Ways To Earn Passive Crypto Income

The ability to earn passive income is one of many attractive features of the cryptocurrency market. Investors can earn rewards on their cryptocurrency holdings in several ways, with varying degrees of risk and technical knowledge. Here are three ways crypto investors can earn passive income in 2022.

1. Staking

Staking is my favourite way to earn interest on crypto because it carries less risk than other options and is relatively easy to do. If your crypto exchange offers staking, you can activate this option at the click of a button. You might need to commit to stake your coins for a set amount of time.

If you can't stake coins with your crypto exchange, you might consider moving your assets to a wallet or platform that does offer this option. Staking can pay rewards of up to 15% APY or more, depending on various factors, such as the platform and the crypto. For example, I am earning around 10% APY on most of my stake-able assets.

Here's how staking works and why you can't stake every cryptocurrency:

* Proof of stake (POS): Some cryptocurrencies use a proof-of-stake system to keep the network secure. Proof of stake is a popular and more sustainable model than the one Bitcoin uses - and you need a POS crypto for staking.

Ways To Earn Passive Crypto Income

* Validating transactions: Validators earn rewards for checking that new transactions are legitimate. In the proof-of-stake model, validators need to own a certain amount of the currency to participate.

* Earning rewards: When you stake your coins, you're usually contributing to a validator node, and you earn a percentage of the rewards from that validator.

Staking Risks

There are risks involved in staking. If you choose to stake your assets from a centralized exchange rather than a crypto wallet, there might be an increased risk of hacking. Plus, some networks punish validators who break the rules, so in the unlikely situation that you choose an unscrupulous validator, this could impact you.

But unlike many aspects of decentralized finance (DeFi) and crypto interest earning, you can see exactly how your rewards are generated. That means you can be more confident there's nothing dodgy going on.

2. Crypto Savings Accounts and Crypto Lending

There are a number of crypto accounts that pay interest, and the rates are often much higher than what you'll find with a traditional savings account. Unfortunately, those higher rates come with correspondingly high risks.

A lot of platforms that offer interest-bearing crypto accounts do so by lending out your assets and giving you some of the interest that's paid on the loan. The level of risk depends on who the platform lends your money to and what collateral they require. A low-risk loan to a big financial institution presents a very different risk compared to an uncollateralized loan to someone that may not be able to pay it back.

Lend-earn accounts usually pay higher rates on stablecoins - cryptos that are pegged to traditional assets like the U.S. dollar - than ordinary cryptos. DeFi apps also offer other types of crypto lending. It's worth watching out for the fees on these apps. If you're using an Ethereum-based platform, you may find gas fees of more than $50 per transaction wipe out the extra interest you'll earn.

Risks of Lend-earn Products and Crypto Savings Accounts

Ways To Earn Passive Crypto Income

The biggest risk with many crypto lending products is that your savings aren't covered by FDIC insurance or other consumer protections. FDIC insurance means that your cash is covered for up to $250,000 in the event of bank failure.

The Securities and Exchange Commission (SEC) recently reached a $100 million settlement with BlockFi, a major crypto lender. The SEC said BlockFi's interest-earning product constituted a security and should have been registered as such. It also said that BlockFi had made misleading statements "concerning the level of risk in its loan portfolio and lending activity." We can expect to see similar actions against other crypto lenders in the near future.

3. Liquidity Pools and Yield Farming

Yield farming and adding liquidity to trading pairs on crypto exchanges are better suited to experienced investors. These are common options on decentralized exchanges, and essentially involve contributing your tokens to a trading pool. You'll usually need an external crypto wallet to participate, and it's important to pay attention to gas fees.

When you put a pair of tokens into a pool, it generates liquidity tokens that can be farmed to earn more rewards. Rewards are often paid in the platform's utility token. You might find rewards of over 100% APY on certain crypto projects, especially new ones. That rate may sound tempting, but there are a lot of risks.

Risks of Liquidity Pools and Yield Farming

When you start to read about liquidity, the first risk you'll learn about is impermanent loss. This stems from the way liquidity pools calculate the price of assets. It's possible to reach a situation where the value of the tokens in the liquidity pool is different from the tokens outside the pool. If this happens, you might lose money when you trade your tokens.

Another significant risk is scams. Yield farms that promise sky-high returns may well turn out to be scams. In the recent Squid Game (SQUID) rug pull, the project's developers drained over $3 million in funds from the liquidity pool, leaving investors with nothing.

Finally, be aware that DeFi tokens can devalue quickly. Let's say you earn a 100% APY that gets paid in the platform's utility token. If that platform is creating unlimited numbers of tokens to pay that high interest rate, the tokens you've earned may be losing value as fast as you earn them.

Generating passive income on your cryptocurrency assets can be a rewarding option. But as with many things in the cryptocurrency world, it is important to understand the risks before you jump in.