



Does Spot Bitcoin ETF Matter? Evidence from Four Perspectives

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Abstract. The approval and quick implementation of spot Bitcoin exchange-traded funds (ETFs) are a milestone in the mainstreaming of decentralized assets in conventional financial markets. Increasing market capitalization and institutional investor take-up of Bitcoin ETFs raise questions regarding their effect on market structure, liquidity, volatility, and financial system resilience. This paper investigates the differences between spot Bitcoin ETFs and conventional ETFs with respect to underlying assets, market characteristics, and regulatory complexities. Based on comparative analysis and a review of new academic literature and regulatory updates, the paper analyzes the effect of Bitcoin ETFs on market efficiency, institutional investor strategies, and cross-border regulatory responses. The findings reveal that Bitcoin ETFs enhance market accessibility, facilitate price discovery, and draw in institutional money but also increase market sensitivity and create new types of systemic risk via cross-market connectivity. This study offers an in-depth analysis of the developing role of Bitcoin ETFs and provides recommendations to regulators and institutional investors who are looking to reconcile innovation with financial resilience.

Keywords: Bitcoin ETF, Institutional Investment, Market Efficiency, Financial Stability, Crypto Regulation.

1 Introduction

Bitcoin has evolved exceedingly quickly in the last ten years, maturing from an esoteric digital currency experiment to an accepted and internationally traded financial asset. It is ever more used as an inflation hedge, a diversification vehicle, and digital gold. With trading infrastructure developing and institutional appetite on the rise, Bitcoin's place in the modern global financial system continues to gain depth [1-2].

Parallel to this development has emerged an important financial innovation—spot Bitcoin exchange-traded funds (ETFs). In contrast to Bitcoin futures ETFs based on derivative instruments, spot Bitcoin ETFs directly hold Bitcoin and expose investors to the market with precision in the absence of technical custody or security complexities [3]. Their approval represents a milestone in the financialization of cryptos. Volumes grew by 35% over the past year on the back of institutional inflow [3]. Increased liquidity has promoted better price discovery and less volatility, as per market data [3].

Importantly, Bitcoin ETFs lower institutional entry barriers into crypto markets, making participation safer and more efficient [4]. Long-term investors, such as pension funds and sovereign wealth funds, increasingly use Bitcoin ETFs as part of broader portfolio strategies rather than merely for short-term arbitrage [5]. This shift contributes to greater price stability, although the asset remains subject to high volatility and macroeconomic uncertainty [6].

In contrast to conventional ETFs—equity- or gold-based—Bitcoin ETFs are imbued with different characteristics and risks. Their decentralized, highly speculative, and poorly regulated underlying asset brings structural and systemic factors that are vastly different from mainstream ETF products [7]. In addition, the regulations of Bitcoin ETFs are different between regions. The U.S. SEC and the MiCA regime of the EU approach market regulation in quite distinct ways [8]. MiCA also offers channels through which future crypto-ETFs can be regulated beyond Bitcoin, such as Ethereum-ETFs and DeFi-based products. Given this context, this paper investigates the impact of spot Bitcoin ETFs across four key dimensions: (1) structural differences compared to traditional ETFs, (2) their effect on liquidity and price discovery, (3) institutional investor behavior and strategy, and (4) global regulatory perspectives and implications.

2 Market Mechanism and Economic Influence

2.1 Comparison of Traditional Types

Spot Bitcoin ETFs are structurally different from conventional ETFs in terms of structure, market environment, and regulatory environment. To put it into perspective, gold ETFs are underpinned by physical commodities whose prices are relatively stable in contrast to Bitcoin that has highly volatile and speculative characteristics [2]. Second, spot Bitcoin ETFs are exempt from tracking errors inherent in Bitcoin futures ETFs that are based on contango and backwardation in the futures market [6].

Another crucial difference is between the functions of liquidity providers and market makers. Traditional ETFs are subject to well-regulated financial markets grounded on mature market structures compared to Bitcoin ETFs grounded in an emerging and in most cases fractured crypto marketplace. In this sense, price manipulation as well as wash trading are of high concerns, thus bearing an overall impact on the efficiency of the marketplace [9].

2.2 Impact on Market Efficiency and Liquidity

Spot Bitcoin ETFs also demonstrated their capability to enhance the efficiency of the market through mainly arbitrage mechanisms driving prices to converge between markets and minimize market fragmentation [10]. Traditional ETFs have demonstrated in empirical studies to lift liquidity and reduce bid-ask spreads [11]. Bitcoin ETFs will similarly exert the same effects, although the magnitude will be highly dependent on the market's maturity and investor activities. As beneficial as spot Bitcoin ETFs are to liquidity and transparency enhancement, their stabilizing effect in the long term has yet to be known. Without institutional long-term usage shift, market efficiency gains

achieved so far will be ephemeral. Thus, ongoing monitoring and investor education are critical to ensuring market integrity.

This can be seen in current market statistics: the mean Bitcoin ETF premium against spot markets decreased by about 40% in Q2 2024 as a result of enhanced arbitrage activity. This reflects better price accuracy and lower price dislocation between spot and ETFs. Meanwhile, the efficiency of the price discovery of Bitcoin markets increased by approximately 75% after the debut of the ETF [12]. However, high-frequency traders in markets in cryptocurrencies can create temporary volatility instead of eliminating it [6].

2.3 Volatility and Financial Stability

The volatility of Bitcoin inherently poses questions as to the capacity of ETFs to reduce or increase price volatility. Institutional investment through the utilization of ETFs causes marketplace maturity to limit excessive speculation [1], but the warning is that the introduction by ETFs of leverage and other risks increases exposure on a systemwide basis [13]. Both market access and integration are enhanced by Bitcoin ETFs but also create the potential to transfer financial shocks between asset classes. Because these instruments are increasing in size, regulators might be required to institute limits on leverage and tighter liquidity protection to reduce system threats.

In addition to this, enhanced institutional ownership in Bitcoin through BTC-ETFs increases the correlation between traditional finance and crypto assets. Institutional-scale ownership through the mechanism of BTC-ETFs would spill over into the global financial markets if Bitcoin's value were to drop significantly [14].

3 Institutional Investment and Market Development

3.1 Institutional Interest and Entry

The availability of spot Bitcoin ETFs has greatly facilitated institutional investors' access to crypto markets—a space many avoided in the past due to custody issues, volatility, and regulatory uncertainty. By using regulated financial products that are familiar to them to get exposure to Bitcoin, institutions don't need to take custody of private keys or engage unregulated exchanges [4].

More institutional players—pension funds, sovereign wealth funds, and insurance companies—are also starting to include Bitcoin ETFs in their portfolios as a diversification strategy [5]. Institutional players use risk-adjusted strategies in contrast to retail investors. Institutional participation increases trading volume, narrows bid ask spreads and increases market liquidity. However, their participation depends on wider economic conditions and regulatory clarity, and these influence both ETF activity and price response.

3.2 Investment Portfolio and Strategies

Institutional investors tend to join Bitcoin ETFs in one of three ways: Institutional investors' varied approaches to Bitcoin ETFs both capture their increased faith in crypto-pegged assets and the ongoing wariness of them. Although this participation gives

Bitcoin credibility, it also increases contagion risk in the financial markets, underscoring the necessity of all-round risk management.

Institutional investors employ one of three primary methods in approaching Bitcoin ETFs. First, some institutions use Bitcoin ETFs in multi-asset portfolios as part of a long-term portfolio strategy. This helps them gain exposure to the potential growth of crypto while hedging against conventional market declines and diversifying into uncorrelated assets [5]. Second, hedge funds and trading desks utilize short-term arbitrage strategies in the market through which they take advantage of price differences between the spot Bitcoin market and the ETF shares in order to profit [6]. Third, Bitcoin ETFs are used as hedging instruments in order to control risk exposure in wider cryptocurrency portfolios or other highly volatile asset classes [12].

This type of institutional activity increases liquidity and market sophistication but introduces additional complexity. For example, such institutional funds can be highly responsive to institutional sentiments so that big portfolio changes can lead to sudden inflows or outflows and generate short-term market volatility. Institutional money can also reinforce procyclical patterns during downturns.

4 Comparative Policy and Regulatory Environment

4.1 United States vs. European Union

Spot Bitcoin ETFs are handled vastly differently based on what side of the globe one is on. In the United States, the SEC has long been conservative in its approach, citing the risk of manipulation, poor investor protection, and the necessity of enhanced market monitoring [15]. While multiple spot Bitcoin ETFs have finally been approved since, the path has been slow and highly scrutinized demonstrating the hesitancy of the regulator.

Conversely, the European Union has gravitated towards a formal and innovation-conducive approach through its Markets in Crypto-Assets Regulation (MiCA). MiCA introduces transparent rules on the issuance, trading, and custody of crypto assets such as ETFs. This approach seeks to foster market growth while reducing systemic risk [8]. More importantly, MiCA is not Bitcoin-specific; it also lays the foundation for other crypto ETFs such as Ethereum and stablecoin-backed products.

4.2 Developments in Other Markets

In addition to the United States and the European Union, some other nations have also achieved significant success in creating regulatory structures in place to support crypto ETFs. Canada, for example, was the initial nation to list a spot Bitcoin ETF and has since become a trailblazer in this regard. By 2024, Canadian Bitcoin ETFs had amassed over USD 5 billion in assets under management. Canada's embrace of strict anti-money laundering (AML) procedures and strong custody measures has served as a key contributor to market stability and investor faith [1].

In the Asia-Pacific region alone, Hong Kong and Singapore stand out as lead players in their proactive approaches to crypto regulations, finding a balance between financial innovation and protection measures. Hong Kong's Securities and Futures Commission

authorized institutional access to authorized crypto investing products, offering an organized channel for market entry. At the same time, the Singaporean Monetary Authority has put in place a licensing regime that guards investors while boosting fintech innovations and responsible market evolution [13].

These dynamic models illustrate that well-considered policy can encourage innovation while maintaining financial integrity. Nevertheless, coexistence between diverse national models continues to be a challenge to worldwide coordination. Lack of a standardized approach could mean a segmented crypto ETF market and constricted cross-border investing and expansion. Having internationally uniform standards will be key to bringing about the long-term sustainable development of financial instruments based on crypto.

5 Conclusion

Spot Bitcoin ETFs mark an important milestone in bringing decentralized crypto assets into mainstream financial systems. This analysis has looked into the structural distinction between Bitcoin ETFs and traditional investment vehicles, the effect of these on efficiency in the market as well as on the behavior of institutional investors, and the differences in regulatory frameworks that govern their global uptake. Overall, these ETFs have enhanced market liquidity, strengthened price discovery mechanisms, and legitimized Bitcoin in mainstream financial architecture. In this respect, spot Bitcoin ETFs are a litmus test of the extent to which traditional financial architecture can embrace decentralized innovation. Development of these will probably transform the narrative of crypto-financial integration with an emphasis on policy frameworks that serve to support innovation and safeguard financial stability simultaneously.

But these changes do not exist outside of risk. Bitcoin's volatility, married with its rising enmeshment with legacy financial firms through ETFs, opens up avenues for potentially destabilizing the system. While ETFs present institutions with a less risky and more convenient way to take exposure to cryptocurrency markets, they also are condensing risk into an otherwise volatile and incompletely regulated marketplace. As the size and scope of these products increase, regulatory capacity must follow in kind to avoid allowing innovation to get ahead of control.

From a policy viewpoint, some priorities emerge. A globally consistent set of regulatory standards is needed to minimize the risk of jurisdictional arbitrage and ensure market integrity. Increasing obligations of transparency and disclosure will assist in countering the risks of price manipulation and excessive volatility. Furthermore, stress testing procedures and liquidity risk management instruments should be considered by the regulators, particularly on those firms with high exposure to crypto exchange-traded funds. In the future, some studies could examine the interactive dynamic between crypto ETFs and decentralized finance (DeFi) systems, analyze diversified crypto portfolio long-term performance, or evaluate the potential impact of the emergence of central bank digital currencies (CBDCs) on investor sentiment and the wider crypto investment environment.

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