

Bitcoin and Blockchain: Embracing the Opportunities, Anticipating the Threats

Transcript

Jenna Dagenhart:

Hello and welcome to Asset TV. Today we're talking to Weitz Investment Management director of equity research. Barton Hooper. Barton, thanks for joining us.

Barton Hooper:

Thanks Jenna, it's great to be back on the Asset TV platform once again.

Jenna:

Yeah, well, great to have you back, and I want to ask you a few questions regarding cryptocurrency, an area that's been exploding in interest recently. For investors, it may seem like you can't read or watch any industry news without hearing about Bitcoin, Ethereum or Dogecoin, and the trend is manifesting with financial advisors. A recent bitwise survey found that 81% of all advisors reported receiving questions from clients on crypto. Barton, what do you think long-term investors should be considering as they sift through all of these headlines and noise?

Barton:

Well, Jenna, I certainly agree with you. It doesn't seem like you can go more than a second before reading another news story or seeing a headline on Twitter, a TikTok even that talks about the greatness of cryptocurrencies. And then you see the volatility - one day the price is up 10%. Next day it's down 5%. And you're right, it could be Bitcoin, it could be ether, it could be ADA, or Doge.

But here at Weitz, what we're really focused on is the underlying technology of these cryptocurrencies, which is called blockchain. Really, what's fascinating about blockchain is that it's the integration of several different disciplines - economics, game theory, computer science, cryptography, and behavioral psychology. So, maybe we should take a step back and say "well, what exactly is the blockchain?" The blockchain is - the technology itself is a decentralized ledger, and that's just a fancy word for a secure, decentralized open-source database. What does that mean for you and I? Well, think about just a piece of information, whether that's your personal data, information about a transaction, or information about a piece of equipment. And that information, if it chooses, can be shared globally in a highly secure, fast, and cheap manner. And that opens up all sorts of implications for the global economy. But really what we've seen lately and what we see in the headlines, is the fact that cryptocurrencies are building out infrastructure, and that interest - that underlying blockchain infrastructure is manifesting itself in the form of these various cryptocurrencies.

But there's real-world implications to the blockchain itself, and you can see that, for instance, in healthcare. Eventually we could see our healthcare records, our personal data, put on a blockchain in a highly secure manner, and that would solve one of the vexing problems that we see in healthcare which is getting information about a patient into the hands of the correct doctors. When that happens, you'll be able to have more individualized care in a higher-quality and cheaper man.

Another area that's sort of exciting is - think about your favorite musician or a blogger or someone that you follow on Twitter - and what's called the creator economy. In music, for instance, what you could see is publishing rights or streaming rights and even things such as tickets to events all be put on the blockchain. And what this would allow is the musicians to earn a higher share of the income created from their music and let them get closer to their fans. So, there's many implications of blockchain, but I want to emphasize it's still very early, and so there are protocols and standards which are still emerging. There's hard problems which need to be solved, so we don't know who the winners are going to be just yet, but our research process is focused on following these developments.

Jenna:

At Weitz you describe your investing process as Quality at a Discount. Where does a potential market disruptor like blockchain fit into this approach?

Barton:

Sure, well, we think we have a great framework for analyzing blockchain's potential impact on our investment universe and portfolio companies. We look at quality and businesses across six different vectors, competitive positioning, capital efficiency, reinvestment runway, cash flow consistency, management quality, and financial leverage.

Jenna:

And I know people can check out those six vectors at AssetTV.com or your website as well with Weitz, but let's talk a little bit more about these disruptors.

Barton:

Certainly, and I think it would help if we just focus on the first three elements, which we think is where blockchain might have the most impact. So, think about something like competitive positioning. What's that going to do to an industry structure? How is it going to affect the pricing power of a business as well as the cost framework in which it operates? And then on the second element, let's look at capital efficiency. Will the same amount of capital deliver the same amount of returns if a business is using blockchain or is threatened by it? And then on the reinvestment runway, how many paths are opened up to invest incremental capital at high rates of return that blockchain would enable, or alternatively, as a threat, are there paths that a business once thought promising that are now blocked because blockchain itself has created an environment where those returns won't be as good as they once were. And then another element in all of this is thinking about the future, and no investment process, of course, can predict the future, but from our standpoint we believe the Weitz research framework helps in that because we can evaluate certain paths that a business can go down and identify businesses that can respond to those and be adaptive and flexible so that when a path becomes clear, and let's say in this case the implications of blockchain are more well known, how those businesses will have the time and the resources to respond accordingly to both opportunities and threats. And where this all adds up for Weitz is in our portfolios which you find are high-conviction, concentrated, competitively advantage businesses that are responding to secular tailwinds and, ultimately, we believe those are great portfolios that will work out well for investors.

Jenna:

Well, I won't ask you to predict the future, Barton, but I do want to drill down even further. Could you share some specific areas of your research coverage that you believe can be influenced by blockchain?

Barton:

Bitcoin was initially thought of as a payment network, and that hasn't really manifested itself yet, but let's look at two companies that are payment networks, Visa and MasterCard, which are in our portfolios. Right now, they're actually taking advantage of blockchain in several ways. For instance, Visa is building a business-to-business payments network based on blockchain, and business-to-business payments are really in the Dark Ages when you think about it, lots of transactions done by checks. So blockchain has the ability to completely digitize the business-to-business payments chain, make it cheaper, and that'll save businesses tens of billions of dollars.

MasterCard is doing something along similar lines, but one product that they have in partnership with a couple of crypto exchanges is an actual credit card that pays rewards in Bitcoin, as well as allowing customers to use Bitcoin to pay for items, and what's happening underneath is these transactions are running on the Mastercard network, but MasterCard is handling the exchange from Bitcoin to U.S. dollars or Euros or what have you. So, both Visa and MasterCard are really providing on-ramps and off-ramps to cryptocurrency right now, and we think that's exciting.

Another example would be outside of payments is Honeywell, which is another Weitz portfolio company. And they're experimenting with using blockchain in their aerospace business. Now, what they're doing with that is providing a way for their suppliers to track each part individually from the time it's manufactured to the time it's put on a plane, so that will allow for, first of all, cheaper inventory management, but second of all, provide assurance to flyers everywhere that the part that went on the plane was actually supposed to be there.

And then a third example is in banking. We have a company called FIS which is working with their banking software customers to help them put - allow their depositors to purchase and sell Bitcoin and ether and other cryptocurrencies so that they will see it in their bank statements right along their normal deposits.

So, lots of exciting things around that for our companies, but I would also say - it's really early. As I mentioned earlier most of these technologies that you see using blockchain or products that are taking advantage of it are what we would call proof of concept more than they are full blown products and opportunities. But we think in the future you'll see more of those come about. So, we're excited.

Jenna:

Yeah, it's interesting, Barton, you know when people think of, say, Honeywell. They might not think of blockchain right away.

Barton:

Exactly.

Jenna:

Well, finally to consider that blockchain and digital assets could be the most transformative innovation since the rise of the internet is both fascinating and profound. Barton, how do you and the rest of the

Weitz investment team track the potential opportunities and threats as well of blockchain that it could create?

Barton:

Yeah Jenna, it's really a fascinating topic, and I think it helps to take a step back. And let's look at a new technology, the internet in the 1990s. And certainly if you were working in broadcast journalism or newspaper or the music industry or, say, at a department store, you felt the pain of the disruption of the internet. But I believe people too often focus on what was destroyed versus what was created, because the internet created far more value for companies and for the world as a whole than it destroyed. I mean, think about what we're doing right now. This would have never been imagined in 1996 that you could get on a video remotely and speak with one another about a fascinating topic like blockchain, which itself was really enabled by the internet. So, we are actually, here at Weitz, cheering for the uber optimists in crypto to be correct, because we think our investment process is adaptable to something like this that allows us to identify, say, the next Google, Facebook, or Salesforce that comes out of this explosion of technology that blockchain is enabling. So, I would say we're really excited about the future and can't wait to see what comes next.

Jenna:

Well, Barton, thank you so much for joining us today. Great to have you.

Barton:

Alright, thanks. Thanks for having us.

Jenna:

And thank you so much for watching. That was Weitz Investment Management's director of equity research Barton Hooper. And I'm Jenna Dagenhart with Asset TV

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Alphabet Inc. (GOOG) 2.2%, 0.0%, 5.9%, 6.7%, 7.0%
Facebook Inc. 0.0%, 0.0%, 4.9%, 3.6%, 4.9%
Fidelity National Information Services Inc. (FIS) 1.5%, 0.0%, 2.7%, 0.0%, 3.4f%
Honeywell International Inc. (HON) 1.2%, 0.0%, 0.0%, 0.0%, 0.0%
Salesforce.com Inc. 0.0%, 0.0%, 0.0%, 0.0%, 2.9%
Visa Inc. (V) 1.6%, 0.0%, 5.0%, 4.0 %, 4.0%
Mastercard, Inc. (MA) 1.6%, 0.0%, 4.6%, 3.4%, 3.7%

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