kcFED Payments System Research Briefing

The Cryptic Nature of Black Consumer Cryptocurrency Ownership

By Terri Bradford

Owning cryptocurrency has become especially popular among Black consumers for reasons related to historical context as well as the forward-looking views of young consumers. While cryptocurrencies have the potential to meet Black consumers' expectations, they also pose risks to privacy and financial security.

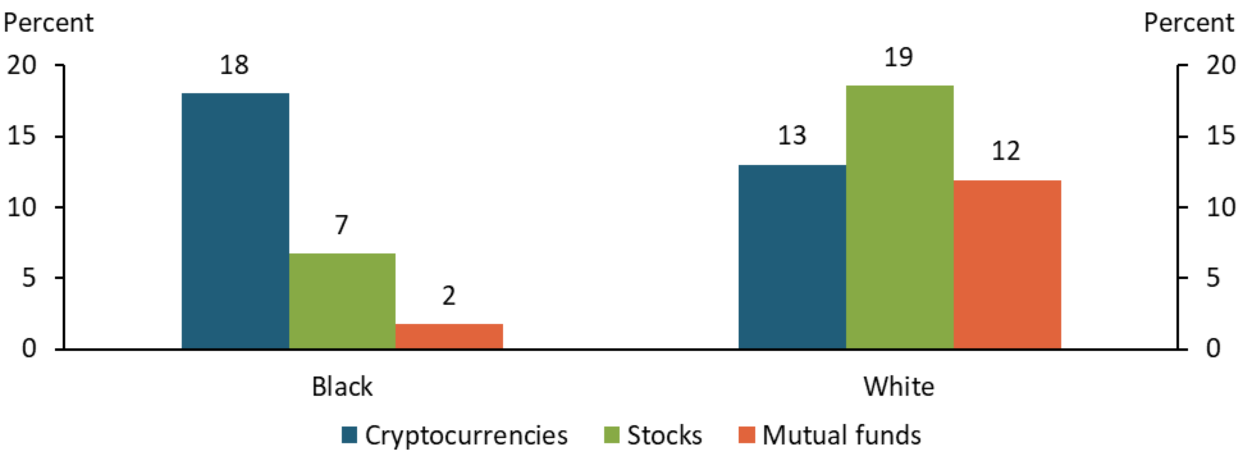
A growing number of U.S. consumers own cryptocurrency, a digital asset that secures transactions through cryptography and distributed ledger technology (usually blockchain). Although cryptocurrency was originally envisioned to function as an alternative currency or payment instrument, cryptocurrencies today (such as bitcoin, Ethereum, and Dogecoin, among many others) are used mainly for investment, and have become particularly popular among people of color. This *Payments System Research Briefing* examines the appeal of cryptocurrencies specifically for Black consumers and the risks cryptocurrency ownership may pose to their wealth building and financial security.

Black consumers' cryptocurrency ownership relative to white consumers

Surveys show that Black consumers are more likely than white consumers to own cryptocurrencies. A 2021 Pew Research Center survey of U.S. consumers, for example, found that 18 percent of Black adults had invested in, traded, or used a cryptocurrency compared with 13 percent of white adults.[1] This difference between Black and white consumers' cryptocurrency ownership contrasts sharply with other traditional assets. For example, according to the Board of Governors of the Federal Reserve System's 2019 Survey of Consumer Finances (SCF), 61 percent of white households owned equity investments compared with 34 percent of Black households—a nearly two-to-one margin.

Unlike white consumers, Black consumers are in fact more likely to own cryptocurrencies than assets such as stocks and mutual funds. Chart 1 suggests that Black consumers have a higher ownership rate for cryptocurrency than for stocks and mutual funds.[2] In contrast, white consumers have a higher ownership rate for stocks than for cryptocurrency.

Chart 1: Black consumers' rate of cryptocurrency ownership is higher than for stocks or mutual funds



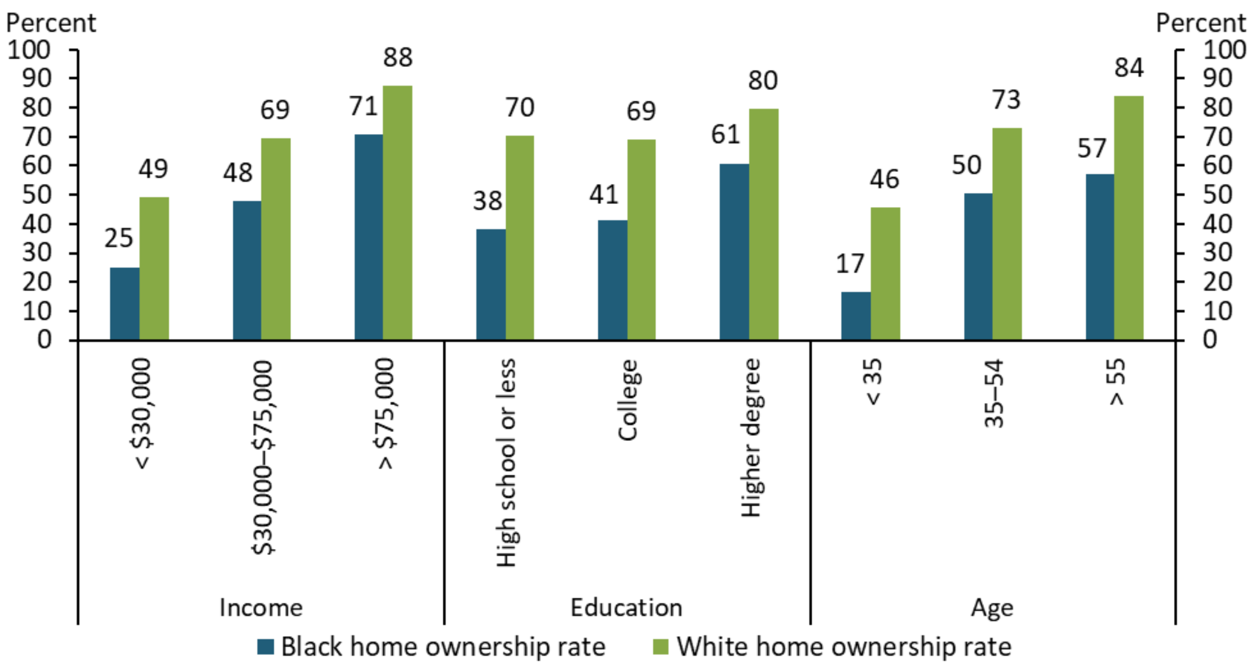
Sources: Pew Research Center, Board of Governors of the Federal Reserve System, and author's calculations.

The appeal of cryptocurrencies for Black consumers

Several factors may explain why Black consumers have been drawn to cryptocurrencies. First, Black consumers may see cryptocurrencies as a relatively quick way to close the wealth gap with other races, particularly white consumers. Black consumers have historically had significantly less wealth than white consumers, and this wealth gap persists. In 2019, Black households' median wealth was $24,100—less than 15 percent of white households' median wealth, which was $188,200 (Bhutta and others 2020).

The current wealth gap derives both from gaps in income and in traditional wealth-building assets such as housing. In 2019, the median Black household income was only about 60 percent of the median white household income (Wilson 2020). Black households have much lower homeownership rates as well. Chart 2 shows that the homeownership rate is lower for Black households (blue bars) than white households (green bars) across all income, education, and age groups. The gap is particularly pronounced among low-income, low-education, and young households. Furthermore, Black homeowners' home values are typically lower than white homeowners' within the same income, education, or age groups. Historically, residential segregation policies resulted in discriminatory real estate practices and lower house appreciation, discriminatory lending practices resulted in higher denial rates for mortgages and a higher propensity to push subprime loan products, and less wealth passed down through generations resulted in insufficient resources for down payments, increasing the cost of purchasing a home and the age of entry into homeownership (Rothstein 2017; Bhutta and others 2020). These disparities can also be observed for other assets, including stocks, mutual funds, and savings and retirement accounts. As shown in Chart 1, Black consumers are less likely to own stocks and mutual funds. Even when they do own stocks, the value of those stocks is likely to be lower: according to the 2019 SCF, the median value of stocks owned was $12,000 for Black stockholders compared with $30,000 for white stockholders.

Chart 2: Black households have lower homeownership rates than white households across all income, education, and age groups



Sources: Board of Governors of the Federal Reserve System and author's calculations.

Given this large wealth divide, Black households may perceive that investing in cryptocurrency could help them gain financial ground relatively quickly. Some survey evidence suggests that Black consumers expect higher returns on cryptocurrencies than white consumers. According to Ariel Investments and Charles Schwab, 27 percent of Black investors expect annualized returns from cryptocurrencies of 20 percent or higher, while only 12 percent of white investors share that expectation (Schwab-Pomerantz 2022).

A second factor drawing Black consumers to cryptocurrencies may be the view that they are more trustworthy than traditional assets. For some Black consumers, a generational lack of trust in financial institutions has been passed down from historical experiences, such as the collapse of the Freedman's Savings Bank. In 1865, Freedman's was chartered by Congress for the benefit of those freed from enslavement, but when the bank became insolvent in 1874, $3 million (about $66 million in today's dollars) in total deposits were lost (Todd 2019). Cryptocurrencies rely on permanent, irrefutable records of ownership and a private key to access funds. Transactions take place on the publicly distributed blockchain ledger, so anyone can look up transaction data, including where, when, and how much of a cryptocurrency was sent from a wallet address and how much crypto is stored in a wallet. This transparency and accessibility may appeal to Black consumers distrustful of traditional financial institutions and of participating in a system that may not work in their best interests.

Third, Black consumers may perceive that cryptocurrencies "level the playing field" by opening opportunities to a more diverse group of investors. Indeed, a study by the Nonpartisan and Objective Research Organization at the University of Chicago (NORC) found that 44 percent of cryptocurrency traders are investors of color, compared with only 35 percent of stock investors (NORC 2021). Cryptocurrencies' decentralized structure has the potential to democratize financial services, offering a way for anyone, including consumers without bank accounts, to access financial services without having to go through a centralized authority. Cryptocurrency can easily be purchased with an internet connection and a computer or smartphone using apps such as PayPal, Cash App, Coinbase, and Stash. Cryptocurrency may help consumers overcome other financial barriers as well: unlike opening an account at a traditional financial institution, creating a cryptocurrency wallet does not require identity verification or a credit check.

Fourth, younger Black consumers may see the potential of blockchain technology even beyond its use in cryptocurrencies. Pew Research reports that more than 50 percent of the Black population in the United States are millennials or younger and are getting involved in STEM, cybersecurity, and other digital technologies (Major 2021). The "Web3" movement, an effort to shift the internet toward networks based on the blockchain, has created new types of investments such as nonfungible tokens (NFTs) and decentralized autonomous organizations (DAOs), with younger investors driving adoption.[3] Younger investors are more likely to view cryptocurrency and NFTs as legitimate growth investments and to believe that DAOs have the potential to improve the way that companies and organizations run (Matsumoto 2022).

Fifth, Black consumers may be influenced culturally to view investing in cryptocurrencies as a prudent move. Black athletes, celebrities, and politicians have promoted cryptocurrencies either by accepting them as a portion of their own compensation, endorsing or investing in the cryptocurrency industry themselves, or advocating for cryptocurrency as a payment option for employees—all of which infers value (Giacomazzo 2022). Crypto advertising appears to be working: a recent Harris Poll found that 58 percent of survey participants who had heard of cryptocurrency and 82 percent of current cryptocurrency traders agreed that advertisements about cryptocurrency do a good job at encouraging more people to trade cryptocurrency (Harris Poll 2022). In addition, information and educational materials about cryptocurrencies are easily accessible to Black consumers through social forums such as chat rooms, blogs, and fintech providers' sites, many of which target Black consumers as their main audience.

The risks of cryptocurrency ownership for Black consumers

Using cryptocurrency to gain financial security or to avoid interacting with centralized authority is not without risks. First, cryptocurrencies are highly speculative, volatile, unregulated, and not backed by a government. As a result, they are vulnerable to scams and wide fluctuations in price with little to no recourse for crypto owners. The steep cryptocurrency sell-off in May 2022 provides a cautionary example: the price of bitcoin plunged to its lowest point since 2020; Coinbase, the largest cryptocurrency exchange, lost a lot of value; and TerraUSD, a cryptocurrency that promoted itself as a stable means of exchange, collapsed. As of May 12, the value of cryptocurrencies had declined by more than $300 billion (Yaffe-Bellany, Griffith, and Livni 2022).

Second, the decentralized design of cryptocurrencies presents risks. If a cryptocurrency owner forgets their password or cannot access their private key, they will lose access to their assets. Unlike most other asset accounts, for which passwords can be reset or recovered from the account providers, crypto accounts have little to no options for password recovery (Popper 2021). Risks also come with using cryptocurrency exchanges. In the absence of FDIC insurance or anything resembling it, individual cryptocurrency owners could simply lose their investments if the exchange goes bankrupt or gets hacked: a 21st century version of Freedman's Savings Bank.

Third, the transparency of the blockchain may lead to privacy concerns, as transaction information is visible to other users. Blockchain technology may be the antithesis of efforts to give consumers "the right to be forgotten" and the ability to opt out of tracking. A related concern is the lack of transparency around transaction costs, as it can be difficult to predict or understand the cost of transacting with cryptocurrency, whether using it for payment or moving it from wallet to wallet.

To mitigate these risks and protect consumers and investors from significant damages, regulators and other government officials are taking action. In response to the nation's largest 401(k) provider, Fidelity, reporting that it would enable participants to put up to 20 percent of their retirement money into bitcoin if their employers allow it, the U.S. Labor Department issued a compliance assistance document reminding plan overseers that they are responsible for choosing "prudent" investment options, and strongly suggested that cryptocurrencies do not yet meet that bar. President Biden signed an Executive Order that charts the way for U.S. regulation of crypto assets (White House 2022). In a recent speech on regulating cryptocurrencies, Treasury Secretary Janet Yellen made the case that regulation should be based on risks, not technologies, and balance the improvements digital assets can offer the payment system with the hazards they present (Hussein 2022). A bipartisan group of U.S. senators recently announced plans to release a bill in June that seeks a legal framework for regulating cryptocurrencies (Competition Policy International 2022).

Conclusion

Black consumers may find cryptocurrencies appealing for several reasons, including historical context and the forward-looking views of younger Black consumers. Although cryptocurrencies have the potential to meet expectations, the highly speculative and volatile nature of cryptocurrencies cannot be ignored. The current steep sell-off of crypto assets is putting cryptocurrency risks on full display. Without the guardrails or remedies that accompany traditional financial services, cryptocurrencies are proving susceptible to some of the same pitfalls that have driven Black consumers from other financial investments. Black consumers' willingness to gravitate to a yet unproven financial asset signals the severity of the wealth gap, as well as the need to find meaningful solutions to address issues of trust and access to traditional financial services.

Endnotes

[1] The Board of Governors of the Federal Reserve System's most recent Survey of Household Economics and Decisionmaking (SHED) also included questions about consumer cryptocurrency ownership in 2021 (Board of Governors of the Federal Reserve System 2022). Although the cryptocurrency ownership rate for U.S. adults overall is slightly lower in the 2021 SHED (12 percent) than in the 2021 Pew survey (16 percent), the findings of the two surveys are generally consistent.
[2] The cryptocurrency ownership rate comes from the 2021 Pew survey, while the data on stock and mutual fund ownership is from the 2019 SCF, so I do not compare the exact ownership rates.
[3] NFTs are digital assets that exist on the blockchain and are being leveraged by creative professionals to exercise control over their work, more easily sell it, and more strongly protect against appropriation. DAOs are based on blockchain technology and enable groups to come together without a central leader or company dictating decisions.

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