

\$KARATE: BEATEN UP ENOUGH

As long-term investors in the digital asset space, we love to see innovative web3 business models where tokens are integral to the functioning of the protocol, along with genuine real-world utility, organic user growth and strong retention. We believe Karate Combat ticks all these boxes at a highly attractive valuation and have recently built a position.

Founded in 2018, Karate Combat is a fighting league where viewers can back fighters ahead of events (roughly once a month) by voting with their \$KARATE tokens. In comparison to UFC, there is less wrestling/jiu-jitsu, and shorter rounds, which is designed to create a more exciting format for casual fight fans. The winners receive a ~5-10% increase in tokens (funded by treasury allocations) and the losers receive their full stake back but are slightly diluted by the associated [distribution](#). This process is described as 'up only gaming'. For further background on the project and the concept of 'up only gaming' we recommend this recent [podcast](#).

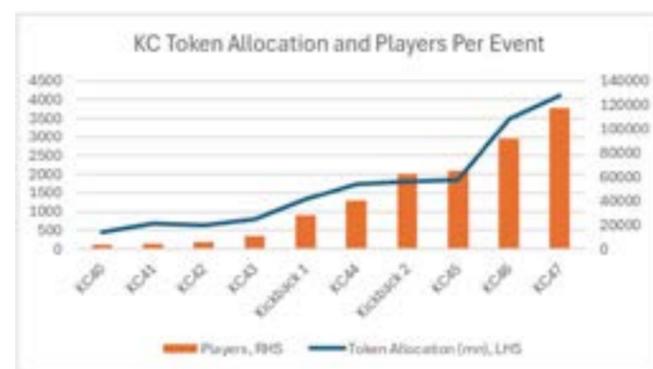
Up Only Gaming

Global sports betting is a \$50bn industry (according to Statista) and is growing at over 7% annually, with roughly 180m users. Boxing/MMA is also one of the strongest verticals at ~5-10% of total spend. But in a world of increasingly intense competition for user attention, sports franchises are trying to develop innovative ways to stay relevant to Gen Z viewers. These people interact with and consume media in a digital-first format and are disconnecting from cable/satellite bundles (major US cable providers lost around 5m viewers in 2023 according to Leichtman Research Group), but are increasingly likely to bet on live sports events. Data from the [Siena College Research Institute](#) suggests 39% of Americans Bet

on Sports and ~30% of Americans between the ages of 21 and 44 gamble on sports at least once a month (according to a 2022 [Morning Consult poll](#)).

We think the Karate Combat model resonates well with this target market (18-45 years old, predominantly male viewers), enabling users to 'wager' for free whilst watching non-paywalled fight content, which has shown strong viewer traction through similar non-web3 sports models like [UFC](#). The founders chose karate as their core sport given that fight leagues are generally easy to bootstrap and have strong fan engagement. This target demographic also has a high degree of overlap with crypto's core user base and the opportunity to win something of value via the token-based backing of fighters dramatically increases viewer engagement and retention. Viewers are encouraged to research the fighters and to become far more invested in and knowledgeable about the league. Furthermore, as viewers don't lose their stake, they generally don't leave after making incorrect initial picks and are more likely to remain engaged. This 'up only gaming' model is also only really viable on web3 as the token is used to bootstrap growth and liquidity, which wouldn't be practical for a web2 business.

Since the app went live in mid-2023, KC's KPIs have shown strong initial momentum as shown below. Recent events have seen \$3-4m staked (over 10% of circulating supply) and the Dubai event in March had over 50 million views, according to the team.



Source: karate.com/dashboard

Revenue model and valuation

The underlying gaming model has a zero take-rate, but the DAO receives revenue in various forms,

from host cities for the fights and increasingly from sponsorship deals. We believe total annual revenue is currently in the region of \$10m+, although costs are likely meaningful given the cost of hosting the events. While the content is not currently monetized, we understand the league has been in discussions with various major streaming platforms and may look to introduce some form of content monetization in future. The team is focused on ensuring any such monetization is managed in an affordable, low friction manner to avoid discouraging user engagement. Importantly, this revenue accrues to the DAO, as the league is owned by the Sensei Foundation, a non-profit organization owned by the DAO.

The founders also see potential in launching the 'up only gaming' model for other sports on the Karate Combat platform, along with potential spin-off revenue initiatives. This could for example take the form of fan tokens for the fighters, possibly with associated airdrops for \$KARATE holders, along with other initiatives to further monetize the Intellectual Property, such as video games.

To give some context around the long-term blue-sky potential, UFC was valued at \$11.3bn in April 2023 and generated revenues of \$1.3bn in 2023 through live events and promotions. Parent TKO Group (which also owns WWE Wrestling) had 2023 revenues of \$1.7bn and an adjusted EBITDA margin of 29%. As another example of a first-class sports league, F1 had 2023 revenues of \$3.2bn, up 25% YoY, with their DHL sponsorship deal bringing in \$40m alone.

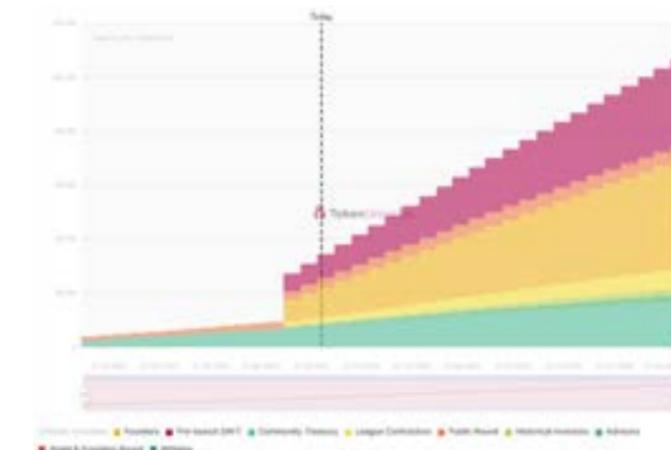
With greater mindshare, we broadly feel annual revenues of \$50m+ are realistic for Karate Combat over the next few years. Applying a 20x P/S multiple gets us to >\$1bn FDV or >15x upside and for context, FDV reached \$700m in January this year. We understand that a portion of these revenues would ultimately be in the form of \$KARATE token purchases on exchange, likely with subsequent transferal to the DAO, thus creating meaningful buy pressure and value accrual for token holders. In the extreme right tail scenario of KC achieving the traction of a UFC, we believe the upside could be 10-20x this number. Overall, in our opinion at \$70m FDV, we see the EV as highly asymmetric on a 2+ year horizon.

Price action and vesting FUD create compelling entry

Yet despite this long-term potential and the fundamentals going in the right direction, \$KARATE's market cap is only \$17m (FDV \$70m). The token has been particularly weak in recent months, following a strong run in Q4. This was likely due in part to profit-taking ahead of the first major unlock this May, but \$KARATE is now only slightly above its Q3/23 all time low, as shown below.



Source: TradingView (19/07/24)



Source: token.unlocks.app (19/07/24)

With regard to the first unlock in May (16% of total supply), it appears from looking at on-chain movements that some of these tokens have been sent to exchange and we can also see this in the OBV line in the chart above (OBV, or on balance volume roughly reflects cumulative buy and sell volumes over time). But the net impact appears to be limited - since May, we can see only a ~\$200k increase in the main Kucoin exchange wallet (the major liquidity venue), a rough proxy for the net sell pressure. Overall, most of the

unlocked tokens appear to have remained unsold, which is encouraging. Going forward, we are facing ~\$2-3m of monthly supply, which is less than ideal, but we feel this is mostly priced into the valuation at this point.

On the subject of further token inflation, obviously the 'up only gaming' business model is dilutive by nature. However, the actual impact is fairly muted, with the annual Treasury allocation to winnings currently at around \$2m, or 2-3% of FDV. This also implies roughly 5 years of dry powder at the current valuation (as the treasury is 15.7% of FDV), so the model is reasonably sustainable. As the token price hopefully grows over time, this should also allow for smaller token allocations, or possibly partial reallocation of DAO revenues to the winners' pot instead. Ultimately, the \$KARATE holders will dictate the future path of important items including token inflation through governance votes.

Catalysts

Going forward, we see several upcoming catalysts:

- The KC events are becoming far higher profile, with the team planning regular events at major crypto conferences throughout the year and with well-known crypto personalities participating
- We understand the team is in conversations with major exchanges, which would help improve the liquidity (currently <\$500k/day), making the token far more investable for institutions
- As discussed, we think a streaming deal with a major network might be on the cards, along with further sponsorship deals
- The founder has hinted at introducing passive staking in a recent governance post ([link](#)) in response to community demand for a deflationary staking/burning mechanism

Conclusion

We think Karate Combat is a genuinely innovative, exciting business model where web3/token integration is a critical 'need to have' feature. The 'up only gaming' angle also captures viewer attention, and as viewers don't lose their stake they are likely

to remain engaged for longer, helping the league bootstrap attention and liquidity. The growth in viewers and staking allocations is encouraging, and we see significant momentum ahead. At these levels, the risk/reward is highly compelling in our view, and we see a credible scenario where FDV is well into the \$billions over the medium term. ■

DISCLAIMER: The content of this document is for information purposes only, you should not construe any such information or other material as legal, tax, investment, financial, or other advice. Nothing contained in this document constitutes a solicitation, recommendation, endorsement, or offer by Hivemind Capital Partners, LLC ("Hivemind") or any third-party service provider to buy or sell any securities or other financial or non-financial instruments in this or in any other jurisdiction in which such solicitation or offer would be unlawful under the laws of such jurisdiction. Nothing in this document constitutes professional and/or financial advice, nor does any information in this document constitute a comprehensive or complete statement of the matters discussed or the law relating thereto. All content in this document is information of a general nature and does not address the circumstances of any individual or entity.

About

HIVEMIND

Hivemind Capital Partners is a Web3 and blockchain technology focused investment firm.

Committed to institutionalizing digital asset investing, Hivemind combines crypto-native technology and expertise with institutional-grade risk management and practices. With a thesis-driven and multi-strategy approach, Hivemind unlocks the potential of digital assets to be an investable asset class by providing curated and scalable access to institutional investors.

Founded in 2021, Hivemind is headquartered in the US with a global presence.

hivemind.capital