



**Weekly Hot Take**

# IBIT Options: Growth Potential & Price Impact

Oct 4, 2024

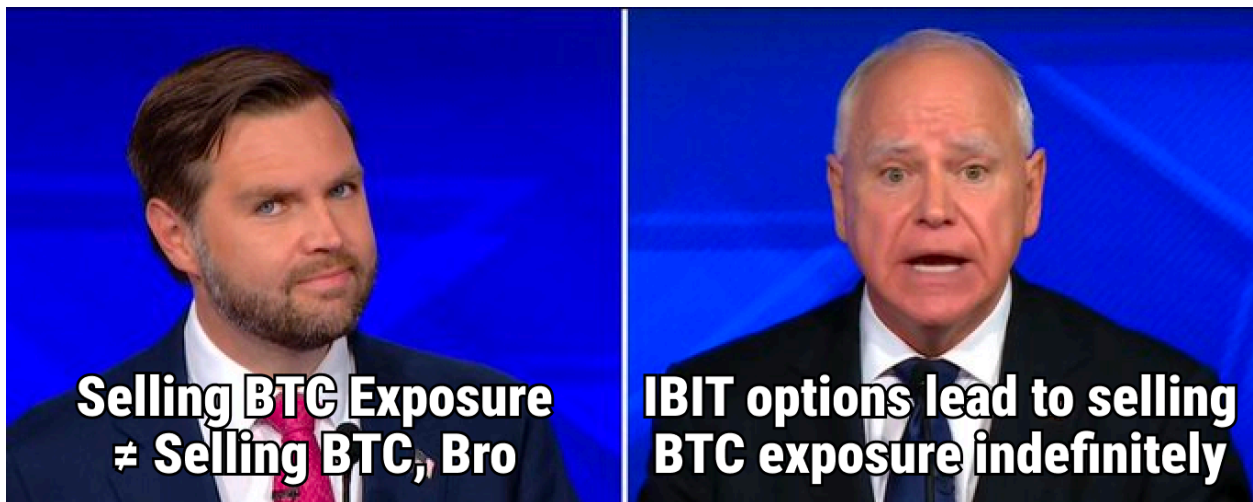
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**Figure 1 : Fact-Checking IBIT Option Transactions**



Source: @timcast, Presto Research

## Summary

- A strong symbiotic relationship between ETFs and ETF options has been observed in major asset class ETFs, such as SPY, QQQ, and GLD. If IBIT options are listed, they are likely to play a similar role within the IBIT ecosystem, reinforcing each other's growth significantly.
  - Having examined the open interest to market cap (OI/MC) ratio of relevant ETFs and their options, we estimate the open interest in IBIT option contracts will reach a \$20-30bn level, based on 1.0-1.4x ratio. Given that the OI/MC ratio for BITO, the closest proxy, is 1.5x, this is a conservative estimate in our view.
  - Concerns that ETF options will drive the BTC price down by enabling the 'indefinite selling of BTC exposure' are misguided, as selling paper BTC exposure is not the same as selling BTC itself. The availability of regulated instruments for hedging, leverage trading, and yield generation enhances Bitcoin's versatility as an investment asset and broadens its appeal to a wider range of investors, bringing more legitimacy to this emerging asset class.
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## 1. Introduction

A lot of commentary has been made on the impact of Bitcoin ETF options since the SEC's approval of the IBIT option on Sept. 20th. Among the various issues discussed, this report focuses on what is likely the most pressing question on the public's mind – i.e., the implications for BTC's price. This is especially relevant given concerns about potential selling pressure caused by the so-called 'paper BTC' supply.

To this end, the report first provides a brief overview of the ETF options market, then discusses the current status of the IBIT option application, and finally analyzes its growth potential and likely impact on BTC's price. While we do our best to keep derivative-speak at bay, those seeking background information on options can refer to Presto Research analyst Rick Maeda's [Crypto Derivatives Series II: Options](#).

## 2. ETF Options Market: Overview

To understand the ETF options market in the US, it can be helpful to make a side-by-side comparison between S&P 500 Index options and SPDR S&P 500 ETF Trust (SPY) options. SPY options are a good proxy for the broad ETF options market as they account for nearly half of the entire ETF options volume<sup>1</sup>.

### 2.1 Symbiosis Between ETF & ETF Option

As SPY's popularity grew after its introduction in 1993, the demand for options contract trading emerged from its investor base over time. Option contracts are agreements between two parties, where one party (the contract buyer) acquires the right, but not the obligation, from the other party (the contract seller) to buy or sell the underlying asset at a specified price at or within a certain time period. While options are primarily used for hedging, they can also be used for leveraged speculation and income generation.

Options on the ETF, rather than the index itself, offer two advantages: accessibility and flexibility. This is summarized in Figure 2.

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<sup>1</sup> 44.28%, according to [SPDR S&P 500 ETF Trust \(SPY\): Delivering Unrivaled Liquidity to Investors](#), State Street Global Advisors

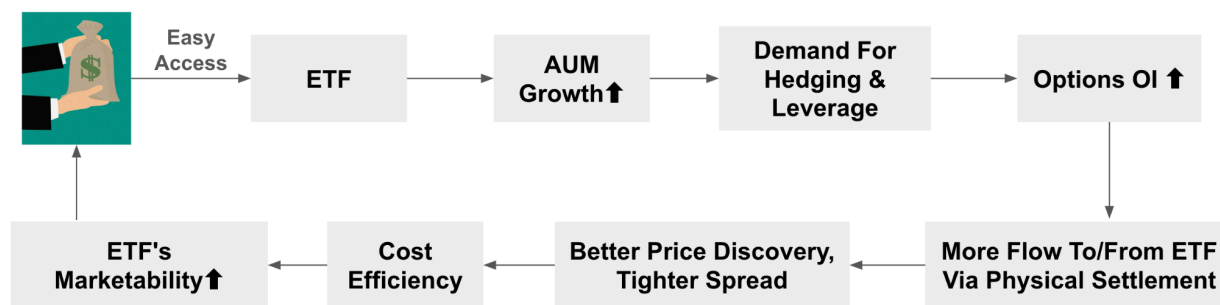
**Figure 2 : Options on Index vs ETF**

Options on	Exchange	Accessibility		Flexibility	
		Underlying	Notional Size (S&P 500=5,500)	Exercise	Settlement
<b>S&amp;P 500 Index (SPX)</b>	CBOE	500 Constituent Shares	\$550,000	European Style (exercisable only on expiry)	Cash
<b>SPY</b>	CBOE	SPY Shares	\$55,000	American Style (exercisable any time before expiry)	Physical

Source: CBOE, Presto Research

In a nutshell, the underlying asset of a SPY option is an ETF, which offers superior accessibility (smaller notional size and easier access to the underlying asset), making its options appealing to a broader audience. Additionally, its American-style exercise provides users with greater flexibility. More importantly, these characteristics create a positive feedback loop between the options and the underlying ETF, as shown in Figure 3, which has helped SPY become the world's largest ETF with \$590bn in AUM. This mechanism does not exist for index options, as settlement occurs in cash and only once at expiry.

**Figure 3 : Positive Feedback Loop**



Source: Presto Research

### 3. IBIT Option: What We Know So Far

The key details from the SEC's September 20th approval notice are as below.

- Listing: Nasdaq ISE
- Position Limit: 25,000 contracts.
- Contract Size: unknown
- Available Tenors: unknown

The timing of the listing is also unknown as the process requires additional approval from both the Options Clearing Corporation (OCC) and the Commodity Futures Trading Commission (CFTC), but neither is under any regulatory deadline for their response.

Historically, there have been instances where options listing applications did not cross the finish line due to a failure to reach consensus among the three agencies. Examples include the Abridged Physical Platinum

Shares ETF (PPLT) and the Abrdn Physical Palladium Shares ETF (PALL). That said, Bloomberg analyst James Seyffart assigns a 70% probability to the IBIT option listing approval before May 2025. He notes that options on futures-based BTC ETFs already trade on multiple exchanges, making a denial of the spot BTC ETF option listing unlikely, as it would likely be considered another "arbitrary and capricious" decision, as per the court ruling in Grayscale vs. the SEC.

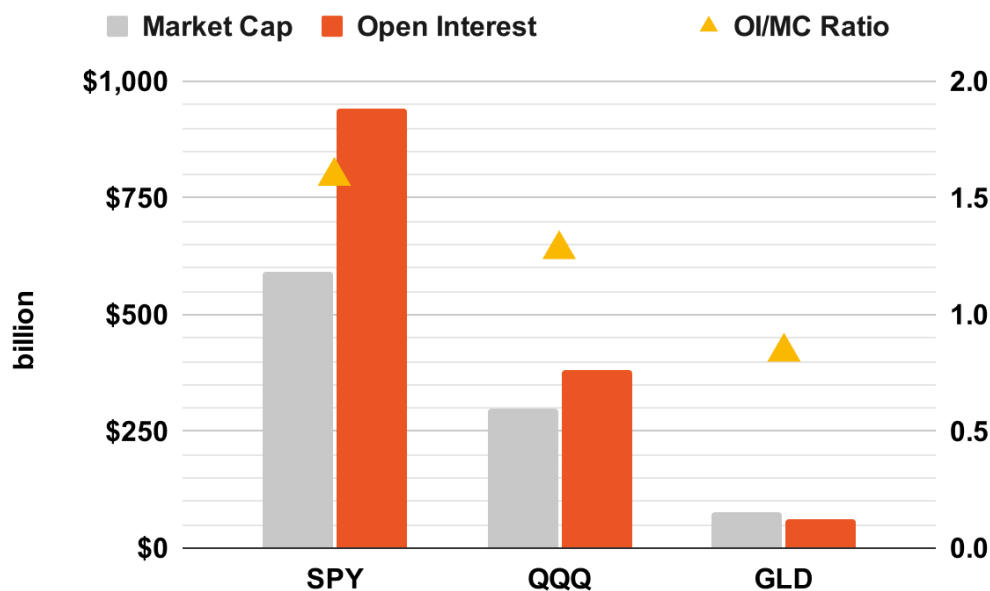
#### 4. Estimating Popularity and Price Impact

##### 4.1 \$20-30bn Open Interest

Useful references for estimating the IBIT option’s growth potential are the relationships between open interest (OI) and market capitalization (MC) of comparable assets. As such, we examine OI/MC ratios of: 1) major asset class ETFs and their options, and 2) bitcoin proxy equities and futures BTC ETFs which already have options. Their profiles and relevant data are summarized in Figures 4 and 5.

**Figure 4 : Major ETFs and Their Options Open Interest**

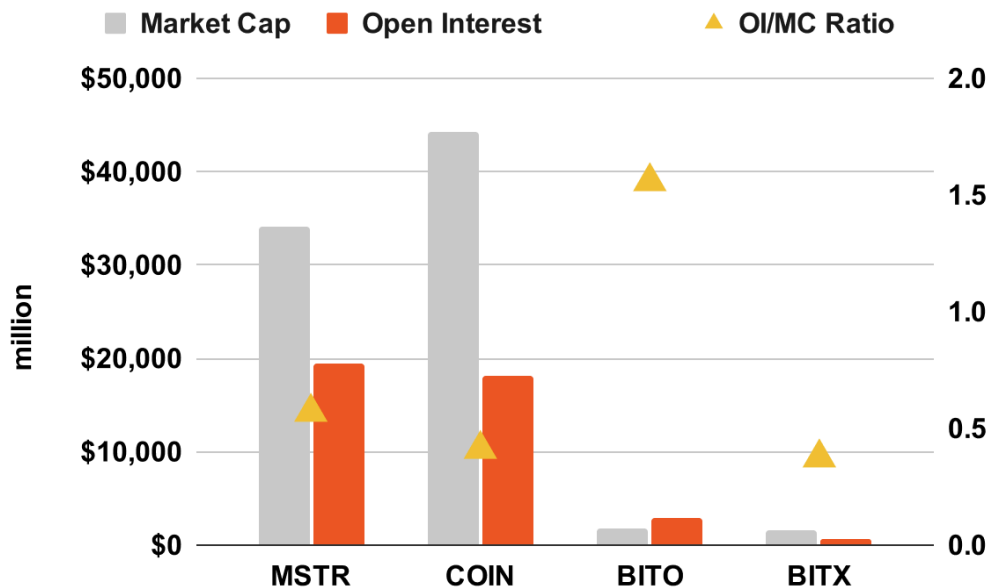
Name	Ticker	Shares Listing Date	Options Listing Date
SPDR S&P 500 ETF Trust	SPY	1/22/93	1/10/97
Invesco QQQ Trust, S1	QQQ	3/10/99	3/15/99
SPDR Gold Trust	GLD	11/18/04	6/3/08



Source: Bloomberg, CBOE, NYSE, as of Sept 27th, 2024

**Figure 5 : BTC-Proxy Equity & Futures BTC ETFs (\$1bn+ AUM) vs Their Options Open Interest**

Name	Ticker	Shares Listing Date	Options Listing Date
Microstrategy, Inc.	MSTR	6/11/98	N/A
Coinbase Global, Inc.	COIN	4/14/21	4/20/21
ProShares Bitcoin ETF	BITO	10/19/21	10/22/21
2x Bitcoin Strategy ETF	BITX	6/27/23	6/27/23



Source: Bloomberg, CBOE, ProShares, as of Sept 27th, 2024

Using the above data as benchmarks, applying a 1.0-1.4 multiple to IBIT's current market cap gives an estimated open interest range of \$20-30bn for IBIT's option contracts. Given that the OI/MC ratio for BITO, the closest proxy, is 1.5x, this is a conservative estimate in our view.

#### 4.2 'Selling BTC Exposure' ≠ Selling BTC

The common bear argument in recent weeks has been that the availability of option contracts makes it easier to 'sell BTC exposure.' While this is true (and it is also true for 'buying BTC exposure,' as well as for all other assets with options), 'selling BTC exposure' is not the same as selling BTC itself. Selling BTC exposure in the context of options trading typically means either: 1) buying the right to sell BTC at a lower price in the future (buying a put), or 2) receiving a fee (premium) for committing to deliver BTC if your counterparty exercises their right to purchase the BTC from you at a certain price in future (selling a call).

The fact that there is no limit on the number of these transactions can lead to confusion, as some associate this with "infinite selling." However, this is a misunderstanding, as these are so-called 'paper-transactions' and none of them *by themselves* create any selling pressure in the spot market. If anything, the opposite is more likely, as the second-order effect is that call option sellers may buy the underlying asset to protect themselves against the risk of a BTC price run-up. As described earlier, call option sellers are contractually obligated to deliver the underlying asset if the option is exercised.

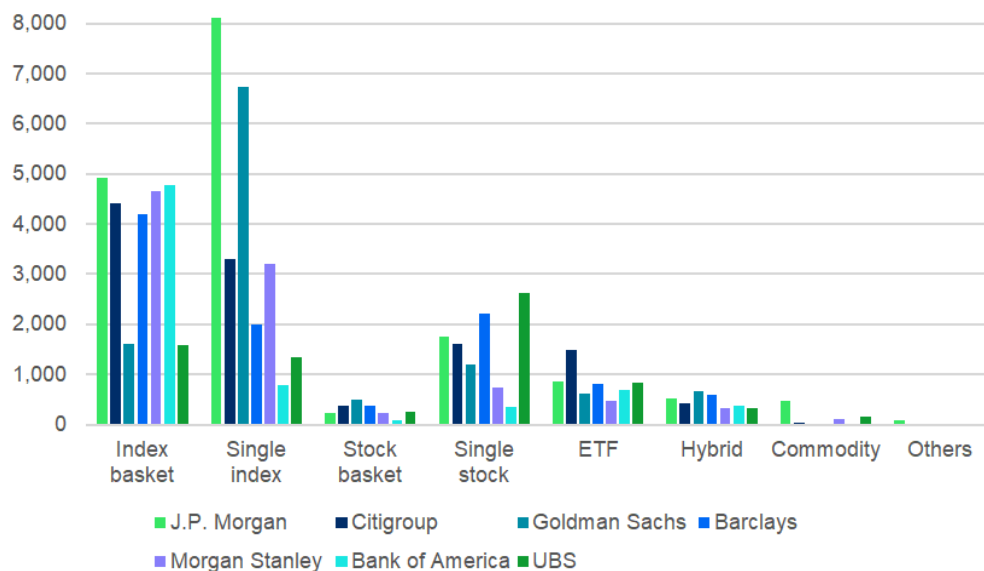
### 4.3 No Negative Precedent From Crypto-Native BTC Options

Crypto natives have been trading BTC options on ‘unregulated’ venues such as Deribit for half a decade, which today boasts a daily notional trading volume of \$40bn. Hedging activities originating from the options market may at times exert short-term impacts on the spot price, but there is no evidence that options trading on these venues creates structural or lasting downward pressure.

### 4.4 Bringing in New Institutional Investor Base

The availability of regulated instruments that can be used for hedging, leverage trading, and yield generation opens the door to a whole new class of institutional investors that were previously inaccessible. Structured notes are a prime example of investment products that utilize the yield generation feature of options (Figure 6). Just as spot ETFs have significantly expanded bitcoin's audience, options contracts further enhance its versatility as an investment asset and broaden its appeal to a wider range of investors, adding more legitimacy to this emerging asset class. A useful analogy may be the introduction of automobile insurance in the early days of the automobile industry, which contributed greatly to its mainstream adoption. Likewise, a put option is effectively insurance against Bitcoin's downside risk.

**Figure 6: Sales of SEC-Registered Structured Notes in 2023 by Asset Class (US\$ mn)**



Source: SRP

## 5. Final Words

Many experts have argued that the implications of Bitcoin ETF options could include lower volatility, increased BTC collateral lending, and futures basis compression.<sup>2</sup> These outcomes may well materialize, especially if the IBIT option grows to a significant size, as we estimated in this report. That said, one thing more certain than any other predictions is that the IBIT option represents a major upgrade to the spot BTC ETF as an investment tool, much like options on SPY, QQQ, and GLD did. This upgrade, which further legitimizes the asset class and attracts a new investor base, is structurally bullish, and its long-term re-rating potential is underpriced in our view.

<sup>2</sup> Episode 711, Why Bitcoin ETF Options Could Unlock Massive Amounts of Capital for Crypto, Unchained

## About Presto

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