Digital Asset Income & Growth Fund (DAIG)

Yearly Review 2020

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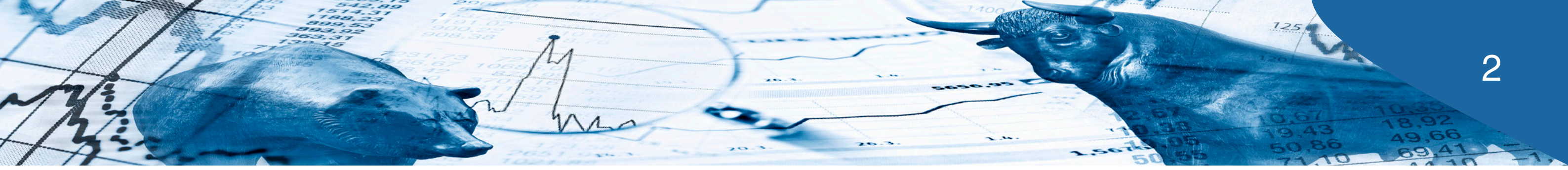
St. Gotthard
Fund Management



Market Review

2020 was a year of big expectations for digital assets. In anticipation of major systemic events such as the Bitcoin halvening and the launch of Ethereum 2, investors in the asset class were finally hoping to see a light at the end of the tunnel following two years of a dire crypto winter. In the end, 2020 did not disappoint, however the road to redemption was far from a smooth one. The markets started the year well with Bitcoin managing to breach the psychologically important $10,000 level and Ethereum doubling over the course of the first month and a half. The gains were however short lived as in early March global investors finally started to realize that the pandemic will be a major fundamental shock for the global economy and markets. A sharp sell-off ensued with Bitcoin briefly going to levels below $4,000 to register a bottom for the year around mid-March. It seemed at that time that luck would once again evade the crypto bulls as the global economy was flung into turmoil and would drag the digital asset market down with it. However, it would prove to be a great and maybe last opportunity to enter the space at such deflated price levels. As politicians with the help of central bankers globally enacted a policy of printing money to support the struggling economies the traditional markets started to recover quickly, surprisingly avoiding a double dip and taking digital assets along with them.

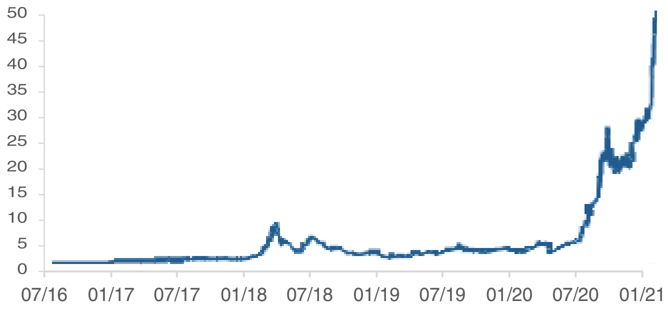
BITCOIN IN USD

Source: Bloomberg

By the time of the halvening in May Bitcoin was advancing on the $10,000 mark once again. The next four months would see relatively range bound trading in an around these levels for most large cap digital assets. There was however an unexpected craze that took the space by storm – Decentralized Finance and "Yield Farming". While DeFi has long been touted as one of the more promising themes in digital assets, few will admit to anticipating the events that took place over the summer. As demand in the hunt for yield grew exponentially with limited supply DeFi tokens grew in price by hundreds and in some cases thousands of percentage points over the course of a couple of weeks. As is often the case, the space got more crowded the rewards declined and by September many assets in question had corrected significantly.

The last quarter of 2020 proved to be pivotal for crypto markets. Since mid-summer we had been witnessing rising interest for digital assets from institutional and corporate players. Key events to highlight were PayPal announcing and launching a crypto offering and MacroStrategy moving part of its treasury into Bitcoin. In Q4 institutional adoption started to materialize at a whirl-wind pace with new fund managers and banks coming out in support of a digital asset allocation on a weekly basis. The old narrative of Bitcoin being a poor medium of payment, something that had been frequently highlighted by representatives of the old economy, was quickly forgotten and a new narrative, namely that of Bitcoin being an alternative to gold in terms of asset allocation, took centre stage. All these factors contributed to a frantic year-end. For most active in the space, the big marker of success was taking the $20,000 level for BTC before year-end and holding it. However, we witnessed this level brushed aside with ease as the BTC price galloped further to finish the year in the $28-29,000 range. Returning circa 400% since the start of the year and 700% since its March lows led to Bitcoin cementing its position as one of the best performing assets in 2020. Those who for a long time believed that the halvening event in May would forever change the dynamics of the digital assets market as a result were richly rewarded.

DEFI MARKET CAPITALIZATION IN BILLION USD



Source: Coingecko

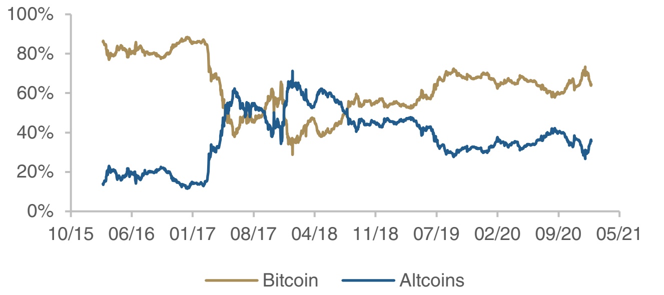
Strategy Review

With the launch of the fund in the last few days of May we initially adopted a cautious approach. We wanted to closely monitor Bitcoin as the leading asset in the space and how its price action would develop following the halvening. On top of this, our firm-wide macroeconomic view at the time was also cautious. Going into the summer, typically a period of lower trading volumes and 2008 fresh in our memory we still at that stage could not rule out a double dip scenario. We therefore decided to monitor the market and use any potential dips as opportunistic entry points. Having said that, some assets in the portfolio that were going to act as the core yield generators were purchased right away and put to work. Another key aspect that we had to keep in mind when making allocations was our operational structure. Designed to significantly lower counterparty risk, the downside at times was that certain actions/trades took longer than anticipated.

The first three months were spent by us in this mode. One development worth highlighting over the period was our more than anticipated deployment of options strategies on Bitcoin to both initiate new positions as well as generate passive income on our existing holdings.

Having verified the soundness of our operational setup and put to bed fears of a further dip in traditional markets in September we held our first Investment Committee (IC) since the launch of the fund. Strategically the key decisions approved were initiation of positions in both Ethereum and Polkadot, closure of our NEXO position and ramp up of capital allocations going into year-end as the fund was still 35% in cash. The basis behind position initiation in Ethereum was the anticipated launch of ETH 2 before year end and the alluring opportunities available in the ETH options space. With volatility higher than that of the BTC options the opportunity for yield generation was too tempting. In terms of Polkadot we favoured it as the main Layer 1 blockchain competitor to ETH with higher adoption relative to other blockchains. NEXO was the only security token in our portfolio to date however having paid a dividend in August the IC felt that funds could be put to better use elsewhere and eventually decided to reallocate these funds to increase our exposure to Cardano.

SHARE OF TOTAL MARKET CAPITALIZATION

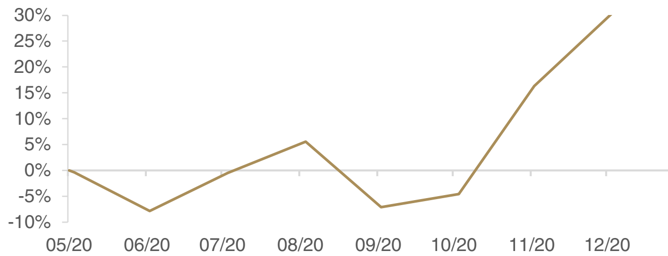


Source: Coin.dance

October was the month that Bitcoin's move really started to gain traction, closing the month at a year high of circa $13,500. In classic crypto market nature this move temporarily drained the liquidity out of other areas of the market as alternative assets were left lagging behind leading to a month of muted performance for the fund. Due to risk management concentration limits in place our fund BTC exposure is capped at 25%. As a result, we were punished for this in both October and November as Bitcoin rallied. Longer-term however we continue to see our core strengths as stringent risk management and fundamental valuation capability and thus our belief in the importance of portfolio diversification was not undermined by these short-term developments. An event worth highlighting was our participation in Ethereum history by contributing a small part of our holdings for staking on the new generation Ethereum 2 network.

By the time of the final IC meeting for the year in December the fund held less than 20% in cash. Having witnessed the influx of institutional money into the space throughout the year, a strategic decision was made to introduce a new core strategy dedicated to the DeFi theme. We did not feel comfortable adding it to the portfolio during the summer hype but felt that at this stage an allocation was justified. It would be replacing the security token core strategy we previously had in our mandate. The logic behind the decision was that DeFi is easier for traditional financiers to understand relative to some more technical themes and after a hollowing out of the bull run in BTC, DeFi may be the next logical theme these investors would feel comfortable making an allocation to. The latest two DeFi projects that were approved by our IC either already offer a fee-based income for token holders or have tokens backed by assets in their corporate treasury. Thanks to these parameters, more traditional methods of valuation can be employed, making these projects a more attractive investment, in our view.

PERFORMANCE SINCE INCEPTION



In summary 2020 was a challenging but good year for the fund. We believe that we have achieved proof-of-concept as one of the only euro-denominated and income-distributing funds in the space. The fund finished the year up 30% in absolute terms and in January our first dividend distribution will be complete. This will result in an annualized yield of 5.7% In euro terms for our existing LPs. The value of this dividend was 40% derived from our on-chain income generating activities (staking/masternodes) and 60% from our option writing strategies on both BTC and ETH. Having been underinvested over our first few operational months, we are confident the yield of our fund will increase over the next six months.

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