SHARIYAH
REVIEW BUREAU

Shadows of Strategy: A Sharia Analysis of Crypto Trading Strategies

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Introduction to Crypto-assets

Crypto-asset is an umbrella term for all cryptos. There are different types of crypto-assets which can be defined as "digital representations of value that use cryptographic encryption techniques" . Crypto-assets are wholly digital in nature and only exist online. These assets utilise cryptography, peer-to-peer networking, and a public ledger to regulate the creation of new units, verify transactions, and secure the transactions without the intervention of any middleman . Thus, they are digital in nature and use cryptography to verify the validity of transactions. Crypto-operations occur on a decentralised peer-to-peer network and the data is recorded on the decentralised public ledger also known as blockchain.

A token can represent an asset, a utility, a service, a right or anything. According to Ernst & Young, a token tends to be designed to support a more narrowly defined, specific use case of distributed ledger technology. A token is not limited to one particular role; it can fulfil a lot of roles in its native ecosystem. Tokens typically exist on top of an existing smart contract platform, like Ethereum.

Shariah Considerations of Different Crypto-assets

The different types of crypto-assets and their potential rulings in Shariah are as follows:

1. Security Tokens

PwC defines security tokens as "digital tokens based on blockchain technology that are similar in nature to traditional securities. They can provide an economic stake in a legal entity: sometimes a right to receive cash or another financial asset, which might be discretionary or mandatory; sometimes the ability to vote in company decisions and/or a residual interest in the entity"[1.]

The US Securities and Exchange Commission wanted a clear test to identify tokens as securities. The most common method to differentiate securities from utility tokens is by using The Howey Test. This test refers to a 1946 US Supreme Court case involving the Howey Company of Florida. In brief, the company decided to lease half of its property to speculators based on the assumption that it would generate profit for them as a result of someone else's labour but failed to register the transactions with the US Securities and Exchange Commission (SEC). When the case finally arrived at the Supreme Court, it was deemed unprecedented and required a new method to assess what constitutes a security. Hence, The Howey Test came into fruition. According to the test, a transaction is considered a security if it meets the following criteria:

- It is an investment of money.
- The investment is in a common enterprise.
- There is an expectation of profit from the work of the promoters or the third party.

A token that passes the Howey Test is treated as a security token in the US. Security tokens are subject to federal securities and regulations since they derive their value from external, tradable assets.

Industry experts differentiate between security tokens and tokenized securities. The critical difference between the two is that security tokens are newly issued securities that function on distributed ledger while tokenized securities are just token representations of already existing financial products. Thus, if an investor has an ownership interest in a new financial product with security features, it is a security token. If an investor takes an existing asset and wraps it in a token, it is a tokenized security[2].

1 PwC (2018), In depth – A look at current financial reporting issues, Available from: https://www.pwc.com/gx/en/audit-services/ifrs/publications/ifrs-16/cryptographic-assets-related-transactions-accounting-considerations-ifrs-pwc-in-depth.pdf

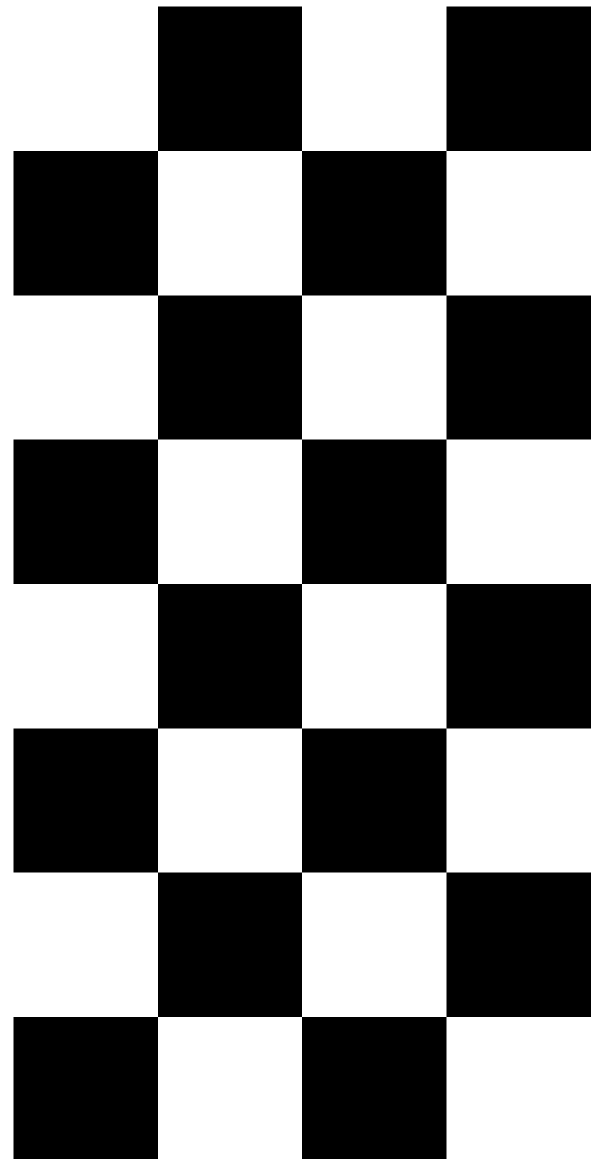
2 Cryptonews, What is a Security Token Offering?, Available from: https://cryptonews.com/guides/what-is-a-security-token-offering-sto.htm

From a Shariah compliance perspective, a security token must undergo Shariah screening. Any token offering whose core business activity is from the following industries is non-Shariah compliant:

- Riba-based conventional financial services
- Exchanges and platforms for conventional non-Shariah compliant investments
- Trading in risk and Gharar such as insurance companies
- Gambling, Qimar and Maysir activities such as gambling and betting platforms
- Alcohol and prohibited beverages
- Pork related products and non-halal food production, packaging, processing or any direct activity linked to unlawful consumables
- Tobacco related products
- Illicit adult industry such as pornography
- Non-Shariah compliant entertainment

If a security token passes the above, it must meet the following criteria:

1. Total interest and income from any non-compliant activity must not exceed 5% of total revenue.
2. Interest-taking deposits must be less than 30% of the market capitalisation or total assets.
3. Interest-bearing debt must be less than 30% of the market capitalisation or total assets.



2. Utility Tokens

Utility tokens are digital tokens functioning within a blockchain that provide users with access to a product or service and derive their value from that right. Utility tokens give holders no ownership in a company's platform or assets and, although they might be traded between holders, they are not primarily used as a medium of exchange. These tokens are usually created with a specific purpose in mind, bespoke to the project that issues them. They can be exchanged for specific services such as distributed storage, in-app currency or for more operational purposes. The value of these tokens is usually based on their expected use in the project for which they were intended. Another way to understand them is to consider them as gateway tokens which:

- Give holders a right to use the network
- Give holders a right to take advantage of the network by voting.[3]

Utility tokens grant access to utility and services. Any token which gives a non-Shariah compliant utility, service or access to Shariah non-compliant activities is impermissible to own and trade. It is not permissible to trade the rights to an impermissible service or utility. The Shariah rulings of *Bay' (trading) will apply to utility tokens.*

3. Asset-backed tokens

According to PwC, an asset-backed token is "a digital token based on blockchain technology that signifies and derives its value from something that does not exist on the blockchain but instead is a representation of ownership of a physical asset (for example, natural resources such as gold or oil)"[4].

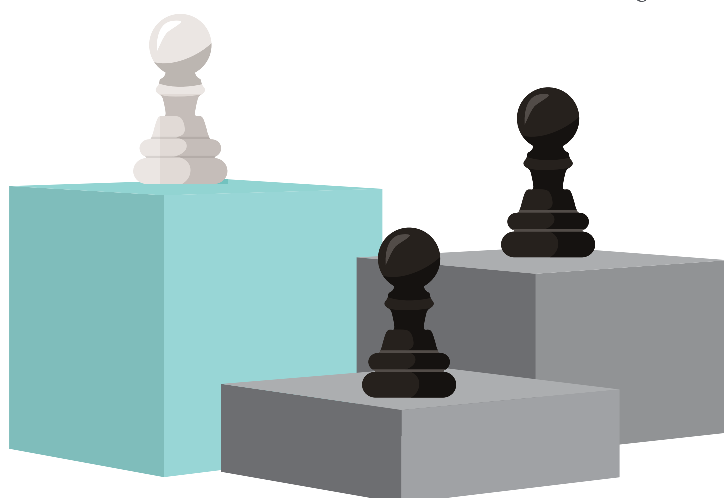
For such a token to be Shariah compliant, the following needs to be ensured:

a. The token represents *Māl*, meaning it is beneficial, has utility, can be stored and it is something humans have an interest in.

b. The token is *Mutaqawwim*, meaning it is lawful in and of itself.

c. The token represents ownership of the underlying asset and not simply a correlation in price to an underlying commodity. This is crucial, otherwise, it can be a derivative token which is not Shariah compliant.

Therefore, every time an asset-backed token is exchanged, it must correspond to the transfer of ownership of the underlying commodity. The token therefore is a digital representation of the commodity and evidence of ownership. An asset-backed token is the tokenisation of an asset. If a Shariah non-compliant commodity is being tokenised and sold, trading such a token will not be permitted as it involves trading Shariah non-compliant assets.



3 Rosic, A, (2017), What is an Initial Coin Offering? Available from: https://blockgeeks.com/guides/initial-coin-offering/
4 PwC (2018), In depth – A look at current financial reporting issues, Available from: https://www.pwc.com/gx/en/audit-services/ifrs/publications/ifrs-16/cryptographic-assets-related-transactions-accounting-considerations-ifrs-pwc-in-depth.pdf

4. Governance tokens

Governance tokens grant their holders governing rights on a protocol. As decentralised protocols increase, the need to grant decision-making processes to users increases. Governance tokens allow stakeholders to collaborate, coordinate and vote how the network is managed. These tokens fuel blockchain-based voting systems. As an example, the Maker Protocol, the governance token is MKR.

For the Shariah compliance of a governance token, the platform or protocol must be Shariah compliant, and the decisions that are being made and the issues being voted for must be Shariah compliant.

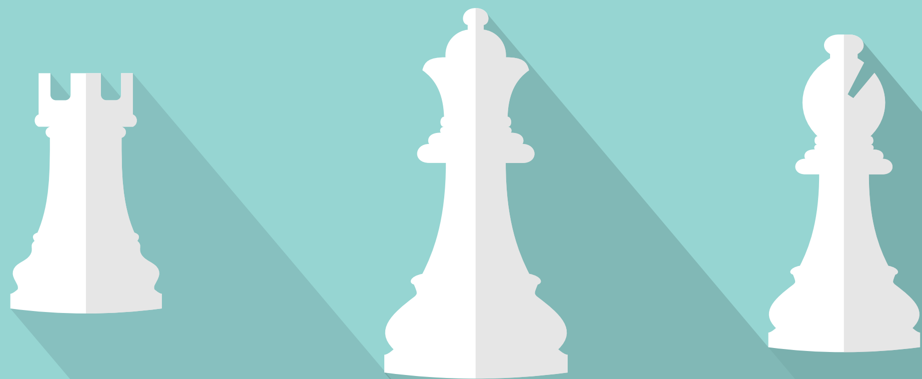
5. Platform tokens

Some industry experts have coined the term platform tokens for tokens used as fuel or gas on a network. For example, Ether (ETH) is used to fuel transactions on the Ethereum network. Tokens can be built on Ethereum, but Ether is still required to send a token. It funds the mining costs (it pays the computers that verify transactions on the Ethereum network). Since these tokens fuel the operations of the platform and network, they are referred to as platform tokens.

From a Shariah perspective, these are digital assets used as 'fuel' on a platform. The utility is fuel and to power transactions and processes.

6. Hybrid tokens

Some tokens have dual or triple use cases and can have multiple benefits. For example, NEO (NEO) is staked in a wallet to earn a dividend. This dividend is known as GAS. Tokens can be built on NEO, just like they can on Ethereum. When sending a token on the NEO network, you need to pay GAS as a transaction fee, the same way that Ether is used to pay Ethereum fees. Similarly, Dash (DASH) allows users to vote on important decisions for the Dash network. If there is an idea suggested to upgrade the DASH network, those holding enough Dash can vote to decide whether the upgrade should happen. These voting rights allow the holders of DASH to have a say in how the project evolves.



Shariah Considerations of the Types of Orders

In this section, we will look at the types of transactions offered by different crypto exchanges from a Shariah compliance perspective.

Crypto exchanges typically offer various types of orders, such as limit order, market order, stop-limit order, trailing stop order, post only order, one-cancels-the-other order, and more[5].

A limit order is an instruction to execute a trade at a level that is more favourable than the current market price. There are two types of limit orders: entry orders (that open a new position) and closing orders (that terminate an existing position). Limit orders allow you to specify the minimum price at which you will sell, or the maximum at which you will buy, an asset.

A market order is an order to buy or sell a stock at the market's current best available price. A market order typically ensures an execution, but it does not guarantee a specified price.

A stop-limit order is an instruction to submit a buy or sell limit order when the user-specified stop trigger price is attained or penetrated. The order has two basic components: the stop price and the limit price. When a trade has occurred at or through the stop price, the order becomes executable and enters the market as a limit order, which is an order to buy or sell at a specified price or better.

A sell trailing stop order sets the stop price at a fixed amount below the market price with an attached "trailing" amount. As the market price rises, the stop price rises by the trail amount, but if the stock price falls, the stop loss price doesn't change, and a market order is submitted when the stop price is hit. This technique is designed to allow an investor to specify a limit on the maximum possible loss, without setting a limit on the maximum possible gain. "Buy" trailing stop orders are the mirror image of sell trailing stop orders, and are most appropriate for use in falling markets.

A stop-loss is a type of market order that involves you setting an off-book instruction to sell at a specific price. As the name might indicate, it's designed to protect you from any significant losses.

From a Shariah compliance perspective, the ruling of all such orders is that they are instructions to your broker (*Simsar*) or agent (*Wakil*), depending on the contractual specifics. These orders are generally Shariah compliant as they are informing one's representative when to trade. In that sense, it is a restricted form (*Muqayyadah*) of representation.

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5 https://cryptonews.com/reviews/binance/
https://blockonomi.com/binance-review/
https://99bitcoins.com/bitcoin-exchanges/binance-review/
https://www.investopedia.com/binance-vs-coinbase-5120852

The Types of Trades and their Shariah Analysis

Margin trading

Margin trading is a method of trading assets using funds provided by a third party. When compared to regular trading accounts, margin accounts allow traders to access greater sums of capital, allowing them to leverage their positions. Essentially, margin trading amplifies trading results so that traders are able to realize larger profits on successful trades. This ability to expand trading results makes margin trading especially popular in low-volatility markets, particularly the international Forex market. Still, margin trading is also used in stock, commodity, and cryptocurrency markets.

In traditional markets, the borrowed funds are usually provided by an investment broker. In cryptocurrency trading, however, funds are often provided by other traders, who earn interest based on market demand for margin funds. Although less common, some cryptocurrency exchanges also provide margin funds to their users.

When a margin trade is initiated, the trader will be required to commit a percentage of the total order value. This initial investment is known as the margin, and it is closely related to the concept of leverage. In other words, margin trading accounts are used to create leveraged trading, and the leverage describes the ratio of borrowed funds to the margin. For example, to open a $100,000 trade at a leverage of 10:1, a trader would need to commit $10,000 of their capital.

Margin trading can be used to open both long and short positions. A long position reflects an assumption that the price of the asset will go up, while a short position reflects the opposite. While the margin position is open, the trader's assets act as collateral for the borrowed funds. This is critical for traders to understand, as most brokerages reserve the right to force the sale of these assets in case the market moves against their position (above or below a certain threshold).

For instance, if a trader opens a long leveraged position, they could be margin called when the price drops significantly. A margin call occurs when a trader is required to deposit more funds into their margin account in order to reach the minimum margin trading requirements. If the trader fails to do so, their holdings are automatically liquidated to cover their losses. Typically, this occurs when the total value of all of the equities in a margin account, also known as the liquidation margin, drops below the total margin requirements of that particular exchange or broker[6].

When trading with margin or a perpetual futures contract (available on Binance), trades will incur daily expenses. Funding fees and interest payments are taken into account on all trades, every day. Daily interest expenses can add up quickly, especially when a position is held over a long period. These fees and interest payments can be avoided altogether when trading a quarterly futures contract. Quarterly contracts on Binance incur no daily interest charges or fees, making them the ideal product for long-term holders.

From a Shariah compliance perspective, when funds of others are used, the transaction falls under the scope of *Qard* - lending in Shariah. It is from among the most sensitive contracts that function for a very specific purpose. Qard is gratuitous, charitable and a form of support to one another, and as such, it cannot be monetised. A famous juristic maxim states: "Any loan which draws an increment is Riba" (Ibn Abi Shaybah). Therefore, crypto margin trading typically charges daily fees for the facility, which is not justified from a Shariah perspective. As a result, margin trading in such a manner is not Shariah compliant.

6 https://academy.binance.com/en/articles/what-is-margin-trading

Swap farming

Instead of trading directly with another party, automated market makers allow a person to trade coins from a liquidity pool. Tokens are pooled together, and the price of each token is decided by its ratio. For example, one user could contribute an equal amount of BNB and BUSD tokens to the BNB – BUSD pool. Someone else could then utilize these tokens to make a fee-based exchange between BNB and BUSD.

Therefore, if swap farming facilitates the use of your deposited tokens by others, then this will again fall into lending. From a Shariah perspective, this would also be impermissible to engage with as the fees would be a form of Riba.

Binance Futures

Futures trading is similar to margin but different in a few key aspects. Firstly, when making a futures trade, traders buy or sell contracts representing the value of a specific cryptocurrency. This means that, unlike with margin trades, the trader does not own the underlying cryptocurrency. Instead, traders exchange a contract that sets an agreement to either buy or sell at a future date, hence the name.

Crypto futures contracts are often used to hedge against volatility and adverse price movements on an underlying asset. Like margin trading, futures contracts allow investors to gain significant capital exposure to protect a portfolio. By hedging, traders need not compromise their cryptocurrency holdings or liquidate them at an unfavourable price.

Because futures contracts don't trade directly with an asset, price volatility opens the door for profit, even when a market crashes. Thus, futures traders can capitalize on market volatility at their discretion despite what may happen in price action.

An important part of futures trades is that they are coupled with protective features to safeguard traders, lenders, and the exchange. For example, exchanges like Binance often operate risk management mechanisms such as insurance funds to protect the liquidity and funds on hand.

The majority of Shariah scholars are of the view that conventional Futures and Forward contracts are not Shariah compliant. This was the resolution of the International Islamic Fiqh Academy as well as the Islamic Fiqh Academy of Muslim World League[7]. The AAOIFI Standard No.20 clearly states:

"5/1 Futures

5/1/1 A contract that is binding under law. It is concluded on the trading floor of the exchange for the sale and purchase of commodities or financial instruments for a period linked to the near future. The transaction is arranged with the mentioning of the quantity, type and category along with the statement of the date and place of delivery. As for the price, it is the sole element that varies, and it is ascertained in the trading hall.

5/1/2 The Shariah rule for futures contracts It is not permitted according to the Shariah to undertake futures contracts either through their formation or trading."

The Shariah scholars object to Futures contracts due to the following reasons:

1. Trading before possession

2. Qimar activity

3. Sale of debt for debt

The exchange of a debt for a debt also known as *Bay' al Dayn bil Dayn* or *Bay' al-Kali bil Kali*. The AAOIFI Shariah Standard No.10 on Salam states:

"Again, any delay in payment of the capital and dispersal of the parties renders the transaction a sale of debt for debt which is prohibited, and the scholars agreed on its prohibition. Ibn Rushd said: "As for sale of debt for debt, Muslim scholars are unanimous regarding its prohibition."

7 International Islamic Fiqh Academy. (1992a). Qararat al-Majma', Seventh Session, Resolution 1 Financial Markets. Jeddah: International Islamic Fiqh Academy.
International Islamic Fiqh Academy. (1992b). Qararat al-Majma', Seventh Session, Resolution 3 Istisna contract. Jeddah: International Islamic Fiqh Academy.
Islamic Fiqh Academy of Muslim World League. 1984. Fatawa al-Majma, Seventh Session-Financial Securities and

Vanilla Options

Options can be explained as having a right to do something at a specific time. Someone who holds an Options Contract has the right to perform a specific action at a given time in the future. A user who holds an Options (Buyer) to the expiration date can choose whether they want to exercise that right (Favourable), or give up that right (Unfavourable). The Seller of an Options is obligated to match the Buyer.

There are two types of options:

1. Call Options: This gives the right to buy a certain quantity of a certain commodity at a certain price within a certain period of time in the future.

2. Put Options: This gives the right to sell a certain quantity of a certain commodity at a certain price within a certain period of time in the future.

For the Seller, profit comes from the cost of the Options. For example, if after buying an Options there is no profit to be made by holding due to the difference between the last price of the underlying asset and the strike price, the Buyer will choose to give up the right to exercise the options. The Options Seller would not need to pay any extra fees and the collateral will be returned to the seller.

Binance Vanilla Options are European-style Options, so the buyer cannot choose whether to exercise their right until the expiration time. From the start time to the time the Options are exercised, the user is able to buy or sell directly.

The AAOIFI Standard 20, Sale of Commodities in Organised Markets has declared the impermissibility of options. The standard describes options and states:

"5/2/1 A contract by means of which a right is bestowed -but not an obligation- for the purchase or sale of an identified item (like shares, commodities, currencies, indexes or debts) at a determined price and for a determined period. There is no obligation in this contract except on the person selling this right.

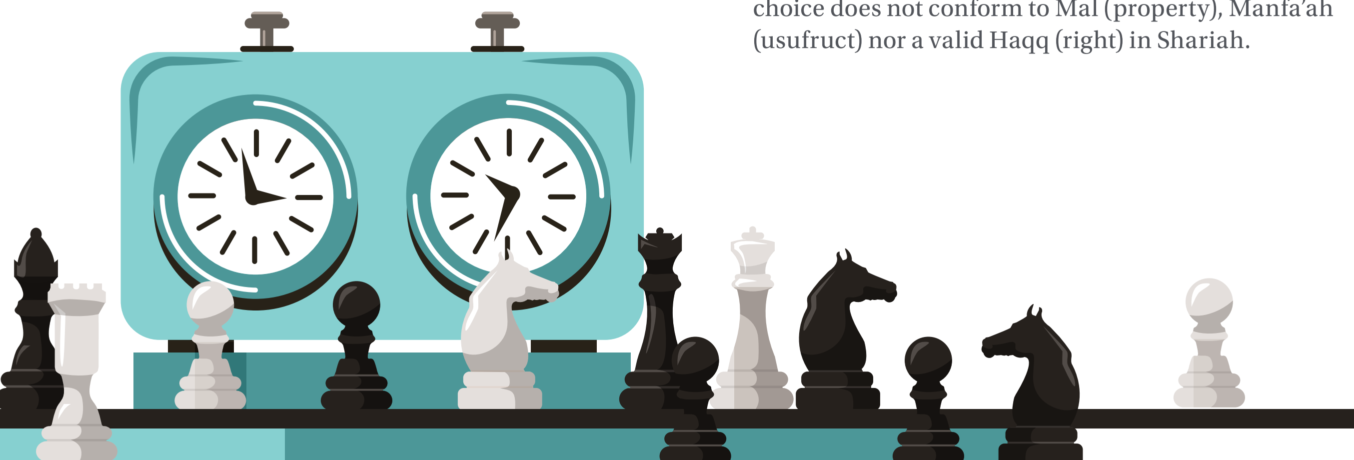
5/2/2 The Shariah rule for options

Options indicated above are not permitted neither with respect to their formation nor trading."

Options are prohibited for two principle reasons: Gharar and an invalid subject matter (mabi') of sale.

Options are a form of bay' al-Gharar. The exercising of the option is unknown and uncertain and hence the uncertainty in the subject matter makes it Gharar. It is a right which enforces another contract, however, the enforcing is uncertain and suspended on an uncertain event.

Another reason for the prohibition of options is the non-compliance of the subject matter of sale with Shariah. An option represents the power, the right to choose. When you own an option, you can choose whether to buy an asset or not, or (with different type of options) whether to sell an asset or not. A choice is not something for which consideration can be given under Shariah law. Selling 'choices to transact' is invalid as a choice does not conform to Mal (property), Manfa'ah (usufruct) nor a valid Haqq (right) in Shariah.

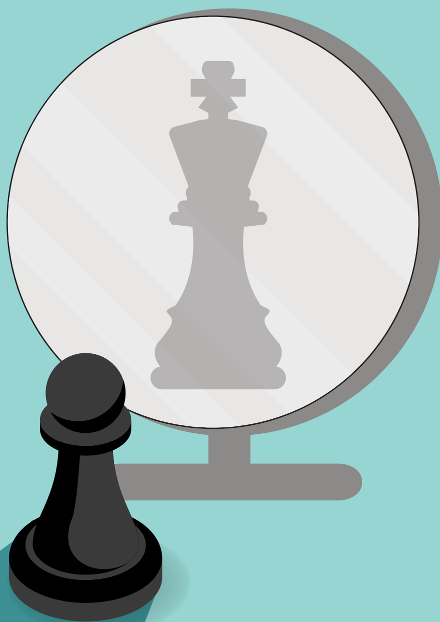


Leveraged Tokens

Another type of trade in crypto markets is leveraged tokens. Binance Leveraged Tokens (BLVT) are a type of derivative product that give you leveraged exposure to the underlying asset. Like other tokens, leveraged tokens can be traded on the spot market. Each leveraged token represents a basket of perpetual contract positions. The price of a leveraged token moves along with price changes in the perpetual contract market, and the leverage level moves up and down accordingly.

Unlike margin trading, leveraged tokens allows a person to gain exposure to leveraged positions without having to put up any collateral, maintain a maintenance margin level, or worry about the risk of liquidation. However, even though they don't have to worry about the risk of liquidation, there are still risks associated with leveraged token positions, such as the effects of price movements in the perpetual contracts market, premiums, and funding rates.

So a BLVT is essentially a tokenized version of leveraged futures positions. Leveraged tokens are not considered as Shariah compliant since they entail futures and are leveraged.



COIN-M Futures

COIN-margined perpetual contracts are a type of derivative that derives its value from an underlying cryptocurrency. They are an alternative way to gain exposure to a cryptocurrency without having to own it.

With perpetual contracts, you can trade cryptocurrencies with leverage, which means you can magnify small movements in price to potentially generate outsized profits.

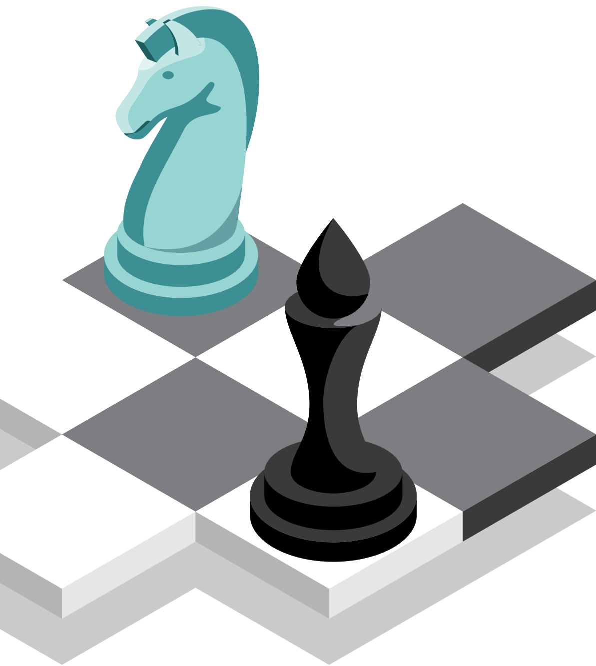
Just like USDT-margined perpetual contracts, COIN-margined perpetual contracts do not have an expiry date. Therefore, users do not need to keep track of various delivery months.

Coin-M futures contracts are not Shariah compliant either. They facilitate exposure to a price without owning the underlying, and without owning anything valid to track the price. Similarly, they have the same arguments against them as expressed in the futures section.

Shariah Considerations of Different Trading Styles

Here, we will define the following types of strategies and then consider the Shariah guidance on them:

1. **Scalping**
2. **Day trading**
3. **Range trading**
4. **Intraday trading**
5. **Swing trading**
6. **Position**



Scalping is a strategy in which a trader takes advantage of small variations in currency prices in lower time frames. Scalping is based on the concept that all the coins make an upward movement after experiencing a fall in prices, yet making accurate predictions is nearly impossible. A scalper attempts to take as many small profits as possible, which is the opposite of the popular concept of HODL.

Day trading is an investing strategy that relies on frequent trades of one or more securities throughout the day to turn a profit. While traditional buy-and-hold investors are concerned with the long-term performance of a company, day traders seek to take advantage of more immediate profit-making opportunities.

Range trading is based on defining a range. Cryptos will constantly define a range they are trading in. Generally, this range will be a type of consolidation (either accumulation, big players getting more coins for the next leg up, or distribution, selling coins at a high before the big players let the market drop). A range trader trades the range and sets stops, they don't really care if they are trading the range at the all-time high, or trading the range at the local bottom, as they are simply buying the bottom of the range with a stop, and then selling the top of it (or scaling out toward the top). This can be a type of day trading or intraday trading, but the goal is to trade the range, not to buy into an uptrend, or buy after a downtrend, etc.

Intraday trading is a style of day trading that allows for holding positions over more than one day. The reality is traders do this and there is no rule that it can't be successful. In crypto, the market never closes, so there is no end to a trading day.

Swing trading is all about finding support and trading to the next resistance level, or more generally picking an entry and a target and holding the position until your target is hit or other exit conditions are met. Swing trading is generally done over the course of days or weeks. Crypto goes up and down in waves, swing trading is all about finding the bottom of the wave and riding it to the top (with long positions; it is the opposite with short positions).

Position trading is like a zoomed out version of swing trading or like the trading version of investing. Here, a trader tries to build/take a long position low or short position high and then stick with that position for weeks, months, or even years.

What makes crypto trading different to shares trading is that in cryptos, possession is immediate as the crypto is sent to one's wallet. Settlement occurs immediately with the trade, whereas in traditional assets like shares and stocks, settlement is typically T+2. Hence, there is acceptability to trade the crypto-asset immediately after taking possession. The above trading strategies must comply with the following rules to be Shariah compliant:

- **Rule 1:** The crypto-asset of sale must be existing at the time of sale.
  Thus, a thing which has not yet come into existence cannot be sold. If a non-existent thing has been sold, though by mutual consent, the sale is void according to Shariah.

- **Rule 2:** The crypto-asset must be in the ownership of the seller at the time of sale.
  Therefore, what is not owned by the seller cannot be sold. In other words, If something is sold before acquiring its ownership will result in making the sale void.
  Example: A sells to B a car which is presently owned by C, but A is hopeful that he will buy it from C and shall deliver it to B subsequently. This sale is void, because the car was not owned by A at the time of sale.

- **Rule 3:** The crypto-asset must be in the physical or constructive possession of the seller when he sells it to another person.

"Constructive possession" means a situation where the possessor has not taken the physical delivery of the commodity, yet the commodity has come into his control, and all the rights and liabilities of the commodity are passed on to him, including the risk of its destruction.

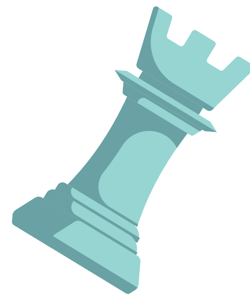
The gist of the rules mentioned in paragraphs 1 to 3 is that a person cannot sell a commodity unless:

(a) It has come into existence.

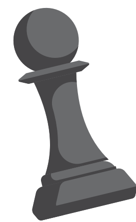
(b) It is owned by the seller.

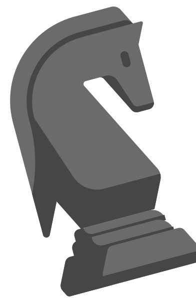
(c) It is in the physical or constructive possession of the seller.

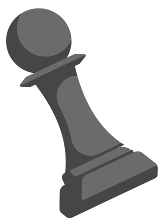
The rules mentioned apply to ordinary sales, however, Bai' Salam and Istisna' are exempted from the above.

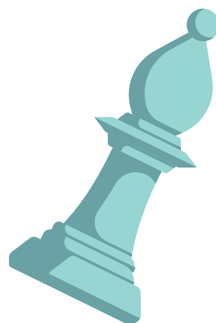


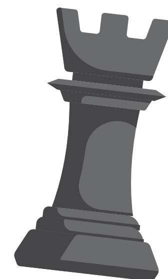
- **Rule 4:** The sale must be instant and absolute. Thus, a sale attributed to a future date or a sale contingent on a future event is void. If the parties wish to effect a valid sale, they will have to effect it afresh when the future date comes or the contingency actually occurs.
- **Rule 5:** The crypto-asset must be a property of value.
  Hence, a thing having no value according to the usage of trade cannot be sold or purchased.
- **Rule 6:** The crypto-asset should not be a token used for unlawful purposes only.
- **Rule 7:** The crypto-asset must be specifically known and identified to the buyer.
- **Rule 8:** The delivery of the crypto-asset to the buyer must be certain and should not depend on a contingency or chance.
- **Rule 9:** The certainty of price is a necessary condition for the validity of a sale. If the price is uncertain, the sale is void.
- **Rule 10:** The sale must be unconditional. A conditional sale is invalid unless the condition is recognised as a part of the transaction according to the usage of trade.

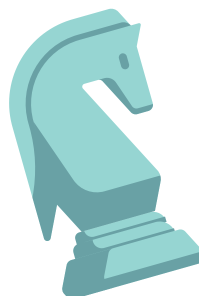


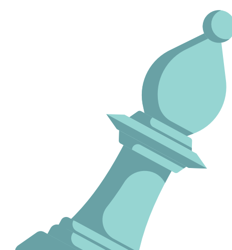












Shariah Considerations of Different Crypto Investing Strategies

An investment strategy is a set of instructions designed to help an investor make investment decisions, including what to invest in, when to invest and how much to buy. There are many investment strategies to choose from, ranging from conservative strategies that focus on low-risk portfolio management, with the objective of wealth protection, to aggressive strategies, which focus on high-risk portfolio management with the goal of capital appreciation. In this section, we will consider the compliance of the following strategies:

1. Hodling

2. Earning a yield

3. Dollar cost averaging

4. Lump sum investing

5. Value investing

6. Value averaging

7. Contrarian investing

8. Growth investing

HODL - which is both known as a misspelling of the word 'hold' as well as an abbreviation for 'hold on for dear life' - is a long-term strategy that has proven to be one of the easiest and more effective approaches out there. The strategy is simple, you buy your tokens, you hold them and you wait. Holding is common for those who invested early in different projects.

Earning a yield is similar to hodling, which is to bring the token holder a financial return over the long term. The difference is that buying and holding involves buying an asset at one price with the expectation that it will increase in value, then selling it at the higher price. Earning a yield involves holding your assets and potentially earning passive income while you hold - like how a savings account pays interest on your balance.

Dollar cost averaging is when an investor allocates an amount of capital to an investment periodically (e.g. investing €500 per month). The benefits of this approach are that investors don't need to worry about short-term volatility, as they will be adding to their portfolio regardless of whether the market is up or down. The focus is long-term returns, as assets with strong fundamentals tend to increase in value over the long term.

Lump sum investing is pretty much the opposite of dollar cost averaging. Instead of investing a small sum regularly, here the investor goes "all in" - they invest all the money they have available at a certain point in time. For example, if a person received a bonus, a or an inheritance of $10,000, with the lump sum strategy they would invest it all at once, rather than splitting that amount into smaller investments (e.g. $1,000 per month).

These two strategies are often compared, with the best strategy for an investor depending on their investment style, the type of asset they want to invest in or how much liquidity they have at any one time.

Value investing focuses on assets that are undervalued, meaning their real value is much higher. The concept was introduced by Benjamin Graham, also known as the father of value investing. It was then made famous by Warren Buffet, the world's most famous value investor. Essentially, if an investor believes an asset is undervalued, it's price should increase once the market sees its value.

Value averaging was introduced by Michael E. Edleson, Managing Director of Morgan Stanley and former Harvard professor. The value averaging strategy is similar to value investing with a slight difference: the amount you invest periodically is more flexible and depends on market situations.

Contrarian investing happens when investors purposefully go against current market trends by buying when most investors are selling, or the opposite. Warren Buffett said "Be fearful when others are greedy, and greedy when others are fearful". This quote summarises what contrarian Investing is about.

Growth investors do not care about the market price or the intrinsic value of an asset. These investors are interested in projects or tokens that display above-average growth signs. This strategy is generally more short-term than the others.

When it comes to strategies, the Shariah is not overly prescriptive. The Shariah has left it to us to try our best to earn a living within a defined framework. As long as a strategy fulfils the guidelines of trading discussed earlier, and is not harming anyone or intentionally manipulating, then it would be acceptable. From the list above, the most concerning is the yield earning strategy, as there are several non-compliant yield-earning strategies in the crypto-market.

Shariah Considerations of Manipulative Actions

1. Pump and Dump

The crypto market's most prevalent offender is the pump and dump, which involves a group of people working together to artificially inflate a coin's value. Pump and dumps usually target low-market cap coins that are available on limited exchanges. The group's insiders will buy a coin early and dump it once there is enough attention from traders and investors buying in. In recent years, pump and dumps have become more accessible via social media communities like Reddit, Telegram and Discord[8].

In essence, they will buy an asset for a low price all at once, prompting the price to rise. This sudden and rampant increase in an assets nominal value will prompt unknowing traders to jump in and purchase the asset as they hope to ride a bull market. The original buyers then sell (dump) the assets to make a quick profit. This shift in supply and demand often causes many users to make a significant loss.

2. Whale Wall Spoofing

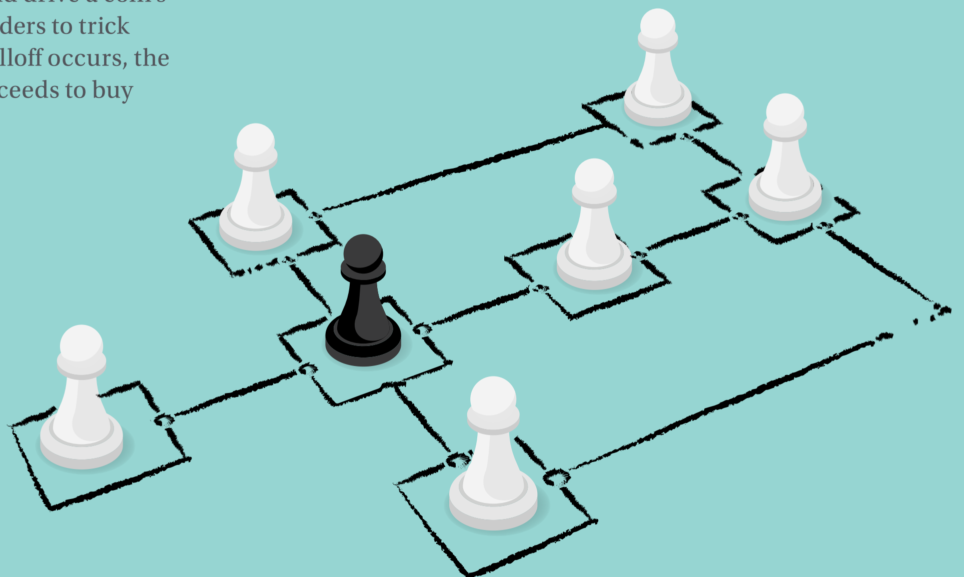
Spoofing was a common tactic used during Bitcoin's early days and still happens on lessregulated exchanges. This strategy involves a whale placing large orders to create fake buy or sell walls in the order books, hence the name spoofing. For example, if they wanted to create a bearish sentiment and drive a coin's price down, a whale will set large sell orders to trick investors into panic selling. Once the selloff occurs, the whale removes their sell orders and proceeds to buy more at a discounted price.

3. Wash Trading

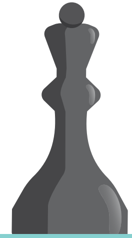
Wash trading is similar to whale wall spoofing because they both feed misleading information to the market. This strategy involves a person or group rapidly buying and selling the same cryptocurrency to inflate the volume artificially. The asset's increased activity gains attention from traders and investors, which distorts the price even more. Smaller, unregulated exchanges will typically perform wash trades to inflate trading volume, generate more commission and entice more users.

4. Stop Hunting

Stop hunting involves whales driving a cryptocurrency's price to a level where market participants have set stop-loss orders. Most people set their stop orders around the same key technical levels. The whale executes multiple sell orders to drive the price down and trigger the stops, which causes high volatility and an opportunity to rebuy the asset at a lower price.



8 https://www.binance.com/en/blog/fiat/what-is-market-manipulation-in-cryptocurrency-421499824684902912



Shariah considerations

It was narrated from Sayyiduna Abdullah ‘ibn Umar (Radiallahu anhu) that the Prophet (salallahu alayhi wasallam) forbade artificially inflating prices. (Sunan an-Nasa’i 4505)

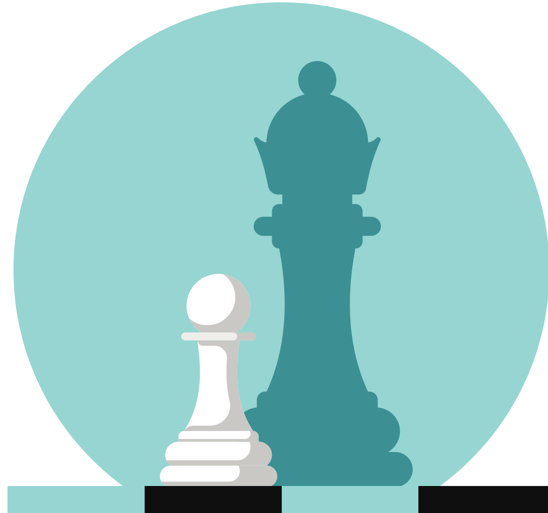
The Arabic word in the above narration is Najash, which refers to artificially inflating prices to deceive others into buying the item. Ibn Abd al-Barr, Ibn al-Arabi, Ibn Hazm understood the level at which artificial price inflation occurs is when it breaks the fair value of the item.[9]

Another example of market manipulation prohibited by the Prophet (salallahu alayhi wasallam) is insider trading and intercepting a delivery of goods designated for the market[10]. This was a commercial practice in early Arabia, where traders would, on hearing of a merchandise caravan, proceed out of the city to meet the caravan on the way for buying the entire merchandise. They would then sell in the city market at a higher price. This practice is only disliked and discouraged if it will economically harm the people in the city market. If this practice is not economically harmful but brings benefit, then such a practice is not disliked[11].

As such, these types of manipulative schemes and market abuse should be abstained from altogether. Those who initiate and promote these types of activities will be liable for the wrong.

9 Dhakirat al-Uqba

10 Sahih Muslim
11 Umdat al-Ri’ayah ‘ala Sharh al-Wiqayah



Conclusion

There are several types of crypto-assets in the markets offering different utilities. A Shariah investor must not only be concerned on the tokenomics and Shariah compliance of a token's use cases and project, they should also be prudent and trade in a Shariah compliant way. Before investing or trading in any token, an investor should review the token thoroughly or refer to a Shariah expert for assessment of crypto-assets. Only when it is deemed Shariah compliant should they proceed with an investment. Tokens are traded on exchanges, and exchanges offer different types of transactions, orders and facilities.

When it comes to orders, they are generally Shariah compliant as they are instructions to one's brokers on how and when to transact. However, many exchanges offer non-compliant trades, such as margin trading, swap farming, futures transactions, vanilla options, leveraged tokens, coin-m futures etc. These are non-compliant and must be abstained. Further, there are various investment styles, such as scalping, day trading, range trading etc. these are acceptable provided that Shariah principles are adhered to. Additionally, Shariah investors need to be aware of their investment strategy. Finally, Shariah prohibits market manipulation and artificially inflating prices. Any such endeavour in the crypto space should be avoided altogether.

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Disclaimer

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