Manole Capital Management
3rd Annual Financial Services Survey April 2020

MANOLE CAPITAL MANAGEMENT

Introduction:

Manole Capital Management exclusively focuses on the emerging FINTECH industry. Over the last few months, the nine 2020 interns of Manole Capital have conducted our 3rd annual financial services survey. This group is comprised of students from Lehigh University (4), the University of Tampa (3), Indiana University (1) and the University of Florida (1). Like our prior surveys, this research specifically targets the thoughts and insights of America's younger generations and how they view various categories of the financial services industry -banking, brokerage, digital currencies and the payment sector.

Generations:

Baby Boomers are often characterized as optimistic, idealistic, self-driven and have shown a tendency to be loyal to one company (average tenure is 15 years). After years of climbing the corporate ladder, many are now interested in retirement and sharing their legacy. The Gen-X generation tends to be somewhat skeptical, pessimistic, independent and focused on having a solid work / life balance. This group is often described as resourceful, as they attempt to build a portable career. The two youngest generations are Millennials and Gen-Z. Early analysis shows that these younger consumers are less concerned about brands, labels or even corporate names. They tend to be quite entrepreneurial, ethnically diverse, socially tolerant and environmentally aware. These two segments were taught at a young age to collaborate and embrace flexibility (at school, at home and at work). They are idealistic and focused on advancement, with fairness.

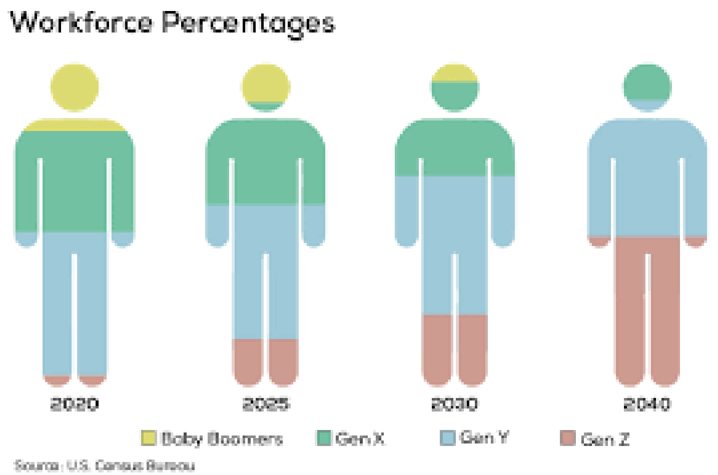
Our Target Audience:

Once again, we targeted Gen-Z (those born after 1995) and Millennials (born between 1980 to 1994) to better understand America's younger generations. In terms of size, Millennials and Gen-Z are both over 20% of the US population. We feel it is important to understand the perspective of these younger individuals, especially since Millennials have surpassed Baby Boomers, as our largest living adult generation (according to the US Census Bureau).

This younger generation, often called the "Internet Generation", doesn't know what life is like without an iPhone or social connectivity. They seek truth, value individual expression and seem to avoid labels. While most of Gen-Z is still in school, a Fast Company survey estimates that this group will account for 40% of all consumers by the end of this year. How will businesses engage, target and attract this group? The three most influential events of their lives are the September 11th terrorist attacks, the Financial Crisis and now this COVID-19 global pandemic. We are attempting to understand how this audience will bank, conduct its payments and invest going forward.

We inquired about four distinct financial services categories and received answers to our series of questions from **247** respondents. Nearly **60%** of our responses were female and **40%** were male. Those that answered our questions come from **28** different US states and attend **33** different colleges / universities. Our target audience was Gen-Z and we successfully hit that mark, as **95%** were between the ages of 18 to 22 years old.

Our Research:



As this chart shows, over the next five to 20 years, the percentage of the US workforce will dramatically shift towards Gen-Z. The questions we asked, as well as the information we received, is summarized below. Where possible, we have attempted to provide our conclusions, takeaways and opinions. While some might be considered controversial, it is simply intended to serve as possible Gen-Z and Millennial perspectives. In addition, since this is our 3rd annual survey, we feel it is interesting to note how certain answers have changed over the last couple of years. Lastly, we have attempted to sprinkle in a few questions pertaining to COVID-19, as this virus was beginning to spread globally, just as our survey had begun.

On Instagram, "influencers" can make millions of dollars for their social influence and popularity. Long before this term became popular, the world has attempted to understand and interpret the thoughts of our younger generations. Young people play a critical role in society, as they create and help shape our future. Older generations may believe these differences are unconventional and progressive, but we believe that understanding different perspectives is critical in adapting to change. By researching the way younger generations think / act, we can provide insight into what the future may hold. We hope you find our research insightful into America's younger generations. We have identified a series of quotes, which has helped to shape our research. We hope you embrace this adaptability and flexibility, as you read our note.

Albert Einstein *"The measure of intelligence is the ability to change."*

George Bernard Shaw *"Those who cannot change their minds cannot change anything."*

Edwards Deming *"It is not necessary to change. Survival is not mandatory."*

Richard Branson *"Every success story is a tale of constant adaption, revision and change."*

Martha Stewart *"The more you adapt, the more interesting you are."*

Before we dive into our survey, we thought it might be helpful to provide a basic working knowledge on our subject matter. Since this new technology and asset class is widely misunderstood, we wanted to weave in some fundamental insights and thoughts on currency versus digital currencies.

What's The Deal With Crypto?

While some digital currencies date back over a decade, they became widely popular in 2017. Over the past couple of years, cryptocurrency (especially Bitcoin) has surged to the forefront of a larger financial debate – Is digital currency a viable currency? Both sides of this argument are equally brash, voicing both support and discreditation. Are digital currencies a legitimate form of currency? Are they a viable store value? Can they be utilized as a medium of exchange for goods and services? Let's start out with a few simple definitions, according to the Webster's dictionary, to help set an elementary framework. OK?

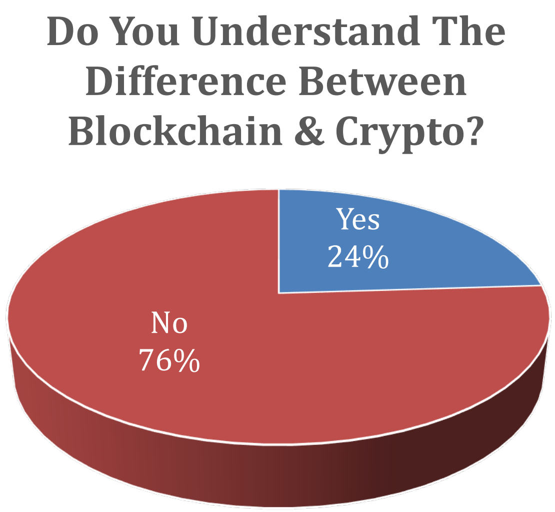
What is Money, Currency, and Digital Currencies?

Webster defines ***money*** as "something generally accepted as a medium of exchange, a measure of value, or a means of payment." It then defines ***currency*** as "circulation as a medium of exchange." Traditionally, governmental agencies create and distribute this currency, as well as back it, in order to ensure that it does not inflate or deteriorate over time. Lastly, ***digital currency*** is "any form of currency that only exists digitally, that usually has no central issuing or regulatory authority but instead uses a decentralized system to record transactions and manage the issuance of new units." Cryptocurrencies substitute computational power and encryption for those traditional governmental guarantees. Crypto creates a currency system which is decentralized and widely accessible, yet extremely unregulated and volatile. Does that simplify everything? Probably not, so let's dive into this a little further…

We believe the simplest way to consider something a viable currency is if can be accomplish two distinct purposes. The first is whether or not the currency can act as a ***medium of exchange***. Can you walk into a store or go online and transact in this currency for the exchange of goods and services? At this point, we do not believe that digital currencies are a viable method to exchange goods. We cannot identify too many retailers or merchants that would accept our digital currencies in exchange for goods and services. While this might change over time, it does not seem to meet rule number one. The second key issue to be considered a viable currency is whether or not it can act as a "***store of value".*** An important aspect of being a store of value is determined by volatility. If an asset is highly volatile, many investors will deem it too unpredictable to be a considered a store of value. For example, one of the most widely accepted store of value items is gold, which use dates back thousands of years.

Now with this introductory knowledge out of the way, let us get into the results of our survey. This is the third year we have performed this digital currency survey, which mostly targeted members of Gen-Z. We've added some new questions for this year, as well as kept questions from past years to see how our audience's perceptions have changed. We will reference our other notes, which can be viewed by searching on Seeking Alpha or by simply clicking here for the 2019 Bitcoin note. We hope you find this intellectually stimulating and that you can maybe learn a thing or two.

Question #1:



Question: Did you understand the difference between cryptocurrencies and blockchain technology?

We wanted to begin our survey with a fairly simple question. We wanted to know if our audience understood the difference between crypto and blockchain. In fact, we found that 76% of those that we surveyed do NOT understand the differences between these two very different concepts. So, it isn't just our parents who don't understand this technology. It is also Gen-Z!

In order to understand the advantages of these digital assets, one must recognize and appreciate their differences. Knowing that blockchain is the infrastructure, technology, and building blocks of many cryptocurrencies is just the beginning. We have heard the terms blockchain and cryptocurrency used somewhat interchangeably, but they are very different matters. Before we proceed to additional questions, we thought it might be helpful to quickly explain the difference between these two topics.

Blockchain vs Crypto:

Quite simply, blockchain is the backbone of cryptocurrency, but its functions can prove useful to many other applications. Blockchain is the engine that allows these currencies to be traded and valued without a central authority. However, blockchain technology by itself is just a way to store data, where each "block" of data holds certain vital information.

This information, or block, contains both its specific transaction details and a reference to the block of information before it. This links all blocks together - into a chain - where changing one block affects the one after it, and so on. This structure of links makes the data virtually unalterable, since changing a single piece of information within the chain requires a change of every block to follow. All of these transactions are listed in a publicly accessible, decentralized ledger where transactions can be independently verified, removing the need for a central authority to control currency use. This technology has enabled cryptocurrency to have the ability to offer a viable alternative to traditional fiat currencies.

Does that make some sense? We hope so…

Cryptocurrencies utilize this secure design to remove the need of a central agency to control the value and distribution of currency. For normal currencies, this is often the job of central banks or a treasury function. With digital currencies, blockchain acts as a ledger, keeping a list of all transactions between users. Without a central agency to control value of the currency, crypto can skyrocket or plummet just like an everyday stock.

Digital currencies use miners to update the ledger in real-time and ensure the properties of the blockchain are verified and permanent. We'll dive into some more details about this process later in the note, but we wanted to try and provide a bit of detail on these two topics. This question shows that Gen-Z still fails to differentiate between blockchain technology and digital currencies, a difference which must be understood in order to fully grasp the workings of cryptocurrency.

Controlling Supply:

By explaining the difference of blockchain and digital currencies we can see clearly how it is vastly different from our traditional forms of currency. The main difference is the lack of a central agency to control the influx of supply into the market. This means the currency is valued based on a simple supply and demand principle, and the value can rise and fall with the market.

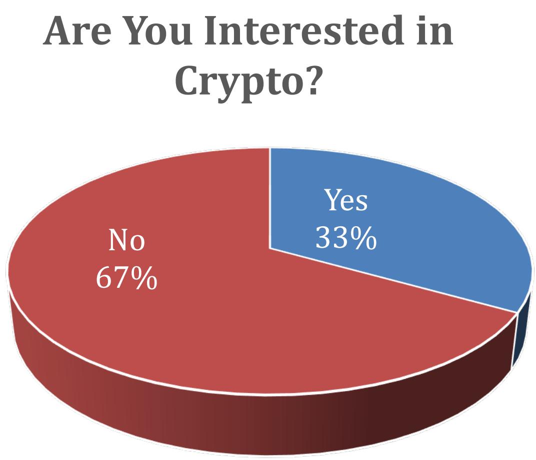
Recall that for every new transaction that occurs, we need a new block to add to our chain of data, which in turn needs to hold a reference to the block that came before it. Remember those miners we mentioned earlier? In the case of Bitcoin, they are responsible for ensuring that the link between each of the blocks is legitimate. This requires a large amount of computational work to fully prove. To reward them, and to provide further incentive, each miner who completes this process is rewarded with a specific number of Bitcoins, which in turn are added to the total currency supply. This reward decreases overtime until becoming zero when the upper limit is reached. We'll save you the messy details on this process, but the number of coins in circulation is currently just shy of 18.5 million, with the upper limit being 21 million.

Question #2:

Question: Are you interested in cryptocurrencies?

Price of one Bitcoin over time. Source: Yahoo! Finance

If 2017 was the first year that cryptocurrencies gained widespread recognition, 2018 was a reality check on that mania. We wanted to ask a simple and upfront question. Are you interested in digital currencies and this emerging asset class? The Gen-Z response was fairly blunt.

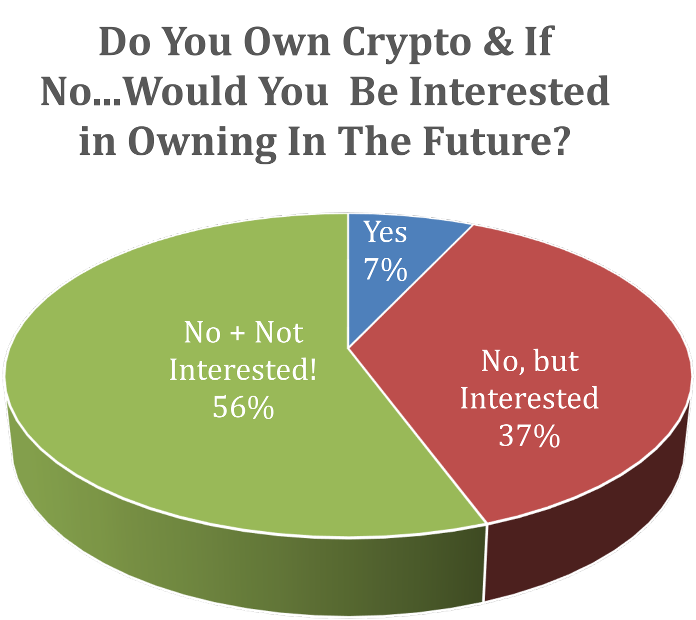


We found that 1/3rd of our respondents were interested, but the vast majority or over 2/3rd's were not. While cryptocurrencies are slowly becoming more prevalent, the sharp price decline in 2018 might have scared off many younger investors. While crypto has its drawbacks, we believe that some of the concern and/or lack of interest can be directly traced to a lack of understanding of the fundamental workings and applications of cryptocurrency.

Was it the more than (70%) decline in 2018 that burned Gen-Z investors? Is it too complicated a technology that worries off this younger generation? Is it the assumption of illicit behavior or illegal transactions that acts as a barrier to wider adoption? These are the questions our research will attempt to frame and better understand.

Question #3:

Question: Does Gen-Z own cryptocurrencies? If not, would they be interested in potentially owning digital currencies in the future?



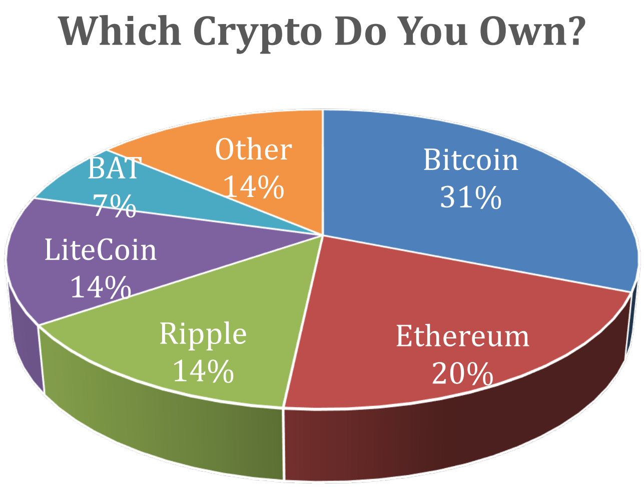
To start, we wanted to better understand if Gen-Z owned cryptocurrency. Only 7% of our survey owns cryptocurrencies. So, an overwhelming percentage of Gen-Z does not currently own digital currencies.

How does that compare to last year's survey? Well, 17% owned digital currencies a year ago, so interest appears to be on the decline. How does that compare to 2018? 12% of our respondents in the inaugural year owned digital cryptocurrencies. This year marked a downward trend after two years of steady ownership growth.

However, we also wanted to see if they were at least interested in owning some in the future. While over half (56%) have no interest in digital currencies and do not plan on owning it in the future, we were intrigued with the 37% that did express some interest. We believe that those that are interested, but not yet invested, might be hesitant for a few reasons. We think it remains challenging to open an account, and it remains difficult to purchase digital currencies. Also, we believe there are challenges to safely storing one's crypto. More on these subjects in a moment…

Question #4: Dominant Cryptocurrencies

Question: If you do own a cryptocurrency, which do you own?



So, the previous question showed that only 7% of our survey even owned cryptocurrencies. We wanted to better understand which cryptocurrencies were the most popular of those that owned them.

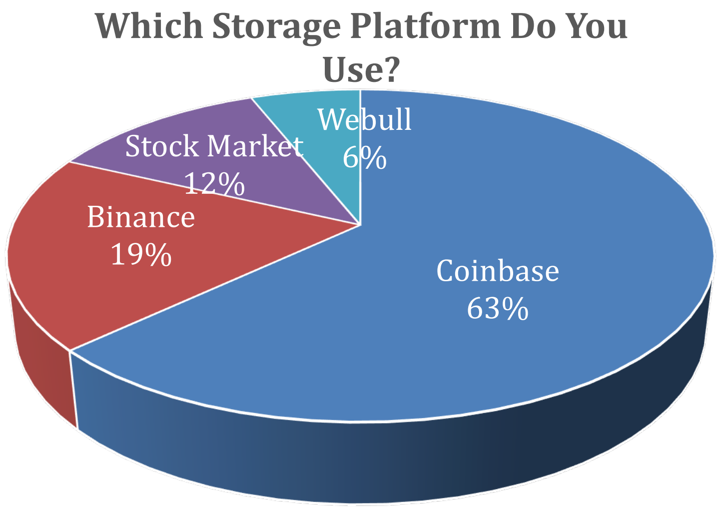
Unsurprisingly, Bitcoin had the largest percent ownership at 31%. The next most popular choice was Ethereum at 21%, followed by LiteCoin and Ripple at 14%. Only a few (7%) owned BAT (Basic Attention Tokens).

In comparison to last year's survey, Bitcoin kept its leading market share at 31%. LiteCoin dropped slightly from last year's result while Ethereum and Ripple stayed approximately the same. We only have data from last year on this metric. The largest difference we noted to last year's results was BAT, which has benefited from its use in the advertising ecosystem. This is done by incentivizing users to watch ads by offering tokens in exchange for their time. The adoption of BAT could be showing a generational shift, in the way users interact with ads. Furthermore, given the increased shift towards an internet-centric society, BAT could be the start of a trend that shows how crypto currencies can in fact be used as a transaction medium.

Question #5: Storage Platform Preference

Question: Which storage platforms were our Gen-Z respondents using?

If you are a crypto owner, tracking and trading your currency can be a very challenging process. Unlike usual securities, most of these currencies require a digital wallet to keep track of transactions. This is because, as odd as it may seem, these digital wallets don't hold any currency. In fact, cryptocurrencies don't physically exist anywhere. Digital wallets allow users to keep a running tab of their personal inflows and outflows of currency, effectively removing the need to store any physical currency. There's an ever-growing number of these services, allowing users access to the ledger and ability to trade. However, the fact that many of these digital wallets are managed by third party companies pose a security risk not present elsewhere.



We found that a large majority (63%) of our respondents used Coinbase to trade and store their digital coins. As the digital currency market continues to evolve, we have seen Coinbase solidify its position as the premier storage and trading platform., up from 44% last year. As Coinbase continues to grow its presence as a digital wallet among the Gen-Z crowd, it will be harder for other platforms to overtake this established market presence.

Right behind Coinbase was Binance at 19%. Last year, Binance had 20% market share, so it seems to be stuck being used by only 1/5th of the Gen-Z population who own crypto. Notable platforms that did not appear to be used by this year's respondents were Kraken, Robinhood, and Bitrex. All of these were selected in prior years, but received no votes this year. We believe that Coinbase's lead might be vulnerable, if a traditional firm with a great brand name enters the arena. While Coinbase has an early lead, the winner has not been crowned (in our opinion).

Webull (6%), and even traditional platforms such as the stock market (12%) offer other alternatives to trading crypto. This may seem impossible since these currencies are traditionally stored in a digital wallet, but investment products are being created which are able to track the price of cryptocurrency, similar to the workings of a commodity backed ETF. These can be traded like any other stock, making cryptocurrency trading more applicable to traditional investors. The most well-known of these vehicles is the Greyscale Bitcoin Trust (Ticker: GBTC), which has become incredibly popular with young investors. In fact, Charles Schwab reported this year that 1.84% of all equity holdings for Millennials are in GBTC, placing it above the traditional blue-chips such as Berkshire-Hathaway, Netflix, Disney, and Microsoft. This proves a shift in the investment interests of millennials, and this trend will likely be mirrored by Gen-Z, possibly even more so, as blockchain technology and cryptocurrencies become more common.

Question #6: Classifications

Question: Does Gen-Z have a grasp of how cryptocurrency should be classified?

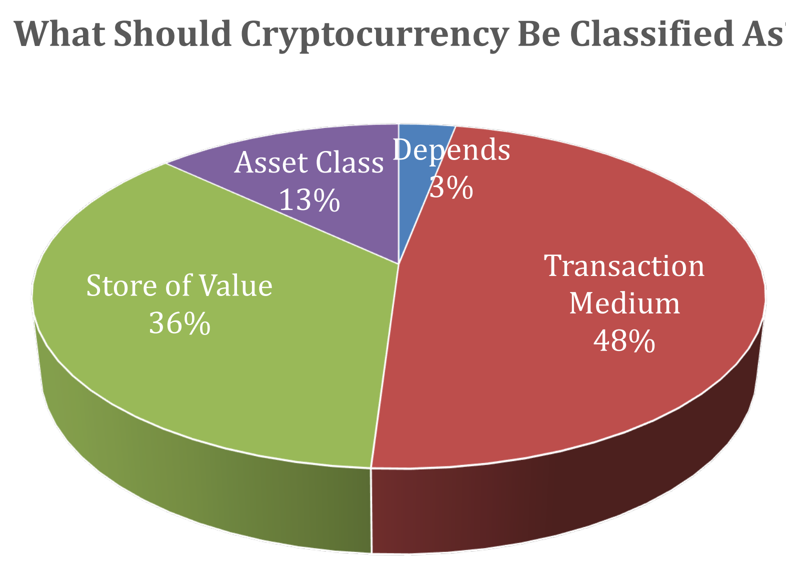
Due to the lack of comparable securities present in the market, finding a way to classify cryptocurrency properly can be a challenging task. In our opinion, three options seem to be the most viable, and we asked our audience if they thought cryptocurrencies should be classified in one of these three ways:

- Store-of-Value: an asset that maintains its value over time without depreciation, gold is commonly referred to as a store of value because the shelf life is perpetual.

- Asset Class: a grouping of comparable financial securities. Each asset class is unique as there is often little correlation between different asset classes and each class represents a different risk and return on investment, often performing differently given certain macro-economic trends.

- Transaction Medium: used to facilitate transactions between two entities. One key identifies is that if a given transaction medium becomes obsolete, then all stores of said medium become obsolete as well.

We found that 48% of our respondents viewed cryptocurrencies as a “transaction medium”. To us, this is interesting and somewhat perplexing. We would avoid classifying cryptocurrency as a transaction medium because there is simply a lack of vendors who accept this as a legitimate form of payment. We were equally surprised with 36% of respondents classifying cryptocurrency as a” store of value”. Due to its extreme volatility, compared to traditional currencies or gold, we personally would not choose this to describe our view of cryptocurrency. Contradicting basic economic theory, a bitcoin today is not necessarily worth more than one a year from now. Recently, cryptocurrencies have been presented (through the news and media) as an “asset class”, but only 13% of our survey agreed. Interesting…

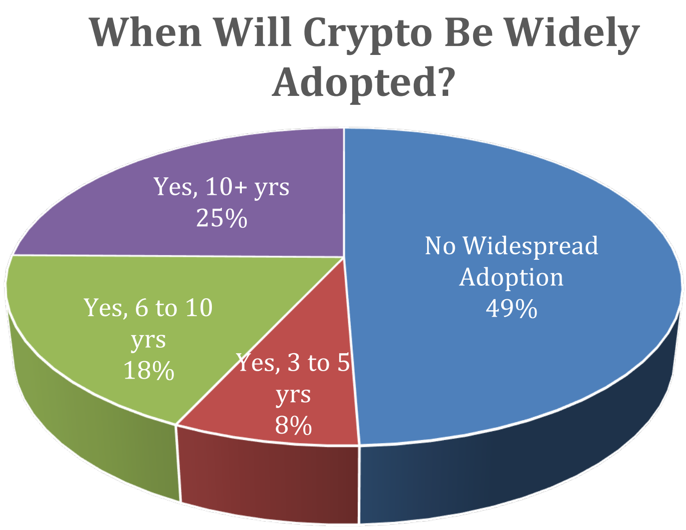


These forms of currency are so volatile and unpredictable that we have to evaluate their purpose on a case by case basis. We see that cryptocurrencies cannot be classified all together, but their purpose can vary for every transaction. This is an interesting question because we see that the results will be always changing due to the market for crypto and what its most popular use is at the time.

The given variability between distinct crypto currencies is one of the main reasons it is not a true transaction medium or asset class. Until there is widespread adoption of cryptocurrencies by merchants and consumers, we believe this will continue to be the case. Bitcoin has been surprisingly resilient, bouncing back to pre-COVID 19 peaks following its crash in the beginning of April. The economic struggles of the COVID pandemic will help demonstrate this cryptocurrency’s potential and whether it has the backing to prevail through slumps in the economy. Is this the occurrence that potentially solidifies Bitcoin’s stance as the premier cryptocurrency?

Question #7: Future Adoption

Question: When will cryptocurrencies become widely adopted for online and in-person transactions? If so, how many years will it take?

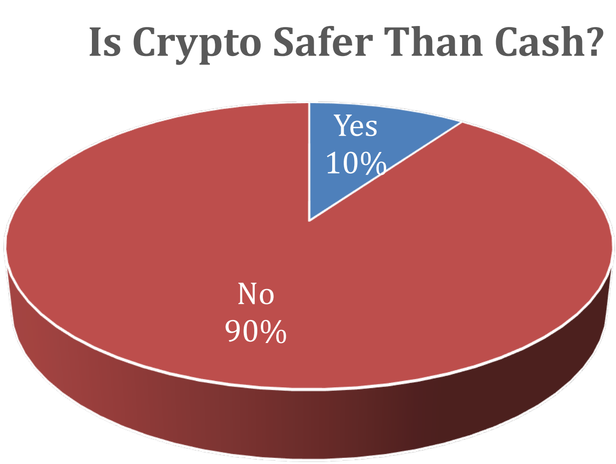


Our survey indicated a near 50-50 split between respondents being optimistic about cryptocurrency being adopted at all. 49% of Gen-Z does not envision cryptocurrency becoming widely used for online or in-person transactions. Of the other half that see crypto eventually going mainstream, it varied on timing. A quarter of our survey expect this shift to take 10+ years, while 18% thought 6 to 10 years and only 8% felt it would occur in the next 3 to 5 years.

Without retailers allowing cryptocurrency transactions, we do not believe it will be able to succeed. Despite its vast potential, many merchants simply do not want to complicate their point of sale. With blockchain advancements, we could foresee better cryptocurrency adoption, but we do not believe it will happen overnight. If crypto adoption is to succeed, we believe a fundamental shift must occur. Digital currencies must be proven to have a “store of value”. Quite simply, it must become less volatile. Once crypto can manage this wild volatility and prove its value, it will have a better chance to succeed.

Question #8: Transaction Security

Question: Would you feel safer making transactions with cryptocurrency instead of cash?

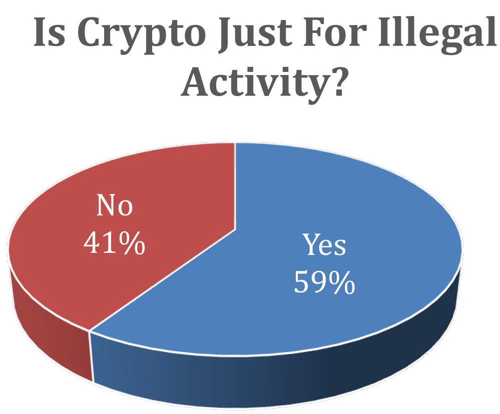


We found the Gen-Z response to our question regarding security interesting. 90% of our respondents feel safer using cash in a transaction than any form of crypto.

We believe some of this response is due to the current flawed digital wallet system and its potential for security breaches and extreme volatility. We wonder if this preference for cash would change, if people saw the CDC study of how many bacteria and viruses can exist on paper US currency. This was the first year this question was asked, so it will be interesting to see if respondents grow more comfortable with crypto overtime.

Question #9: Funding Illicit Activities

Question: Do you associate cryptocurrency with illegal transactions?

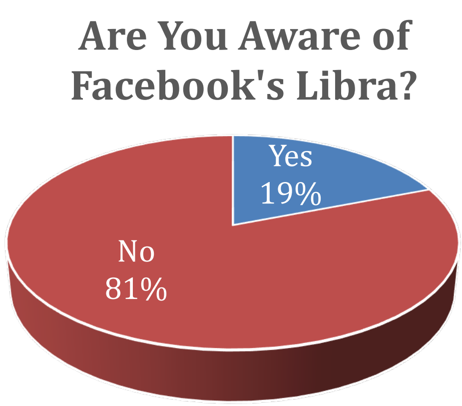


We wanted to understand if Gen-Z had the perception that crypto was usually associated with illegal activities. A majority (59%) of Gen-Z respondents said they associate crypto with illegal transactions. This is the first year this question was asked, so we will begin to track responses over the next few years.

We find this "illegal perception" somewhat unfair. Bitcoin and other cryptocurrencies can be used for illegal transactions, but so too are US dollars, right? Research has found that only 0.2% of all 2019 Ripple transactions were found to be illegal transactions. While this 0.2% equates to $400 million in illegal transactions, it does not show that the majority of transactions are illegal in nature. We know the number of transactions and dollar amount of illegal activity occurring with US dollars and other fiat currencies to be significantly higher. While we understand this poor perception, we believe this opinion might lessen over time.

Question #10: Libra

Question: Are you aware of Facebook's Libra currency proposal?



To our surprise, only 19% of our respondents were aware of Facebook's Libra proposal.

Manole Capital discussed Libra in June of 2019 (click here), with its article titled *"Libra: If Facebook and Bitcoin Had A Baby."* We discussed the flaws with bitcoin and what constitutes a digital currency. We went into detail on Libra, how it works and what we believed Facebook's primary goal was for launching it. Lastly, we highlighted flaws we foresaw with Facebook's goals and the where we believed it would run into trouble / problems.

Quickly after its launch, numerous politicians (from both sides of the aisle) had some harsh comments towards the new FB initiative. Launching Libra while politicians were still dispensing negative commentary towards Facebook for its Cambridge Analytica scandal was fairly gutsy. Many politicians thought this was a terrible time to launch a new technology and they began to throw up some legislative and regulatory speed bumps for Facebook. In our opinion, it seemed like an inopportune and somewhat odd time to launch a digital currency and wallet. Regulators also questioned for-profit entities like Facebook and their desire to create and launch digital currencies. After this unkind reception, Facebook quickly pivoted its strategy towards a product more like PayPal's Venmo.

Libra began with high expectations, but quickly unraveled as some of its early supporters decided to leave. The Libra project began as an ambitious digital payment endeavor, but overtime has been dialed back to appease lawmakers and regulators. Facebook created a new currency called Libra tokens, which were held in Facebook's digital wallet called Calibra, each of which utilize blockchain technology and a decentralized ledger system.

In the case of Facebook's Libra proposal, it is our opinion that the underlying use of Libra as a method to allow global users to transfer funds and pay for goods and services easily and quickly is viable. Whether or not Facebooks Libra proposal takes off will be determined by its users and the general public. The public will need to see a use for Facebook's digital wallet and currency. Ultimately, this decision will be determined by trust. We look forward to seeing its implementation evolve, as one of the first major tech companies to bet on crypto's adoption.

Conclusion:

It is our opinion that digital currencies have struggled to become widely adopted because they fail as a currency. We believe cryptocurrencies are not a stable "store of value" and they are not considered a viable "medium of exchange". Additionally, its reputation as a "currency for criminals" has not helped matters.

As our survey found, Gen-Z is still searching for answers on cryptocurrencies. For more widespread adoption, we believe Gen-Z will have to better understand the differences between blockchain technology and various digital currencies. In addition, more merchants and retailers will need to begin to accept digital currencies at the point of sale. This begets the traditional "chicken and egg" dilemma. Why would merchants spend the money to begin to accept crypto payments, if none of their customers want to transact in digital currencies? Why would consumers look to buy up crypto, if no merchants accept it as a medium of exchange? This is a vicious cycle that does not seem to be getting resolved.

We believe that our survey found that Gen-Z does not view digital currencies as a practical method to conduct trade. Once these obstacles are removed, digital currencies might be more readily accepted. Regulations might ease and banks might begin to accept these currencies as a legitimate form of payment. However, we do not believe this will occur in the short-term (say 5 to 10 years).

Crypto has a marketing problem and it will need to be viewed in a more positive light, in order to gain traction and succeed. As of today, whether or not it is a fair statement, it seems that digital currencies are the "go to" currency for illegal activity. This only feeds crypto's pre-existing negative perception. In movies or shows, digital currency is the preferred illegal way to transact, without those pesky regulations or banking rules. So, why would anyone want to use cryptocurrency given this inherent risk? First and foremost, there is the possibility of realizing large gains when investing in cryptocurrency before a large rally. This potential revenue draws in investors who do not hold the currency as a means of transaction, but rather as an asset to be eventually liquidated. Additionally, it can be appealing due to low or no fees, growing accessibility and the difficulty in tracing transactions. However, widespread adoption should be slow especially if younger generations (i.e. Gen-Z) are unwilling to fully embrace digital currencies.

Hearing happens when one is able to recognize a sound, while ***listening*** happens when one puts in the effort to understand what it means. We believe it requires focus and a commitment to encountering the experience and intent behind the words. We hope our survey and its findings helped to expose you to some new ideas, maybe even something you were possibly avoiding. Thanks!

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