

Investment Insights:

Bitcoin Group SE



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Bitcoin Group: Crypto Exposure Through Equity And A Growing Exchange Business For Almost Free

As Modern Portfolio Theory would have it, a strong case exists for the inclusion of cryptocurrencies within investor portfolios to improve their risk-reward profiles. However, for the individual, investing in crypto is inherently challenging and cumbersome, due to administrative burdens and security risks associated with crypto accounts. Bitcoin Group provides an opportunity to gain indirect exposure to crypto through equity, bypassing these issues. This little-known, German-based company has amassed a vast portfolio of crypto assets from commissions through bitcoin.de, their exchange business. The fair value of these assets almost equates the market valuation, which appears to value the growing and increasingly profitable bitcoin.de platform at near-zero. Having surpassed one million users ahead of schedule, Bitcoin Group now plans to accelerate its other growth initiatives. In this article we explore how the exchange could turn into a reputable destination for both retail and institutional customers in the future.

About Bitcoin Group

Bitcoin Group SE operates bitcoin.de (through its subsidiary futurum bank AG), which is Germany's only regulated exchange for the commonly traded cryptocurrencies like Bitcoin and Ethereum. It is one of the most secure crypto exchanges in the world and operates a P2P trading system where customers keep their fiat currency rather than it being held unsecured on an external bank account. This eliminates the risk of total loss in the event of the exchange becoming insolvent. The exchange is also the first and only of its kind to have its customer credit

balances audited once a year by a publicly appointed audit company.

The platform has grown its user base to over a million users, contributing to revenue growth of 185% over the year since H1 2020. Impressively, EBITDA growth has shown an even larger increase of 243% over the same period, suggesting there has been operational improvements in running bitcoin.de. The group earns commission by taking a portion of the cryptocurrency during each transaction. Given the rallying of cryptocurrency prices throughout 2020 and into 2021, Bitcoin Group has substantially grown the value of its assets. Remarkably, in September, the market capitalisation of Bitcoin Group was smaller than the value of these crypto assets and is now valued at a similar level. This is despite the exchange business driving net profit of €10.2m in H1 2021 exceeding the entire 2020 fiscal year (€9.5m). The market therefore appears to be ignoring a growing and increasingly profitable exchange business

Long-term strategic goals

In the long-term, Bitcoin Group's mission is to become the first independent German crypto bank and has seen success in efforts to streamline regulatory and operational requirements across the companies it owns. The strategic focus is to offer a custody and trading solution licensed under one umbrella, in order to be free from third parties and promote efficiencies across the business. No one currently operates this model within Germany. If the enthusiasm and adoption of cryptocurrencies continues into the future, this could prove to be a lucrative venture for Bitcoin Group as they would own a one-stop-shop model within the ecosystem, as well as in one of the most affluent countries. With this unique infrastructure, management believes the group can command a market share of 10-20% in Germany over the next 2-

3 years. Moreover, the German parliament cleared new legislation whereby 'Spezialfonds' can now invest 20% of their portfolio into digital currencies. These institutional investment funds represent a €2tn tsunami of assets which could act to further legitimise cryptocurrency as an asset class; the maximum allocation would bring €400bn. Such an allocation is perhaps unrealistic given risk-averse insurance companies and pension funds dominate the investor base of Spezialfonds. A more likely scenario would be a single digit % allocation in investor portfolios in the future; a 1% allocation would amount to around €2bn flowing into cryptocurrency in Germany. This would benefit Bitcoin Group twofold by increasing the value of their cryptocurrency holdings and encouraging more customers to trade through its platform. An influx of institutional capital could therefore spell a new wave of growth for Bitcoin Group.

Given the turmoil in financial markets triggered by the pandemic and the multi-billion support programs in the context of historically low interest rates, the demand for cryptocurrencies has increased significantly among both private and institutional investors. It is becoming an increasingly popular inflation hedge trade and an alternative to gold as a safe haven asset. There are also clear diversification benefits given low correlation to other asset classes. The success of Bitcoin Group is ultimately tied to the persistence of this trend and the road ahead will certainly be a bumpy one given the volatility in cryptocurrency prices. It will be crucial to monitor ongoing changes to regulation in Germany and across Europe as blockchain technology is a novel issue; applying 20th century regulation to 21st century innovation is unlikely to work. Furthermore, bitcoin.de will have to evolve to compete with European and overseas

exchanges by expanding its product offering and improving the platform interface.

Conclusions

Ultimately, the market is yet to de-link the two parts of the business: crypto owner and crypto exchange owner. Bitcoin Group's portfolio of crypto assets recently exceeded its market valuation, which would be reasonable if their exchange business was value destructive. However, on the contrary, higher trading commission has lifted revenues by 185% over the last year and importantly, EBITDA has more than tripled. Bitcoin Group appears to be successfully delivering its growth strategy as the number of users on its exchange reached one million ahead of schedule. New offerings like the popular 'Dogecoin' have been added, and management is confident that the range of cryptocurrencies can expand in the future which should garner further interest. Their push to become both a licensed custodian and trading platform offering a unique solution could turn them into a reputable destination for both retail and institutional customers in the future. The current market valuation and size of their own crypto portfolio represents an opportunity to own this promising exchange business and pay almost nothing for it.

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