De-Coding Crypto
Weekly Analysis

'All correlations go to 1'

March 18, 2020

In this week's issue, we look at last week's collapse in BTC price, explain what we can about it, and set out some guidelines for managing risk in the coming weeks.

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Our Market View

May you live in interesting times. No other way to put it – Armageddon. There is not a single coin in the market that isn't down at least 30% on last week right now, and given that it's indisputably been pushed there by the entire macro situation, there's precisely nothing to say that this is anywhere near where it ends.

We offer as full a discussion of BTC as it's possible to give in today's research. For alts, we will simply say this: the only small ray of sunshines were that a) as a class, they didn't dump quite as much as they historically have, b) there may be room for a couple to overperform the overall trend slightly (BCH in particular). Broadly, however, it's as we've long said: there is basically no alt that can resist BTC's gravitational pull, and even the recently least-correlated of them (XTZ and LINK being the big two) not only dumped but actually have outpaced BTC on the way down.

Please direct all enquiries about this week's research to jedwards@enigma-securities.io.

Major

Ticker	Price	7D	1M	6M	12M	Cap
BTC	5160.39	-34.37%	-46.65%	-48.39%	29.26%	94.3B
ETH	113.226	-42.48%	-55.96%	-47.33%	-17.17%	12.47
XRP	0.14355	-30.73%	-49.12%	-50.40%	-53.67%	6.29B
BCH	176.87	-33.22%	-56.48%	-43.26%	6.91%	3.24B
LTC	33.4194	-30.70%	-54.10%	-54.35%	-44.73%	2.15B
EOS	1.92499	-36.50%	-55.61%	-51.89%	-47.26%	1.77B

Selected

Ticker	Price	7D	1M	6M	12M	Cap
XTZ	1.34421	-46.94%	-56.01%	25.30%	88.38%	0.95B
LINK	1.83724	-52.64%	-57.11%	-2.12%	-20.67%	0.64B

'All correlations go to 1'

This is going to be a slightly shorter piece than usual this week. Of course, this is not because there is nothing to discuss, because clearly, there is a lot; however, the key thing is that we are not in a position where we can make any sort of grand prognostication anymore with regards to potential movements over any extended period, which makes things somewhat difficult. However, with regards to navigating the immediate future, there are a few points in particular that are worth covering.

First, the elephant in the room: Black Thursday. From $7800 to $3900 in 24 hours. This was a nightmare scenario, and went further than anyone could have expected, but we do have to note here: this has been a known risk for at least for a small while now. As our research last week discussed at length:

> A move below $7800 likely takes us directly to $7000 - in other words, we fully retrace the move up. The very act of getting back to $7000 in such short order in turn undermines $7000 as a support, and that point, we risk a 2018-style cascade that takes us all the way down to the $5500-$6000 range.

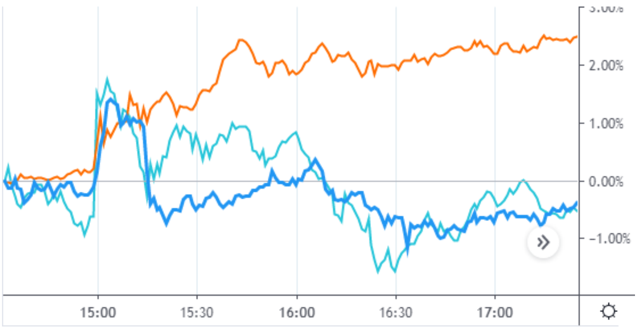
Credit: Tradingview. BTCUSD, Coinbase.

This ended up playing out in the ugliest possible way. We published that piece on the afternoon (UTC) of the 11th; we proceeded to test $7800 starting at around 4pm, bounce at it but test it again at 1am and proceed to lose it fairly decisively (which we will freely admit that we did not particularly anticipate), and in a single hour (10am on the 12th), we then went to $5600.

We then went even further at the Asian open, as traders and exchanges alike attempted to grapple with markets in which an outsized number of participants are excessively leveraged and where liquidity had been pulled off essentially all books.

We did then bounce fairly dramatically from there; as much as there's a slight ring of absurdity to calling a 25% drawdown in a hour 'controlled', it did not feel like a panic or structural issue in the same way as the latter move then did, and the fact that we entirely retraced it within hours rather demonstrates that.

However, we overall tend to see the movements on Black Thursday on the crypto markets specifically as something of an unloading of tension rather than a freak one-off. The BTC-equity correlation has been increasing over the last few weeks (we are sure that the fact that BTC's last big test above $10,000 - 19th February - coincided exactly with what looks to be very obviously the SPX's long-term all-time high will not be lost on future hindsighters), with the rate cut response on 3rd March (as discussed in our 4th March issue) serving as the biggest red flag that it needed to be watched more and more closely:



Credit: Tradingview. BTC in blue, GOLD in orange, SPX in cyan.

Since 19th February, BTC had been tracking incredibly closely to the SPX right down to raw percentage change:

Credit: Tradingview. SPX in blue, BTC in orange.

This never felt entirely sustainable in this sense: if the correlation between equities and BTC is to hold medium-term, why is BTC, a more naturally speculative instrument than even US equities, holding the same (or slower) pace downwards compared to them?

We tend to think that it was mostly being buoyed by the multiple technical and psychological support levels, and that the magnitude of Thursday's move and the associated loss of structure meant that we essentially saw the overflow of a week or two of negative pressure finally manifest itself. This, then, brings us on nicely to our next point: where do we go from here?

By far the most important thing to understand here is this: we are treating this, in essence, as a market with no real support levels. Technically, there isn't much down here anyway; we talked last week about how empty $6000-$8000 actually was, but where we are now ($4000-$6000) is far worse in that regard:

Credit: Tradingview. BTCUSD, Coinbase.

In any case, it barely matters. There is nothing that can be taken for granted right now. The essence of major BTC support levels have always been that, for one reason or another, there is likely to be significant demand for BTC at said prices - they represent levels at which they're collectively (and again, this is a retail-dominated market, so we are talking in terms of retail consumers here) held to represent an undercosted valuation for BTC.

Something we talked about a little about back in our initial issue on coronavirus (on January 29th), where we noted that one of the big concerns was that, because BTC is a) a speculative asset and b) incredibly easy to liquidate, it may run into problems if the virus spread in such a way to force mass city shutdowns and led to consumers needing to make inroads into savings. At the time, we said this:

> This is at least a valid enough point to be a concern, and the augurs of said demand will need to be read closely over the coming weeks. In general, though, we tend to think even this comes out at least neutral, and in likelihood positively, for BTC, at least in the short term; the number of people across both China and East Asia as a whole who are going to be caught up in situations that put significant personal economic pressure on them (e.g. city lockdowns) are going to be a fairly small proportion of the overall market even in worst-case scenarios, especially compared to the number that will instead see themselves with unexpected discretionary surpluses from lockdowns on travel and similar.

This does seem to have borne out to at least some extent in China, at least in terms of it not being a net negative; markets have been noticeably quiet during Asian hours over the last few months for the most part, standing in stark contrast to last year, but in any case, we did not see much noticeable downward pressure during the Chinese lockdowns. However, the difference is that China locked things down early enough to get some semblance of control over the situation (outside of Wuhan itself); the situation as it stands for the United States and Western Europe is far, far bleaker.

Pressure to liquidate assets on both a personal and institutional level (moreso personal with relation to BTC and cryptoassets) is now a real concern, but to bring back to the points about support levels: even if this doesn't happen (and it should be noted that on-chain data so far has suggested that liquidations of long-term holdings weren't really a factor on Black Thursday - we may talk about this in coming weeks, but for now, Coin Metrics' report is worth reading on this front), it's hard to see where new demand comes from on a mass scale.

With regards to providing something by way of a summary, here is what we would say:

1) The singular thing we are looking for right now with regards to regaining any sort of structure is 'the decoupling'; that is, the fading of the tight equities correlation. We are down 25% right now on the SPX, barely a technical bear market; there is still so, so far left to fall, and until conclusively proven otherwise, our assumption would be that BTC moves with it (there has been very little evidence of this being close so far).

2) As mentioned, there is no real floor. $4000 is unlikely to hold if tested, same probably for $3100; if there is a significant demand pool to emerge anywhere, it would probably be $2000-$2500. That is still not to say that we are guaranteed to go that low (since we could decouple, and equities velocity could decrease), but any risk calculation has to hinge on the possibility now.

3) Attempting to chart out longer theses right now is a fool's errand.

What we're reading

Bakkt raises $300 million Series B funding round (The Block): Something that's very, very important to note here that we've not seen too many talk about: the language of the raise announcement makes it very clear that Bakkt is treating its work in institutional-grade cryptocurrency solutions more as a proof-of-work (pun intended) than anything else. "Bakkt gives users control over their digital assets. Whether it's miles from your favorite airline, loyalty points from the local grocery store, or bitcoin you've purchased, the Bakkt app enables you to aggregate all of these assets into a single digital wallet. In just a few taps you can use those assets to shop at your favorite merchants, send them to family and friends, or convert them to cash." – they are driving overwhelmingly to becoming a retail-facing and retail-centric company. Lower expectations (and excitement about a crypto company raising $300m) accordingly.

Retail Investors Are Buying the Bitcoin Institutions Are Selling, Traders Say (Coindesk): This feels like one of those headlines that nobody except the subeditor and the SEO specialist is happy about having out there, but in any case, we should make clear: it's not a case of there being zero retail demand on these downward shocks. It's just a question of this: how many are going to be still willing to buy after each successive shock?

Wave Financial to Tokenize $20M Worth of Bourbon for New Whiskey Fund (Coindesk): "Known as the Wave Kentucky Whiskey 2020 Digital Fund, investors will be able to purchase asset-backed tokens linked to an inventory of whiskey barreled this year. Stored and maintained by the Wilderness Trail Distillery, Wave estimates that the fund will represent as many as 4 million bottles of bourbon." A really inventive project. Initiatives like these are small in the grand scheme, but going to be very important for setting the stage for the emergence of STOs over the next couple of years.

Bitcoin, Gold May Both Hit $1K in Race to the Bottom — Peter Brandt (Cointelegraph): We don't have the expertise on the ins and outs of gold specifically to pass judgement on whether this might bear out, but it's interesting to hear it being talked about in similar terms to what ended up happening with BTC last week.

Until next week – thank you for reading.

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