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RESEARCH BRIEFING: Bitcoin’s Core Narratives – The Evolution:

Executive Summary:

Bitcoin’s core narratives have evolved significantly since inception. This research piece will focus on the key narratives which catalysed the rapid growth that BTC has seen, on both a practical and speculative level. Starting with Genesis, readers will gain an understanding of why Satoshi launched BTC; in response to central failures by both governments and central banks, as well as understanding how BTC could provide a solution to some of these problems. Furthermore, this piece will break down 3 core narratives which underpinned demand for BTC as an asset.

Firstly, BTC’s central role as a reserve currency in the crypto markets, albeit a role which has diminished over time due to the rise of stablecoins. Secondly, some insight into BTC’s role as a P2P monetary system which enabled instantly verifiable, digital transactions to facilitate trustless exchanges of value, as well as the various forms of utility this provides to global markets. Finally, BTC’s role as a censorship-resistant inflation hedge is explained, with consideration about its value compared to another scarce asset such as gold.

Importantly, this piece will also consider BTC’s current use case in light of the current Ukraine-Russia conflict and in what forms BTC has been used to protect regular people on both sides of the conflict. The conflict is likely to exacerbate the fundamental use case behind BTC, showing how useful a censorship-resistant inflation hedge and peer-to-peer monetary network can be in tumultuous times such as these.

The Genesis Block:

Before delving into some of the key narratives that surround Bitcoin presently, it is worth considering how these narratives have evolved since Bitcoin’s inception. When Satoshi launched the Genesis Block in 2009, he made sure to include a special message.

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Figure 1: Bitcoin’s Genesis Block

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The message, as shown in *Figure 1* above derives a headline from the London Times on 3rd January 2009 which stated, “Chancellor on brink of second bailout for banks.” This important quote highlights one of the key reasons why Bitcoin was created in the first place. People mistrusted the banks due to their role in the Financial Crisis in 2008. Satoshi’s response was to create an inclusive, peer-to-peer monetary network, which was governed by decentralisation, shifting power away from centralised entities who could misuse their authority at the expense of ordinary citizens towards a trustless system. This mistrust extended to Central Banks as well, with Satoshi making it clear that the debasement of fiat currency is to be expected because of their actions. In other words, Satoshi believed that people did not have sovereignty over their finances due to overarching interference and creating the Bitcoin Network was a way of solving this.

Through BTC’s creation, people would retain full sovereignty over their assets without the need for a bank, requiring only a PC with an internet connection. Satoshi’s absence has ultimately driven BTC to sustain its high level of decentralisation, with narratives becoming malleable by design as there is no central driving figure to determine what that narrative might be. Ultimately, these narratives are applied by the market depending on what use case suits BTC best at any given time. The aim of this piece is to break down some of the key narratives attributed to BTC throughout its history to gain a better understanding of the fluidity of the market and the versatility of BTC as an asset.

1) Reserve Currency for Crypto Markets:

Before delving into the more theoretical applications of BTC’s use case and the discussions surrounding those, it is important to highlight BTC’s role within crypto and its relationship with Altcoins. Altcoins are defined as any cryptocurrency that is not BTC and first rose to prominence in 2013. Altcoins were mainly set up to rival BTC’s dominance as the E-money currency, for example Litecoin or Peercoin. Given the significant upside BTC saw throughout the year, many investors looked to riskier and more speculative investments in the market.

In the early stages (2013-2017), BTC acted as the dominant base asset in the crypto ecosystem because it was the proven market leader and had the most liquidity on offer to trade against. At the time, stablecoins were underdeveloped and therefore BTC was seen as the ‘safest’ asset within crypto. BTC’s position as a reserve asset also filtered through to the naming of ‘Altcoins,’ essentially separating every other coin with BTC itself. This normalised the view that all Altcoins should be compared to (and priced in) BTC which also helped legitimise BTC’s classification as a digital currency because it was used as crypto’s unit of account.

In 2017, the market had matured, and derivatives arrived on the scene. Bitmex famously introduced the Perpetual Swap Contract, which required BTC as collateral but allowed users to trade with leverage up to 100x. This innovation contributed to BTC’s position as the reserve asset and revolutionised how derivatives are traded. However, as the market was becoming more sophisticated, infrastructural developments were taking place.

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As infrastructure improved, stablecoins became more visible on exchanges and added a new dimension to crypto trading. Only trading BTC pairs meant constant market exposure, whereas stablecoins allowed traders to ‘go flat’ without having to exit the ecosystem using on/off-ramps which were costly and time-consuming. USDT-denominated pairs were less complicated, could act as a total hedge against the crypto market and were better suited for derivatives trading. As the space developed, traders would begin to utilise derivatives in much larger volumes, allowing for stablecoin trading dominance to rise as a result. *Figure 2* shows the “Tetherisation” of the crypto market following the macro top in Bitcoin in January 2018.

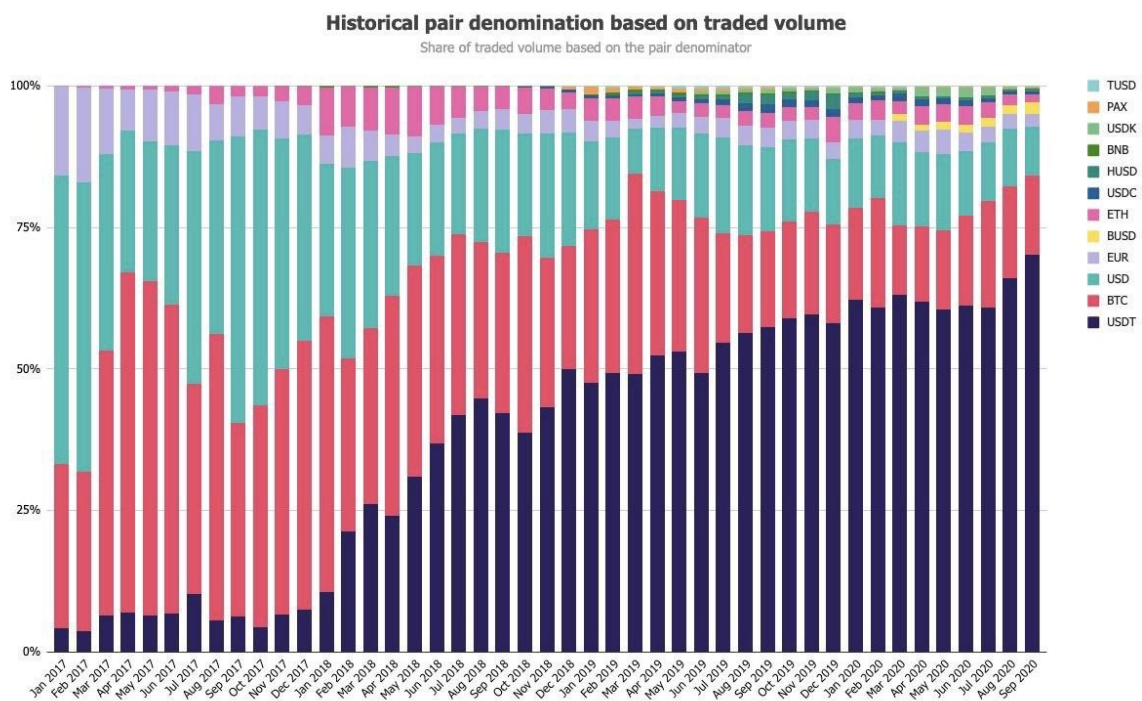


Figure 2: Crypto Pair Denomination by Volume – The Block Crypto

The evidence clearly shows BTC being utilised less as the denominator in Altcoin pairs in favour of stablecoins. However, some would argue this is a natural progression as BTC’s narrative shifted from being a peer-to-peer payment system, facilitating trades in digital markets, towards becoming a Censorship-Resistant Safe Haven and taking on the narrative of Gold 2.0. As there is less incentive now to spend BTC over USD on speculative trades, its role as the reserve asset would naturally decrease over time.

2) Peer-to-Peer (P2P) Payment System – Decentralised PayPal?

Bitcoin’s earliest narrative (2009-2017) revolved around its use as a cheap peer-to-peer (P2P) payments network. Most people viewed it solely as a medium of exchange. As Bitcoin was so

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immature, its volatility profile was even larger than it is today. Many sceptics believed that due to its immense volatility it could not succeed as a currency. However, Bitcoin gained popularity (and notoriety) for its use as the currency of the dark web. People could finally spend money digitally without the need for a financial intermediary. This was the first scalable use case for Bitcoin, with the Silk Road dark web marketplace trading around 10 million BTC during its existence (2011-2013). During this period, BTC clearly succeeded as a P2P payment system for microtransactions, given the main characteristics required for success centred around digital convenience and low transaction fees, of which both were seen in BTC's case. Although BTC was used to purchase illicit goods digitally, it provided an early case study and perspective into why BTC could succeed as a digital monetary network.

In January 2013, BitPay announced 10,000 Bitcoin merchant transactions took place within the month. This may not seem significant, but it represented progress by merchants to willingly accept BTC whilst still in its infancy. However, by February 2015, over 100,000 retailers worldwide accepted BTC payments. Companies such as Microsoft, Dell, Wikipedia, Twitch, Expedia and PayPal led the way and legitimised BTC's role as a form of digital currency. This rapid mobilisation by merchants to consider accepting BTC as a form of payment dominated the narrative throughout these years, with much of the speculation concerning which company would be next.

In 2017, SegWit was launched. It fixed a bug known as transaction malleability, but more importantly it created the rails to allow integration with the "Lightning Network." The Lightning Network is a Layer 2 scaling solution and would allow unlimited and cheap transactions to take place off-chain, further addressing the scalability issues that BTC faced as its adoption increased exponentially. Currently, the Lightning Network is one of the most important infrastructural developments within Bitcoin and has made a real impact in El Salvador, where BTC is now legal tender. The premise behind BTC becoming legal tender centres around the success of BTC as a P2P payment network.

The El Salvador announcement in September 2021 catalysed the growth of the Lightning Network as shown in *Figure 3* below. BTC's role as legal tender requires a scaling solution such as Lightning Network in order to meet the economic demands of potential nations. Other countries in South America have expressed a favourable view on this topic. Therefore, the outcome of the El Salvador experiment is likely to have far-reaching consequences. Having the infrastructural rails to support global adoption is vital if BTC is ever going to achieve a global role as a unit of account, so continued growth of channels in the Lightning Network is expected over time. This supports the view that although the dominant narrative may have changed when informing some BTC investment theses, the use case for e-money is only going to improve as infrastructure such as the Lightning Network becomes adopted.

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Bitcoin: Lightning Network Number of Channels



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Figure 3: Bitcoin: Lightning Network Number of Channels – Glassnode

Although there has been a shift in the dominant narrative away from P2P and towards a safe haven, in many countries around the world there is a desperate need for an efficient P2P system. For example, the World Economic Forum states over 57% of the African population remains unbanked. Therefore, the majority of people living on the continent are unable to save money efficiently, as well as engage with credit, insurance, and other services. The World Bank states some of the key reasons why the population remains unbanked includes the cost, travel distance and amount of paperwork involved in opening an account. In BTC's case, barriers to entry are significantly lower. All that is needed is a mobile phone with data or a PC with an internet connection. Setting up a BTC wallet is usually free.

Through BTC, the unbanked will benefit from; lower transaction costs for international payments such as remittances, fast and secure payment processing through the security of the blockchain and the ability to save and store wealth in an appreciating asset against fiat currencies. However, despite these benefits, some banks and governments in Africa have restricted access to crypto products. In a truly decentralised manner, people have turned to non-custodial P2P platforms to exchange BTC instead. Figure 4 below shows no other continent uses P2P platforms at a higher rate than Africa, with a significant portion of this being BTC. This suggests that citizens like to transact using BTC in a P2P fashion and have valued doing so at a higher rate than any other continent.

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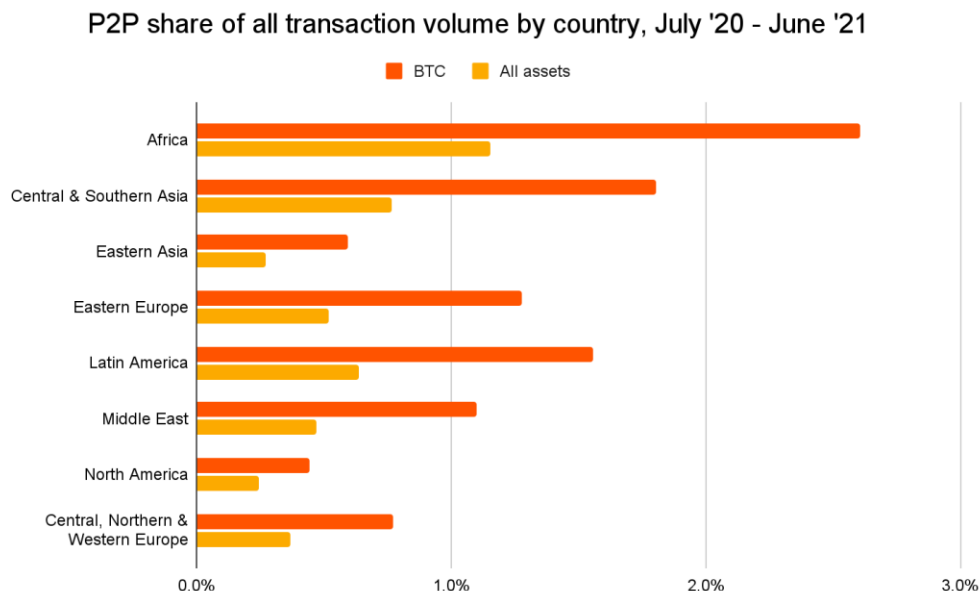


Figure 4: P2P Share of Transaction Volume by Country, July 2020 – June 2021 – Chainalysis

3) Censorship-Resistant Safe Haven – Gold 2.0?

Although for most of its life BTC has been considered best suited to act as a form of e-money, it still possessed an economic design that by nature is disinflationary and would cause a seismic shift in its utility. Bitcoin’s programmatically determined supply of 21 million BTC means users do not need to trust the system, all they need to do is verify the source code. Having a pre-determined supply schedule makes Bitcoin amongst the “hardest” forms of money to exist. This is because even if demand for BTC increases exponentially, the supply schedule will not be altered in any way regardless of how many additional resources are expended. *Figure 5* references BTC’s Total Circulating Supply. It shows the supply curve decelerating in line with the way in which BTC mining rewards are halved approximately every 4 years. Taking a supply-side viewpoint, the expectation is that BTC’s price should in theory continue to appreciate against fiat currencies over the long-term provided demand remains.

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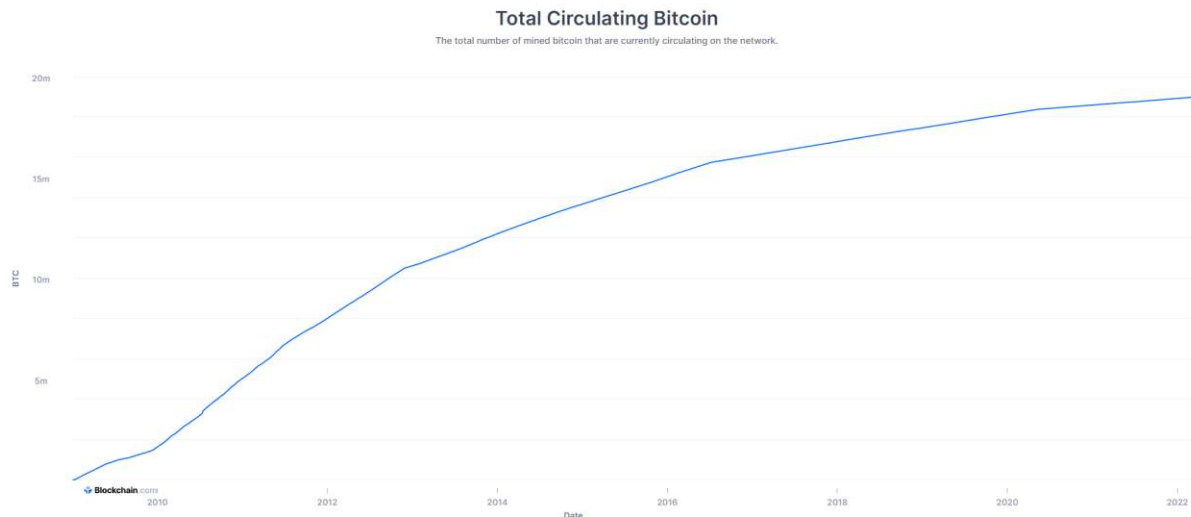


Figure 5: Total Circulating Supply of Bitcoin – Blockchain.com

BTC is even “harder” money than a precious metal like gold. Although gold is a scarce asset, miners can still accelerate their production through new technologies if it was profitable to do so. This is not possible for Bitcoin, where rewards are constrained according to the code. In comparison to gold, BTC is digital and is therefore more portable. It can be transacted digitally and verified instantaneously. Custody of BTC takes place in a cold wallet of which only the owner has access. Contrastingly, custody of gold and subsequent movements of it will likely require third party involvement given its physical nature. Therefore, some believe BTC can be referred to as “gold with wings” or “Gold 2.0”, given that it takes many of the benefits offered by gold and supposedly improves upon it. One such use case for both assets is acting as a safe haven store of value.

The creation of fiat money allowed Central Banks to have total control over monetary policy via the Money Supply. The rate at which they print is not constrained by a piece of code, it is at the sole discretion of the institution. Therefore, BTC’s role as a safe haven asset is to protect users from the debasement of fiat currencies over a long period of time. As Central Banks have proliferated a credit expansion through fractional reserve policies, the consequence of this has been endemic inflation and a reduction in the purchasing power of fiat money over time. This is typically exacerbated in developing economies, but more recently has become the main talking point for the U.S. Economy, which is facing record levels of inflation.

Throughout BTC’s history, it has increased its purchasing power significantly against currencies such as the U.S. Dollar. *Figure 6* below plots BTC-USD against M2 Money Supply. This chart indicates the ratio between both assets when changes in supply are removed. In other words, the chart displays the purchasing power of BTC vs. USD. By definition, an inflation hedge is an investment which protects purchasing power in the face of rising inflation.

As shown, BTC has demonstrated a clear ability to act as a hedge against inflation due to its ability to increase purchasing power over long time horizons against the USD. As central banks and

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governments fail to control inflation, BTC’s disinflationary design should in theory continue to support its purchasing power expansion and combat the debasement of fiat currencies.



Figure 6: BTC/USD Plotted Against M2 Money Supply (BTC-USD/WM2NS) (Logarithmic Scale) – PSG Cryptonomics

In contrast to BTC’s exceptional performance since inception, gold has only managed to retain the same level of purchasing power that it held in 2008. In theory, it has succeeded in its goal as an inflation hedge as it has protected wealth for buyers of Gold then. However, since gold’s last high in purchasing power in 2011, it has lost around 55% of that as shown in Figure 7 below. One might argue the excessive inflation experienced over the last 5 years should have led to stronger purchasing power for gold, rather than being a flat hedge. However, BTC’s introduction as a gold 2.0 may have seized a portion of demand that would have otherwise flowed into gold. The flows of demand will be vital to watch as the demand for safe havens is likely to continue due to the macroeconomic and geopolitical issues which are dominating headlines.

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Figure 7: Gold/USD Plotted against M2 Money Supply (Gold-USD/WM2NS) (Logarithmic Scale) – PSG Cryptonomics

Interestingly, the sound money principles of BTC conflicts with its previous use as a P2P payment system. This is because people would prefer to save assets that are likely to increase in value whilst spending assets that are either stable or decreasing in value. In 2018, “forks” of BTC such as Bitcoin Cash (BCH) were created to amend the BTC source code and make alterations which would improve the scalability of BTC through increased block sizes and lower fees, but decrease the security of the network. However, the market decided that these changes were unnecessary and reflected continued support for BTC’s current form. The failure of BTC forks suggests that the market believes the current design of Bitcoin is optimal, valuing the security of the network above its ability to increase throughput on the native chain. Other scaling solutions via Layer 2 would emerge, therefore allowing scalability whilst retaining the original properties of BTC.

Although inflation is a hot topic with reference to BTC, the censorship-resistant design is also key. No single entity controls who can transact within the Bitcoin network. Therefore, it cannot be altered to suit a political agenda and is open to all. Given that there are many historical instances of governments constraining the financial sovereignty of its people, it does make sense to hedge against this possibility and protect excess wealth through other instruments which are censorship resistant. Drawing on Canada’s decision to invoke the Emergencies Act as a way of constraining financial activity by trucker protesters in Ottawa, it is clear that governments can and will implement legislation which constraints financial independence for political reasons. BTC is a way to ensure citizens are protected against potential tyranny.

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Ukraine-Russia Conflict – Bitcoin’s Impact:

When the geopolitical climate reaches extreme points as we are currently seeing, Bitcoin’s use case is exacerbated. As a P2P monetary network, we have seen BTC act as an incredibly efficient use of distributing aid to Ukrainians where other methods have been costly or impeded by a significant delay. The Ukrainian Foreign Minister specifically announced wallet addresses for donations to be made. Transactions to those addresses are instant and do not require any financial intermediaries. Donations are guaranteed to reach the intended recipient in full without suffering the administrative costs that are typically associated with charity and international payments.

Moreover, sites like Patreon were being used to raise funds but these efforts were shut down due to conflicts with their terms of service. In one example, over £300,000 of raised funds were withheld because of a terms violation, which spurred the organiser to create NFTs instead, raising over £6m as a result. The immutable and censorship-resistant nature of BTC allows anyone to effectively contribute in a cheap and convenient way. Given the emergency laws that were introduced in Ukraine, citizens saw ATM withdrawals capped and international bank transfers banned. BTC provided them a way of transacting globally and ensured monetary flow into and out of the country.

In Russia, citizens have been punished for the actions of their government and as a result have seen their wealth deteriorate in terms of purchasing power. The crash of the Ruble has provided yet another use case for why citizens should look to protect their financial sovereignty. BTC mainly benefits those with smaller balances. Large accounts are likely to be under significant scrutiny by centralised exchanges and banks processing fiat withdrawals from crypto given the level of sanctions that are being applied to Russia. However, for the average citizen, BTC provides a safe haven against the tyranny of the Kremlin which allows them to protect their wealth. In practice we have seen this play out. Ruble-denominated crypto volumes increased dramatically since the invasion was announced. This suggests Russians believe in the various use cases that BTC can provide in times of extreme uncertainty and government overreach.

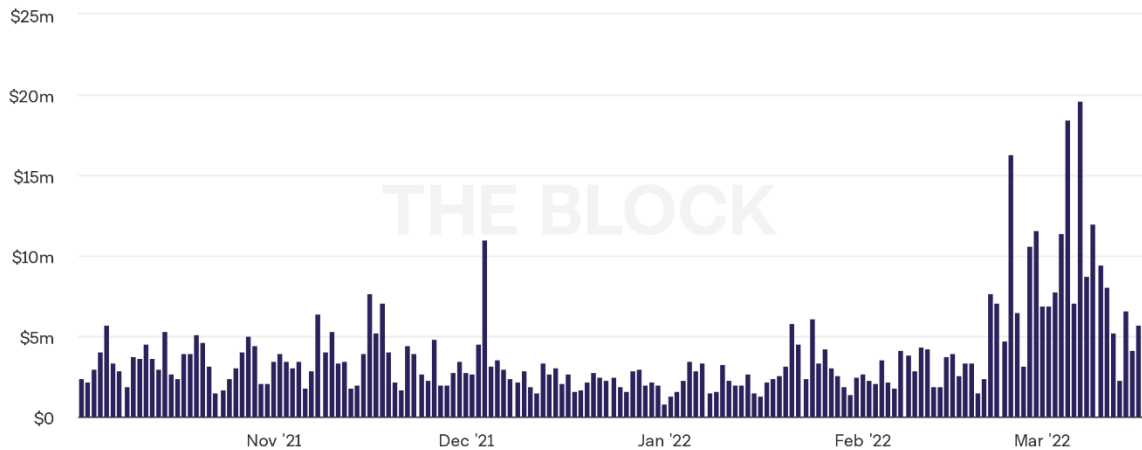
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Total Daily Ruble Volume for BTC/RUB Pairs



SOURCE: KAIKO
 UPDATED: MAR 17, 2022

Figure 8: Total Daily Ruble Volume for BTC/RUB Pairs – Kaiko via The Block Crypto

Globally, there is a large amount of economic uncertainty. Inflation concerns due to supply-side pressures, spiralling debt and geopolitical conflicts disrupting economic flows would all cause investors to flock towards ‘risk-off’ safe havens such as gold. *Figure 9* below shows the performance of 4 core investments since Ukraine was invaded officially on 24th February (as at Daily Open); Bitcoin (BTCH2022), Gold (GCJ2022), S&P500 (ESM2022) and Nasdaq (NQM2022). In theory, gold’s fundamentals have improved relative to other stores of value such as bonds and USD whose desirability as a safe haven have decreased dramatically. Bonds in a low yield environment have a higher opportunity cost, whilst USD is losing its power as a store of value. However as shown by *Figure 5* the market has dictated that BTC is much more desirable than gold since the start of the invasion. The expectation should be that gold outperforms BTC, but clearly this has not been the case. Investors have priced BTC above Gold as a store of value since the invasion. The performance comparison between gold and BTC during these tumultuous times is vital to understand whether BTC has indeed confirmed its position as the leading safe haven asset in the market currently.

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Figure 9: BTC +7.48% (Red) vs S&P E-mini Futures +3.21% (Green) vs Nasdaq E-mini Futures +3.12% (Blue) vs Gold Futures Continuous +1.52% (Orange) – Performance since invasion announcement 24/02/22 – PSG Cryptonomics

Concluding Thoughts

The fluidity of BTC as an asset demonstrates its resilience and versatility to effectively tackle global issues relating to financial sovereignty. The dominant narrative may be what forms investment theses and leads to consensus about how best to use BTC within a defined context. However, it is important to note that BTC can still fulfil all the use cases that have been considered in this piece. As BTC does not have a central authoritative figure driving the narrative it is up to the people to decide where BTC’s use case best suits them. This malleability is by design and is there to allow BTC to mould itself into solutions for a diverse range of problems.

We should expect the use case of BTC to evolve going forward as infrastructure continues to improve and scaling solutions such as the Lightning Network offers a stronger experience transacting with BTC. As the world continues to display macroeconomic and geopolitical uncertainty, BTC has an opportunity to shine by offering practical solutions to the problems everyday people are facing as a result of their governments and the economy. Furthermore, as El Salvador has opened the floodgates for nation states to consider using BTC as a mechanism to protect the wealth of citizens and raise additional investment, it could prove to be an excellent case study portraying BTC’s success as a currency on a national level. The shifts in narrative have been organic and decided by the broader market. BTC’s utility will ultimately ebb and flow depending on where it is needed most.

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What is clear, is that it is becoming more widely accepted and adopted globally. As the world’s technological and digital capabilities continue to grow, the assimilation of BTC into everyday life is likely to accelerate. Younger generations are already comfortable with complex technologies and are very open to the utility that BTC and other cryptocurrencies can provide. Its digital properties are hugely beneficial compared to the analogue shortcomings of gold. Its convenience is likely to rival international payment systems such as bank transfers or businesses such as TransferWise.

Figure 10 below considers user adoption of the internet against crypto. The chart shows crypto adoption is comparable to the swift adoption of the internet in the 1990s. During this time period, the internet hit an inflection point whereby adoption rates grew parabolically, and at a rate faster than any other advanced technology. In a similar sense, crypto adoption looks to be approaching a comparable inflection point with the possibility that adoption rates surpass that of the internet given the current growth trajectory. As the network effects that come into play result in crypto hyper-adoption, we should expect growth in the networks to be reflected through sustained price appreciation over a long-time horizon. This idea is especially seen in BTC’s case, given that it has a significant range of utility to offer users which has only become more entrenched by the current political and economic climate.

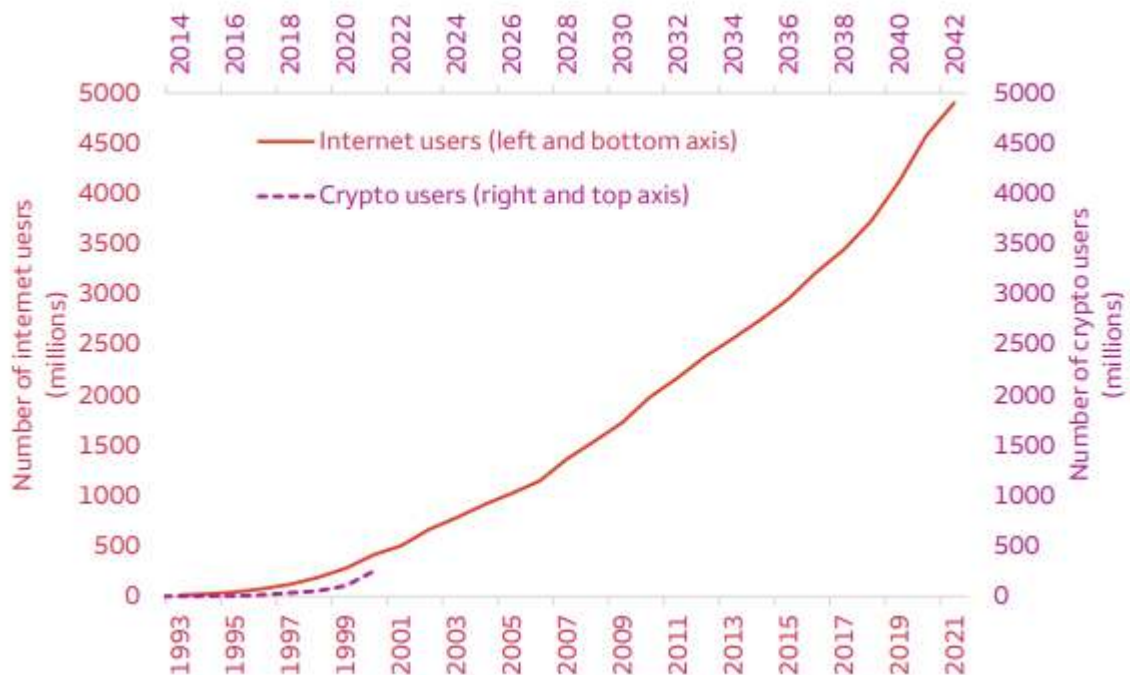


Figure 10: Crypto Users Vs Internet Users – Wells Fargo Investment Institute

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