

What Is Tokenomics?

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A Breakdown of Tokenomics

Tokenomics — the topic of understanding the supply and demand characteristics of cryptocurrency.

In the traditional economy, economists monitor the issuance of a currency using official money supply data. The numbers they report are generally called M1, M2 and — depending upon the country — M3 or M4 as well. An in-depth explanation of the four M categories is beyond this tokenomics analysis: just know that M1 is a measurement of the most liquid monies, M2 is less liquid, and so on. These numbers help to enable transparency and monitoring of different aspects of the supply of a currency.

These numbers are important because throughout history, kings, queens and governments have had a habit of creating additional money in their country. It turns out that running a country or fighting a war can be very expensive, and it was not always easy to raise revenues or balance a budget, which meant that it was often politically expedient to simply create more currency.

In the modern world, things like bank bailouts and pandemic responses have required governments around the world to create substantial amounts of new currency very quickly.

While governments oversee this process, creating additional currency can cause a slow, or sometimes fast, reduction in the value of the existing money. We call this reduction “inflation” and it is most visible when the prices of the things we buy increase year after year.

In contrast to this process, cryptocurrencies and tokens built on blockchain have pre-set, algorithmically created, issuance schedules. This means that we can predict with quite some accuracy how many coins will have been created by a certain date in time. Though it is possible for most cryptoassets to have this issuance schedule altered, it will normally require the agreement of many people and is very difficult to implement. This provides some comfort and security for owners, because they know to what degree their asset will be created in a way that is much more predictable than governments creating money.

What Is The Total Bitcoin Supply?

In total, there will be just 21 million [Bitcoin](#) produced. The entire process will end in around 2140. Until then, the number of new coins that are created via

the mining process will decrease by half, roughly every four years. This is known as the Bitcoin halving and was designed to create what economists call scarcity, therefore providing upwards pressure on prices.

While 21 million may sound like a very large number, when compared to the 8 billion or so people on earth, it is obviously incredibly small. It is this imbalance that leads many people to compare Bitcoin to gold and think of it as “hard” money.

As the first crypto to be created, the issuance process and schedule of Bitcoin has led the way for others. For example, [Bitcoin Cash](#), [Bitcoin SV](#) and [Zcash](#) also have a hard cap of 21 million coins. Others, such as [Litecoin](#), use the same framework but have a larger overall number.

However, there are coins whose schedule is very different. For example, both [Dogecoin](#) and [Grin](#) have issuance that is identical for every new block created forever, which means that their token supply is essentially unlimited. The founders of Grin hope that this feature will make it easier to maintain a stable price and thus become a more usable currency. It will take years to understand whether this actually happens.

In between these two positions are plenty of coins and a lot of tokens — many operating on [Ethereum](#) — that have a maximum issuance in place, but that number is very high. For example, [Tron](#) has a total supply capped at more than 100 billion.

There are also situations where the number of coins or tokens will reduce. Some projects have created rules in which a certain number will be burned —

which means that they will be transferred into a wallet that cannot be recovered — at set intervals. Burning usually relates to operating fees, so that the more an asset is used, the faster its tokens are burned.

Why Is Tokenomics Important When Investing in Cryptocurrency?

In his famous investment book, *Margin of Safety*, value investing legend Seth Klarman explains that, “In the short run supply and demand alone determine market prices.” If we believe that to be true and that it applies to cryptoassets using blockchain technology as well as the stock market, then understanding the factors that will impact either supply or demand are of vital importance to both speculators and investors.

In which case, there are a number of factors to consider. Perhaps the most important is to understand how the digital currency will be used. Is there a clear link between usage of the platform or service being built and the asset? If there is, there is a strong chance that a growing service will require purchases and usage that ultimately helps to increase the price. If there is not, what can the token be used for?

Other important questions to answer include the following:

- How many coins or tokens currently exist?
- How many will exist in the future and when will they be created?
- Who owns the coins? Are there some set aside to be released in the future to developers?
- Is there any information to suggest that a large number of coins has been lost, burned, deleted or are somehow unusable?

Tokenomics is also helpful as guidance to understand how much an asset

might be worth in the future. For example, many people new to crypto will think something like, “If this coin becomes as valuable as Bitcoin, then one day...” while in reality it might never be possible. As an example, let’s think of two coins mentioned above, Bitcoin Cash and Tron. Bitcoin Cash has the same total supply as Bitcoin, so thinking that one may become as valuable as the other in time has some legitimacy — it is possible. However, with more than 100 billion Tron existing, for one coin to be valued in the thousands of dollars, Tron would need to become the most valuable business in the history of the world — how likely is that to happen?

While these questions may seem to require complex answers, they will provide an extra way to view cryptoassets and help to understand whether one asset is more likely to have a great future than another.