NUS Temasek Stock Pitch

**Alpha Capital**

Investment Themes: **Digitalisation**

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**Figure 1: Coinbase Revenue Growth Against Bitcoin’s Quarterly Returns**

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**Figure 2: Coinbase Revenue Breakdown**

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**COINBASE** (NASDAQ: COIN)

Recommendation: BUY (+30% Upside) Current Price (30th August 2021): $260

Sector: Financials (NASDAQ) 12 Month Price Target: $338

**Early Innings Of Fintech Disruption**

Business Description

Coinbase is the leading crypto trading platform for retail and increasingly institutional alike to trade and invest in different cryptocurrencies. We maintain a strong BUY recommendation on COINBASE with a 30% upside target based on the investment theme of digitialisation and the increasing applications of digital assets and use of exchange platforms like Coinbase to facilitate the development and democratisation of money.

In this report, we will take a closer look at Coinbase’s unique comparative advantages and strategic outlook as well as its tremendous future business potential in the cryptocurrency ecosystem that is still in the early infancy phrases of growth and adoption.

* Coinbase > Buying Bitcoin as an investment: Coinbase has continued to diversify revenue streams and innovate on its product and services to be the defensive during potential “crypto winners” or severe drawdowns on cryptocurrency prices. Coinbase is a safer investment that just buying Bitcoin or Ethereum because its business model has expanded beyond simply collecting commission fees from trading, which traditionally has been highly correlated with the volatility of crypto asset prices.
* Coinbase’s revenue growth outpaces growth in Bitcoin prices: Coinbase has built a great reliable platform that looks to be the first touchpoint for new investors, as the cryptocurrency asset class gains widespread adoption. In addition, Coinbase has also positioned itself well to take advantage of new innovations and development in the crypto space such as NFT marketplaces and stablecoins used in DeFi ecosystem such as cross-border payments.
* Preferred platform for financial institutions which will drive next phrase of strong revenue growth: Coinbase has always been synonymous with being a platform of retail traders, which in the second quarter of 2021 recorded $1.8 billion in trading revenue. But increasingly over 9000 financial institutions have adopted Coinbase as a one-stop for all the services they need including trading, custody, lending, yield generation, data and more across a broader spectrum of crypto assets. Financial institutions trade with much larger size and capital and that presents more revenue opportunities as they expand their suite of product and service offerings.

**Figure 3: Coinbase’s Revenue Model**

Chart

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**Figure 4: Various Coinbase’s Subscription & Services Revenue Streams**

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**Coinbase is not an exchange**

Coinbase has traditionally been viewed as an exchange where retail and institutions alike can deposit fiat money and buy/sell cryptocurrencies. They collect commission fees per transaction and this transaction revenue represents over 90% of their total revenues each quarter.

Coinbase has also continued to innovate to bring new revenue streams and value-add their existing retail and institutional customers. New subscription revenues arise from asset-based services such as borrowing, yield generation and lending of cryptocurrency assets as well as custody and brokerage solutions for more sophisticated customers.

These new revenues subscription and service streams brought in $100 million in the second quarter of 2021, up 82% compared to Q1 2021. In particular, Custodian fee revenues were up 35% QOQ as well as earn revenue up 60% QOQ, demonstrating strong demand and response for new initiatives launched by Coinbase for retail and institutional customers.

In the future, Coinbase looks to operate less like a traditional exchange and more like a neo-bank. Coinbase is looking at offering big-bank bundle of services and product offerings on a new digital financial paradigm for both retail and institutional clientele to help manage, build and grow their cryptocurrency assets.

We anticipate the growth rate of subscription and service revenue to outpace traditional transaction revenues streams which could potentially be eroded as new crypto exchanges come into the scene.

Subscription services initiatives introduced by Coinbase helps bring forth the value proposition of Coinbase as a safe, secure, reliable, easy to use and all-encompassing super-app for all your crypto financial needs.

Macro Analysis

The cryptocurrency market is still in its infancy and therefore there are bounds for periods of high volatility. Amongst all the cryptocurrencies, Bitcoin has the biggest market cap at over $900 billion as of 30th August 2021 followed by Ethereum at $375 billion. Bitcoin also records the highest trading volume amongst all other cryptocurrencies, at over 30 billion in average trading volume in the last 3 months.

Chart, histogram

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**Figure 5: Bitcoin/USD trading volume since 2015 on Coinbase (Source: Bitcoinity.org)**

The uncertainty and the volatility of the cryptocurrency market is one of the reasons why plain investment in particular cryptocurrency assets like bitcoin presents clear risks. Many crypto assets like Bitcoin are not backed by any tangible assets, but rather the price action are pure representations of market supply and demand.

**Crypto as a new assets?**

The general impression of cryptocurrency is that they are nothing more than potentially a hedge for inflation and the devaluation of fiat currencies like the US dollar following the Covid-19 pandemic. However, many question crypto assets like bitcoin as a store of value due to inherent high volatility, zero practical use and zero utility.

Industry Overview & Competitive Positioning

**Industry Outlook**

While Coinbase was one of the early founders of a cryptocurrency marketplace and exchange, it is now not the only cryptocurrency exchange. Global exchanges like Binance, Square’s Cash App as well as even Paypal has set-up similar competitive exchanges offering low transaction fees and access to a wide variety of currency pairs. However, all exchanges in this space are facing increasing regulatory roadblocks from governments around the world, which questions the validity of Cryptocurrency as a safe and reliable asset class.

**Regulatory Challenges**

Recent regulatory crackdowns by various governments around the world including China, Malaysia and Brazil where bitcoin is mined illegally using cheap electricity as well as heightened tax scrutiny in the US have contributed to the recent nosedive of crypto asset prices from their all-time-highs back in April 2021.

The lack of regulatory clarity has been the major stumbling block for mass adoption of cryptocurrency as an asset class in many fund manager’s portfolio today.

However, new and rapid developments in the crypto space like NFTs and DeFi Stablecoins have increasingly made it difficult for many to turn a blind eye to the cryptocurrency ecosystem. While still in its infancy, cryptocurrency undeniably has the potential to be a fully digital, global asset class that is accessible for all and thriving digital ecosystem for many innovations for a more borderless, frictionless world.

**Maturity Of Coinbase’s Business Model**

Coinbase has transitioned from a transaction-based business model to a more expansive ecosystem supporting a new service and subscription model. In the early years, Coinbase generated revenue by sending and receiving transactions. At the end of 2013, services for investing followed. This transition allowed Coinbase to be less concerned about short-term

Financial Analysis & Projections

Coinbase business model comprises of two key revenue streams: transaction revenues which make up over 95% of total revenues at 1.9billion in Q2 2021, and subscription and service revenues which make up 5% of 100million in Q2 2021.  **Figure 6: Coinbase Revenue Breakdown For Q1-2 2021**

When retail or institutions buy or sell cryptocurrencies, Coinbase collects a commission fee from that transaction and that revenue falls under transaction revenue. Due to the extremely volatile nature of many cryptocurrency asset prices, transaction revenues are more uncertain and unpredictable in the short run as strong declines in prices of Bitcoin and Ethereum, like the ones we saw in April 2021, will negatively impact trading volume and thus impact the commissions generated from transactions. However, in the long run, we expect Coinbase’s transaction revenues to continue to grow at a Compounded Annual Growth Rate (CAGR) of 30% YOY as more retail and institutional investors embrace cryptocurrency as a new asset class and store of value.

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| US$m | FY 2019 | FY 2020 | FY 2021 | FY2022 | FY2023 | FY2024 |
| Transaction Revenue | 415.602 | 995.146 | 4930.630 | 3,745.43 | 3,507.93 | 6,993.86 |
| Transaction Revenue Growth | -Incomplete data- | 139% | 395% | -24% | -7% | 99% |
| Subscription Revenue | 17.319 | 45.1 | 270.6 | 207.5 | 168.3 | 358.6 |
| Subscription Revenue Growth | -Incomplete data- | 160% | 600% | -23% | -19% | 113% |
| Total Revenue | 432.919 | 1,040.246 | 5,201.230 | 3,952.930 | 3,676.230 | 7352.460 |
| Revenue Growth YOY% | -17% | 140% | 400% | -24% | -7% | 100% |
| Adjusted EBITDA | 24.27 | 527.35 | 2,669.43 | 2,365.99 | 2,530.29 | 6,102.16 |
| EBITDA Margin % | 56% | 50% | 51% | 70% | 69% | 83% |
| Net income | -30.4 | 322.3 | 1,889.0 | 1,674.0 | 1,792.4 | 2,246.4 |
| Net profit margin % | -7.0% | 31.0% | 36.3% | 42.3% | 48.8% | 59.3% |
| EPS | -0.17 | 1.58 | 10.33 | 11.16 | 11.94 | 20.11 |

**Financial Overview**

The chart above reveals Coinbase’s current financial condition since IPO as well as future projection for the next five years, with an emphasis on revenue growth in FY2021, FY2022 and FY2024 attributing to the sudden soar1 of bitcoin in late FY2020 and early FY2021, and the bitcoin halving of 2024 in a similar fashion. This explains the negative YOY growth in FY2022 and 23.

We believe that this projection is very modest, given our usage of yearly data and NASDAQ: COIN’s IPO not long ago. Since bitcoin prices have been heavily correlated to the tran For eg, Year to Q2 Adjusted EBITDA is already $2,267m while our forecast for 2021 is only $2,669.43m and EPS in table is $10.33 for FY2021 while in reality, it is $11.78 for EPS six month ended June 30.

Financial Analysis – Revenue Growth

Net growth of 774% from FY2019 to FY2024. This demonstrates the ability of Coinbase in capturing a greater % of market share in the Crypto space going forward. Notwithstanding the ongoing efforts of COIN in expansion in Asia and adopting a wider range of payment methods2.

Financial Analysis 2 – Profit Margins

Our team asserts that Coinbase will see a steady increase in Coinbase’s profit margins as we have mentioned before, Coinbase’s poaching of Kate Rouch4 who saw Facebook rise from a small company into the Tech Giant it is today. Our team stands that Coinbase has the potential to follow in its footsteps.

Valuation

Valuation Price Target: 320.51 ; derived from PE method (Used this method as Coinbase is growth stock)

Price/estimated EPS (11.16 of FY2022)= Trailing PE (is 28.72 as of tdy)

Revenue projections

Our revenue model included the 5 revenue-generating segments of the Company – (a) Custodial Fee (b) Blockchain (c) Earn Campaign (d) Interest, and (e)Other subscription and services.

For each of segment, we took the no. of MTUs multiplied by the revenue per user.

We projected the future growth of the volume and revenue per user based on our industry and BTC Price Cycle. (Although Altcoins have been getting more popular, Altcoins have been known to move in tandem with BTC prices)5

Figure : BTC prices, 31 AUG 2021 from Coinbase

Relative valuations: (incl charts here)

Valuation

**Valuation**

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Figure : EBITDA margins % against competitors/Ndaq

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Figure : EPS against competitors/Ndaq

Background pattern

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3 <https://sg.finance.yahoo.com/news/coinbase-names-former-facebook-executive-182339036.html>

4 <https://www.businessinsider.com/coinbase-poaches-facebook-vet-kate-rouch-as-its-cmo-2021-8>

5Ahmet Faruk Aysan , Asad Ul Islam Khan and Humeyra Topuz. Bitcoin and Altcoins Price Dependency: Resilience and Portfolio Allocation in COVID-19 Outbreak. MDPI risks. **2021,** 4 of 13.

**Investment Risks**

Individual Risk Analysis

Market Risk | Fluctuations of prices of Bitcoin and other crypto assets (MR)

Users make use of Coinbase to purchase and sell cryptocurrencies by depositing fiat money. Transaction fees are charged per transaction, and it accounts for 94% of Coinbase’s revenue each quater.

Given the high volatility of prices of Bitcoin and cryptocurrency in general, Coinbase’s revenue might be unstable.

To mitigate this risk, Coinbase plans to diversify its revenue streams by encouraging existing customers to branch out to using their new products and services, which includes lending and staking. Coinbase also plans to offer NFTs (Non Fungible Tokens), which are blockchain-based tokens that surged in usage in recent months.

Regulatory Risk | Uncertainty of regulatory and ESG developments (RR)

As climate change and sustainable development comes to light in recent times, more world investors are concerned about environmental, social and governance aspects. We are uncertain if any strict regulations will be imposed to ensure ESG compliance, and unsure if major financial institutions would be participative in opting cryptocurrency as an asset class.

However, the upside would be that technology is evolving to be able to incorporate ESG-friendly practices in blockchain based bonds. According to Coinshare.co, 74% of Bitoin mining is actually run on green energy, and enhanced research and adoption of green energy would reduce electricity usage and carbon emissions.

Structural Risk | Dual-class structure of shares (SR)

Coinbase went public with a dual class share structure, in which Class A shares comes with voting rights unlike Class B shares. Coinbase insiders hold more than 60% of voting control, which then naturally excludes public and institutional investors. Imperfect information about the company’s internal affairs and the lack of control might put off potential investors.

Catalysts

Rise of Non Fungible Tokens (NFTs)

NFTs are digital blockchain based tokens which can be used by consumers to represent a unique ownership of an asset or item. Common and popular uses include digital art, music and even real estate. A NFT token can only have one owner at a time and is secured by the Ethereum blockchain. A recent transaction of $69 million NFT token was made in the form of an artwork auction. With the rise of unique technology, the future usage of NFTs and in turn potential revenues of Coinbase cannot be neglected.

Rise of 5G mobile connectivity

As cryptocurrencies usually require more complex and more demanding functions to process transactions, the up and coming 5G network would provide the much needed high speed and low latency quality to complete transactions more efficiently. According to Statista, 48.20% of people in the world have smartphones today, up from 33.58% in 2016. As 5G internet gradually roll out in developed countries in at least the next 5 years, and cements its place in the society in the next 10-20 years, the usage of cryptocurrency and consequently Coinbase would be tremendously facilitated.

**ESG**

ESG rating

According to CSRHub, Coinbase ranks 91 out of 24,939 companies[[1]](#footnote-2).

Electricity usage

According to the Cambridge Bitcoin Electricity Consumption Index, annual electricity consumption of Bitcoin rose from 4.67 TWh in Jan 2016 to 91.01 TWH in 2021[[2]](#footnote-3).

Effects on carbon emissions

According to a 2019 study in scientific journal Joule, Bitcoin mining is estimated to generate between 22 and 22.9 million metric tons of carbon dioxide emissions a year[[3]](#footnote-4).

Sustainable Future

Despite the increasing electricity usage and relatively high carbon emissions of Bitcoin, which suggests there exists environmental damage as a whole, there are increased attempts to make cryptocurrency greener. The competitive nature of cryptocurrency mining would incentivize miners to constantly source and innovate for solutions to minimize electricity usage. With the increased emphasis on ESG standards in investments, there is also incentive to shift towards

powering cryptocurrencies with green, renewable energy.

In Siberia and Canada[[4]](#footnote-5), there exists ongoing projects such that the production of Bitcoin is driven away from fossil fuels to using renewable energy like hydropower. There are also attempts to channel heat generated by mining to other needs such as agriculture and heating. For instance, using power generated by flare gas - a by-product from oil extraction usually burned off - for crypto mining.

1. [CSR & sustainability info for Coinbase Global Inc | CSR Ratings (csrhub.com)](https://www.csrhub.com/CSR_and_sustainability_information/Coinbase-Global-Inc) [↑](#footnote-ref-2)
2. [Cambridge Bitcoin Electricity Consumption Index (CBECI)](https://cbeci.org/) [↑](#footnote-ref-3)
3. [How big is Bitcoin's carbon footprint? (nbcnews.com)](https://www.nbcnews.com/tech/tech-news/big-bitcoins-carbon-footprint-rcna920) [↑](#footnote-ref-4)
4. [How big is Bitcoin's carbon footprint? (nbcnews.com)](https://www.nbcnews.com/tech/tech-news/big-bitcoins-carbon-footprint-rcna920) [↑](#footnote-ref-5)