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EXECUTIVE SUMMARY

The foundational strength of Bitcoin remains unshakably secure. As the network celebrated its billionth transaction last week, we are reminded that aside from all the attributes Bitcoin holds as a store of value and a hedge against monetary policy inflation, it is also still a fast and cheap way to transfer assets from peer-to-peer, with no intermediaries, banks or governments to act as a centralised authority.

In the last week, however, Bitcoin has come under selling pressure and it has seen its price drop from about $65,000 earlier in the week to $60,000. The source of the selling seems to be mainly short-term holders (holders for 155 days or less), but they have not been joined by long-term investors. Indeed, the previously observed long-term holder distribution that was seen in April seems to have waned, and on-chain data indicates that they do not seem to be participating in the latest sell-down.

If this trend persists, then we might be able to soon conclude that the bottom is already in and upside growth potential has increased. The recent volatility in daily net flows into the US Bitcoin ETFs also suggests that there is mixed investor sentiment, indicative of a near-term floor for the price being reached. Last Wednesday for example, there were no flows at all into all but one of the US Bitcoin ETFs; on Friday Blackrock's popular ETF saw inward flows but these were dwarfed by the outflows from the Greyscale ETF, GBTC. But on Monday of last week as well as on the previous Friday, every fund, including GBTC saw net positive inflows. This ongoing ebb and flow of capital into BTC ETFs, with no clear direction either way, supports our view that the bottom could almost be in.

In the macroeconomy, we also see a market turning cautious ahead of any clear direction emerging. The Fed's hawkish approach to inflation has led to a tightening in lending and a decline in US wholesale inventories. The contraction in both inventory levels and borrowing activities implies that businesses are bracing for a slowdown, adjusting their operational strategies in anticipation of softer economic conditions.

This cautious sentiment is also mirrored in consumer behaviour, with US consumer confidence dropping to a six-month low in May, driven largely by heightened concerns about inflation.

Meanwhile, in crypto-land, the US House of Representatives passed a resolution against the SEC's requirement for banks to account for customer-held crypto on their balance sheets. While this is viewed as a positive development, President Biden has opposed the resolution, advocating for the necessity of regulatory guardrails to ensure the stability and integrity of the crypto industry.

The SEC is also at the centre of the ongoing litigation that it has taken against Ripple Labs, with the SEC challenging Ripple's defence against allegations of recklessness in its XRP transactions. The SEC is arguing that it should be able to impose punitive measures against Ripple to deter it from potential future violations - even though Ripple has not recorded any breaches of SEC rules since 2020.

Have a good trading week!

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WHAT'S ON-CHAIN THIS WEEK?

Bitcoin Network Fundamentals Remain Strong Amidst Market Turmoil

Milestone Achieved: One Billion Transactions

Over eight hundred weeks since the genesis block on January 3, 2009, Bitcoin has achieved a new milestone, processing its one billionth transaction on May 6th. This coincides with a period of significant activity on the Bitcoin blockchain over the last 12 months, spurred by protocols such as Bitcoin Ordinals and Runes, and the introduction of spot Bitcoin ETFs, which have all played a role in boosting the network's usage.

The milestone illustrates the enduring popularity and usage of the Bitcoin network. On May 6th, more than 625,000 on-chain transactions were executed alone, an indication of the health of the blockchain and its adoption as a digital currency. It also points to the scalability and security of the network, which continues to handle a large volume of transactions effectively.

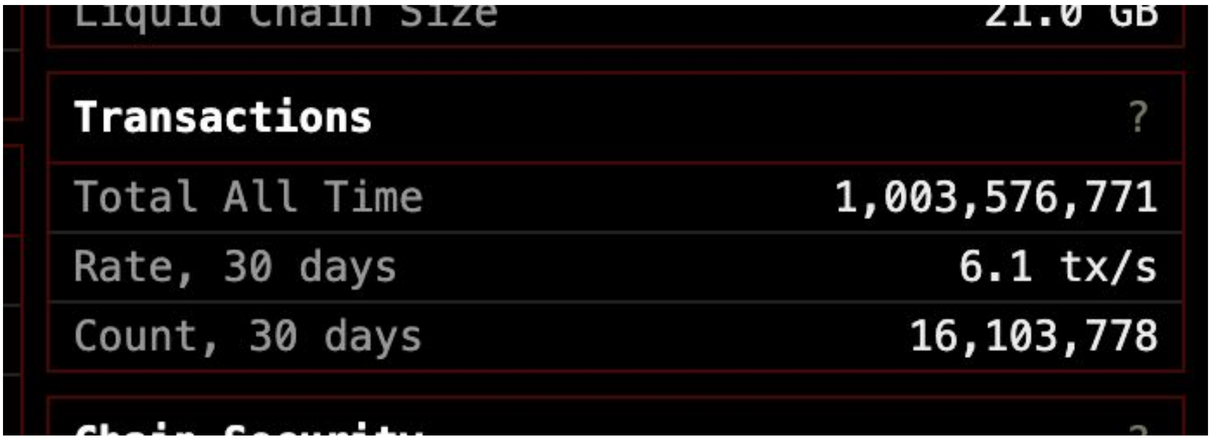


Figure 1. Bitcoin Total All-Time Transactions (Source: Clark Moody Bitcoin Dashboard)

Despite being widely regarded as a digital store of value, Bitcoin also continues to function effectively as a medium of exchange. With the current user base, the system operates efficiently, though scaling is still necessary to accommodate billions of users in the future. Today, Bitcoin has fulfilled so much of the vision its creators had for it. It is actively used for the transfer of billions in value globally, without the need for intermediaries like banks or governments.

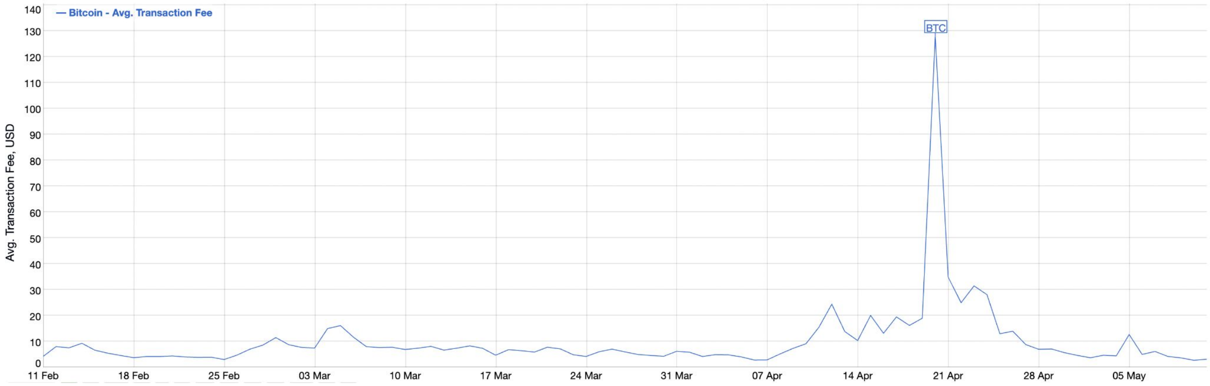


Figure 2. Bitcoin Average Transaction Fee (Source: https://bitinfocharts.com)

Post-halving, daily transaction fees have decreased, yet the average number of transactions processed weekly on the blockchain remains high relative to historical figures.

Figure 3. Bitcoin Inflation vs Bitcoin/USD Price

Bitcoin's inflation rate is now under one percent annually (refer Figure above). With the supply increasingly constrained, demand can only be met by the existing supply.

Adjustments in Mining Difficulty

One of the most noteworthy developments this past week was a six percent reduction in mining difficulty (refer figure below), the largest decrease since a seven percent drop in December 2022.

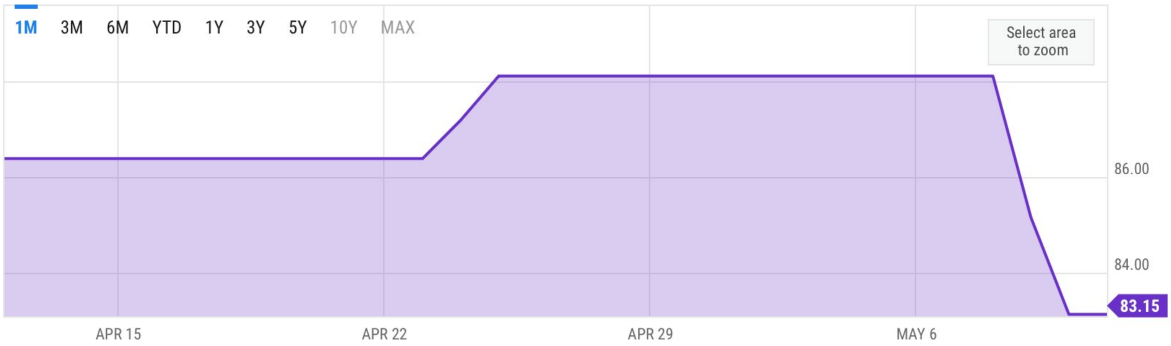


Figure 4. Bitcoin Mining Difficulty in Terahases. (Source: Yahoo Finance)

The difficulty measure for Bitcoin mining is a dynamic metric that indicates how challenging it is to mine a new block. This difficulty is recalibrated automatically every 2016 blocks, or approximately every two weeks, to maintain an average block time of about 10 minutes, irrespective of the number of miners active at any given time. The difficulty measures how many hashes (statistically) must be generated to find a valid solution to solve the next Bitcoin block and earn the mining reward. As more miners join the network, the difficulty increases. However, when the number of miners decreases, the difficulty is reduced, making it less challenging for the remaining miners to find new blocks.

After the halving event, miners operating less efficient ASICs or facing high operational costs have found it unprofitable to continue and subsequently shut down their operations. This reduction in competition is advantageous for the miners who remain, as a six percent decrease in difficulty translates to approximately a six percent increase in Bitcoin earnings for the same level of computational effort. This adjustment provides a valuable boost for those who miners who have continued operating after the halving.

Market Volatility and Investor Behaviour

Bitcoin has struggled to maintain much stability above $63,000 over the past week. Negative economic indicators from the US and cautious statements from the Fed have dampened any bullish sentiment.

In terms of trading behaviour, short-term Bitcoin holders (who have held their positions for less than 155 days) have also been realising substantial profits. The "Spent Output Profit Ratio" for this group recently exceeded one for the entire week, on a seven-day exponential moving average basis (used to smoothen the noise plot of the metric). This indicates that profits are outpacing losses once again, since prices spiked in March and the Bitcoin All-Time High was reached. This surge in profit-taking by short-term holders could be seen as a source of increased selling pressure, potentially capping or reversing price rallies if not supported by long-term investor purchases. The Short Term Output Profit Ratio (SOPR) is an analytical metric that tracks the spending of short-term market participants and values above one indicate that they are “moving” their coins at a profit.

On chain data indicates however, that long-term holders are not selling.

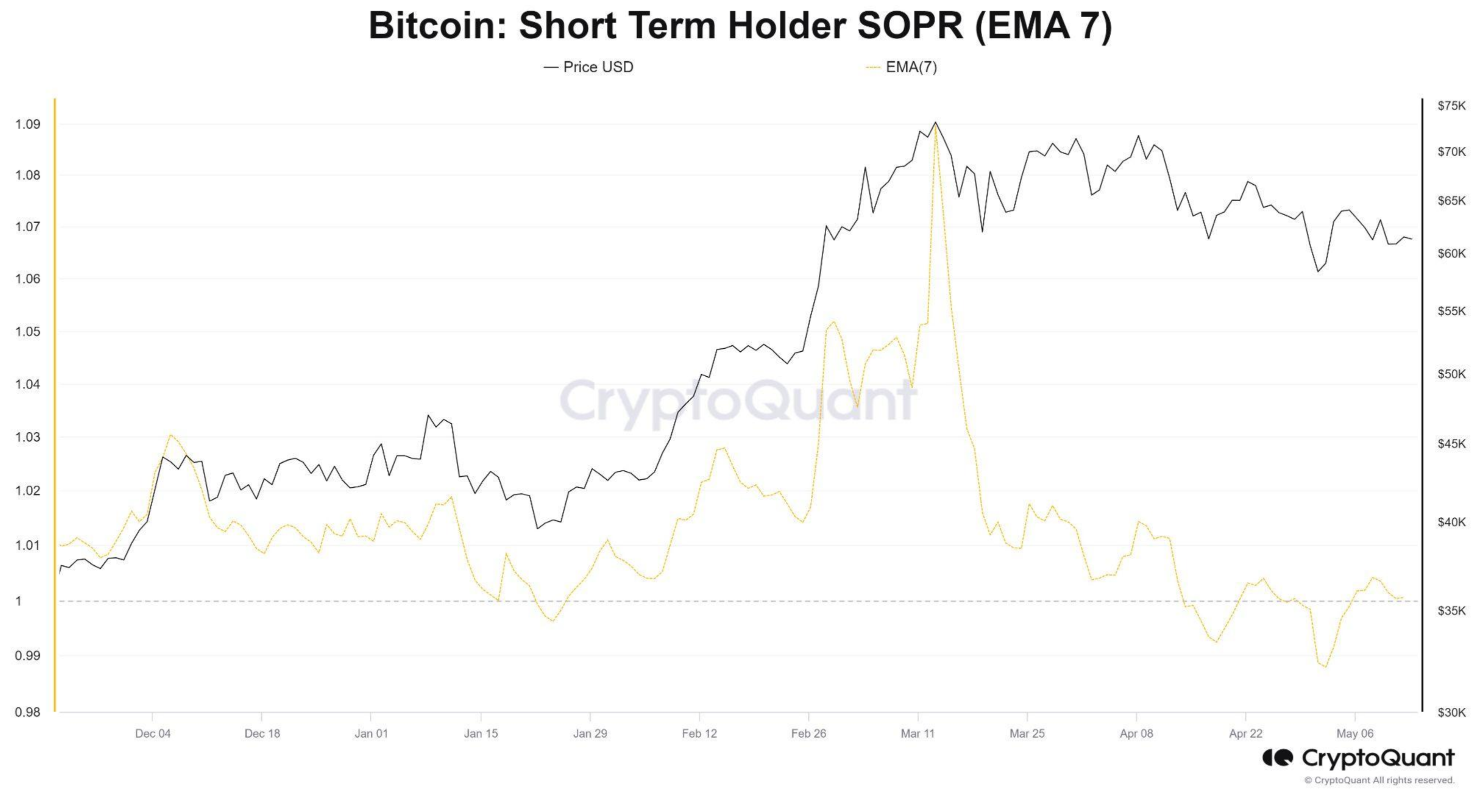


Figure 5. Short-Term Holders Spent Output Profit Ratio. (Source: CryptoQuant)

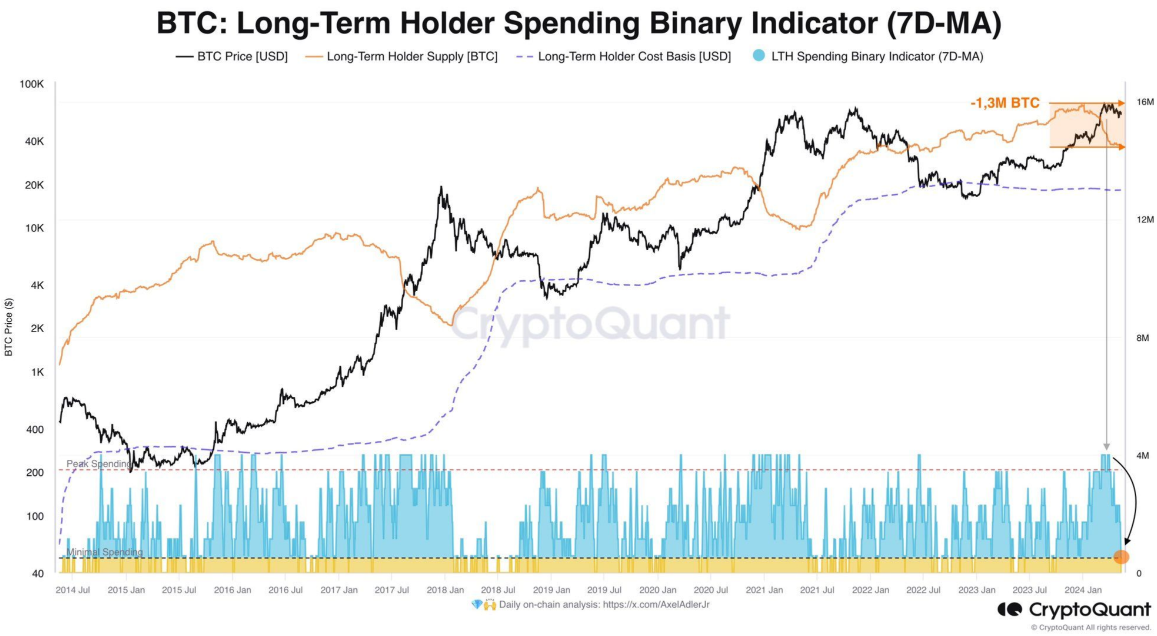


Figure 6. Long-Term Holder Spending Binary Indicator (Source: CryptoQuant)

The Long-Term Holder Spending Binary Indicator, however, suggests that long-term holders have been holding onto their assets over the past couple of weeks, and is reflective of their strategic positioning for potential entry points at market lows.

This is a regime shift, where it appears that the long-term holder distribution that has characterised recent market activity, seems to be finally waning, and supply inactivity is increasing. At the same time, the short-term holder selling of Bitcoin could be a sign of panic for that cohort as well as a shift of liquidity towards altcoins, which the recent decline in Bitcoin dominance would support. If such circumstances and market dynamics were to persist, it would be prudent to assume the short-term bottom for the market in general is already in and that our current multi-month range can potentially resolve to the upside.

As Bitcoin surpasses the significant one billion transaction threshold, its foundational strength is further underscored by several key factors that position the network for future value appreciation. The decrease in mining difficulty presents an advantageous scenario for existing miners, potentially stabilising the network's hash power and reducing the urgency to sell mined Bitcoin to cover operational costs. This shift is complemented by the steadfastness of long-term holders, whose reluctance to sell not only buffers the market against fluctuations driven by short-term profit-taking but also signals collective confidence in Bitcoin's enduring value.

Significant Volatility for Bitcoin ETFs

US Spot Bitcoin ETFs experienced both highs and lows last week. Last Monday alone, Bitcoin ETFs saw an influx of $217 million where notably, even the Grayscale ETF, GBTC, saw inflows of $3.9 million after registering inflows for the first time in the previous week on May 3rd. Additionally, Fidelity's Bitcoin ETF (FBTC) drew in almost $200 million across two days. Despite this, however, the tide turned, with three out of five days last week experiencing net outflows.

Bitcoin ETF Flow Table (US$m)

Date	IBIT	FBTC	BITB	ARKB	BTCO	EZBC	BRRR	HODL	BTCW	GBTC	DEFI	Total
23 Apr 2024	37.9	4.4	23.2	33.3	(0.3)	1.9	0.0	(1.9)	0.0	(66.9)	0.0	31.6
24 Apr 2024	0.0	5.6	0.0	4.2	0.0	0.0	0.0	0.0	0.0	(130.4)	0.0	(120.6)
25 Apr 2024	0.0	(22.6)	(6.0)	(31.3)	0.0	1.9	(20.2)	0.0	0.0	(139.4)	0.0	(217.6)
26 Apr 2024	0.0	(2.8)	(3.8)	5.4	0.0	0.0	0.0	0.0	0.0	(82.4)	0.0	(83.6)
29 Apr 2024	0.0	(6.9)	6.8	(31.3)	0.0	1.8	2.7	0.0	0.0	(24.7)	0.0	(51.6)
30 Apr 2024	0.0	(35.3)	(34.3)	3.6	(2.4)	0.0	0.0	0.0	0.0	(93.2)	0.0	(161.6)
01 May 2024	(36.9)	(191.1)	(29.0)	(98.1)	(5.4)	(13.4)	(9.7)	(6.5)	(6.2)	(167.4)	0.0	(563.7)
02 May 2024	0.0	0.0	0.0	13.3	1.5	3.4	2.3	0.0	0.0	(54.9)	0.0	(34.4)
03 May 2024	12.7	102.6	33.5	28.1	33.2	60.9	35.6	8.7	0.0	63.0	0.0	378.3
06 May 2024	21.5	99.2	2.1	75.6	11.1	1.8	0.0	1.8	0.0	3.9	0.0	217.0
07 May 2024	0.0	4.1	0.0	2.8	6.0	0.0	0.0	0.0	0.0	(28.6)	0.0	(15.7)
08 May 2024	0.0	0.0	11.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	11.5
09 May 2024	14.2	2.7	6.8	4.4	2.2	1.8	0.0	0.0	0.0	(43.4)	0.0	(11.3)
10 May 2024	12.4	5.3	0.0	0.0	0.0	0.0	0.0	0.0	0.6	(103.0)	0.0	(84.7)
Total	15,502.5	8,141.4	1,766.4	2,249.1	286.8	351.6	479.9	480.3	59.2	(17,632.9)	(2.1)	11,682.2
Average	184.6	96.9	21.0	26.8	3.4	4.2	5.7	5.7	0.7	(209.9)	(0.0)	139.1
Maximum	849.0	473.4	237.9	200.7	63.4	60.9	43.4	118.8	6.6	63.0	11.9	1,045.0
Minimum	(36.9)	(191.1)	(34.3)	(98.1)	(37.5)	(13.4)	(20.2)	(6.5)	(6.2)	(642.5)	(14.7)	(563.7)

Figure 7. Bitcoin ETF Flow Table (Source: Farside Investors)

The volatility in Bitcoin ETF flows over the past two weeks is an indication of mixed investor sentiment towards the asset. Last Wednesday, none of the 10 US ETFs saw any flows, apart from the Bitwise ETF (BITB), which saw a positive inflow of $11.5 million.

Last Friday saw more inflows into Blackrock's iShares Bitcoin Trust (IBIT) and Fidelity's FBTC, but Grayscale's GBTC reported significant outflows of over $100 million, and contributed to total net outflows for the day of $84 million across all Bitcoin ETFs.

Similar sentiment is afflicting the new spot-based Bitcoin and Ethereum ETFs in Hong Kong, which have also seen a mix of enthusiasm and setback. Bitcoin ETFs saw $2.3 million net inflows last week while Ethereum ETF saw $1.8 million net outflow.

The BTC price has also arguably reflected some of this sentiment, dropping from $63,000 to $60,000 on Saturday. BTC ETF flows remain a valuable indicator of sentiment on the asset.

HK Crypto ETF Flow Table
(US$m)

Coin	BTC	BTC	BTC	BTC	ETH	ETH	ETH	ETH	
Provider	Bosera	AMC	Harvest	Subtotal	Bosera	AMC	Harvest	Subtotal	Total
Ticker	9008 HK	3042 HK	3439 HK		9009 HK	3046 HK	3179 HK		
Seed	61.1	123.6	63.0	247.7	12.3	20.2	12.4	44.9	292.7
02 May 2024	2.0	3.1	5.0	10.1	1.2	2.0	1.4	4.6	14.7
03 May 2024	1.2	5.3	1.5	8.0	1.5	0.0	0.0	1.5	9.5
06 May 2024	0.0	(4.9)	0.0	(4.9)	3.2	0.0	0.0	3.2	(1.7)
07 May 2024	6.4	0.0	0.0	6.4	3.1	(3.4)	(1.4)	(1.7)	4.7
08 May 2024	6.2	0.1	0.0	6.3	(0.9)	(0.8)	(0.2)	(1.9)	4.4
09 May 2024	(0.6)	(4.9)	0.0	(5.5)	0.0	0.0	(1.4)	(1.4)	(6.9)
10 May 2024	-	0.0	0.0	0.0	-	0.0	0.0	0.0	0.0
Total Flow	15.2	(1.3)	6.5	20.4	8.1	(2.2)	(1.6)	4.3	24.7

Source: Farside Investors
Note: The above table is generated manually. Data based on a number of sources, including the ETF provider websites and third party financial information providers. The data in the table contains estimates. The data is likely to contain errors. Farside Investors is not liable for any errors or inaccuracies in the data.

Figure 8. Hong Kong Crypto ETF Flow Table (Source: Farside Investors)

GENERAL MACRO UPDATE

Loan Demand Cools as Fed Tightens Policy, But Real Estate Shows Resilience

The Federal Reserve's more hawkish stance in the first quarter has slowed lending. The recent Fed Senior Loan Officer Opinion Survey (SLOS) released last Monday, May 6th, highlights a decline in loan demand, particularly in the commercial, industrial, and consumer sectors. This shift marks a reversal from the slight recovery noted in the latter half of last year.

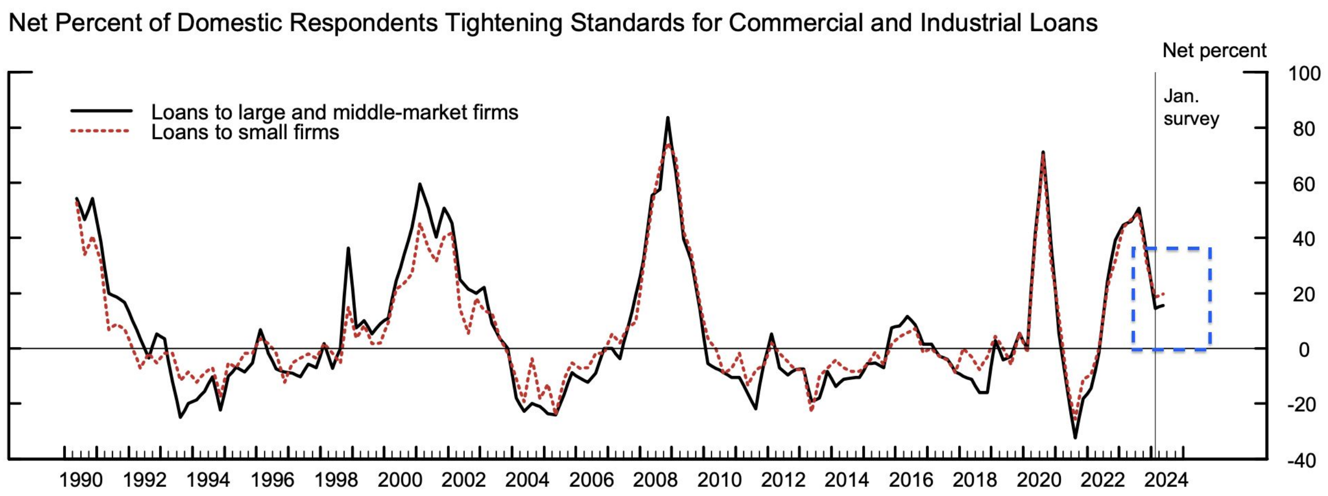


Figure 9. Net Percent of Respondents Tightening Standards for Commercial and Industrial Loans (Source: Federal Reserve)

The SLOS report detailed particularly stringent standards applied to commercial and industrial loans, while for households, the report pointed to a broad deterioration in loan demand, with auto loans hitting their lowest interest levels in a year.

In contrast, the real estate sector emerged as a notable exception. Indicators suggest improvements in demand due to a stabilisation of interest rates which have coaxed buyers back into the market - now adjusted to the 'new norm' of higher mortgage rates - and unwilling to postpone purchases any further.

Further optimism is also drawn from recent labour market data and a potential easing in housing costs expected later this year.

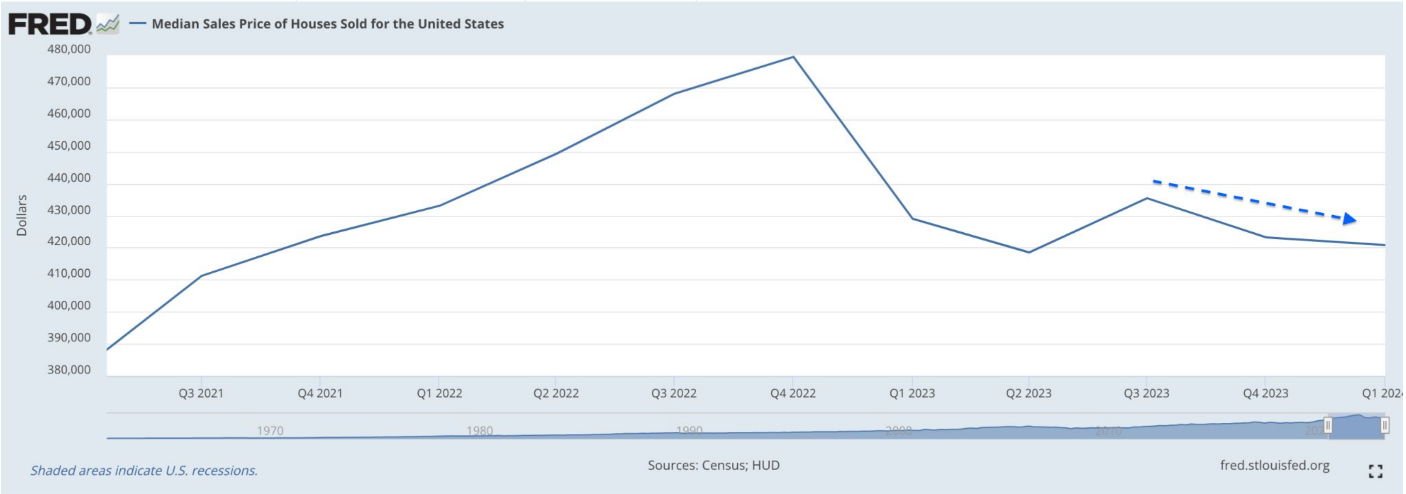


Figure 10. Decline in Median Home Prices in the US in the Last Two Quarters (Source: US Census Bureau)

Highlights of the SLOS Report:

Business Loans:

- There was a general tightening of standards and weakening of demand for commercial and industrial (C&I) loans across firms of all sizes. The tightening covered aspects such as the maximum size of credit lines and the spreads of loan rates over the cost of funds.
- Major reasons cited for tightening C&I loan standards included a less favourable economic outlook, reduced risk tolerance, and worsening industry-specific problems.
- Demand for C&I loans decreased, with notable declines in customer financing needs for mergers, acquisitions, and investments.

Commercial Real Estate (CRE) Loans:

- Standards tightened for all types of CRE loans, with the tightening more prevalent among smaller banks.
- Demand for CRE loans generally weakened, particularly for loans secured by nonfarm nonresidential and multifamily residential properties.
- Over the past year, banks reported tightening all surveyed terms for CRE loans, including interest rate spreads, maximum loan sizes, and loan-to-value ratios. The primary reasons were less favourable outlooks for CRE market conditions and increased regulatory concerns.

Household Lending:

- Residential Real Estate (RRE) Loans: Standards tightened for some categories, such as non-qualified mortgage (QM) jumbo and subprime loans, while demand weakened across all RRE loan categories.
- Home Equity Lines of Credit (HELOCs): Both standards and demand have tightened and weakened respectively.
- Consumer Loans: Banks reported tightening standards and terms for credit card, auto, and other consumer loans, with significant increases in minimum credit score requirements and interest rate spreads. Demand for these loans also weakened.

Overall Trends:

- While the tightening of lending standards continued across most loan categories, the extent of tightening was less severe compared to the previous quarter.
- The survey also highlighted a general decrease in the number of inquiries from potential borrowers, indicating a broader slowdown in loan demand.

Decline in US Wholesale Inventories Dragged Economic Growth in Q1

MONTHLY WHOLESALE INVENTORIES

MARCH 2024	$894.7 billion	-0.4%
FEBRUARY 2024 (revised)	$898.7 billion	+0.2%*

Next release: June 7, 2024

* The 90 percent confidence interval includes zero. There is insufficient evidence to conclude that the actual change is different from zero.
Data adjusted for seasonality but not price changes.
Source: U.S. Census Bureau, Monthly Wholesale Trade Survey, May 8, 2024.

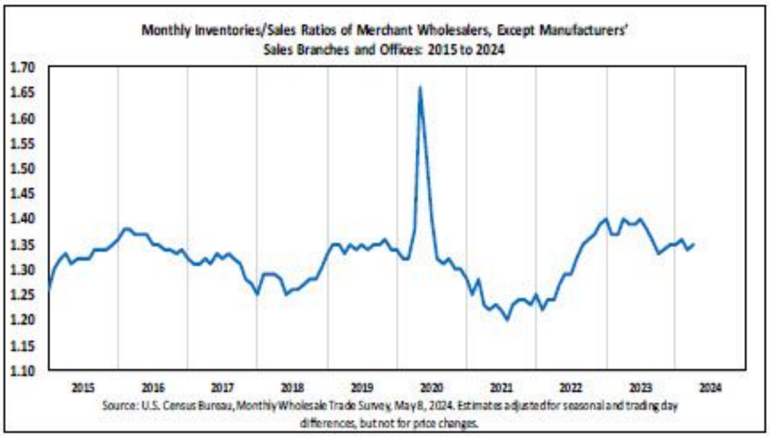


Figure 11. Monthly Wholesale Inventories

March witnessed a reduction in US wholesale inventories, indicating that investments in inventory was a drag on economic expansion during the first quarter. According to the March Wholesale Trade report, issued last Wednesday, May 8th, there was a 0.4 percent decrease in wholesale inventories. This decrease follows a modest rebound in February where stocks at wholesalers saw a slight increase of 0.2 percent.

Additionally, sales at wholesalers also saw a downturn, decreasing by 1.3 percent in March after a previous increase of two percent in February. As a consequence, the time it will take for wholesalers to clear their shelves increased slightly, moving from 1.34 months in February to 1.35 months in March.

The reduction in private inventory investment is acting as a drag on overall GDP growth, and marks the second consecutive quarter where inventory cutbacks have impacted the economy.

This contraction is echoed by findings from the recent SLOS survey (discussed in the previous chapter) which highlighted a downturn in loan demand across commercial and industrial sectors. These indicators together suggest that businesses might be anticipating slower economic growth and are accordingly adjusting their strategies, impacting both inventory levels and borrowing activities.

US Consumer Sentiment Hits Six-Month Low

Preliminary Results for May 2024

	May 2024	Apr 2024	May 2023	M-M Change	Y-Y Change
Index of Consumer Sentiment	**67.4**	77.2	59.0	-12.7%	+14.2%
Current Economic Conditions	**68.8**	79.0	65.1	-12.9%	+5.7%
Index of Consumer Expectations	**66.5**	76.0	55.1	-12.5%	+20.7%

Figure 12. Preliminary Results for University of Michigan Consumer Sentiment

In May, US consumer sentiment declined to its lowest level in six months, as concerns over inflation rose.

The University of Michigan Consumer Sentiment survey, issued last Friday, May 10th, noted a significant drop in confidence across various demographic groups, irrespective of age, income, education level, or political affiliation.

The May index registered at 67.4, marking a decrease from April's final reading of 77.2 and falling short of the 76.0 consensus forecast. This decline reflects broad-based anxiety over economic conditions, and represents the weakest sentiment reading since last November.

Additionally, the report indicated an uptick in inflation expectations, with the one-year outlook rising to 3.5 percent in May, up from 3.2 percent in April. This level remains notably higher than the 2.3-3 percent percent range observed before the pandemic. The five-year inflation forecast also edged higher to 3.1 percent from three percent last month, continuing to hover within the narrow range noted over recent years but still above pre-pandemic levels.

We believe however that these results might be more reflective of past conditions rather than indicative of future consumer spending. With stabilising gasoline prices and a generally upward trend in stock market values, these heightened inflation concerns are likely exaggerated.

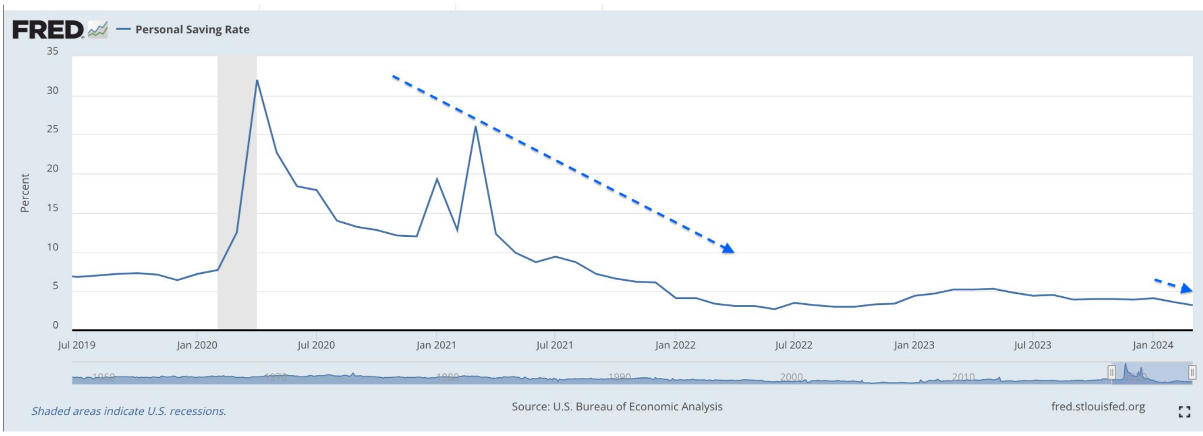


Figure 13. Further Decline in Personal Savings Rate from the Beginning of 2024 (Source. Bureau of Economic Analysis)

We see indications of this, for example, in the sentiment among higher-income groups, which remains strong, buoyed by gains in the stock market that have bolstered wealth. In contrast, lower-income groups feel the pinch of inflation more acutely as their pandemic-era savings dwindle. We believe that with more evidence of an overall improvement in inflation, and potential shifts in Fed policy later this year could brighten prospects for these more vulnerable populations in the near future.

Next week, investors will eye readings on inflation in the form of the consumer price index (CPI) and producer price index (PPI), as well as retail sales data. What will matter most in the upcoming data is not so much the magnitude, but the direction.

NEWS FROM THE CRYPTO-SPHERE

House Approves Overturning SEC Crypto Rules, Biden Vows Veto

May 8, 2024
(House)

STATEMENT OF ADMINISTRATION POLICY

H.J. Res. 109 – Congressional Disapproval of "Staff Accounting Bulletin No. 121" Issued by the Securities and Exchange Commission

(Rep. Flood, R-NE, and four cosponsors)

The Administration strongly opposes passage of H.J. Res. 109, which would disrupt the Securities and Exchange Commission's (SEC) work to protect investors in crypto-asset markets and to safeguard the broader financial system. H.J. Res. 109 would invalidate SEC Staff Accounting Bulletin 121 (SAB 121), which reflects considered SEC staff views regarding the accounting obligations of certain firms that safeguard crypto-assets. Moreover, as explained in staff's accompanying release, SAB 121 was issued in response to demonstrated technological, legal, and regulatory risks that have caused substantial losses to consumers. By virtue of invoking the Congressional Review Act, it could also inappropriately constrain the SEC's ability to ensure appropriate guardrails and address future issues related to crypto-assets including financial stability. Limiting the SEC's ability to maintain a comprehensive and effective financial regulatory framework for crypto-assets would introduce substantial financial instability and market uncertainty.

If the President were presented with H.J. Res. 109, he would veto it.

* * * * * * *

Figure 14. House Approves Overturning SEC Crypto Rules, Biden Vows Veto

- **The US House of Representatives has passed a resolution against the SEC's crypto policy, SAB 121**
- **President Biden threatens to veto, citing the need for regulatory guardrails in the crypto industry**

On May 9th, the US House of Representatives voted to overturn the SEC's controversial crypto accounting policy, Staff Accounting Bulletin No. 121 (SAB 121). The policy, which mandates banks to include customer-held digital tokens on their balance sheets, has been criticised for stifling banks' involvement in the crypto sector.

The US administration has expressed strong opposition to the resolution, highlighting the risks and potential for consumer losses without these regulations. He stated that overturning SAB 121 would lead to financial instability and confirmed he would veto the measure if it reaches his desk.

The resolution now moves to the Senate, where its fate will be decided. If passed, it would block any similar SEC regulations in the future, significantly affecting the regulatory landscape for digital assets in the US.

SEC and Ripple Labs Edge Closer to Conclusion in Legal Dispute Over XRP

Figure 15. SEC and Ripple Labs Edge Closer to Conclusion in Legal Dispute Over XRP

- **The SEC has submitted its final reply in the ongoing lawsuit against Ripple Labs, arguing against Ripple's claim of non-recklessness in its XRP dealings and emphasising the potential for future violations despite no breaches since 2020**
- **The SEC disputes Ripple's assurances of compliance and structural changes post-lawsuit**

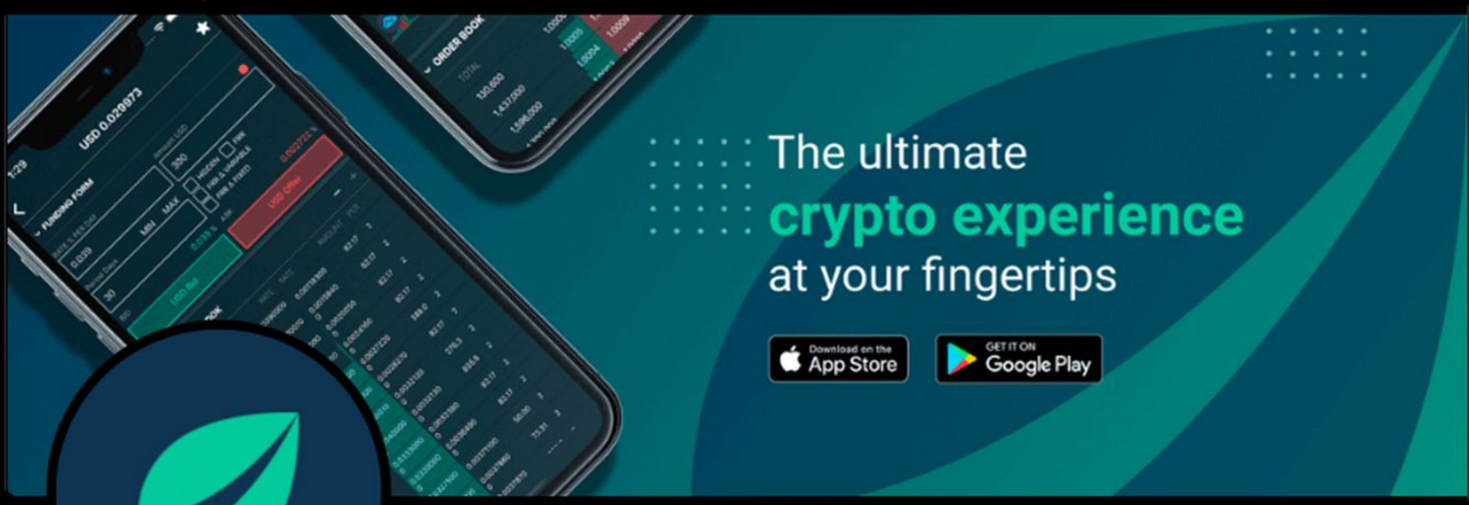
In a significant development in the ongoing legal battle between Ripple Labs and the United States Securities and Exchange Commission (SEC), the SEC has submitted its final response during the lawsuit's remedies stage last Tuesday, May 7th. The agency has taken a firm stance against Ripple's claim that it operated without recklessness in its dealings with the cryptocurrency XRP, despite a previous court decision that dismissed Ripple's "fair notice" defence.

The SEC argues that there remains "widespread uncertainty" regarding the legal status of XRP. The agency continues to express concerns over Ripple's potential future violations, despite Ripple not having breached any regulations since the lawsuit commenced in 2020.

Throughout the remedies process, Ripple has sought to minimise its culpability while emphasising its cooperation with the SEC since the initial coin offering of XRP in 2013. However, the SEC points out that Ripple's lack of violations post-2020 does not guarantee that there won't be any future infractions.

Moreover, the SEC has dismissed Ripple's claims that it only conducted sales outside the US, and to accredited investors, noting that these defences were dropped during the summary judgement phase. The SEC also refutes Ripple's adjustments to contracts for on-demand liquidity sales, stating that these contracts lacked essential restrictions, thus failing to address the violations identified.

The SEC maintains that Ripple's arguments do not eliminate the necessity for injunctions to avert potential future violations. As the case nears its conclusion, the SEC's latest filings highlight the ongoing debate over the compliance and future conduct of blockchain enterprises like Ripple in the regulatory landscape.



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