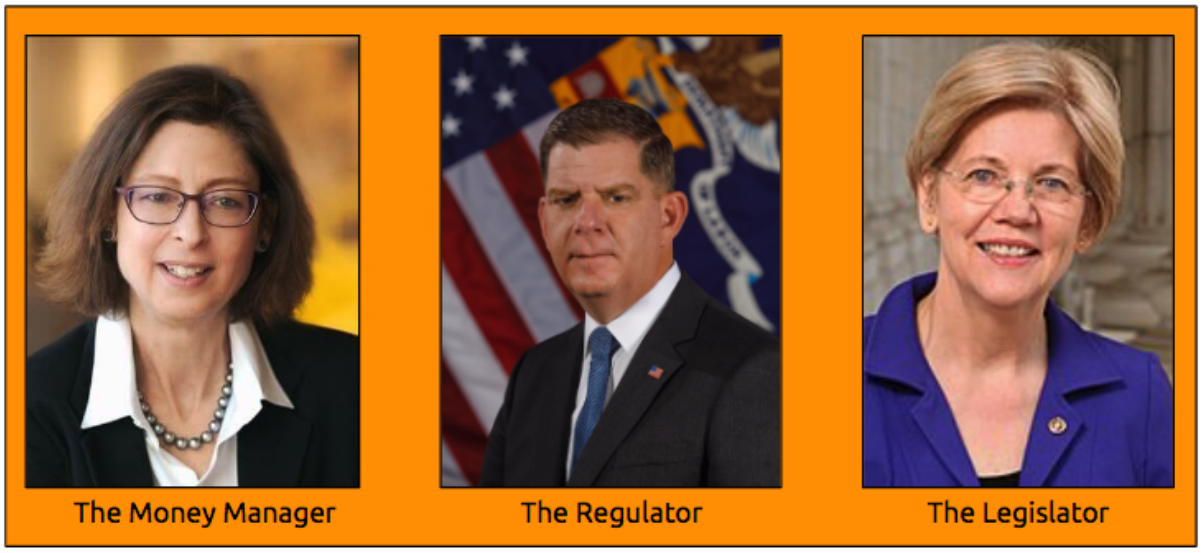
Blockchain Assets
CRYPTOASSET MANAGERS • EST 2017



Dear Investors,

With estimated wealth of USD 25b Abigail Johnson (The Money Manager) is the 6th wealthiest woman in the US. The fund management firm she Chairs - which was founded by her Grandfather - is Fidelity Investments. Fidelity manages USD 3.6 Trillion of client assets. More than 32 million Americans are clients of Fidelity. Ms Johnson has publicly declared that '...We Love Bitcoin…' and her firm provides an on-ramp to Bitcoin and Ether via its 401(k) investment plan menu and its retail investor platform.

US Democrat Senator Elizabeth Warren (The Legislator) has spent much of her political career focusing on consumer protection, equitable economic opportunity, and the social safety net. Senator Warren is strongly against Fidelity's approach to Bitcoin and crypto as a retirement savings asset.

We will get to The Regulator later!

In this newsletter I examine some of the letters, regulatory guidance and court proceedings involving these powerful leaders. It offers us great insight into the regulatory tensions that are emerging in the United States of America.

But first - The Cryptomarkets Summary

This past quarter has been one of the most painful we have endured since the Fund's inception. Although our Fund was not invested in FTX the impact to the overall market has been severe. Our unit price was down 25% for the quarter and down 69% for the 12 months ended 31 December 2022.

The recent deleveraging we have seen is an excellent reminder to us of the importance of 'playing safely in a highly risky environment'. Our conservative approach has kept us away from yield opportunities we did not fully understand and prevented us from allocating to projects where the level of transparency was not sufficient.

The question on everyone's mind is when will market sentiment improve, when can we see the return of crypto summer? My prediction of the last bull run was accurate. In November 2020 I wrote '*...Short term price predictions are a fools game. But I get a sense that FOMO (of the institutional variety) will kick in when Bitcoin is over USD 25,000 (currently USD 18,000) and Ethereum is over USD 800 (currently USD 580) and I would not be surprised to see this happen within the next 6-8 months…*'. One year later Bitcoin reached it's all time high of over USD 64k and Ether of over USD 4.6k in December 2020.

We are still in the foothills of 'Mt Adoption'. The false peaks we have seen thus far are well below the summit levels we and many others are expecting. As mentioned in earlier newsletters, there are credible reports and analytics that support valuations of USD 1mio and USD10k for Bitcoin and Ether respectively. The trough we are in at the moment is deep and painful but it is temporary and we will be through it sooner than we think, but probably not as soon as we hope.

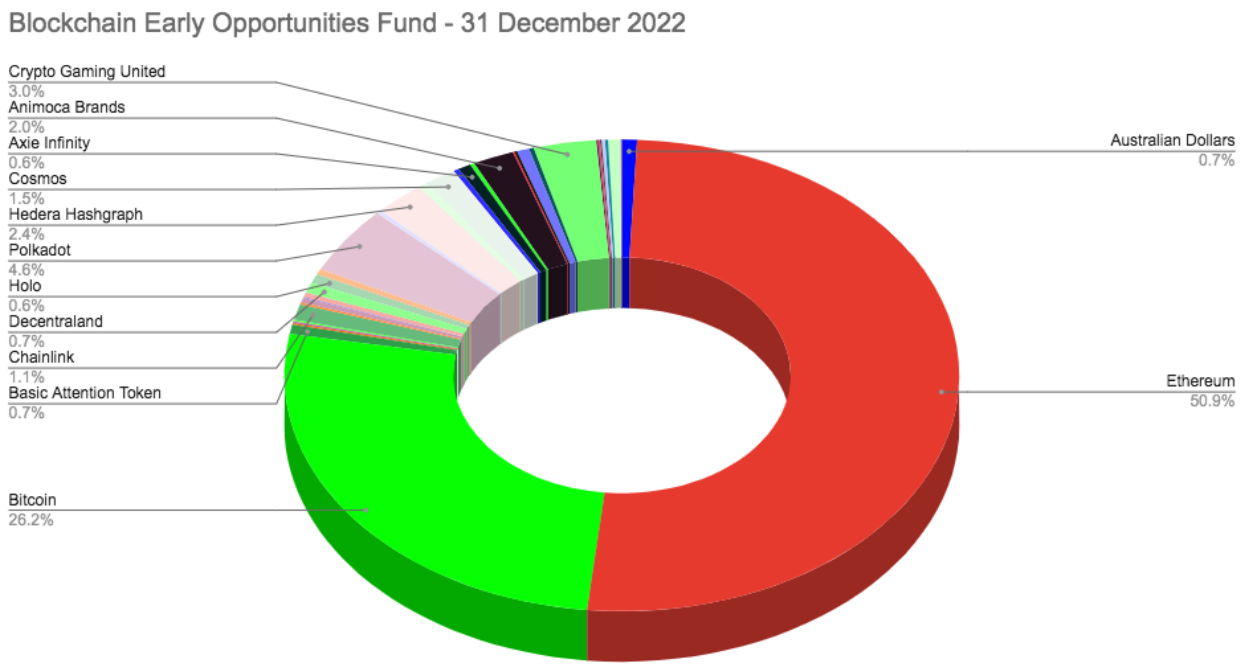
There is nothing in the FTX, Terra Luna or other collapses that gives me pause for thought relative to the path we are on with our portfolio. These failures were inevitable and it's good that they have been cleaned out. As Caitlin Long (one of the people I listen to and have an enormous amount of respect for (see here)) says '...good riddance to the grifters…'.

Bitcoin and Ether as technologies are completely unaffected by the type of corporate malfeasance, frauds and incompetence that has caused these failures.

[End of this Section]

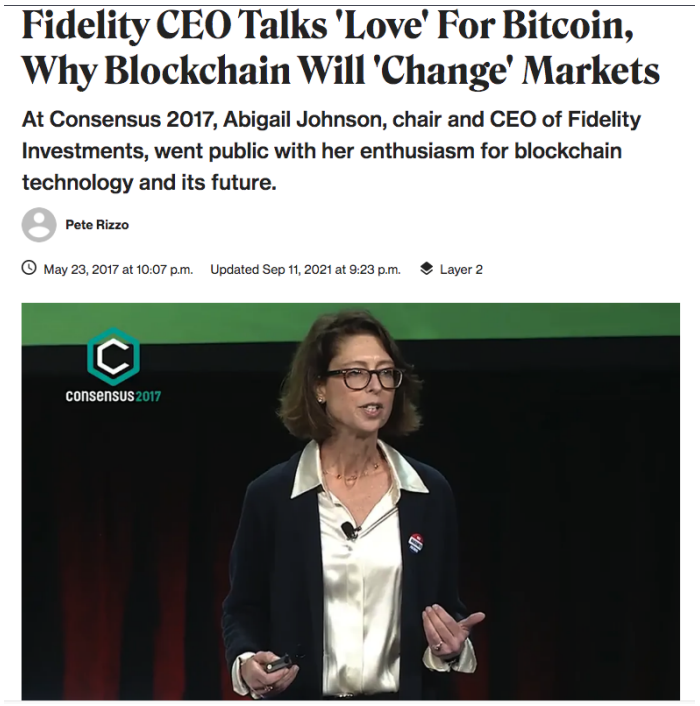
Fund Assets and Key Metrics

Metric	30 September 2017	31 December 2017	31 March 2018	30 June 2018
Unit Price	$0.93	$2.14	$1.18	$1.09
Return Since Inception	-7.00%	114.00%	18.00%	9.00%
Metric	**30 September 2018**	**31 December 2018**	**31 March 2019**	**30 June 2019**
Unit Price	$0.7480	$0.5178	$0.5507	$0.9501
Return Since Inception	-25.20%	-48.22%	-44.93%	-4.99%
Metric	**30 September 2019**	**31 December 2019**	**31 March 2020**	**30 June 2020**
Unit Price	$0.5270	$0.3937	$0.4408	$0.6034
Return Since Inception	-47.30%	-60.63%	-55.92%	-39.66%
Metric	**30 September 2020**	**31 December 2020**	**31 March 2021**	**30 June 2021**
Unit Price	$0.9449	$1.6575	$4.5682	$3.4543
Return Since Inception	-5.51%	65.75%	356.82%	245.43%
Metric	**30 September 2021**	**31 December 2021**	**31 March 2022**	**30 June 2022**
Unit Price	$4.9905	$5.7599	$5.3393	$2.1182
Return Since Inception	399.05%	475.99%	433.93%	111.82%
Metric	**30 September 2022**	**31 December 2022**	**31 March 2023**	**30 June 2023**
Unit Price	$2.3768	$1.7762		
Return for the Quarter	12.21%	-25.27%		
Return for the past 12 months	-52.37%	-69.16%		
Return Since Inception	137.68%	77.62%		
Assets Under Management	$17,184,558.72	$12,741,156.24		



Fidelity's 'We Love Bitcoin' moment

I first became aware of Fidelity's interest in Bitcoin in May 2017 at the Consensus conference in New York when Abigail shouted from the rooftop that…'We Love Bitcoin'. The 5000+ people wedged into the massive Grand Ballroom at the Marriott Times Square went bananas. This was a really unexpected and a positive thing to come from the highly regulated, ultra conservative, blue blooded traditional side of town.



Fidelity CEO Talks 'Love' For Bitcoin, Why Blockchain Will 'Change' Markets

At Consensus 2017, Abigail Johnson, chair and CEO of Fidelity Investments, went public with her enthusiasm for blockchain technology and its future.

Pete Rizzo

May 23, 2017 at 10:07 p.m. Updated Sep 11, 2021 at 9:23 p.m. Layer 2

Actually Fidelity had been researching Bitcoin since 2014 and had been steadily developing a client service model from the start. In 2018 Fidelity Digital Assets was launched. In July 2020 they released their Bitcoin investment thesis which values Bitcoin at USD 1m per coin. Then on 26 April 2022 they announced the rollout of their 401(k) investment plan service which (now) enables clients to invest directly in Ether and Bitcoin via the Fidelity platform.

There is no regulatory roadmap to follow when setting up a cryptoasset management business. There are no roadmaps for pioneers and this is what Fidelity has always been, they have not become one of the worlds largest fund managers through complacency. But this crypto exploration thing is the next level in terms of implications for existing road networks. Of course Fidelity would have been consulting with regulatory agencies from the start. Their aim has been to obtain a green light to offer Bitcoin and Ether Custody and Trading to their clients. But then with no green light coming, but also no red light, they forged ahead with their product in a compliant and cautious manner.

US Department of Labor

Because the services being offered touch on the retirement savings of millions of Americans, one of the key regulators is the US Department of Labor (DoL) and it

was the DoL that fired the first shot across the bow of Fidelity even prior to the launch of their product.

On 10 March 2022 the DoL released 'Compliance Assistant Release No, 2022-01 401(k) Plan Investments in 'Cryptocurrencies''. (CAR) This document is brutal. While it stops short of an outright prohibition on holding cryptos in 401(k) plans, it gives notice to service providers that doing so will invite challenge. Specifically the CAR advises that holding crypto may be a breach of fiduciaries duty to act solely in the financial interests of plan participants and adhere to an exacting standard of professional care.

Fidelity was not intimidated by the CAR at all. They responded on 12 April 2022 setting out significant concerns they have with a number of aspects of the CAR (see here), they then proceeded with the launch of their product 14 days later on 26 April. Fidelity is not the only party with significant concerns about the CAR. On 2 June 2022 US company Forusall Inc. filed a suit against the DoL and Martin Walsh (the Secretary of the DoL - The Regulator) seeking to set aside the CAR under the Administrative Procedure Act. The case is continuing.

United States Senate

This is where Senator Elizabeth Warren enters our story but before I get into that, let's consider first the general political environment around Bitcoin and crypto in Washington DC.

Even before the FTX blow-up Washington's approach to Bitcoin and crypto was difficult to gauge. We definitely know some powerful people who support Bitcoin (Texas Republicans for example). See also here an excellent interview with Senator Pat Toomey (Republican - Pennsylvania) recorded shortly after the blow-up of FTX.

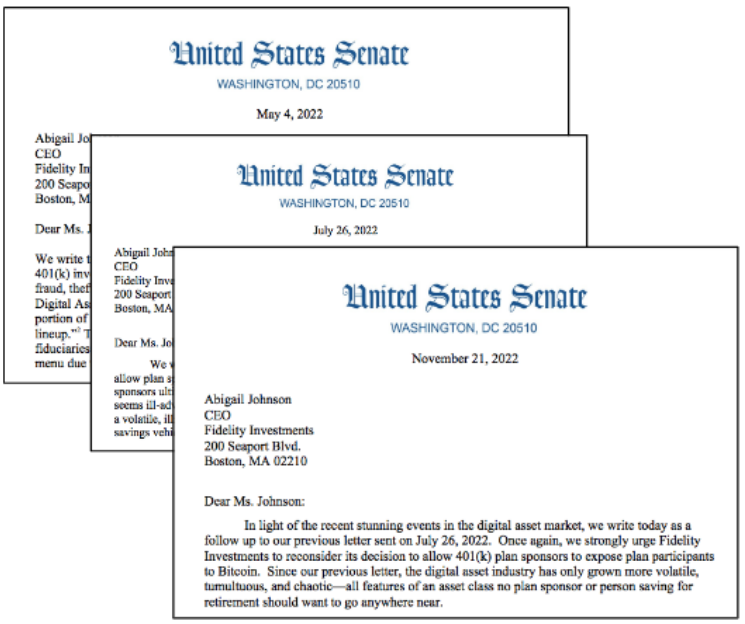
There are also some Senators who are furiously against it, a small group of Democrat Senators have formed the so-called 'bullshit caucus' who, as the name suggests, feel that all cryptocurrency is bullshit (see here).

Senator Toomey is of the view that it is not a bi-partisan issue and that most people in congress on both sides of the houses have still not really fully engaged with the topic and that much more education is needed.

We know that Banks and TradFi lobby congressional people and that there are now many lobby groups for the crypto industry. Thankfully we have an excellent research and advocacy centre (see here) in Washington DC whose mission is '...to defend the rights of individuals to build and use free and open cryptocurrency networks…'. I tend to follow their work to keep myself up-dated on US regulatory developments.

Back to Senator Warren. On 4 May 2022, 8 days after Fidelity launched their crypto product, Senators Warren and Smith wrote to Abigail Johnson seeking answers to a number of questions. In short they consider '...investing in cryptocurrencies is a risky and speculative gamble, and we are concerned that Fidelity would take these risks with millions of Americans' retirement savings…'. (see the letter here). If Ms Johnson replied, it has not been made public.

On 26 July 2022, after the District Court action started (mentioned above), a follow-up letter was sent to Ms Johnson. This one bluntly asks '...why Fidelity, a trusted name in the retirement industry, would allow plan sponsors the ability to offer plan participants exposure to Bitcoin'. (see letter here). If Ms Johnson replied, it has not been made public.


United States Senate
WASHINGTON, DC 20510
May 4, 2022

United States Senate
WASHINGTON, DC 20510
July 26, 2022

United States Senate
WASHINGTON, DC 20510
November 21, 2022

Abigail Johnson
CEO
Fidelity Investments
200 Seaport Blvd.
Boston, MA 02210

Dear Ms. Johnson:

In light of the recent stunning events in the digital asset market, we write today as a follow up to our previous letter sent on July 26, 2022. Once again, we strongly urge Fidelity Investments to reconsider its decision to allow 401(k) plan sponsors to expose plan participants to Bitcoin. Since our previous letter, the digital asset industry has only grown more volatile, tumultuous, and chaotic—all features of an asset class no plan sponsor or person saving for retirement should want to go anywhere near.

Then, just as we were thinking that 2022 could not get any worse, the FTX fraud was exposed. Ten days later on 21 November 2022 Senators Warren, Durbin and Smith wrote to Ms Johnson once again '...we strongly urge Fidelity Investments to reconsider its decision to allow 401(k) plan sponsors to expose plan participants to Bitcoin.'. (see letter here). If Ms Johnson replied, it has not been made public.

My take on these letters? They are toothless. They are policy positioning statements to her constituents and

political donors. This current issue (DoL overeach and Fidelity's approach to Bitcoin and Ether) will either die from lack of interest or it will be played out in the courts under existing laws. It remains to be seen how the balance of powers in congress will view crypto legislation/regulation in the medium term. The Biden administration's approach as set out in the 16 September 2022 Executive Order (see here) lacks detail (see Brookings Institute opinion here). In the short to medium term I expect the level of outrage from Senator Warren and others of similar views to increase. However, in the Land of the Free, it is more likely than not that this technology will move from a sideshow to the mainshow in a shorter space of time than we can imagine.

Massachusetts Mutual Life Insurance Co. and NYDIG

While Senator Warren has Fidelity in her line of sight there are other 'blue blood' financial institutions that are adopting Bitcoin. In December 2020 Massachusetts Mutual announced a USD 100m purchase of Bitcoin and an investment in New York Digital Investment Group LLC (NYDIG) , an institutional grade Bitcoin only service provider. News of this has been quiet since but it is still significant. Massmutual is a 171 year old ultra conservative insurance company, they can see that Bitcoin can play an important part in a long term investment portfolio. They have only dipped their toes in the water at this stage and only time will tell if their interest holds, but as recently as August 2021 they advised that 'As MassMutual explores ways to integrate cryptocurrency into different areas of its business, MMLIS saw a growing demand from our financial professionals and their clients to gain bitcoin exposure," said Daken Vanderburg, Head of Investments at MML Investors Services.'.

The New York Digital Investment Group (NYDIG) is part of the Stone Ridge Asset Management business based in New York. NYDIG is an institutional grade Bitcoin only service provider. NYDIG is partnering with banks and credit unions across the US with the view to making Bitcoin directly accessible to their millions of customers.

If Senator Warren has sent a letter to Massmutual or NYDIG it has not been released in public.

Texas, Florida and Wyoming

The US is far less federated than Australia. State rights and independence override Federal law in many more aspects than we have in Australia. This creates intrastate competition which is healthy as it creates a stronger whole.

There are many States across the US vying for the mantle of '...the silicon valley of crypto…' Three such States are Texas, Florida and Wyoming.

> "If America wants to remain the global financial leader, we need to foster innovation. Strike's announcement is a valuable contribution toward bringing America's financial system into the 21st century. I am working to bring smart legislation to the digital asset space, so that innovations like this can be integrated into America's financial services industry. By doing so, we can protect consumers and empower individuals and small businesses by encouraging responsible innovation."
>
> – U.S. Senator Cynthia Lummis

Of course Ted Cruise is a Bitcoin supporter. But so too is the Governor of Texas (see here) and more importantly the head of the Texas electricity grid Brad Jones (see youtube explainer clip here and here).

Miami Mayor Francis Suarez is positioning his city as Bitcoin central. Miami plays host to the largest Bitcoin only conference in the world Bitcoin Miami. In this video Stripe CEO Jack Mallers sets out the case for Bitcoin as a monetary network and how his company is bringing Bitcoin to the world via the lightning network.

In Wyoming Senator Cynthia Lummis is a fan of Stripe but also of Crypto Bank (Custodia Bank) Founder Caitlin Long. Caitlin's interview here about the collapse of FTX sets out her explanation of the importance of on-shore regulations that accommodate Bitcoin. This is fully supported by Senator Lummis, see her interview here. Her comments on the Fidelity position are particularly interesting.

Where to Next for Regulation

Right now we have three bad things happening with regulation all of which leaves the wider public very exposed to unacceptable levels of financial risk.

1. We have the public going offshore using bad operators and getting hurt (FTX International).
2. We have regulators not supporting existing financial institutions with their cryptoasset offering (Fidelity and the DoL).
3. We have regulators walking at 'snail's pace' to 'help' crypto native businesses navigate the regulatory environment (Custodia Bank).

The demand for cryptoassets is not going away. If people cannot get access to them onshore they will go offshore. This we know.

The approach taken by Senator Warren would, if adopted, lead to even more people going offshore and an increased risk exposure for retail investors.

The slow walking regulator approach is harmful to emerging crypto native businesses. In June this year Custodia Bank filed a suit against the US Federal Reserve in the District Court of Wyoming (see here) for slow walking their application for a Master Account with the Fed (which would give them access to the Deposit Guarantee system).

The only approach I can see working is increased regulation on-shore but regulation that allows both existing market participants (Fidelity) and emerging businesses (Custodia) to compete on an equal footing.

Consider. If all the investors who held their crypto on the FTX International exchange had instead held their crypto via Fidelity they would have lost none of their assets. So why is Senator Warren making Fidelity the enemy? I would have thought she would instead be thinking - thank goodness we already have regulated retail platforms for buying, selling and holding (some) crypto assets, at least in the US.

Everyone is concerned about consumer protection, I feel sure Abigail and Elizabeth have that in common. So too they would agree on providing equal financial opportunity.

I feel that legislators like Senator Warren are on the wrong track because their focus appears to be on the assets themselves, not on the venues where they are traded and the operators of those venues. If the focus is on the venue it would have been very clear that FTX International is not a good venue for retail or indeed any investor to use. So what then drove US investors away from the US operations of FTX? Well FTX Bahamas could offer more products and services that were not able to be offered in the US. This is the issue. Because the US leg could not offer regulated products and service clients went offshore into the abyss…the lack of regulation in the US was one of the contributing factors to the harm done to US citizens.

I do not think it is helpful, if we want to protect investors, to ask existing on-shore fully regulated service providers to stop offering such services. Instead regulations should encourage a broadening of products and services. The days of 'protection by exclusion' are gone, it is no longer acceptable for legislators to decide

what citizens can or cannot invest in for their retirement or otherwise. Fidelity, Massmutual, NYDIG, Microstrategy, Yale Endowment Fund, Paul Tudor Jones, Stan Drukenmiller, Ark Invest, Bakkt, Coinbase, Kraken, Custodia Bank, Anchorage and others are investors in Bitcoin, they are not nefarious actors.

Australia

The US is very different from Australia and quite a few steps ahead. We do not have a Fidelity Investments. I feel it would be highly unlikely for, say, AMP, to launch a crypto product to their clients unless they had a strong green light from APRA, ASIC and the RBA. It would be even less likely that they would challenge a regulator in the way Fidelity has challenged the DoL and indeed the US Senate. It also probably does not help that our large financial institutions have a dreadful track record of compliance with the law and even fail basic ethical standards (see here and here and here).

That is not to say that our money managers are doing nothing, there is movement, but it's slow motion. On 21 April 2022, 4 months after the Commonwealth Bank announced their potential Bitcoin offering in November last year (see here), APRA issued a letter setting out risk and policy aspects of cryptoassets (see here). We have not heard anything from the CBA since.

Our legislators have been very slow to start work on cryptoasset specific initiatives and when they have started they have been few and far between. In August 2017 Labor senator Sam Dastyari and Liberal senator Jane Hume co-convened the 'Parliamentary Friends of Blockchain' group. Senator Andrew Bragg while in Government took this early work forward and in opposition is continuing to press for the regulation of crypto asset secondary service providers. Well done Senator Bragg but he is a lone voice, we are waiting to see what the current Government does on this front in the new year.

Closing Comments

One notable exception to the complacency in the Australia fund management industry is Holon who, as far as I can see, are the first traditional fund manager to become engaged in cryptoassets. They have

suffered some regulatory setbacks recently (I think unfairly), but are definitely one of Australia's traditional managers pioneering cryptoasset adoption at an institutional level. Also of note is ETF manager BetaShares who are starting to engage in this space.

I have to say that it is surprising to me that after more than 5 years of operations we are still one of the very few cryptoasset fund managers. It is hard to understand why Macquarie Bank or AMP or indeed any of the hundreds of traditional fund managers have not ventured into this space, even if it was to make a tiny allocation to Bitcoin in one of their technology based equity funds.

It seems to me there is a lot of groupthink and inertia in the fund management business. This will change, the time will come when 'the group' adopts crypto, it is inevitable, and when that happens we will well and truly benefit from the early start we had in the foothills of Mt Adoption.

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As always, please do not hesitate to contact me on 04 5090 0151 or at ian@bca.fund if you have any questions.

Best Regards

Ian Love

Founder and CEO

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