BITFINEX Alpha

Issue: 03-04-2023
bitfinex.com

EXECUTIVE SUMMARY

The current macroeconomic landscape presents a mixed outlook with several challenges still to overcome. In a recent speech, Federal Reserve Governor Philip Jefferson made it very clear that the US central bank's commitment to addressing high inflation while minimising adverse effects on the US economy, was unwavering.

In the US housing market, the rise in pending home sales provides optimism that buyers are entering the market, but the residential construction sector is still experiencing a downturn. High mortgage rates and tightened lending standards cast uncertainty on the housing market's future. A weaker housing market can have exaggerated effects on any economy given the wealth effect people feel in relation to the value of their homes. If house prices go up then people tend to feel happier, but if they go down the impact can be profound.

A slight increase in jobless claims and lower GDP growth, driven by reduced service spending and corporate profits, indicate that the economy is weakening. Indeed, worries over the possibility of a recession are reflected in the University of Michigan's latest survey on consumer sentiment, which shows a decline in March - the first decrease in four months.

In the face of this data, however, the Fed's preferred inflation gauge, spending, as well as income data for February showed a cooldown, suggesting that the Federal Reserve's efforts to combat inflation are making progress.

The moderation in inflation helped stocks achieve their third consecutive weekly gain, with the Nasdaq Composite up over 17 percent for Q1 2023. Despite a banking crisis and a changing interest rate outlook, the stock market reported impressive quarterly gains.

That optimism is also reflected in some Bitcoin metrics, but not all. Non-zero balance addresses surged, hit a new record, but the number of active addresses and the number of daily transactions have experienced a fall. While this is not a bearish indicator, it suggests that amid range-trading conditions, the short-term market outlook is unsettling.

In contrast, BTC and Ether options open interest on the CME reached an all-time high, indicating an increase in institutional trading activity, but Bitcoin's recent price performance has also brought it in closer correlation again with the S&P 500, raising questions about its vulnerability to macroeconomic headwinds. Low liquidity in the crypto market also raises concerns about increased price volatility and market stability. The current market situation calls for caution against over-leveraging or a heightened risk appetite during this transition period in the crypto market.

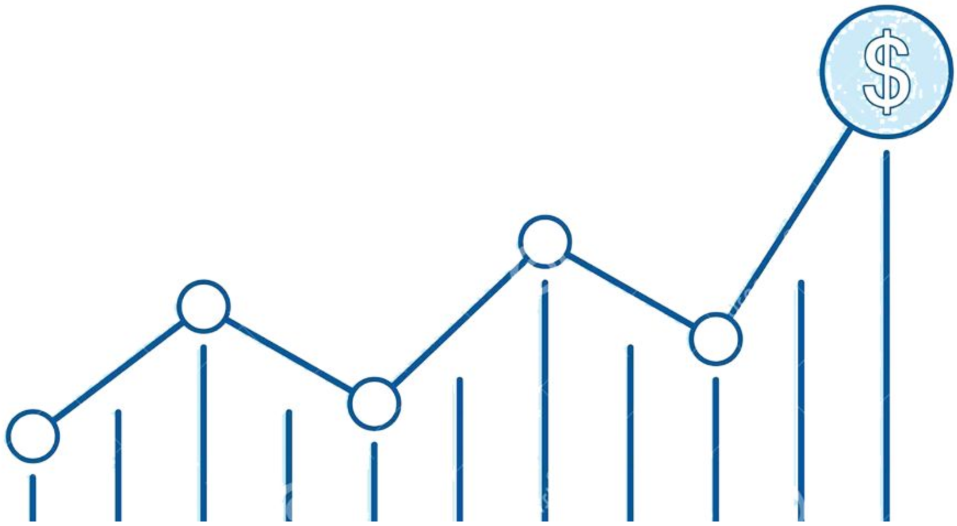
Meanwhile, the crypto world continues to be nothing but interesting, and forms a colourful backdrop to the economic and market sentiment we report on weekly.

The CFTC filed a lawsuit against Binance, alleging multiple violations of the Commodity Exchange Act (CEA), including KYC and AML laws. Binance CEO Changpeng Zhao denies the allegations. A US District Court also blocked Binance US' acquisition of troubled Voyager Digital, casting doubt on the future of the deal. FTX founder Sam Bankman-Fried now faces bribery charges in a new indictment, accusing him of bribing Chinese officials; and Galaxy Digital reported a $1 billion loss in 2022, with founder Mike Novogratz calling it a "formative year" for the company.

In more positive news, Michael Saylor's MicroStrategy continued its Bitcoin buying regime, increasing its holdings by 6,455 BTC. Tether's USDt stablecoin dominance surged in March 2023, reaching an all-time high of 57.5 percent of the total stablecoin market share; and Ethereum's Shapella upgrade is set to launch on April 12, promising significant improvements to transaction processing, security, and network efficiency.

Happy Trading!

INDEX



GENERAL MARKET UPDATE

Federal Reserve Governor Cautions That Curbing Inflation will Take Time

Federal Reserve Governor Philip Jefferson emphasised during a speech last week that the US central bank's commitment to tackling high inflation while minimising any adverse effects on the economy was absolute. During his speech at Washington and Lee University in Lexington, Virginia, Jefferson acknowledged the stickiness of some key inflation inputs, in particular services excluding housing. He also highlighted the need for a cautious approach to returning inflation to a target of two percent.

The Federal Open Market Committee (FOMC) is striving to balance price stability with financial stability in the wake of the second-largest bank failure in US history. Jefferson stated: "It is going to take some time because there are components of inflation that have turned out to be quite persistent — for example, services excluding housing." He added, "We have to do it in a way that does not damage the economy any more than is necessary."

To this end, the Federal Reserve raised interest rates two weeks ago, by 25 basis points (bps) in its March Federal Open Market Committee's (FOMC) meeting, which is part of more than a year-long effort to cool price pressures despite the recent turmoil in the banking system. The new policy benchmark is now a target range of 4.75 to five percent, up from near zero just a year ago. Such a progression demonstrates the determination the Fed has exhibited in tackling inflation over the last 12 months. The median projection of the 18 Fed officials suggests that rates may reach 5.1 percent by the end of the year, implying one more hike, as we indicated in last week's *Bitfinex Alpha*.

Despite the recent turmoil in the banking system, economic data through February reveals a robust labour market with a low unemployment rate of 3.6 percent and resilient consumer spending. However, the collapse of Silicon Valley Bank earlier this month led to a trust deficit among market participants which has impacted credit availability, a situation policymakers will monitor closely. Jefferson further stated that the Federal Reserve is still learning about the full effect of its tightening policy so far given the long, variable and highly uncertain lag effect between monetary tightening and real economic impact.

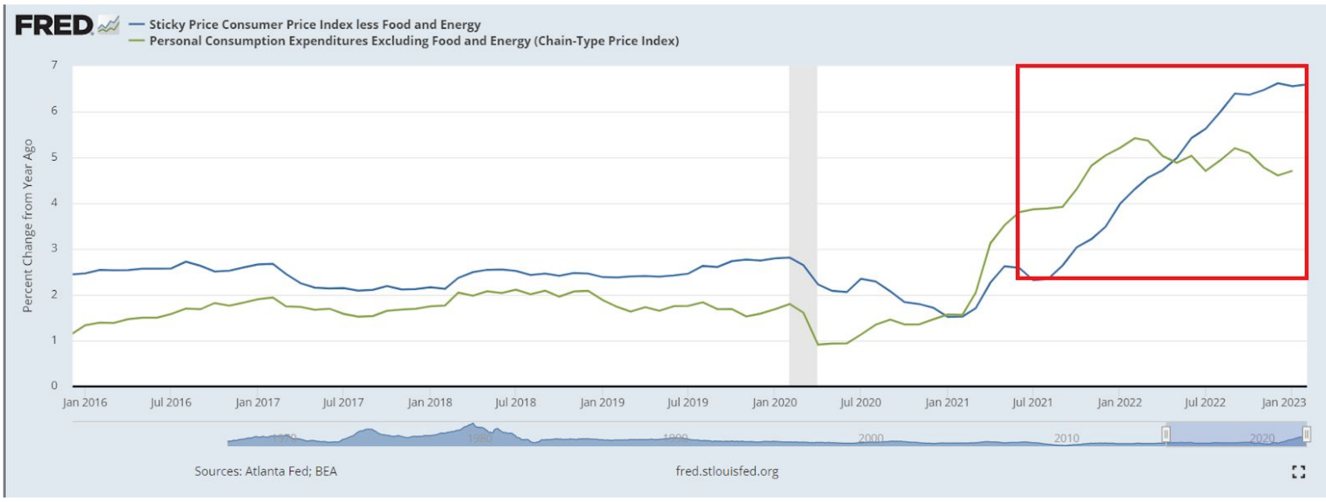


Figure 1. Core Consumer Price Index and Core Personal Consumption Expenditures still remain elevated, above pre-pandemic levels.

Despite the Fed's efforts to tighten monetary policy, stubborn inflation remains a challenge. Though it is showing signs of easing, the inflation rate is still significantly higher than pre-pandemic levels (Figure 1). The persistence of inflation can be attributed to several factors, including supply chain disruptions, labour market tightness, and energy prices. In recent months, inflation has shown some signs of easing, but the full impact of monetary policy tightening is yet to be realised.

In conclusion, the Federal Reserve is committed to bringing down the current high inflation rate in the US economy to two percent as soon as possible. While recent data shows a slight easing in inflation, it is essential to remain cautious about the future price trajectory for goods and services. Considerable work lies ahead for the Fed in managing and controlling inflation. As the Fed continues to seek a balance between inflation and financial stability, close monitoring of economic indicators and effective use of monetary policy tools will be crucial in navigating the complexities of the current economic landscape. As the full effects of monetary policy tightening are yet to be realised, it is essential for policymakers, market participants, and the public to remain informed and prepared for any shifts in economic conditions.

US Pending Home Sales Rise Amid a Mixed Housing Market Outlook

Pending home sales is increasing, indicating positive news for the US housing market, but residential construction is still experiencing a downturn. This is concerning for the future of the housing market, as it will likely contribute to an increase in prices at a time when mortgage rates are and lending standards have tightened.

In February, pending home sales in the United States increased for the third month in a row. An increase in pending home sales indicates buyers are entering the market and thus providing some optimism for the housing market. The National Association of Realtors (NAR) monthly index, released on Wednesday, March 29, reported a 0.8 percent increase in US pending home sales. However, this increase was smaller than the previous month's 8.1 percent rise. This development comes amid a generally slowing economy and concerns about the state of the residential construction sector.

While the pending home sales data offers some positive news, there are mixed signals from the residential construction sector. According to the US Census Bureau, the Seasonally Adjusted Annual Rate (SAAR) of residential construction spending hit a record high of $945.2 billion in May 2022. However, spending dropped steadily each month for the remainder of the year, reaching $857.2 billion in December (refer to Figure 2).

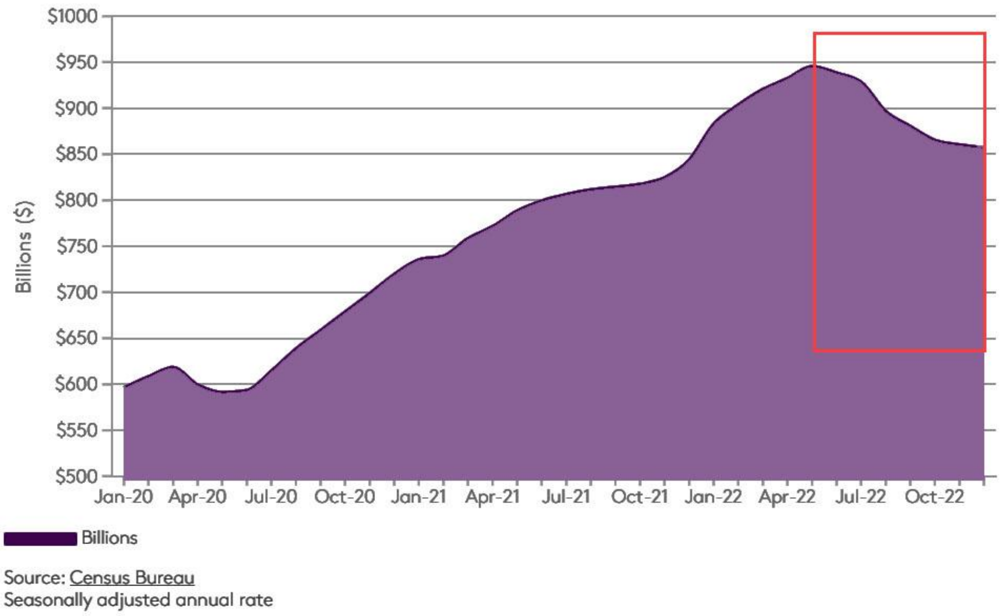


Figure 2. US Residential Construction Spending Falls from the First Half of 2022 (Source: Census Bureau)

The issuance of building permits, a reliable leading indicator for residential construction spending, peaked in March 2022 and has not shown signs of bottoming out yet. This suggests a significant uptick in residential construction spending is unlikely within the next three to four months.

The declining residential construction spending and rising pending home sales amidst higher mortgage rates suggest that home buyers may be expecting mortgage rates to remain high and possibly go higher. Consequently, prospective homebuyers may be more inclined to consider older homes that are currently on the market instead of waiting for new homes to be built.

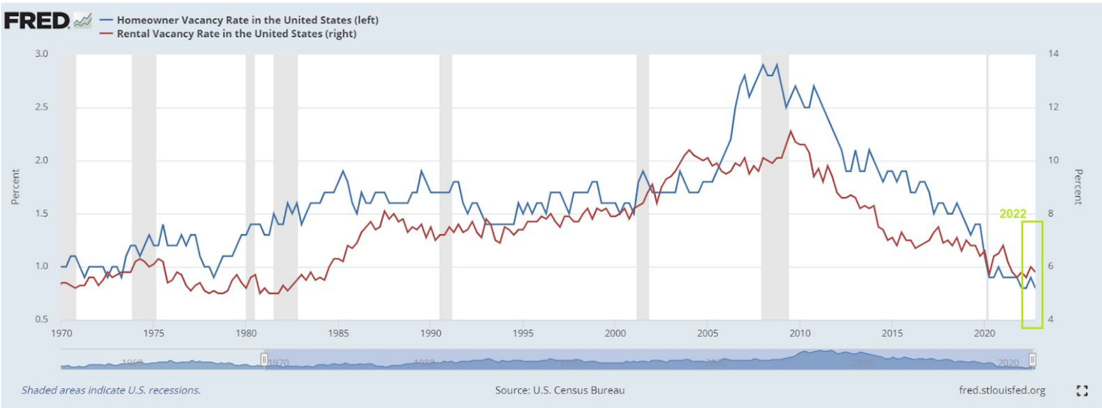


Figure 3. Home Vacancy Rate for the United States (Source: US Census Bureau)

Another possible reason for the increase in pending home sales is the inadequate supply of new housing to meet the demand for homes, resulting in a shortage of available properties. This could be attributed to factors such as labour shortages and elevated material costs.

The US already has a multimillion-home shortage. This trend of home shortages can be seen in vacancy rates, both for homeowners and tenants. The US Census reports that vacancy rates are at historic lows (Refer to Figure 3).

A low rate of homeowner and rental vacancies implies a shortage in housing supply, as it indicates that there are insufficient units available to meet the needs of potential tenants and buyers. The vacancy rate refers to the percentage of occupied rental and owned housing units. The homeowner vacancy rate was 0.8 percent in the final quarter of 2022, the first time it has been this low in 66 years. The rental unit vacancy rate was 5.8 percent at the end of 2022, with the last recorded vacancy rate at this level occurring in the late 1980s. With the Federal Reserve's attempts to slow lending and cool the economy by raising interest rates, it is unlikely that the housing supply shortage will be eased soon.

Despite the rise in pending home sales, the Average US mortgage rate has doubled since January 2022 and currently sits at 6.32 percent as of March 30, according to *Freddie Mac*, a government-sponsored mortgage loan company. We expect this to climb higher if the Fed continues hiking this year, potentially impacting home buyers' purchasing power.

In conclusion, the recent rise in US pending home sales offers a positive short-term relief in the housing market. The housing market's long-term outlook, however, is uncertain. The housing market has been squeezed by high mortgage rates from the aggressive interest rate hikes delivered by the Federal Reserve in its battle to tame high inflation. Moreover, financial market stress has caused banks to tighten lending standards, which could make it harder for prospective homebuyers to borrow. Supply also remains tight, which may prevent an outright decline in house prices.

Jobless Claims Inch Higher; Revised GDP Shows Softer Economic Growth

Although unemployment claims in the US remain at historically low levels, there has been a slight increase recently. Gross Domestic Product (GDP) growth has also been softening with lower service spending and corporate profits showing up in the numbers. Both job and GDP data suggest a slowdown in economic growth and an increased risk of a recession.

The United States has seen a moderate rise in jobless claims, reflecting a slight hiccup in the labour market's otherwise tight conditions. The number of Americans filing for unemployment benefits surged to a three-week high of 198,000 last week from 191,000 in the prior week, according to the Department of Labour on Thursday, March 30 (refer to Figure 4). However, the latest data on initial claims is 43 percent lower than the historical average of 356,283, from 1969 to 2019 (pre-pandemic).

The four-week moving average of initial claims, a more reliable measure of labour market trends which irons out week-to-week volatility, dropped to 202,500 from the previous week's revised average of 208,000. This figure marks the lowest level since 1969, highlighting the continued strength of the US labour market.

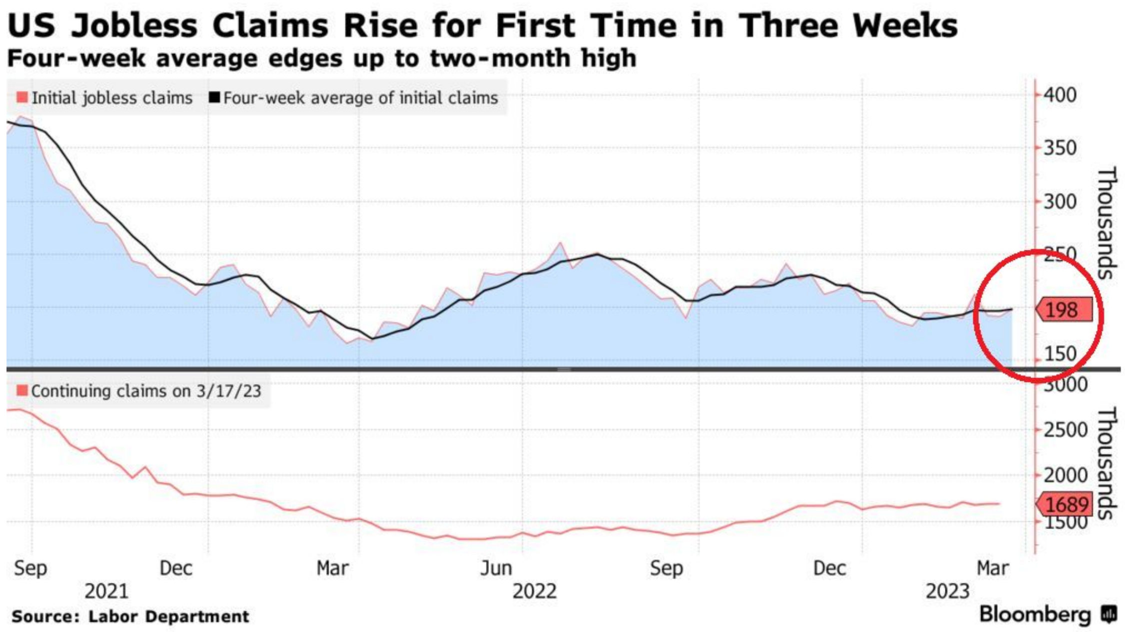


Figure 4. US Initial and Continuing Jobless Claims (Source: Labour Department, Bloomberg)

Meanwhile, continuing claims are still low at 1.69 million, unchanged from the previous week (refer to Figure 4). However, a gradual rise since last year implies it's taking job seekers longer to find new jobs. Jobless Claims numbers have been consistently low recently, showing a resilient labour market where demand for labour continues to be robust.

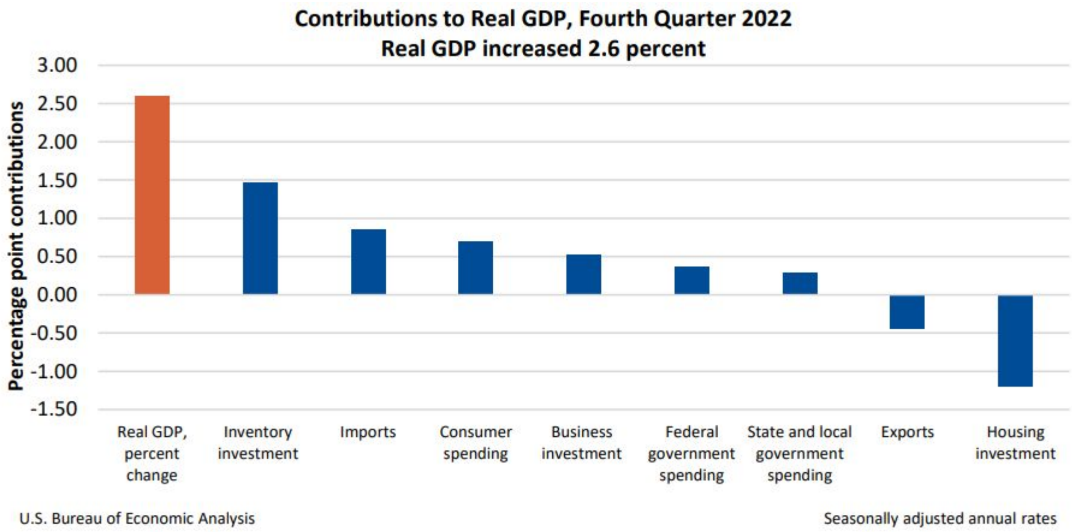


Figure 5. Real GDP and its Components for the Fourth Quarter of 2022 (Source: US Bureau of Economic Analysis)

In a separate report from the [Bureau of Economic Analysis](), GDP for the fourth quarter was 2.6 percent (Figure 5), down from 2.7 percent in the last quarter. This is a slight revision from the initial data released in February 2023, which indicated a GDP growth rate of 2.7 percent, and was driven by a downward revision in personal consumption.

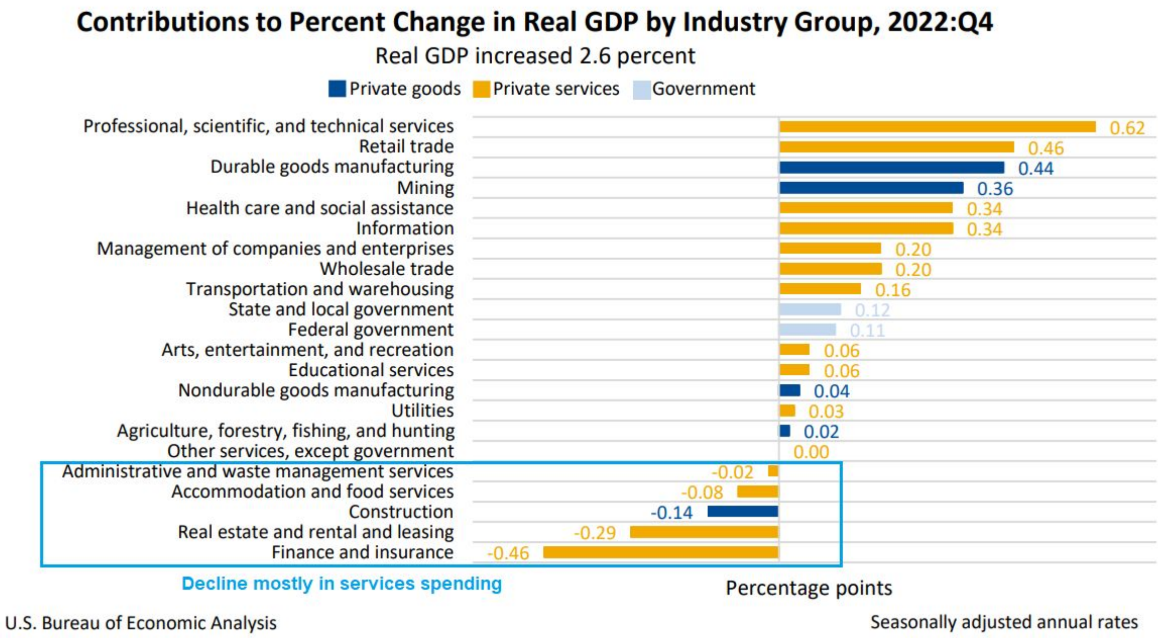


Figure 6. Contributions to Percent Change in Real GDP by Industry Group, Fourth Quarter of 2022 (Source: US Bureau of Economic Analysis)

Spending on Consumption grew by only one percent, down from the initial estimate of 1.4 percent in February. This was driven by the decline in service spending (Figure 6), growing only by 1.6 percent compared to 2.4 percent from the previous estimate.

Figure 7. GDP Formula

Although GDP is a backwards-looking measure, with the final GDP figures for Q4 2022 being released just as Q1 2023 is coming to an end, softer service spending may be viewed positively by the Fed as it strives to control and reduce inflation. A reduction in service spending indicates that consumers are cutting back on non-essential spending in areas such as healthcare, education, and leisure activities, in response to economic uncertainty. Figure 7 explains the factors that are used for GDP calculation.

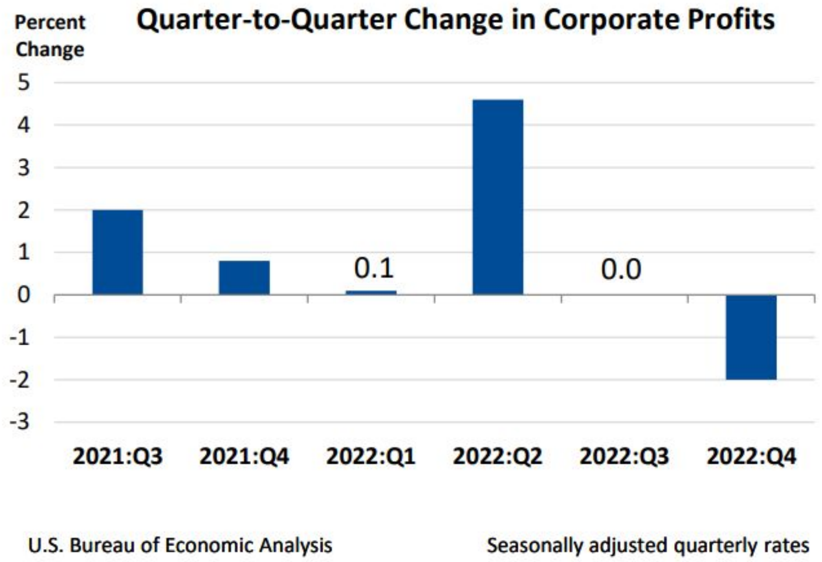


Figure 8. Quarter-to-Quarter Change in Corporate Profits (Source: Bureau of Economic Analysis)

The GDP report also showed a decline in corporate profits for the second straight quarter. Corporate profits are a component of the business investment in calculating the GDP, which refers to the spending by a business on physical capital. Corporate profits in the United States fell 2.7 percent to USD 2.47 trillion in the fourth quarter of 2022, following a 0.8 percent gain in the previous period. With monetary and fiscal support waning and interest rates high, it is apparent that corporate earnings have already peaked.

The combination of rising initial unemployment claims, decreased service spending as a component of GDP, and lower corporate profits indicate a potential slowdown in economic growth and an increased risk of a recession. With reports of worsening economic conditions and the recent bank failures, businesses may become more cautious in their hiring practices, which could weaken the labour market. The labour market is currently the most resilient aspect of the US economy.

PCE: The Fed's Preferred Inflation Gauge, Softens in February

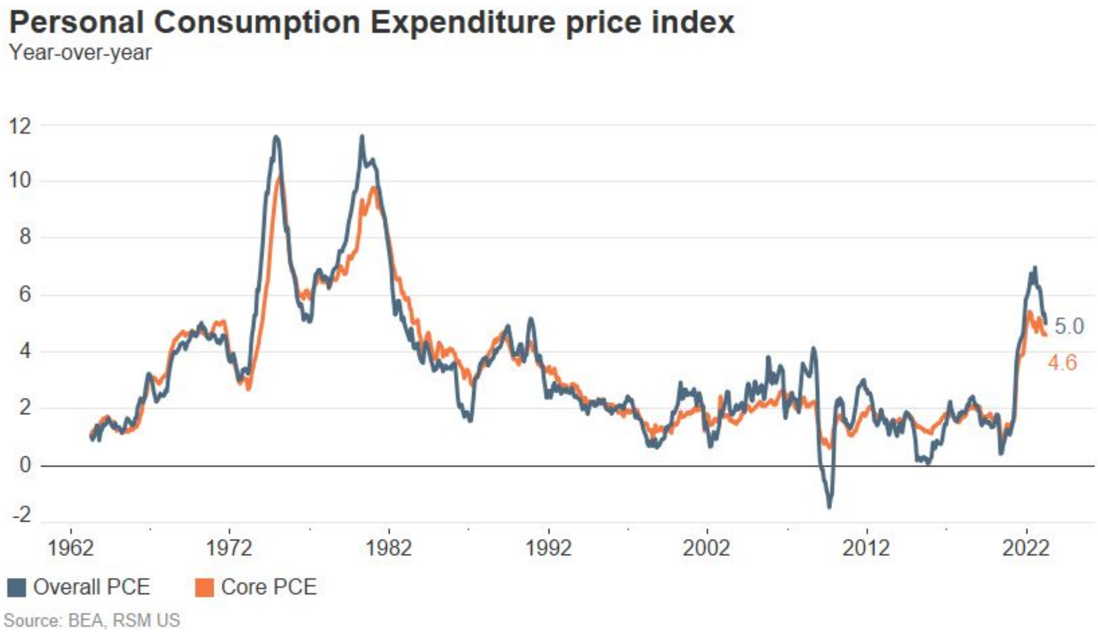


Figure 9. Personal Consumption Expenditure Price Index (Source: Bureau of Economic Analysis, RSM US)

Key inflation, spending and income data released on Friday, March 31st, came in softer than expected, indicating that the Federal Reserve's efforts to combat inflation are making some headway.

Although February's report showed a cooldown in all three indicators, inflation remained over the Federal Reserve's two percent target rate.

The Commerce Department reported on Friday, March 31, that the Personal Consumption Expenditure (PCE) index, the Federal Reserve's preferred gauge of inflation, eased in February after an unexpected uptick the previous month. The index increased by five percent for the 12-month period ending in February, which is lower than the 5.3 percent gain in January, marking its lowest level in over a year and a half. The index also rose by 0.3 percent on a monthly basis, which is lower than the 0.6 percent increase recorded in January.

The central bank pays especially close attention to the core PCE, which excludes the volatile food and energy components. The core rate of inflation slipped to 4.6 percent in the past 12 months from 4.7 percent in January. This is lower than Wall Street's forecast of 4.7 percent. On a monthly basis, the index shows inflation increasing by 0.3 percent, lower than January's 0.6 percent increase.

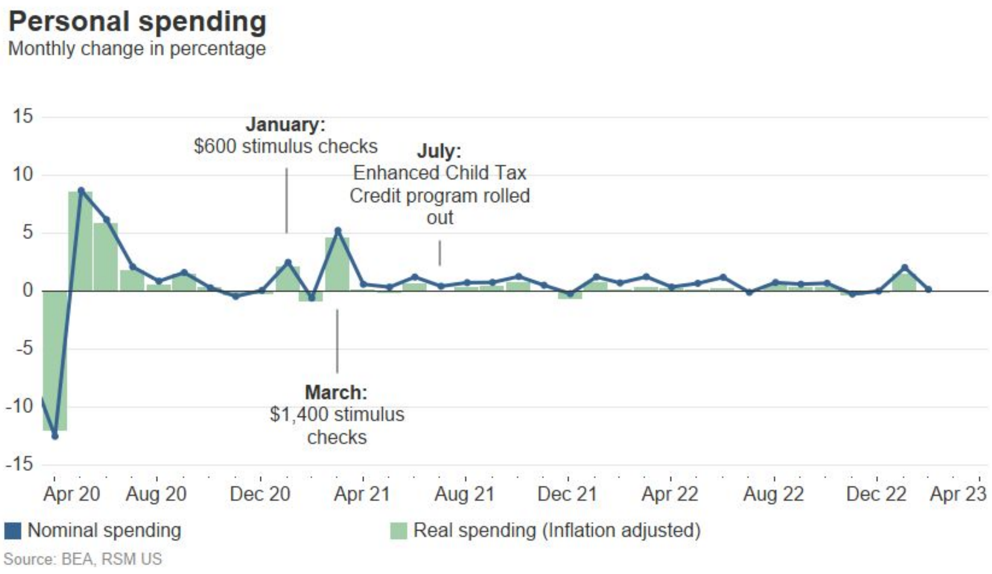


Figure 10. Monthly Change in Personal Spending (Source: Bureau of Economic Analysis, RSM US)

Personal spending growth slowed significantly in February, rising by 0.2 percent from 1.8 percent a month earlier. Income growth fell to 0.3 percent from 0.6 percent a month earlier.

As shown in last week's *Bitfinex Alpha*, the Fed's dot plot shows a peak target rate of 5.1 percent this year. Higher interest rates can curb inflation by slowing down the economy, but there can be a lagging effect. The Federal Reserve does not want to raise interest rates too high, as this may cause further stress to the US financial system in the wake of the banking crisis resulting from the stress caused by the collapse of Silicon Valley Bank.

If inflation stays hot, the central bank is likely to keep raising interest rates, increasing the likelihood of a recession. On the other hand, if inflation steadily cools down, this will increase the likelihood that the Fed will start cutting rates before the year ends.

Stocks End First Quarter on a High Note

The unexpected softening in the Personal Consumption Expenditure (PCE), which is the Federal Reserve's preferred inflation gauge, helped stocks achieve their third consecutive weekly gain.

Signs of cooling inflation reinforced optimism that the Federal Reserve could soon potentially end its aggressive interest rate hiking cycle, sending stocks soaring on Wall Street. Nasdaq reached its greatest quarterly percentage gain since June 2020.

For Q1 2023, the tech-focused Nasdaq Composite was up by more than 17 percent, while S&P 500 index ended the quarter seven percent higher, though still well below its December 2021 peak. The blue-chip Dow Jones Industrial Average ended the quarter slightly above where it started. (Q1 performance depicted in Figure 11)

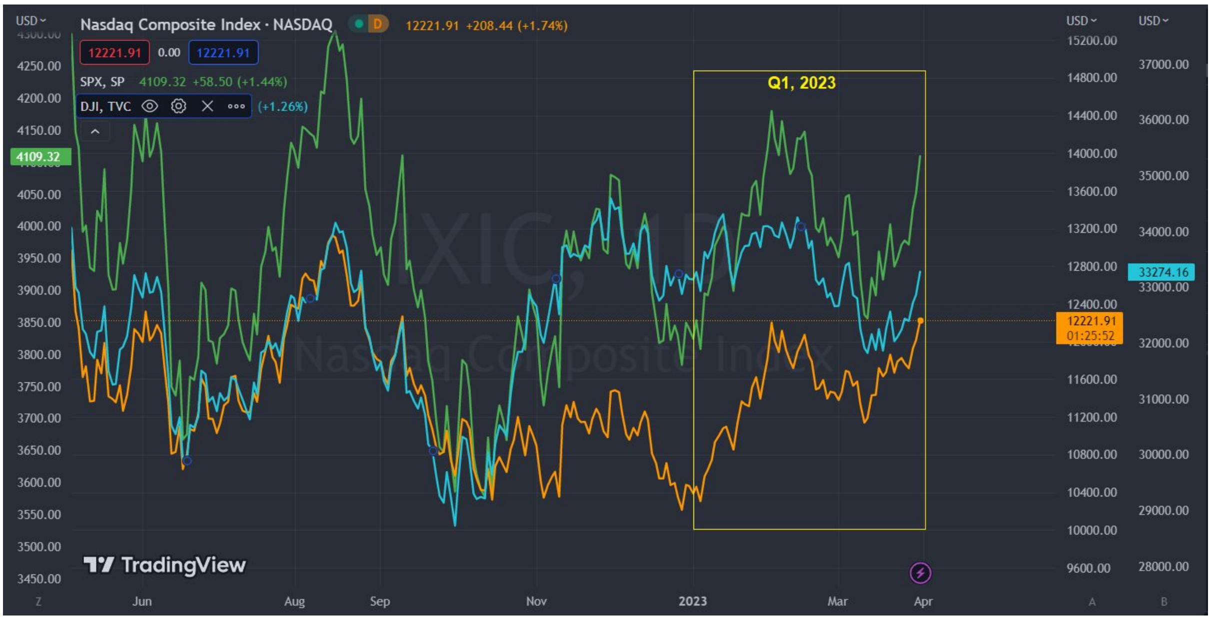


***Figure 11. Nasdaq Composite Index (Orange), S&P 500 (Green), Dow Jones Industrial Average (Blue) Price action** (Source: Tradingview)*

On Friday, March 31, Nasdaq Composite was up 1.74 percent at 12,221. The S&P 500 Index rose 1.44 percent to 4,109 and Dow Jones industrial average was up 1.26 percent at 33,274. This is important as we saw these metrics rise immediately after the release of the PCE data.

The banking crisis and changing interest rate outlook, amidst concerns about economic growth and high inflation, have resulted in investors withdrawing their money from banks. This could have an impact on banks' lending activity since lower demand for bank deposits may lead to a decrease in the supply of loans made by banks. Banks usually rely on deposits to make loans, and a decline in deposit levels may prompt them to reduce their lending activity.

This reduction in lending activity can have a ripple effect throughout the economy, which can lead to slower economic growth and lower inflation expectations. As a result, investors may become more risk-averse and seek the safety of Treasury bonds, including two-year Treasury bonds. This increased demand for Treasury bonds can drive up their prices and push down their yields.

As a result of the increased demand, the two-year US Treasury note yield posted its steepest monthly decline since 2008 on Friday, March 31.

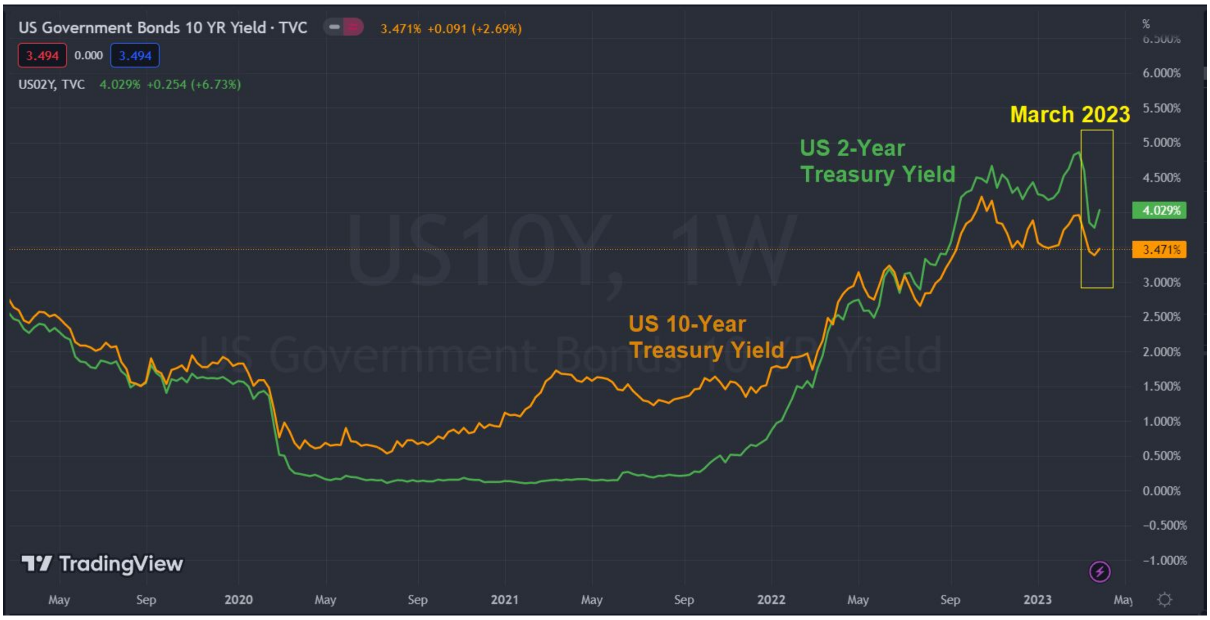


Figure 12. Two-Year and Ten-Year US Treasury Bond Yields (Source: Tradingview)

On Friday, the yield on two-year bonds was around 4.03 percent, down nearly 17 percent month-over-month, and the yield on 10-year bonds was around 3.47 percent, down around 13 percent month-over-month (Figure 12). Treasury yields steadied at the end of a quarter of wild swings.

As investors bet on a softening in central-bank policy, amid recession worries and the slowdown in new injections into money market funds, fears of an ongoing bank run eased. US futures extended gains for a third straight day, led by the Nasdaq 100 which is set for its best March in more than a decade. Nasdaq 100 futures contracts were up 0.3 percent (Figure 13) as of 31 March. The tech-heavy index rose by nearly 7.7 percent this month, marking its largest monthly gain in March since 2010. Meanwhile, the S&P 500 is poised for a modest monthly gain. Futures on the S&P 500 index increased by 0.2 percent, reaching their highest point in six weeks (Figure 14).

Figure 13. S&P 500 E-mini Futures (Source: Tradingview)

Figure 14. Nasdaq 100 E-mini Futures (Source: Tradingview)

Despite a significant sell-off in bank stocks this month after the failure of Silicon Valley Bank and Signature Bank, and fears of a wider financial crisis, the stock market as a whole was nevertheless able to report quarterly gains.

Consumer Sentiment Poses First Decline in Four Months

The University of Michigan's survey of consumer sentiment shows that there was a decline in March, marking the first decrease in four months. The reading fell to a four-month low of 62, likely reflecting concerns about the possibility of a recession.

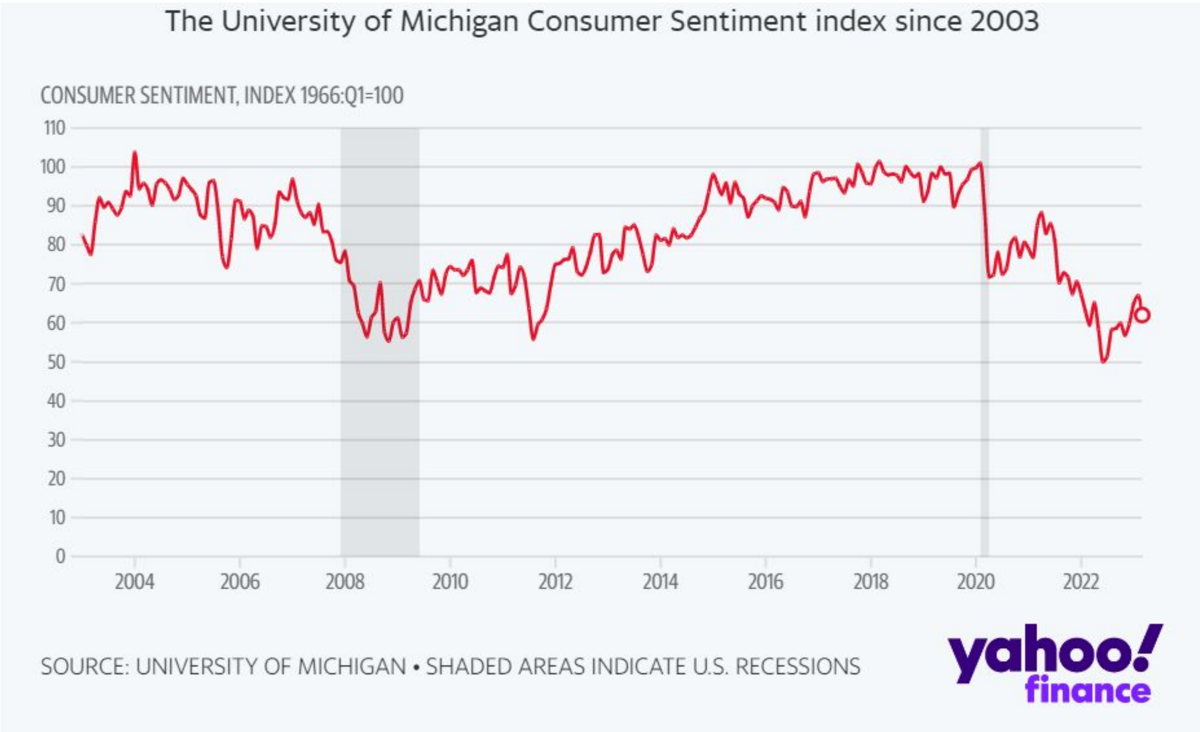


Figure 15. Survey on Consumer Sentiment (Source: University of Michigan, Yahoo Finance)

In the University of Michigan's monthly Consumer Sentiment Survey released on Friday, March 31, the index slid to 62 in March from 63 in February (refer Figure 15). US consumer sentiment fell for the first time in four months in March as consumers worried increasingly that a recession is coming, although the turmoil in the banking system has yet to resonate extensively among American households.

However, there was more encouraging news on the inflation front. A survey from the University of Michigan on Friday confirmed that consumers expected inflation to subside over the next 12 months.

The survey revealed that consumers' perceptions of inflation in the near future moderated during the course of the month. Inflation forecasts for one year decreased to 3.6 percent from 4.1 percent in February. This was the lowest number since April 2021. This report will be a welcome data for Fed officials who were concerned about inflation becoming unanchored.

WHAT'S ON-CHAIN THIS WEEK?

Bitcoin Non-Zero Balance Addresses Surge, But Some Key On-chain Metrics Weaken

As Bitcoin's non-zero balance addresses reach new heights, on-chain metrics reveal the need to be cautious, suggesting a market in transition. A transition state is characterised by choppy market conditions where the price consolidates in a tight range before trending in either direction. Despite an influx of new market entrants, the sustainability of this phenomena of both rapidly growing non-zero balances and tight range-trading for Bitcoin remains uncertain.

According to Glassnode data, the number of Bitcoin wallets holding a non-zero BTC balance has surged to a new record of 45.388 million in the past week.

Figure 16. Addresses With Non-Zero BTC Balance. (source: glassnode)

This is the fastest rate at which the Bitcoin network has added non-zero wallet addresses since early 2021. The increase in the number of wallets with a non-zero balance is a positive development for the Bitcoin price, as it suggests that more investors are entering the Bitcoin market or, put simply, that demand is growing. This metric is often used as a proxy for Bitcoin demand from new and smaller investors.

However, key on-chain metrics, such as Bitcoin Network statistics, suggest potential market weakness. Bitcoin network statistics are metrics that allow us to gauge the increase or decrease in activity for on-chain transactions for the blockchain.

The seven-day moving average of the number of active addresses interacting with the Bitcoin network on a daily basis recently fell to its lowest level since late January as seen in Figure 17 below.

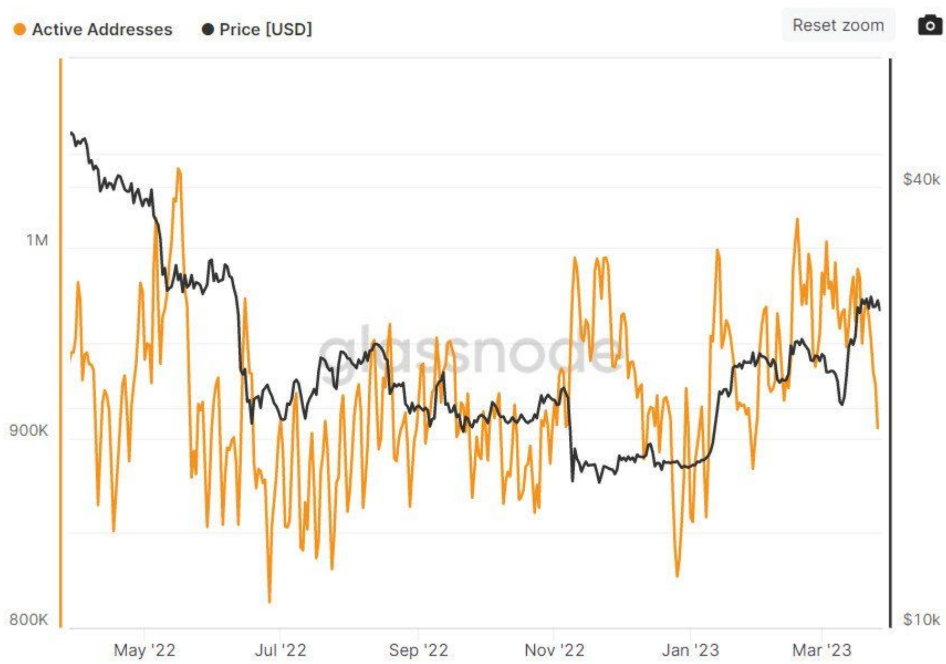


Figure 17: Seven-day Moving Average of daily active addresses on the Bitcoin network. (source: glassnode)

Over the past two weeks, the number of daily transactions on the Bitcoin network has also dropped sharply. The seven-day moving average of this metric recorded 293,058 transactions on March 30th, down by over 13 percent since March 8th, as seen in Figure 18 below.

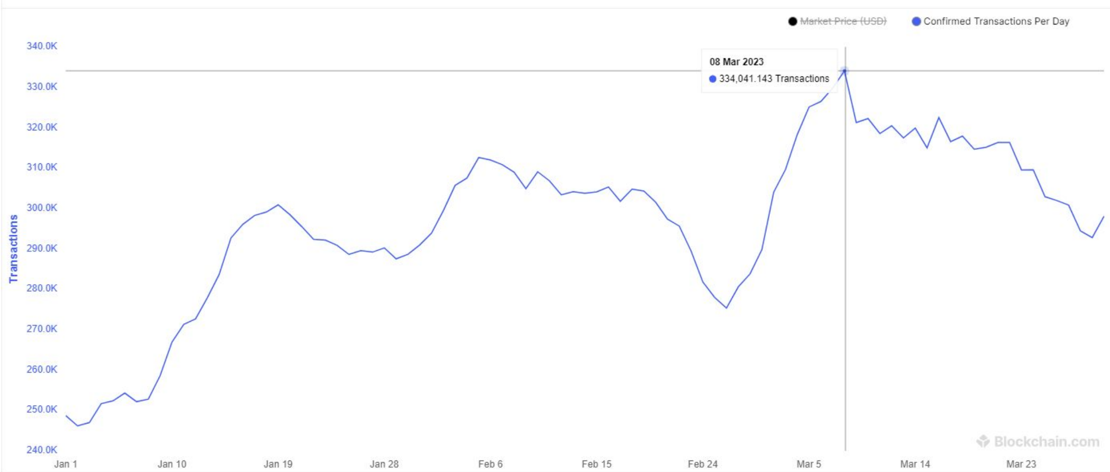


Figure 18: Confirmed Transactions Per Day On Bitcoin network. (source: blockchain.com)

The number of daily confirmed transactions highlights the value of the Bitcoin network as a way to transfer funds without a third party securely. While this is an inconclusive indicator in terms of bullish or bearish signals, daily activity and transactions decreasing for Bitcoin have always occurred at transitionary phases in the crypto market. They suggest indecision and an unsettling predicament for both bulls and bears.

BTC and Ether Options Open Interest Hit ATH on CME

As Q1 2023 concludes, open interest and trading activity for BTC and Ether options markets on the CME have continued to accelerate, with both contracts reaching a new all-time high open interest of 15,089 contracts combined on March 27th.

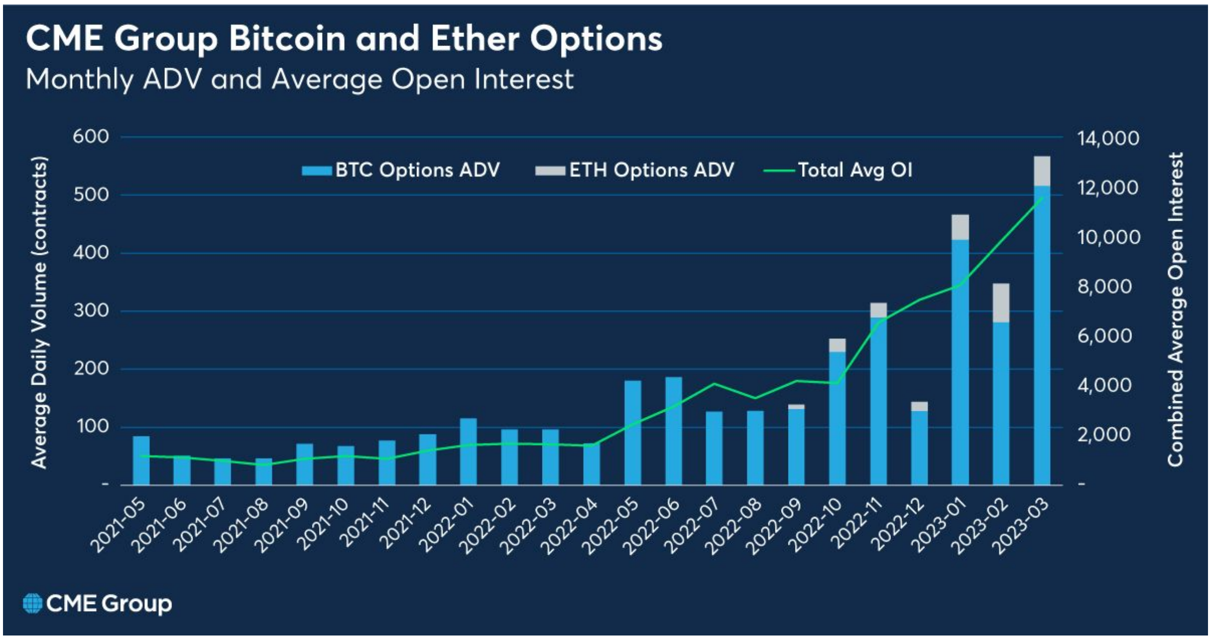
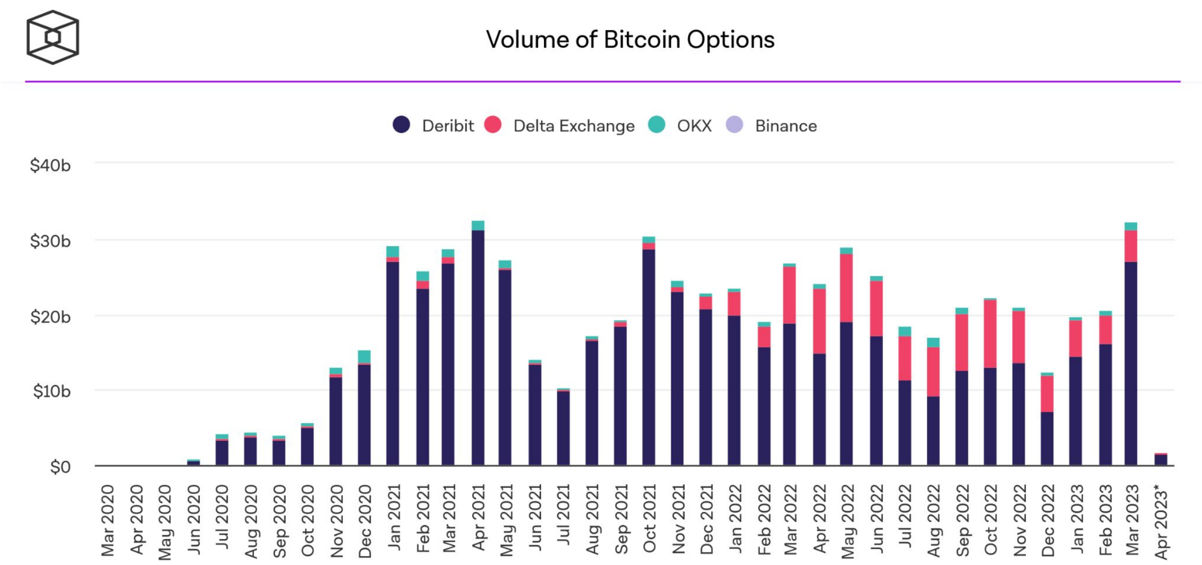


Figure 19: CME Group Bitcoin and Ether Options Open Interest And Average Daily Trading Value. (source: CME Group)

Amid the current banking crisis and a recent rally in Bitcoin prices, the volume of Bitcoin options and the open interest on the Chicago Mercantile Exchange (CME) have both reached unprecedented levels.

Open interest on the CME recorded a 67 percent increase in March since the start of 2023 to $1.3 billion. (Refer to Figure 19 above) Similarly, Bitcoin options volumes experienced a significant increase, surging to $1.67 billion in March from $832 million in February. Notably, the previous all-time high for Bitcoin options volume was $1.1 billion in January.
Total Bitcoin options volume across all exchanges is also close to its all-time high at $32.17 billion for the month of March (refer Figure 20 below).



SOURCE: THE BLOCK
UPDATED: APR 2, 2023

Figure 20: Volume of Bitcoin Monthly Options

Bitcoin options are a popular choice for investors who wish to hedge against or speculate on price fluctuations. As Bitcoin options are considered to be a more sophisticated asset class, they are commonly traded by professional trading desks and institutional investors, which make up a significant proportion of the overall trading volumes in the options market.

The recent surge in Bitcoin options volumes may indicate that institutional trading activity is on the rise. Another indicator of increased institutional involvement is the recent spike in open interest for Bitcoin options.

BTC Correlation With The S&P 500 Is On Track To Be Restored

Investors have been speculating if Bitcoin is more prone to macro headwinds now that its correlation with the S&P 500 index and the NASDAQ composite is increasing.

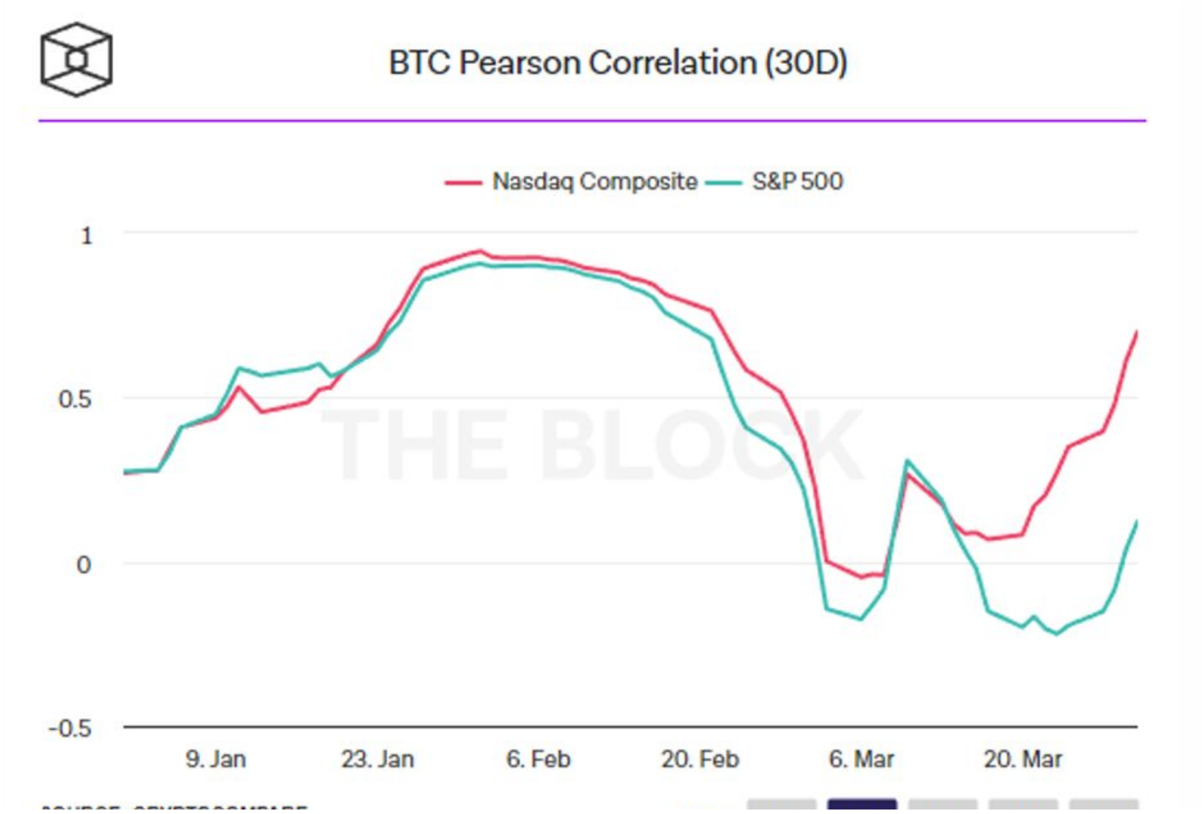


Figure 21: BTC Pearson Correlation (30D) for S&P500 and NASDAQ composite. (source: TheBlock)

Bitcoin's correlation metric with the S&P 500 fell below zero earlier in March. Any correlation below zero means that it is negatively correlated with Bitcoin. So an upward move by the S&P500 would see a downward move in Bitcoin.

In recent weeks however, with the BTC price remaining relatively stable above $27,000 and $28,000 levels, the Pearson correlation metric has risen to 0.61 for the NASDAQ composite and 0.12 for the S&P 500, indicating more positive correlation with these equity indices. (refer Figure 21 above)

Despite concerns about Bitcoin's vulnerability to macroeconomic headwinds, it ended the quarter with its best performance since Q1 2021 (refer Figure 22 below).

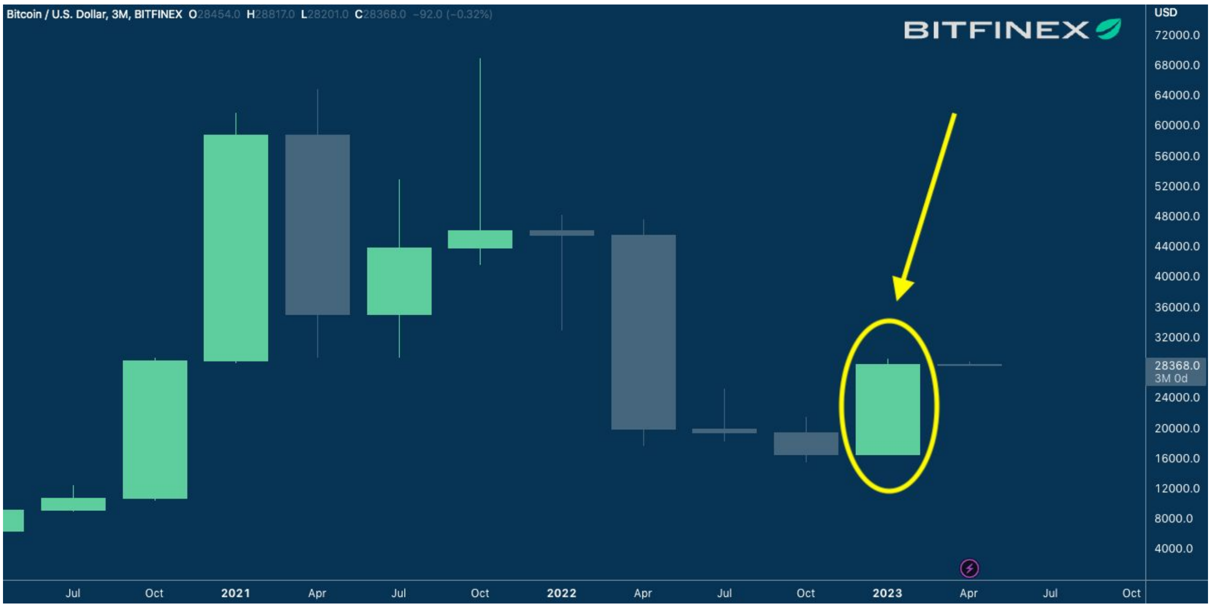


Figure 22. BTC price quarterly chart (Source: TradingView)

In March, Bitcoin has also benefited from reduced liquidity, which allows for upward price movements to be more pronounced. According to analysts at *Kaiko*, liquidity has hit a 10-month low, with market makers losing access to USD payment rails due to the ongoing regional banking crisis in the US.

"Crypto markets exhibit their greatest volatility when liquidity is limited. With prices receiving less support both to the upside and downside, this could help to explain Bitcoin's rapid 17 percent gain since the start of the month," said Conor Ryder, *Kaiko* analyst.

Another factor contributing to the upward trajectory of Bitcoin in March has been the treatment of the asset, by some market participants, as a safe haven in times of banking crises. As stablecoins like USDC falter, Bitcoin has seen significant inflows, causing its dominance (i.e., the ratio of Bitcoin's market capitalisation to that of the entire crypto market) to reach its highest level since June of last year.

Low Liquidity in Crypto Market Raises Concerns as Wider Market Impact Looms

As liquidity in the cryptocurrency market tightens, concerns arise regarding its potential impact on the broader financial landscape. We urge caution as low liquidity could exacerbate price volatility and hinder market stability.

The market depth for Bitcoin has reached concerning levels. Current liquidity in the Bitcoin market has reached a 10-month low, even lower than after the collapse of FTX.

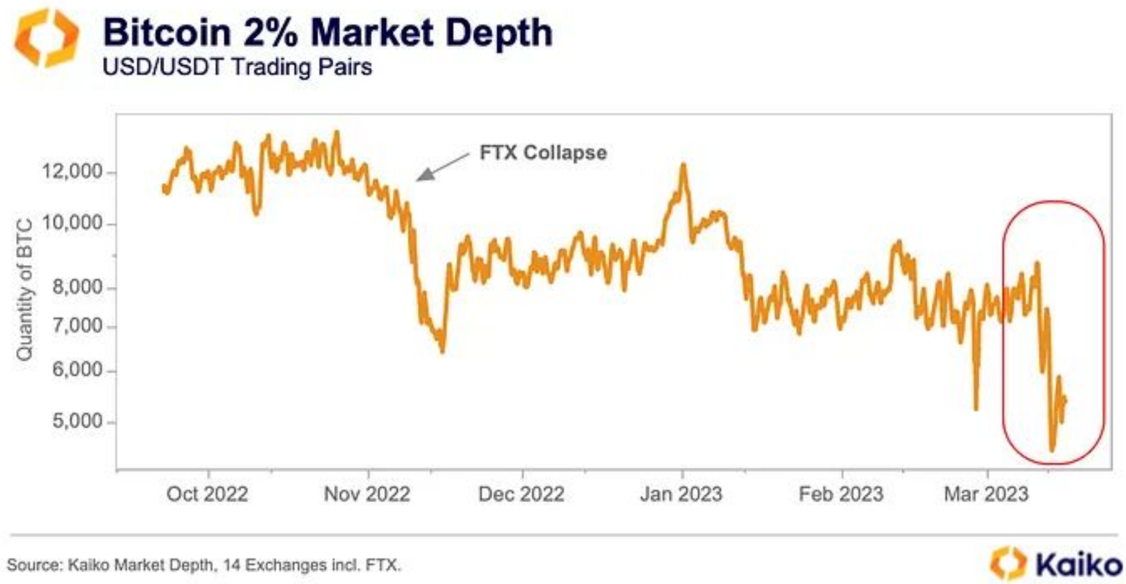


Figure 23: Two percent Market Depth for Bitcoin's USD/USDt trading pairs. (source: Kaiko)

At the time of the FTX/Alameda downfall, there was a large drop in liquidity which was dubbed "the Alameda Gap" due to the absence of one of the industry's most prominent market makers. That gap is still yet to be filled, and with the recent banking issues, liquidity has taken another hit.

The spread on exchanges, which is the difference between the best bid and the best ask of popular crypto assets, is another way to gauge market liquidity. The USD versus USDt pairs also indicate that the recent banking issues have resulted in more volatile USD spreads, which went from two basis points (bps) to four bps following the shut down of Silvergate.

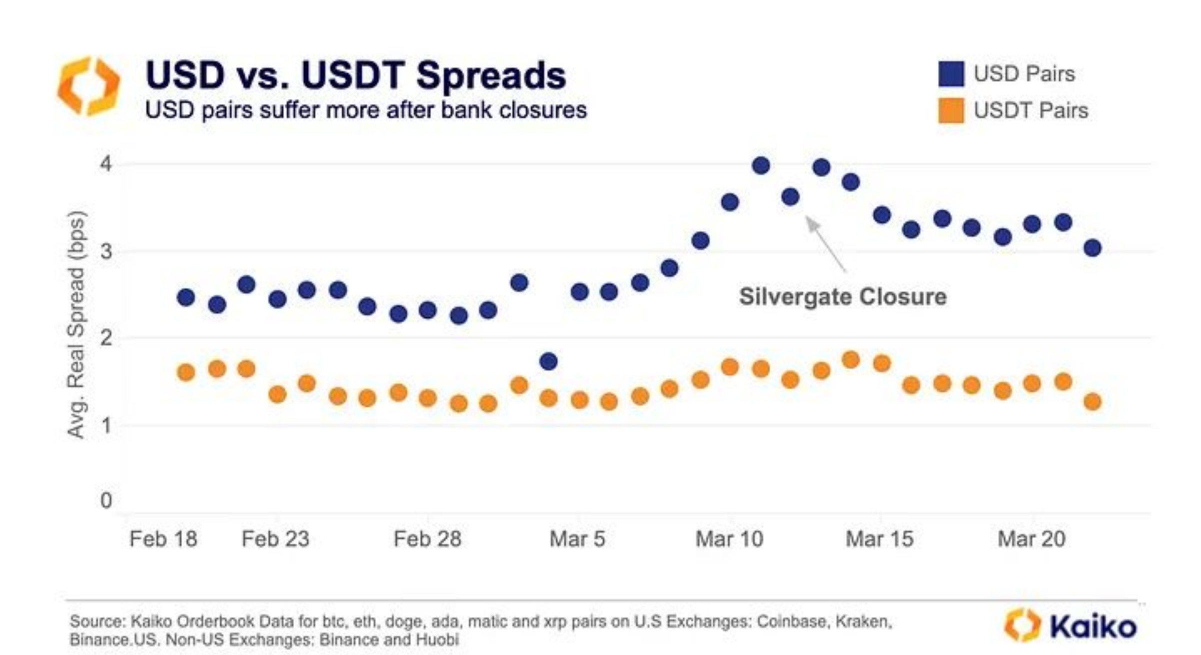


Figure 24: USD vs USDt Spreads for BTC, ETH, DOGE, ADA, MATIC and XRP orderbooks on major exchanges. (source: Kaiko)

Similarly, as we saw with market depth, the USD-linked exchanges and USD pairs experienced declining liquidity as the logistical concerns surrounding the shutdown of fiat payment rails became evident. The longer it takes to establish a viable alternative to the Silvergate Exchange Network or Signet networks, the more volatility we can expect to see in spreads and depth as market makers confront new operational challenges and withdraw liquidity from exchanges until they can obtain more clarity.

Apart from the banking issues, Binance also announced that it would end the zero-fee program for BTC trading pairs. The impact of this development on market liquidity cannot be underestimated; The zero-fee program enabled Binance to gain over 20 percent in market share since July, with over 61 percent of volumes coming from zero-fee pairs. The adjustment in spreads was evident as the previously volatile BTC spreads on Binance, due to a lack of taker fee, decreased substantially once a fee was reintroduced, bringing BTC spreads lower than ETH spreads.

Tighter spreads reduce the profitability of market makers to provide liquidity on a given pair. With the reintroduction of a taker fee, investors are disinclined to pay a higher spread. This has resulted in a significant depletion of liquidity from the BTC-USDt pair on Binance, with market makers seeking more profitable markets on other exchanges and pairs. Overnight, the liquidity of the BTC-USDt pair on Binance plummeted by 70 percent as seen in Figure 25 below.

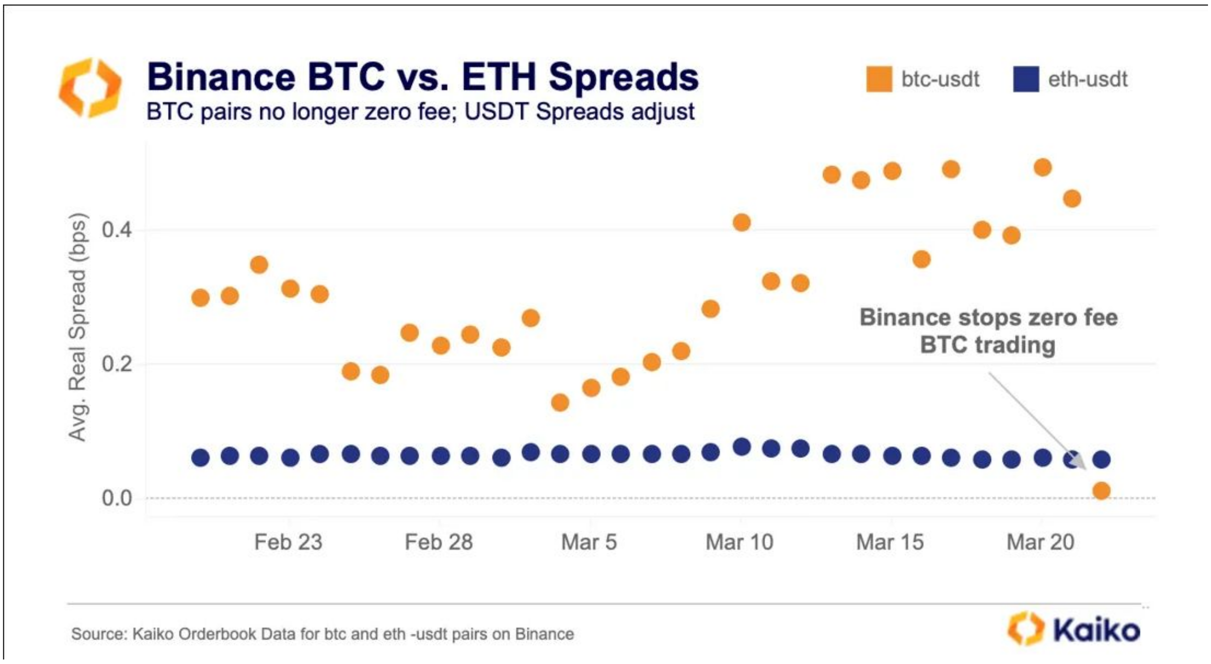


Figure 25: Binance BTC vs ETH spreads. BTC/USDt spread almost plummeted to zero on the closure of the zero-fees program by Binance. (source: Kaiko)

As a result of this low liquidity, volatility metrics are starting to pick up. The Crypto Volatility Index (CVI) has reached its highest level since the second week of January 2023. (Refer Figure 26 below)

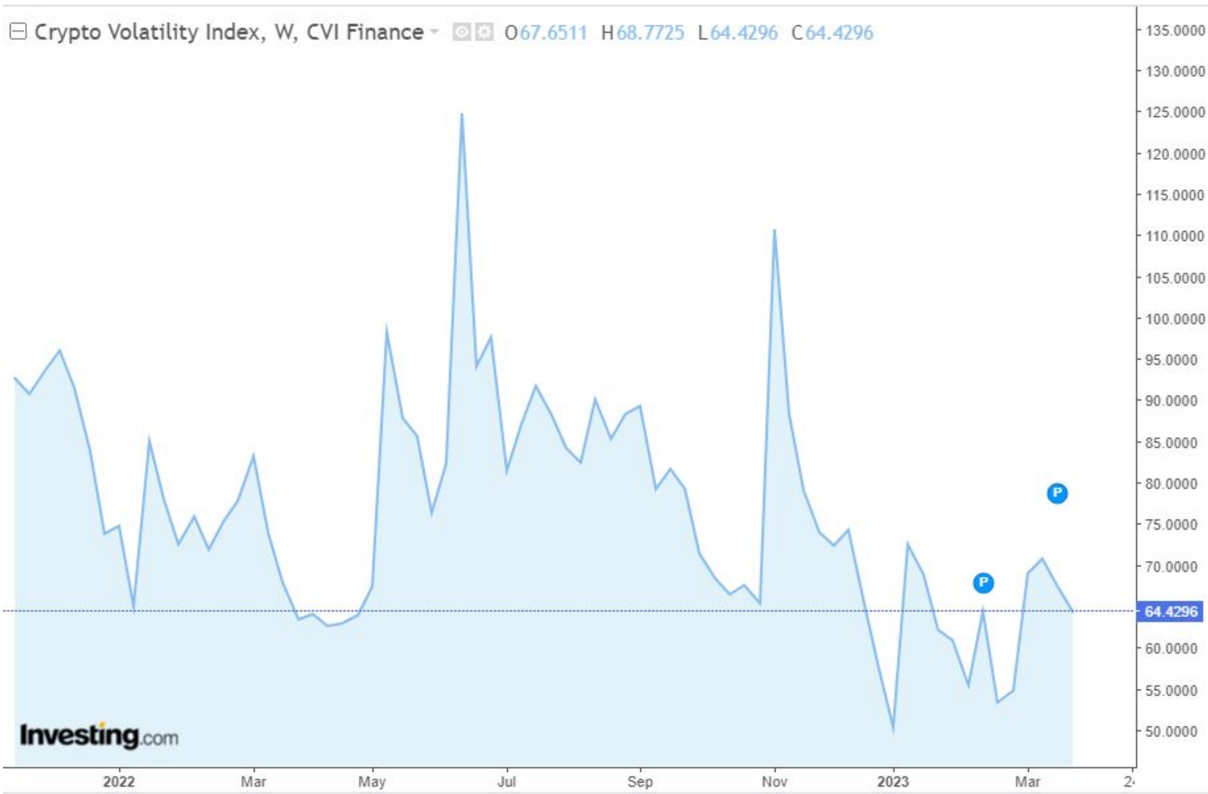


Figure 26: Crypto Volatility Index. (source: Investing.com)

In conclusion, this reiterates our lower timeframe stance that the market is indecisive right now.

Volatility in either direction is probable despite the strong uptrend in the crypto market since the 2023 yearly open.

However, most metrics caution against over-leveraging or a heightened risk appetite during a transition period in the crypto market. This does not imply that the current bullish trend is reversing yet, or that our long term outlook of being at the latter stages of a bear market is invalidated.

NEWS FROM THE CRYPTO-SPHERE

CFTC Sues Binance. Claims to have records to Internal Company Chats of CZ and the management.

Figure 27. CFTC filed a lawsuit against Binance

The Commodity Futures Trading Commission (CFTC) has filed a lawsuit against Binance, alleging multiple violations of the Commodity Exchange Act (CEA), including KYC and AML laws.

The CFTC claims that Binance engaged in multiple violations of the Commodity Exchange Act (CEA) between 2017 and 2020, including providing leveraged, margined, or financed retail commodity transactions to US customers without proper registration as a futures commission merchant (FCM), failing to implement adequate anti-money laundering (AML) and know-your-customer (KYC) procedures. The lawsuit also highlights Binance trading on its own accounts within the exchange, raising further concerns.

As part of the investigation, the CFTC claims to have gained access to Binance CEO Changpeng Zhao's (CZ) mobile phone and special records, which may provide crucial evidence in the case. The legal action could expose the exchange to potential fines and stringent oversight.

Here are the key aspects of the lawsuit in detail:

- Alleged Violations: Binance purportedly provided leveraged, margined, or financed retail commodity transactions to US customers without proper registration as a futures commission merchant (FCM), thereby violating the CEA.

- Regulatory avoidance: By failing to adhere to mandatory registration requirements, Binance is accused of sidestepping the regulatory framework designed to protect market participants and ensure the integrity of US commodity markets.

- AML and KYC deficiencies: The CFTC has accused Binance of failing to implement adequate anti-money laundering (AML) and know-your-customer (KYC) procedures, exposing the exchange to potential money laundering and other illicit activities.

- Access to evidence: The CFTC claims that it has gained access to CZ’s mobile phone and special records, which may offer critical insights into the alleged violations and the exchange's operations during the relevant period.

- Internal trading concerns: The lawsuit highlights that Binance has allegedly been trading on its own accounts within its exchange, raising questions about potential conflicts of interest and manipulation.

- Legal ramifications: The lawsuit seeks restitution for affected parties, disgorgement of the supposedly ill-gotten gains which would mean paying back account holders who have supposedly fallen victim to liquidation engines or price manipulation, the imposition of civil monetary penalties, and permanent injunctions against future violations of the CEA.

Binance Bitcoin Trading Volume Plummets

Binance's recent termination of its zero-fee trading policy has also had implications for the exchange's trading volume. According to data from *Kaiko*, Binance's Bitcoin trading volume has hit its lowest level in eight months following the termination of the policy. (See Figure below). This decline in trading volume could have a significant impact on Binance's revenue, as trading fees are a major source of income for the exchange.

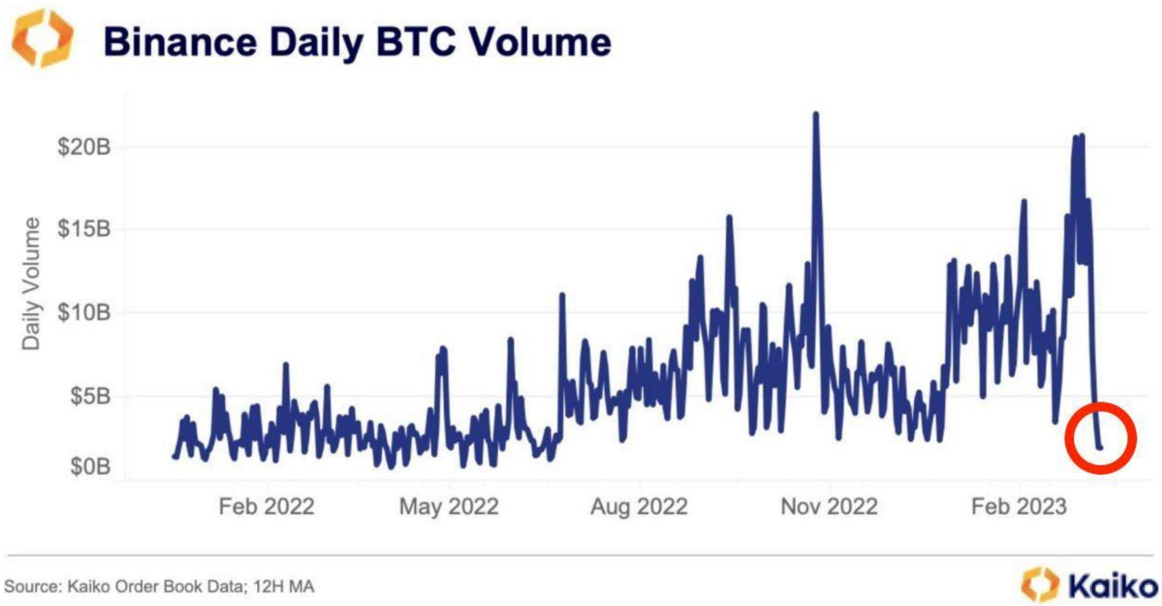


Figure 28. Binance Daily BTC Volume

CZ has [responded]() to the allegations, stating that Binance has always been committed to complying with all applicable laws and regulations. He rejects the allegations of market manipulation and regulatory avoidance and expresses his confidence that the exchange will be able to address the concerns raised by the CFTC.

The widening legal scrutiny facing Binance highlights the importance of regulatory compliance in the cryptocurrency industry. As regulatory requirements evolve, exchanges will need to adapt and ensure compliance to maintain the trust of users and regulators alike.

Michael Saylor's MicroStrategy Continues Its Bitcoin Buying Regime

Figure 29. Michael Saylor's MicroStrategy acquires more Bitcoin

On March 27, 2023, MicroStrategy announced that it had repaid its Silvergate loan and increased its Bitcoin holdings by 6,455 BTC.

The company's commitment to Bitcoin has been unwavering, as evidenced by its consistent accumulation of the digital asset. MicroStrategy reported having purchased 6,455 BTC for roughly $150 million (about $23,238 per coin) over the past five weeks. This brings their holdings up to 138,955 BTC purchased at an average price of $29,817 each.

It also announced that it had paid back its loan to Silvergate Bank. The loan was paid off at a discount due to early voluntary repayment, after the crypto bank filed for liquidation earlier this year. The loan payoff amounted to $161 million, compared to the sum of $205 million borrowed in March 2022. A total of 34,619 bitcoins held as collateral were returned to MicroStrategy's custody.

MicroStrategy's Bitcoin investment began in August 2020, with the company making continuous purchases in the following years. With the current value of Bitcoin around $28,000 per coin, the company's holdings are worth roughly $3.89 billion.

The company reported strong fourth-quarter results in 2022, with total revenues of $195.1 million, a 23 percent increase compared to the prior-year period. The company's stock price has also experienced notable growth this year, rocketing by 100 percent in 2023 as the firm continued to buy Bitcoin amid the 2022 market crash.

Saylor's history as head of Microstrategy has not been without its challenges. In the early 2000s, during the dot-com bubble, Saylor faced significant losses due to overinvestment in the company's infrastructure. Nevertheless, he has since bounced back, leading MicroStrategy to its current success and innovative Bitcoin investment strategy.

Tether's USDt Dominance Surges in March 2023

Figure 30. USDt's market dominance reaches all-time high

The digital asset landscape has witnessed significant changes as Tether's USDt stablecoin reached an all-time high in terms of market dominance in March 2023.

According to a recent *CryptoCompare* report, USDt now accounts for 57.5 percent of total stablecoin market share, marking its highest level since June 20, 2021. (See Figure below) This development underscores Tether's ongoing importance in the global cryptocurrency ecosystem, especially in light of recent events involving its competitors.

As mentioned in last week's *Bitfinex Alpha*, Tether also estimates it will earn a $700 million profit in the first quarter of 2023, according to the company's chief technology officer, Paolo Ardoino. Which would bring Tether's total excess reserves to over $1.6 billion for the first time.

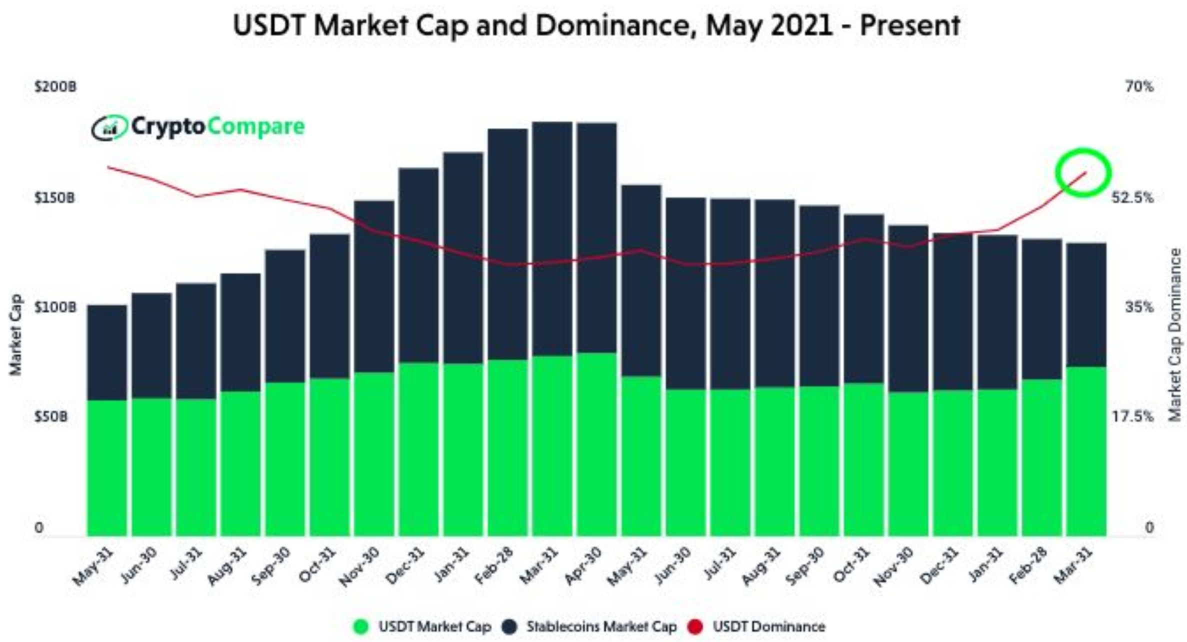


Figure 31. USDt Market Cap and Dominance, May 2021-present (Source: CryptoCampare)

On March 10, USDt competitor, USDC, experienced a depegging event following the collapse of one of its banks, Silicon Valley Bank (SVB), which held $3.3 billion of its reserves. USDC's value fell as low as $0.877 on March 11. Other stablecoins holding USDC as collateral in their reserves, such as DAI, MIM, and FRAX, also faced devaluation, reaching lows of $0.865, $0.911, and $0.920, respectively, on the same day. (As illustrated in the following chart)

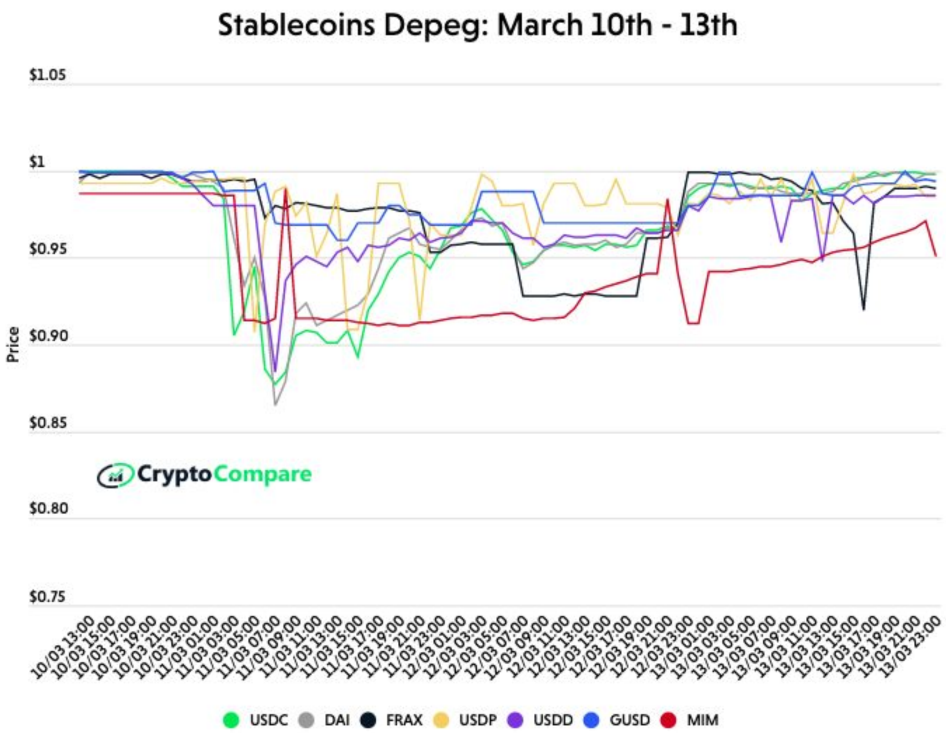


Figure 32. Stablecoins Depeg, March10th-13th (Source: CryptoCompare)

As a consequence, stablecoin market dominance fell to 11.4 percent, down from 12.6 percent in February, reaching its lowest end-of-month market share since April 2022. This decline in stablecoin dominance however also highlights the rally in crypto asset prices amidst the recent depegging of USDC and other stablecoins.

In contrast, USDt has continued to strengthen its stablecoin dominance. According to data by *Coingecko*, its market capitalisation rose by 10.9 percent in March to $79.8 billion and increased by $7.9 billion since USDC's depegging on March 10th. This is the highest market cap for USDt since April 2022.

With another stablecoin, BUSD, halting the minting of new tokens and USDC facing concerns following the collapse of SVB, USDt has emerged as the dominant stablecoin in the market. The stablecoin's prominence reflects its growing adoption for various applications and its vital role in the decentralised finance (DeFi) ecosystem. As regulatory initiatives progress, the future trajectory of USDt and the broader stablecoin market will depend on stakeholders' capacity to navigate and adapt to emerging challenges and opportunities.

Ethereum's Shapella Upgrade Set to Launch on April 12

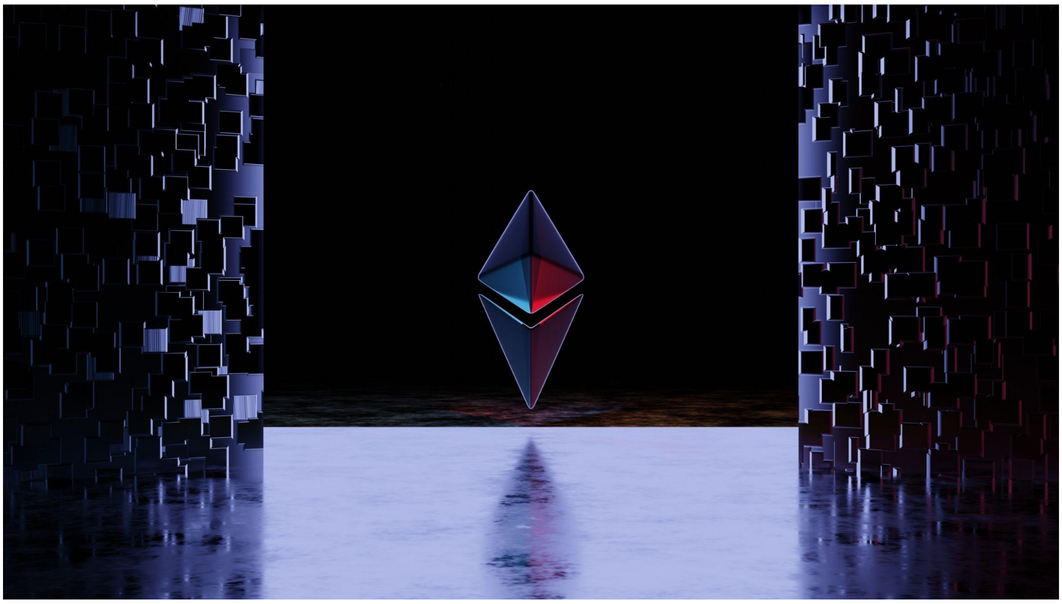


Figure 33. Ethereum Shapella is now set for April 12

Ethereum enthusiasts have a reason to celebrate as the core developers officially confirm the Shapella upgrade for April 12. This will bring major updates to the Ethereum network.

This eagerly-awaited update promises significant improvements to transaction processing, security, and network efficiency, making it a game-changer for users and developers on the platform.

The announcement, which appeared on the Ethereum blog, outlines the various enhancements that the Shapella upgrade will bring. Among these changes, the introduction of withdrawals stands out as a critical feature, as reported by *Cointelegraph*. This functionality will enable users to move assets seamlessly within the Ethereum network, further bolstering its usability and accessibility.

Leading up to the Shapella upgrade, Ethereum developers have been diligently working on the proposal, testing, and fine-tuning the network's features. The Ethereum community has been actively discussing these forthcoming improvements on social media and other platforms, showcasing their enthusiasm and support.

The Shapella upgrade marks another essential milestone in Ethereum's journey, ensuring that the platform remains competitive and meets the evolving needs of its users.

As the crypto community eagerly anticipates this landmark event, they can expect a more efficient, secure, and user-friendly Ethereum network come April 12.

District Court Blocks Binance US' Acquisition of Troubled Voyager Digital

Figure 34. District Court halts the sale of Voyager Digital to Binance.US

A federal judge has put the brakes on the acquisition of the embattled Voyager Digital by Binance US. This intervention casts doubt on the future of the deal and raises questions about the next steps for both companies.

As reported by *Bloomberg* News on March 27, the US District Judge Jennifer Rearden granted the US government's request to halt the sale of Voyager Digital to Binance US. The specific reasons for this move remain undisclosed, but the decision has undoubtedly shaken expectations surrounding the acquisition.

Voyager Digital, once a prominent player in the crypto industry, faced significant challenges, ultimately leading to its collapse. The company's issues can be traced back to its exposure to among others the failed crypto hedge fund Three Arrows Capital and its other web of exposures, which, as reported by *CoinDesk*, resembled those of a traditional bank. Voyager's fall was a stark reminder of the risks involved in the fast-paced and evolving crypto space.

In December 2022, Binance US emerged as the winner of a bidding war to acquire Voyager Digital's assets in a deal worth $1 billion in crypto tokens, as reported by *Forbes*. The acquisition was seen as a strategic move for Binance US to expand its presence in the United States market, capitalising on Voyager's client base and existing infrastructure.

However, the recent intervention by the District Court has thrown a spanner in the works, leaving the fate of the deal uncertain. It is unclear how Binance US and Voyager Digital will respond to the court's decision and what implications it will have on their plans moving forward.

Voyager's collapse and the uncertainty surrounding its acquisition could also impact investor confidence, affecting both retail and institutional investors and traders in the crypto market.

FTX Founder Faces Bribery Charges in a New Indictment

Figure 35. FTX founder and former CEO Sam Bankman-Fried

FTX founder Sam Bankman-Fried has been hit with a new indictment by the U.S. authorities, accusing him of bribing Chinese officials.

The charges brought against SBF allege that he directed a bribe to Chinese authorities with the aim of unfreezing trading accounts belonging to Alameda Research. These accounts, which held over one billion dollars worth of cryptocurrency, had been frozen by Chinese officials, prompting Bankman-Fried to resort to illicit means to regain access to the funds.

Forbes also reported in its Digital Assets publication that SBF’s legal fees are being funded by Alameda money gifted to his father, Joe Bankman.

Galaxy Digital Reports $1 Billion Loss in 2022

Figure 36. Galaxy Digital lost one billion dollars in 2022

Galaxy Digital reported a net loss of one billion dollars for the 2022 financial year. Founder Mike Novogratz calls it a "formative year" for the company.

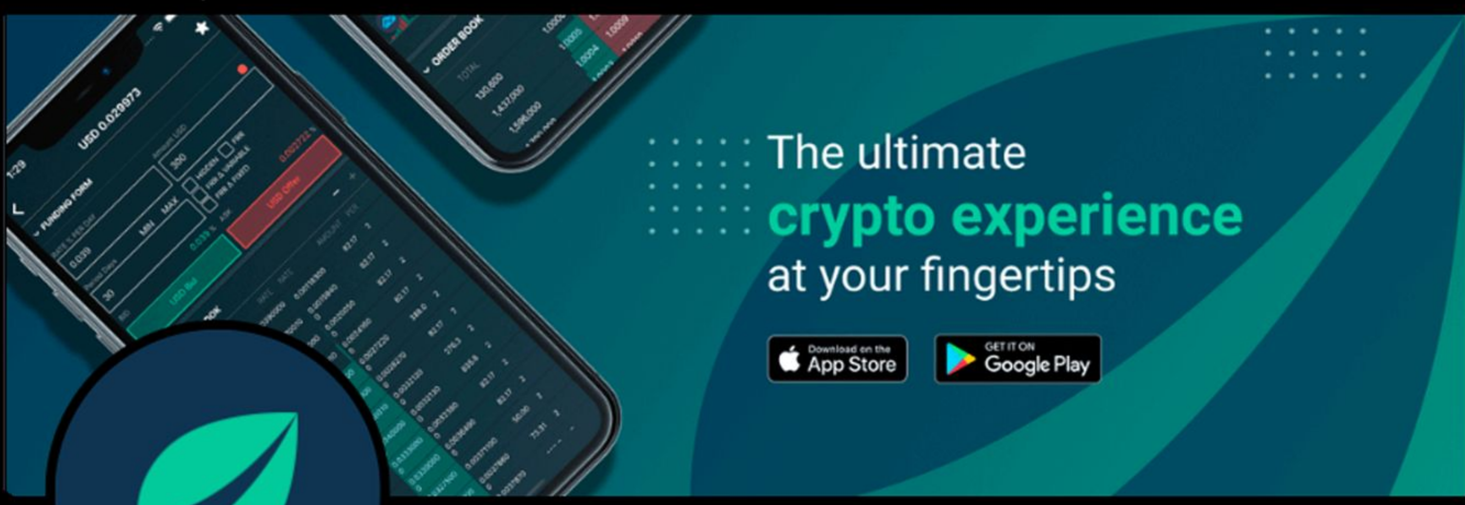
On March 28th, 2023, Canadian investment firm Galaxy Digital, operated by blockchain personality Mike Novogratz, announced its preliminary pre-tax income of $150 million for the first quarter of 2023 from January 1st to March 24th.

This announcement followed a one billion dollar net loss in 2022, which was largely attributed to a $659 million unrealized loss on digital assets and a $496 million unrealized loss on other investments.

Novogratz stated, "2022 was a formative year for Galaxy, and while we and our industry faced unprecedented macroeconomic events, we succeeded in staying the course and were able to opportunistically take advantage of strategic opportunities to build our operating businesses for the future."

On May 19th, 2022, Novogratz claimed that he was "permanently humbled" by the collapse of the $40 billion Terra ecosystem and reiterated the crypto industry looks stronger than ever and isn't "going away any time soon."

A year earlier, on February 3rd, 2021, *Cointelegraph* reported that Galaxy Digital invested $25 million into the Terra protocol. Galaxy Digital also reported a net income of $1.7 billion in 2021 during the height of the crypto bull market.



https://t.me/bitfinex

BITFINEX Alpha