



ENIGMA
SECURITIES



De-Coding Crypto

Enigma Weekly

24th September 2020

Written by Joseph Edwards, Head of Research at Enigma Securities.

Our Market View

May you live in interesting times. A down week across the board, with BTC seeing significant losses, and almost all assets falling back to some degree. We discuss the broader context at length in this week's issue. For BTC, we remain at something of an uneasy point – last week saw us break back above the crucial \$10,500 mark, but at the time of writing, we find ourselves having slipped back below it again after a drop on Monday. We would tend to lean neutral to slightly bearish unless we see re-establishment above that point again.

ETH and other alts continued to fall back heavily in both fiat and BTC terms, and our expectation is towards more downside across the board; on ETH in particular, we still tend to think that we're a decent distance above significant price support, and with hype over yield farming and other immediate-term DeFi projects dying down, it's hard to see how it arrests its current decline at least for the time being.

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

Major

Ticker	Price	7D	1M	6M	12M	Cap
BTC	10460	-5.60%	-10.98%	67.18%	27.25%	193.4B
ETH	338.55	-8.52%	-16.03%	157.70%	94.66%	38.2B
XRP	0.23131	-5.61%	-19.78%	31.40%	-4.60%	10.4B
BCH	214.60	-8.06%	-25.87%	0.08%	-5.70%	3.98B
LTC	44.44	-8.52%	-28.67%	14.03%	-19.96%	2.91B
EOS	2.545	-6.02%	-24.52%	15.30%	-10.26%	2.39B

Selected

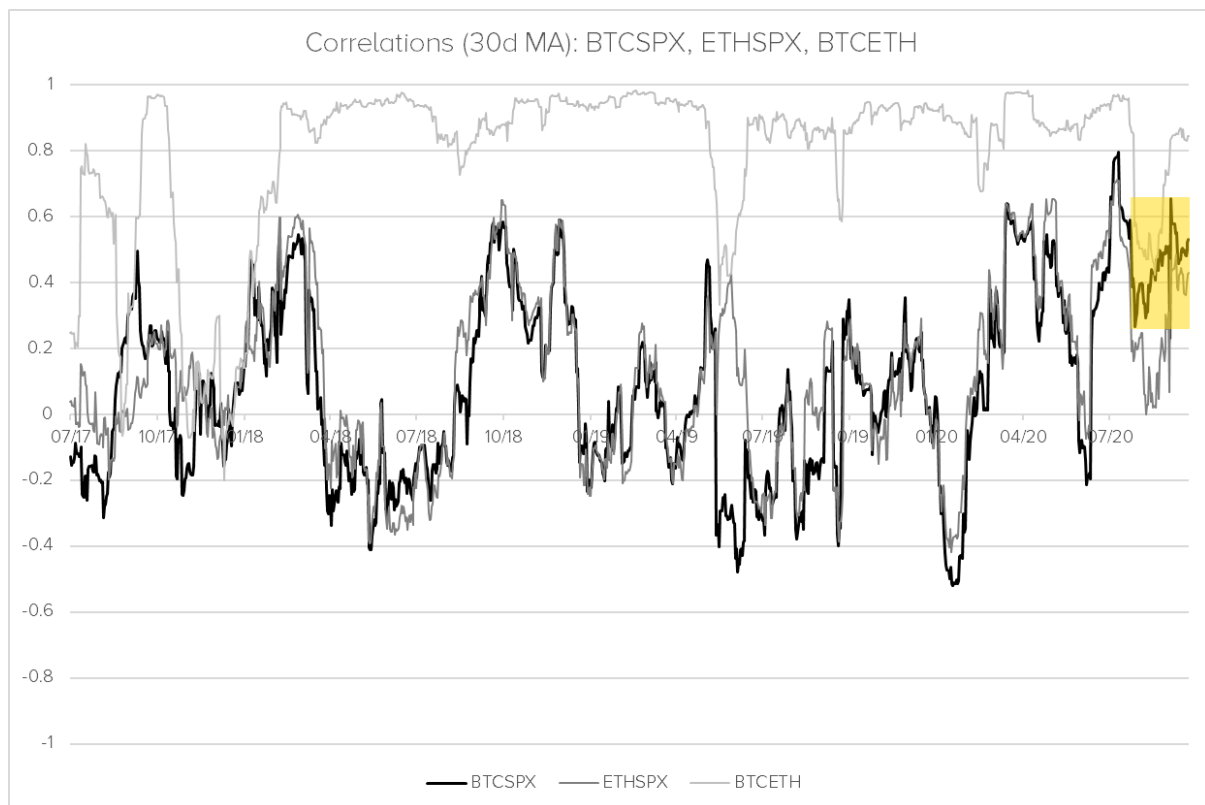
Ticker	Price	7D	1M	6M	12M	Cap
LINK	8.204	-24.00%	-45.69%	283.30%	388.90%	2.87B
ADA	0.08086	-10.75%	-35.34%	170.50%	108.70%	2.51B
XTZ	1.992	-20.12%	-46.01%	27.20%	123.80%	1.46B

SPX correlation latest: risk outlook for Q4

We last wrote about SPX correlation on July 22nd, and as we did then, we will quote our April 1st issue:

One of the big truisms that has emerged over the last few weeks has been this: in the short-term at least, BTC and [US] equities are marching in lockstep, and will likely continue to march in lockstep. This is something that we first noticed in earnest back on 3rd March...at that point, the short-term relationship looked fairly existent, but not so aggressively to serve as confirmation...Following the events of the last month or so, however, the relationship now looks far stronger and far more 'confirmed' that it did then, to the extent of forming a valid truism at least to some degree.

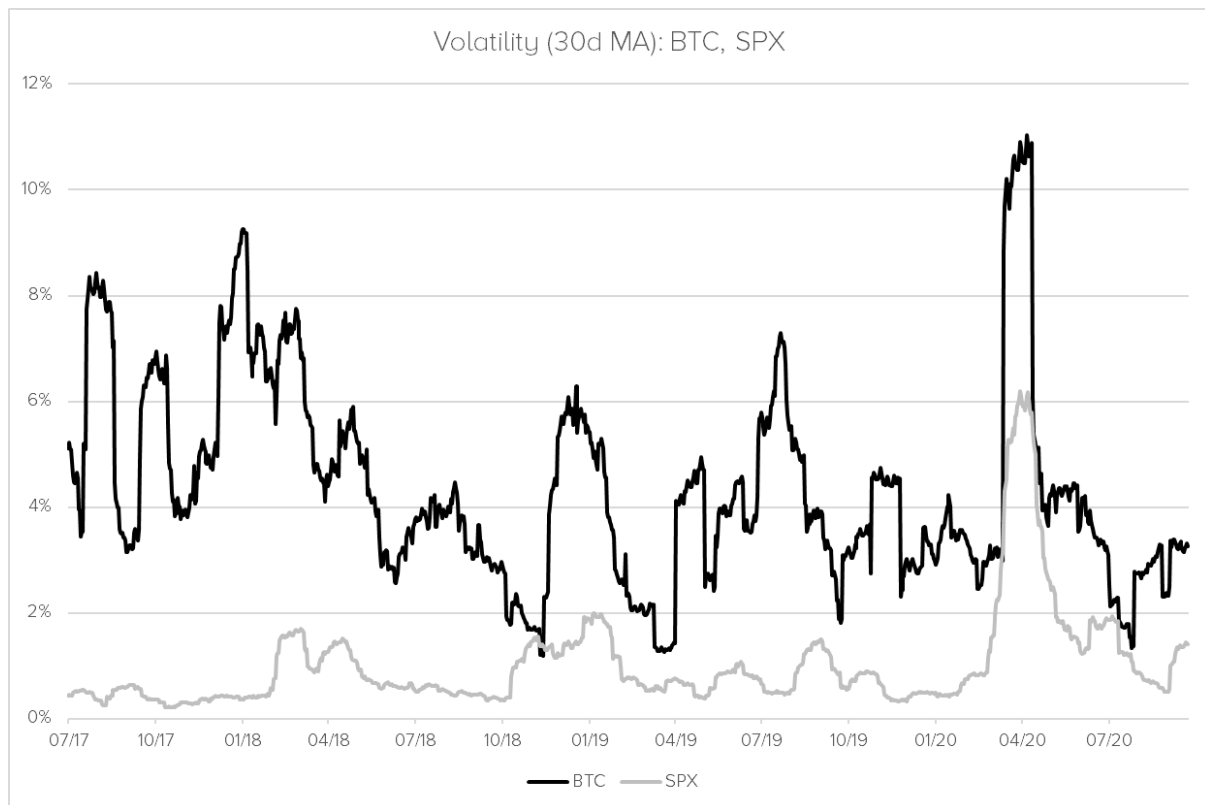
As we will explore, the question of correlation between BTC and SPX is an extremely relevant one going into Q4; given recent price action, it seems opportune to check back in on developments in that regard.



Data via Tradingview. Crypto reference prices Coinbase vs. USD.

The first thing to say is that in terms of raw correlation (as measured via Pearson correlation), we did peak going into that issue. However, in spite of that, we do remain at historically high levels in that regard; 30-day MA as of Tuesday was at 0.53 - some distance below that 10th July peak, but still clearly elevated compared to historical norms. Notably, this has held in spite of significant divergence from ETH, which, while still heavily correlated even on a 30-day MA, moved apart from BTC in a significant manner for the first time in over a year.

For the past few months, this has been a curiosity more than anything else. Note, for instance, BTC volatility against SPX volatility over the course of the summer:



Data via Tradingview. Crypto reference prices Coinbase vs. USD.

Two things stand out here. First, that both saw volatility progressively drop over much of the summer before returning recently (especially in BTC's case); secondly, that volatility actually reached similar levels on both, something that has only ever happened once before (in November 2018). The mean 'multiplier' on historical volatility since mid-2017 for BTC against the SPX has been 6.73, and for 2020, it's been 3.06; at the nadir on 4th July, the ratio was down to just 1.12.

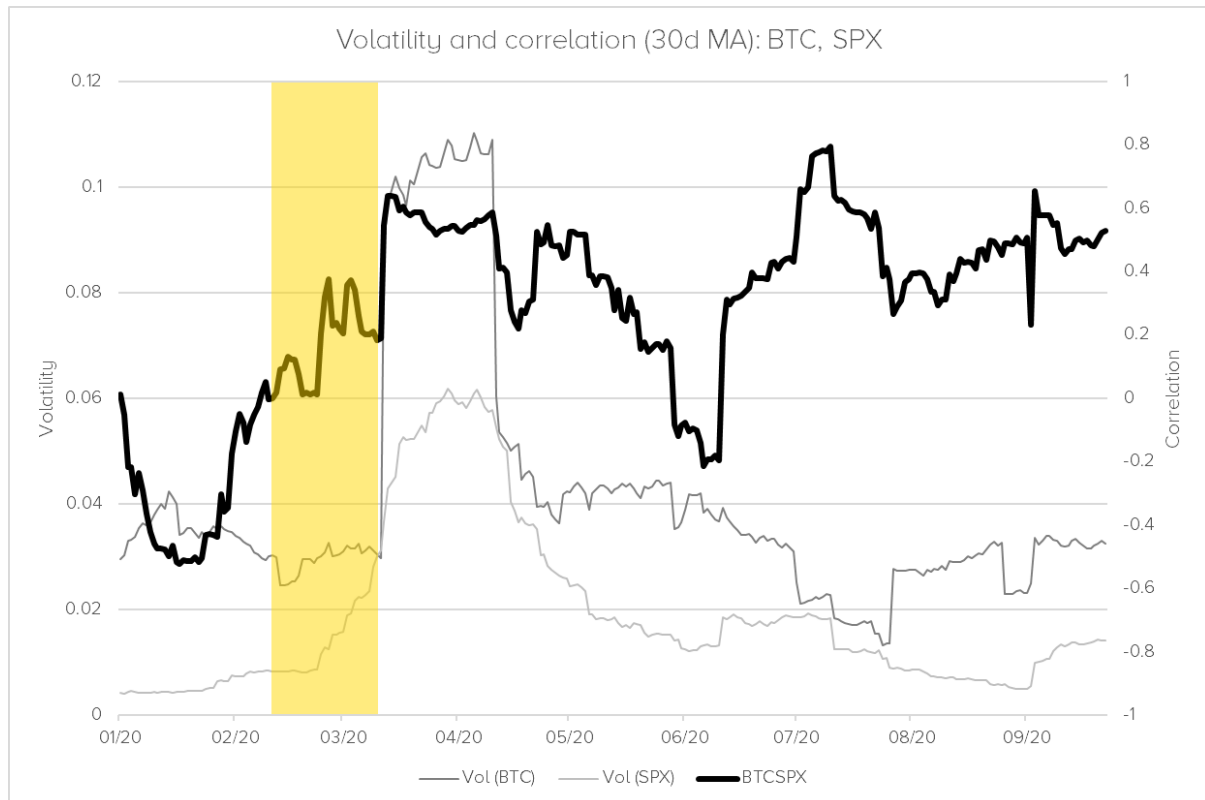
To give a better picture, let's look at the top 10 (out of 65) trading days comprising June, July, and August for the SPX, and compare them to BTC's returns on those days:

Date	SPX	BTC	ETH
03/06/2020	1.36%	1.54%	2.90%
05/06/2020	2.58%	-1.83%	-1.29%
12/06/2020	1.28%	2.11%	3.21%
16/06/2020	1.86%	0.99%	1.90%
29/06/2020	1.46%	0.78%	1.28%
30/06/2020	1.54%	-0.57%	-1.02%
06/07/2020	1.58%	2.96%	6.16%
14/07/2020	1.35%	0.22%	0.49%
29/07/2020	1.24%	1.61%	0.20%
12/08/2020	1.39%	1.56%	2.20%
Average	1.56%	0.94%	1.60%

Data via Tradingview. Crypto reference prices Coinbase vs. USD.

The relationship has been relatively tight, but a 1:1 positive relationship in this regard is profoundly uninteresting for an asset of BTC's nature; hence, it has remained as curiosity.

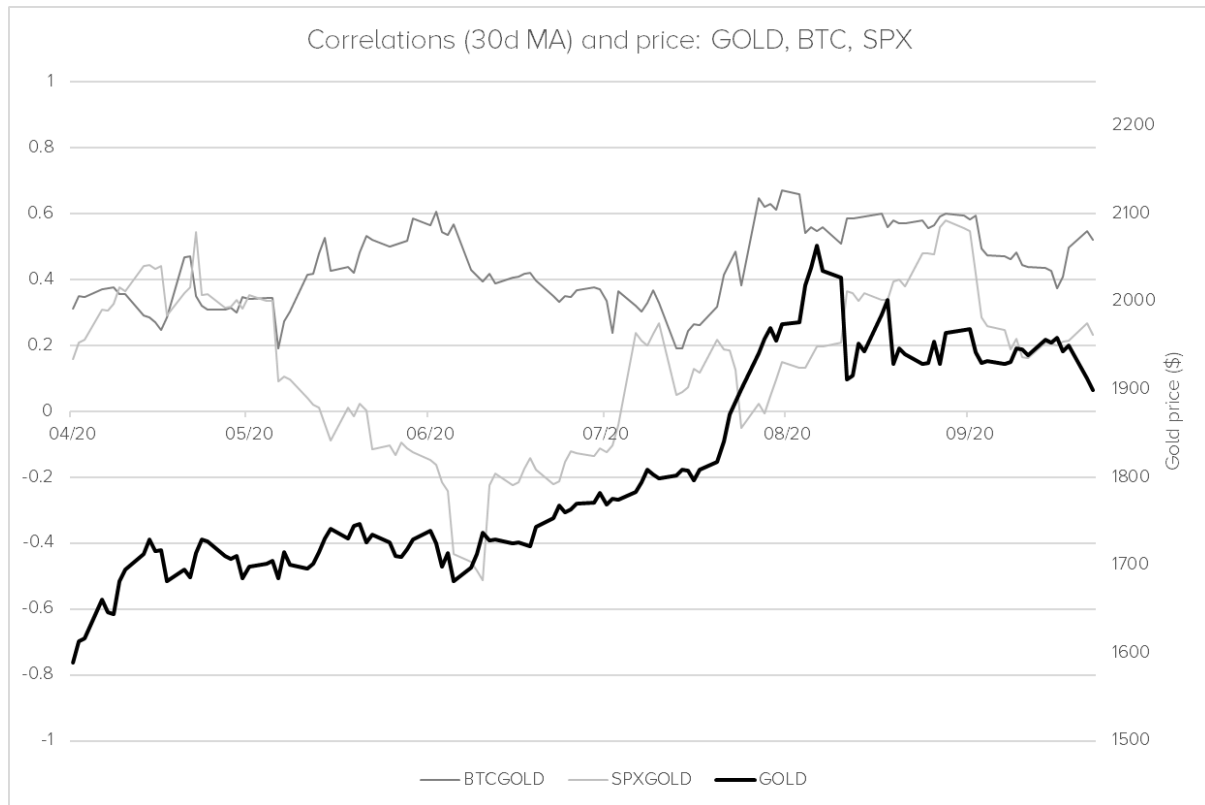
The problem, of course, is that the situation is now shifting against that. Volatility is ticking upwards, on both BTC and equity markets, and in that regard, curiosity turns to a concern. In particular, we would highlight what we saw with regards to the pre-crash environment in terms of both correlation and volatility in Q1 with regards to steady growth of correlation, a slow rise in BTC volatility after a nadir, and SPX volatility rising to meet it:



Data via Tradingview. Crypto reference prices Coinbase vs. USD.

The obvious refrain in response is that the parameters of the March crash (with regards to market panic and the associated liquidity crisis) are what defined said crash above all else, and that even on a bearish outlook, we are unlikely to see the same now. That is, of course, true; the SPX is unlikely to have another 12% down day, and BTC is possibly less likely to have a 40% down day.

However, while we're unlikely to see a stampede for the doors with quite the same velocity (which, one must note here, was without precedent even compared to the likes of 1929), we still tend to think that if momentum continues to build negatively, we are likely to see a similar pick-up in correlation (towards the downside) as we did back in March. One of the big point that we are inclined to mark out in this regard is recent price action on gold, and gold-SPX and gold-BTC correlations:



Data via Tradingview. Crypto reference prices Coinbase vs. USD.

Gold-SPX has historically had an inverse relationship more often than not, but has been positive for much of 2020, and currently sits relatively high in that regard compared to both BTC and SPX after briefly decoupling in late Q2 and early Q3.

As the cliché goes: "in a crisis, all correlations go to 1". Our view on US equities, and the global macro situation in particular, remains bearish. As we said in our July issue:

It does, however, bring back that impetus to pay close attention to the state of equities markets going forward, and it does somewhat colour our view poorly for Q4 - between earnings season in October, the Presidential race ending in November, and the potential disaster scenario of attempting to deal with a still-ongoing pandemic during the winter months for the US and most other traditional markets hubs, there is clearly a huge amount of risk accumulating.

Absolutely nothing has changed since that issue in that regard, and indeed, we would double-down on those concerns to some extent: the heights we ended up reaching in Q3 (going straight through the March high just below 3400 and through to nearly 3600) suggest to us a market that not only has failed to price in Q4 risks appropriately, but has probably priced in further assistance (particularly with regards to stimulus spending in the US) that was probably in truth never likely to come through before the election.

We have already seen significant drawdowns over the last month, with five days in the span of 12 trading days on which the SPX fell at least 1% (against five in the previous 50 before that). The results for BTC (and ETH) on those days have not been good:

Date	SPX	BTC	ETH
03/09/2020	-10.73%	-12.98%	-3.53%
08/09/2020	-2.40%	-4.59%	-2.82%
10/09/2020	1.16%	4.83%	-1.75%
18/09/2020	-0.06%	-1.25%	-1.12%
21/09/2020	-4.62%	-8.33%	-1.17%

Data via Tradingview. Crypto reference prices Coinbase vs. USD.

On only one of the five did BTC or ETH end up positive on the day, and the particularly concerning one is of course 3rd September; this did admittedly come in the context of a drawdown starting from the previous day (which in turn came after rapid gains on both ETH and BTC on the days and weeks leading up to that), and our working theory is that traditional market losses on the day steepened rather than caused the observed degree of losses, but still: this is a point of significant concern. Our argument going all the way back to Q2 has been that the biggest challenge for BTC for the remainder of the year was going to be to decouple itself from traditional markets. So far, evidence suggests no such action; and, with such significant potential for further pain as we move into October and November, this has now become something of a black cloud hanging over the asset.

As in July and August, BTC is not in the driver's seat; unlike in July and August, we have relatively low mid-term confidence in the driver (ETH then, global macro and equities now), and while we tend to still think that potential downside on crypto assets is probably still of far lesser magnitude than we saw in March, we still tend to think that said scenario would represent significant enough downside as to balance out the structural upside from current levels for an overall short-term bearish bias.

With regards to broader crypto markets, we are more strongly short-term bearish. The positive momentum on ETH and related assets has dissipated somewhat, and as a recent research piece from Iconic Funds ([Investigating the Myth of Zero Correlation Between Crypto Currencies and Market Indices](#)) illustrates, non-BTC assets were actually more closely correlated with traditional market indices during the Q1 2020 crisis (not too surprising given that they lack even the narrative of risk-off potential that BTC still clings onto):

	MXWO	MXWD	IGLO LN	FXNAX	BCOM	MXWOORE	PSPIV	IGF US	WOOD US
Bitcoin	50% *	51% *	27%	43%	51% *	32%	47%	58% **	45%
Ethereum	62% **	63% **	24%	38%	65% **	49% *	60% **	66% **	60% **
XRP	70% ***	71% ***	30%	44%	64% **	56% **	66% **	71% ***	66% **
Tether	46%	44%	39%	36%	31%	48% *	40%	44%	47%
Litecoin	55% **	56% **	23%	34%	52% *	42%	54% *	60% **	50% *
EOS	52% *	53% *	23%	34%	46%	39%	50% *	57% **	47%
BinanceCoin	58% **	59% **	24%	38%	56% **	42%	53% *	61% **	53% *
Tezos	Hasn't reached trading volume of 500 million USD yet								
Chainlink	26% *	27% *	12%	16%	27% *	23%	24%	31% **	27% *
UNUS SED LEO	Hasn't reached trading volume of 500 million USD yet								

* Significant at the 10% level
 ** Significant at the 5% level
 *** Significant at the 1% level

Credit: Iconic.

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.

DISCLAIMER:

The information contained in this report issued by Enigma Securities Limited is not intended to be advice nor a recommendation concerning cryptocurrency investment nor an offer or solicitation to buy or sell any cryptocurrency or related financial instrument. While we provide this information in good faith it is not intended to be relied upon by you and we accept no liability nor assume any responsibility for the consequences of any reliance that may be placed upon this report. Enigma Securities Limited is an Appointment Representative of Makor Securities London Ltd which is authorized and regulated by the Financial Conduct Authority (625054)