

# LISTEDRESERVE

**Fund:** The ListedReserve Managed Fund

**Date:** 30 June 2020

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Dear investor

Our unit price stands at \$1.35 up 30% in 2020, but down from what was its peak at a \$1.62 in June last year.

I'm delighted everyone is making money but the performance is far from what we are looking for. I think it is important that expectations are set correctly. We are not running this fund for 20% years and as you will see in the detail, there are good reasons to believe more compelling returns are in front of us.

## **Economic backdrop**

The economic backdrop we foresaw is really the whole premise of our fund and it is simple.

- Governments and consumers globally are deeply indebted;
- Populations are ageing and the liabilities associated with those cohorts are unfunded and growing;
- Debt will continue to grow as a percentage of GDP and governments will print money in response because they have no choice, pushing up the value of our fund.

I think we can say with confidence that this is playing out as per our expectations, which is great.

Even so, as I have explained many times before in the weekly updates, bitcoin (the dominant asset in our fund) does not really behave like other assets because it has features that other assets do not have, so it can be hard to predict.

For example, take TESLA. When their stock price surges they can (and do) simply issue more equity to take advantage of that surge, new supply can quell the price rise. That can never happen with bitcoin. When the price rises it causes supply to *fall* because miners and others are less inclined to sell in a rising market and we get very strong runs in price. The last time that happened was February 2019 when the price was US\$3,400, by 30 June that year it was over US\$10,000.

## **USA**

From an economic perspective, we could not be in a better position. I cannot see the United States ever balancing a budget again. Their deficits are now so huge that interest will become their number one line item by 2030, ahead of defence and social security. They have no option now but to print US dollars until nobody wants them anymore and that is exactly what they are doing. I expect aggressive monetary policy action up to the election in November and I cannot imagine that either Trump or a new President will miss the opportunity to announce very grand plans for 2021 and beyond.

US government debt stands at \$26.5 trillion. It will go through \$30 trillion in 2021, these are unimaginably large numbers. Bitcoin's market capitalisation is only \$170 billion. The American government is on course for an annual deficit this year of \$2.8 trillion dollars. Every 22 days they borrow bitcoin's market cap. I cannot emphasise enough how small that makes bitcoin and how large it makes the opportunity

The move out of the USD for investors has begun. Looking at gold it now has a market cap of \$9 trillion (up from \$7 trillion last year). Over 50 times the size of bitcoin. Both assets play a very similar role though in wealth protection. Bitcoin is superior in many ways, so much easier to assay, store and transfer. Gold on the other hand has 5,000 years of history behind it.

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## Europe

Europe is in an awful economic mess. Covid or not, their Euro project is a failure and it will cost billions of Euros before there is any sort of admission of that. The fact is that Germany is now so strong it calls the shots, the German Constitutional Court recently ruling that ECB's quantitative easing is unlawful and needs to be approved by the Bundesbank. It was quite the moment in the Euro power struggle about who is in fact in charge. Be in no doubt that it is Germany and the Euro will survive for exactly as long as the German public is willing to pay for it. Let's give it 10 years.

Before the end, a lot of money is going to leave the Euro. For the USD? I don't think so and Europe's recent history with storing wealth in gold is very ugly indeed. That is why the Swiss banks are telling clients to put some money in bitcoin.

## Investor behaviour

### *Advisors*

We know that private banks around the world are suggesting to their clients they take a position in bitcoin. Anywhere from 1%-5% of their portfolio. We aren't at the point yet where this is general advice to the population, but high net wealth individuals have over \$60 trillion to invest and there are about 14 million of them worldwide. There are only 21 million bitcoins, its 1.5 bitcoin for each HNW person. From this you can see just how scarce bitcoin is, even for such a select cohort. Keep in mind the *minimum* investment in our funds is the equivalent of 10 bitcoins. As these groups start to take an interest, price pressure will build.

### *The Grayscale Bitcoin Trust*

In the US the main vehicle for bitcoin ownership is the Grayscale Bitcoin Trust. Incredibly, clients pay a premium over the bitcoin price to buy into this fund (because it's not an ETF). The premium can be as high as 30%. Even so, they now have the equivalent of 400,000 bitcoin under management, 2% of all supply with one manager.

Demand has been particularly strong relative to supply this year and Grayscale are now consuming a large proportion (indeed in some weeks all) of the mined supply.

Suffice to say, on the demand side we are seeing what we want to see. The supply side of bitcoin speaks for itself. Only price can impact it, the higher the bitcoin price, the more supply in dollar terms.

### *Retail investors*

Bitcoin made its debut on the ASX this year too with the Raiz ETF including 5% bitcoin in its portfolio for clients. Raiz is a spare change round up tool. The great news about this is that regulators are now so comfortable with bitcoin that it is allowed on the ASX and as a retail offering, very encouraging.

While on the topic of retail investors it's interesting the number of people who say to me that "bitcoin isn't really doing much". If being up 30% in 2020, having the halving occur so that the inflation rate of bitcoin drops below gold and a hash rate rising to all time highs is not doing much, then long may that continue.

All told though, the general press on the sector has been far more positive this year than ever. Much of that is simply because so many other asset classes got riskier and this one relatively much less risky as a result.

## Outlook

I'd like to tell you that I'm really pleased with how things are going and I'm delighted to be 45% up in 2 years, but that would not be true. Our fund is early in a risky asset class. We have ridden out some tough times particularly in late 2018 when prices fell sharply.

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While I'm not happy, I am not disappointed either. Everything we predicted economically is happening, history is repeating itself. Bitcoin is getting stronger, supply is falling, demand is rising and that will ultimately reflect in price. The very reason we started our funds is playing out in real time

In what circumstances will the printing presses stop? If they did interest rates would rise sharply bankrupting most companies (and individuals) globally. There would be an immediate reversal as there was in 2018 from the Fed. Simply, governments and central banks are on the path of no return. Only inflation can erode the giant debt burden and as they print, we will gain.

As a team we appreciate your investment and I would encourage you to follow us on twitter @listedreserve where some of our more esoteric economic takes can be enjoyed.

As always, we will continue to provide industry and economic updates in the weekly newsletter.

It's happening.

Regards

A handwritten signature in black ink, appearing to read 'D. Pickering', with a long, sweeping underline.

Daniel Pickering

Chief Investment Officer

*In the appendix we cover some of the other assets in the Managed Fund as well comparative performance and some other metrics of interest*

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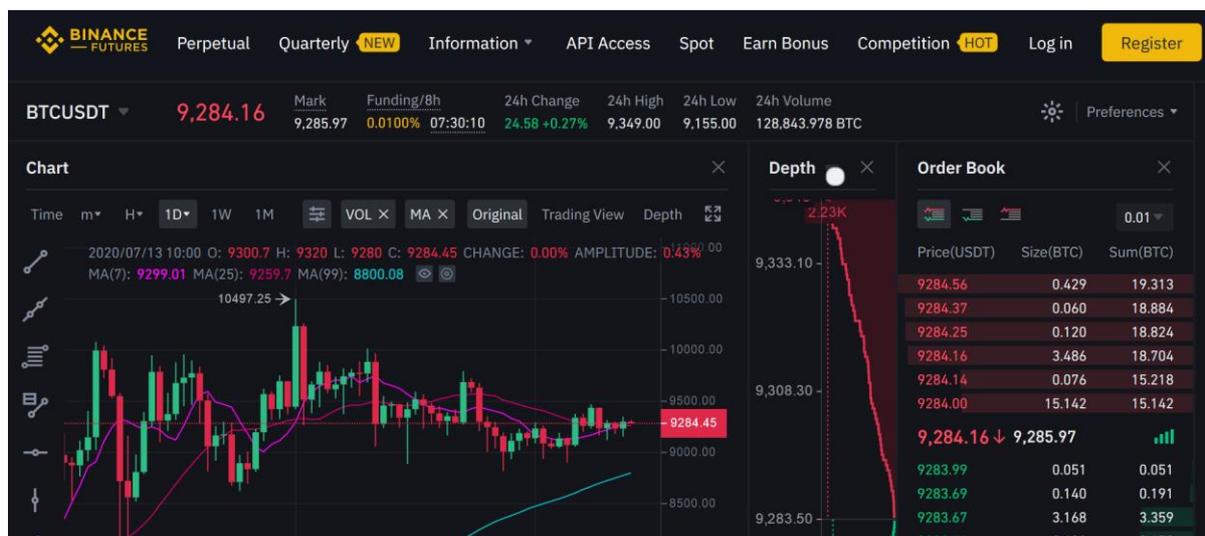
## APPENDIX

### Binance

Binance is a cryptocurrency exchange launched in 2017. Their original jurisdiction was Malta and they took activity from around the world. Then, in 2019, Binance closed down all business from American clients prior to the launch of Binance-US.

The approach has been, launch quickly, get big, legitimise quickly. That may sound rather dangerous but cryptocurrency is new and the laws in many countries are very unclear. Binance has done an excellent job of launching a business in the US in a very highly regulated market.

It's not just their management of regulation though, it is the suite of quality products they are able to release. In three years they have gone from bitcoin exchange to having a product suite rivalling any stock exchange. Below is a screenshot of their perpetual futures product, they have leveraged futures, options, high speed APIs it's really impressive. Their developers are the best out there if product experience is anything to go by.



Finally, clients of Binance were the targets of a hack in May 2019. While this did not compromise the exchange itself, it did expose weaknesses in the two factor authentication Binance was using. It was a \$40 million theft and was not really the fault of Binance. Impressively, they immediately made their clients whole for the full amount.

It speaks to the long term perspective of their CEO, he's looking after the brand and the business for the long term. We're long here and will remain so.

### Ethereum

Our position in Ethereum is now small, at only 4% of the fund. Ethereum still dominates as the basis of many tokens in the cryptocurrency eco-system. For example, the largest USD stable coin Tether, is primarily running on Ethereum. The issue with this is tether now has a market capitalisation of \$9 billion, Ethereum itself is worth \$23billion. The base layer cannot safely carry more value than it has itself because that becomes a security risk so successful projects will have to migrate away from Ethereum. We can see with Tether they also have Tron and Liquid versions for this very reason.

That said, Ethereum still dominates decentralised finance projects, it is favoured by developers because of its ease of use and for some reason, venture capitalists love it. So there is a good chance with the investment that goes into the ecosystem something good comes from it.

Ethereum 2.0 was due early this year, it's very late. It is a totally new blockchain, requires a complete migration from Ethereum 1.0. Version 2.0 uses something called sharding which is proposed as a solution to the scaling problem. Sharding itself is not new in computer science. It is used to manage large databases, however it is new in blockchains, which are not databases. Ethereum is at risk of becoming a very highly centralised database project so we are watching closely.

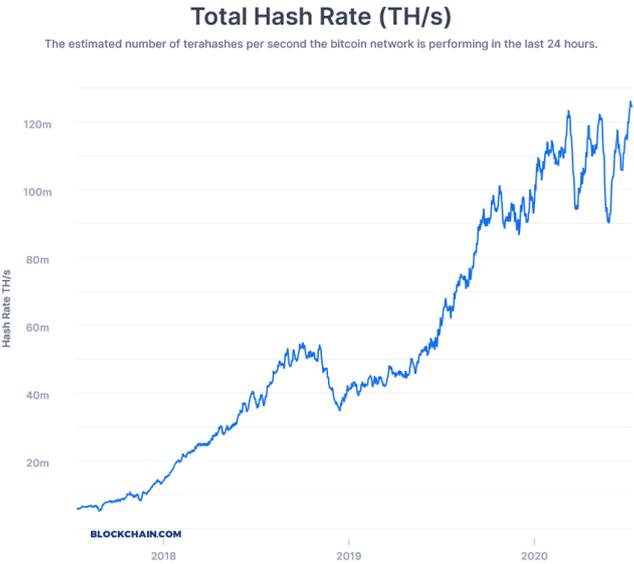
Further delays in Eth 2.0 (inevitable) and further growth in Tether (paradoxically) mean we will likely reduce further over the next 12 months.

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## Other metrics

### Bitcoin mining hash rate

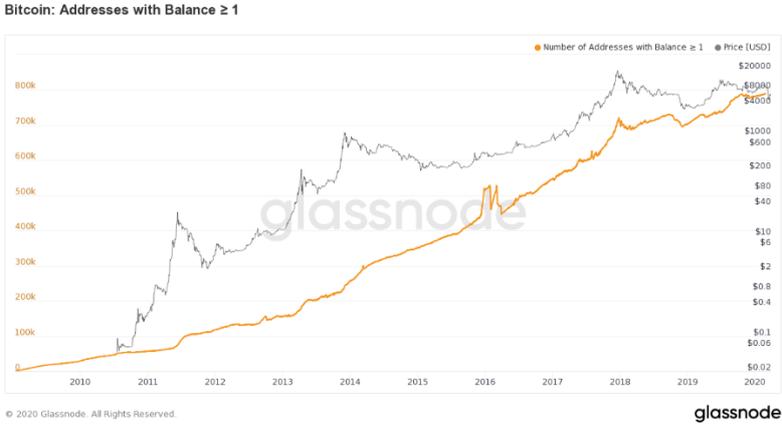
I take the bitcoin mining rate as the heartbeat of bitcoin. You can see it rising very strongly through 2019 and then the palpitations begin in 2020. That is the bitcoin halving, a very dramatic event for bitcoin miners. As you would know by now the reward for miners halves every 4 years and in May it dropped to 6.25 coins per block. Many miners turned off their operations as a result and we saw several weeks of steep decline in hash rate, before a recovery to all-time highs.



Miners are at the forefront of bitcoin, they choose which transactions are processed each 10 minutes, they risk millions in energy bills and capital payments. I think it is the highest risk/reward ratio activity in the ecosystem. That investors and venture capitalists (Peter Thiel among them) are willing to risk millions and millions in the pursuit of mining revenues speaks volumes. Hash rate, in our opinion, is much more important than price as a health indicator because it is less subject to the daily volatility than price, it is also a sign of longer term interest because the capital requirements are so high and they cannot be repurposed. Putting that another way, if I buy \$1billion of bitcoin, I can sell them tomorrow and move on. If I buy \$1billion of bitcoin mining equipment, I'm stuck with it for 2-3 years and I have to make it work. The large investment in mining is really a sign that people are here for the long haul.

### Bitcoin distribution

This chart from glassnode research shows 800,000 addresses now have more than 1 bitcoin. This tells us two things, firstly distribution is still quite narrow and secondly it is rising all the time. The higher this figure goes the better. Bitcoin is still quite concentrated in terms of ownership, rising price will solve this over time but this is a metric we need to see continuing to rise.



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