (BITI) is also an inverse ETF, but that product offers short exposure to bitcoin only."

The fund's principal investment strategy is to use equity derivatives to short BLOK, or potentially stocks correlated to BLOK, to get inverse exposure. Essentially, for every \$100 invested, the exposure is \$100 short of BLOK. The fund rebalances daily. If BLOK falls by 1% today, then IBIT will go also up 1%, minus fees and expenses. If an investor holds IBIT for a week, the return will be the summation of the change in BLOK for each day of that week. If BLOK falls 1%, and IBIT goes up 1%, IBIT becomes shorter the next day, so compounding works in the investor's favor over time if BLOK keeps falling.

There are a few benefits of leveraged inverse ETFs compared to taking an outright short position in stocks or ETFs, says Jablonski. Specifically, investors do not need a margin account, and the loss is limited to the amount invested in the position.

Inverse ETFs tend to perform close to 100% the inverse of the fund they track, and they increase in value as the market declines. However, investors should be aware that the performance may deviate, especially when the market is extremely volatile. Moreover, range-bound volatility is not good for leveraged inverse ETF products because they are designed to reflect a view on the direction of the underlying assets.

IBIT could be of interest to retail investors, who are the dominant participants in the cryptocurrency and digital asset markets. It could also be a tool for registered advisors, family offices, pension funds and large institutions that have allocations to cryptocurrencies, blockchain, digital assets or crypto mining companies. Some investors may use IBIT as a short-term tool. Others may choose to hold it in a portfolio for the long term; for example, they could maintain a 5% position in IBIT if they want to 5% hedge of their crypto exposure. A long-short fund could use IBIT to generate alpha on the short side when the stocks in BLOK fall, or as a hedge against falling prices.

Jablonski stresses that IBIT is a valuable tool, but it is not one to set and forget. She encourages investors and traders in leveraged inverse funds, including IBIT, to monitor their positions daily.

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