

Arculus

Digital Assets Research

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TL;DR

- A metal payments card pioneer bringing a unique crypto hardware wallet to market
- Novel tech approach to a cold storage wallet using 3FA
- Company uniquely positioned to bring product to market due to industry relationships and manufacturing capabilities
- **Risks:** Regulation, competition, inability to maintain strategic relationships, adoption

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Arculus: A wallet bridging security and usability

CompoSecure Holdings, LLC ("CompoSecure," or the "Company") designs and manufactures metal payment cards for many of the world's leading financial institutions. The Company was the first to produce a metal card in 2003 in partnership with American Express and has since forged deep relationships with additional issuers/resellers such as JP Morgan Chase, Capital One, and Fiserv (Slide 12). The Company produces cards for a variety of proprietary and co-branded programs and has demonstrated a history of improving security and customer experience through various design improvements. The Company is now leveraging its experience in secure payment hardware solutions to enter the digital asset space starting with the launch of its Arculus Cold Storage Wallet.

- **CompoSecure enters SPAC deal.** CompoSecure and Roman DBDR Tech Acquisition Corp. (NASDAQ: DBDR), a special purpose acquisition company, recently entered into a definitive merger agreement valuing the combined entity at approximately \$1.2 billion. The transaction is expected to close in Q3 2021 and proceeds from the transaction will be used to implement its growth strategy centered around the cryptocurrency cold-storage and security solution, Arculus (Slide 3).
- **Crypto goes mainstream.** Digital assets have emerged as an entirely new asset class for institutional and retail investors alike. There are an estimated 100 million users across all cryptoassets and in 2020, crypto surpassed \$1 trillion in total market cap (Slide 21). Recently, rising demand for cryptoassets has led to an increase in hacking activity across the entire digital asset landscape. As crypto becomes increasingly ubiquitous, the need for better security options becomes paramount (Slide 22).
- **Demand for better wallets.** Wallets are tools employed by crypto users to store, manage, and swap cryptoassets. There are several types of wallets – exchange-based, digital, hardware, and paper – all of which suffer from the historically inevitable tradeoff between usability and security (Slide 8). "Cold Storage" hardware devices have become increasingly popular as digital asset holders seek secure storage solutions that are offline and offer the highest security level (Slide 24). Unfortunately, most of these hardware solutions are cumbersome USB-like devices and require a connection to a desktop, leading to a subpar user experience.
- **Arculus wants to bridge the best features of hot and cold wallets.** Arculus is three-factor authentication (3FA) security platform created with the mission to promote digital asset adoption by offering a simple, secure way to buy, sell, and store digital assets. The envisioned platform is a multi-year endeavor that commences with the launch of the Arculus Cold Storage wallet in Q3 2021. The wallet is comprised of a mobile interface through which a user can easily manage and transact their digital assets and a metal card that is applied as the third level of authentication and is where any private keys are stored in an "air-gapped" environment (Slide 16).
- **CompoSecure is positioned to bring Arculus to life.** A byproduct of its successful legacy business is a unique foundation upon which the Company can build its Arculus platform. The Company's manufacturing capacity can satisfy high scaling requirements, and its proprietary manufacturing processes may result in favorable unit economics for the Arculus hardware product. Further, the Company can tap into its longstanding relationships with premier card issuers to sell its wallet product via the Arculus brand or a white-labeled solution (Slide 26).
- **Risks.** Unforeseen regulatory hurdles that raise costs and create unanticipated operational burdens, an inability to sustain and ultimately leverage business relationships with key partners, degradation of relationships with American Express or JP Morgan Chase, increased competition from within the crypto space, and slower than anticipated mass adoption of hardware wallets (Slide 31).

Bottom Line: The Arculus Cold Storage Wallet has yet to launch, so we lack tangible KPIs to observe, but it does appear that CompoSecure is skating to where the puck is going within the crypto industry. We expect operational cold storage wallets to gain popularity for long-term investors and digital assets traders who are cautious about leaving their assets on an exchange or a non-custodial hot wallet. If CompoSecure successfully leverages its payments industry relationships and achieves its projected unit economics, the Arculus business has the potential to make waves in crypto security.

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CompoSecure Overview

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Arculus Overview

A payments innovator looks to bring a novel crypto solution to market

Figure: CompoSecure and Arculus Overview

Summary



- **CompoSecure** provides premium financial payment cards to some of the world's largest financial institutions. The Company pioneered metal credit cards, which improved user experience and encouraged increased spending among end-users.
- The Company leverages its trove of innovative IP and proprietary manufacturing methods to produce high-grade and secure products. CompoSecure has longstanding relationships with some of the world's largest banks and financial institutions, such as J.P. Morgan Chase and American Express.
- CompoSecure and **Roman DBDR Tech Acquisition Corp.** (NASDAQ: DBDR), a special purpose acquisition company, have entered into a definitive merger agreement. Upon closing of the transaction, the combined company will operate as CompoSecure, Inc. and plans to trade on the Nasdaq stock market.
- CompoSecure plans to combine its longstanding history in payments innovation with Roman DBDR's leadership capabilities in the technology ecosystem to bring a cryptocurrency cold-storage and security solution, **Arculus**, to market.

Transaction Highlights

- **CompoSecure Financials:** 2020 Net Revenue of \$261 million and Adjusted EBITDA of \$116 million (45% margin)
- **Implied multiples:** 4.2x 2021E Net Revenue, 3.4x 2022E Net Revenue, and 11.5x 2022E Adj. EBITDA (company projection)
- **Pro Forma Enterprise Value:** \$1.2 billion
- **Financing:** \$130 million fully-committed exchangeable notes and a \$45 million common stock PIPE financing led by BlackRock and Highbridge Capital Management
- **Transaction Announced:** April 19, 2021
- **Expected Close:** 3Q 2021

Source: Fundstrat, CompoSecure

CompoSecure Team – Innovators, Designers and Thinkers Unite

Applying diverse experiences to create a unique product ecosystem



Figure: CompoSecure Key Team Members



John Wilk CEO	Tim Fitzsimmons CFO	Gregorie (Greg) Maes COO	Adam Lowe, PhD CIO
<ul style="list-style-type: none"> • 20+ years of experience in banking, management consulting, and private equity companies • Former President of PayChoice, a leading SaaS-based payroll company (Acquired by Sage Software) • Former Head of Product and CMO for JP Morgan Chase's Consumer Bank • Received MBA from Kellogg Graduate School of Management 	<ul style="list-style-type: none"> • 30 years of experience in accounting and finance and 10 years of direct industry experience • Founder of own consulting firm CFO Controller • Former Global Controller at GE Capital • Former Controller of Plastic Card Operations for DataCard North America 1991 • Received MBA from Drexel University and BS from St. John's University in New York 	<ul style="list-style-type: none"> • 25+ years of experience in card payments • Former Global COO for ABCorp • Held leadership positions at IDEMIA and Gemplus (Gemalto, now part of Thales) • Chemistry and Physics degree from Graduate School of Chemistry and Physics of Bordeaux, France 	<ul style="list-style-type: none"> • Joined CompoSecure in 2014 as Principal Research Engineer and has held several positions of progressive responsibility • Held an innovation development role at SRC Inc., a not-for-profit R&D company supporting US defense and intelligence communities • Received MBA and PhD from Cornell University and BS from Syracuse University



Source: Fundstrat, CompoSecure

Roman DBDR Brings a Finance, Tech, and Innovative Approach

Tech industry veterans with ample operating and investing experience

Figure: Roman DBDR Key Team Members



Dr. Don Basile, PhD <i>Chairman and Co-CEO</i>	Dixon Doll, Jr. <i>Co-CEO</i>	John Small <i>CFO</i>	Dixon Doll <i>Senior Director</i>
<ul style="list-style-type: none"> • 20+ year of technology industry experience across software, hardware, IT, telecom and private equity • Executive, investor or board member in 30+ Silicon Valley growth companies • Current CEO of Monsoon Blockchain Corporation, a blockchain enterprise solutions company • Received PhD and M.S. in Electrical Engineering from Stanford University 	<ul style="list-style-type: none"> • Former CEO and Chairman of DBM Cloud Systems, a pioneer in data management software • Former COO and Director of Violin Memory, a flash-memory storage maker • Managing Director of Longstreet Ventures, an investments and private equity advisor specializing in technology startups • Received MBA from University of Michigan and a B.A. from Georgetown University 	<ul style="list-style-type: none"> • 20+ years of experience in investment management • CFO of Monsoon Blockchain Corporation, a blockchain enterprise solutions company • 11 years as TMT portfolio Manager at GLG Partners • Former CFO of Viggle • Received B.A. from Cornell University 	<ul style="list-style-type: none"> • 35+ years of experience influencing entrepreneurs, investors and executives in communications, internet and other technology industries • Co-Founder of DCM Ventures and Accel Partners (Telecom vertical) • Received BSEE from Kansas State University, MS and PhD University of Michigan College of Engineering

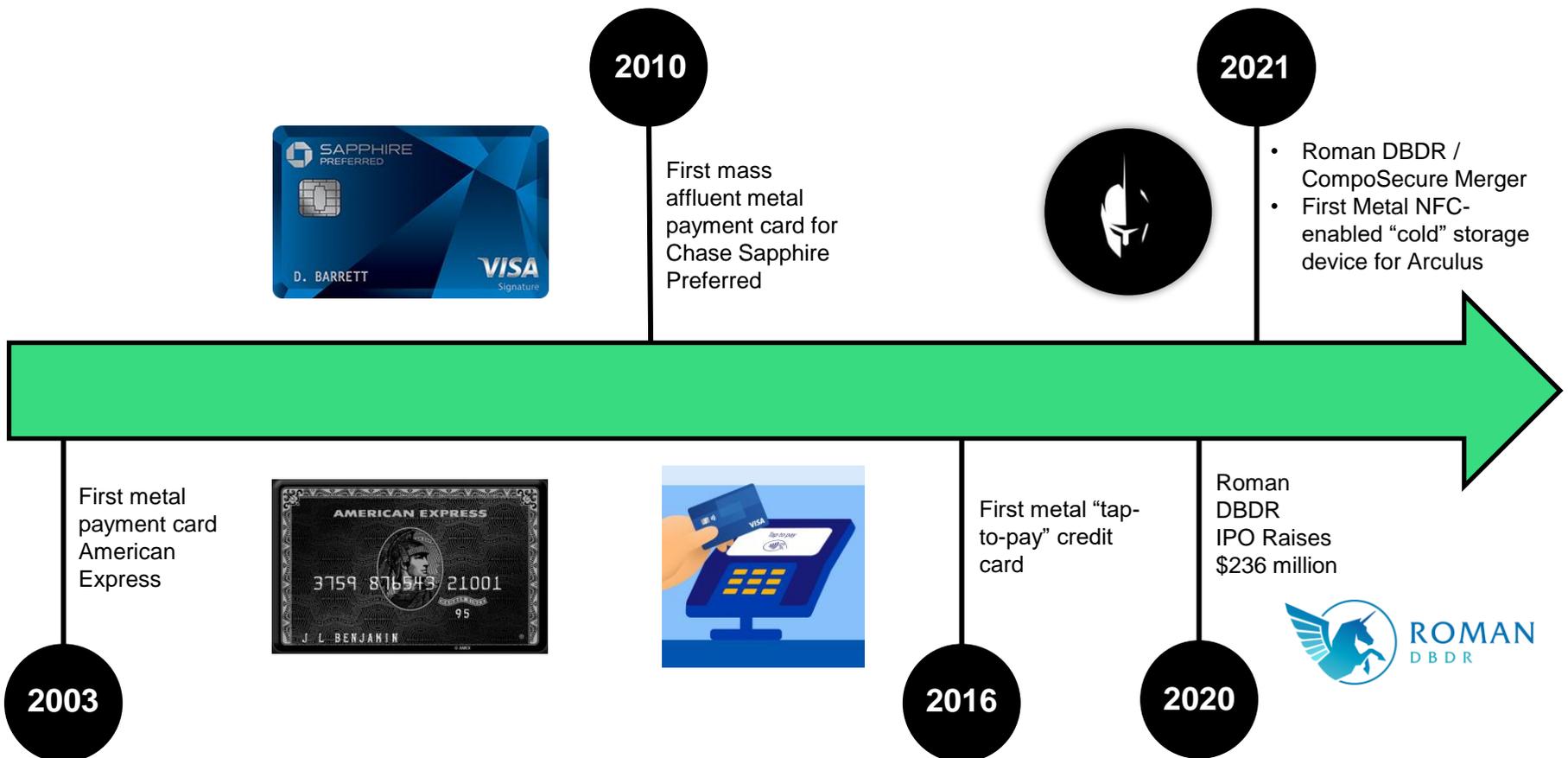
Source: Fundstrat, CompoSecure

CompoSecure's History of Payment Card Innovation

The Company was first to market with metal payment cards

- CompoSecure has demonstrated a history of improving the user experience for its end users and establishing relationships with premier issuers in the payments industry
- From 2010 through 2020, CompoSecure produced and sold 92 million metal payment cards.

Figure: CompoSecure, Milestones and Roadmap



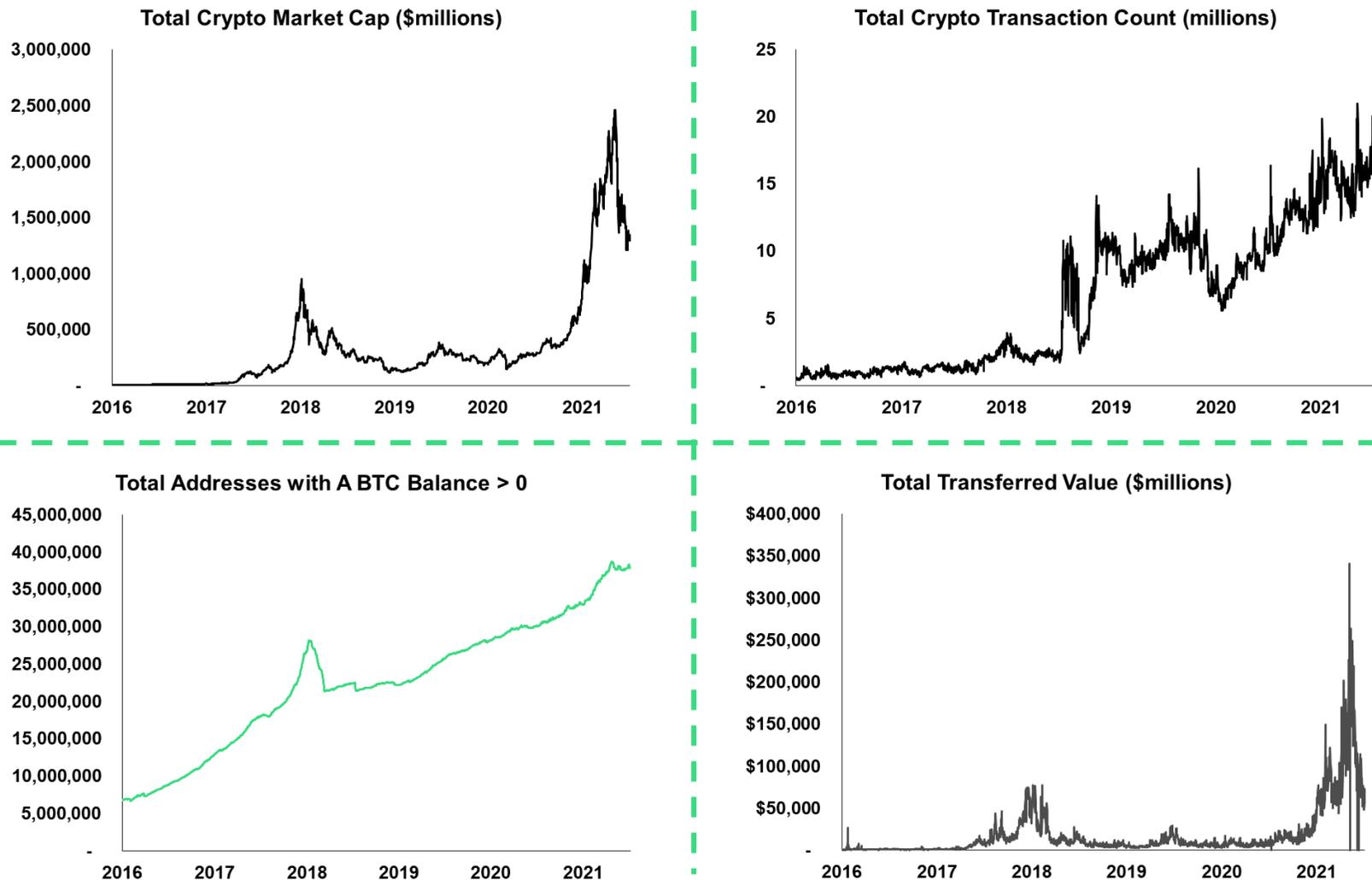
Source: Fundstrat, Roman DBDR

Crypto is Shifting From a Fad to an Asset Class

Growth in crypto market cap and volumes reflect mass adoption

- As demonstrated by increased network activity and a rising total crypto market capitalization, investor adoption of cryptoassets continues to proliferate.

Figure: Crypto Market Trends



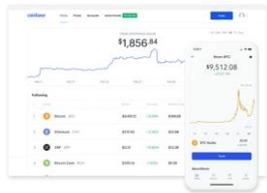
Source: Fundstrat, CoinMetrics

Digital Asset Wallets Grant Owners Control and Mobility

The different types of wallets and their varying levels of security

- Unlike traditional wallets that store cash, crypto wallets do not actually store cryptoassets, as your Bitcoin, Ethereum, or other digital asset “lives” on-chain. Crypto wallets store your private keys - the password-like string of letters and numbers that give you access to your cryptoassets. They also allow you to send, receive, and spend cryptocurrencies like Bitcoin and Ethereum.
- There are several types of wallets, the most popular of which are exchange-based wallets. As crypto becomes more ubiquitous and custodial options become more user friendly, we expect that crypto users will migrate to the more secure options.

Figure: Overview of Crypto Wallets



Coinbase Exchange Wallet

Exchange Wallets – The typical onramp for crypto investors is the exchange-based wallet. Users can store, manage, and trade cryptoassets seamlessly. Keys are generated via the exchange and exchange has access to them and are stored in their data bases. By having keys managed by the exchange, leaves users vulnerable to a hack of either a user’s exchange app or a hack of the exchange itself. Historically, approximately 10-15% of the circulating supply of BTC and ETH are stored on exchanges but could expect this number to increase as the prevalence of crypto increases.



Metamask Digital Wallet

Digital Wallets – These are non-custodial “hot” wallets through which users maintain possession of their own keys, but these keys are stored digitally on a software application. These apps are normally accessed via desktop and mobile app and require two-factor authentication to access them. They are slightly less usable than exchange wallets, but have an increased level of security, although can still be vulnerable to attacks.



Trezor One Hardware Wallet

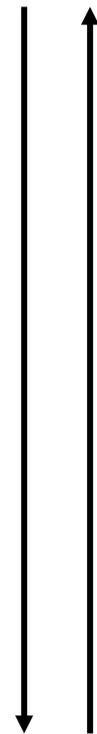
Hardware Wallets – These are the most typical type of “cold” storage wallets. The typical hardware wallet stores users’ keys on a device that is akin to a USB and must be either plugged into a desktop or, in certain cases, connected to an internet-connected device via Bluetooth to sign transactions. The point is to store users’ keys on a device that is not connected to the internet and therefore hack-resistant.



A Paper Wallet

Paper Wallets – This is the least-used but most secure option. Users’ keys are written on a piece of paper and normally stored in a personal vault or a safety deposit box. This method is often employed for long-term investment of large amounts.

More User-Friendly



More Secure

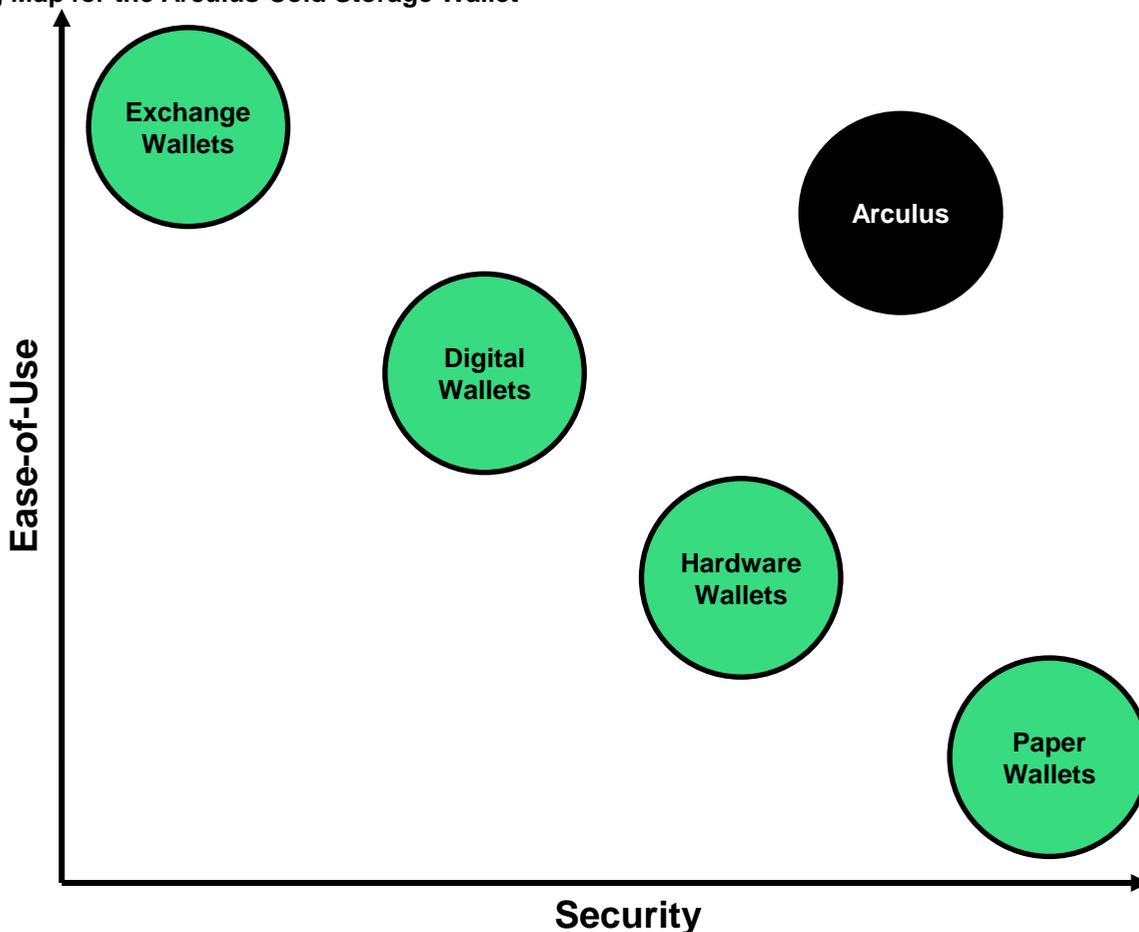
Source: Fundstrat

Bridging Usability and Security

Arculus is building a product with elements of hot and cold wallets

- In the wallet ecosystem there is a clear tradeoff between user experience and security. Exchange-based accounts and hot wallets are more vulnerable to hacks, while non-custodial hardware solutions are secure, but cumbersome or time-consuming to use frequently.
- The Arculus Cold Storage Wallet plans to offer a solution that bridges security and usability through a unique product form factor coupled with innovative and proprietary security features.

Figure: Market Positioning Map for the Arculus Cold Storage Wallet



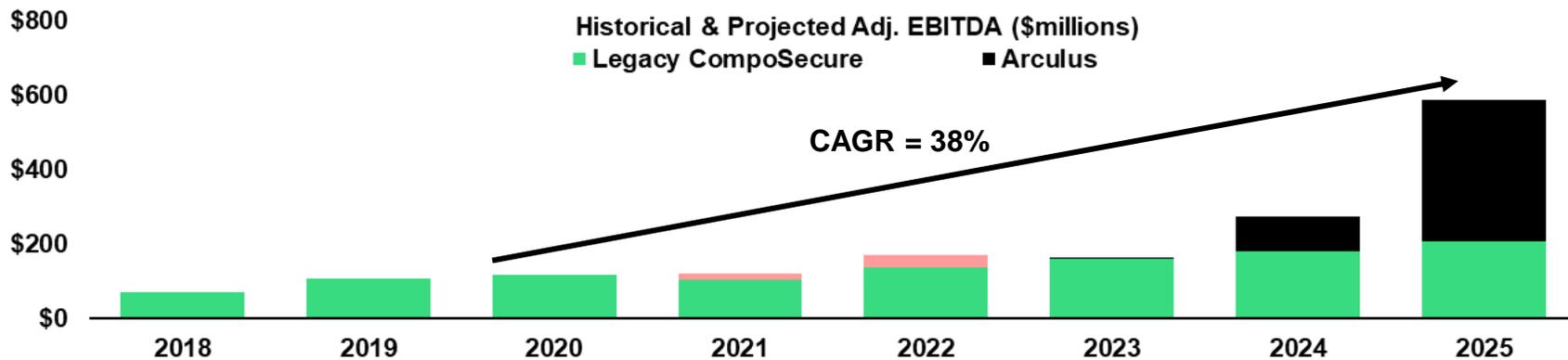
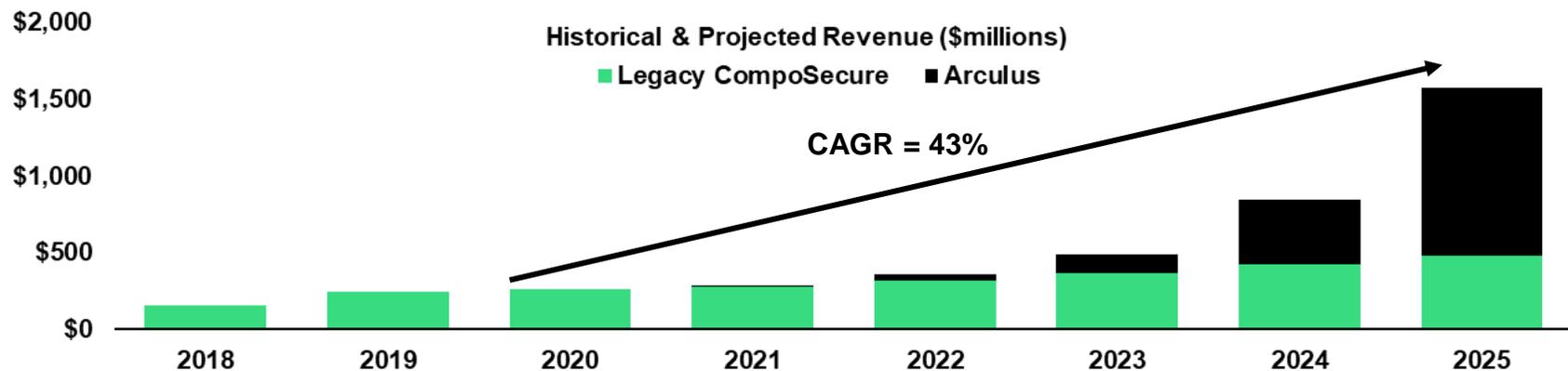
Source: Fundstrat, CompoSecure

Significant Projected Growth from Arculus Ecosystem

A steady base supports a new, high-growth business

- Management expects revenue and adjusted EBITDA to increase at an annualized rates of 43% and 38%, respectively.
- The Arculus ecosystem launches with its Cold Storage Wallet in Q3 2021 and is expected to comprise the majority of revenue by FY 2024.
- The RomanDBDR management team considers the Arculus projections to be conservative.

Figure: Segmented Growth in Revenue and Adjusted EBITDA



Source: Fundstrat, CompoSecure

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Metal Payment Card Solutions

CompoSecure is a leader in delivering premium card solutions

- CompoSecure brought metal cards into the mainstream, starting with the first metal payment card created for American Express in 2003. The Company has since produced and sold 92 million cards worldwide.
- CompoSecure has produced metal cards for more than 100 branded and c-branded card programs including the Visa , Mastercard®, American Express®, and China Union Pay payment networks.
- Dual-Interface payment cards are embedded with a chip that enables both contact and contactless payment. They comprise the majority of CompoSecure sales volume due to the speed and convenience they offer to cardholders.

Figure: Company Product Milestones and Key Clients

Notable Company Milestones

- **2003** – Created the world’s **first** metal payment card for American Express’ Centurion program (the “black card”)
- **2009** – Created the world’s first commercialized metal payment cards with embedded **EMV**
- **2010** – Created the first metal card geared towards the “**mass affluent**” segment for JP Morgan Chase’s Sapphire program, expanding the addressable market of metal cardholders
- **2017** – Introduced the first **NFC-integrated Dual-Interface** metal payment cards for American Express Platinum cardholders. These cards are generally sold at a higher price than contact-only cards

American Express Platinum



Chase Sapphire Preferred



Sample Large Issuer Relationships and Card Portfolios	Issuer/Reseller	CHASE	AMERICAN EXPRESS	Capital One	fiserv.
		JP Morgan Chase	Amex	Capital One	Fiserv
Proprietary Programs	Sapphire Preferred Sapphire Reserve JPM Reserve	Centurion Platinum Gold	Venture Savor Spark Business		
Co-Branded Programs	Amazon Prime Whole Foods United	Amazon Prime Business Mariott Delta			Verizon Morgan Stanley

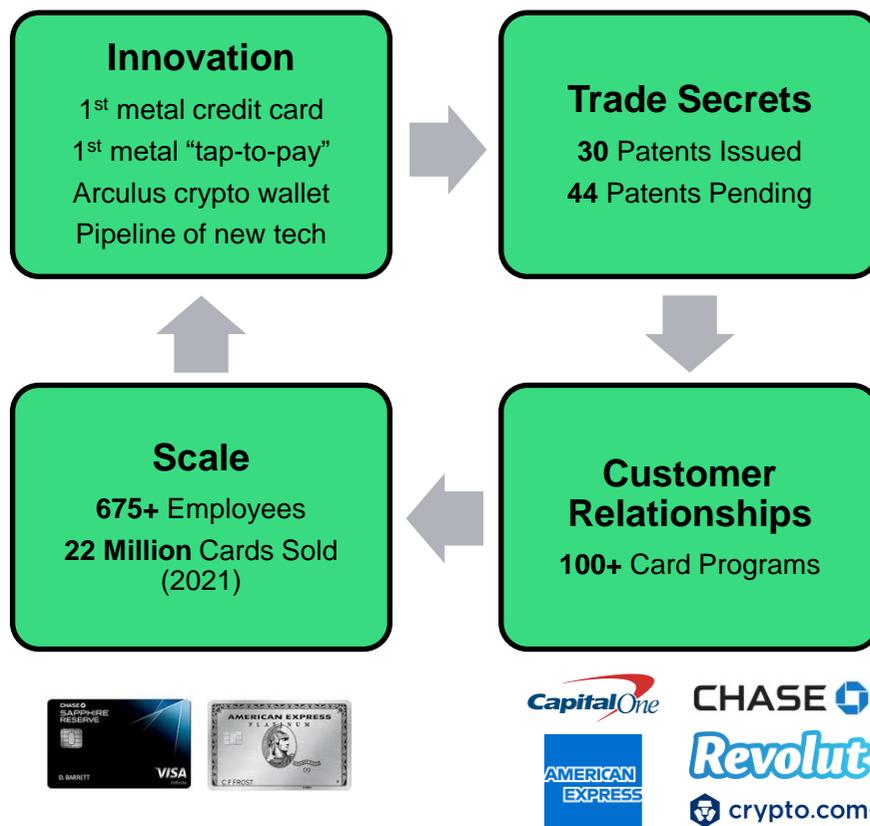
Source: Fundstrat, CompoSecure

CompoSecure Competitive Advantages and Roadmap

Innovative products and strong customer relationships drive growth

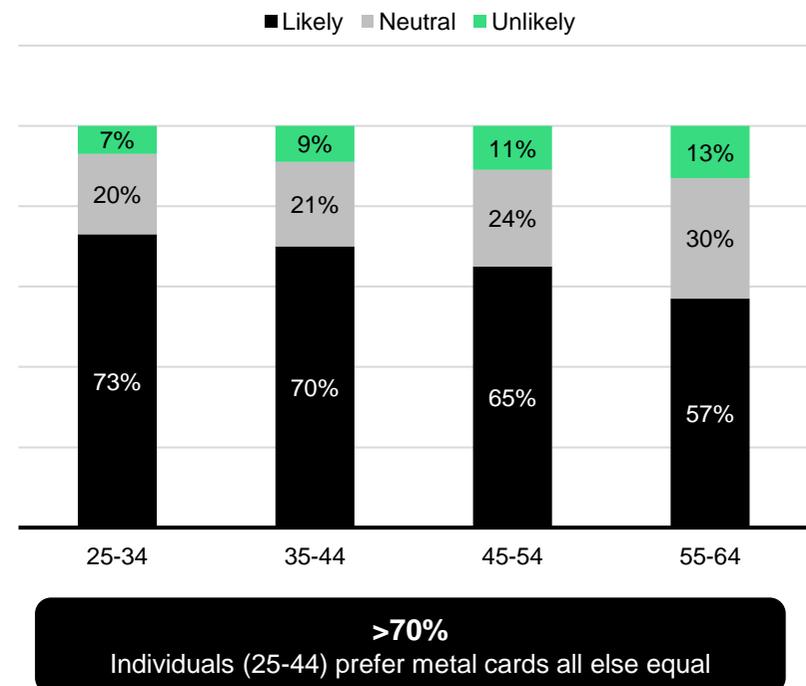
- Competitive advantages include innovative products, IP, embedded customer relationships, and scale.
- The Company has benefited from favorable demographics as millennial consumers demand metal cards at a higher rate than older generations. Millennials enjoy using metal cards to highlight status and wealth on social media and in person – creating a flywheel of free advertising for metal cards.
- Advertising also comes from issuing partners who frequently feature CompoSecure’s products in branded materials.

Figures: Competitive Advantages, Consumer Preference for Metal Cards Survey



Consumer Preference for Metal Cards by Age Group

Survey Question: How likely are you to select a metal card offer when you are looking for a new credit or debit card?



Source: Fundstrat, CompoSecure, Edgar, Dunn & Company

Financial Snapshot and the Arculus Impact

A strong margin profile and potential growth from Arculus

- CompoSecure reported revenue growth of 57% and 7%, respectively, for FY 2019 and 2020, and projects the legacy Payments Hardware business to grow 6% in 2021, followed by 15% annual growth throughout the forecast period.
- Total revenue is expected to increase rapidly in outer years of the forecast, driven by adoption of the Arculus wallet and subsequent launches of other products (Digital Assets, eGaming, and Insurance) within the Arculus ecosystem.
- CompoSecure has maintained a steady cost profile, achieving Adjusted EBITDA margins of 44-45% from FY 2018 through FY 2020. Management anticipates significant investment in launching the Arculus platform but projects a return to 37% Adjusted EBITDA margins in the outer year of the long-term forecast.

Figure: CompoSecure Financial Snapshot & Management Forecast

CompoSecure Historicals and Management Forecast Using Midpoint of High and Low Cases								
FYE	Actuals			Forecast				
	2018	2019	2020	2021	2022	2023	2024	2025
Revenue								
Legacy - Payments Hardware	155	243	261	276	316	363	418	480
Arculus - Crypto & Arculus Payments Solutions	-	-	-	10	40	93	261	612
Arculus - Digital Assets, eGaming & Insurance	-	-	-	-	-	33	168	485
Total Arculus Revenue	-	-	-	10	40	127	429	1,097
Total Revenue	155	243	261	286	356	490	847	1,577
% Growth - Legacy - Payments Hardware	NA	57%	7%	6%	14%	15%	15%	15%
% Growth - Total Arculus Revenue	NA	NA	NA	NA	300%	217%	238%	156%
% Growth - Total Revenue	NA	57%	7%	10%	24%	38%	73%	86%
Adj. EBITDA								
Legacy - Payments Hardware	69	107	116	120	138	158	181	208
Arculus	-	-	-	(18)	(33)	2	93	379
Total Adj. EBITDA	69	107	116	102	105	160	274	587
% Margin - Legacy - Payments Hardware	45%	44%	45%	43%	44%	43%	43%	43%
% Margin - Arculus	NA	NA	NA	-180%	-83%	1%	22%	35%
% Margin - Total Adj. EBITDA	45%	44%	45%	36%	29%	33%	32%	37%

Source: Fundstrat, CompoSecure

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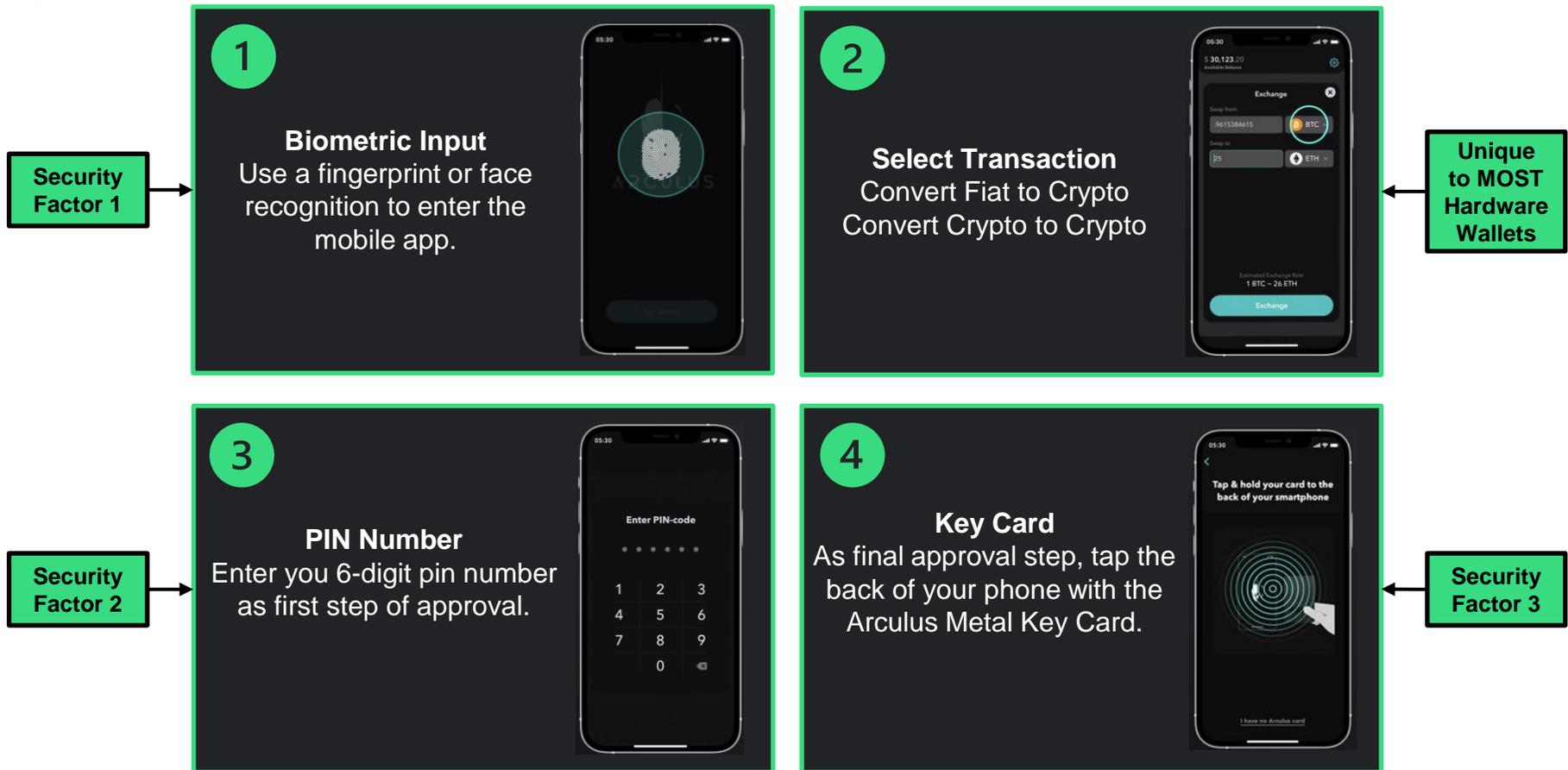
Appendix

Arculus Cold Storage Wallet

Biometric input, PIN number, and key card prevent improper use

- Arculus is three-factor authentication (3FA) security platform created with the mission to promote digital asset adoption by offering a secure and simple way to buy, sell and store digital assets.
- The envisioned platform is a multi-year endeavor that commences with the launch of the Arculus Cold Storage wallet in Q3 2021.
- At launch, the wallet will support BTC, ETH, BCH, and 10 popular ERC-20 tokens, with expected near-term integrations with DOGE, LTC, and other various ERC-20 tokens.

Figure: User Interface of the Arculus App



Source: Fundstrat, CompoSecure

Product Comparison

Security protocols differ from each wallet, but the main purpose remains

- “Cold” Storage hardware devices have become more popular as digital assets investors seek offline secure storage solutions that grant flexibility and the highest level of security. These devices range in security protocols, authentication and password recovery methods, but all offer the safest storage solution for digital asset users.
- We expect simple operational “cold” storage hardware wallets to gain popularity for long-term investors as well as digital assets traders who are cautious about leaving their assets on an exchange or non-custodial “hot” wallets.

Figure: Cold Storage Wallets Overview

										
Brand	Ledger	Trezor	Elipal	SecuX	D'Cent	Arculus	ShapeShift	Keevo	NGRAVE	Shift Crypto
Product / Price	Nano S / \$59 Nano X / \$119	One / \$60 Model T / \$194	Titan / \$169	V20 / \$160 W20 / \$99 W10 / \$67	Biometrics/\$119 Klaytn/\$23 Ethereum/\$23	Arculus / \$80-120	KeepKey / \$49	Model One / \$299	Zero / \$587	BitBox2 Multi / BTC-only/
Authentication	2FA - Pin & Device	2FA - 9 Digit Pin & Device	2FA - QR Code & Device	2FA - Pin & Device	3FA – Biometric, Pin, & Device	3-FA – Biometric, Pin, & Card	2FA - Pin & Device	4FA - Pin, Biometric, Device (2)	2FA - QR Code & Device	2FA - Pin & Device
PW Reset	24-word phrase	Recovery Seed	Passphrase Mnemonics (12 words)	12-, 18-, and 24-Word Recovery	24-word Code D'Cent Card (Select Assets)	12-word Passcode	12-, 18-, and 24-Word Recovery	Carbon Key	2-Part Encrypted	MicroSD Card & Recovery Words
Secure Element	CC EAL5+	None	None	CC EAL5+	CC EAL5+	CC EAL6+	None	None	CC EAL7	None

Observations

We note that D'Cent has a card wallet that has a similar “tap-to-verify” feature as the Arculus card, however, the cards are only compatible with Ethereum, ERC20, ERC721, Klaytn, and KCT tokens.

NGRAVE is the only product with a higher-level secure element, but its price point is 5x that of Arculus and the product is device-centric, as opposed to Arculus' mobile-centric user experience.

Source: Fundstrat, Company Source, Hardware-Wallets.net, techradar.com

Product Comparison

Proprietary technology enhances UX and security at the same time

- The Arculus Cold Storage Wallet offers a unique form factor described in further detail below. Its goal is to combine the usable interface of a hot digital wallet with the security of cold storage.

Figure: Arculus' Differentiating Factors

How Arculus Differs From Other Cold Wallets

- **Truly “Air-Gapped” Cold Storage** – As opposed to most other hardware wallets, which require a physical connection to an internet-connected device, a users’ private keys are stored offline on the Arculus Key Card, kept in a completely isolated form factor using a CC: EAL 6 secure element, and consistently remain in an offline environment. The only time the card communicates with an internet connected device is when the card is waived over the phone and a transaction is signed over a secure, encrypted NFC channel.
- **Three-Factor Authentication** – Advanced security across: (1) biometric (i.e., fingerprint and/or facial recognition); (2) personal identification number (PIN); and (3) encrypted NFC connection with the Arculus Key card. Other hardware wallets use 2FA, many of which require additional hardware devices connected to a desktop, which can be cumbersome, and leaves the user vulnerable various types of hacks.
- **Innovative Form Factor** – The slim, metal card, which does not require a battery or charging, offers a “premium” user experience and heightened hardware protection through an easy-to-use, encrypted NFC connection (“tap-to-transact”). There is a familiar feel to a card that is endemic in traditional personal finance.
- **Fully-Featured Mobile Wallet App** – Send, receive, and trade digital assets including fiat-to-crypto and crypto-to-crypto. This combines the best features of hot wallets with cold storage security. Currently, there are apps from other providers such as Ledger Live, which allow for full exchange functionality, but require a Bluetooth or USB connection to the Ledger hardware device to transact.



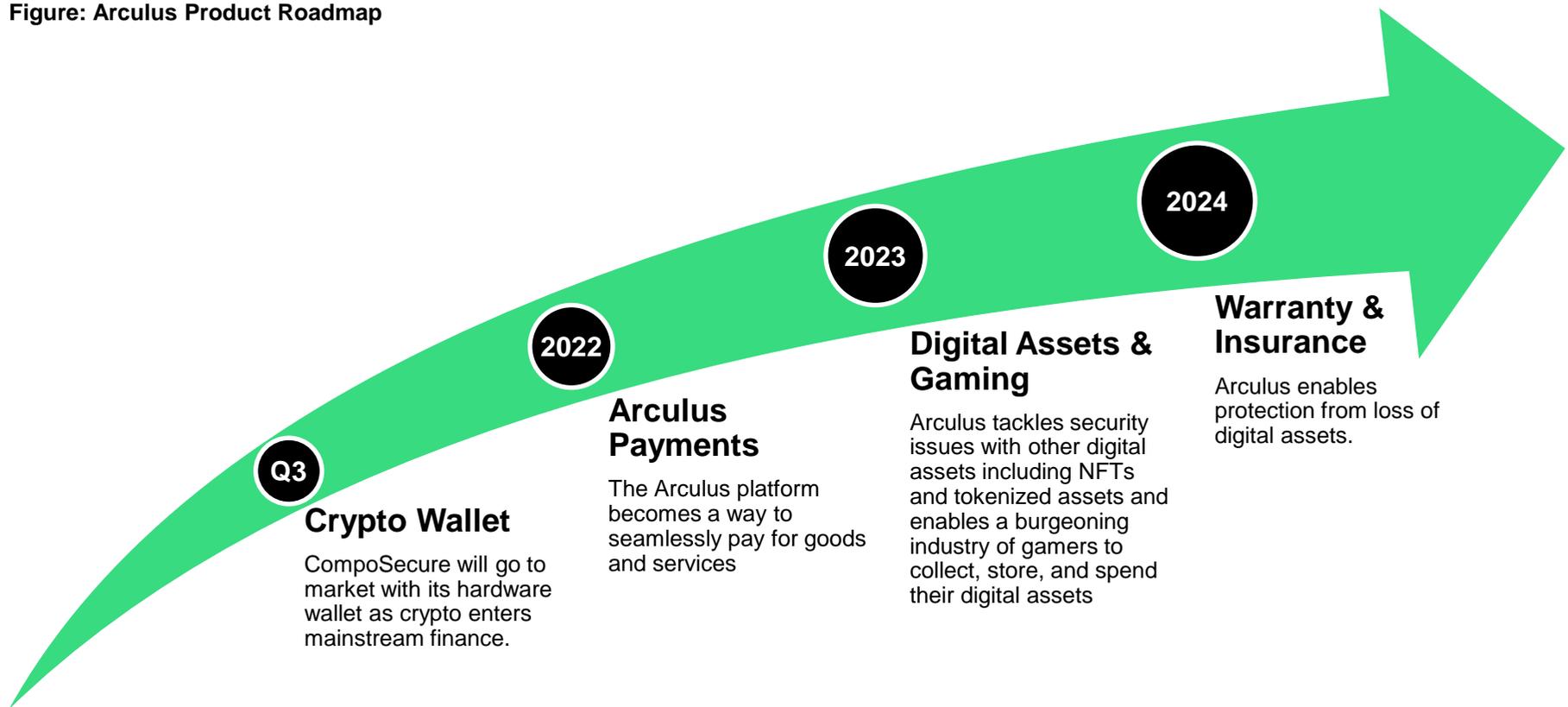
Source: Fundstrat, CompoSecure

Arculus Ecosystem Product Roadmap

Management's vision puts Arculus at the center of digital commerce

- Management's long-term roadmap for Arculus moves beyond wallet functionality and into payments, gaming, and asset insurance. If the Company can achieve adoption and user assets migrate to the Arculus platform, it could potentially serve as user's primary financial account.
- We view Arculus' unique form factor and mobile-first orientation to be a key advantage for moving into other verticals. Other hardware wallets are cumbersome and require a desktop to transact, which makes ubiquity as a payment application difficult to achieve.
- CompoSecure plans to internally develop the Arculus Platform but may also consider the acquisition of businesses and/or assets which might accelerate market entry for various elements of the Arculus Platform.

Figure: Arculus Product Roadmap



Source: Fundstrat, CompoSecure

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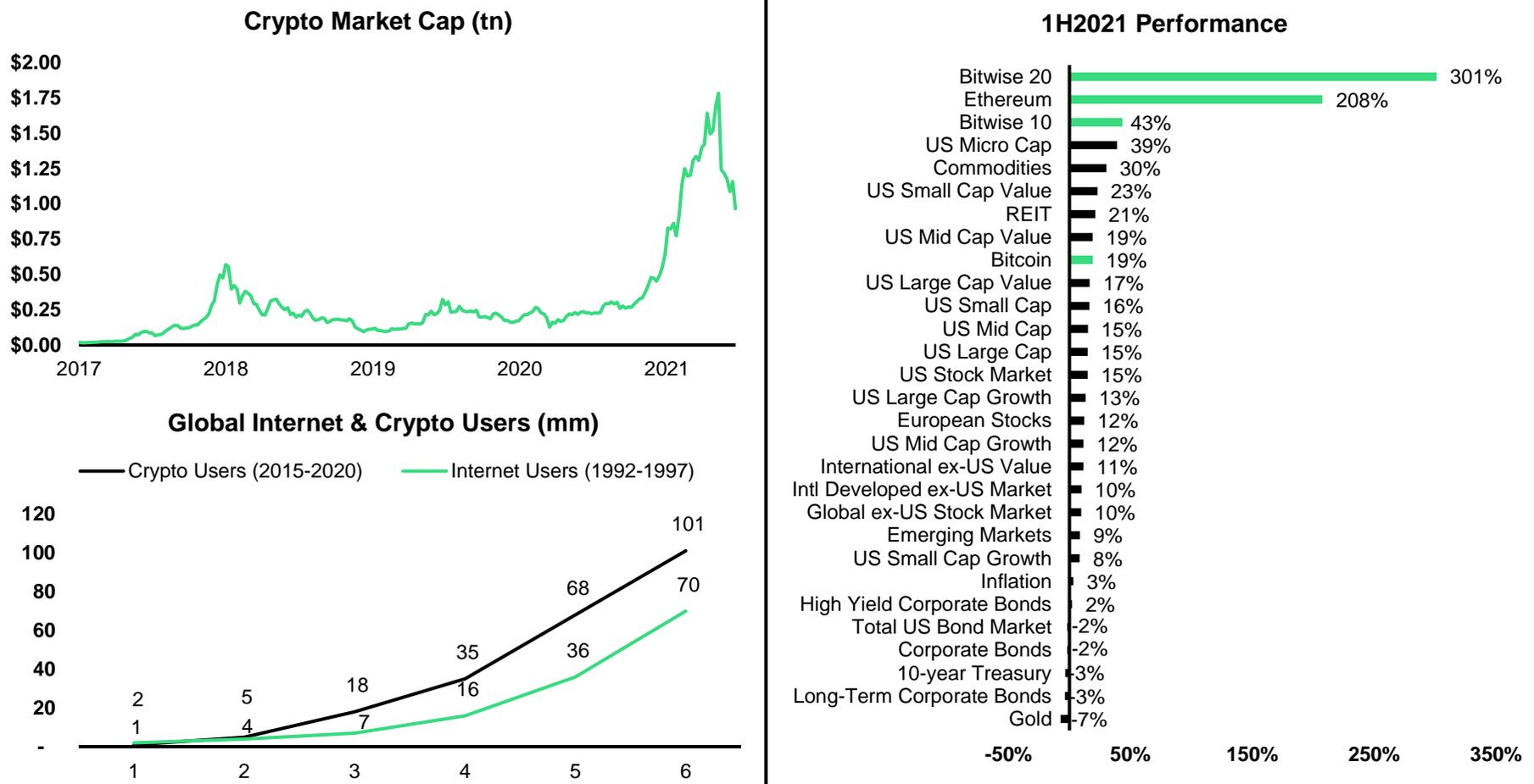
Appendix

Crypto is Shifting from Fad to Asset Class

Growth in crypto market cap and users reflect mass adoption

- The global crypto market has crossed \$1 trillion in total value and over 100 million users – putting crypto on a similar growth trajectory as the internet in the mid '90s.
- In the first half of 2021 crypto assets outperformed traditional financial assets, highlighting diversification benefits.
- El Salvador became the first country to make bitcoin legal tender paving the way for broader adoption.

Figures: Total Crypto Market Cap, Global Internet & Crypto Users, 1H2021 Asset Performance



Source: Fundstrat, University of Cambridge, Statista, Bloomberg

Crypto Growing Pains

The emerging asset class has not been a hallmark of security

- As both retail and institutional capital flows into the crypto ecosystem, incentives for bad actors to increase their hacking efforts increase.
- According to data presented by Atlas VPN, Q1 2021 was a successful quarter for cybercriminals. Hacked decentralized applications, crypto wallets, and exchange accounts had \$108.3 million stolen from them, a 46% increase from Q1 2020. This is largely driven by the recent bull run in crypto prices.
- According to data presented by Finaria, when factoring in all types of fraudulent actions, bad actors stole \$1.9 billion in 2020.

Figure: Headlines Related to Examples of High-Profile Fraud

A cryptocurrency exchange hack with a North Korean accent

The infamous Lazarus group's newest campaign is really hard to detect. Bonus: How cryptocurrencies, cybercriminals, and ramen noodles are connected.

Turkish Crypto Exchange Goes Offline, CEO Missing

The report by government-controlled Anadolu Agency comes a week after the country's central bank announced it was banning the use of crypto for payments.

Cryptocurrency News

Hacked Ledger Database Dumped On RaidForums

CryptoCoin.News - December 21, 2020

For Desperate Mt Gox Victims, Long-Shot Bitcoin Deal Beats Endless Wait

NEWS
by Sergio Gaschenko

11 hours ago

31505



FBI Warns Digital Currency Exchanges and Crypto Owners of Possible Threats

June 26, 2021
3:09 PM EDT
Last Updated 16 days ago

Technology

S.Africa crypto exchange brothers disappear after client cash vanishes, lawyers say

Source: Fundstrat, CompoSecure, CoinDesk, Reuters, Bitcoin.com, Atlas VPN, Finaria

Not Your Keys, Not Your Coins

Key ownership differentiates secure assets from vulnerable ones

- Custodial wallets enable you to buy, sell, and swap crypto, but they do not allow you to manage and store your own keys, leaving you subject to the security measures employed by the cryptoexchange and the corresponding app.
- Non-custodial “hot wallets” are left vulnerable because they are connected to the internet. This provides malicious actors with a gateway to your device and, consequently, your keys.
- Taking your keys off exchanges and storing them offline is the best way to prevent thieves from accessing your cryptoassets.

Figure: Examples of Typical Crypto Hacking Methods

Sim Swap

SIM swaps are an increasingly prevalent hacking method that occurs when a person gains access to your phone and locks you out with the intent to access any important or sensitive accounts. The hacker will collect info from a victim and call the victim’s phone provider pretending to be the intended target. The hacker then switches the victim’s mobile number to the number that corresponds to the SIM card on the thief’s phone and gains access to any saved passwords or multi-factor authentication messages.

Phishing and Malware

This is the most standard hack in the book and is the way that most cryptoexchange hacks occur. Phishing occurs when a hacker pretends to be a reputable entity in order to deceive a victim and collect their sensitive information. The most common phishing attacks employ fraudulent emails that convince the user to enter sensitive information into a fake website. While it may seem like this is easy to avoid, hackers have evolved to become very personalized and effective, and it only takes one slip up to compromise your assets.

Keylogging

Keylogging involves malicious surveillance software installed on a victim’s computer that records keystrokes typed. Hackers can employ this technology to derive crypto passwords, bank account login information, and more. Keylogging software can be easily installed onto a computer or a smartphone using links or banners or by disguising itself as a proper installation file.

Solution

These are just a few examples of methods with which malicious actors can access cryptoassets. The common denominator among all methods is that an offline (“Air-gapped”) authenticator that is in a person’s physical possession would prevent the hackers in the situations described above from getting away with any of the victim’s digital assets.

Source: Fundstrat

Demand is Evident

Search data and high profile fundraise point to increased demand

- Ledger, a leader in the hardware wallet market, recently received a round of financing that valued the company at \$1.5 billion. We touch upon the range of values of the Arculus business implied by this transaction on slide 27. It is important to note that Ledger was compromised by hackers nearly 12 months ago, leaking customer data to the cybercriminals. While no crypto was stolen, the fact that investors are participating in such a large round shortly after this event indicates to us that there must be insatiable demand for new hardware wallet solutions.
- By looking at Google trends over the previous 5 years, we can see that there was a relative increase in queries for crypto wallets during the 2017 bull run, but those figures were dwarfed by the search queries during the most recent bull run. This correlates with commensurate increases in wallet addresses and overall market cap of cryptoassets.

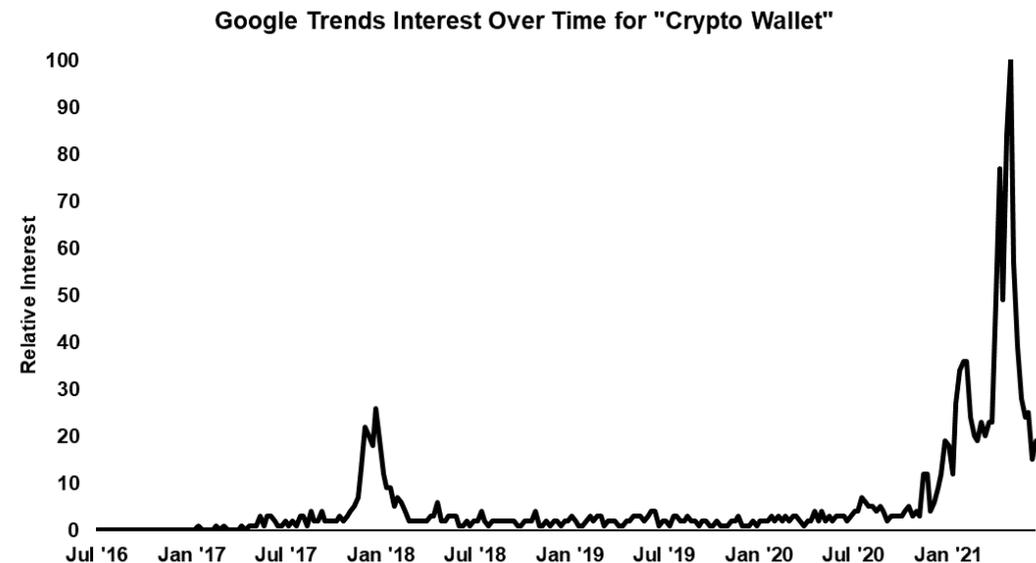
Figure: Ledger Fundraise and Google Trends

Hardware Wallet Maker Ledger Gets \$380M in Series C Funding Round

Funding will go towards furthering innovation of its hardware products and expanding its enterprise capabilities.



Ledger wallet (Ledger)



Source: Fundstrat, Google, CoinDesk

Demand is Evident

A key voice in the Bitcoin community pushes for a hardware solution

- Jack Dorsey, Square and Twitter CEO, and a Bitcoin evangelist, recently announced the Square will be launching its own Bitcoin hardware wallet for users to store and manage their own Bitcoin keys.
- In Dorsey’s Twitter thread discussing the need for better wallet solutions, he implies that current solutions fall short for the average person due to the lack of a mobile-first orientation and the sacrifice of usability for security.
- While eccentric, Dorsey has a fiduciary responsibility to Square shareholders and therefore would not launch a product if there was not the potential for an economically beneficial outcome for his company.

Figure: Jack Dorsey and Bitcoin Wallets



Source: Fundstrat, Twitter, The Block

CompoSecure Positioned to Bring Arculus to Market

Unique product, strong IP, and key industry partnerships

Figure: Competitive Advantages of CompoSecure as it Relates to Bringing the Arculus Ecosystem to Market

Unique Product Backed by Seemingly Strong IP

The Arculus hardware wallet has a unique form factor and a mobile-first orientation which facilitates a user experience that directly addresses a key shortcoming of comparable hardware wallet products. These design characteristics set the product apart from any existing hardware wallets on the market.

Its novel technology is supported by a company with a lengthy track record of protecting trade secrets and IP related to metal cards and customized equipment. As of May 20, 2021, CompoSecure had more than 36 U.S. and foreign (utility and design) patents issued, more than 41 U.S. and foreign patent applications (utility and design) pending, and new technologies under development. While on a long enough time horizon, we would conclude that any technology is replicable, we do think it is important that this company and management team have an impressive history of maintaining a technological leg up on the competition.



Key Relationships & Unique Go-to-Market Strategy

CompoSecure has longstanding, trusted customer relationships with leading card issuers such as Visa, Mastercard, American Express, and China Union. Incumbent players in the crypto wallet space (Ledger, Trezor, etc.) generally do not have such relationships with established payments companies.

Management possesses a unique opportunity to leverage these outlets as sales channels, by either selling Arculus-branded products to card customers or by applying a white-label approach. As traditional consumer finance companies look to provide crypto and crypto-adjacent services, CompoSecure will be in an optimal position to utilize these strategic relationships as a key part of their go-to-market strategy.



We see similar examples of crypto industry players utilizing relationships with established players in traditional financial services to sell and distribute their products. For instance, digital asset management firm NYDIG, a subsidiary of Stone Ridge, has established a relationship with NCR to make crypto purchases available at 650 banks and credit unions, one of many partnerships they have established to service customers through a partnership model.

Source: Fundstrat, CompoSecure

CompoSecure Positioned to Bring Arculus to Market

Manufacturing capabilities, and strong unit economics



Figure: Competitive Advantages of CompoSecure as it Relates to Bringing the Arculus Ecosystem to Market

Manufacturing Scale

CompoSecure is a legacy hardware company that has perfected a secure manufacturing process for metal payment cards. The company has produced nearly 100 million metal payment cards to date, 20 million of which were manufactured in 2020. It owns a 173,000 square foot manufacturing facility subject to regular security audits. Such capabilities will enable the CompoSecure team to immediately respond to any sudden increases in demand for its Arculus Cold Storage Wallet.

Favorable Unit Economics

CompoSecure's legacy Payments Card business operates with an average selling price (ASP) of \$13 and has historically maintained a 44-45% adjusted EBIDTA margin. This demonstrates the Company's ability to produce massive quantities of a low-priced consumer product at a profitable rate. The Company plans to apply similar scaling techniques to the Arculus Cold Storage Wallet.

Currently, Management estimates an ASP of \$90 for the Arculus Cold Storage Wallet based on extensive market research. The wallets will be produced at margins that are slightly lower than those garnered by the payment cards business but are projected to ultimately approach the 35-37% range in the outer year of the 5-year forecast.

To stress-test Management's projections, we conducted a high-level sensitivity analysis in which we decreased Adjusted EBITDA margins for the Arculus business by 50% throughout the forecast period. This reflects a scenario in which the Company is unable to maintain its current projected cost profile. As demonstrated by the figure below, even a dramatic decline in profitability still results in rather palatable unit economics for the business.

	2021	2022	2023	2024	2025
Adjusted EBITDA					
Base Case	\$102	\$105	\$160	\$274	\$587
Sensitivity	\$93	\$88	\$159	\$227	\$397
Adjusted EBITDA Margin %					
Base Case	36%	29%	33%	32%	37%
Sensitivity	32%	25%	32%	27%	25%

Source: Fundstrat, CompoSecure

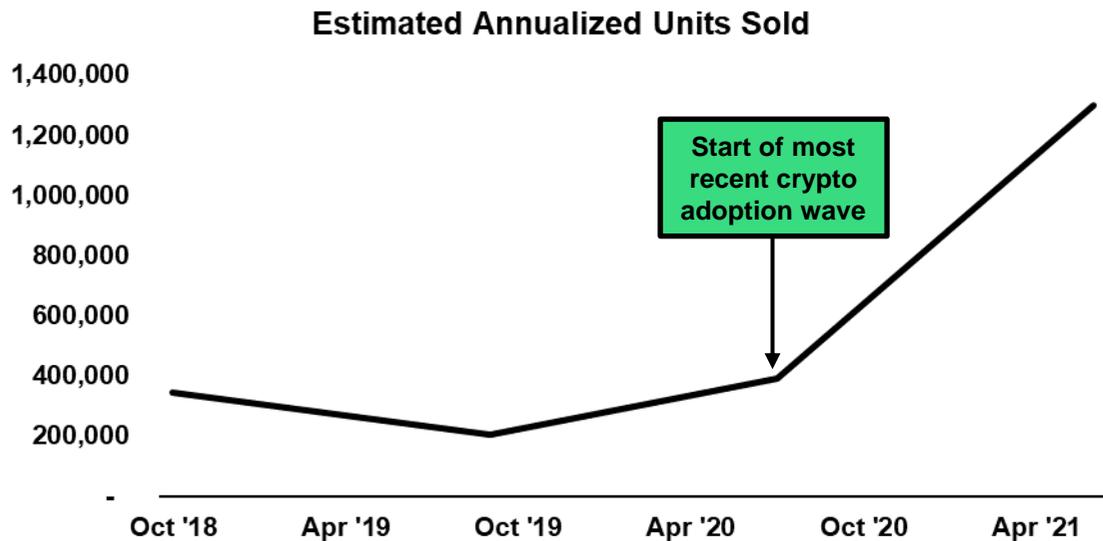
Illustrative Indication of Value from Ledger Transaction

Recent Series C financing round may imply a fair valuation for Arculus

- Ledger, a market leader in cold storage, raised \$380 million in a Series C financing round on June 10, 2021, led by 10T Holdings, implying a total enterprise value of \$1.5 billion for the company.
- Based on publicly available figures, we can estimate a range of multiples at which the company was valued and apply those multiples to the current forecast for the Arculus business.

Figure: Ledger Estimated Unit Sales

Ledger Sales Figures From Various Public Sources					
	Dec '14	Oct '18	Sep '19	Jul '20	Jun '21
Total Units Sold Since Inception	-	1,300,000	1,500,000	1,800,000	3,000,000
Units Sold Since Last Record Date	NA	1,300,000	200,000	300,000	1,200,000
Estimated Annualized Units Sold	NA	344,118	205,714	389,892	1,297,297
<i>% Growth</i>	NA	NA	-40%	90%	233%



Pictured: Ledger Nano S

Source: Fundstrat, CompoSecure, Ledger

Illustrative Indication of Value from Ledger Transaction

Recent Series C financing round may imply a fair valuation for Arculus

- We can imply trailing multiples from known performance metrics and derive forward multiples from growth rate assumptions of 100% and 50% for FY+1 and FY+2, respectively. We may be able to ascertain the reasonableness of the Arculus valuation based on the implied multiples for the legacy CompoSecure business.

Figure: Ledger Estimated Revenue and Illustrative TEV Calculation for the Arculus Business

Implied Revenue Multiples from Ledger Financing			
	Jun '21	Jun '22	Jun '23
Current Annualized Units Sold	1,297,297	2,594,595	3,891,892
% Growth	233%	100%	50%
Avg. Unit Price - Low	\$59	\$59	\$59
Avg. Unit Price - High	\$119	\$119	\$119
Annualized Revenue (\$millions) - Low	\$77	\$153	\$230
Annualized Revenue (\$millions) - High	\$154	\$309	\$463
Implied TEV from Series C Round (\$millions)	\$1,500	\$1,500	\$1,500
Implied Revenue Multiple - High	19.6x	9.8x	6.5x
Implied Revenue Multiple - Low	9.7x	4.9x	3.2x

To derive forward revenue multiples, we assumed forward growth rates of 100% and 50% for the theoretical FY+1 and FY+2 reporting periods, respectively.

Prices of the two primary Ledger products, the Ledger Nano S (\$59) and the Ledger Nano X (\$119). These prices set the bounds for projected Ledger revenue.

Since our growth assumptions were admittedly arbitrary, we conducted a sensitivity analysis. The lowest implied TEV from the table below is \$190 million, and the highest is \$700 million.

Illustrative Implied TEV of Arculus Payments & Crypto Solutions (\$millions)					
Period	Metric	TEV / Revenue Multiple		Implied TEV	
		Low	High	Low	High
FY 2021 Revenue	\$10	9.7x	19.6x	\$97	\$196
FY 2022 Revenue	40	4.9x	9.8x	194	392
FY 2023 Revenue	93	3.2x	6.5x	303	610
Implied TEV of Arculus Business (Rounded)				\$200	\$400

Arculus TEV - Growth Rate Sensitivity				
FY + 2 Growth	FY + 1 Growth	FY + 1 Growth		
		0%	100%	200%
0%	0%	\$700	\$375	\$270
50%	0%	\$545	\$300	\$215
100%	0%	\$470	\$260	\$190

Source: Fundstrat, CompoSecure, Ledger

Illustrative Indication of Value from Ledger Transaction

Recent Series C financing round may imply a fair valuation for Arculus

Figure: Illustrative TEV Calculation for the Legacy CompoSecure Business and Implied Share Price for Arculus (As of July 26, 2021)

Illustrative Implied TEV of Legacy CompoSecure Business (\$millions)		
	Low	High
Implied CompoSecure TEV from Merger	1,206	1,206
Implied TEV of Arculus Business	(200)	(400)
Implied TEV of Legacy CompoSecure (Rounded)	\$1,000	\$800
Implied TEV Multiples of Legacy CompoSecure		
FY 2021 Revenue	3.6x	2.9x
FY 2022 Revenue	3.2x	2.5x
FY 2023 Revenue	2.8x	2.2x
Median of Legacy CompoSecure Comps		
FY 2021 Revenue	9.4x	9.4x
FY 2022 Revenue	7.7x	7.7x
FY 2023 Revenue	6.9x	6.9x
Illustrative Implied Share Price of Arculus Payments & Crypto Solutions (\$millions)		
	Low	High
Implied CompoSecure TEV from Merger	1,206	1,206
Pro Forma Net Debt	(380)	(380)
Implied Equity Value of Combined Company	\$826	\$826
% of TEV from Arculus	17%	33%
Implied Equity Value of Legacy CompoSecure	\$138	\$275
Pro Forma Shares Outstanding (millions)	82.6	82.6
Illustrative Implied Price Per Share of Arculus	\$1.67	\$3.33

We can illustrate that the TEV range of \$200 - \$400 million for the Arculus business implies a FY 2021 revenue multiple range for the legacy metal cards business of 2.9x – 3.6x. This range is significantly lower than the multiples observed in the set of publicly traded comparable companies, indicating that the CompoSecure business is possibly being valued conservatively.

To back into an illustrative price per share of the Arculus business, we subtracted pro forma net debt of the combined company from the implied TEV of the combined company and then multiplied the resulting implied equity value by the % of TEV derived from the Arculus business to estimate the implied equity value of Arculus. We then divided that figure by the pro forma shares outstanding to determine a share price range for Arculus.

Source: Fundstrat, CompoSecure, Bloomberg. Comparable companies include: Cognex Corporation, SolarEdge Technologies Inc., Universal Display Corporation, Shoals Technologies Group, Roper Technologies, TransDigm Group, Zebra Technologies, Dolby Laboratories, and Mercury Systems Inc.

Key Risks to Consider

Adoption, competition and regulatory hurdles

Figure: Risks to the Arculus Ecosystem

Regulatory Risk

Regulatory authorities around the world are constantly amending and updating their views on how to regulate cryptoassets. There are possible scenarios in which a government presiding over a large economy that Arculus serves will be subject to further regulation, and there may be a consequential decline in appetite for cryptoassets due to the difficulty of acquiring cryptoassets. There may also be unforeseen licensing, audit, or registration costs that are incurred by the CompoSecure due to changes in governmental frameworks. While we do not share the view that governments can stop the crypto industry, they could stall a centralized company operating in the crypto space long enough for that company to become insolvent.

Adoption Risk

As with any burgeoning industry, there is the risk that a market does not develop beyond the high point of the current bull market. The growth that is priced into the Arculus model contemplates a large market of mature crypto investors that want to securely and effectively custody their own assets. Should industry growth be stunted for whatever reason, then the Arculus business would lag projections.

Competition Risk

As evidenced by the preceding slides, Arculus is not the first hardware crypto wallet to market, and certainly will not be the last. Should an existing player in the crypto ecosystem be able to replicate Arculus' seamless user experience coupled with effective security measures, Arculus could be facing significant headwinds in bringing a brand-new product to market.

Revenue Concentration Risk

American Express and JPMorgan Chase represented approximately 72% and 77% of CompoSecure's net revenue for the year ended December 31, 2020 and quarter ended March 31, 2021, respectively. CompoSecure will also seek to leverage these key relationships in bringing its Arculus ecosystem to market. If either or both of these relationships were to deteriorate in any way, both the legacy payment cards business, and the new crypto offering could be adversely affected.

Source: Fundstrat, CompoSecure

Executive Summary

CompoSecure Overview

Arculus Overview

Investment Opportunity

Appendix

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