

ATLANTA BUSINESS CHRONICLE

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Bitcoin threatens payments sector



Digital currency
is entering the
mainstream.

BY PHIL W. HUDSON AND URVAKSH KARKARIA
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Digital currency bitcoin has crept out of the shadows of Silicon Valley basements and into the national spotlight. Venture capitalists – and billionaires – have bet more than \$100 million on the virtual currency, which

can be used to pay for vegan cupcakes and \$100,000 electric cars.

The momentum of cost-efficient digital currencies threatens to disrupt the payments processing industry that has built billion-dollar companies fattened on processing lucrative credit card transactions

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BIG DATA

STARTUP LUCENA TAKING ON WALL STREET



JOANN VITELLI

CEO Erez Katz: Software mines data to find trading strategies for investors.

BY URVAKSH KARKARIA
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Predictive analytics startup **Lucena Research**, armed with the imprimatur of one of Atlanta's most prominent super angels, is using software to replace "quants" – the math wizards who are the engines of the financial investment industry.

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COVER STORY



PHOTO/SPECIAL

Aerospace industry flies south

Georgia has added thousands of jobs, despite losing some key deals to Southern neighbors.

STORY BY Amy Wenk, 26A

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'Prank-vertising' can help companies distinguish their brands, or not.

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and fees. For metro Atlanta, a national payments processing hub, that disruption could hit hard.

More than 60 percent of companies in the payment processing industry call Georgia home, including **Total System Services Inc.** (TSYS), **Global Payments Inc.**, **First Data Corp.** and **Elavon Inc.** About 70 percent of all U.S. payments processed annually run through the state.

Bitcoin is a good alternative where credit cards don't work well, such as overseas e-commerce, or to pay for low-value items. Bitcoin is a faster and less expensive way to move money overseas than wire transfers.

Bitcoin is not issued by a government or bank, but "mined" by high-powered computers that solve complex math problems. Of the up to 21 million bitcoins that can be potentially mined, more than 12 million are in circulation. Bitcoins are stored in "digital wallets" and can be used to buy products and services from more than 20,000 merchants worldwide. Bitcoins are bought and sold on virtual exchanges such as Bitstamp or BTC China.

If digital currencies catch on – and it's a big if – the payments industry will be forced to pivot and embrace the new technology. For now, most are taking a wait-and-see approach.

"We have seen some interest from bitcoin people already, and I think there is going to be more," said **H. West Richards**,



H. West Richards

executive director of **The American Transaction Processors Coalition**. "Wisdom will be shared and relationships will be formed between the digital currency people and the payment processors."

Some of those "digital currency people" already call Atlanta home.

The largest bitcoin payment processor, **BitPay**, develops software tools that allow online merchants to collect payments over the bitcoin peer-to-peer payment network.

"Our goal is to be the First Data of bitcoin," BitPay CEO **Anthony Gallippi** said.

BitPay, which is backed by British business magnate **Richard Branson** and Hong Kong billionaire **Li Ka-Shing**, recently raised \$30 million in a round led by **Index Ventures**, with participation by **Founders Fund**, **Felicitis Ventures**, **RRE Ventures LLC**, **AME Cloud Ventures** and Atlanta's **TTV Capital**.

Bitcoin, while the most popular digital currency, continues to be buffeted by price volatility and controversy. In February, Tokyo-based **Mt. Gox**, one of the largest bitcoin exchanges, said it had lost 744,000 bitcoins to hackers. Mt. Gox closed, wiping out \$480 million worth of bitcoins held by its customers.

Bitcoin has not gone unnoticed by Congress and the Federal Reserve.

While digital currencies "may pose risks related to law enforcement and supervisory matters, there are also areas



SHUTTERSTOCK

Bitcoin is a good alternative where credit cards don't work well, such as overseas e-commerce, or to pay for low-value items. Bitcoin is also faster and less expensive than overseas wire transfers.

in which they may hold long-term promise, particularly if the innovations promote a faster, more secure and more efficient payment system," former Fed Chairman **Ben Bernanke** wrote in a letter to senators last year.

Others are not so sure. **Federal Reserve Bank of Atlanta** President **Dennis Lockhart** referred to bitcoin as an "interesting little experiment."

"In my mind it is very unlikely to become a substitute for the dollar," Lockhart said at **Mercer University** in February. "It could be a flash in the pan; it could be something that sticks forever."

Venture capital is bullish on bitcoin. Nineteen bitcoin firms in North America have collectively raised nearly \$100 million in venture capital, according to Boston-based **Aite Group LLC**. **Pantera Capital Management L.P.** has formed a \$147 million investment fund for bitcoin, according to **Bloomberg**.

Whatever the long-term prospects of bitcoin, digital currencies are having an impact on payment processors today. Bitcoin has added to the sense of urgency, and is causing financial institutions to feel a little less complacent about the current model, said **Kevin Hagler**, commissioner of the **Georgia Department of Banking and Finance**.

Bitcoin will add competitive pressure to improve the traditional payment processing systems, Hagler said.

"In fairness to the legacy systems, I think they were already working toward faster processing times, but digital currency may quicken their pace a bit," he said.

An Atlanta venture capitalist who invests in fintech and payments companies concurs. The established payment processors are taking a wait-and-see approach to digital currencies, said **Gardiner Garrard**, managing partner at **TTV Capital**. The venture firm recently raised a \$40 million Fund III from investors including TSYS and Global Payments.

Once bitcoins get market traction and user adoption, Garrard expects traditional payment processors to dive in.

"I think they will wait until there's real validity and traction," he said. "They'd rather pay up a little bit later [to get into the game] than to take the risk now."

Garrard doesn't see digital currencies eliminating the credit card processing business. When credit cards emerged, they didn't kill off checks, he said.

"What we've learned in the payments business is that more is better and it's not necessarily a zero-sum game," Garrard said.

Garrard views the payment processors as potential acquirers and partners, rather than competitors. By investing in venture funds, the payments behemoths are dipping their toes in the digital currency space and other technologies. Next, payment processors could partner with bitcoin-focused companies offering to resell services to their customers.

"If the digital currency gets mainstream adoption and regulations get buttoned up, then I think they'll start taking steps to enter the market," Garrard said.

One payment processing industry insider sees the bitcoin ecosystem as an evolution.

"I see the evolution being driven by the merchants, by the consumers, I see it being driven some by existing innovation happening in Silicon Valley, and I see it being driven by some innovation that is going to start taking place here in Atlanta," the source said, requesting anonymity. "Add all of those things up, and

the bitcoin investors may be pleased to know that the aspects of what they have invested in are indeed, at some point in the future, going to be used by the processors."

BitPay's Gallippi realizes the 800-pound payments industry gorillas are eyeing his turf. "They are starting to come to the conclusion that bitcoin is an efficient way to conduct a payment," Gallippi said. "The longer they wait to support bitcoin, the more traction that's going to give us ... to take advantage of the interest there is in the market."

If Gallippi is concerned about deeper-pocketed competition, he's not showing it.

"BitPay's advantage is that it has a three-year head start," he said. "If others were to start building a platform now for bitcoins, they would go through the growing pains and scalability issues that we had, and we solved, a long time ago," Gallippi said.

BitPay can compete on price and features, Gallippi said.

"Being a startup with a better technical solution and [leaner] operations, I think we can compete very well," he said.

Gallippi sees the legacy players as potential partners, or even acquirers, when they decide to get into the game.

"It's a possibility that someone like a First Data, or even **Visa** or **American Express**, could buy a bitcoin startup," he said.

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