ENIGMA SECURITIES

De-Coding Crypto

Weekly Analysis

Past the abyss? The implications of $7000 (again)

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In this week's issue, we look at BTC's return to the $7000 level, and examine what's different now that we're approaching it from the downside.

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Our Market View

May you live in interesting times. Decent gains over the course of this week; the downwards test that looked very likely at the start of last week never truly materialised, and after setting a solid foundation at $6600, we were able to move up at the Monday open and regain the $7000 level we opened the year at once again. This week's research discusses the implications of that in more detail.

The more surprising story this week was a mini-rally on alts – mostly only showing slight outperformances against BTC, but a few (most notably ETH) doing the January trick once again of essentially doubling BTC's gains to the upside. It should still be kept in mind here that this is still coming from a position of relative weakness (very few assets are above their pre-Black Thursday levels in BTC terms), but it's a trend that will need to be watched over the next couple of weeks.

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

Major

Ticker	Price	7D	1M	6M	12M	Cap
BTC	7249.92	15.05%	-6.64%	-12.72%	43.08%	132.8
ETH	167.335	27.07%	-13.97%	-7.07%	2.09%	18.48
XRP	0.19628	12.37%	-3.23%	-28.27%	39.98%	8.63B
BCH	263.53	19.12%	0.28%	16.79%	-5.75%	4.84B
LTC	45.4541	17.53%	-6.83%	-18.86%	-41.92%	2.93B
EOS	2.66743	20.88%	-9.41%	-13.08%	-49.92%	2.46B

Selected

Ticker	Price	7D	1M	6M	12M	Cap
BSV	209.597	26.97%	8.46%	136.90%	194.00%	3.85B
XTZ	1.99048	27.77%	-16.00%	125.00%	103.50%	1.40B
LINK	2.81155	27.52%	-27.88%	8.27%	21.50%	0.98B

Past the abyss? The implications of $7000 (again)

As we said on March 11th:

> 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.

This ended up playing out almost immediately on Black Thursday, and our view on the landscape after the fact was fairly simple: the move represented a shattering of the market structure, that nothing could be taken for granted short-term, and that we might have a long way to go in terms of getting to levels where retail investors in particular would feel confident investing in BTC again, with particular focus on $7000 given its psychological importance (as a support level that had been repeatedly defended in November and December, and as the effective yearly open).

We say this because, for now at least, we are firmly back above $7000 - after a couple of rejections across last week, we quietly made it over during the early hours of Monday morning, and as of now have yet to re-test it. Hence, we are led to do something of a rewind - if going towards and below $7000 had such dire consequences, is going back above it similarly meaningful? We tend to think there are three main points to consider here.

1) Some indications of bullish sentiment within futures markets, but OI remains a shadow of what it was

One of the big developments over the last week or so has been the return to contango in the futures market. Historically, as with most things, BTC futures have traded at a premium to spot (and slowly closing to 0 towards expiry); this premium has tended to be fairly aggressive. Take, for instance, the June 26th 2020 BTC contract on BitMEX (XBTM20), which started trading in mid-December:

Date	XBTM20	Index	Premium	AnnPre
16-Dec	7007	6878	1.88%	**3.55%**
23-Dec	7513	7315	2.71%	**5.31%**
30-Dec	7437	7216	3.06%	**6.25%**
06-Jan	7973	7762	2.72%	**5.77%**
13-Jan	8352	8105	3.05%	**6.74%**
20-Jan	8909	8628	3.26%	**7.52%**
27-Jan	9220	8995	2.50%	**6.05%**
03-Feb	9638	9281	3.85%	**9.75%**
10-Feb	10321	9851	4.77%	**12.71%**
17-Feb	10192	9700	5.07%	**14.24%**
24-Feb	10060	9661	4.13%	**12.26%**
02-Mar	9211	8917	3.30%	**10.37%**

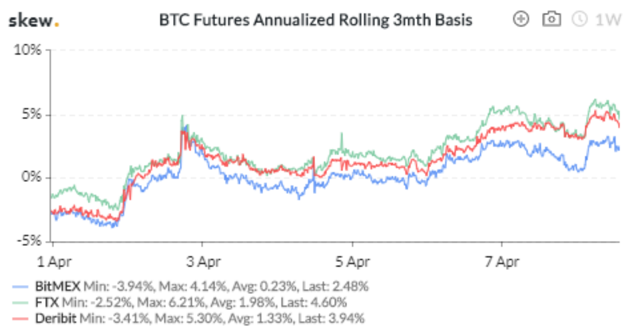
Data via BitMEX. Monday close.

Even during generally negative trends, BTC rarely goes into backwardation (i.e. futures trading at a discount to spot, fundamentally implying a generalised expectation of lower value on expiry), and the contango is aggressive enough that the 'cash and carry' trade (buying spot or perpetual contract BTC and selling the equivalent in futures contracts for a typical return of 5-10% annualised) has attracted significant attention from the cryptoasset community from time to time. This trade, as with so many other arbitrage strategies, fell apart on Black Thursday and beyond:

Date	XBTM20	Index	Premium	AnnPre
09-Mar	8123	7932	2.41%	**8.06%**
10-Mar	8046	7890	1.98%	**6.68%**
11-Mar	8092	7938	1.94%	**6.62%**
12-Mar	*3943*	*4861*	*-18.89%*	***-65.03%***
13-Mar	5443	5634	-3.39%	**-11.78%**
14-Mar	5007	5165	-3.06%	**-10.74%**
15-Mar	5296	5343	-0.88%	**-3.12%**
16-Mar	4893	5036	-2.84%	**-10.16%**
17-Mar	5224	5332	-2.03%	**-7.32%**
18-Mar	5340	5413	-1.35%	**-4.92%**

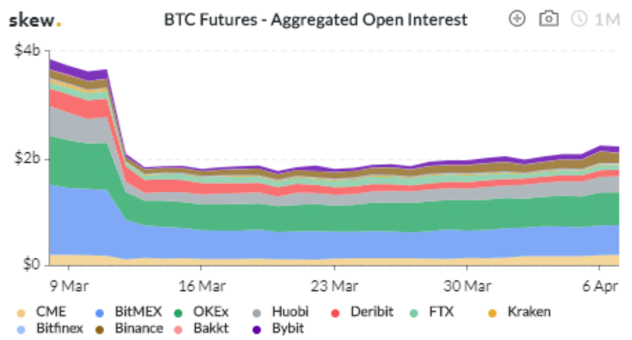
Data via BitMEX. Daily close.

We should note here that BitMEX saw an unusually stark degree of reversal here, but essentially all retail venues saw futures contract fall into backwardation following the drop and over the next couple of weeks. The good news over the past week is that we have, generally-speaking, emerged from backwardation. There is a decent amount of variance from venue to venue, but most moved above break-even between Wednesday and Friday last week, and BitMEX - which has fairly consistently had the lowest annualised rate over the last month - moved above 0% on Monday and has stayed there:



Credit: Skew. BitMEX in blue, FTX in green, Deribit in blue.

This, then, is a cause for optimism. On the other hand, to put a slight damper on said situation, we should note that open interest on said retail venues for the most part has not recovered. This was a figure that had exploded in prior weeks - [The Block's Larry Cermak noted that aggregated OI passed $5bn at the market peak in mid-February](), and going into Black Thursday, it was still at nearly $4bn. This proceeded to collapse, and has only modestly recovered since:



Credit: Skew.

We should note that not all venues are created equal here:

Venue	09-Mar	13-Mar	06-Apr	->13-Mar	->06-Apr
BitMEX	1300	607	558	-53.31%	-57.08%
Deribit	345	245	120	-28.99%	-65.22%
FTX	130	92	99	-29.23%	-23.85%
OKEx	893	461	618	-48.38%	-30.80%
Huobi	511	143	293	-72.02%	-42.66%
Binance	158	80	217	-49.37%	37.34%
CME	192	137	185	-28.65%	-3.65%

Data via Skew.

The derivatives-focused exchanges (which are mostly Western-centric) have seen very limited recoveries, while on the other hand, primarily spot exchanges (some of which have only fairly recently launched futures and/or options offerings) have fared better, and CME numbers are back where they were. Still, there has clearly been no race to re-establish positions in these markets for the most part, which while not necessarily actively bearish, is at best disappointing with regards to demand dynamics.

2) Alts are showing some interesting things with regards to demand

As mentioned at the start, the last few days have seen a small rally of alts against BTC, punctuated by a big surge towards the start of the week. Our general outlook on alts has been bearish, and what we're seeing right now isn't dramatically changing that; even with that surge, for instance, ETH isn't close to reclaiming pre-crash levels against BTC, let alone against USD. As we said two weeks ago:

> To gain as a class, then, alts not only need a significant BTC-run (there is a chicken-and-egg question with regards to whether alts or BTC would lead such a run, but that isn't enormously relevant for the terms of this discussion), but it needs to be a run of a type closer to 2017 than 2019 - in other words, a run that had speculative undertones to it and was part of a major resurgence in public interest over cryptocurrencies and cryptoassets as a group.

Alts as a class are only likely to gain against BTC in a true speculative run - which is what makes recent outperformance, however brief and however small in magnitude, interesting. In particular, we would single out XTZ and LINK, a pair of assets that we have frequently mentioned in the past because their demand is particularly speculatively-driven even by cryptoasset standards, have been right at the head of the pack over the last week or so:

Credit: Tradingview. BTC in blue, XTZ in orange, LINK in red.

3) The elephant in the room: how far to the upside can we run, and for how long?

If we were absolutely forced to boil it down to one word, our near-term outlook right now is bullish. Even if we throw out the absolute low at sub-$4000, and start measuring from $5600 or so (the point we found support at before the second stage of the meltdown, and a point that we technically closed at the next day), that still marks a 30% increase in about a month.

Furthermore, we now look to have established ourselves at a support level that has proven itself in very recent history to be extremely solid. So, where's the problem? The answer is that it's hard to see how far this can really run:

- Technically, this is a difficult range; one of the things that really started attracting excitement during the January/February run is that we encountered levels that had in the past offered significant resistance ($7500, $8600, $9500 all come to mind) and had overcome them relatively easily. Our entire argument for a collapse sub-$7800 back in March was that there was a lot of open air below; this isn't really true in the inverse.
- Institutional demand has increased, but doesn't appear to be entirely back yet (CFTC figures are still not painting a pretty picture with regards to a return by the 'class of 2020'), and retail demand is showing signs of picking up but isn't showing substantively yet.
- We tend to think of things as on something of a timer here. We still think it is extremely unlikely that current valuations on traditional markets for risk-on assets (as always, we are primarily thinking of equities here) reflect the reality of what is to play out economically over the coming months, even in the absolute best possible case with regards to dealing with the coronavirus situation in public health and economic terms. Our working assumption is still that there is at least one major leg down to come.

The manner in which we have returned to $7000 has actually made a decent case that, when (or if, if you prefer) we see another leg down, BTC might be able to resist that gravity on the second go around; the example of gold in 2008 is still the reference point on that (which effectively bottomed in October and started moving in opposition to still-falling equities from November onwards). If markets were to turn drastically south tomorrow, however, we still would probably expect BTC to go with them; the current level is a strong platform to build on from, not a guarantee.

BTC has a good shot at proving that it can separate itself (particularly as the economic effects hit in a far different manner to early March's pure panic/liquidity crisis), but $7000 is not the bar this time; we will need to see further strength over the coming weeks. We tend to think that we will more likely than not see $8000 again within coming weeks, but it's entirely unclear how markets will react at that level, and it's entirely unclear how long we actually have to get there and prove strength; this remains the big worry.

Until next week – thank you for reading.

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