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Silicon Valley catches Bitcoin fever

By Richard Waters in San Francisco

Silicon Valley is starting to catch Bitcoin fever – though the entrepreneurs and venture capitalists being drawn to the virtual currency claim that the biggest profits will come from using it to build a new digital finance industry rather than just as a vehicle for speculation.

Digital currency companies that have attracted early rounds of venture capital in recent weeks include Circle Internet Financial, headed by Jeremy Allaire, a serial entrepreneur from the media technology industry, and Ripple Labs, whose founder, Chris Larsen, was behind pioneering peer-to-peer lending company Prosper.

Prominent investors who have been drawn to the field include Jim Breyer, a partner at Accel and early backer of Facebook, as well as Google's venture capital arm, which has invested in Ripple and Buttercoin, a Bitcoin exchange.

Bitcoin's tech industry backers argue that the shared protocols and common technology standards on which it is based echo the open technologies that lie at the heart of the internet. That could make it the foundation for a low-cost, standards-based financial system independent of the traditional banking industry.

"It reminds me of the internet protocols in the mid-1990s," said Mr Breyer, who is also a director of retailer Walmart. Bitcoin was an "enormous ecommerce opportunity" for merchants, because it could greatly reduce transactions costs and make it easier to buy online, said Mr Breyer, who contributed to a \$9m investment in Circle – the biggest first-round financing for a payments start-up, according to the company.

"It's sort of like we're in 1996," said Mr Larsen. That could make possible the same sort of disruption in finance that the media and communications worlds faced with the rise of the internet. While riding the Bitcoin wave, his company has also created its own virtual currency, Ripples.

An open digital currency platform made it possible for start-ups to create a wide range of financial applications, similar to the way companies such as Google broke into the media world by building on the internet's HTTP protocol, Mr Larsen said.

However, Silicon Valley faces a number of hurdles if it wants to take a lead in the creation of a virtual financial system. Regulators in the US have been more cautious than in other countries, making banks nervous about setting up accounts for Bitcoin companies and putting a chill over investment in the new field.

Brazil, Germany and Russia had taken a more open stance, contributing to a wave of Bitcoin exchanges and other virtual currency start-ups in those countries, said Micky Malka of Ribbit Capital, a Silicon Valley investor in financial services. China has become the focal point for much of the innovation, according to venture capitalists, given the speculative investment frenzy there and lower penetration of traditional financial services.

Silicon Valley's Bitcoin start-ups claim that comments by regulators at a Senate hearing two weeks ago show that US attitudes are changing. In written testimony, Ben Bernanke, chairman of the Federal Reserve, said virtual currencies held "long-term promise" for innovation in finance, though they also raised the risk of money-laundering and other crimes.

The bubble

Fans say Bitcoin's open protocols make it possible for payments to flow as freely and cheaply as email, leading to a race to build low-cost payment systems founded on the virtual currency. Entrepreneurs such as Mr Allaire

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at Circle say this gives merchants a strong incentive to adopt the currency, in that they would escape charges from payment card companies. “There’s an enormous 3 per cent tax on a large share of the world’s payments,” he said.

- Jim Breyer, Accel

For consumers, using currencies like Bitcoin could present a way round fees and foreign exchange costs, which consume up to 10 per cent of international remittances, said Mr Larsen.

Meanwhile, the huge volatility in the Bitcoin price, which soared above \$1,000 last week, has created a headache for start-ups that hope it will come to be seen as a stable and widely accepted medium of exchange rather than a speculative commodity.

“The bubble craziness of the currency was not a positive for me in any way,” said Mr Breyer at Accel.

The tech start-ups claim they will be able to sidestep into other virtual currencies should faith in Bitcoin evaporate. Some, like Ripple, have invented their own.

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