De-Coding Crypto

Enigma Weekly

2nd September 2020

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Our Market View

May you live in interesting times. At the time of writing, the table below is already slightly outdated; the market as a whole dropped somewhere in the order of 6% on most alts on Wednesday afternoon (slightly deeper on ETH, shallower on BTC) on a mixture of factors, principally relating to reports that South Korean exchange Bithumb had been seized by local authorities (in connection to a 2018 token sale).

In any case, an odd week. Very quiet for the most part from BTC – we did briefly touch above $12,000 again on Tuesday, but quickly slipped back below, and ultimately are trading in much the same range that we have been for a while now. Still looking towards a firmer break (above $12,200) for next leg up; closes below $11,000 and $10,500 would be concerning.

The elephant in the room, of course, is that market has been more led by ETH than anything else; even with today's drawdown, it remains the best-performing large-cap by far. Price at time of writing is around the $430 mark, which is a little worrying; it had taken out resistance at $440 yesterday (moving all the way to $490 at its peak), and we do want to see strength at that point again over the course of the next 24 hours or so to have short- and even perhaps medium-term confidence in bullish continuation.

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

Major

Ticker	Price	7D	1M	6M	12M	Cap
BTC	11581	1.74%	1.68%	30.12%	10.45%	214.0B
ETH	459.32	20.65%	17.13%	94.20%	158.80%	51.64B
XRP	0.2865	3.78%	-7.86%	21.60%	10.52%	12.89B
BCH	280.82	2.28%	-3.92%	-15.14%	-6.30%	5.20B
LTC	60.61	4.97%	3.31%	0.42%	-11.71%	3.96B
EOS	3.292	6.32%	9.14%	-9.41%	-7.35%	3.09B
Selected						
Ticker	Price	7D	1M	6M	12M	Cap
LINK	15.20	4.97%	79.09%	250.00%	758.60%	5.32B
ADA	0.1186	4.68%	-13.85%	143.50%	159.20%	3.08B
XTZ	3.250	-4.79%	6.33%	8.91%	219.80%	2.38B

Institutional latest: CME and Bakkt

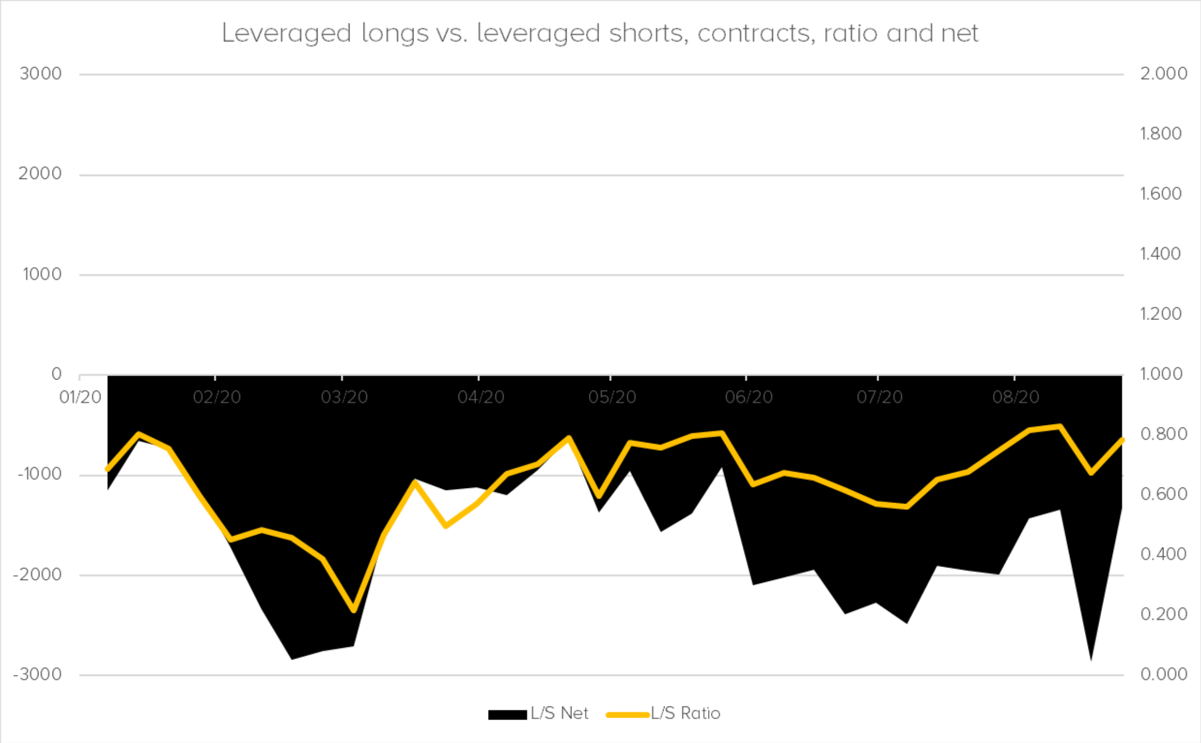
Open interest and volumes

As one would tend to expect, the break on $10,500 in late July almost immediately opened the floodgates with regards to open interest; positions on 28th July sat at 14,459 contracts ($797m at the day's close), up 51% in BTC terms and 76% in USD terms on the previous week. Since then, however, performance has been surprisingly sluggish:

Date	OI (contracts)	OI ($m)	Price ($, at close)
04/20 (avg.)	5733	206	7810
05/20 (avg.)	9778	448	8850
06/20 (avg.)	9748	467	9195
07/07/20	8635	402	9320
14/07/20	8726	406	9310
21/07/20	9603	452	9405
28/07/20	14459	797	11020
04/08/20	13460	765	11365
11/08/20	13969	787	11265
18/08/20	15501	934	12050
25/08/20	12444	702	11290

Data via CFTC.

The 14,459 contracts didn't quite represent a local high (18th August was slightly higher in both BTC and USD terms), but so far, it has been relatively close. It should of course be said that we are still sitting far higher than we ever have been before in both regards, but this is still slightly troubling. The most interesting component of said OI in the past has usually been positions from leveraged funds:



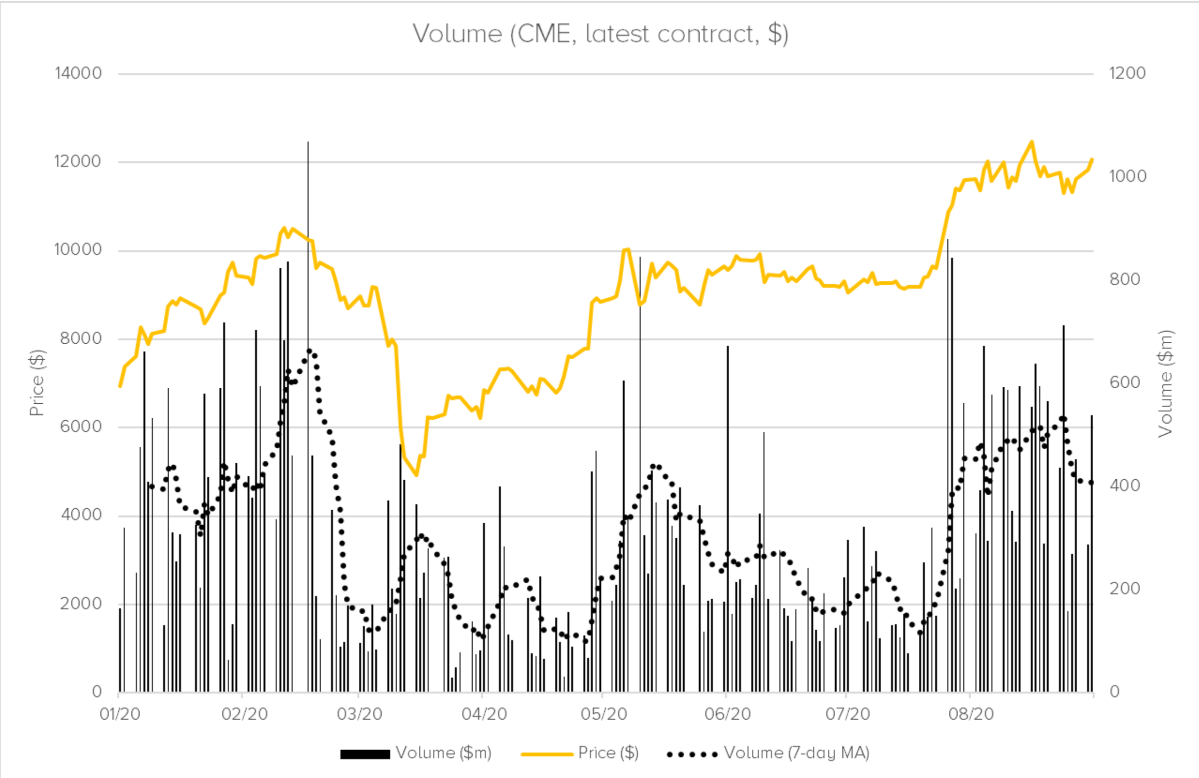
Data via CFTC.

For the most part, while still net short (as they almost always are), leveraged funds have been drifting longer since early July and especially after the move up, with the exception of the August 18th reporting period (just after the fakeout break of $12,200), where we briefly saw a record-breaking short position (8839 contracts short, -2858 net) which was wound back the following week (6160 contracts short, -1320 net).

The picture here isn't giving a strong indication with regards to pure directionality; the tendency in the past has more often than not been that such shifts are a counter-indicator generally (which would hence make the recent movements overall concerning), though that's been less reliable over the past few quarters than it was for much of 2018 and 2019.

That being said, the massive short shift before and after the $12k retest does tend to make us think that, even among those individuals and firms currently holding an overall bearish outlook in the short or medium-term, there's relatively limited conviction in any such retest going much deeper than it has in recent price action (technical long-term support is at $10,500; as it stands, we have seen hourly closes close to $11,000 in August, but have yet to go back below it).

With regards to trading volume:



Data via TradingView.

The break on $10,500 was the highest-volume trading day, but encouragingly, volumes in both BTC and USD terms remain some distance above that seen over the past few months (though, for the most part, below February in BTC); we would like to see slightly stronger sentiment at this stage in the quarter, but overall, this is reasonably positive with regards to sentiment (if not overwhelmingly so).

Trader count

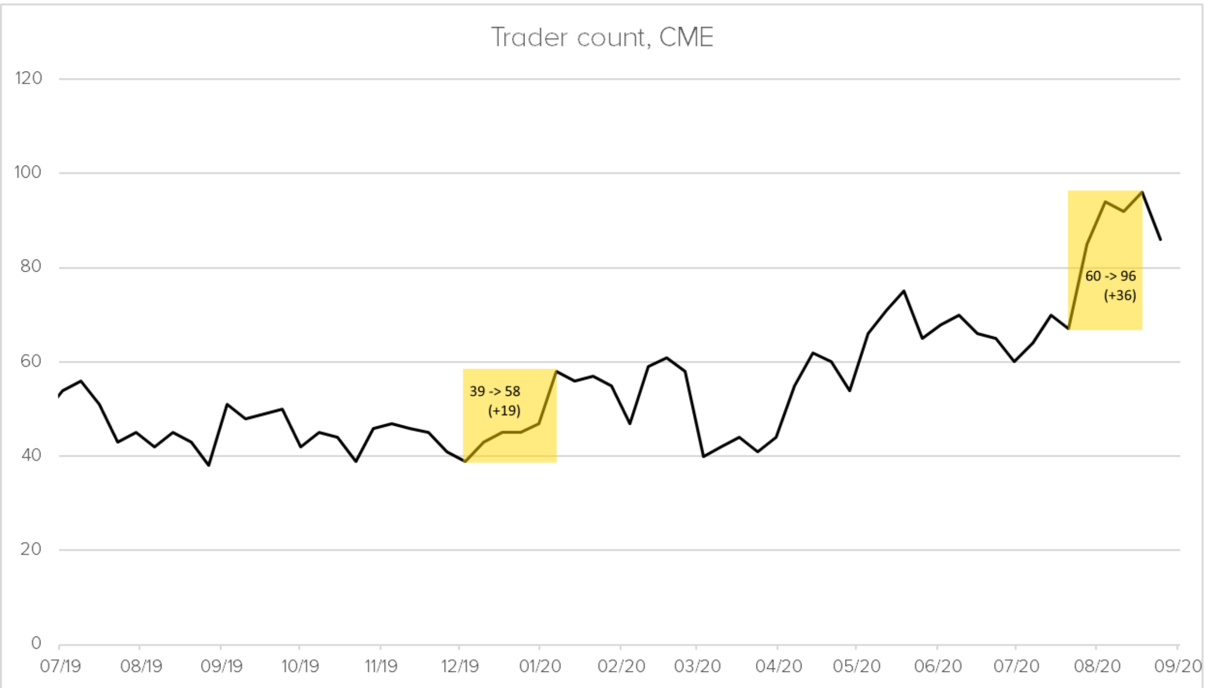
To give our usual explanation here: one of the unique things about CFTC reports and hence CME BTC products is that we get an exact count of certain categories of traders with open positions at given time; while imperfect, these figures tend to be interesting for what they tell us about the composition of the market and the inflow of new entrants.

The numbers over the last month or so in that regard are extremely interesting:

Date	Total	Lev. L	Lev. Sh	Other L.	Other Sh.
04/20 (avg.)	58	16	19	15	3
05/20 (avg.)	69	19	21	19	5
06/20 (avg.)	66	19	18	18	5
07/07/20	64	16	19	18	5
14/07/20	70	19	20	19	6
21/07/20	67	21	16	18	6
28/07/20	85	31	19	23	5
04/08/20	94	36	18	25	7
11/08/20	92	35	16	23	8
18/08/20	96	32	16	32	7
25/08/20	86	30	19	22	7

Data via CFTC. Highlight = new all-time high.

We would naturally enough tend to expect an inflow of traders on both a move upwards and a renewal of volatility in general; however, the scale here was extremely significant here, outpacing January in terms of raw count (as well as positioning):



Data via CFTC.

Apart from scale, the really interesting difference here was that we saw a huge jump in both leveraged funds and other reportables. Leveraged funds have typically made up the overwhelming majority of the market in both headcount and money; they still do so on the latter count, but at the moment, not on the former. For clarity, the CFTC definition of an 'other reportable' is as follows:

> Reportable traders that are not placed into one of the first three categories are placed into the “other reportables” category. The traders in this category mostly are using markets to hedge business risk, whether that risk is related to foreign exchange, equities or interest rates. This category includes corporate treasuries, central banks, smaller banks, mortgage originators, credit unions and any other reportable traders not assigned to the other three categories.

It's not particularly clear who hence comprises this influx of other reportables, though with regards to that question of hedging risk, we will note that that a large number of these new positions over the last few weeks have actually been on the short side, which is somewhat positive; sample size is small, but we have tended in the past to see the ratio skew longer before trouble (most notably with short postions being wound to precisely 0 in the March 3rd report).

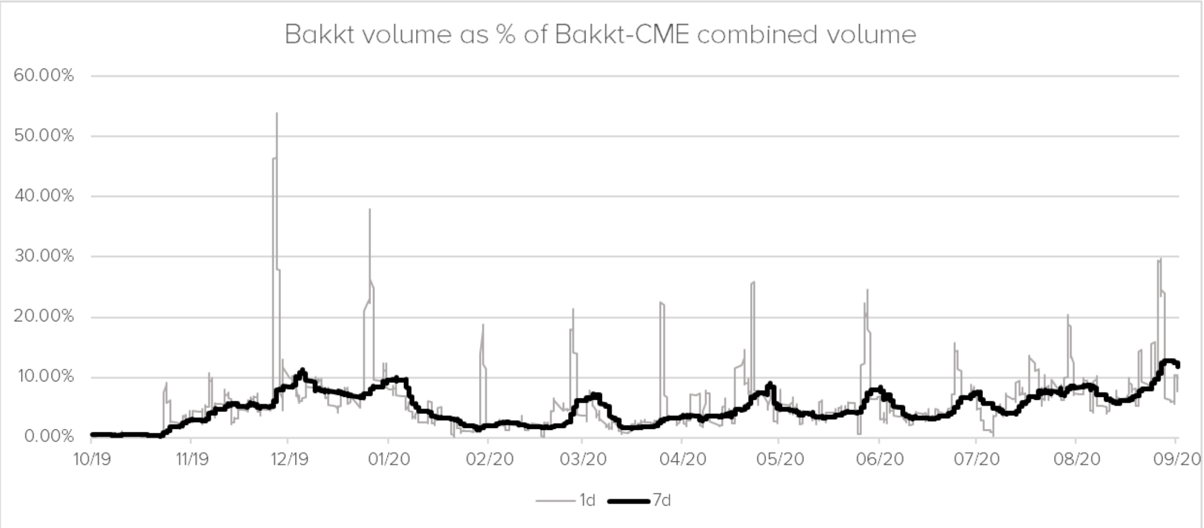
CME and Bakkt

Our tendency in these institutional pieces is to focus on the CME’s BTC products; however, there is of course another horse in the race, in the form of Bakkt. The overriding reason why we don't talk about Bakkt is that, quite simply, it has so far been something of a failed experiment.

The driving idea behind Bakkt was to become a full-suite entity that would become a hub for institutional crypto trading in the US (as emphasised by its focus on physical delivery and on providing an extremely expedited timeline between its futures launch and options launch) - the implicit proposal being, by doing so, that Bakkt would then be in a position to take market share away from rival offerings (i.e. CME, and at the point of genesis Cboe, products).

The fact that you likely have not heard about Bakkt since the new year probably tells you most of what you need to know. To be fair, there actually has been some very slight progress over the last few months, and if you had heard of Bakkt, it would likely be in the context of it setting an all-time high for volume on August 25th at 12,791 BTC ($148m) on the day.

It should still be said here that market share remains miniscule compared to CME; taking rolling 1-day and 7-day volume sums for both, we see that Bakkt peaked at under 30% of total 1-day volume (and even that being more a statistical artifact than anything else), and just 12% of 7-day:



Data via TradingView.

In addition, note that this is only concerning futures; Bakkt options have seen zero volume since mid-June, even as options markets on both the CME and retail venues have blossomed. We will continue to keep an eye on Bakkt, but it remains an extremely small component of the institutional market in BTC at this point and hence not of particular interest analytically (and it would be surprising to see that change substantially).

Conclusion

Our main takeaway from all of this is less about specific directionality and more about volatility. Even with recent struggles and pullbacks, we are still trading higher right now than at almost any point in BTC's history (the last four weekly closes were all higher than any other close since January 2018, including the 2019 rally); these are relatively uncharted waters in technical terms, and there can be a tendency (as we have shared at times at least) to overestimate potential velocity coming out of a given level.

It is probably time to reassess those theses somewhat, or at least better define them (we did share not exactly dissimilar sentiments in the August 19th issue). Our overall view on BTC is still best defined as bullish, especially looking towards 2021; nothing has changed with regards to the factors in its favour (tailor-made macro environment, institutions seeing enough of a track record to handle it, constriction of supply post-halving). However, we would on the whole tend to say that expectations should probably be tempered somewhat for how quickly we move in each stage until we start seeing more concretely positive indicators with regards to sentiment.

The most encouraging directional sign that we saw in the CFTC data was with regards to trader count; even then, however, the tendency would be to think that this more speaks to slightly further down the road, perhaps even as late as Q1 2021. Institutional interest is quietly, appreciably growing, but the reality is that interest is no longer enough; it needs to translate to further inflows for any sort of major move, and while things may change very quickly, there hasn't been evidence of that happening recently as it stands.

Until next week – thank you for reading.

ABOUT US

Enigma Securities is a leading, regulated liquidity provider, offering its clients bespoke liquidity solutions through the use of a proprietary electronic trading platform and API access.

The firm was founded in 2017 as a subsidiary of Makor Partners Limited (UK), amid growing institutional demand for digital asset trading. Looking to seize the new, exciting opportunities presented by cryptocurrencies and blockchain technology, Enigma became one of the first regulated brokerage firms to set up banking relationships and custody solutions to meet institutional standards.

Since its launch, the firm has expanded its capabilities to the broader Fintech arena, leading innovation while working to bridge the gap between the traditional financial services industry and cryptocurrency markets.