MULTICOIN CAPITAL

MULTICOIN CAPITAL

- About Us
  - About Us
  - Careers
  - Press
- Contact
- Education
  - Curated Reading List
  - FAQ

August 31, 2017

Ripple ($XRP) Analysis

by Myles Snider

An executive summary is presented below. Download our complete 12 page analysis:

Download

Executive Summary

Ripple is a blockchain protocol for inter-bank settlements. Unlike many other blockchains, Ripple is designed to work with existing institutions to facilitate the ability to quickly transact *any* asset globally. While the Ripple protocol has a native currency, XRP, this cryptocurrency is only required to pay transaction fees on the Ripple network. It can be used in other instances, but banks have the option to transact IOUs in any asset, including USD, EUR, and other fiat currencies, directly on the Ripple network. Ripple is primarily designed as a back-end infrastructure tool that facilitates decentralized exchange of assets between banks.

The Ripple protocol is designed and maintained by Ripple Inc., a California-based C-corporation that's raised over $93 million in venture capital. Ripple Inc. currently holds the vast majority of XRP tokens and also maintains a great deal of control over the network, though it has outlined plans to democratize control in the future. Both of these are major risks.

We recognize that the Ripple protocol has an opportunity to displace legacy inter-bank networks, but we must distinguish between a good use for a blockchain and a good investment opportunity. We believe that the Ripple protocol satisfies the former, but that XRP does not satisfy the latter. The Ripple protocol can impact trillions of dollars of economic activity, but this commerce is unlikely to be conducted in XRP. The XRP token has little core utility beyond fee payment and is unlikely to grow in value proportional to Ripple network usage.

Ripple Protocol Value Proposition

The Ripple network replaces the existing inter-bank exchange network with a blockchain– eliminating friction, speeding up transaction and settlement times, and greatly reducing costs. In many ways, this is a perfect use case for blockchain technology. The legacy system is slow, expensive, and error-prone; banks must coordinate transfers of value across different internal databases, making it extremely difficult to settle transactions quickly. Not only is this process slow, it adversely impacts a bank's working capital. Banks often have to open accounts with other foreign banks and fund them with local currency (these are known as nostro accounts). This money sits idle until banks need to make a payment in that currency, creating working capital inefficiencies. Banks that can't afford to fund many nostro accounts, or that need to make a payment in a currency for which they don't have an account, must rely on third-party liquidity providers for that currency. Not only does this subject the banks to counterparty risk, it often requires that their capital be tied up in transit for days at a time.

Ripple allows banks to move from a system of disjointed databases to a single distributed global database, the Ripple ledger. Banks can trade IOUs for any asset with other banks that they trust, and all of the transactions are contained on a shared ledger. This gives transactions a fluidity and speed that can't be achieved in the legacy system, and it greatly frees up working capital for banks. This solves a huge problem for financial institutions.

XRP Utility

Transaction fees must be paid in XRP, and accounts must have a minimum of 20 XRP (about $4 USD at time of publication) in their wallets in order to transact on the network. These mechanisms are designed to prevent network spam. Additionally, transaction fees are burned (they are not paid to validators), making XRP a deflationary currency. Finally, XRP can be used as a "bridge currency" for instant transactions on the Ripple network. In these instances, XRP functions much like any other blockchain-based cryptocurrency. Banks have the option to issue their own IOU-backed assets on the Ripple network, or they can send payments using XRP.

While the Ripple network allows for IOUs to be transacted quickly, globally, and on a single distributed database, these IOUs must be settled periodically with actual monetary transfers. If banks instead send payments using XRP, settlement can happen much more quickly than it does with legacy systems, as long as there is a party on each side of the transaction that is willing to either receive XRP or immediately exchange it for the preferred fiat currency. This is a major caveat, and the fundamental source of our bearishness on XRP.

XRP Risks

Cross-border settlement functionality is not inherent to XRP. Banks could just as easily use Bitcoin, Ether, DASH, or another cryptocurrency for the actual settlements. In the future, banks are most likely to conduct settlements in blockchain-based fiats or whichever cryptocurrency becomes the global reserve. We don't believe that having a currency specifically for inter-bank settlements is a compelling, and is in fact counterproductive because it introduces unnecessary exchange risk. Banks will want to settle IOUs with widely accepted and stable global reserve cryptocurrencies. Ripple Inc. has not presented a plan for XRP to fulfill this mission.

In its current form, Ripple also faces significant centralization risk because of Ripple Inc.'s control of network servers and its ownership of the majority of XRP. Furthermore, multiple researchers have expressed uncertainty over the security of Ripple's native consensus algorithm. These concerns and risks are detailed in our full analysis.

Conclusion

XRP currently has a network value of about $8.5 billion, excluding the 62 billion XRP that are owned by Ripple, Inc. We believe that most of this value is a result of speculation due to major partnership and customer announcements by Ripple, Inc. The company has made major progress on several fronts and continues to sign important partnerships with banks and other financial institutions around the world. We recognize the value in the service that Ripple Inc. is providing, and we believe that inter-bank settlements are one of the best use cases for blockchain technology.

However, it is important to recognize that a good use of blockchain technology does not always justify the value of a chain's native token. In the case of XRP, we believe that the token holds little utility beyond payment of negligible fees, and thus is unlikely to maintain and build value in the long term. While we expect that XRP tokens will continue to see price spikes as Ripple Inc. makes announcements, we don't believe that the fundamentals of the protocol will build sustained value for XRP. An investment in XRP is not an investment in Ripple Inc. The company may do well offering a useful service to banks, but XRP's value is likely limited. For these reasons, we are bearish on XRP at current prices.

News

- Previous
-
- Next

Subscribe For The Best Research And Insights In Crypto

Email address... Subscribe

?

Designed + Built By AMSD

-
-
-

Email Address * Email Address

First Name * First Name

Last Name * Last Name

Error: Please enter a valid email address

Error: Invalid email

Error: Please enter your first name

Error: Please enter your last name

Error: Please enter a username

Error: Please enter a password

Error: Please confirm your password

Error: Password and password confirmation do not match

Download