

Coinbase Global, Inc.
First Quarter 2021 Earnings Call
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Anil Gupta, Vice President, Investor Relations

Thank you. Good afternoon, and welcome to the Coinbase first quarter 2021 earnings call. Joining me on today's call are Brian Armstrong, Co-Founder and CEO, and Alesia Haas, CFO. I hope you've all had the opportunity to read our shareholder letter which was published on our Investor Relations website earlier today.

Before we get started, I'd like to remind you that, during today's call, we may make forward-looking statements. Actual results may vary materially from today's statements, information concerning risks, uncertainties and other factors that could cause results to differ from these forward-looking statements is included in our SEC filings and shareholder letter available on our IR website at investor.coinbase.com. Our discussion today will include references to adjusted EBITDA, a non-GAAP financial measure. We believe that certain non-GAAP measures of financial results provide useful information to management and investors, regarding trends relating to our financial condition and results of operations. Non-GAAP financial measures should be considered in addition to, not as a substitute for, or in isolation from GAAP measures. You can find additional disclosures regarding adjusted EBITDA, including a reconciliation to net income, the comparable GAAP measure, in our shareholder letter and current report on Form 8-K, which are posted on our IR website. Last week, we announced that we will use Say Technologies to enable all Coinbase shareholders the opportunity to submit and upload questions for our management team. Thank you to everyone who participated in this process. We will start today's call by answering some of the most upvoted questions. We will also take live questions from Wall Street analysts, many of whom have done significant amounts of work to understand our business, which we are very appreciative of.

So with that, let's dive into the first question. Jordi Y. asks, when will users be able to trade Doge?

Brian Armstrong, CEO: All right. I'll take that one. Thank you for the question Jordi. And asset addition is something that's near and dear to my heart. There's more and more assets being created in the crypto economy. I think it's going to be something, kind of, like apps in the App Store or on the iPhone where there's eventually millions of these assets created over time and so we're putting a lot of work and thought into how do we accelerate our pace of asset addition, and one of those is Doge, as you mentioned, which has been getting a lot of attention recently. So, to answer your question directly, we plan to list Doge in the next six to eight weeks. And then more broadly, we're going to be focused on how we can accelerate asset addition in the future.

Anil Gupta: Our next question comes from Garrett H., who asks, as volatility increases with the crypto market, can we expect to see a continuous profit and revenue growth, as with the most recent quarter. In addition, can we look forward to additional ventures to cover the potential fee-less future of crypto trading?

Alesia Haas, CFO: Thanks, Anil. I'll take this one. Garrett, thanks, this is a great question and there's a lot to unpack here. I want to start by saying that we do not believe in a fee-less future of crypto trading. At least in the near term. That said, we are definitely focused on building new products and services and to diversify our revenue streams. Many of these new revenue streams are reported as subscription and services revenue, which generated \$56 million of revenue in the first quarter. Our goal is to become the primary financial account in the crypto economy for our users and to achieve that goal, we're focused on introducing our customers to new products, services, adding new assets, as Brian just mentioned. Over time, we believe, all of this will drive diversification of our revenue.

But going back to the first part of your question as to whether we can expect to see continuous profit and revenue growth when volatility increases. I think it's really important to understand, crypto volatility and crypto asset prices can and have fluctuated meaningfully quarter-to-quarter. And historically, when we're in periods where we see a high bitcoin price and higher crypto asset price volatility, those two factors have driven to higher trading volume and therefore higher transaction fee revenue periods for Coinbase. However, those are not assured. We could see periods of increased stability or decrease. In our shareholder letter, we included an outlook for Q2, along with full year 2021 outlook. Quarter-to-date for the second quarter, we have seen a continuance of the strong crypto price cycle with high levels of volatility, both retail and institutional. We expect total Trading Volume to meet or exceed the Q1 levels if our performance continues at the current pace. And we have seen growth in MTUs since the end of Q1, driven by the continued strength in the crypto market. To remember, to close, I think it's important to remind you all that our revenue and growth can be volatile and we could see periods of growth, we can see periods of stability, and we could see a decline in our revenue.

Anil Gupta: Our next question comes from Allan L, who asks, as crypto becomes more mainstream, how does Coinbase view competition with decentralized exchanges?

Brian Armstrong: Yes, I'll take that one. So we are very excited about decentralized exchanges, I think this is a really important innovation in the cryptoeconomy, and it's a great example of the kinds of services out there that our customers want to use, even if it happens to be somewhat competitive with one of the products that Coinbase offers, which is a centralized exchange. So I think in the future, there's going to be centralized exchanges, and also decentralized exchanges. We need to make the full breadth of those products available to our customers. I'm not a fan of trying to force people to use something just because it happens to be our product, we need to give our customers access to everything they want to use in the cryptoeconomy. And they can do that today through our self custody wallet, Coinbase wallet. They can also – they can access decentralized exchanges directly through that product. We also have something called a smart order router that our institutional customers use, which can basically route orders to whatever exchange has best pricing and so in the future, you may see us integrate that into our retail product as well, where every order that comes through, it can be routed behind the scenes. The customer doesn't even really need to know, is it going to a centralized exchange, a decentralized exchange, something run by Coinbase, something out there in the world, as long as they're getting the best pricing, they probably don't really care, and that's a feature that we hope to offer in the future.

Anil Gupta: So we have several other top questions that have similar themes, so we'll combine them here. One from Shunri G., one from Li L., John B. and Tim G - they asked about longer term product strategy, a potential new DeFi service offering, an update on staking and thoughts on introducing an NFT marketplace?

Brian Armstrong: Yes, so again, I'm happy to jump in here. So, there's a ton of innovation happening in the cryptoeconomy, this is great, so we heard a lot of examples here with DeFi and NFT's. There's a lot of third-party applications -- some people call them dapps or decentralized apps, DeFi is another name for that and kind of like I said in the previous answer, we want to make all of these things available to our customers, and just make them easy to use and trusted. And so, we're going to do that in a number of different ways. Again, Coinbase wallet is an example of our subcustody app, where you can – people are already using a number of these things. And we hope to integrate that kind of functionality further into the main Coinbase app as well. In a perfect world, people will be able to just tap and open one of these third-party applications and it'll already have their wallet connected, because of course, our strategy is to be that primary financial account in the cryptoeconomy and in the future, maybe even their identity and everything is already connected when they just open one of these third-party applications. So, I think that's going to be a really important part of how the

crypto economy grows. In terms of staking, since there was a question about that as well, this has been going really well. We actually crossed a million customers using our staking products in Q1 and it's become a nice source of revenue for us.

Anil Gupta: Our next question comes from Yashasvi A, who asks, what is Coinbase's strategy to deal with other exchanges with cheaper fees, apart from pricing, what are the levers can you pull to attract more customers?

Alesia Haas: Why don't I take that one? So, just to be clear, our biggest focus right now is to keep up with the current demand. We are not focused on competing with fees, we're not trying to even win on fees, we're trying to win on being the most trusted, easiest to use, on providing all the assets that our customers want to transact with, on being able to provide a yield on crypto assets, the opportunity to engage in defi as Brian just talked about. Our customers choose us because they trust us to keep their assets safe. We provide an easy to use platform and a growing number of ways to transact and use crypto assets. Our institutions are choosing us for our secure storage as well offered by our custody solution, the deep liquidity we offer on our exchange, and our best trading execution where we are able to route orders across more than 10 liquidity venues, including other exchanges to find the best price to execute client orders.

On the retail side, we're bundling custody and storage services into our trading fee and our customers really see value in the fees that we provide, based on the services. Crypto is so dynamic and is expanding and evolving every single week, which is to say, this is not a commodity service, and therefore, fees are not the sole basis that customers select who they engage with. In Q1, we saw our MTUs use grow up to 6.1 million, up over 200% compared to Q4 2020. So, while the crypto economy exploded, more and more users are choosing Coinbase and our services to access the crypto economy.

Anil Gupta: We have another question from Allan L, who asks, what is Coinbase's stance on government regulation over crypto currency? Are there any long term risks associated with this to Coinbase's core business model?

Brian Armstrong: Yes, so our stance on regulation is that we have always decided to embrace regulation and we've always assumed that for this industry to reach a billion people using the crypto economy which is what we want to do, it's going to have to be a regulated industry. And from the earliest days of Coinbase, we actually proactively reached out to regulators and sought to be an educational resource for them to teach them about crypto and tried to be thoughtful and proactive in our steps and doing a reasonable thing even if it wasn't necessarily required yet in the law. So, we're going to continue to follow that strategy. In fact, this week I was actually in DC meeting with a number of policymakers in the United States and we do that in a variety of countries around the world where we operate and our goal is really to continue to help educate and create clear regulatory frameworks where the entire crypto economy, not just Coinbase, can thrive, because we need lots of startups and businesses to be built in this space. So, we generally see a lot of value in regulation we can -- we see it as a business enabler. We see it as an important long-term strategy.

The question also asked about, are there any long-term risks associated with this. I mean I think the risk is that, basically, it causes us to move more slowly, it takes time to operate in that environment. There are certain occasions where there's products that our competitors might offer that we don't feel comfortable offering because of the feedback that we're getting from regulators. And so the risk is it's really around speed of execution, but I think the right approach is to not try and cut any corners, it's to try to work with regulators to create a trusted environment and help the industry grow in that framework.

Anil Gupta: Our next question comes from Samir G. who asks, what is your plan for international growth, which countries outside the U.S. are you most bullish on?

Alesia Haas: Thanks for the question Samir. International growth is a top priority and we are bullish on the global market overall. And while I say that, we are moving more slowly than we would like. We would always like to move faster in our approach to growth in the international markets. However, this is a multi-step, multi-quarter and sometimes multi-year process, and just like Brian just shared, it's because we take a regulated approach, and sometimes taking the regulated approach means that it is a little bit slower than we would like. We need to seek licenses to operate in these new countries. We seek new bank partnerships so that we can offer fiat to crypto rails, and those things take time to obtain.

There's actually no single country outside the U.S. that we are most bullish on as our goal is to create economic freedom for all and that has no borders. We do have some current initiatives and process in Asia to begin expanding our offerings in that region, but we are looking globally and hope to be expanding as much as we can in all international markets.

Anil Gupta: Our next question comes from Adam P., who asks, as cryptocurrency becomes more institutionally accepted and used by the banking industry, how will Coinbase respond? Will there be more of a push to work with these institutions rather than individuals?

Brian Armstrong: So we don't think of it as institutions rather than individuals, actually both of our those customer segments are equally important to us, both retail and institutional, and I think for -- there's a lot of fiat money in the world, both in institutions and with retail individuals, and so we need both of them to be served equally to get the cryptoeconomy really off the ground and to have a billion people using it. Now, in terms of banks starting to work with cryptocurrency, I think there's actually an opportunity here for Coinbase to help and by that I mean, there's a lot of really difficult technology problems that we've had to solve in terms of how we integrate with dozens of blockchains, how we store cryptocurrency securely in a geographically distributed way, which is very difficult, how we do compliance on blockchains and do blockchain analytics and transaction monitoring in a way that meets our compliance obligations. And so what I think we can do is start to expose some of these solutions that we've built that other companies can build upon, and we're doing that through a product called Coinbase Cloud. You can imagine it is kind of like our AWS for crypto where we're starting to offer more APIs and services like this that other banks and really any other kind of company can use to integrate with the blockchain. So I think that'll be a big opportunity for us over time.

Anil Gupta: Ed M. and Nathanael C. both asked this question, what parameters are used to qualify various coins or tokens to add to your selection and why aren't there more choices? Additionally, how quickly can you process add debut issue coins as new coin prices can escalate quickly such that other exchanges get a new listing advantage?

Brain Armstrong: Yeah, this is a great question, similar to the first one about Doge in a way where I mentioned that I think there's going to be millions of different crypto assets out there, especially as we see new assets being created for new companies being created and there's even NFT's and individuals who are tokenizing their time and so in a world where there's going to be millions and millions of these crypto assets out there, we get this question a lot, how are you deciding, which ones to add, and how can you accelerate it? So, today, we use a number of factors, we look at cybersecurity around the coin to make sure that there's not going to be an issue that would cause customer loss. We also look at it from a legal point of view and a compliance point of view. There's various concerns out there about securities, for instance, and we've worked with things like the Crypto Rating Council to help create clear regulatory frameworks for this.

So these are all things that we look at, but there's no doubt that we need to accelerate the process by which we review assets and we add them to the site, because we're quickly going to be in a world here where there's so many that we're not going to be able to keep up, unless we accelerate that process. The last thing I'll just mention -- well, sorry, the question also asked about debut coins, we sometimes call those day one listings. I think these are really important. In the past, we would sort of say, is this coin, has it reached some substantial scale, and then we would add it. But I think what we're going to have to do in the future is actually be first to list the number of these coins. And that's going to be really important to our business.

The last thing I'll say is, we did launch a product called Coinbase Asset Hub. And the goal of this is to really help asset issuers out there to get more clarity about the process of how to get listed on Coinbase. So, any asset issuers can go there, submit a request, and we'll hopefully get more real time feedback from our team about making their way through that process and so we can demystify it, accelerate it and we've had hundreds of asset issuers submit through there and there's a backlog of assets that we need to get through.

Anil Gupta: Our next question comes from Ryan D., who asks, I've seen significant Coinbase advertising as of late. What efforts are being put into user base growth? What is the anticipated growth for this year? And does Coinbase expect this growth trajectory to remain constant in the coming years?

Alesia Haas: Thanks, Ryan. I'm glad that you've seen our advertising. So, historically, we spent less than 5% of revenue on sales and marketing, if you look at our financial results for 2019 and 2020. As we shared in our outlook, we're planning to make significant investments to increase our spend here, up to 12% to 15% of our net revenue. And we're beginning to see some early signs these investments are having traction, as evidenced by our update in our shareholder letter that our Q2 quarter-to-date MTU trends have been increasing from our Q1 levels. And also, what we've seen in Q2 is over two weeks our app has been at the top 10 free apps on iOS and Android. So we are seeing these efforts into our sales and marketing paying off.

As we've shared earlier, we don't provide specific outlook on the growth, we provide scenarios about what the potential growth of our MTUs could be. And the other thing I would just note on your question at this point, expect this growth trajectory to remain constant in the coming years. Coinbase has shared with you historically, there's a lot of volatility in our revenue, as our revenue is influenced by trading volume on our platform, which in turn really reflects the overall cryptoeconomy conditions, price of Bitcoin, crypto asset price volatility, the number of coins that are out in the market. And so, consistency is not a feature of our platform, we do expect volatility, but we do think we can grow over long term and over priced cycles in MTUs and the engagement of users on our platform.

Anil Gupta: Great, so Erica we'll turn it over to questions from the analysts.

Operator: Your first question comes from the line of Lisa Ellis with MoffettNathanson.

Lisa Ellis: Hey, good afternoon. Thanks for taking my question and for doing this call. Great content already covered. I wanted to ask a follow up on the question about how, I guess, partnering potentially with some of the traditional digital wallets and retail brokerages that are beginning to offer crypto investing to their consumers? Are you finding, you're engaging with these players like more as competitors or more as partners, I mean you called out in the shareholder letter that you're seeing interest in like white label versions I guess, it's sort of a Coinbase inside type of model, kind of what's your overall strategy, as we're seeing this like pretty rapid ramp of crypto capabilities at traditional brokerages? Thank you.

Brian Armstrong: Yeah, so I'll take a crack at it and Alesia, feel free to jump in. I think that, as I mentioned previously on the call. There are a lot of really hard technology problems that we had to solve in building Coinbase, and it's probably not, necessarily clear from the outside what some of those are. I think integrating with these blockchains turns out to be really difficult there, you need to be constantly in sync with them, they're upgrading, they're having various issues, where you need to have alerts and sync with the way we store cryptocurrency turned out to be an incredibly hard problem from a cyber security point of view and we've gotten a number of intellectual property, things in place and a ton of infrastructure.

So what we're seeing is that as a variety of companies out there begin to integrate crypto, whether they're brokerages or other fintechs or just regular companies, it could be anything at this point, or startups. They are often reaching out to us to say, hey, how can we build on top of this platform that you've built. I don't think that's going to necessarily be true with every company out there, some of them will try to build it in-house, some of them will try to use others in the space but we are seeing inbound interest and the strategy is essentially to productize the services that we've built in what we call Coinbase Cloud. And that's something that we're investing in actively and have, you know, a sales team around and things like that. Alesia, anything you want to add?

Alesia Haas: No, I think that's right I think that we're optimistic that we can help get a billion users into crypto and part by being B2C, where we help get our own customers our problem but also in being B2B, where we can help other existing financial institutions offer crypto to their customers and hope that this creates a very vibrant crypto economy.

Brian Armstrong: Yeah I mean, just add to that, it's like some of those other companies may even be competitive with Coinbase, right and we're okay with that. We want the entire crypto economy to grow. We think that, if other fintechs are offering some of these things but it's powered by Coinbase, that's great. It's bringing more and more people into the crypto economy and so, at this stage, it's a lot of – it's a little bit like we're just trying to grow the size of the pie, kind of like, in the early days of the internet, you know, Google wanted there to be more websites out there, so we need the whole crypto economy to grow and offering those services can help.

Kyle Voigt, KBW: Hi, good evening. Maybe just one on the retail transaction fee rate in the quarter, it came in closer of 120 basis points versus where you were at last year at around 140 basis points. Was that driven by Coinbase Pro users hitting higher volume tiers or was it simply a mix of volume shifted towards the Coinbase Pro users versus the Coinbase.com users and then can you just also, if it was driven by that volume mix, just wondering whether you're seeing any migration of customers from Coinbase to Coinbase Pro, or was it just about those existing Coinbase Pro users simply trading much more. Thank you.

Alesia Haas: Thanks Kyle, I'll address that question. You're absolutely, right. What we saw in Q1, given the heightened volumes, we saw higher volumes amongst the Coinbase Pro users. And just for others listening on the call, within our retail suite, we have some of our customers using the Coinbase consumer app and some using the Coinbase Pro app, and the Coinbase Pro app offers tiered pricing based on volume. So, the more volume trades, the fee is at a lower rate. And so as those Pro users increase their volume, their weighted average fee rate came down. We did not see any material movement between the two products between the consumer app and the Pro app and so it really was just additional volume coming on the Pro app that drove lower fees in Q1.

Kenneth Hill, Loop Capital: Great. Hey good afternoon everyone. I wanted to go back to that question on geographic outlook for Coinbase. Alesia, I think you said you're moving a little more slowly in other regions as

given you're taking a more regulated approach. I was hoping you could talk to maybe a little bit about maybe what countries have the most mature regulatory environment? I think about a quarter of your revenues today come from rest of world. And then kind of as you think about expanding outside the US, how do you kind of pitch the sales and marketing effort there? Maybe where your brand loyalty isn't as strong or regular safeguards aren't quite as important to customers in maybe some of those other markets? Thanks.

Alesia Haas: Thanks. And Brian maybe I'll start and please feel free to jump in. So, today we offer a full suite of products and services in the US and in the UK and in Europe. So, when we've disclosed our rest of world step today, most of that -- 99% of that 25% that you mentioned, is in the UK and Europe and that's where we offer fiat to crypto services. We do market in those countries, similar to the approach that we do in the US. We do not have significant efforts in global marketing outside of those regions at this time and so when I was addressing the comment earlier, what we're really looking to do is expand our fiat to crypto services and more and more countries as that's what we can provide the full suite of the Coinbase platform, and the benefits that we offer to add more users and more countries. And so to do that that is what requires getting licenses, getting bank partnerships to be able to provide those fiat rails. And once we do that, we would then extend marketing in those countries and introduce the Coinbase brand. Obviously, we would need to do the proper research and localize the product offering as appropriate. But we are in the early days where we're getting the infrastructure set up to do more global expansion and we're not yet at the point of marketing.

Mark Palmer, BTIG: Yes, thank you for taking my question. Wanted to get your take on what kind of demand you are seeing on the institutional side for your new prime brokerage product from hedge funds, from large mutual fund complexes. How would you assess that demand? And if you could give some insight as well on the lending aspect of the prime brokerage product and what its prospects are? Thank you.

Alesia Haas: Great, maybe I'll start here again and Brian, please jump in. So, we're seeing great interest from all corners of institutions, whether they're hedge funds, asset managers, corporate, pensions, endowments, insurance, I mean you name it and people have started to explore interest in Bitcoin, Ethereum, and increasingly even a longer tail of crypto assets. And they're coming to us and looking for our services and custody and our liquidity pools that we provide on our exchange and then our smart order router which enables us to get best pricing on a number of these transactions. So, incredible interest from all corners. Institutions are right now doing a lot of work on assessing these platforms, doing their due diligence, ensuring that they have trusted service providers in the space and we are proud to say that we are winning many of those mandates and growing our customer base. Today what we offer as you see in our financials is largely trading and custody. We are looking to expand our Borrow & Lend products we've been building out the full suite of prime brokerage services that those firms will be accustomed to see in a traditional financial services prime broker, but the Borrow & Lend products are very nascent at this time, and we expect to see future growth in that area.

Brian Armstrong: Yeah. The only thing I would add is one other customer segment we're seeing interest from there is corporate treasuries as well.

Mark Palmer: Thank you.

Harshita Rawat, Bernstein: [inaudible]...it's front row seat in the development of the crypto ecosystem, you've coined the term cryptoeconomy. I know it's a hard question, given the early innings that we are in, but can you talk about some of the most powerful applications of crypto in the next five, ten years in terms of [inaudible] the store of value, payments? And how can Coinbase participate as an on ramp to the crypto economy? Thank you.

Brian Armstrong: Yeah, I mean that's a great question about the future, and in some ways we were in a tough spot trying to predict the future here, we can give you a couple of themes that we're excited about. But I think if we were sitting here in 1999 trying to predict what the internet would be in five or 10 years, we probably would have gotten a lot of it wrong.

So, I think we're seeing crypto, first, be used as for investment, people are trading it. We're now, that will come at the stage one. Stage two is crypto in financial services, and so that's where you're starting to see things like decentralized exchanges, DeFi, decentralized borrowing and lending, decentralized insurance. And so I think that trend will continue and you'll see greater adoption of DeFi. And then I guess in the third phase, what we're going to see here in the future is really around crypto as an app platform. And so that could mean people using crypto as kind of like the next version of the internet, they will build their application natively on blockchains, even if they have nothing to do with financial services, and we're seeing some early signs of that, people are doing things like identity management, they're creating games, they're doing things like artwork with NFT's, very creative things like that, they could be even used in virtual world, social sites like Reddit, for instance, has come out and said they want to use Ethereum in certain ways on their application. You could imagine new versions of social media being created on blockchains perhaps in a way where users own their own data, which could be interesting.

And I think you'll see new forms of governance and voting too where people are creating new types of autonomous organizations where proposals can be voted on by people with these coins and all over the world coordinating on various problems and challenges. So that's just like a hint at what's happening, by the way there's also, I think more and more central banks will start to create digital currencies, we've seen a lot of activity there in China, and I think and hope that the U.S. and other countries will follow. Coinbase is coin agnostic and so we want to support every crypto asset out there that's legal and safe for customers and so we would include those assets as well along the way. So I think you'll just see it really is, kind of, like we're at the very early days of the internet, and I think you're seeing a ton of innovation and hopefully that gives you a sense of some of the opportunities in the future as well.

Anil Gupta: Erica, we have time for one more question.

Owen Lau, Oppenheimer: Good afternoon and thank you for taking my question. I think it's still in early days, but I think your cash balance almost doubled to \$2 billion in three months and your second quarter trading volumes so far I think seems to be strong. So what is the capital management priority regarding reinvesting back to the business, M&A, buybacks and things like that? And if there's a disconnect between the fundamentals of Coinbase, as a whole, in the stock price, how would you think about even initiating buybacks? Thank you.

Alesia Haas: Thanks for the question. Our focus is on growth. Our focus is on investing both organically and inorganically in growth, so expanding our product suite, growing our MTUs, expanding geographically as we spoke about earlier. And we'll do that through hiring, we'll do that through investing in technology and through acquisitions, where that makes sense with our product roadmap. We are not focused on deploying that cash for share repurchases at this time, nor for dividends or any other capital actions, as we've shared with you, there is a lot of volatility in our earnings and we are investing in growth when revenues are high and when revenues are low, until we use the cash that we build up on our balance sheet in these periods of high revenue and high profitability, to prepare for potential crypto winters where we could see a decline in our revenues. And we want to ensure that we have the balance sheet that can support us in all environments, because we're building for the long term, and think that we're going to have amazing future of profitability at some point in time, but we need to invest in this product suite and revenue diversification to get there.

Owen Lau, Oppenheimer: Thank you very much.

Anil Gupta: Great. Well, thank you everyone for joining us today and we look forward to speaking with you on our next call.