Beware of Crypto Frauds

"It's a nonproductive asset. It has no intrinsic value. It's a breeding ground for 'charlatans' who take opportunities to rip off people trying to get rich in something they don't really understand." – Warren Buffet

"This is Pete, our cryptocurrency expert."

I am not a cryptocurrency expert, but I do have an opinion on this commodity-like instrument. Ultimately, I believe it will end in tears, as I find it hard to believe powerful governments, such as the United States of America will stand by and willingly give-up control to tax, spend, and create money. The U.S. Dollar is the world's reserve currency, and its status provides benefits far beyond economics.

Many participants in the cryptocurrency market are true believers, but there are also a significant number of players who will prey on humanity's collective greed. Get rich quick operators are abundant in this space, as are criminals whose sole purpose for dealing in this market is to monetize their illicit activities. It's just a matter of time until the hammer comes down.

Greed clouds judgement, and this is what I believe is going on with this current mania. Buyer beware – if it appears too good to be true, it probably is.

Please see the below article courtesy of The Wall Street Journal.
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Crypto Frauds Target Investors Hoping to Cash in on Bitcoin Boom

FTC says consumers have reported losing more than $80 million to crypto-investment scams since October

By Alexander Osipovich
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Scams are running rampant in the cryptocurrency markets as a huge rally in bitcoin, a lack of regulation and the anonymity of digital money have created a ripe environment for fraudsters.

Consumers reported losing nearly $82 million to crypto scams during the fourth quarter of 2020 and first quarter of 2021, more than 10 times the amount from the same six-month period a year earlier, according to the Federal Trade Commission.

From October to March, the price of bitcoin jumped 450% to nearly $59,000, while rival coins such as ether and dogecoin also surged. Bitcoin has since retreated to around $36,000, still substantially higher than where it traded for all of last year.

Scammers have targeted everyone from small investors scouring social media for investing tips to the Wall Street veterans who backed an Australian crypto-fund manager recently charged with running a $90 million fraud.

Sebastian, a 28-year-old pharmacy technician, is still kicking himself after he lost about $10,000 in ether to a crypto venture whose anonymous creators vanished in May, leaving behind hundreds of unhappy investors.

The creators of "LUB Token" purported to be building a crypto exchange based on the Telegram messaging app. On their now-defunct website and in a press release distributed on multiple crypto websites, they touted LUB, a new cryptocurrency that promised daily returns of up to 10%.

Sebastian, who lives in the suburbs of London, said he normally researches crypto projects carefully before investing, but he broke his own rule and dove in. He made several deposits into a digital wallet controlled by LUB and even plugged the venture on Reddit himself before others warned him it was a scam. By then it was too late. Unlike credit-card purchases, crypto transfers generally can't be reversed.

"I feel ashamed and still can't get my head around how stupid I was," said Sebastian, who asked that his last name not be published so he wouldn't be targeted by internet trolls.

Hundreds of people with similar stories, mostly in Europe, have since joined Telegram groups such as "LUB Token = SCAM !!!" An administrator of one group, who uses the name Tobias, estimated victims in Germany lost between €500,000 and €1.5 million ($600,000 to $1.8 million) to the scheme. German police are investigating complaints about the LUB scheme across the country, said a police spokesman in the city of Aalen, which received one complaint in May.

It is difficult to say how much money investors lose to crypto fraud. The FTC's figures are based on self-reporting by scam victims and largely limited to the U.S., so they likely reflect only a slice of total losses. CipherTrace, a blockchain analytics firm that tracks reports of crypto crime worldwide, says fraudsters are taking in less than they used to—from $4.1 billion in 2019 to $432 million during the first four months of this year. CipherTrace's tallies for 2019 and last year were elevated due to the exposure of a few large Ponzi schemes in Asia.

Still, CipherTrace says fraud is surging in the buzzy area of DeFi, or decentralized finance. DeFi is a broad term for efforts to provide financial services—such as lending, asset trading or insurance—using blockchain, the technology behind bitcoin.

DeFi projects offer yields on investors' crypto assets far higher than conventional interest rates, and even some legitimate DeFi projects are run by anonymous teams. That makes it easy to carry out "rug pulls," a scam in which unscrupulous operators raise money for a project, only to abscond with investors' funds.

From January through April, DeFi fraudsters stole $83.4 million, more than double the haul from all last year, according to CipherTrace. DeFi has "exploded and there are a lot of innovative products, but it's also ripe ground for fraud," CipherTrace CEO Dave Jevans said.

Fraud frustrates crypto advocates who have pushed for mainstream acceptance of digital currencies.

"Bad guys are always going to follow the money," said J. Christopher Giancarlo, a former chairman of the Commodity Futures Trading Commission who is now on the board of crypto startup BlockFi. “As the industry matures and surveillance tools get better, hopefully the cops will catch up.”

Even sophisticated investors can fall victim to crypto frauds. In February, crypto hedge-fund manager Stefan Qin pleaded guilty to one count of securities fraud. In a New York federal court, the 24-year-old Australian confessed he had lied to investors for years about the returns of his $90 million flagship fund, Virgil Sigma Fund LP. He now faces up to 20 years in prison.

Mr. Qin had claimed a near-perfect record of profitability, saying the fund made monthly returns sometimes greater than 20%, by arbitrage trading—using computers to exploit price differences between crypto exchanges. He was featured in an article in The Wall Street Journal in 2018, which repeated some of his false claims.

“Mr. Qin has accepted full responsibility for his actions and is committed to doing what he can to make amends,” his attorneys with law firm Kaplan Hecker & Fink LLP said in a statement.

Virgil drew dozens of well-heeled investors, with balances ranging from $103,000 to $5.7 million, according to one court filing. Two of those investors, who spoke to the Journal on condition of anonymity, are New York-area financial professionals who have worked for multinational banks.

In retrospect, the two investors said they overlooked a red flag: the fund never produced audited returns, a situation Mr. Qin chalked up to the nascent nature of crypto. “Being on the leading edge of the industry has put us ahead of regulators and accounting firms, and often there are no standard paths to follow,” Virgil told investors in a 2019 email.

Court filings show Mr. Qin came under pressure last year after investors sought to pull money from the Virgil Sigma Fund. In December, Mr. Qin urgently sought to withdraw money from a separately managed sister fund, Virgil Quantitative Research, telling its employees that he needed to pay off Chinese loan sharks, according to a Dec. 22 lawsuit filed against him by the Securities and Exchange Commission.

Alarmed employees alerted the SEC, triggering Mr. Qin’s downfall, a person familiar with the matter said. An SEC spokesman declined to comment.

One of the investors texted Mr. Qin after learning about the SEC’s lawsuit. In a reply seen by the Journal, Mr. Qin said he couldn’t discuss the suit. “It kills me to say that, but my firm belief is that things will be OK and the justice system will prevail,” he added.

Six weeks later, he pleaded guilty.

—Ruth Bender contributed to this article.

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Based on the recent price action, leveraged money appears to be short bonds. Broadly speaking, market professionals who utilize leverage are usually the first to bailout when price action fails to meet expectations. The recent rally in bonds smells of a positioning adjustment by short term traders.

From here, I think medium and long-term interest rates will stabilize and ultimately continue lower, as it becomes more apparent the inflation scare will turn out to be transitory. Should this play out as expected, low bond yields could provide good support for equity markets in general. The game plan is to stay the course. The stock market has legs to run higher.

ASSET CLASS & SECTOR OPINIONS		
OVERWEIGHT	**NEUTRAL**	**UNDERWEIGHT**
U.S. Real Estate & Related Equities	**Communication Services Sector**	**Energy Related Equities**
Large Capitalization Technology	**Healthcare Biotech & Pharmaceuticals**	**Financial Services Sector**
Consumer Discretionary Sector	**Healthcare Equipment**	**Consumer Staples**
Small Capitalization Stocks	**Mortgage Backed Securities**	**Materials Sector**
Aerospace & Defense	**Local Currency EMG Bonds**	**Leverage Loans (Floating Rate Debt)**
Leisure & Hospitality	**High Yield Corporate Bonds**	**Treasury Inflation Protection Securities**
Emerging Markets Equities	**Investment Grade Corporate Bonds**	**Gold & Gold Miners**
U.S. Treasury Notes & Bonds	**International Developed Market Equities**	

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Justin Kobe, CFA
Founder, Portfolio Manager & Adviser
Pacificus Capital Management

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