

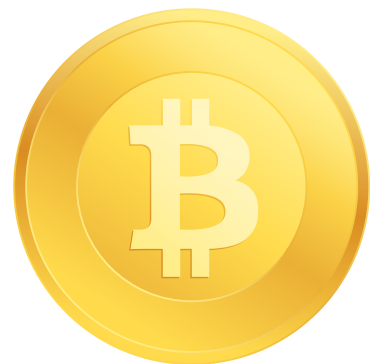


Bitcoins:

History, recent events, challenges and opportunities

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Why am I so excited about Bitcoin?

When I accepted my first Bitcoin I was instantly addicted. Unlike any other payment vehicle online Bitcoin gives power to the little guy.

Imagine this. A big TV producer just called. She wants to do a half hour show about YOUR product. You might do 6 or 7 figures in sales within 24 hours of it airing.

Will your bank, shopping cart or Paypal underwrite this for you? Chances are the answer is no. Unless you are in a position to put a substantial upfront cash deposit on hold to mitigate the risk.

Your account will be frozen the minute things go above acceptable norms established by you.

With Bitcoin. There is no risk department to slow your growth. If you want to make a million dollars in a day you can. Nobody will call you to ask why you are doing this and make decisions about your financial future.

The best part is Bitcoins can be traded for real dollars in seconds using the [exchange](#).

Bitcoin isn't owned by anyone. It's owned by you and me. Read on to find out more about this disruptive technology.

[Download and install Bitcoin](#) for free while you read this report (it takes a LONG time to install so leave it overnight).

What is a Bitcoin and how does it work?

Bitcoin, is the world's "first decentralized" digital currency that operates on a peer-to-peer system made up of fellow users' machines. Unlike traditional currencies, which are issued and backed by central banks and government (and therefore, protected), Bitcoin has no central monetary authority that monitors, verifies, approves transactions or manages the money supply. Instead, it relies on this peer-to-peer network.

First [launched in 2009](#) by a mysterious person or persons named Satoshi Nakamoto, Bitcoins can be bought or earned through "mining" which involves powerful computers (much more powerful than traditional laptops) solving [difficult number-crunching tasks](#). Successful miners are then rewarded with 25 Bitcoins. The system is set up so that the total number that can ever be mined is limited to around 21 million ([the number of bitcoins set to top out at 21 million around 2040](#).) Limiting the supply prevents a flood of new Bitcoins from entering the market and devaluing those already in circulation. Inversely, hoarding can also cause the value of Bitcoins to increase.

Bitcoins (or fractions of bitcoins known as satoshis) can be exchanged for goods and services or traditional currency on several exchanges (such as Mt. Gox). They can also be directly transferred across the internet from one user to another, using appropriate software. Currently, there are around 11 million Bitcoins in circulation and 25 new Bitcoins are produced every 10 minutes. They are traded through [online exchanges like Mt.Gox](#).

A log is collectively and publicly maintained of all transactions with new transactions being verified to prevent counterfeiting. Because of this public reporting, Bitcoin transactions are not entirely "anonymous" as many have claimed.**

According to an article from The [Economist](#), “All transactions are secured using public–key encryption, a technique which underpins many online dealings. It works by generating two mathematically related keys in such a way that the encrypting key cannot be used to decrypt a message and vice versa. One is made public; the other is kept private by the individual (the payer) to approve any transfers to a recipient's account.”

Bitcoin users can sign up for an online wallet service through which all transactions are carried out. Or, the wallet can be installed on a user's computer. However, once the wallet is lost to say a computer crash or hacking, [so are the bitcoins](#).

History and challenges

At only four years old, Bitcoin has already gone through [several years of boom and bust cycles](#). In August 2011, it hit a low of \$7 after hitting a high of \$32 two months earlier. Recently, Bitcoin hit a high of \$266 on April 10 and then the next day dropped to \$120. However, after each crash, Bitcoin has bounced back and actually overtaken its previous record.

Justin Fox of the Harvard Business Review writes, “The issue is simply that if the overall money supply can’t grow, you will probably get deflation. Something that costs 10 bitcoins today will cost 5 next week. Which may sound great, but is [no way to run an economy](#).”

Because of its volatility, many financial experts have [warned against Bitcoin](#). Veteran UBS stockbroker Art Cashin has [compared the interest in Bitcoin to the tulip mania](#) the 17th century, which is considered the first “recorded speculative bubble”. Also, since the currency is not backed by any government or bank, there is no protection for an investment.

Some experts have speculated that Bitcoin rises and crashes can be traced back to real-world banking crises, like the one in Cyprus. However, others think that increased interest and awareness of the currency has led to speculation, causing increased rises in the currency independent of current global financial trends.

Cyber-attacks and hacking is another challenge to the currency. Recently, Mt. Gox, one of the largest Bitcoin exchanges, has been battling with denial-of-service (DDOS) attacks. The exchange believed the attack was [intended to swing bitcoin's price](#).

According to an article on PCWorld.com, “When Mt. Gox's website slows or goes offline, trading becomes more uncertain. Traders may also suddenly sell large volumes of bitcoins, causing a panic and driving the price down.”

“Miscreants are also trying to manipulate the virtual currency's price by using Mt. Gox's API (application programming interface) to submit trades for very small fractions of bitcoins. Entering lots of small sell orders, for example, can give the impression that bitcoin's price is falling even if it doesn't represent the broader market sentiment.”

To combat this, Mt. Gox, said the exchange is slightly limiting the number of mini-transactions a trader can submit and capping the transactions during high trading times and also work on a new trading engine that will run separately from its front-end website. <http://www.pcworld.com/article/2036060/largest-bitcoin-exchange-mt-gox-throttles-trading-to-tame-price-swings.html>

Challenges outlined by Jeremy Liew, managing director at [Lightspeed Venture Partners](#), are hacking, theft and fraud involving Bitcoin exchanges, wallets, or investment vehicles (not including the accounts and wallets of personal bitcoin holders).

Whether [Bitcoin or any other electronic currency is even legal](#) is another challenge, according to Wharton legal studies and business ethics professor [Andrea Matwyshyn](#). In the U.S., as in most countries, only the federal government can issue legally recognized tender.

"Whether these types of alternative currencies can co-exist with traditional models is an unanswered question," says Matwyshyn to the [Knowledge@Wharton blog](#). "It's such a new regulatory space that the law isn't there yet."

Steve H. Hanke, a professor of applied economics at Johns Hopkins University suggests that governments will not allow Bitcoin to get much of a foothold in their countries.

"If this becomes a commercial threat to the state production of money," says Hanke to the [Knowledge@Wharton blog](#), "there will be a million reasons trotted out to restrict it or prohibit it."

Opportunities

“Venture capitalists will have three ways to profit,” said Nicholas Colas at ConvergEx to MarketWatch.com, “exchanges, service offerings for individuals, and service offerings for businesses.”

Jeff Berwick, who designed the [first Bitcoin cash machine](#), is an example of such a service. His machines will convert a person's Bitcoins into the currency of the country where they are withdrawn.

Berwick told the [BBC](#) that, “Over 200 people have said they're interested in buying a machine or more than one from 30 different countries. This is a way to transact outside of the traditional, regulatory monetary system,” he said.

BitPay, which functions like a credit-card processor, [calculates a dollars-to-Bitcoins exchange rate](#) and generates a unique code, which customers can scan to transfer money. Customers at one midtown lounge in New York [are offered tablets by wait staff with BitPay](#) in order to pay their bill.

“It’s funny, because New York has one of the largest concentrations of Bitcoins, but there aren’t a lot of businesses that take them,” said Charlie Shrem, owner of EVR Lounge in [an article by the NY Post](#).

Jeremy Liew, managing director at [Lightspeed Venture Partners](#), told [TechCrunch.com](#), that there are three key markets in Bitcoin:

- **Wallet.** Holding your Bitcoins for you, serving some of the checking account functions of a bank.
- **Exchange.** Converting from USD to Bitcoins and back.
- **Payments.** Helping merchants accept Bitcoins for their transactions.

Liew only sees success in these markets if more people and businesses start using and accepting Bitcoins or if the currency is "[legitimized](#)" by governments.

"Bitcoin usage would have to become mainstream," said Liew. "The only way to get there is through merchant preference because of the lower transaction costs. This could be appealing to industries with low net margins (e.g. grocery, Amazon.com), or with high transaction costs (e.g. cross border trade, micro transactions), and these may be the industries that pioneer Bitcoin acceptance."

Widespread usage is somewhat of a challenge for Bitcoin says Wharton marketing professor [Eric T. Bradlow](#), who says that it is [unclear what market need Bitcoin is fulfilling](#).

"Why do people need Bitcoins?" Bradlow is quoted as saying in the [Knoweldge@Wharton](#) blog. "The 'product' has no obvious customer segment, point of differentiation and obvious consumer need that it is satisfying in comparison to other competing products. Therefore, it will struggle to be highly adopted."

So how are larger, well-established companies such as banks, credit card companies and other financial companies reacting to Bitcoin?

Western Union Co. (WU) and MoneyGram International Inc. (MGI) are studying ways their customers could use their services to send and receive money transfers denominated in bitcoins, according to a story by [FoxBusiness.com](#). However, both these companies and credit card giants Visa and MasterCard are not too concerned about Bitcoin because it is not widely-used and its value remains so volatile.

Changing and challenging the system

Perhaps the most attractive aspect of Bitcoin is the freedom the currency offers and its removal from government oversight, politics and financial organizations. As writer for [Andrew Leonard said in an article for Salon](#), “Bitcoin is a currency with an ideology. By its very nature, Bitcoin is made for people who don’t want other people to know what they are doing.”

Many users feel safer with their money in Bitcoin, especially after recent events such as the economic crisis in Cyprus which just approved a \$13 billion bailout from international lenders. The bailout comes with steep austerity measures which included depositors at the Bank of Cyprus taking a 60 percent loss on deposits over 100,000 euros and an overall 300–euro daily withdrawal limit to prevent a run on the banks.

Bitcoin lives outside any government’s (or bank’s) control. The currency is borderless and can be accepted world–wide without costly transaction fees while traditional currency exchanges go to big corporations and banks, which many users object to and hold in contempt. Payments and transfers can also occur instantaneously on the network 24/7 and doesn’t depend on “business hours.”

Slowly, businesses both large and small are starting to accept Bitcoins as forms of payment. Reddit, Wordpress, Foodler, and OKCupid, have started accepting Bitcoins. Even Paypal is looking at ways to [integrate Bitcoins in with its payment network](#)

“Virtual currency is something that’s here to stay,” said eBay Inc. (and Paypal) Chief Executive John Donahoe in an interview with The Wall Street Journal.

Pizzaforcoins.com allows users to use their bitcoins to order from popular pizza franchises like Domino’s and hopes to include Papa John’s and Pizza Hut to their list. Still other smaller businesses are cutting out the need for a middle man and just accepting the currency directly.

Joerg Platzer, the owner of bar Room 77 in Kreuzberg, Berlin, has formed a group in order to promote Bitcoin to local businesses in his city. He told a news videographer for the U.K. newspaper The Guardian that he wants to establish the first Bitcoin-based local economy.

“There are certain reasons that could make one believe that there are flaws to our current economic and financial systems to which Bitcoin, or something like Bitcoin, could be the solution,” said Platzer.

“So every day we do not start using a free currency like Bitcoin, we actually actively vote for the current system to continue.”

Appendix

Footnotes:

** Jeff Garzik, a member of the Bitcoin core development team, wrote to Adrian Chen of Gawker after Chen wrote an article entitled "[The Underground Website Where You Can Buy Any Drug Imaginable](#)" to say that bitcoin is not as anonymous as the denizens of Silk Road would like to believe. Garzik explains that because all Bitcoin transactions are [recorded](#) in a public log, though the identities of all the parties are anonymous, law enforcement could use sophisticated network analysis techniques to parse the transaction flow and track down individual Bitcoin users.

"Attempting major illicit transactions with bitcoin, given existing statistical analysis techniques deployed in the field by law enforcement, is pretty damned dumb," Garzik wrote.

Resources

Cool stuff for online entrepreneurs...

Dpassport.com

All the graphics, plugins, reports, and content you need to run your online business.

VectorToons.com

Vector clipart with royalty free usage rights. Use them in your next presentation, sales letter or website.

[Chronic Marketer](#)

The awesomely hilarious book about online marketing written by Brad Gosse. Get it on Kindle or paperback.

