BITFINEX Alpha

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INTRODUCTION

After a week of all our predictions coming through, with the Fed raising rates by 75bps (not 100bps), and confirmation of two consecutive quarters of negative economic growth; this week we focus on what the latest economic data is telling us, what the markets are telling us, and how the Fed is going to guide its policy decisions going forward.

The data is important. The Fed and the White House claimed that two negative quarterly GDP prints was not a recession (!), so we dive into what would count as a recession. We conclude that beyond the GDP numbers, we are still seeing demand destruction from consumers and corporates, and the labour market (contrary to Fed proclamations) is beginning to weaken. We are not out of the woods yet.

Despite this, the bond market is sanguine and appears to indicate that inflation will reach the targeted 2% range by next year. The Fed says it will continue to respond to data to guide monetary policy. The net result is that Bitcoin is up, but we are in for a very interesting few months.

In the crypto industry, partnerships and innovation continue apace. Bitfinex and Tether launched Holepunch, a new peer-to-peer platform and delivered the alpha version of Keet, a video chat app, which will operate on Holepunch. As a P2P solution, it is highly secure and extremely private. Such technology solves the Big Tech problem, where data harvesting is big business, by providing a viable, easy-to-use technology that is fast, free and private.

We also saw Meta signing a partnership with Oasis Labs, Apple being accused of suffocating the Metaverse, and Pancakeswap introducing a governance mechanism without issuing a new token.

For our On-Chain section - it is all about Ethereum and its outperformance as The Merge approaches. We discuss how sustainable this rally is and utilise on-chain data to explain its origin. We also revisit how the Long Term Holders are behaving in the current market conditions.

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GENERAL MARKET UPDATE

75 BPS Hike: Not-so-bad news is good news

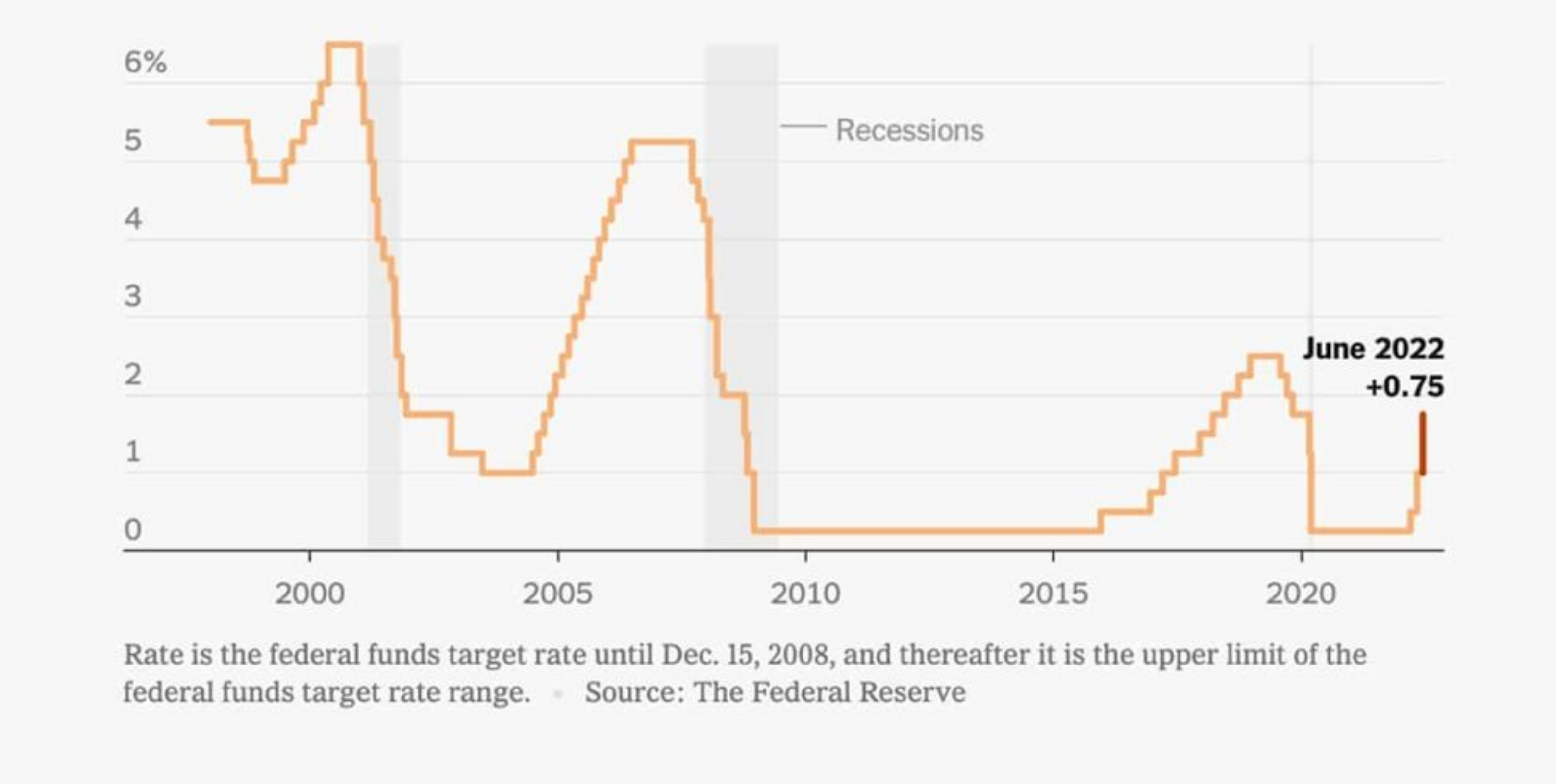


Figure 1. Federal funds target rate (source: livemint)

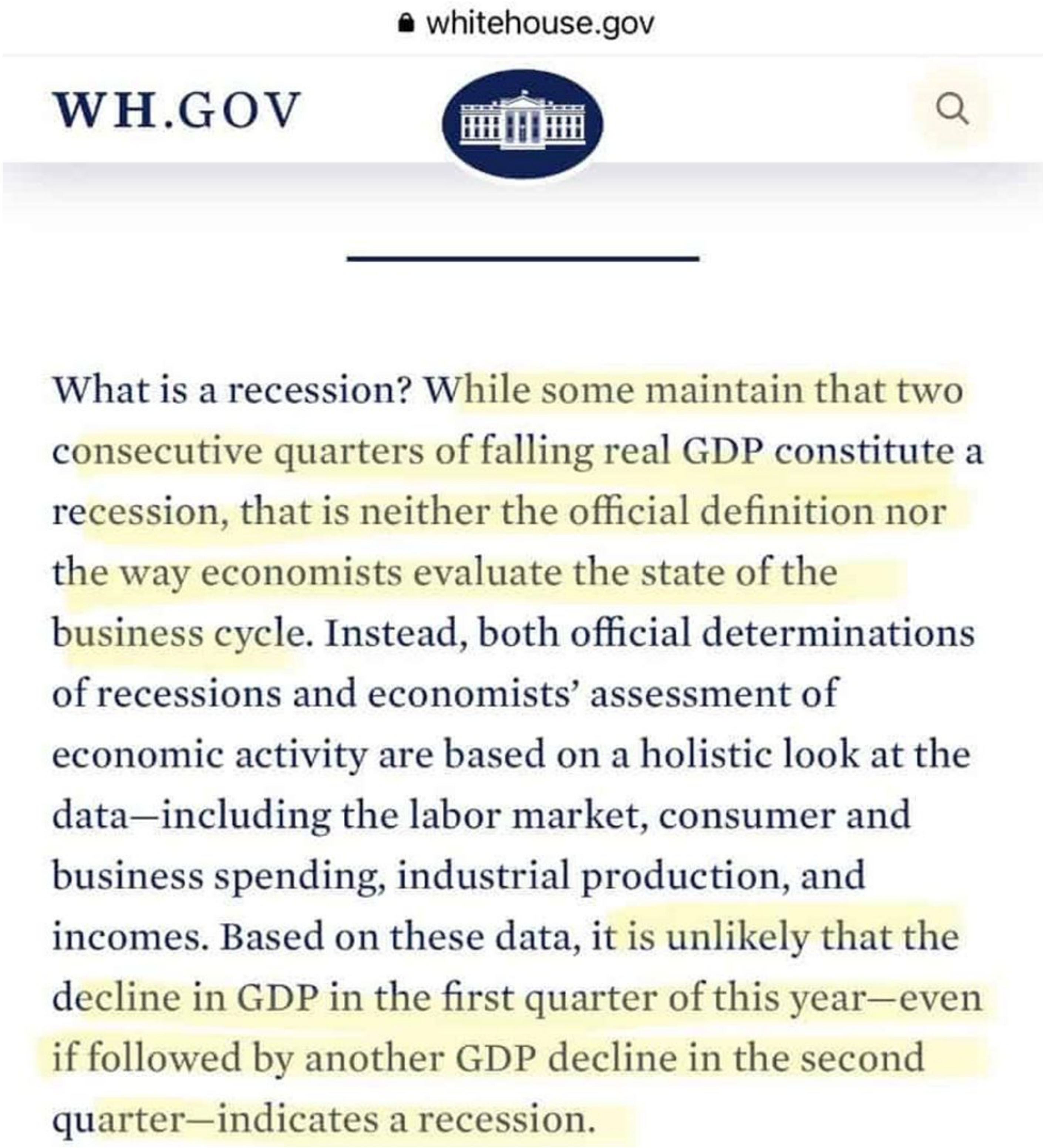
Federal Reserve Chairman Jerome Powell reiterated his commitment to curb inflation during last Wednesday's Federal Open Market Committee ('FOMC'). The Federal Reserve raised the target range for the Fed Funds rate by 75 bps to 2.25%-2.5% during its July 2022 meeting. As expected by market forecasts, it is the fourth consecutive rate hike pushing borrowing costs to their highest level since 2019.

Prior to the meeting, high inflation had fueled speculation of an entire percentage point hike. However, according to Powell, a 100-basis point hike was not appropriate, based on spending and production levels, which indicated the economy is still in the process of slowing down. Powell also rejected speculation that the economy was in a recession, citing a strong labour market and low unemployment rate.

The FOMC seeks to achieve an inflation rate of 2% while keeping the unemployment rate as low as possible. Though the Fed admits a recession is not impossible, it is still committed to reducing the level of Treasury securities and agency mortgage-back securities on its balance sheet, to fulfil its statement released last May.

Government: We are not in a Recession

Jerome Powell introduced the stiffest interest rate increase in roughly four decades. During the FOMC press conference, the Fed Chair was peppered with questions about whether the U.S. economy was in or on the cusp of a recession - a notion he rejected because U.S. firms continue to hire in excess of 350,000 additional workers each month.



whitehouse.gov

WH.GOV

What is a recession? While some maintain that two consecutive quarters of falling real GDP constitute a recession, that is neither the official definition nor the way economists evaluate the state of the business cycle. Instead, both official determinations of recessions and economists' assessment of economic activity are based on a holistic look at the data—including the labor market, consumer and business spending, industrial production, and incomes. Based on these data, it is unlikely that the decline in GDP in the first quarter of this year—even if followed by another GDP decline in the second quarter—indicates a recession.

Figure 2. whitehouse.gov definition of a recession (source: Delphi)

An observation by a *Delphi* article noted that the official website for the White House has changed the definition of a recession ahead of the GDP numbers. The White House is perhaps trying to give the market an early warning about the GDP data, which confirms a second consecutive quarter of negative growth. GDP trends have long been used in attempts to forecast economic recessions, but the White House and the US Government continue to downplay that for the time being.

That brings us to a more critical discussion, what is a recession?

Economists have long maintained the definition of a recession as "a period in which real GDP declines for at least two consecutive quarters". It is a widely adopted definition taken from the popular *Economics* textbook by Paul Samuelsen and William Nordhaus. Instead, the US government prefers the National Bureau of Economic Research's (NBER) loose definition, "a significant decline in economic activity that is spread across the economy and lasts more than a few months". The White House thinks that Samuelsen and Nordhaus' definition of a recession is not applicable, despite the fact this definition has correctly defined recessions around the world for several decades.

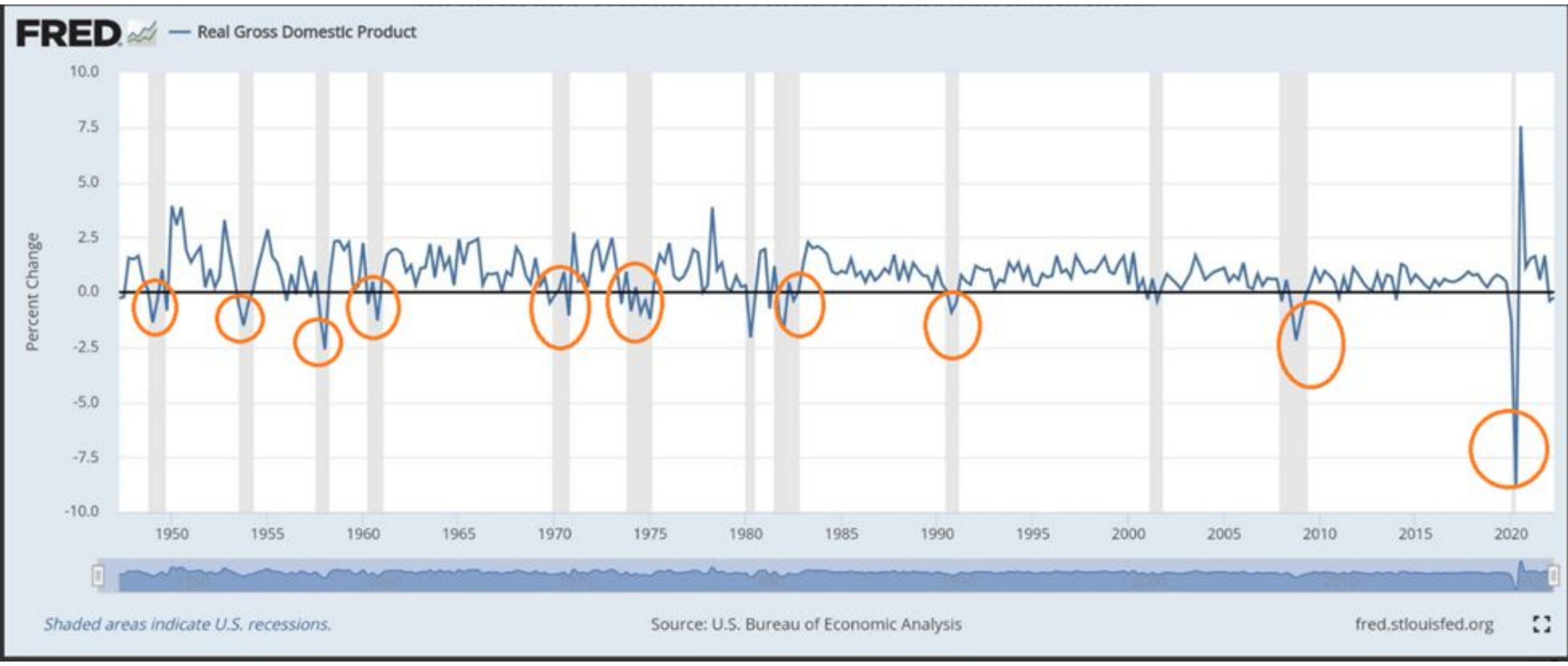


Figure 3. Real GDP percentage fluctuation for the US (source: FRED)

The circles (red in the graph) indicate how accurately two negative quarters of GDP growth have indicated oncoming recessions in the US.

How is GDP calculated?

A nation's Gross Domestic Product or GDP is a widely used indicator of an economy's size, hence, an economic slowdown would mean a shrinking GDP. GDP is the total value of a country's finished goods and services. How exactly is GDP calculated?

GDP is the sum of the country's private consumption, government spending, business capital spending and net exports.

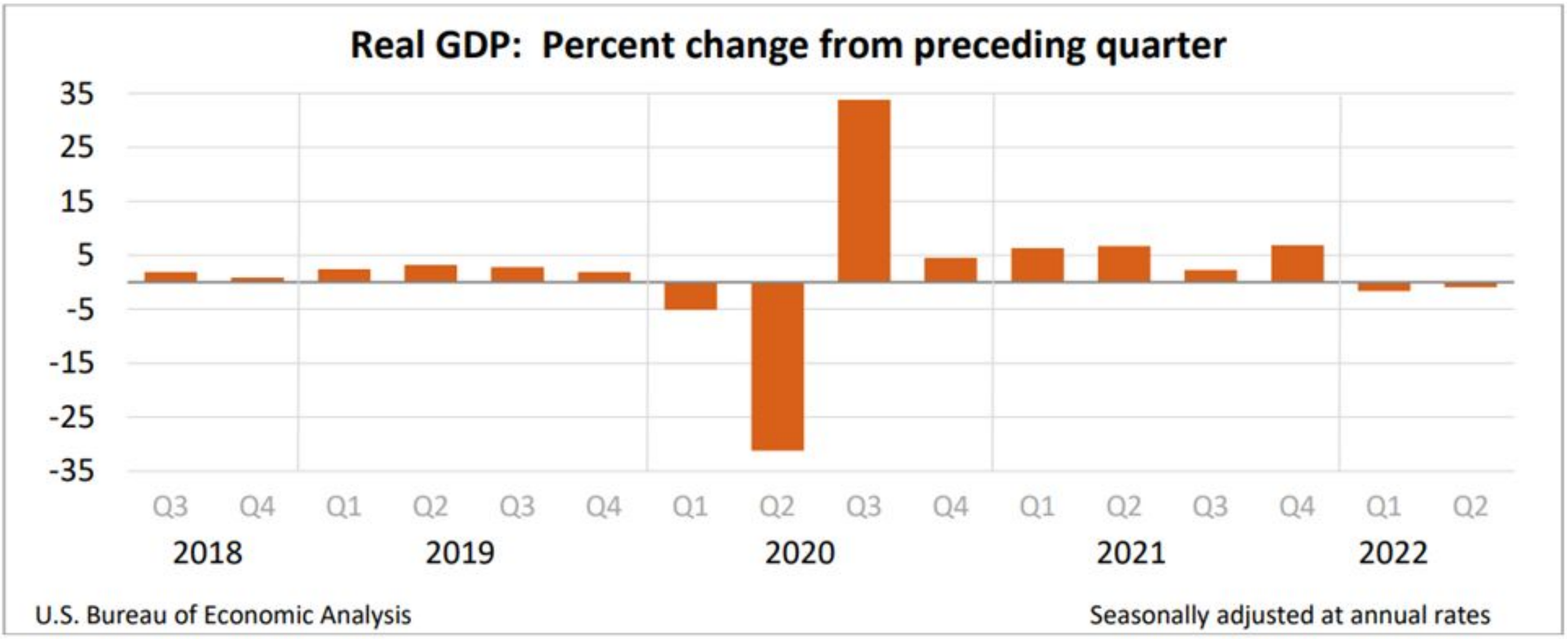


Figure 4. Percentage change in real GDP per quarter (source: US BEA)

US GDP has fallen 0.9% year on year, according to the advanced estimate report from the Bureau of Economic Analysis (BEA), following a decrease of 1.6% in the first quarter. A second quarter of negative GDP thus meets the familiar base view of a recession, but the government does not want to call it that, as we have discussed above.

The Personal Consumption Expenditure Price Index or PCEPI is monitored by the Fed. It is a measure of inflation and follows the change in prices of goods and services consumed by households. Compared to Consumer Price Inflation, which measures out-of-pocket expenditure for a basket of goods, the PCEPI is broader and timelier. The Core PCE price Index is the less volatile measure of the PCE price index, excluding the more volatile and seasonal food and energy prices.

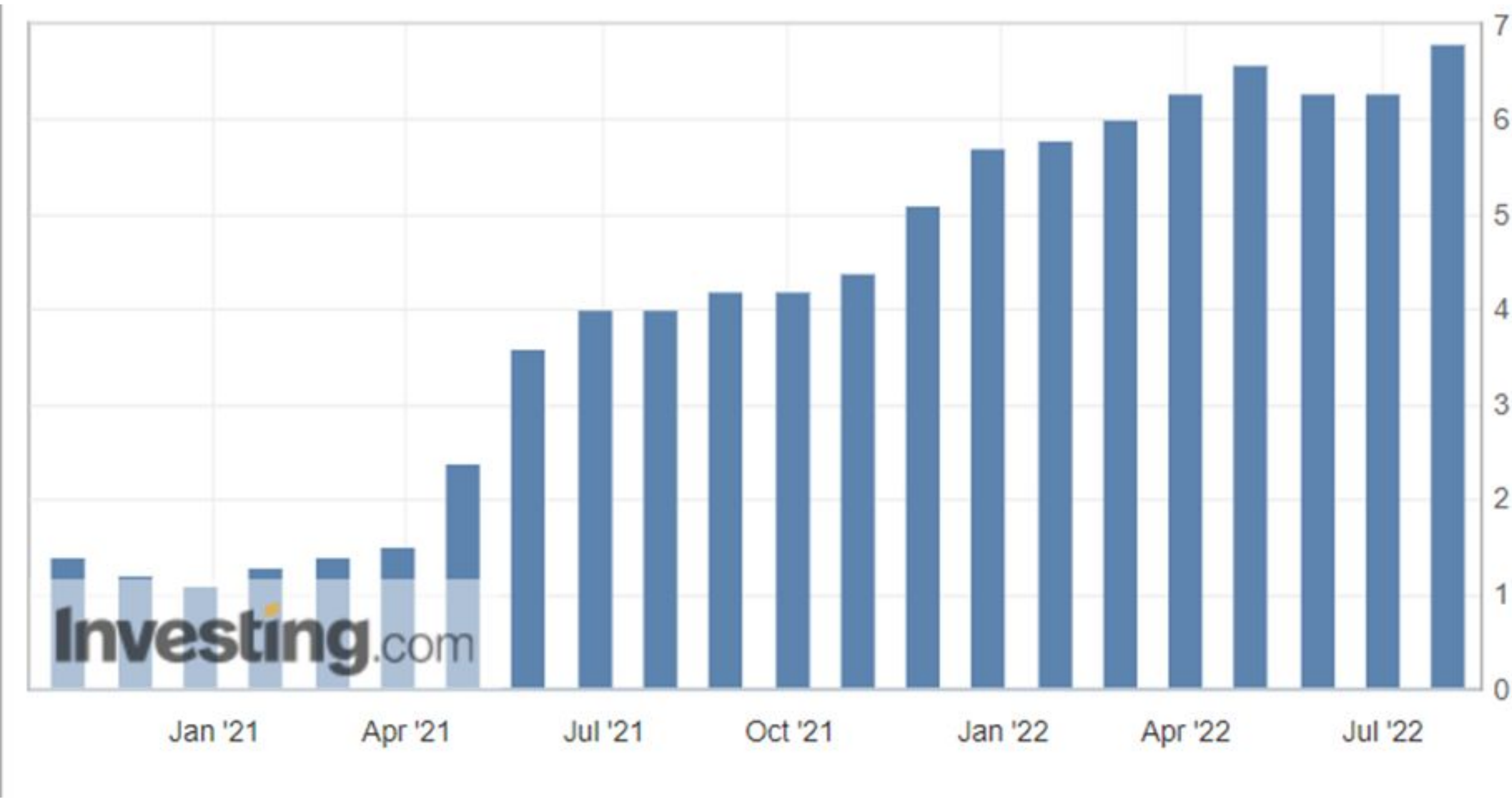


Figure 5. PCEPI percentage change monthly YoY estimate (source: Investing.com)

According to the BEA, the PCEPI rose by 6.8% in July year on year (YoY). This is a new 40-year high. Month on month, the PCEPI rose by 1% in June. US Core PCE Price Index YoY rose **4.79%**, compared to 4.67% last month. In June, gas prices hit record-high levels. Energy prices grew 43.5%, and food prices increased by 11.2% - and were key drivers of the current PCEPI print.

If consumer spending increased in the second quarter, what caused the decline in GDP growth? According to the United States Commerce Department, the decrease in GDP came from lower government spending and a reduction in investment in residential and non-residential buildings alongside a reduction in investments to populate their inventories for businesses. Businesses are less willing to invest as the rate of borrowing increases with the Fed's aggressive rate hikes.

Figure 6. Gross Private Domestic Investment (source: FRED)

Demand Destruction

Inflation is driven by consumer demand. Economists have a term for when prices rise too high for people to keep spending: “demand destruction”. The idea is that when the prices of commodities get too high for too long, it destroys demand for such commodities. Is the current inflation hot enough to eliminate demand?

We look at the University of Michigan’s Consumer Sentiment Index to understand how consumers take inflation pain. This tracks the sentiment among households and consumers towards their personal finances, general business conditions and market conditions. In previous recessions, the Consumer Sentiment Index has consistently declined. This July, the index reported a value of 51.5. Though the number can be seen to have somewhat eased, this is significantly lower than the average of 85, which tells us about the consumer’s pessimism about the current economy.

This can be confirmed by Consumer Confidence, a survey conducted by the Conference Board that also tracks the behaviour of the American Consumer. US consumer confidence has declined to its lowest since February 2021, decreasing for the 3rd the third month to 95.7.

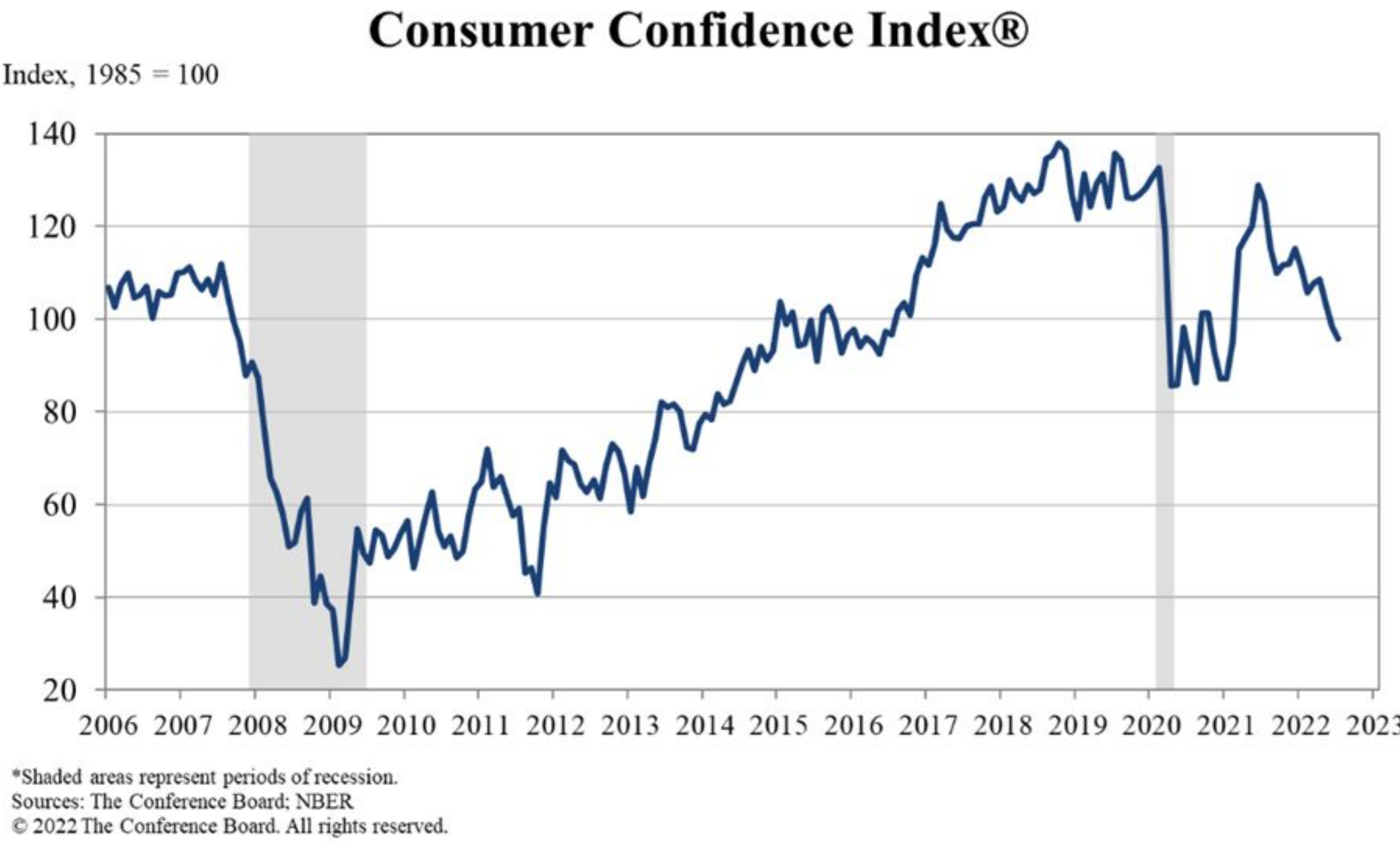


Figure 7. Consumer Confidence Index by the NBER

Conference Board NBER’s Consumer Confidence Index: Sections Covered by the Survey [1]	University of Michigan’s Consumer Sentiment Index: Sections Covered by the Survey [2]
• Current business conditions • Business conditions for the next six months • Current employment conditions • Employment conditions for the next six months • Total family income for the next six months.	• Current Economic Index • Personal Finances Current • Buying Conditions Durables • Expected Economic Index • Personal Finances Expected • Business Conditions 1 Year • Business Conditions 5 Years
[1] The Conference Board. "Consumer Confidence Survey Technical Note - May 2021." [2] University of Michigan-Surveys Of Consumers. "Table 1B-Components of the Index Of Consumer Sentiment."	

If we look at the sections covered by both surveys, Consumer Confidence tends to pick up sentiment related to the job market. In contrast, the Consumer Sentiment index is a better measure of personal finances and expenses, like the price of gasoline. This tells us that consumers have picked up the relief in gas prices but still have persistent pessimism regarding the job market.

A data-driven Fed

The Fed also noted that with new data still be reported, including revised GDP, unemployment and inflation, we would have a clearer picture of how much growth had slowed in the second quarter. Powell said some of the impact of Fed rate increases to date is still building in the economy, and depending on how inflation responds in the coming months, the central bank could begin to slow rate increases.

What is the takeaway for an investor? The Federal Reserve has adopted a systematic and data-driven approach to inflation.

An excerpt from the press conference after GDP numbers were announced reads:

Journalist: "Mr. Powell, due to the recent bond and equity market rally, financial conditions have eased quite a lot: what's your take?"

Powell: "The appropriate level of financial conditions will be reflected in the economy with a lag and it is hard to predict. We will be fully data-dependent."

The bond market however already has a firm opinion on how inflation will develop.

Figure 8. Expected inflation using CPI inflation swaps (source: TheMacroCompass)

TheMacroCompass created a custom indicator utilising CPI inflation swaps to indicate one-year forward inflation expectations. Given the Fed targets core PCE numbers, as discussed in the above sections, bond markets through CPI inflation swaps are indicating that inflation will slow down very aggressively and roughly hit the Fed target in the second half of 2023. Expected inflation between July 2023 and July 2024, represented in the chart above, sits at 2.9%.

Housing Market

With low borrowing costs and excess cash from government stimulus, the demand for houses boomed during the pandemic, leaving potential homebuyers with elevated house prices.

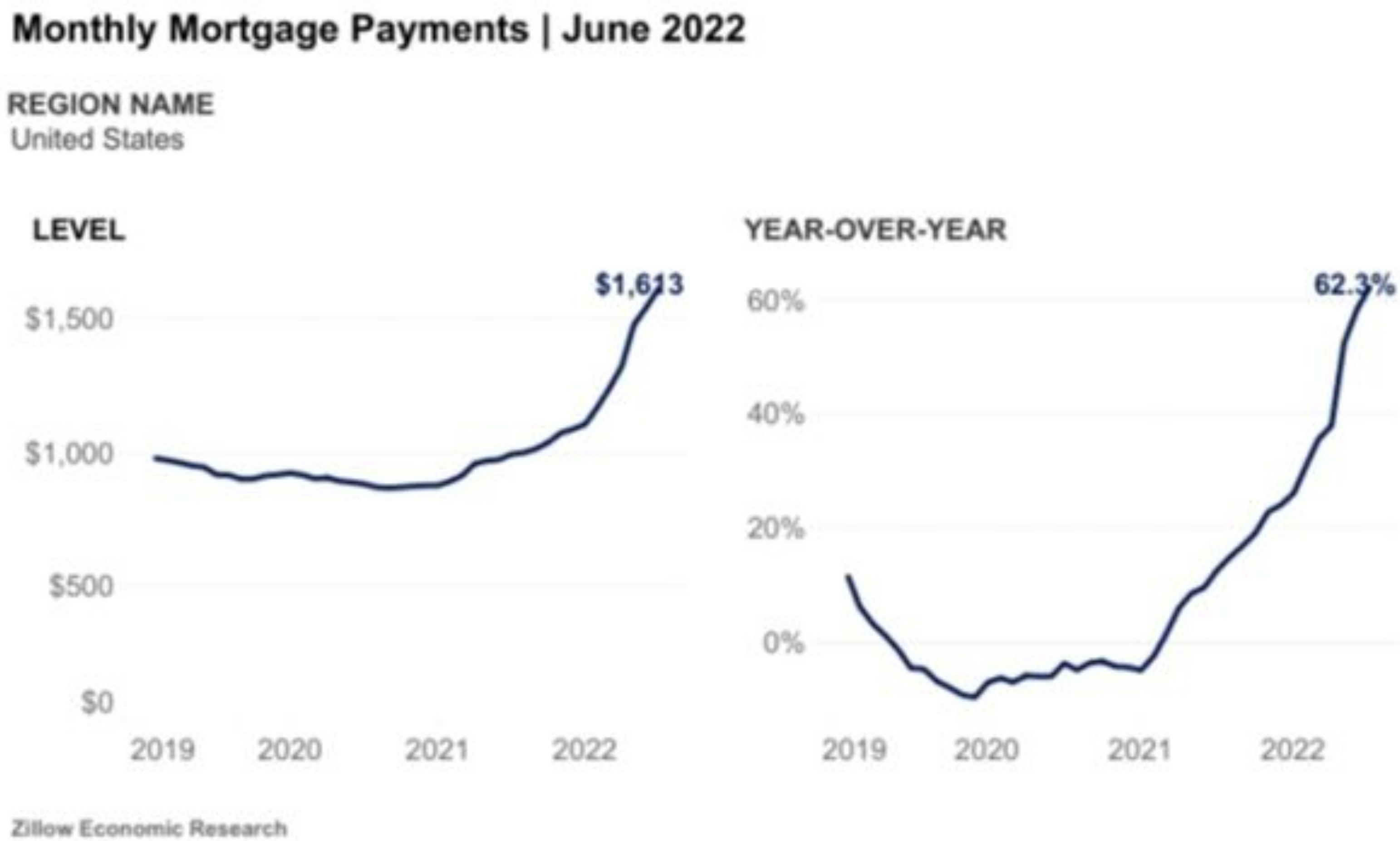


Figure 9. Year-Over-Year monthly average monthly mortgage payments (source: Zillow)

Zillow's monthly housing market report indicated that the monthly mortgage payment for an average home in the US has increased by 4.5% in the past month and 62.2% from last year. The Fed's aggressive interest rate rises have negatively affected the affordability of houses for potential home buyers.

Asking prices for houses are still up, but a portion of home sellers are cutting their prices. According to Realtor.com, the median home price nationwide is at $450,000 and last week, the median listing price continued in its 32nd straight week of double-digit growth that reached 16.6% over last year. However, these are just asking prices, and buyers are not stepping up. Backing up this conclusion, *Realtor.com* listing data shows that the share of homes that reduced their list price has increased to 14.9% in June from 7.6% a year ago.

Car Market

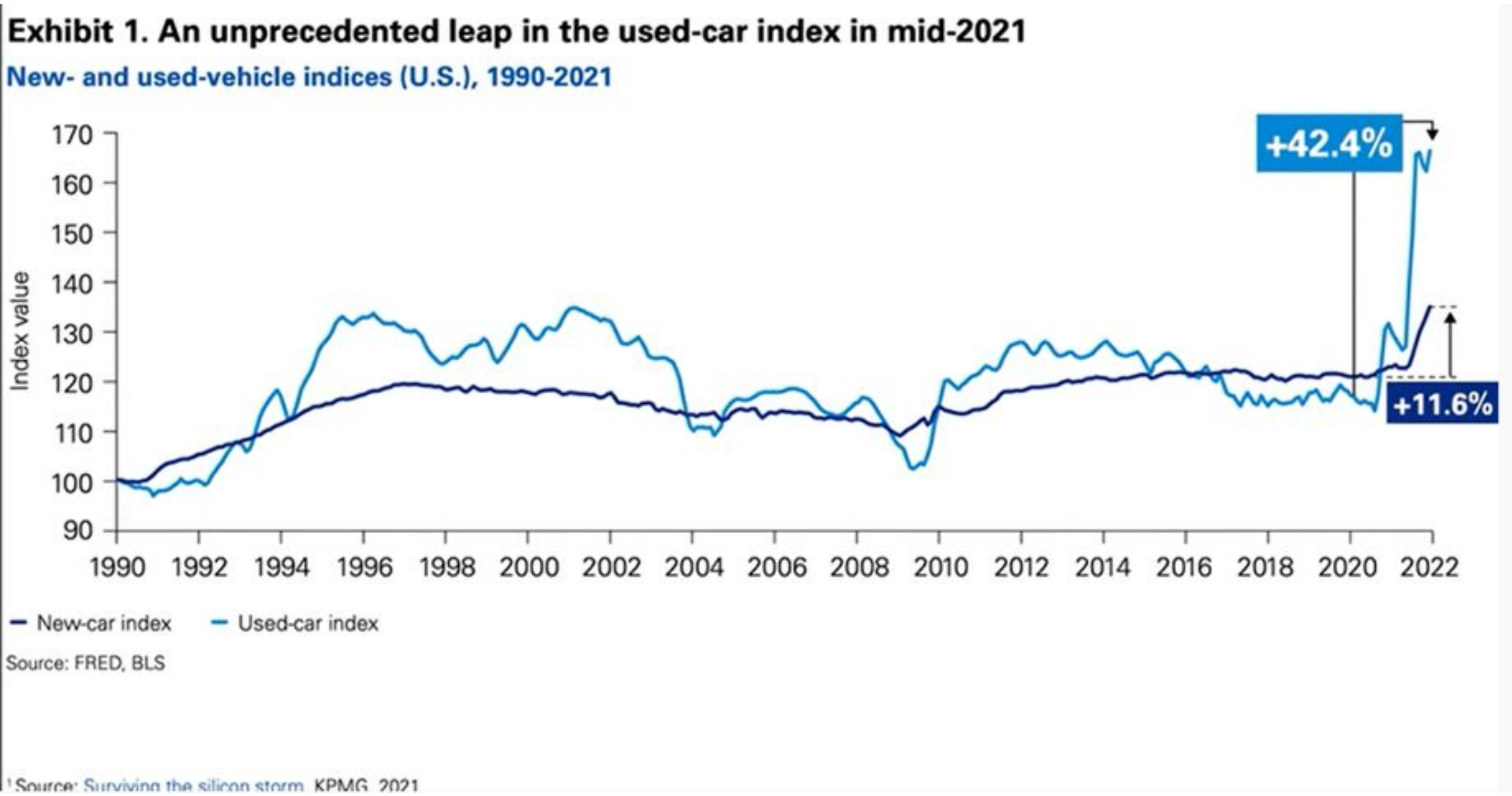


Figure 10. New car index against the used car index in the US has grown 30% more in 2 years. (source: BLS)

- Right now, Americans owe $1.46 trillion in auto loan debt, which represents 9.4% of all consumer debt. It's right below student loan debt which is currently at 10.1%
- Car payments went up from 2020 to 2021 by 18.1%
- *Moody's analytics*: 41.3 months of income to buy a new car
- Majority of car buyers are overpaying for their cars.

The Car market is worth looking at because while standard economic metrics are GDP, Fed fund rates, yield curves and credit spreads, if you take a look at an ordinary American citizen and how they treat car payments during an economic headwind, car payments are usually the first to stop. Currently, we are seeing a record high in default rates while the number of new loans is skyrocketing – which coincides with stimulus check payments.

More than 20% of the loans ending in default and repossession are seen to have been originated on the exact dates of the US government stimulus payment, and banks have been seen to be very loose with their lending, with 96% of borrowers not income verified. Washington DC and Southern states have approx. 30% of their car loans past due. (link: www.experian.com)

The surge in car prices is caused by pent-up demand during the lockdown, the stimulus checks from the government and supply chain shortage due to parts shortages and shipping disruptions, for brand new cars.

Auto loan defaults are rising, though still below the pre-pandemic levels. As of Q1 2022, about 4% of auto loans were 90 days past due. However, subprime borrowers are more likely to default, according to the latest data. In March, 8.5% of subprime borrowers defaulted on their car loans, according to Equifax.

If a consumer stops paying his auto loan and the repo man pays a visit, the bank will be left with an asset that is depreciating rapidly and hence time is of the essence for used cars. We have now seen five consecutive weeks of overall market softening. Since late June, wholesale used car prices have declined by 1.42% from all-time highs.

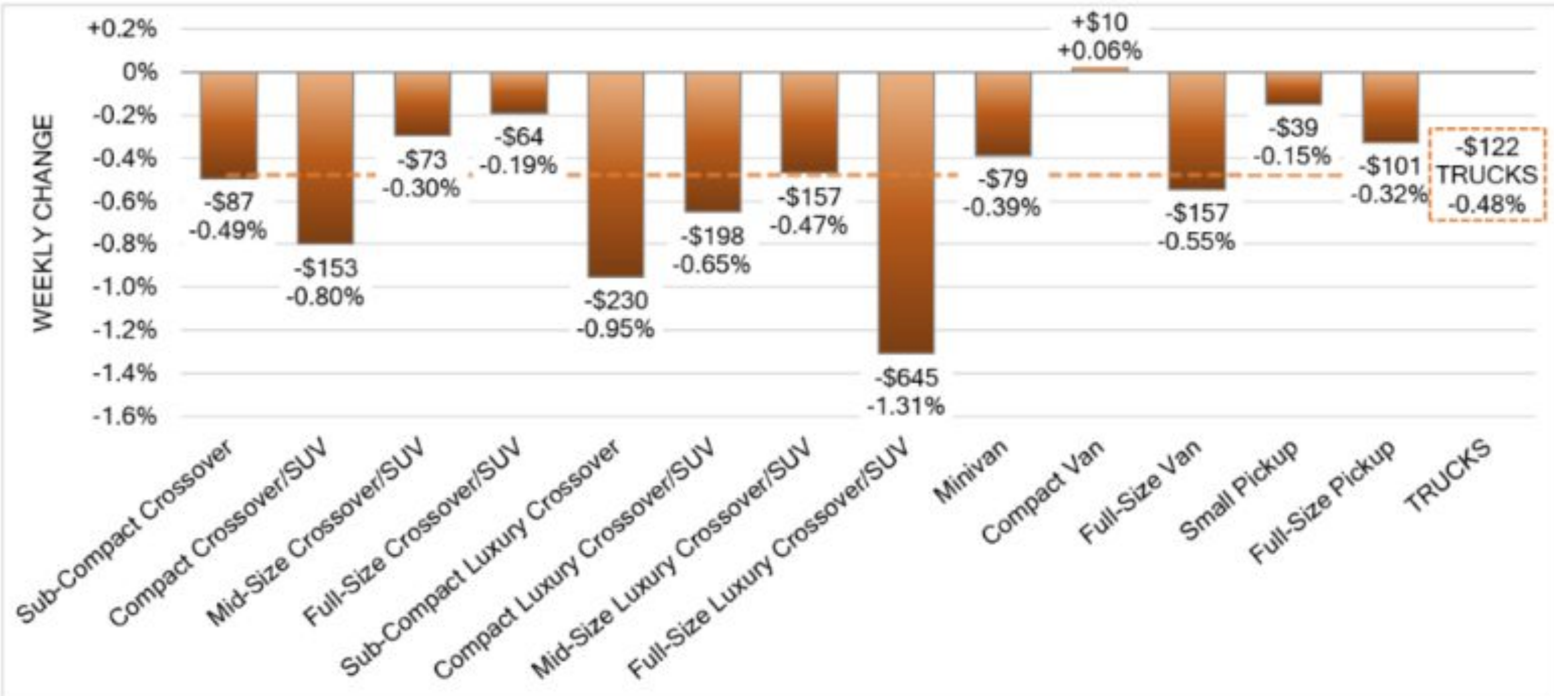


Figure 11. Used crossover, SUV, van and truck prices the week of July 26, 2022. Source: Black Book

Labour Market

We are already in the early stage of demand destruction, yet further pain is expected if the Fed remains hawkish for too long or inflation persists longer than expected. The Fed's most persuasive argument that counters the recession narrative is how strong the labour market is. Thus, it is vital to question if that statement is well-founded.

When the Fed was aggressively hiking rates, it increased the borrowing rate for companies; this affected the growth sector the most. Growth companies rely heavily on cheap cash, and these companies primarily belong to the technology sector. Over the past month, the job postings in the Tech sector have dropped by 17.3%, higher than other sectors such as Media and Communications or Human Resources. (Source: hiringlabs.com)

Though the Tech sector is the earliest to experience this sharp fall in job creation, it is not yet universal. The demand for workers in other sectors remains strong and exceeds the 53% pre-pandemic baseline. The graph below shows that the growth has slowed, but the Fed is convinced this is moderate. Considering the unemployment rate is way below the historical average, the labour market might continue to remain solid.

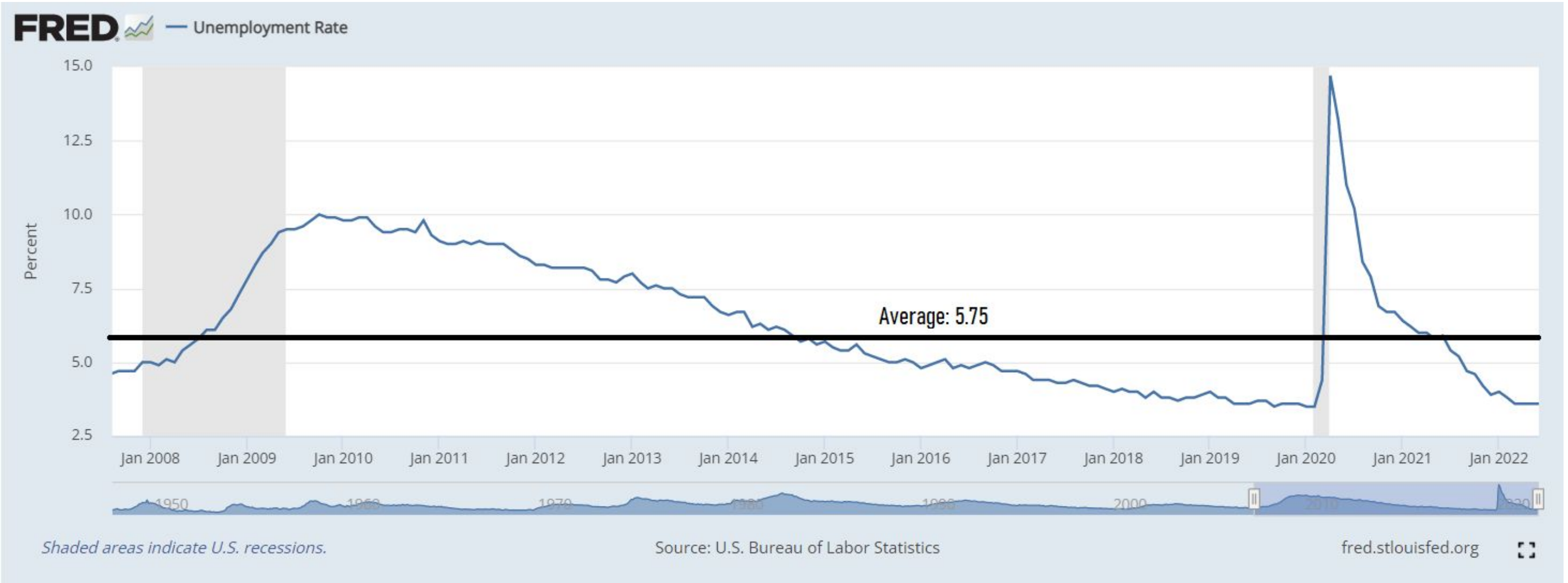


Figure 12: Unemployment rate in the US. We see the percentage fall well below the average of 5.75 to 2020 lows. (source: FRED)

To say that the labour market is robust solely based on unemployment may not be the best method to gauge how American workers are doing in real life. When a company is starting to experience a decline in revenues, the most common behaviour is to cut wages rather than lay off the labour force. According to the Bureau of Labor Statistics, real average hourly earnings for all employees on private nonfarm payrolls decreased by 3.6% from June 2021 to June 2022. The change in real average hourly earnings combined with a decrease of 0.9 per cent in the average workweek resulted in a 4.4 per cent decrease in real average weekly earnings over this period.

Equity Market Update

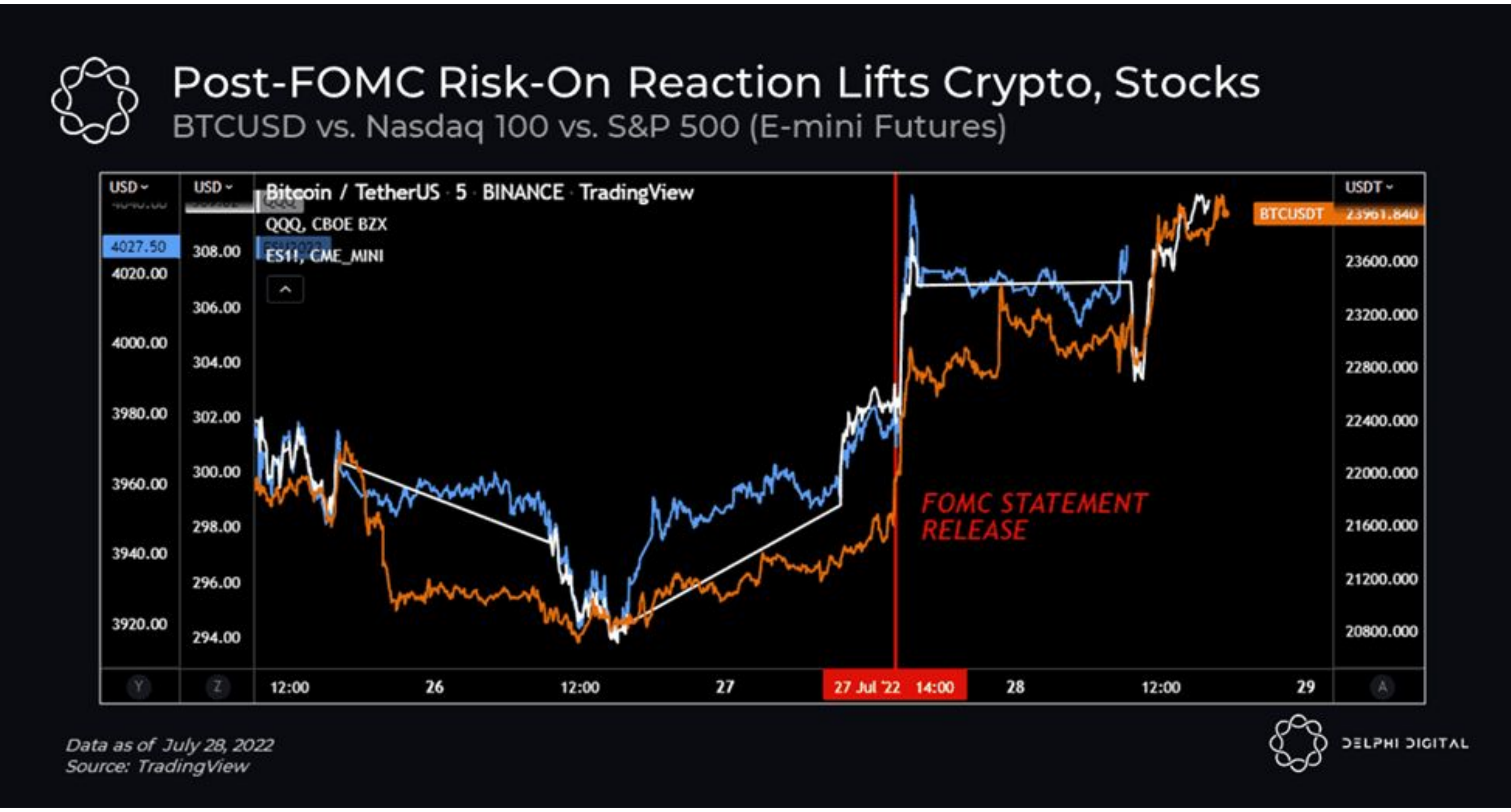


Figure 13. Post FOMC reactions across markets (source: Delphi)

The stock market experienced an unusual rally after the FOMC meeting. When the Fed raised rates in June it jolted the stock market.

Fed Chairman Jerome Powell noted that rates were in line with its estimates of neutral interest rates, a theoretical interest rate that the Fed sees as neither accommodative or restrictive.

Essentially, the neutral rate is the prevailing rate at which the economy delivers its potential GDP growth rate - without overheating or excessively cooling down.

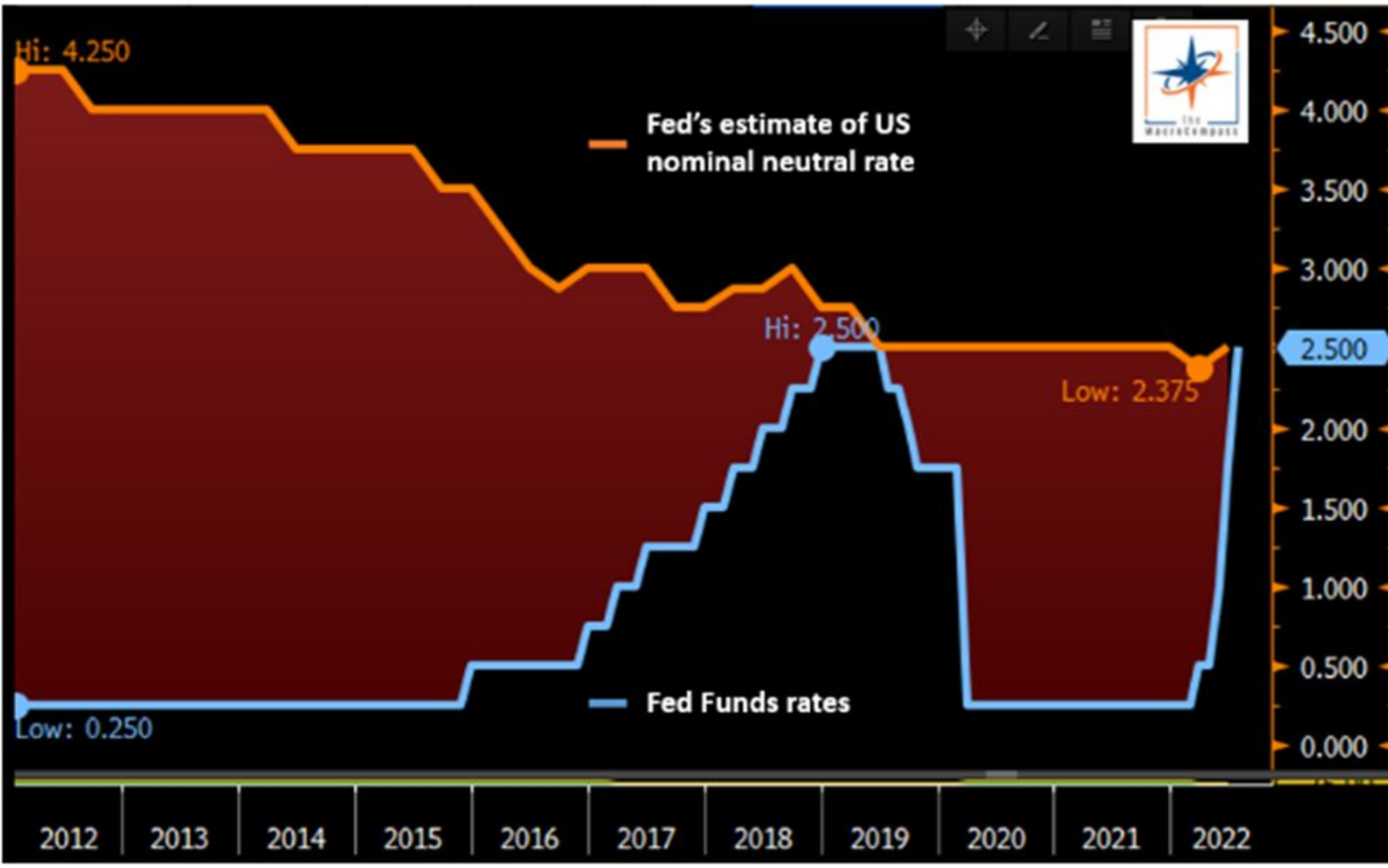


Figure 14. Fed Funds rates vs Nominal Neutral rate (source: Bloomberg)

A fundamental fact is that markets are always forward-looking. If we have neutral rates now, then further hikes are restrictive. If the market hopes that the Fed is close to a deceleration in hikes, it rallies.

Inflation expectations have gone down, as shown earlier in the CPI swaps data, which leads investors to presume that the Fed has done enough. This gives the market the confidence that bond yields will go down, and the market is pricing all other assets around this base case scenario.

When real bond yields decline, investors are more willing to buy higher-risk assets for a better return. When borrowing rates fall, the market expects companies will want to expand. This is especially the case for tech stocks which have higher growth assumptions built into them, hence the Nasdaq, S&P500 and Bitcoin all rallied.

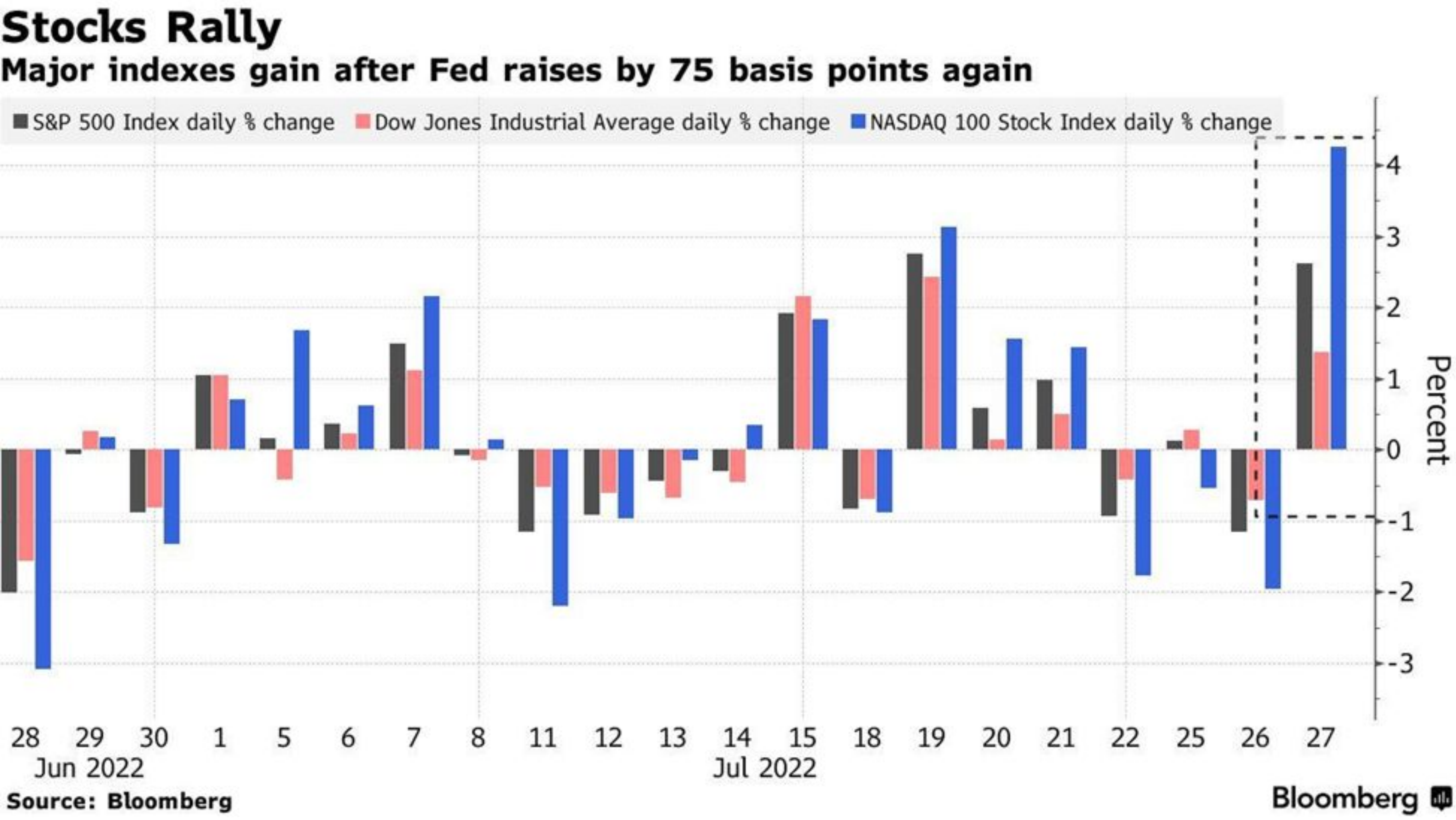


Figure 15. Fed Funds rates vs Nominal Neutral rate (source: Bloomberg)

Earnings Overview

- As of Friday, 10% of the companies in the S&P 500 have released their Q2 earnings
- Apple beat analysts' expectations with record revenue of $32 billion. Earnings per share was $1.20 versus $1.16 expected.
- Microsoft consensus EPS forecast was $2.28, versus reported EPS of $2.23
- Amazon reported a net loss of $2 billion; revenue is currently at $121.1 billion, compared to an expected $119.45. EPS had negative growth of -0.20%.
- Tesla reported total revenues of $16.93 billion, which beat expectations by $2.05 billion and reported an EPS of $2.27, beating expectation by 0.48%
- Google's parent company Alphabet reported weaker-than-expected earnings and revenue. Its revenue is $69.69 billion compared to an expected $69.9 billion with earnings per share of $1.21 vs $1.28.
- Meta Platforms Inc., the recently renamed social media company for Facebook and Instagram, reported its first quarterly sales decline. Shares dropped more than 4% after it reported $28.8 billion in revenue, missing the $28.9 billion average estimate.

Why are these big technology companies important? Because the largest companies in the S&P 500 are dominated by the technology sector. The top 20 stocks, by earnings contribution, are expected to determine 35% of the second quarter's total index earnings, and the top 50 companies comprise 53% of the index's earnings.

The share of S&P 500 companies with positive three-month revisions has declined over the past year from almost 70% to about 30%.

***Figure 16.** Charles Schwab, Bloomberg, as of 7/22/2022.*

Looking at individual sectors for the current quarter, the Energy sector is seeing the highest upgrades while Tech is seeing the most significant downgrades. Higher expected earnings from the energy sector come from rising oil prices and the effect of a more dynamic economy post lockdowns.

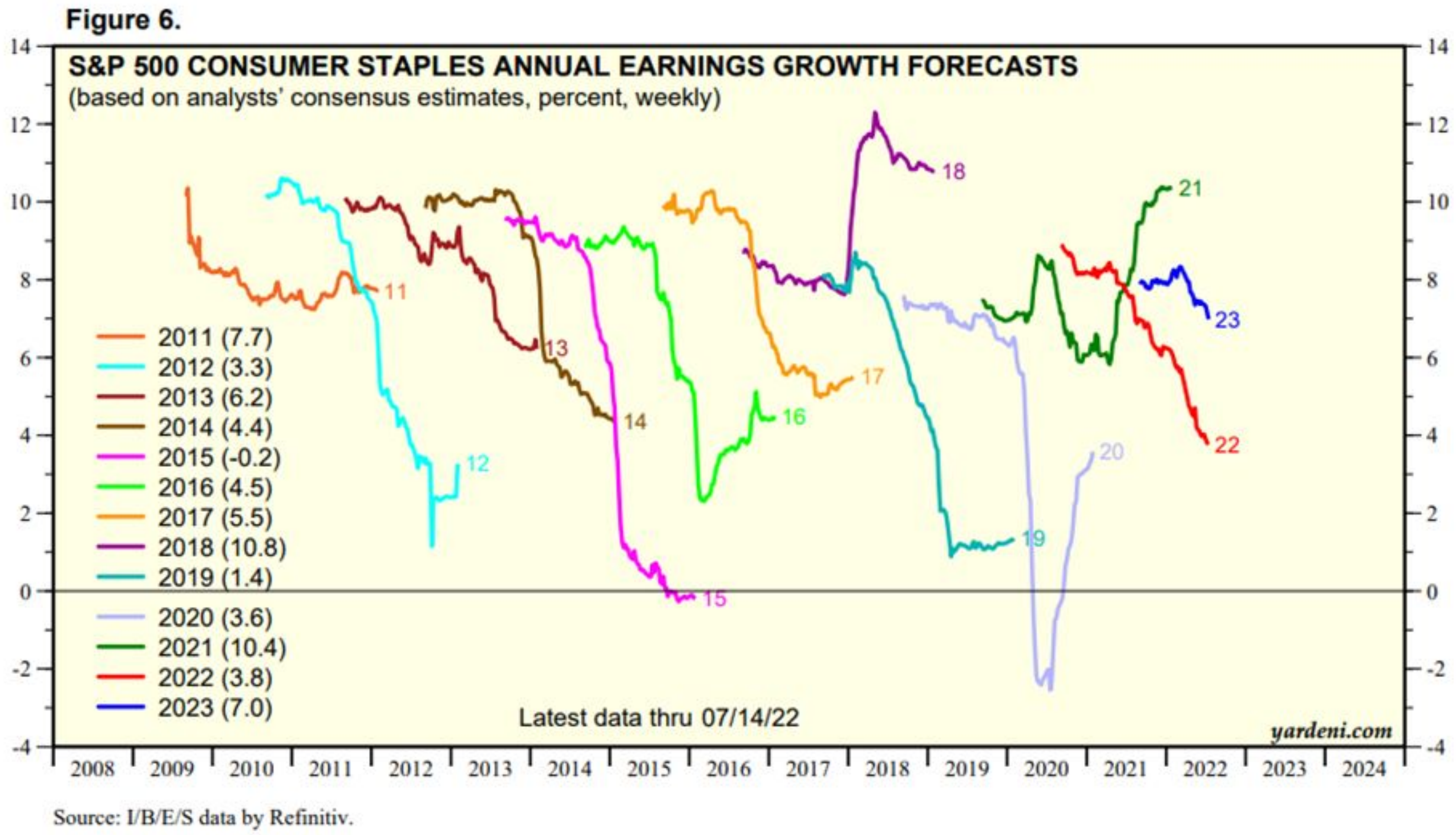


Figure 17. S&P 500 Consumer Staples Annual Earnings Growth Forecast(weekly percentages). (Source: yardeni.com)

Though consumer staples are generally considered a defensive investment for bearish market conditions, the sector is currently at the bottom of the revisions leaderboard, due to higher prices and compressed margins.

CRYPTO NEWS

Oasis Labs and Meta Partner Together

Oasis Labs announced that it was in partnership with Meta, the parent of Facebook, to assess fairness in Meta's products while protecting privacy, using Advanced Privacy Technologies. The partnership was revealed in a Medium blog post on Thursday.

According to The Oasis Labs, the initiative will promote fairness measurement in AI models, benefiting society and improving people's lives.

Built by Oasis Labs, the Oasis Network is a decentralised blockchain network that permits safe and private data sharing and control. The Oasis Network's native token, ROSE has seen strong recent performance among the top 120 cryptocurrencies by market cap. Following the news, ROSE outperformed other significant cryptocurrencies by rallying 35%.

Figure 18. Oasis Labs claims the collaboration with Meta will enable assessment of the fairness of Meta's products while maintaining user privacy

To prevent either the facilitators or Meta from accessing the user's survey results, the data gathered by a third-party survey provider will be shared with third-party facilitators. The facilitators then calculate the measurement using encrypted prediction data from AI models that Meta has supplied cryptographically. Meta then reconstitutes each facilitator's aggregate and encrypted findings into fairness measurement results.

Is Apple suffocating the metaverse?

Figure 19. In an effort to dominate market share in the immersive computing sector. Apple is accused of suffocating competitor growth.

According to Matthew Ball, managing partner of venture capital firm Epyllion Co. and author of "The Metaverse and How It Will Revolutionise Everything," [Apple may be stifling metaverse development](#).

While Apple appears to be in a position to "thrive in the next era" of more immersive computing, Ball believes its control over popular distribution networks is crimping the industry.

"Apple does not permit crypto-based virtual worlds," Ball said Thursday on *CoinDesk* TV's "First Mover" show. "They are successfully stifling a particular type of disruptive innovation and category."

By avoiding complex virtual worlds, the tech behemoth wields undue influence over "what is available and what isn't," according to Ball.

The metaverse is a new computing category that some see as promising. However, the hype surrounding the space, mainly due to crypto market participants, has led to concerns among the tech giants about erosion of their market share.

Pancakeswap introduces vCAKE

Figure 20. The introduction of vCake could potentially revolutionize governance mechanisms in crypto.

PancakeSwap is a decentralised exchange (DEX) based on the BNB Chain that uses an automated market maker (AMM) model to swap BEP-20 tokens. CAKE is their native token.

In a blog post published on Wednesday, the Pancakeswap team announced the launch of vCAKE. vCAKE has a voting power weighted based on the user's number of locked CAKE. According to the team, vCAKE represents the increased voting power based on a user's fixed-term CAKE staking position.

The vCAKE number will also be added to a user's total voting power. vCAKE, unlike iCAKE, is not a new token and is not transferable or tradeable.

CAKE has played a crucial role in governance and voting, two major characteristics that have distinguished PancakeSwap from the competition since its inception. Everyone who has CAKE in their wallet or is staking in the PancakeSwap farms, CAKE pool, or other syrup pools will be able to participate in the governance voting or submit their community proposal for voting.

This new development is essential for the crypto space that has long been drowning in a sea of governance-based tokens with no real utility. Such incentivisation without the issuance of a new token can hopefully be the beginning of a positive trend without token unlocks being feared events which are followed by whales dumping these governance tokens. This could help promote retail investor-based backing of projects and protect some projects from the 51% attack wherein a solitary external party takes control of a majority share in the governance process.

Facebook parent Meta lost $2.8 billion on its Metaverse division in Q2.

Figure 21. Facebook inc was rebranded to Meta Platforms Inc in 2021.

According to its earnings report released Wednesday, Meta Platforms (FB) reported a $2.81 billion loss in its Facebook Reality Labs ('FRL') division, which includes its augmented and virtual reality operations. According to *FactSet*, this was slightly lower than the division's loss of $2.96 billion in the first quarter and better than analyst estimates of a loss of $3.67 billion for the quarter.

FRL earned $452 million in revenue in the second quarter, down from $695 million in the first. That was a small portion of the $28.4 billion generated by Meta's family of apps, which includes Facebook, Instagram, and WhatsApp, in the third quarter.

According to the company, reality Lab's revenue is expected to be lower in the third quarter compared to the second quarter.

In the fourth quarter of last year, Meta announced that it would break out results for the division to show performance and investments in a group that it considers critical to the next generation of online social experiences.

For 2021, Meta reported a loss of $10.2 billion for FRL, on revenue of $2.3.

Babel Finance loses $280 million of customer funds.

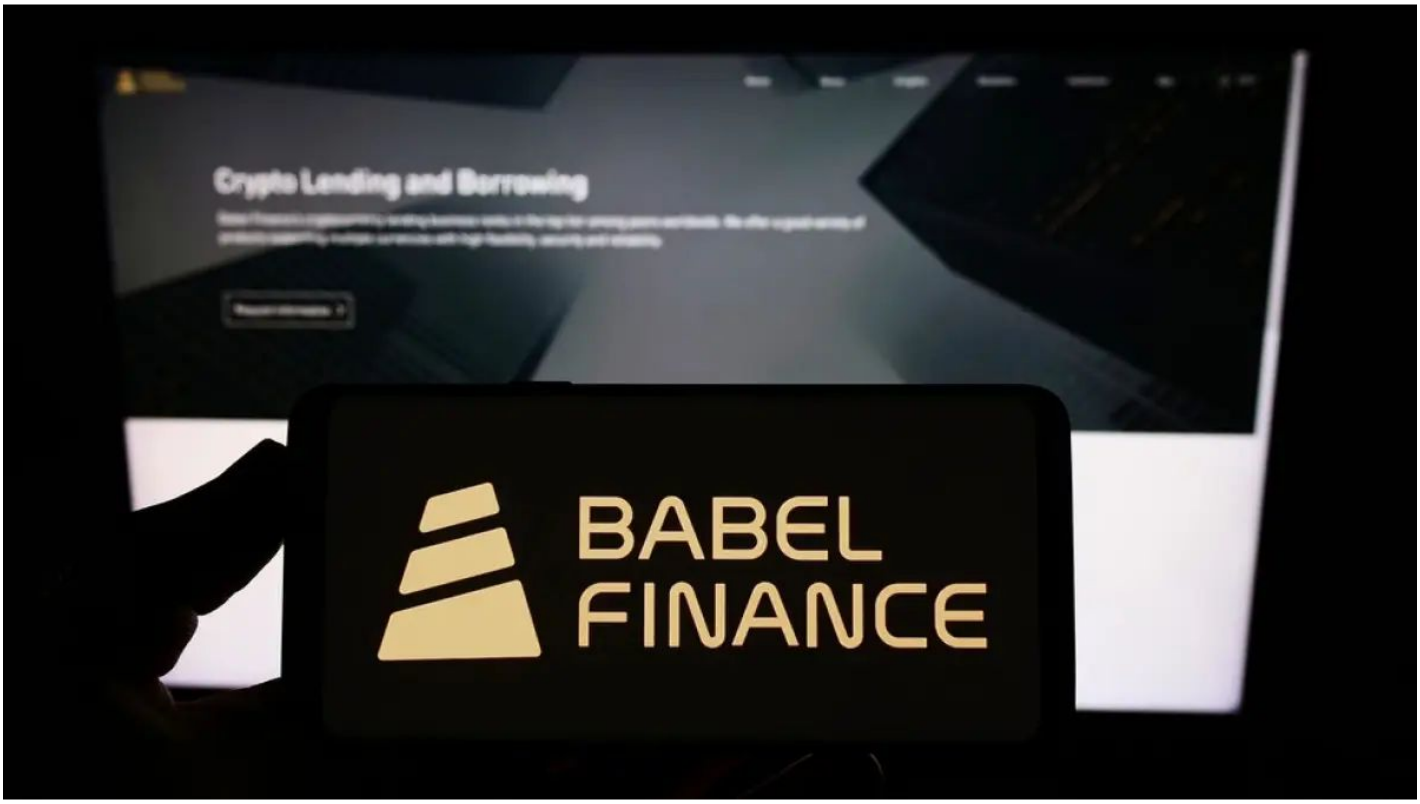


Figure 22. After freezing withdrawals in June. Babel Finance has been forced to liquidate assets.

The Block reported that Babel Finance, the embattled Asian crypto lender that unexpectedly froze client withdrawals last month, sustained substantial losses owing to proprietary trading with customer funds.

Babel Finance lost more than $280 million in Bitcoin (BTC) and Ethereum (ETH) owing to a proprietary trading disaster, losing over 8,000 BTC and 56,000 ETH in June after being forced to liquidate assets due to a substantial market collapse.

"During [a] turbulent week in June, when BTC plummeted abruptly from 30k to 20k, unhedged positions in [proprietary trading] accounts notched up large losses, directly contributing to the forced liquidation of numerous Trading Accounts and wiping out 8,000 BTC and 56,000 ETH," a presentation on Babel Finance disclosed.

"Conclusion: Single point of failure - The Proprietary Trading team's unsuccessful operation lies outside of the company's typical operations, which has otherwise been running well with sufficient management and control," Babel Finance said.

Babel Finance's proprietary trading operation is described as "risky," yet it failed to hedge its bets.

According to the presentation, "a proprietary trading team manages various trading accounts that are not managed or supervised by the Trading Department; no trading mandate or risk controls were applied for these accounts, and no PnL [profit and loss] was recorded."

Ethereum chain split following the Merge. Will the price of ETC continue to rise?

The proof-of-work ('PoW') model for Ethereum, powered by GPUs, brought in almost $19 billion in income for miners of ETH in 2017. However, these sources of income are in jeopardy since Ethereum is anticipated to switch to a proof-of-stake (PoS) network through "the Merge" in September.

After the hard fork chain split, miners may then rebel against the new upgrade by continuing to mine on the outdated Ethereum PoW.

Following the completion of five crucial steps, according to Ethereum founder Vitalik Buterin, Ethereum will be able to handle "100,000 transactions per second". The five steps are The Merge, The Surge, The Verge, The Purge and The Splurge. Below is an illustrated flow.

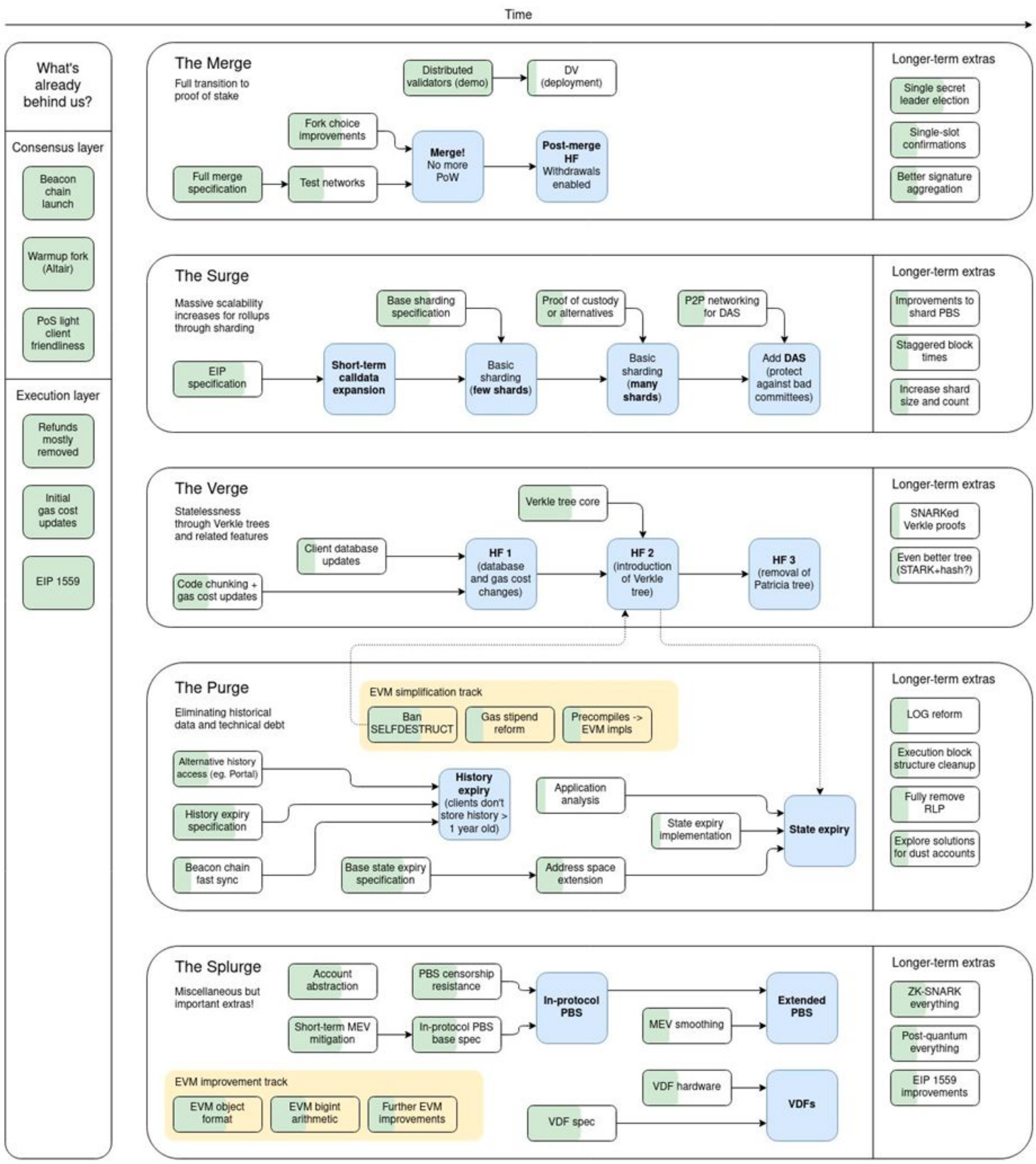


Figure 23. Flow diagram for the 5 step process for Ethereum.

According to a study conducted by cryptocurrency hedge firm Galois Capital, 33.1% of respondents think that the Merge would result in the creation of two parallel blockchains, ETH1 (PoW) and ETH2 (PoS).

This helps to explain why Ethereum Classic's continued price surge (up from $25 to almost $45 in the last week) looks highly speculative, given that the chain is still only being used by a small number of projects. As a result, following the Merge, ETC is at risk of a "sell the news" situation. Additionally, a future ETH1 PoW chain may reduce interest in ETC drastically.

Bitfinex, Tether and Holepunch launch Keet

On July 25th, Holepunch announced the launch of a fully encrypted video calling application called Keet.

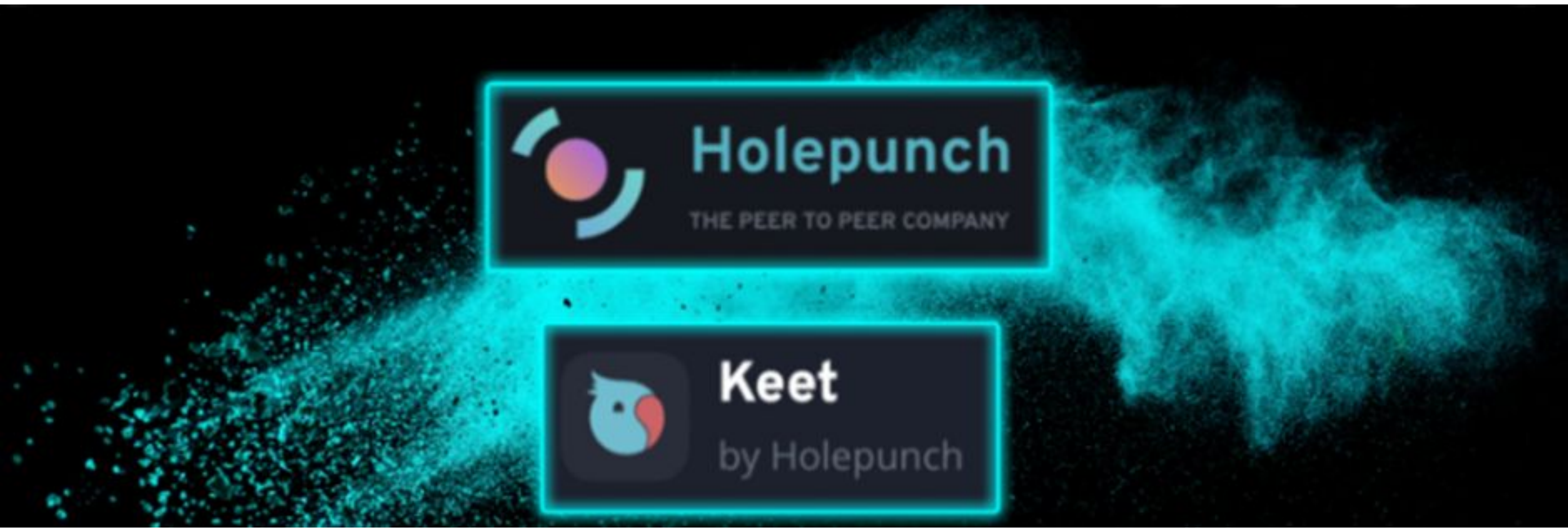


Figure 24. Keet aims to eliminate the need for central servers for communication while protecting user data at an unprecedented scale.

Harvesting user data has become the primary revenue source for big tech. After the Facebook data breach in 2021, when more than 500 million users (as per official numbers reported), possibly billions, had their private information leaked, mass legal action regarding data privacy followed suit. Despite various efforts, the monopoly of certain technology companies in the social media and communication industry has prevented any substantial change.

Holepunch is a fully encrypted platform for building peer-to-peer(P2P) applications. They aim to combat censorship, data harvesting, and to empower freedom of speech while facilitating global communication via P2P technology. Keet is the first product to be built on Holepunch and is in the same pursuit of privacy and an escape from freemium services for data storage. It is a free app that utilizes P2P connections to facilitate free video/audio calls and file sharing without size restrictions. Keet users can initiate a call directly to another individual's computer. This allows for video chatting to take place without a central server or company operating the network.

Backed by Bitfinex and Tether; the Tether and Bitfinex CTO Paolo Ardoino also serves as Chief Strategy Officer for Holepunch. He announced the project and updated that tens of thousands of people are already utilising Keet while praising the unprecedented potential of the project.

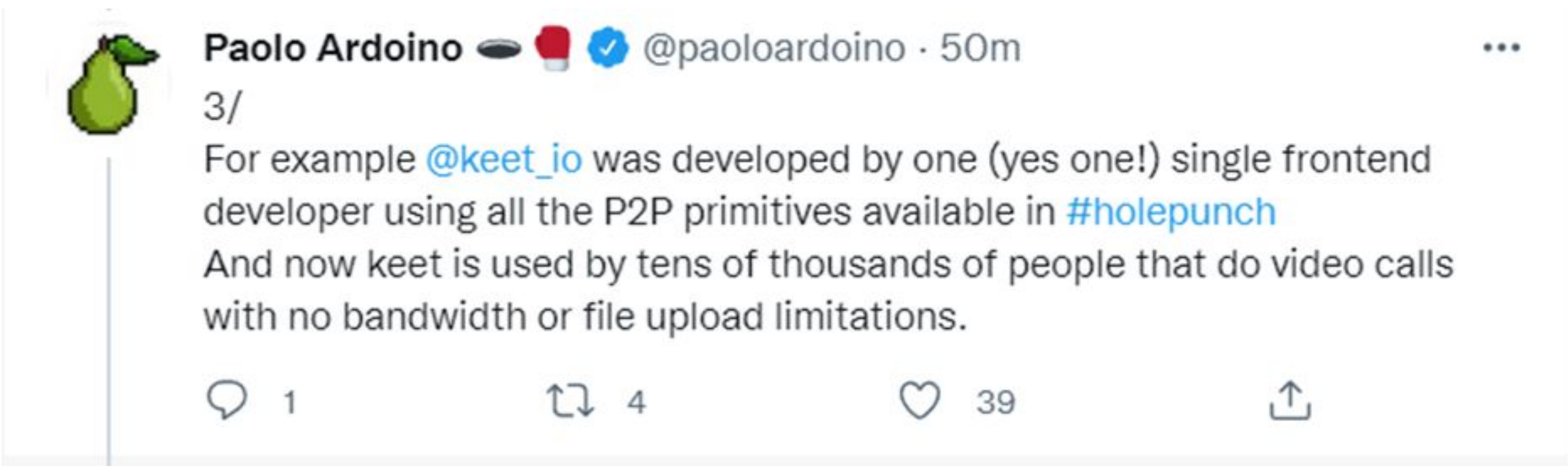


Figure 25. Paolo Ardoino talks about how Keet is revolutionizing calling and file sharing with no bandwidth and file size limitations. (source: https://bit.ly/3zdz724)

WHAT'S ON-CHAIN THIS WEEK?

Reasoning behind the recent uptick

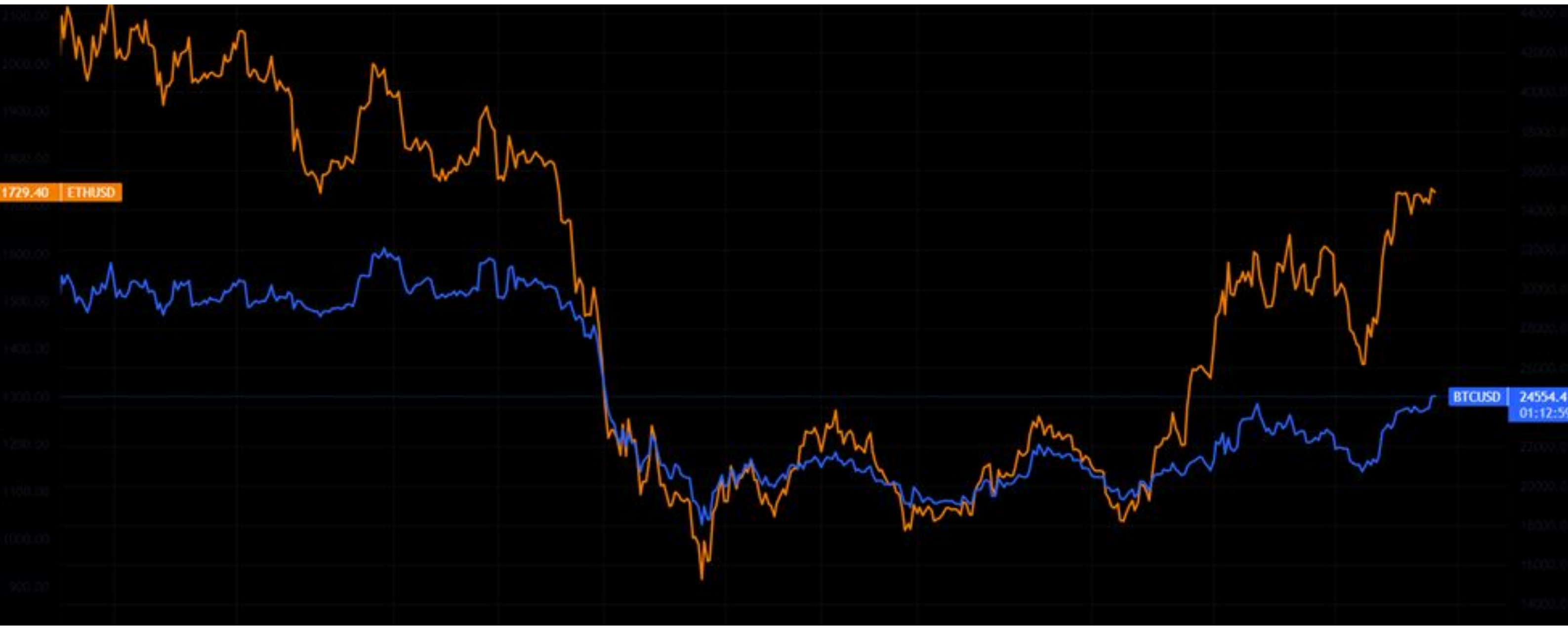


Figure 26. Update on BTC and ETH price action over the week

The price of Ethereum saw an unexpected surge last weekend. In four days, the price of ETH rose by more than 40%, while the price of BTC rose by less than 10%. There was groaning among the shorts: more than $600 million in Delta 1 contract shorts were liquidated, while Ribbon Finance, one of the well-known sellers in the OTC crypto options market, added an at-risk position in ETH options with a notional value of $57 million overnight, as reported by *Deribit.*

Figure 27. Liquidation data for BTC (source: Deribit)

The liquidation data for Bitcoin reveals that the recent move up was primarily initiated by significant absorption of market sell orders and then fueled by short liquidations. As such, it is important to carefully assess market conditions before re-entering.

Ethereum leading the crypto market

As discussed above, Ethereum has outperformed Bitcoin for two consecutive weeks after months of underperforming BTC, even in bearish market conditions.

Figure 28. Futures Open Interest on ETH across major exchanges (source: coinglass)

With the “Merge” narrative alongside a fresh tailwind for the crypto markets after a 75 bps rate hike, ETH contracts and derivatives have amassed the most interest from investors as we witness retail on-chain presence in the market for the first time since April-May.

However, ETH’s implied forward yield has not changed significantly from last week as liquidity has not improved at the macro level. This means that the overall bid ceiling for investors in the current situation is still relatively low. As buyers and sellers balance out, prices and exposure rise together, creating a peculiar steady status in the bear market.

Figure 29. Futures premium above index price for Ethereum (source: Deribit)

This steady state is probably temporary. In addition to the Bitcoin short squeeze data, with the arrival of delivery of options, the release of margin and hedging positions will bring considerable selling pressure. Positive delta of nearly 90,000 ETH (based on *Deribit* data) has accumulated in the options contracts expiring at the end of July alone, which is comparable to the quarterly contracts expiring on September 30. There should be significant selling pressure after options delivery. Thus, with the Bitcoin and Ethereum price action and on-chain data at such a crossroads, the only thing that is a certainty is volatility.

MVRV-Z score update

While we have covered the Market Value Realised Value-Z score and its relevance to Bitcoin in previous issues, it is beneficial to assess the model for Ethereum as well, which itself has historically provided insight into the behaviour of the entire altcoin market.

MVRV Z-Score is an on-chain metric that is defined as the ratio of the difference between market cap and realized cap and the standard deviation of market cap. Further, the realized cap is a variation of the market cap that uses the price at which tokens were last moved, instead of the current market price.

In a nutshell, a sub-zero MVRV Z-Score means that a majority of spot Ethereum purchased is trading at a loss as the market price now trades below the realized price.

Figure 30. Ethereum price vs MVRV-Z score contrasted (source: Delphi)

A score below zero has previously been efficient to gauge mid to long term bottoms for Ethereum as well as Bitcoin. The metric turned highly negative in March 2020, when it reached -0.5 (approx.) to mark the bottom for the next two years. Similar MVRV-Z levels have been witnessed in June and July.

A confluence of various relevant metrics is crucial to any analysis and thus, the score must be used in tandem with other metrics that we discuss further before we feel comfortable with a bottom confirmation. With a macro-driven market, further downside or a consolidation period may be required to establish a proper bottom.

Purchasing power and Long Term Holder update

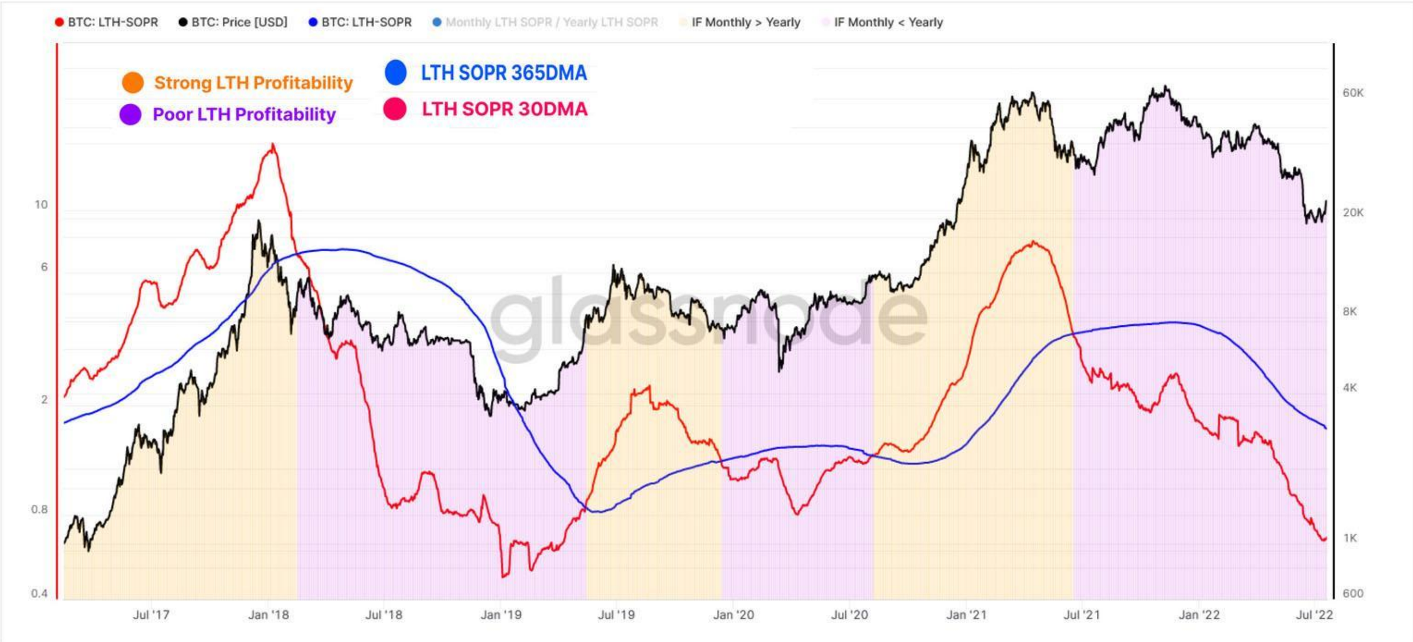
Figure 31. SSR ratio for Bitcoin.

Above is the stablecoin supply ration ('SSR'), the ratio of the market cap of BTC divided by that of all stablecoins. Low values of SSR suggests that stablecoins can purchase a large percentage of the BTC supply (if we imagine a closed vacuum in the market between BTC and stablecoins).

A decreasing trend shows us the rising status of stablecoins' buying power. We believe this shows us that on the higher time frames, users are still waiting for the macro environment to change to risk-on, holding their capital in stablecoins.

During a bear market, long term holders experience significant drawdowns. Below is the monthly and annual spent output profit ratio ('SOPR'), for long-term holders. The SOPR is the ratio between the selling price (realised loss/mitigation of further drawdown) and the purchase price of the coins.

LTH SOPR Monthly / Yearly



 glassnode

Figure 32. Monthly and Yearly SOPR on BTC (source: glassnode)

When the monthly profitability is greater than the annual profitability, it means that the market is overheated. When annual profitability is greater, it means that long-term holders are experiencing stabilised higher returns but short term drawdowns could potentially be severe. We can see that the current levels of the monthly long-term holder SOPR has already reached the level close to the 2019 bottom and has fallen way below the 2020 bottom.

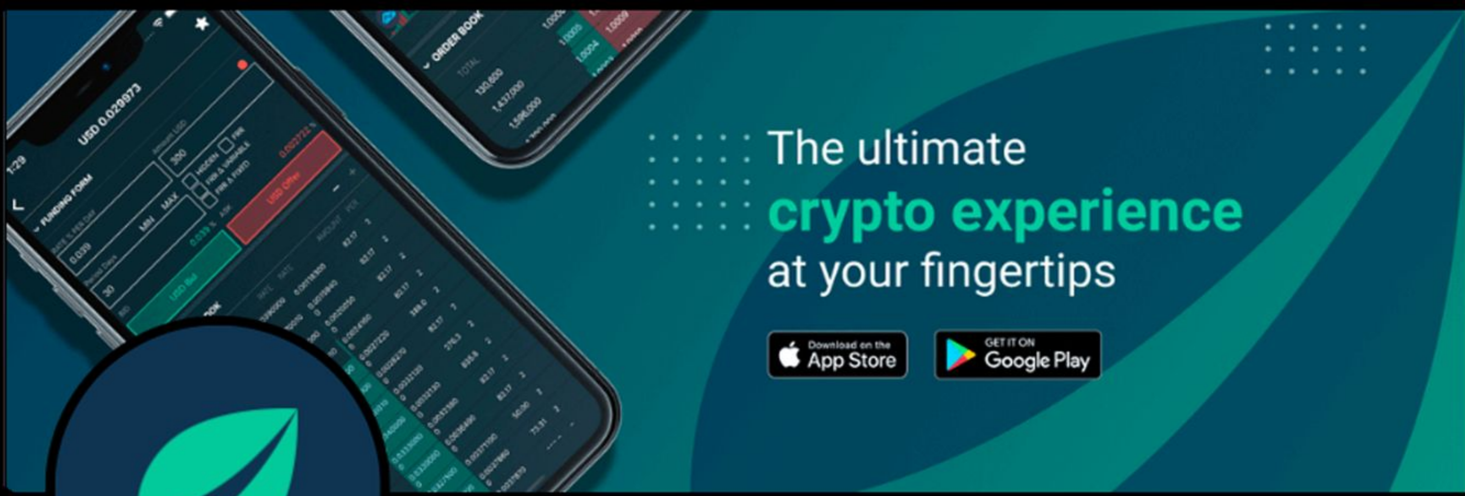
Bitcoin: Net Unrealized Profit/Loss (NUPL)

 glassnode

Figure 33. Net Unrealized PnL on Bitcoin with emotional index. (source: glassnode)

The Net Realized Profit/Loss is an on-chain indicator that shows if the market is in a state of aggregate loss. It is the difference of unrealized loss and unrealized profits. The indicator is negative when the unrealized losses are higher than unrealized profits and opposite is true when unrealized profits are higher than unrealized losses.

On June 13 the NUPL turned negative first time since March 2020. Now, the NUPL has moved to positive territory. When NUPL crossed the negative to the positive territory, this has historically marked the bottom of the bear market. This happened in the 2015, 2018 and 2020 bottoms. The current rise of NUPL to the positive territory can be a sign that the market could be back on track after a capitulation.



https://t.me/bitfinex

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