MONTHLY REPORT – FEBRUARY 2024

VIKĀRA

February 2024

Global Digital Assets

The time to invest in digital assets is now.

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FOMO is always required for investors to jump into an emerging market. Bitcoin has made fresh relative all-time highs versus the US 30-year bond, the Russell 2000, and it is knocking on the door relative to the S&P500 and NASDAQ. It is also close to its absolute all-time high.

A portfolio without digital asset exposure is fast becoming an underperforming one. Digital assets capture the return streams of novel business models and the demand from high net worths, family offices and institutions via the new launched spot ETFs is a first step towards a shift in capital flows.

The game theory of digital assets is structured for early adopters to be rewarded the most. Digital scarcity is real and an ever-expanding monetary system is fuelling adoption. As we've repeated – infinite fiat supply is meeting finite token supply. Sadly, much of the outperformance will have been earned by few by the time most realise the potential.

We are 23-months into the fastest tightening cycle in history and what many believed was a rate sensitive, long duration asset class, is teetering on new highs. We continue to ask investors the same question we have been asking since we launched: what are you waiting for?

Vikara launched in October 2022 and it felt like the worst possible time. Hindsight is 20:20 (Chart 1).

Chart 1 – Total digital asset market capitalization excluding Bitcoin and Ethereum (2019-2024)

Source: Tradingview.com

Many continue to claim they don't understand the space, that there are better returns elsewhere, or that digital assets won't be around long-term. In the last cycle, the ex-Bitcoin and Ethereum market capitalization rose 27x in 22-months. This opportunity doesn't exist elsewhere.

The next iteration of the digital economy is being built and adopted in real time. We are front row investors into what will be foundational infrastructure running global commerce. Just as Apple was to Blackberry and Netflix to Blockbuster, Web3 will be to Web2.

As an example, Uniswap (the largest decentralized exchange) proposed this week that wants to start charging fees for its services. If approved, it would have a price to earnings ratio overnight. Uniswap captured its audience, built its service, and will now monetize its work. Sounds like Web2 right?

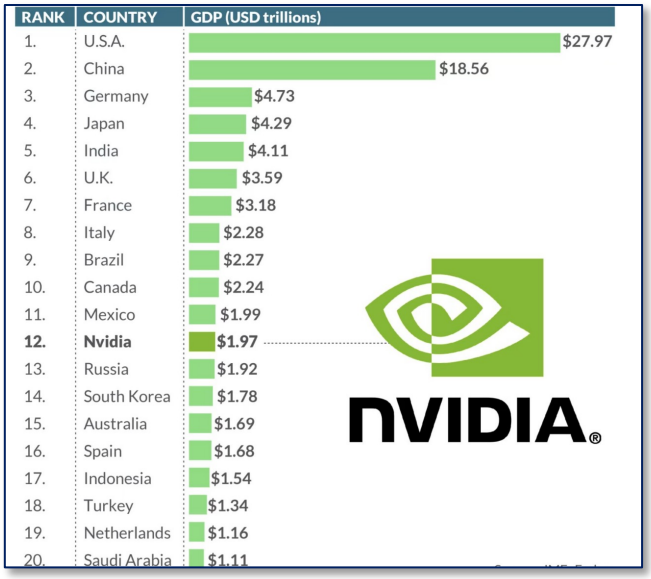
Uniswap has had $1.8 trillion in cumulative traded volumes in four years, earning $3.3bn in fees. With average monthly volumes of >$40bn, even a 0.2% fee would see ~$1 billion in fees sent to holders, translating to a ~10x price to earnings ratio. This is remarkably cheap given its growth potential.

Understanding digital assets and investing in the space is an all-encompassing task. The opportunities are incredible, and the pace is exponential. We built Vikara because we knew many would want exposure and needed a trusted partner to do this work for them.

We have spent the three years conducting due diligence on hundreds of tokens so that our portfolio is ready to capture this opportunity. We are ready. We hope you are too.

As Nvidia catapults higher, and a growing chorus of people scream “bubble”, is it too simple to acknowledge that this is the digital acceleration we have all been waiting for? Valuations aside, the message we take from Nvidia’s earnings is that Vikara is focused on the right place.

Chart 1 – Total digital asset market capitalization excluding Bitcoin and Ethereum (2019-2024)



Source: Tradingview.com

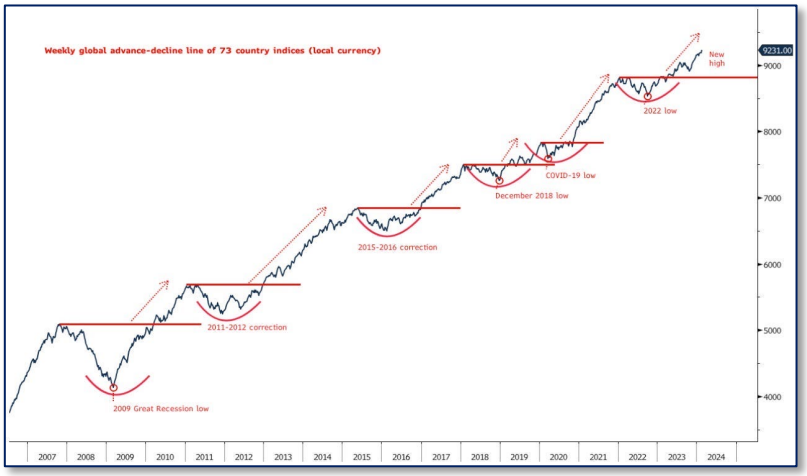
Market analogues should be taken with a grain of salt, but Chart 3 below is closest to how we feel right now. Capex is rising. Productivity is improving. Inflation is subsiding. Fiscal policy is supportive globally and monetary policy is peaking. We know this will trigger some, but we are bullish.

Chart 3 – In 1994, IT capex and productivity started a multi-year uptrend for Nasdaq

Source: Macrobond

When you put a bullish lens on, there is a lot to like. The global advance-decline line of 73 country indices continues to make all-time highs despite seeing some divergences in some of the second derivatives (Chart 4). Global markets are agreement that improving times are ahead.

Chart 4 – Weekly advance-decline line of 73 country indices (2007-2023)



Source: BoFa Global Research, Bloomberg

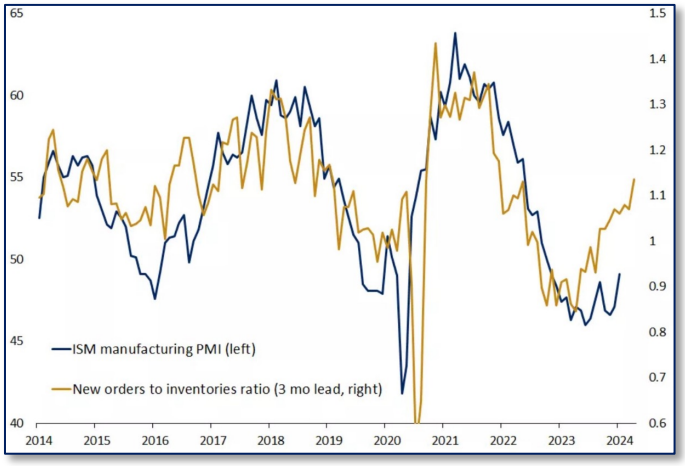
As we have noted in our past three updates, global industrial demand is improving. Asian export trends demonstrate this rebound, an indicator that is historically correlated with US PMI (Chart 5).

Chart 5 – Export growth (2000-2024)

Source: @BobEUnlimited

US ISM manufacturing PMI has turned and the leading new orders to inventory ratios are supportive of further growth moving forward (Chart 6).

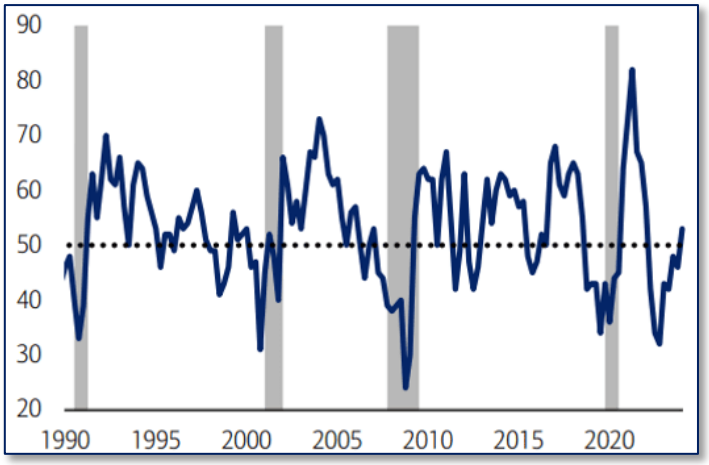
Chart 6 – ISM Manufacturing and new orders to inventory (2014-2023)



Source: Bloomberg, Edward Jones

CEO confidence is also rebounding, moving back above 50 for the first time in two years (Chart 7).

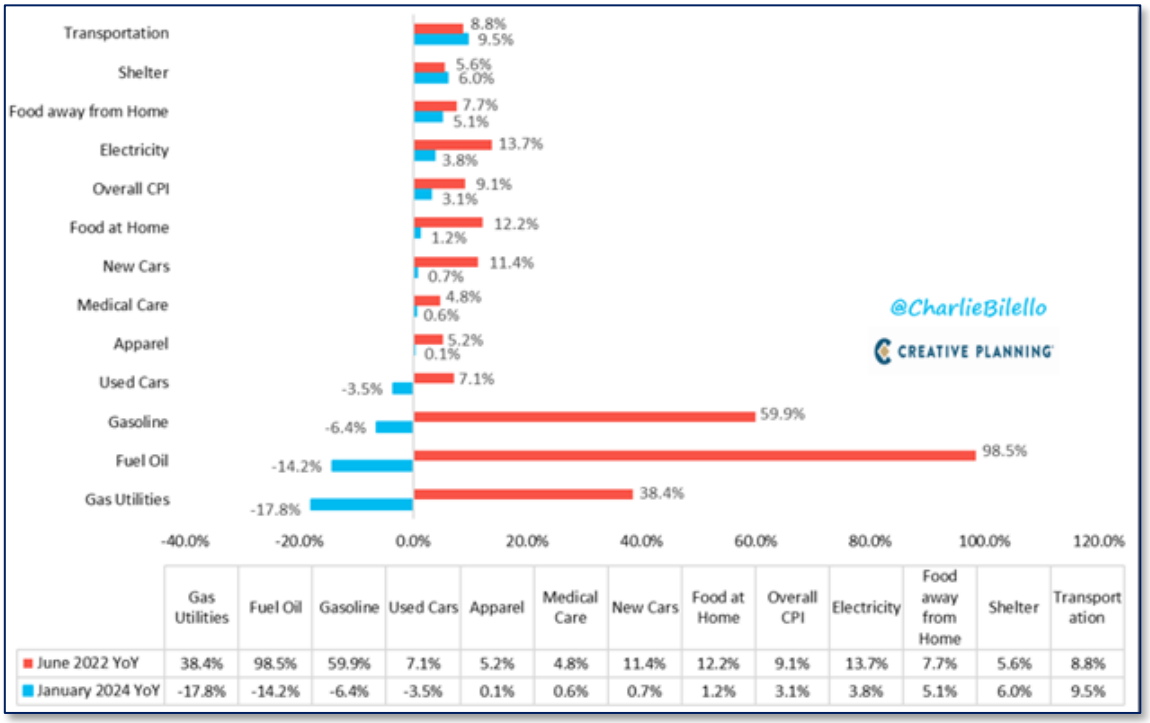
Chart 7 – Conference board CEO confidence index (1990-2024)



Source: BofA Global Research, Conference Board, Dailyshot.com

This has all happened within a backdrop of a fear that inflation is about to accelerate. As we have said before, we don't see it. Demand is increasing as prices fall. It is a supply side push rather than a demand side pull. Take a look at the YoY components for January inflation in the US (Chart 8).

Chart 8 – CPI YoY% (June 2022 versus January 2024)



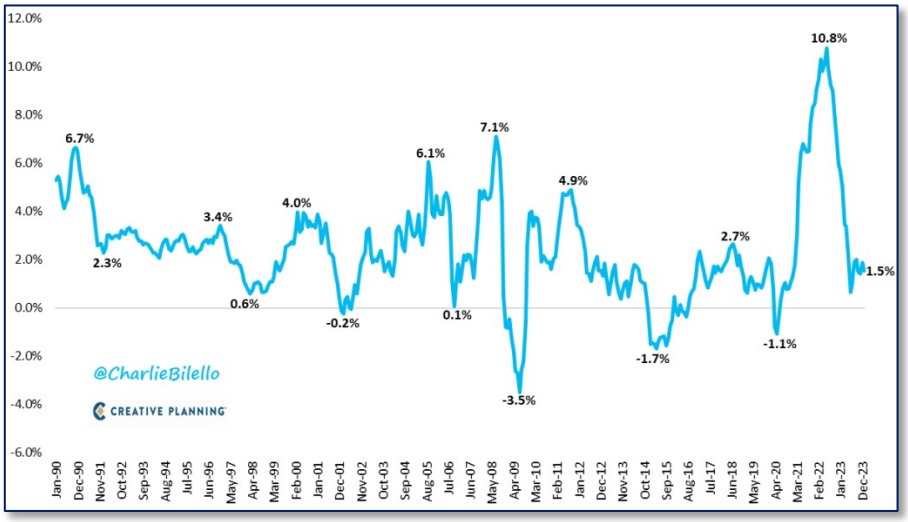
	Gas Utilities	Fuel Oil	Gasoline	Used Cars	Apparel	Medical Care	New Cars	Food at Home	Overall CPI	Electricity	Food away from Home	Shelter	Transportation
June 2022 YoY	38.4%	98.5%	59.9%	7.1%	5.2%	4.8%	11.4%	12.2%	9.1%	13.7%	7.7%	5.6%	8.8%
January 2024 YoY	-17.8%	-14.2%	-6.4%	-3.5%	0.1%	0.6%	0.7%	1.2%	3.1%	3.8%	5.1%	6.0%	9.5%

Source: @CharlieBilello, Creative Planning

Shelter is the primary reason inflation remains elevated. It is the largest single component of CPI and makes up around one third of the index. It increased 0.6% in January and 6.0% over the past year, it is single-handedly preventing the index from moving back down to the Fed's 2% target.

If shelter is removed from the index, CPI has increased only 1.5% over the last year. That's the 8th consecutive month below 2% and this is the only metric we are focused on (Chart 9).

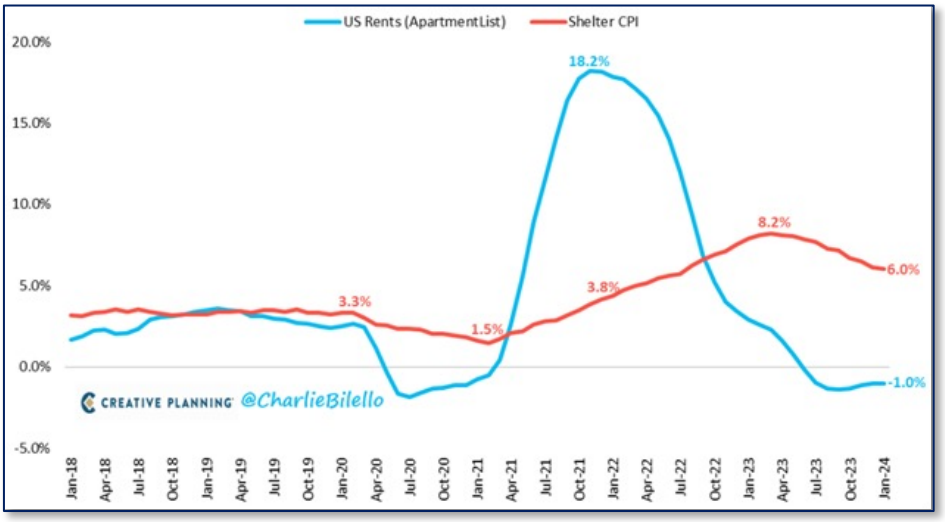
Chart 9 – US Consumer Price Index Ex-Shelter (YoY% change) (1990-2023)



Source: @CharlieBilello, Creative Planning

Shelter CPI is still elevated despite rents being down 1% over the past year because it is a lagging series in the index (Chart 10). As shelter heads lower throughout the year, inflation will come down.

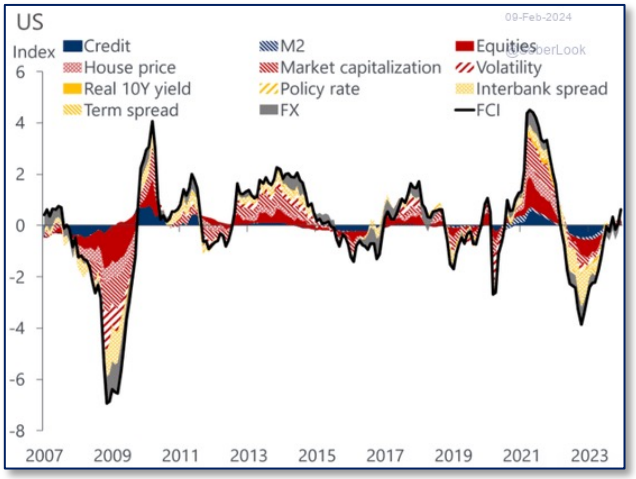
Chart 9 – US Consumer Price Index Ex-Shelter (YoY% change) (1990-2023)



Source: @CharlieBilello, Creative Planning

Looking at US financial conditions, recessions do not happen when money is being made. The rise in interest payments, equity markets, and global M2 provides a favourable tailwind as inflation moderates (Chart 11). Demand is not going anywhere, and likely rises from here.

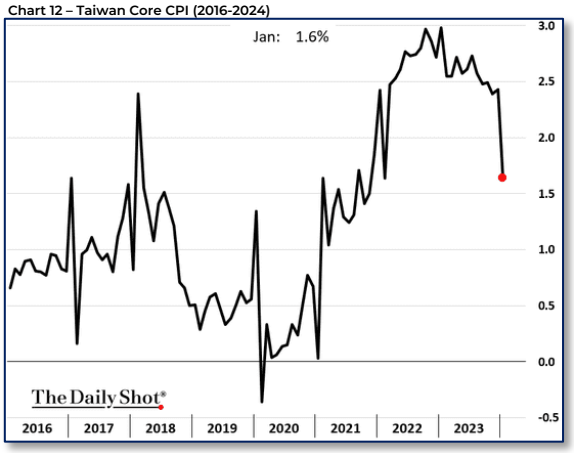
Chart 11 – US financial conditions (2007-2024)



Source: Oxford Economics, Haver analytics, theDailyShot.com

We understand markets are worried about stronger demand, as it risks driving inflation higher and the delaying the Fed's rate cutting cycle. This is unlikely. Disinflation, and in fact deflation is spreading across the world. Take a look at CPI in Taiwan, China's deflation is starting to leak out (Chart 12).

Chart 12 – Taiwan Core CPI (2016-2024)



Source: TheDailyShot.com

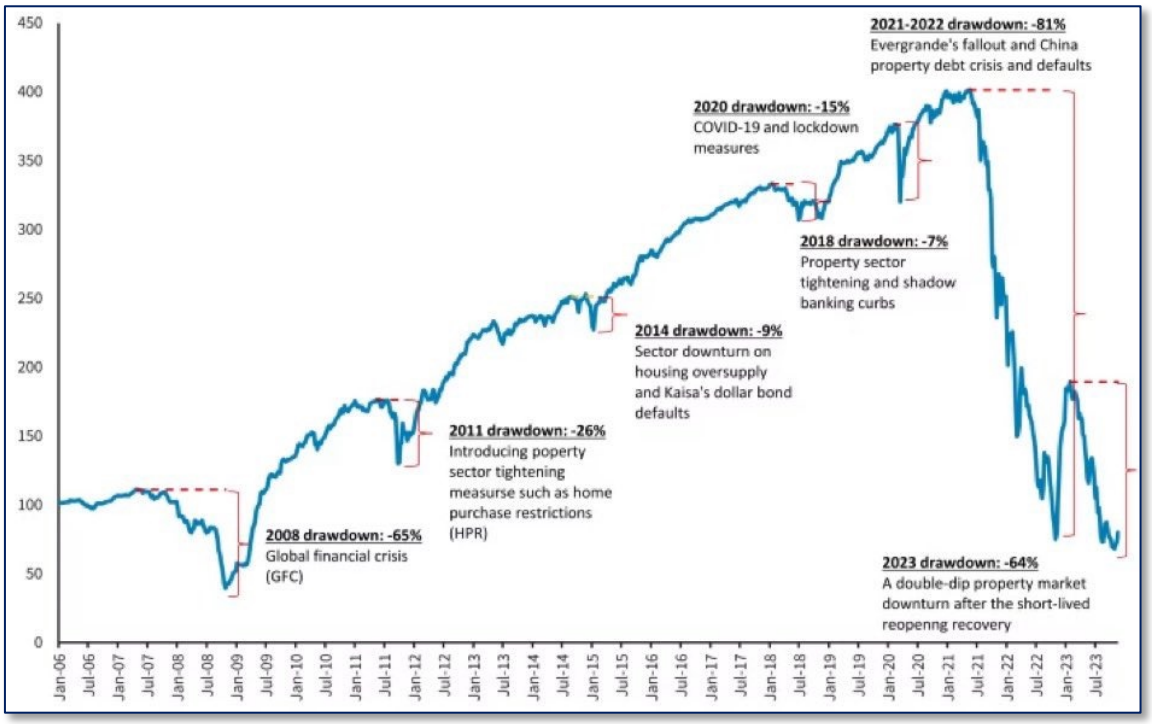
China's deflationary bust is showing up everywhere, its equity markets are collapsing, its treasury yields are in free-fall (Chart 13) and with the PBOC owned and operated by the government, there is no one is coming to help until the CCP nationalizes the assets it wants.

Chart 13 – China's 30-year treasury yield (2019-2024)

Source: Tradingview.com

It all centres around its real estate market, which is down a whopping 81% from 2021-2022 and another 64% from its rebound in 2023 (Chart 14).

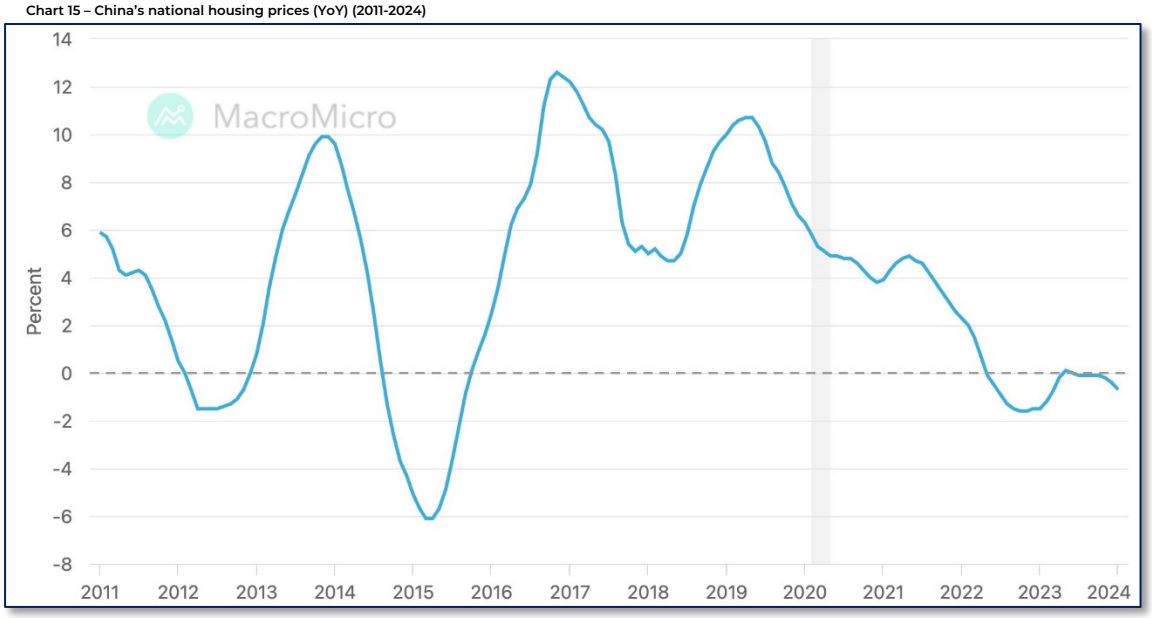
Chart 14 – China's real estate drawdown (2006-2024)



Source: @Barchart

Things are not getting better either. China's new home prices took fell 0.7% YoY in January, the largest drop in ten months and a worsening from December's 0.4% YoY decline. This marks the 7th consecutive monthly decline, hitting the fastest pace since March 2023 (Chart 15).

Chart 15 – China's national housing prices (YoY) (2011-2024)



Source: MacroMicro.me

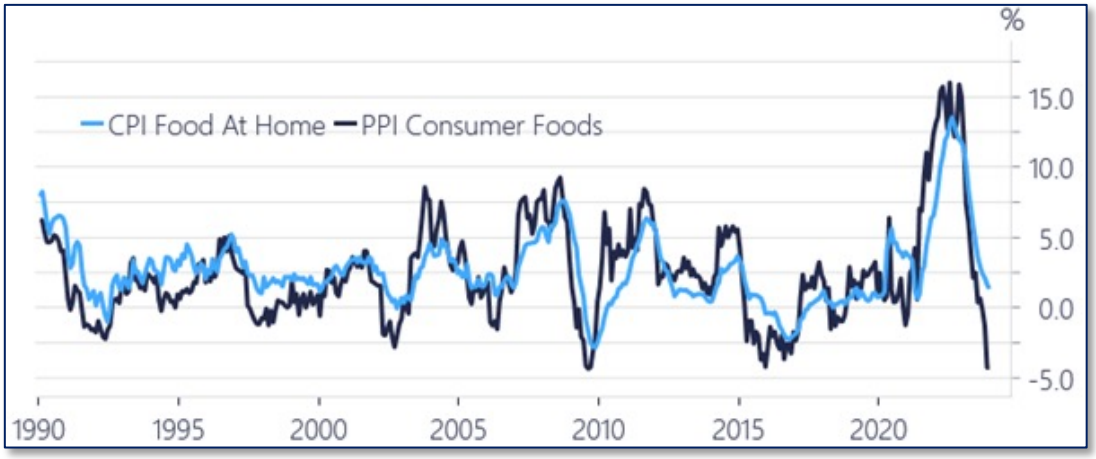
As we learned in the west in 2008, inflating a popped bubble isn't easy, and Beijing's efforts to address the property crisis and fragile economic have not helped so far. In fact, observing Chinese car prices, this is the deflation we are seeing exported to the rest of the world (Chart 16).

Chart 16 – Consumer price index of vehicles (YoY) (2002-2023)

Source: Financial times, China's National Bureau of Statistics, Wind

Food inflation is also a thing of the past, and while many manufacturers will try to hold onto margins as input costs fall, we expect to see declines in the near term in the grocery stores (Chart 17).

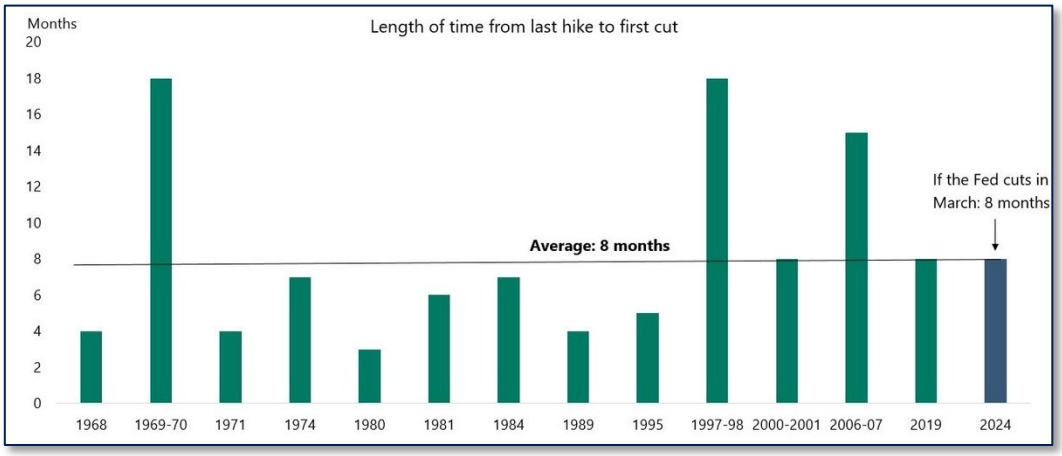
Chart 17 – CPI and PPI in food is starting to moderate (1990-2024)



Source: Steno Research, Bloomberg and Macrobond

With consumer goods, food, and rent prices likely to fall, the federal funds rate no longer needs to be >5%. People look to history for a reason, and we believe the data is quickly turning, allowing global central banks to communicate a need for looser monetary policy (Chart 18).

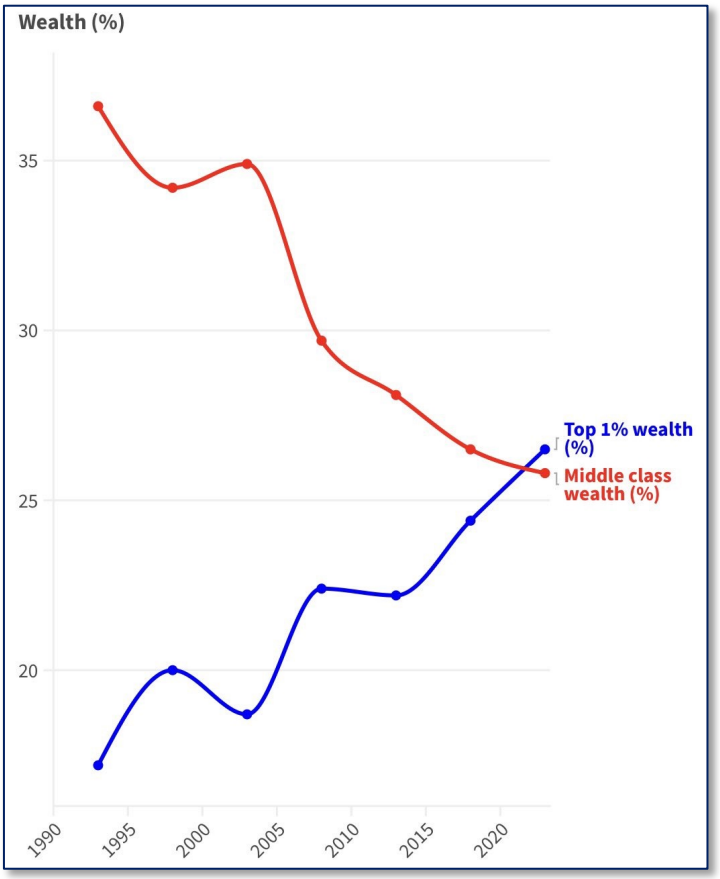
Chart 18 – It takes 8-months on average from the last Fed hike to the first Fed cut (1968-2023)



Source: Apollo

Forgive our scepticism, but falling inflation is music to the ears of the top 1%. Inflation is a risk for the rich. It turns the common person against them and makes them ask questions. As you can see, keeping the commoner focused on their lives, not the economy, works better for the rich (Chart 19).

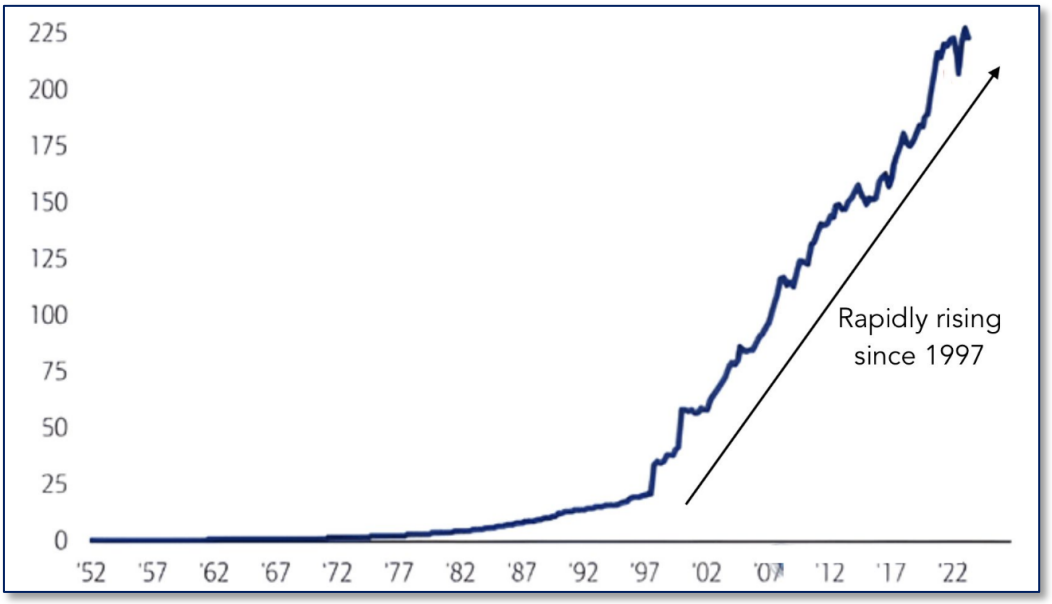
Chart 19 – Top 1% of earners now have more wealth than the entire middle class (1990-2024)



Source: @NorthmanTrader

So as global government debt spirals higher, and as the minority keeps taking the majority, it is not lost on us that the new digital ecosystem is the only escape for the majority (Chart 20). Sophisticated investors peer over the fence and label it as gambling, we see it as a desperate attempt to escape.

Chart 20 – World debt has crossed $225 trillion (1952-2024)



Source: BoFa global investment strategy, Bloomberg

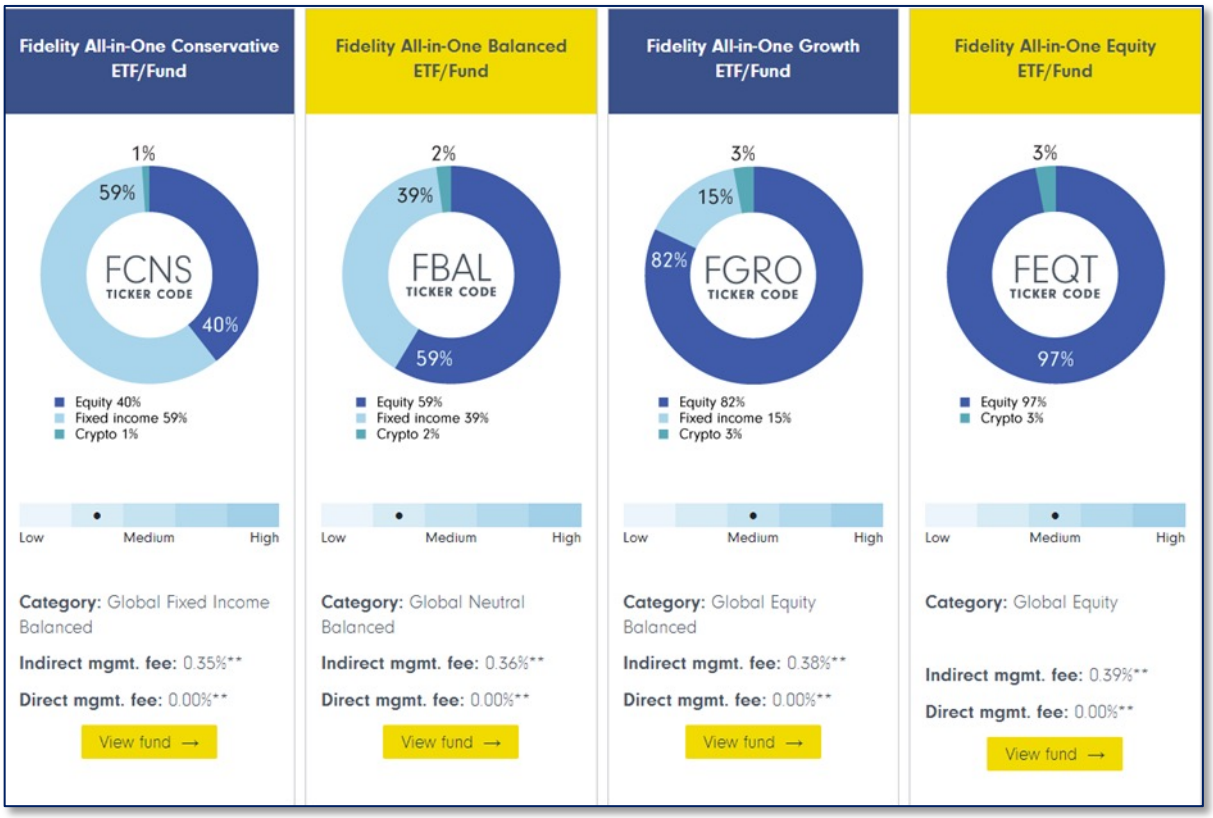
Blackrock and Fidelity are now two of the largest Bitcoin owners globally. ETH Denver pumping. Nvidia AI hardware sales drive massive interest in AI digital assets. JP Morgan upgrades Coinbase to hold after a 500% share price increase (LOL). That's just in the past week...yet, it's likely that only the appetizers are being served.

The tailwinds have been blowing for many months now. Here's a recap of what has and is likely to happen that drives digital assets to new all-time highs.

- SEC taking L's (Ripple, Coinbase) with regulatory framework shaping up globally (ex-USA)
- Bad actors cleaned up with SBF in jail and CZ's imminent sentencing
- Less than two months to halving with two previous cycles returning 56x and 17x through to peak, respectively
- Spot BTC ETF approved with spot ETH ETF approvals due in May, driving huge flows of capital into crypto
- Financial institutions from Blackrock, Fidelity, Franklin Templeton and Van Eck, pumping cryptos tyres
- RIA platforms onboarding digital assets and financial institutions begin to recommend digital assets as a core part of a diversified portfolio (Figure 1 below where Fidelity Canada recommending clients have between 1-3% of their assets in "crypto" as part of a diversified portfolio)
- Accommodative monetary policy likely with rate hike cycle largely complete (global monetary growth (M2) highly correlated to digital asset price increases)
- Significant market growth potential with global digital asset market cap ex-BTC and ETH less than 0.50% of global equities ($600bn vs $130trn)
- Populist / nationalist government leadership gaining momentum favoring alternatives to the USD / fiat systems

If we are right and it is still early days, what lies ahead is going to be a wild period.

Figure 1 – Fidelity Canada recommending clients allocate between 1-3% to crypto



Source: Fidelity.ca

News we found interesting during February 2024 includes:

- Uniswap ($UNI), the world's leading DEX, announced a proposal to begin distributing a portion of protocol fees (currently earned by liquidity providers) to token holders who have staked and delegated their UNI votes. The token nearly doubled on the news.
- VanEck announced the launch of SegMint, a Non-Fungible Token (NFT) marketplace and digital assets platform that aims to simplify self-custodial crypto sharing, bridging accessibility and security gaps.
- Citi brought a Wellington Management-issued private equity fund onto the Avalanche ($AVAX) blockchain to test on-chain trade execution and settlement. The fund's distribution rules were encoded into the smart contract and embedded within a token transferred to hypothetical WisdomTree clients. Citi was quoted as saying in the announcement: "Tokenization unlocks the value in traditional markets to new use cases and digital distribution channels while enabling greater automation, more standardized data rails and even improved overall operating models, such as those facilitated by digital identity and smart contracts."
- Ondo Finance ($ONDO), a tokenized real-world asset (RWA) platform, announced that they have integrated their tokenized U.S. treasury-backed product (USDY) onto Layer 1 Aptos ($APT), adding to USDY existing availability on Ethereum ($ETH), Solana ($SOL) and Mantle ($MNT).
- GoDaddy and Ethereum Name Service ($ENS) announced a partnership that will allow ENS domain holders (.eth) the ability to their DNS (domain name on GoDaddy) and use the website name in a host of Web3 applications at no cost, creating a seamless bridge between a Web2 and Web3 applications.
- Franklin Templeton filed for a spot ether ETF, joining the likes of Blackrock, Fidelity and ARK Investments.
- Avalanche purchased a stake in Sports Illustrated Tickets and will transition its NFT-enabled ticketing service, Box Office, from Polygon to its own Layer 1.
- ReadyGG announced Shawn Layden, who served as Chairman of Sony Interactive Entertainment (SIE) Studios and President and CEO of Sony Computer Entertainment America, Sony's PlayStation division, has joined the blockchain gaming infrastructure start-up.
- World Wrestling Entertainment (WWE) announced the launch of a digital Donruss Elite card set on the Panini blockchain.
- Japan Airlines announced a collaboration with marketing firm Hakuhodo on a project called Kokyo NFT that aims to tokenize local experiences and real-world assets (RWAs) as NFTs.
- EtherMail, a Web3 email solution, has launched its email-as-a-wallet (EaaW) solution, enabling users to create non-custodial wallets through Gmail or Apple accounts. EaaW allows users who currently do not have a digital wallet to access Web3 services as well as seamlessly buy, send and receive digital assets.
- Meso, a start-up founded by former Paypal and Venmo executives, is launching a new product that allows a seamless transition between crypto wallets and fiat banking apps without having to first send the fiat to a centralized crypto exchange. This will increase on ramp times while simplifying the process, hopefully leading to greater crypto adoption.

As noted above, Uniswap is putting forward a proposal to share revenue with stakers (essentially members of the Uniswap community).

This is nothing new. Multiple parts of crypto have shared "fees" or revenue with their communities. GambleFi, for example, has had a strong run on the back of fee sharing arrangements where stakers or liquidity providers share in the profits made by the house. Rollbit ($RLB) was one of crypto's best performers last year and micro caps like Bazed Games ($BAZED), Dubbz ($DUBBZ) or Blockchain Bets ($BCB) outperformed the broader crypto universe. This has led to dozens of new GambleFi platforms springing up as of late. While we're not sold on GambleFi as there are seemingly low barriers to entry and potential regulatory risks, we appreciate the revenue sharing aspect of their business models.

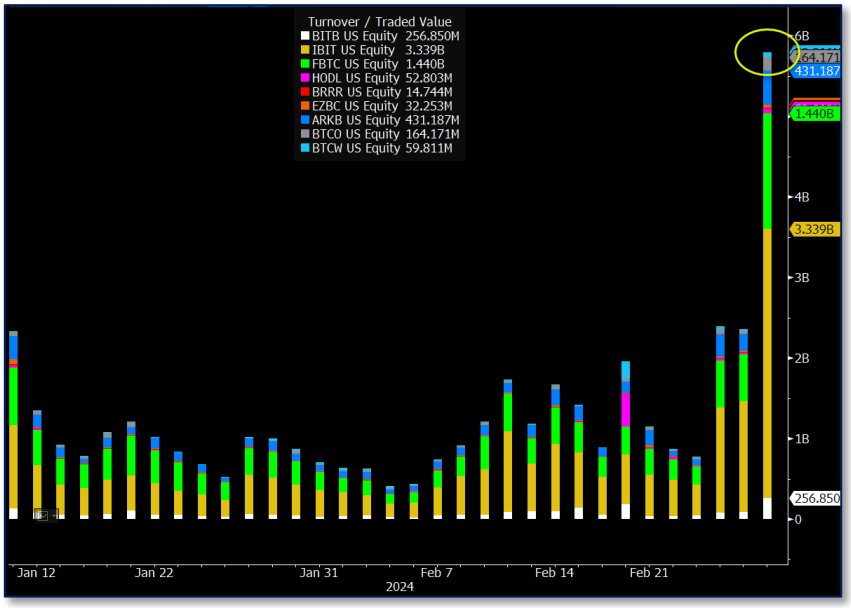
Following the Uniswap announcement, DeFi protocol Frax Finance ($FXS) said they will follow Uniswap's lead and issue a proposal to distribute a portion of protocol fees to stakers of its native token. FXS token was up 15% on the announcement.

Additionally, Telegram announced that they will begin sharing ad revenue with users starting in March, with channel owners receiving 50% of ad revenue. All payments and withdrawals will be settled on the TON blockchain ($TON), which was built by the Telegram team but was split from the messaging service in 2020. Token TON surged over 60% on the news.

We expect to see continue to see similar strategies as projects look to increase total value locked (TVL) within their ecosystems. Further, revenue sharing with the community helps create continual engagement with token holders and hopefully translates into a network effect and in turn a higher token price.

Bitcoin has rightly grabbed most of the attention as ETF inflows continue to explode with $6bn traded on Monday, February 26, with Blackrock totalling $3.3bn and Fidelity $1.4bn (Chart 21) that day alone, and the BTC price approaching all-time highs.

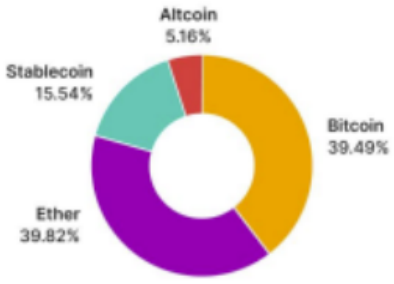
Chart 21 – Bitcoin ETF Turnover/Traded Volume (through February 26, 2024)



Source: x.com @EricBalchunas

That said, Ethereum is on the top of the mountain in terms of institutional ownership. Bybit's recently released quarterly analysis showed that institutional portfolio allocation to Bitcoin and Ether surged from 50% to 80% from September 2023 to January 2024, with Ether at 38.9% to Bitcoin's 39.5% (Chart 22). Reminder that ETH is the digital asset ecosystem bellwether. Just wait until there is an ETH ETF.

Chart 22 – Institutional Asset Allocation (as at January 31, 2024)



Source: Bybit – Navigating Bull and Bear Markets: A Dive Into User's Asset Allocation (2024Q1)

Also of note is the low institutional allocation to altcoins, although this is not surprising given we are still likely in the early stages of a crypto bull run. Altcoins tend to significantly outperform BTC and ETH as the cycle progresses.

While we haven't discussed tokens for several months, we wanted to highlight one token that many who have been involved in the crypto world prior to this recovery are familiar with but may have long forgotten.

Theta ($THETA) was born out of a desire to decentralize video streaming, data delivery, and edge computing, making it more efficient, cost-effective, and fair for industry participants. They started their journey as a blockchain-powered video streaming network but have since pivoted to edge computing and in turn are benefiting from those looking to gain exposure to AI (more on that later).

Founded in 2018 by Mitch Liu and Jieyi Long, who have backgrounds in gaming, virtual reality, and large-scale distributed systems, they brought in Steve Chen, co-founder of YouTube, and Justin Kan, co-founder of Twitch, as lead advisors, from the industry they were looking to disrupt.

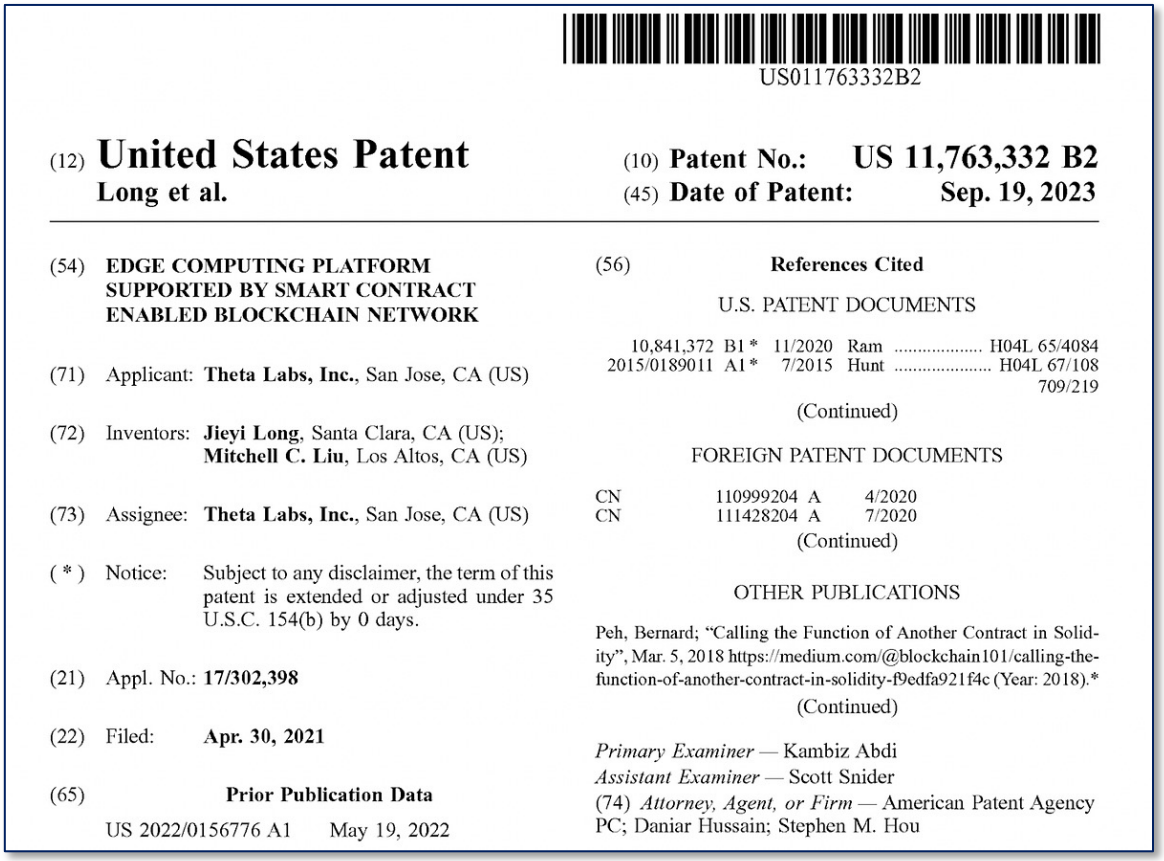
The Theta mainnet was launched in 2019 and operates as a decentralized network where users share bandwidth and computing resources on a peer-to-peer basis.

As part of their original plan to disrupt traditional video distribution, the Theta Edge Network was launched in 2021 focused on GPU intensive video processing required for encoding, transcoding and distribution. This global network of nearly 10,000 active edge nodes run by community members comprises one of the largest clusters of distributed GPU computing power in the world with approximately 77,538 TFLOPS or about 80 PetaFLOPS, roughly equivalent to 250 NVIDIA A100s, always on and always available. Combined with Theta's access to an additional >800 PetaFLOPS through cloud partners they can deliver >2,500 equivalent NVIDIA A100s, enough to train and serve some of the largest language models (LLMs) globally.

Fast forward to today with the imminent release of Theta EdgeCloud phase 1, estimated to launch on May 1, 2024. It is being advertised as one of the most advanced decentralized software platforms in edge computing. Its mission is to provide developers, researchers and enterprises with unlimited access to GPU processing power for any AI or video task, at the most optimal cost.

While there are many companies chasing distributed GPU processing power, Theta took a novel approach early in EdgeCloud's development. In 2021, Theta first filed a patent for the "Edge Computing Platform supported by Smart Contract enabled blockchain network", which was granted in September 2023 (Figure 2).

Figure 2 – Theta's Patent US 11,763,332 B2



US011763332B2

(12) **United States Patent**
Long et al.

(10) **Patent No.: US 11,763,332 B2**
(45) **Date of Patent: Sep. 19, 2023**

(54) **EDGE COMPUTING PLATFORM SUPPORTED BY SMART CONTRACT ENABLED BLOCKCHAIN NETWORK**

(71) Applicant: **Theta Labs, Inc.**, San Jose, CA (US)

(72) Inventors: **Jieyi Long**, Santa Clara, CA (US); **Mitchell C. Liu**, Los Altos, CA (US)

(73) Assignee: **Theta Labs, Inc.**, San Jose, CA (US)

(*) Notice: Subject to any disclaimer, the term of this patent is extended or adjusted under 35 U.S.C. 154(b) by 0 days.

(21) Appl. No.: **17/302,398**

(22) Filed: **Apr. 30, 2021**

(65) **Prior Publication Data**

US 2022/0156776 A1 May 19, 2022

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(Continued)

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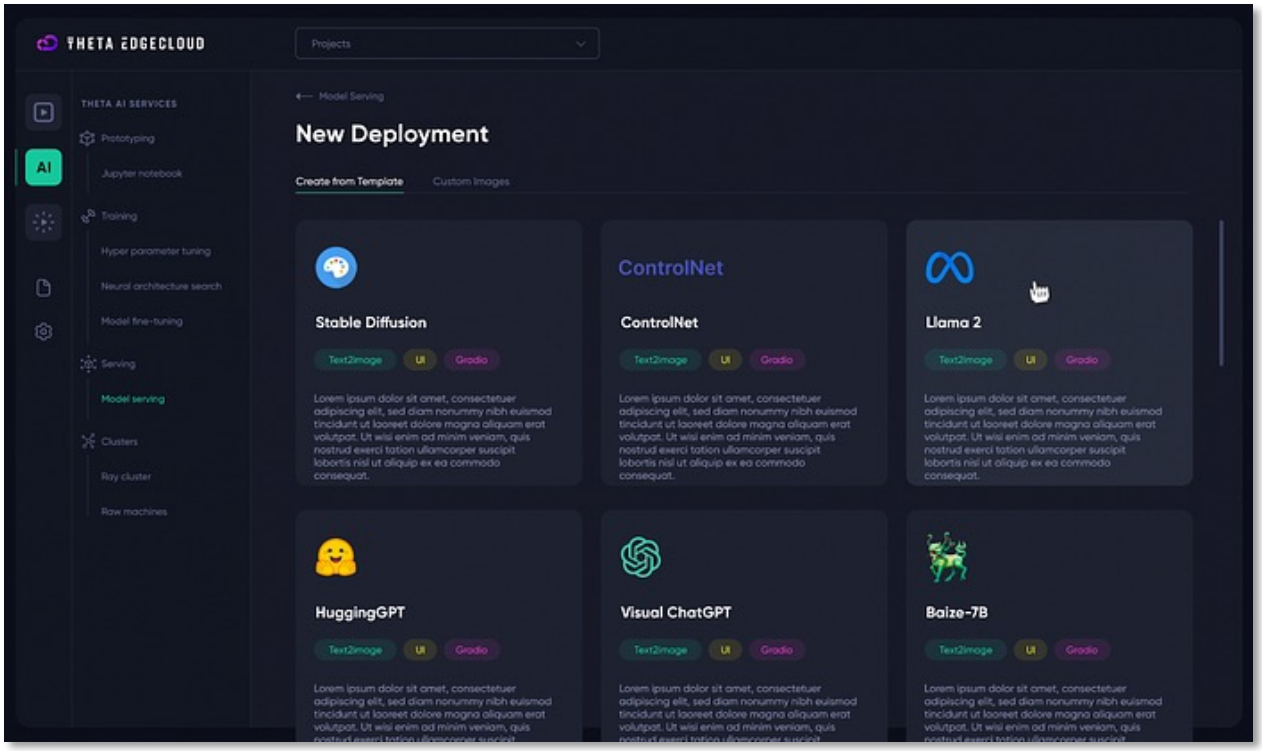
Source: uspto.

This allowed for the capability to build a next generation hybrid computing architecture, where computation tasks are registered on a blockchain, and assigned to an edge computing node within a decentralized computing network through a secure peer-to-peer connection. The solution may be verified on-chain by a smart contract and a token reward may be given to the participating node.

Additionally, Theta has been working with partners to build natural language processing (NLP) and machine learning applications. For example, they have recently partnered with Google Cloud to develop an "AI Model Pipeline for Video-to-text Applications" with applications in semantic video search and e-sports game highlight video generation, for example.

Back to the coming launch of EdgeCloud phase 1 in less than three months. The platform will allow AI developers to select and deploy popular models for genAI text-to-image, text-to-video models (Stable diffusion, Llama 2) and cutting-edge new text-to-3D models with just a few clicks (Figure 3).

Figure 3 – Theta EdgeCloud AI Developer Platform



Source: Theta Labs

This library of templates can be expanded over time to capture the most popular AI models including today's chat bots, generative AI as well as new future models.

Looking forward, Theta intends to deploy the first hybrid cloud computing platform built on a fully distributed edge architecture, where edge nodes operated by community members will work seamlessly and in tandem with cloud operated infrastructure.

While there is no doubt hype surrounding AI and its potential impact, good and bad, on society, there are few ways to properly get exposure to the trend without taking significant risk. We view Theta's pivot to computational power and AI as one way to do just that.

Contact Us

Vikara is an open-ended fund, with investors able to add or redeem monthly. Please contact Luke or Mark if you would like to discuss anything further.

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Vikara, in Sanskrit, describes the process of change. Its definition is constantly evolving, changing with economic cycles, technology, and geopolitics. It is a transformation of thought or logic, a modification in the direction of travel, an alteration in action or participation. It is one thing to want change, but another to drive it. We believe in a world where commerce doesn't

need intermediaries. Where people are paid directly for content, time, and effort. Where privacy, data and free speech is given, not something to opt-in for.

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