August 2022 Investor Update

ProChain in the News

Bitcoin Drops to Three-Week Low; ***Bloomberg TV***; Aug 19

Market expert predicts stocks will rally through September; **Fox Business**; Sept 1

Where There is Smoke There is Fire - Crypto Rising; ***OETV***; Sept 1

1. Adoption

a. Investment.

- According to a recently-released report, approximately one-third of traditional hedge funds have some exposure to digital assets
    - Remarkably, that percentage has almost doubled year-over-year
    - More importantly and encouraging for a forthcoming rise in crypto prices, most of the funds surveyed have modest exposure to digital assets, with 57% reporting less than 1% of total AUM, and 67% intend to increase their exposure by the end of this year.
- As ProChain has highlighted in the past, some of the greatest positive effects of crypto are being seen in financially distressed economies, such as, Argentina, where adoption continues to rise despite the pullback in price of cryptocurrencies, because cryptocurrency is a superior alternative to the traditional fiat currency.
- In respect of the upcoming **Ethereum Merge**, this is the best webinar that we have listened to, and here is the related slide deck.
- **FTX** Ventures, the venture-arm of **Sam Bankman-Fried**'s FTX, the second-largest crypto exchange, has purchased 30% of **Anthony Scaramucci**'s **SkyBridge Capital**.
- As with all markets that count paper-gains toward total value, no one should take crypto's $3 trillion total value too seriously.

b. Currency and Use.

- **USDC** (the 2nd largest stablecoin in circulation)
    - **Rune Christensen**, the founder of **MakerDAO**, the company behind stablecoin **DAI**, has always been leery of any form of centralization, and now he's concerned about his company's $1.6B in USDC.
        - The **US Treasury**'s recent sweeping action against **Tornado Cash** is *Christensen's scariest nightmare come true*. As detailed in ProChain's July investor update, DOT, sanctioned Tornado Cash, blacklisting the protocol and its smart contracts under the guise of a "national security risk." As a result of the sanctions, many US citizens/entities have been caught in the snarl, unable to transact in their

            own crypto due to the broad banning of any addresses associated with Tornado Cash.
        - As a further result, and out of fear of failure to comply with the DOT, **Circle**, the entity behind the **USDC** stablecoin, immediately blacklisted 38 Ethereum addresses, and a host of apps have frozen user funds with even a marginal connection to Tornado Cash.
        - Currently, MakerDAO holds $1.6B of USDC in reserve to back its own DAI stablecoin. More than one-third of DAI is backed by USDC.
        - These circumstances have left Chrestensen considering options to distance and insulate MakerDAO and DAI from being collaterally damaged in a future case.
        - **Coinbase** (**COIN**) is proposing to hold MakerDAO's $1.6B USDC in exchange for 1.5% annually ($24mm).
            - Although this does provide some additional cash-flow for DAI, it doesn't seem to alleviate the concerns around centralization and wanton regulatory action.
            - Incidentally, Coinbase is backing a lawsuit against the US Treasury's actions in connection with Tornado Cash.
    - **Binance**, the world's largest crypto exchange, will no longer allow its customers to trade USDC.
        - Binance will automatically convert customers' dollar-pegged stablecoins, including USDC, into **Binance USD** (**BUSD**), effectively delisting competing coins on the exchange.
        - As of now, the plan will not include **USDT** (**Tether**), the largest stablecoin, but Binance said it "may amend the list of stablecoins eligible for auto-conversion."
        - This seems to be the first shot in the upcoming USDT/USDC/BUSD race to become the leading stablecoin over the next years. Tether and Circle will undoubtedly react

2. **Regulation and Legal**
- If the **SEC**'s continued failure to propose crypto-specific regulations wasn't bad enough, the SEC has sustained the confusion of legislators, other regulators, and the investing public with somewhat-random legal actions against crypto-exchanges and cryptocurrency issuers and **SEC Chair Gary Gensler**'s endless unclear rhetoric and soundbites.
    - The venerable **Matt Levine** (*Bloomberg*) has written "The SEC has been suing crypto projects for illegally issuing securities for about five years now, but in that time it has not issued any rules, or proposed any rules, or put anything on its rulemaking agenda, about adapting the securities disclosure rules to crypto projects. And Gensler sees no problem with that; he feels that existing securities' regulation is clear, sufficient, and comprehensive." For most, it is anything but.
        - Levine continues, "if you are an ambitious financial regulator who wants to regulate crypto, you have to regulate crypto! You have to put in the work! You have to sit down to try to understand how the crypto market operates, what investors need to know, and what is required to encourage useful capital formation. You have to write rules that anyone can read and that create some plausible path for how crypto developers can register their tokens and how exchanges can trade them. And then you have to focus your enforcement efforts on actual consumer protection, going after the crooks instead of just the people who are naive enough to walk into your office. If you don't do that, then,

what? Then the US will not be a leader in crypto innovation, is the traditional answer, and US investors will not have access to all the great crypto projects."

- Although some members of Congress have released comprehensive draft legislation relating to crypto, the realistic expectations for this Congressional term were limited to bipartisan rules for **stablecoins**, arguably the simplest and the most needed area for rules. Now, it is increasingly likely that Congress will not achieve legislation on stablecoins prior the November midterm elections.
  - **Fed Chair Powell** isn't happy about the delay. He believes that stablecoin legislation is needed ASAP.
- As anticipated, the **While House** released a report on the climate and energy implications of crypto-assets in the US.
  - The report concludes that energy usage by Proof-of-Work protocol ("PoW"; Bitcoin mining) is threatening US climate goals. And, depending on the power usage, the White House or Congress may have to eventually regulate the industry's power usage.
- The **US Treasury** will recommend a **CBDC** (Central Bank Digital Currency) if it is in the "national interest". This is a leak from an upcoming report from the US Treasury.
  - ProChain believes that we are at least years away from a CBDC in the US. It is more likely that we will never have a CBDC in the US out of concerns for privacy and vitally sensitive information contained in a person's CBDC holdings and spending.
- The most dramatic episode in crypto-land in recent weeks was the report and accompanying videos supporting the claim that Layer-1 coin, **Ava Labs** (**Avalanche**; **AVAX**), had weaponized its law-firm to sue its rivals and draw regulators' attention to the rivals. Also, in the course of the suits, the law firm was able to uncover confidential information on other Layer-1 protocols and share it with Ava Labs, allowing it to best its rivals.
- The **FBI** published an alert regarding cyber criminality and DeFi.
- **a16z** (**Andreessen Horowitz**) has published proposed licensing guidelines for **NFTs**. Listen to this podcast for a16z's General Counsel thorough explanation.
  - It is encouraging to witness well-respected industry participants proposing industry standards and self-policing initiatives, which are in the best interests of the industry.

3. Public Companies

- **David Rubenstein**, co-founder of the **Carlyle Group** (**CG**), one of the largest private-equity firms, who was a previous skeptic of cryptocurrency, has acknowledged that he has invested personally in a few crypto companies. And he anticipates that the industry successfully deal with Congress.
- **Michael Saylor**, the previous CEO and now Chairman of **MicroStrategy** (**MSTR**), is being sued by the District of Columbia for evasion of $25mm of taxes. The basis of the claim is that Saylor fraudulently claimed to be a resident of other lower-tax jurisdictions.

David D. Tawil
President
+1-646-479-9387

david@prochaincap.com

ProChain
CAPITAL