ENIGMA SECURITIES

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2 October 2019

The Enigma Weekly

De-Coding Crypto

Our Market View

May you live in interesting times. All eyes were on the possibility of a second shock towards the end of last week, and it did happen – but, crucially, lower supports were not realistically tested, and BTC settled at and around $8000, and at the time of writing has been settled between $8100 and $8400. With worst-case scenarios no longer on the table, we look primed for a consolidation going forward into Q4; the precise nature of that consolidation remains unclear, but we expect the tells to start surfacing across October. We have particular eyes towards conference season for miners, and the evolution of production variables, over the next month or so. We do, however, believe that the potential magnitude of the upside is growing, especially looking past Q4 and into Q1 2020.

In this week's issue, we take a look at one of the more interesting price patterns of the last week – Ripple – and how it relates to social media and the production of a narrative. We also discuss the future of the 'privacy coin', and whether it can find a home as currently constituted in a 2020 cryptocurrency ecosystem.

Performance Snapshot as of 14:30 GMT 2/10

Name	Ticker	Wk Close	Change 7D	Change 1M	Market cap
Bitcoin	BTC	8248.11	-2.23%	-20.63%	148,164,000,000
Ethereum	ETH	177.16	4.10%	-0.78%	19,127,000,000
Ripple	XRP	0.25	2.34%	-3.57%	10,887,000,000
Tether	USDT	1.00	-0.13%	-0.16%	4,113,000,000
Bitcoin Cash	BCH	223.81	-1.86%	-23.79%	4,037,000,000
Litecoin	LTC	55.80	-3.03%	-16.80%	3,537,000,000
EOS	EOS	2.96	3.10%	-10.93%	2,766,000,000
Binance Coin	BNB	15.70	-2.28%	-31.12%	2,441,000,000
Bitcoin SV	BSV	83.80	-3.11%	-37.46%	1,498,000,000
Stellar	XLM	0.06	3.04%	-6.41%	1,187,000,000

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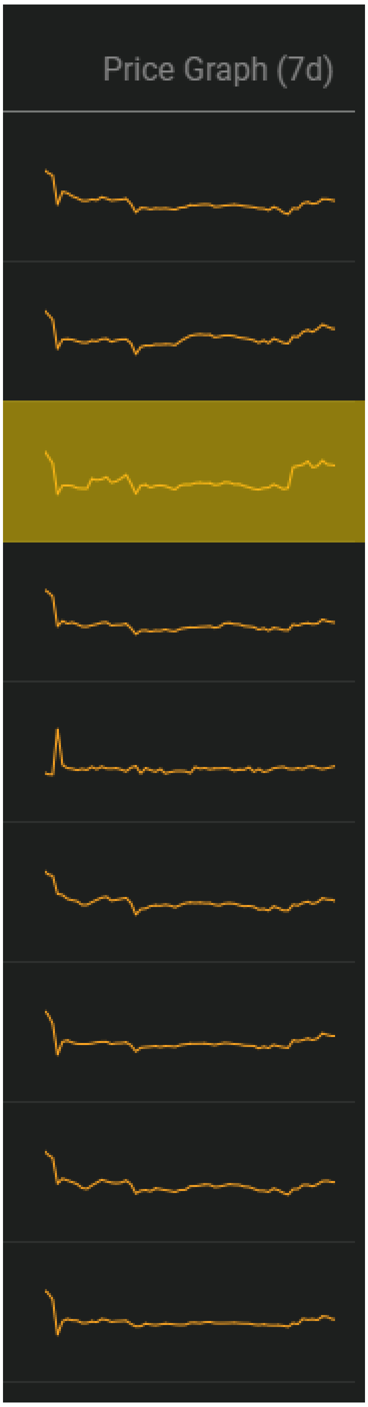
Ripple's bounce and the benefits of narrative

Monday morning in America opened to a rally across the markets, with practically all coins ending the day in the green – still down on last week, but still moving notably positively.

This was notable, but not all that exceptional; much of the movement can be ascribed to a mix of a rising tide effect, a cautiously optimistic reaction to [the announcement of the Crypto Rating Council (CRC)]() by a number of major exchanges, and a general correction as BTC and other markets avoided challenging that dreaded second support. Yet, there was one trend that stands out even to the most naked of eyes. The highlighted graph (right) is that of Ripple (XRP).

Ripple moved earlier than everyone else, and its gains - while still merely representing a return to its position just a week ago - came thick and fast, even compared to its closest structural and use-case contemporaries; EOS followed fairly closely, but XRP was the clear focus and the longest gainer in early trading:

Credit: tradingview.com. XRP in blue, EOS in orange, XLM in green.



Credit: coin360.com
Data as of 01/10 13:00

As it turned out, this would ultimately serve mostly to take it in line with the rest of the market a couple of hours later; XRP initially outperformed contemporaries, but fell back behind the following day. Yet, it remains of interest, precisely because it demonstrates just how much a good narrative can influence cryptocurrency markets still.

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There will be those even among the most knowledgeable actors in the space that will ask at this point: what narrative? There was nothing new to report about Ripple specifically over the weekend. Certainly, the coin looks to have been a beneficiary of the day's news; all coins that had been experiencing concerns over potential securities classification and SEC sanction (the significant ones being XRP, EOS, XLM, and TRX) saw significant gains as details over the initial ratings came out across late morning and early afternoon UTC. The light sanction for EOS by the SEC over potential securities violation further strengthened sentiments coming into Tuesday.

But why Ripple over EOS, LTC, or any other altcoin? There had been one announcement - a launch of operations in Iceland, and the acquisition of an Icelandic trading firm - but, while significant, we do not believe that this on its own should have moved the market.

The key to understanding goes back, across the weekend, and all the way to Thursday. On that day, Ripple's blog put out a short piece, authored by Global Head of Government Relations Michelle Bond, talking about a 'new' FCA report, and pointing to this:

> "Specifically, the FCA classifies digital assets as one of three types of tokens: exchange, utility and security. These classifications are critical because they define the use cases for each type of token. For example, XRP is classified as an exchange token because of its role in facilitating cross border transactions."

The FCA regulations, crucially, were not a new development; the guidance document referred to had come out on July 31st, and had been reported on extensively in the cryptocurrency press, though said reporting at the time had tended to emphasise the applicability to BTC and ETH more than XRP. Neither report seemed to alter the market significantly at the time; in the latter caseXRP had dropped, as all coins did, in Thursday's aftershock:

Credit: tradingview.com. XRP in blue, BTC in orange, ETH in green.

However, going forward, a narrative had been set - with continuing concern over XRP's status as a potential security (something that has been kept in the public eye by Brad Sostack's ongoing lawsuit), a safety valve was now presented - that being, a move away from the United States to a foreign jurisdiction. In truth, Bond's post is not exactly subtle about this:

> "So just as the U.S. helped lead on Internet regulations, the U.K. is taking important first steps to regulate digital assets and blockchain. There are a number of other countries around the world that have already proven friendly to blockchain technology—including Switzerland, Abu Dhabi, Thailand and Singapore—and many more that might take important cues from the FCA and co-learn their own regulations. "

By this, then, a piece of news that would typically have been completely overlooked appears to instead have been the catalyst for significant short-term movement.

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Monday would, in all likelihood, have been a good day for Ripple no matter what, given their market status and similar questions over securities status to EOS. We do, however, still think that the nature of their rise is of note, and represents a useful showcase in how developers in the crypto space can prepare the ground for market-altering narratives.

Privacy coins: a class unaccommodated

Monero, Dash, Zcash. Is there a way forward for the major 'privacy coins'? The augurs look increasingly grim, and it seems that the collective class of coins are coming to a state of sans domicile.

It is, simply put, becoming harder and harder for retail investors to even trade on most such coins by the day. The Financial Action Task Force (FATF) announced in June that it would allow a 12-month window (through to June 2020), among exchanges, for the full implementation of sufficient per-transaction information on the identity of all partners to comply with the 'travel rule' - a long-standing FATF regulation requiring banks and exchanges to track and share certain customer information in the pursuit of preventing cross-border money laundering.

For most coins, and most exchanges, this merely represents an inconvenience; for privacy coins, given that their entire use case is based around obfuscation of said information, this represents an existential threat. While FATF rules are not on their own binding - they represent recommendations for legislation among member countries and are not enforceable on their own - there is in general an expectation that exchanges will look to move towards compliance. The first major moves to this tune came in mid-September, with major South Korean exchanges OKEx Korea (on September 16th) and Upbit (on September 21st) both delisting.

On the one hand, this does not necessarily mean the start of the avalanche for international delisting. "Dark coins", as OKEx's report describes them, are a geopolitical issue in the context of the Korean peninsula; Monero in particular has become associated in both local and international media with North Korean cybercrime and money laundering initiatives. OKEx's international exchange as it stands will continue to offer the coins, and no other major international exchanges have as of yet moved to delist; in fact, Binance's Lending Service announced that it would expand to offer all three major privacy coins on September 17th, although this should be tempered by the context of Binance's involvement in a number of extremely aggressive expansions into new coins and products over the last month (including the opening of a new US platform, the listing of Tezos pairs, and an expansion into the Chinese OTC market upcoming).

However, even the loss of activity in South Korea could be enough to deal severe damage to a class of coins that already finds itself struggling. Privacy coins have always been, and continue to be, disproportionately traded in South Korea; as of Monday, Bithumb (the largest Korean exchange to not make moves towards delisting as of yet), according to Blockchain Transparency Institute (BTI) data, reported a 24h volume of $56m for DASH and $20m for XMR (compared to $39m for BTC and $6.5m for ETH).

Critics have complained of significant wash trading inflating volumes both for South Korean exchanges and for privacy coins as a class. BTI data lists XMR at a 91% wash rate, and DASH at 98%; BTC by comparison is at 49% (and ZEC, it should be noted, is only at 42%). A BTI report on September 23rd slammed OKEx for having one of the highest wash rates in the world - though OKEx has questioned the validity of BTI's research - and similar concerns have cropped up with Upbit in the past (the latest BTI report does now have Upbit among best-in-class now).

While some privacy coin developers - particularly Zcoin - have gone to lengths to stress their view that they are either currently able to comply with FATF rules, or that they can find a way to achieve compliance, on the whole it seems like there is little light at the end of the tunnel as it stands for privacy coins as a class. XMR in particular has shown significant losses over the last month, but all three find themselves down significantly against both BTC and other major coins, with no light on the horizon.

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If there is a future for privacy coins in the greater market in 2020 and beyond, it seems likely to be through Zcash with its opt-in privacy structure; even then, it remains a risky bet, particularly with development for Ethereum-based alternatives to privacy coins, such as Tornado Cash, remaining very much in progress.

Catalyst Calendar

02/10 – 03/10: b.Tokyo Blockchain Conference (Tokyo, Japan)
02/10 – 04/10: Disrupt SF (San Francisco, United States)
03/10 – 04/10: Global Blockchain Summit (Denver, United States)
07/10 – 15/10: Japan Blockchain Week (Osaka, Japan)
08/10 – 10/10: API:WORLD (San Jose, United States)
10/10 – 11/10: Crypto Games Conference Kiev (Kiev, Ukraine)

What We're Reading

Zcash Bug Could Reveal Shielded Full Nodes' IP Addresses (Coin Telegraph) – "A bug has existed for all shielded addresses since the inception of Zcash and Zcash Protocol. It is present in all Zcash source code forks. It is possible to find the IP address of full nodes who own a shielded address (zaddr). That is, Alice giving Bob a zaddr to be paid, could actually allow Bob to discover Alice's IP address. This is drastically against the design of Zcash Protocol."

Crypto Exchange Bithumb's $333 Million Acquisition May Be in Jeopardy (Coindesk) – "In October 2018, BTC Korean Holdings had agreed to sell 51 percent of its share in Bithumb to BK Global Consortium for $333 million. Since the deal was brokered, BK Global reportedly made a down payment of $100 million…However, the report said BK Global has again missed a Sept. 30 deadline for the final payment."

Asian Institutions Are Finally Warming to Crypto Hedge Funds (Coindesk) – ""The pace of [institutional] investor allocation to crypto this year has been much faster," said Jett Li, chief investment officer at BBShares who formerly worked at Bank of New York Mellon. "Demand for secure and efficient institutional asset allocation into crypto is quite strong.""

SEC fines Block.one $24 million for unregistered ICO worth billions (Engadget) – "According to the SEC, the company conducted the ICO between June 2017 and June 2018, raising several billion dollars' worth of digital assets, but did not register it as a securities offerings as stipulated by federal securities law. The SEC says this meant investors were not given the information they needed to make informed decisions. Block.one has agreed to pay the fine, but has neither admitted nor denied the SEC's findings."

Chinese Bitcoin Investor: CNH Tether Avoids USDT Regulatory Risk (Coin Telegraph) – Zhao Dong: "According to the ongoing discussions and measures being made by the central bank, authorities harbor a prudent and positive attitude towards the digitization of the Chinese yuan. It remains to be decided by the trends of policy, the grand economic environment and the market needs."

Why building a new protocol for money is the only way to truly change the game for people (Medium/David Marcus) – "Long story short, building on top of existing rails and across disconnected payment networks won't reduce cost, open up the market to more innovation, nor lower the barrier of access to modern financial services as much as building a new infrastructure with a very stable, high quality global medium of exchange supporting it."

Until next week - thank you for reading.

Please reach out to info@enigma-securities.io with any questions.

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