BITFINEX Alpha

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EXECUTIVE SUMMARY

In the last issue of *Bitfinex Alpha*, we suggested that the fall to $53,000 for Bitcoin, could be a local bottom based on on-chain and order flow metrics. As price rebounded over 13 percent from the lows, closing the week up 8.76 percent. BTC has now retested the 125-day range low of $60,200, a critical level it broke through on July 3rd after news of selling by the German government.

However, the weekend recovery does not necessarily mean that the downturn is over. Indeed weekend driven mini-rallies have been common over the past few months, which have then been followed by a retracement during the week. We are therefore watching closely how the start of this week plays out before drawing any firm conclusions about the market’s possible future trajectory.

One positive driver is that the near constant sell-pressure from Long-Term Holders (LTHs) appears to have subsided, with LTH supply stabilising at around 14.8 million bitcoins, from 16.2 million Bitcoins in January. This stabilisation indicates a reduction in selling pressure, a dynamic that is supported by the the LTH Spent Output Profit Ratio metric, which shows a decrease in profit-taking aggressiveness.

Indeed, with LTH supply stabilising, the focus is inevitably shifting to Short-Term Holders, whose supply has notably increased since January and remained consistent at around 4.8 million BTC. This influx of STH supply is largely due to new investors entering the market via ETFs and attempting to buy the dip during the last correction.

However, the current downward price movement has pushed over 2.8 million Bitcoins held by STHs into unrealised net losses. This scenario places considerable pressure on these recent investors to decide whether to hold and wait for a potential recovery or to sell their assets at less favourable prices. Despite the current bearish trends and supply pressures from entities like Mt. Gox creditors, the market may be nearing a point of equilibrium.

The weekend's upward movement suggests potential for a short-term recovery, but the market remains sensitive to news and external influences. Monitoring how STHs manage their holdings and the market's reaction at the start of the week will be critical in determining the short-term direction of BTC prices.

In the meantime, the US economic landscape exhibits a mix of promising trends and ongoing challenges. Notably, consumer prices decreased for the first time in four years, primarily driven by lower gasoline prices and a deceleration in rent increases. This shift has bolstered the perspective that disinflation is becoming a sustained trend within the US economy, potentially paving the way for the Federal Reserve to lower interest rates in September.

Even though producer prices experienced a modest rise in June, largely attributed to increased service costs, the components driving the rise are historically volatile, and the Producer Price Index calculation does not account for falling shelter costs—a significant factor in the fall in consumer prices.

Similarly, the Small Business Optimism Index also rose, recording the highest reading of the year so far, however the index remains below its historical average of 98, a benchmark it has failed to meet for 30 consecutive months. Inflation remains the dominant concern for small businesses, which continue to navigate these uncertainties while keeping a close watch on economic developments and the Fed's forthcoming decisions.

Further signs of stress in the US economy is the surge in consumer borrowing to a three month high, as of May. This is being predominantly driven by a rise in credit card balances, pushing consumer debt to record levels. Given that much of this debt carries high interest rates, the persistence of elevated rates will heighten financial strain on households, potentially curbing future consumer spending and, consequently, slowing economic growth.

In recent developments within the crypto industry, Germany's selling of Bitcoin appears to be over, while the US Securities and Exchange Commission (SEC) has also concluded their investigations into Hiro Systems and Paxful.

However, US lawmakers' attempts to override President Biden's veto of a measure designed to overturn the SEC's Staff Accounting Bulletin (SAB) 121 fell short of the required two-thirds majority in the House. SAB 121 mandates that banks must list crypto holdings as liabilities, effectively barring them from offering digital asset custody services.

Have a good trading week!

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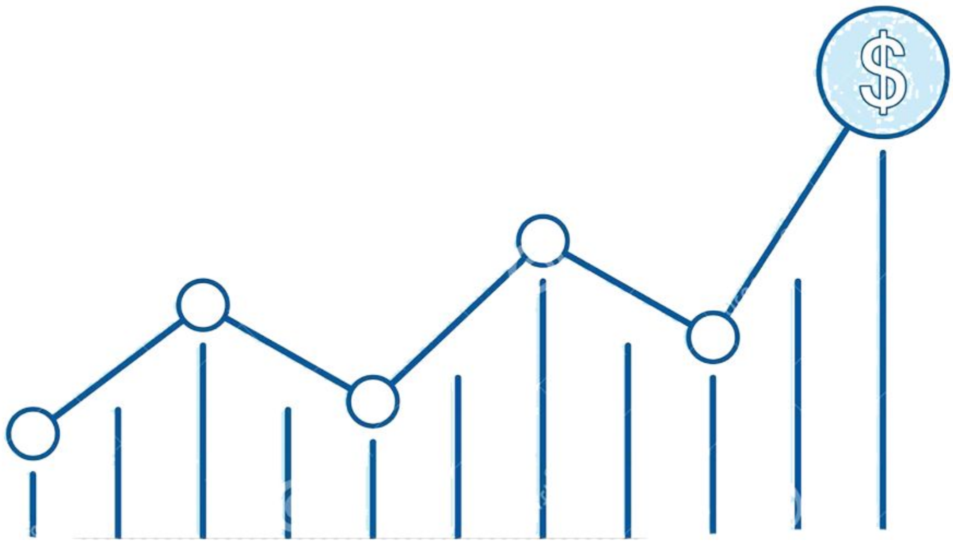

WHAT'S ON-CHAIN THIS WEEK?

BTC Retests $60,000 Level After Breakdown from Range

In last week's *Bitfinex Alpha*, we took the view that the fall in bitcoin prices to $53,000 could be at least a local bottom based on on-chain and order flow metrics. Our view was vindicated after the price moved up more than 13 percent from the lows, and closed the week 8.76 percent in the green. We have now risen back above the 125-day range low of $60,200 that we broke through on July 3rd, after news of selling by the German Government hit the market.

Figure 1. BTC/USD Daily Chart. (Source: Bitfinex)

It is noteworthy however that a significant portion of the recent upward movement in BTC has occurred over the weekends. Given the recent news-driven environment it will be critical to see how the market reacts at the start of this week, particularly if the supply concerns that have been [alleviated over the weekend] re-emerge when traditional markets open.

The recent supply pressure from Germany now appears to have been factored into market prices, and market sentiment began to improve on Saturday following reports that wallets associated with the German Government had nearly emptied. However, with the coins transferred to trading desks and exchanges, it does not necessarily mean the end of selling pressure as much depends on how these desks execute their trades.

This shift in sentiment highlights the market's capacity to quickly integrate new information and adjust expectations accordingly, however we believe it is still important to focus on the market's reaction over the first two trading days of the week for two reasons.

Firstly, the weekly close at around $60,200, which has been a support level of the range low, is now acting as a potential resistance level given the drop through $60,000 two weeks ago. We are now in no man's land until we get clear resolution above or below this level.

Secondly, trading patterns over the past three months, and especially over the past four weeks (as shown below), suggests that markets usually see upside over the weekend. This seems to especially occur on Saturdays when supply pressures seem to subside, as selling possibly decreases, only for a retrace to emerge in the new trading week.

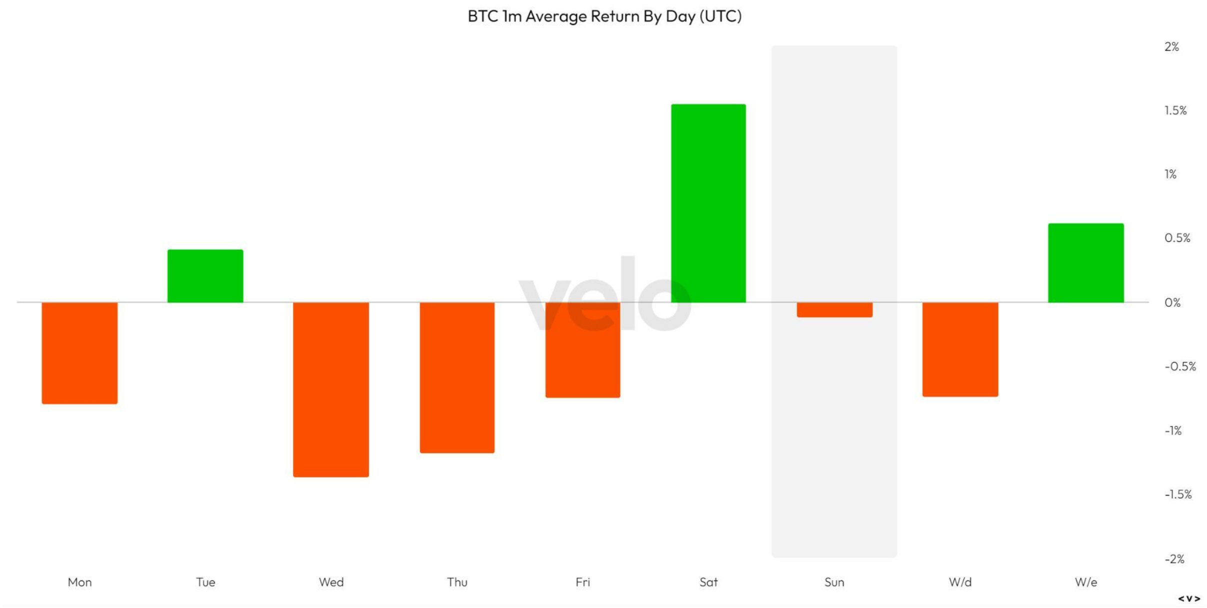

Figure 2. BTC Seasonality Over The Past Month By Average Returns By Day. (Source: VeloData)

Over the past month, Saturdays have seen an average return of 1.6 percent for BTC, reflecting a noticeable uptick in weekend performance (indicated as W/e in the chart above). When broadening the scope to include the entire 'summer range', covering the past three months, the average return on Saturdays slightly decreases to 0.9 percent. This data suggests that weekends, particularly Saturdays, have been relatively favourable for Bitcoin investors during this period, with a consistent pattern of positive returns.

The chart below highlights the past six Saturdays dating back till June 8th when we were last at our range highs above $70,000.

Figure 3. BTC/USD Daily Chart. (Source: Bitfinex)

The above figure clearly demonstrates how weekends have provided temporary relief in the overall recent downturn we have seen in BTC, however it also makes the case for the need to exercise caution.

Another important factor is that, in our view, crypto asset prices in general in the current period have been determined by the news agenda, rather than fundamentals. Selling pressure concerns have not completely disappeared as Mt. Gox creditors are also scheduled to receive their BTC payouts over the next couple of weeks. We expect these headlines to continue to have some impact on price before a complete pricing in of the situation.

Long-Term Holder Profit-Taking Is Stabilising

Our assessment of a potential local bottom in the bitcoin market was partly based on the noticeable slowdown in profit realisation by Long-Term holders (LTHs). The supply held by these LTHs has stabilised around the 14.8 million bitcoins mark, following a significant drop from 16.2 million bitcoins in January 2024. This stabilisation over the past three months indicates a reduction in selling pressure from this cohort of investors.

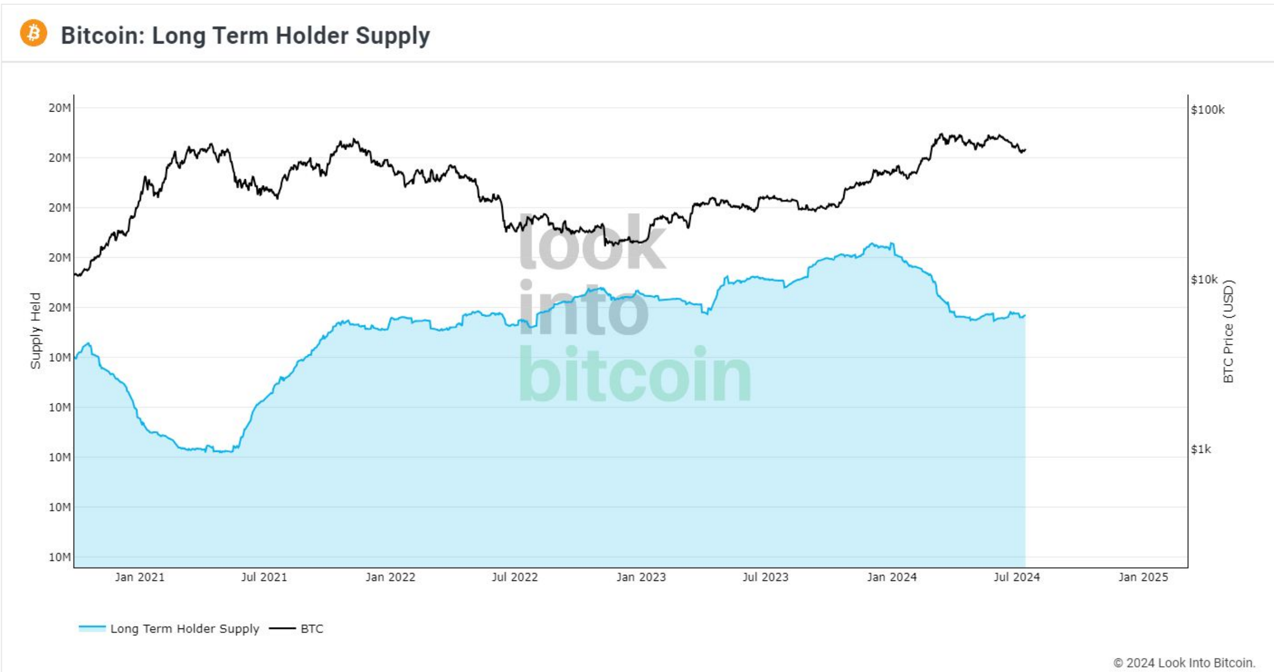

Figure 4. Bitcoin Long-Term Holder Supply. (Source: LookIntoBitcoin)

All Long-Term Holder metrics we use are associated with tracking wallets that have held their BTC without moving it for a period of 155 days or more. It is also important to note that it is possible that coins moving from an LTH wallet are not necessarily being moved to sell.

The current movement from the LTH Supply metric is analogous to a similar period when LTH supply was distributed between November 2020 and May 2021, at which point BTC found a bottom. In fact we see these rotations in LTH Supply as being quite cyclical, and which have been repeating since 2017. The current stabilisation around the 14.8 million mark therefore, could signal that the current mid-cycle correction could potentially end over the next month. Historical patterns suggest that once long-term supply starts ranging in a zone, following a 4-5 month period of distribution - which has been the case since the end of January 2024 - the price finds a bottom in the following four to six weeks.

The Long-Term Holder Spent Output Profit Ratio (LTH SOPR) and other related metrics further support this view, showing a decrease in the aggressiveness of profit-taking among long-term holders. These indicators suggest that LTHs, who typically exert a stabilising influence on the market due to their tendency to hold through volatility, are becoming less inclined to sell their holdings at the current price levels.

SOPR compares the combined USD value of all coins spent on a particular day to the combined USD value of these coins when they were initially acquired or roughly when they were purchased. A SOPR value of one indicates that, on average, sellers are breaking even, neither realising a profit nor a loss on their transactions. Values above one suggest that sellers are on average selling their coins at a profit, as is the current case.

The LTH SOPR value peaked on May 28th at 6.2 and has been declining since with a small spike on July 6th and 7th. (refer Figure below)

Figure 5. Long-Term Holder Spent Output Profit Ratio. (Source: ChainExposed)

This behaviour aligns with the patterns often observed at market bottoms, where the rate of selling begins to taper off as holders start to anticipate potential future gains rather than taking immediate profits. As such, the current metrics provide a strong indication that the market may be nearing a point of equilibrium, where selling pressure diminishes and a foundation for potential price recovery is established.

An important point to note is that bitcoin is currently experiencing its most significant drawdown of the current cycle, trading at more than 27 percent below its all-time high (ATH). However, when placed in historical context, this drawdown is relatively mild compared to previous cycles, where deeper contractions were common.

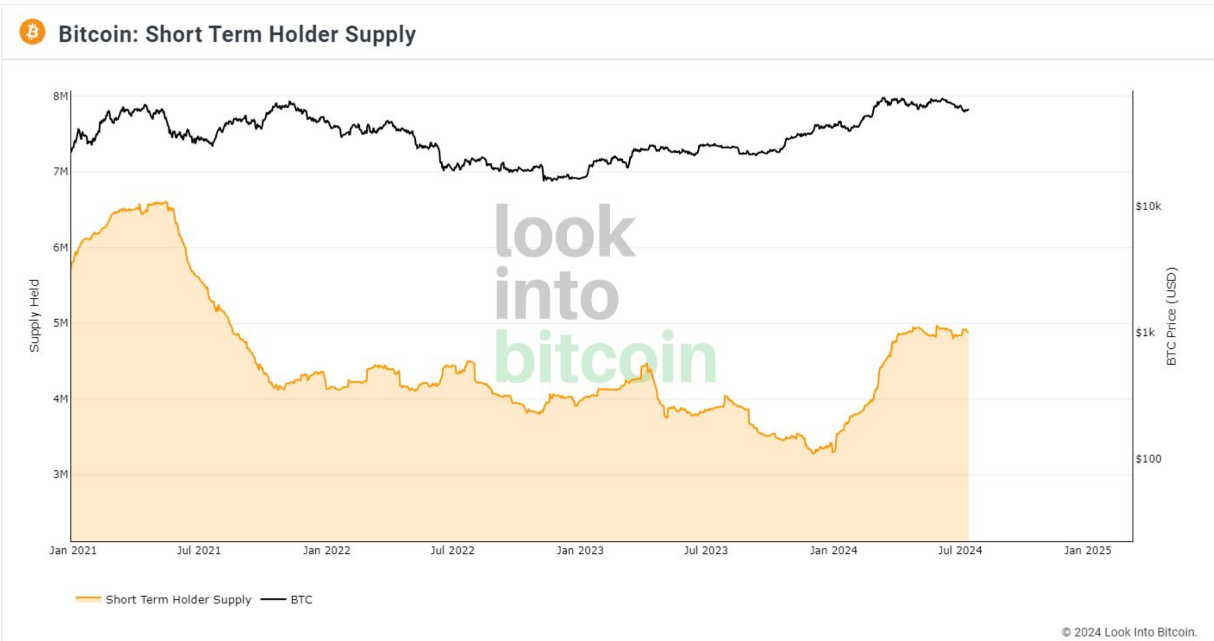

Figure 6. Short-Term Holder Supply. (Source: LookIntoBitcoin)

During this current market correction, we've observed a stark contrast between the behaviours of Long-Term Holders and Short-Term Holders (STH). While LTH supply has declined, STH supply has notably increased since January and remained consistent at the 4.8 million bitcoins mark throughout the current range and subsequent price decline.

This influx of STH supply is largely due to new investors entering the market via ETFs who have been attempting to buy the dip during this cycle's most significant correction. However, the continued downward price movement has pushed a substantial number of these short-term holders into unrealized net losses. Specifically, over 2.8 million bitcoins held by STHs are now valued below their on-chain acquisition prices. (refer Figure below)

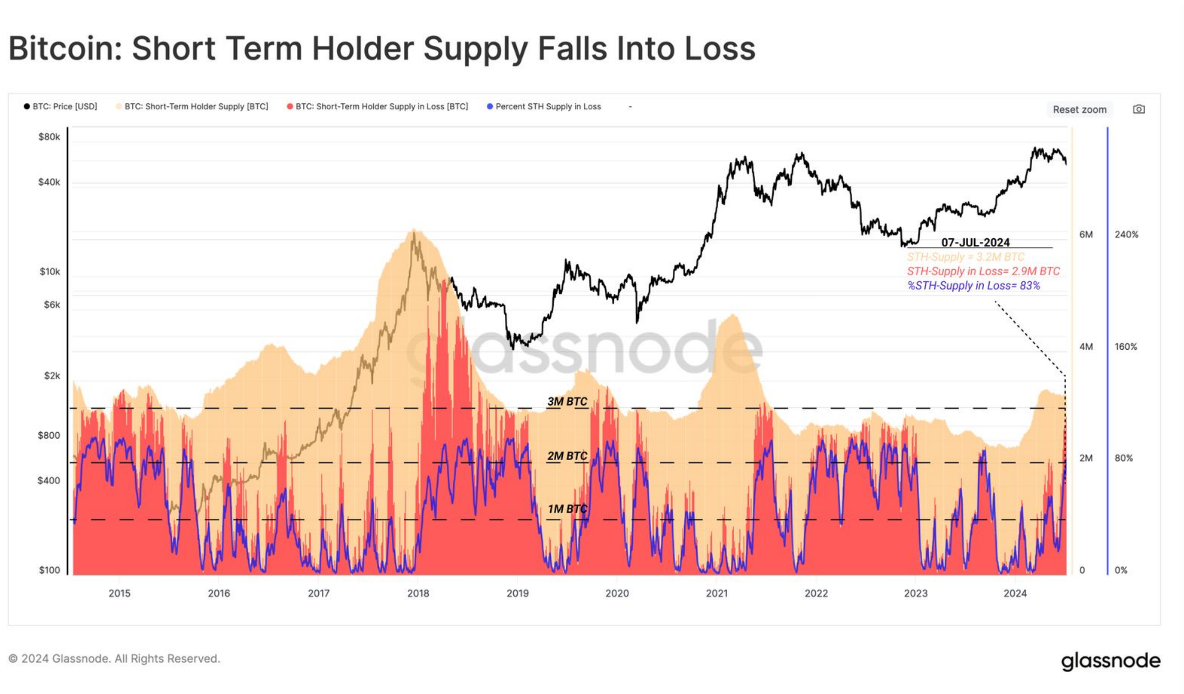

Figure 7. Bitcoin STH Supply In Loss. (Source: Glassnode)

This scenario places considerable pressure on these recent investors, who must now decide whether to hold and wait for a potential market recovery or to sell their assets to cut losses, albeit at less favourable prices.

The impact of this drawdown extends beyond individual investment strategies. The collective actions of STHs, particularly if many choose to sell, could significantly influence market liquidity and price stability. Such decisions are crucial as they not only affect the financial outcomes for individual holders but also shape overall market sentiment and the potential pathways to market recovery. How STHs manage their holdings in the coming weeks will be critical in determining the market's short-term direction.

GENERAL MACRO UPDATE

US Inflation Moderates, Paving Way for Potential Fed Rate Cuts

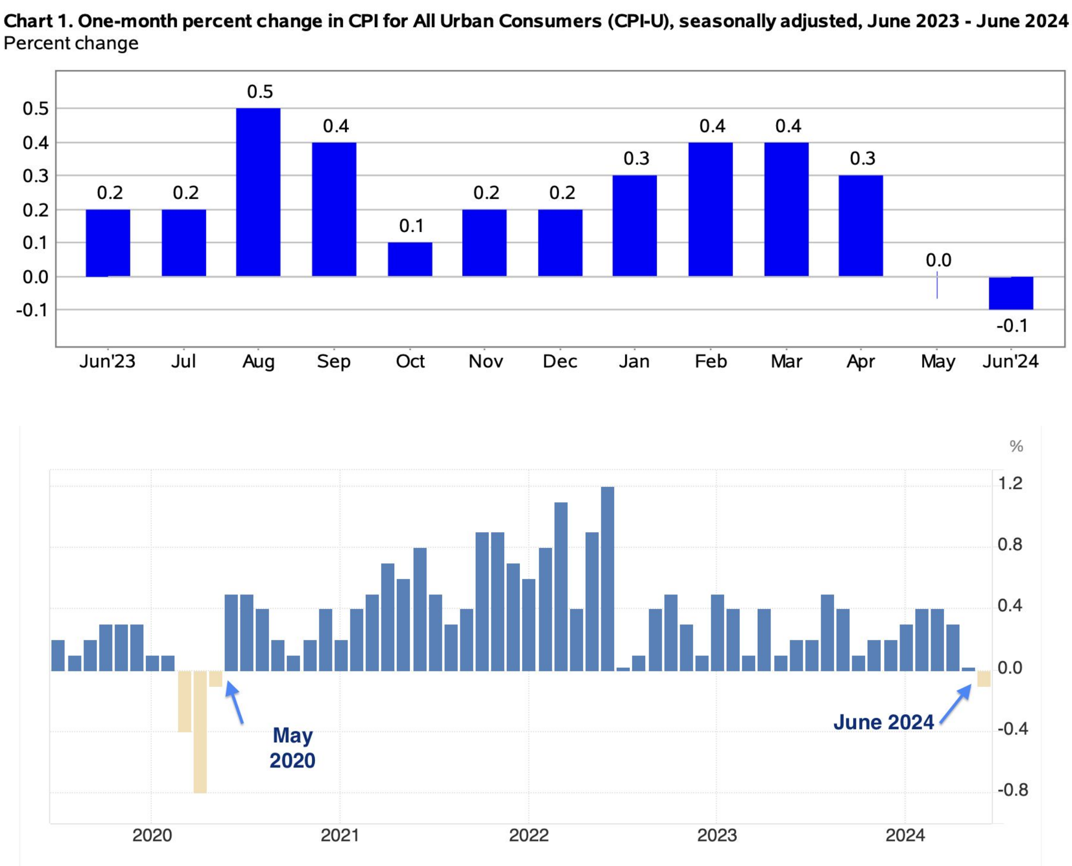

Figure 8. One-Month Change in CPI (Source: Bureau of Labor Statistics)

Consumer prices came down in June for the first time in four years, driven by lower gasoline prices and slowing rent increases. The data reinforces the view that disinflation is becoming entrenched in the US economy, and will bring the Federal Reserve closer to considering an interest rate cut in September.

The narrative of disinflation in energy and core goods has been a feature of the inflation landscape since last year. Consumer Price Index data for June, which was released last week, indicated that this trend was beginning to spread to other areas of the economy after it reported its first decrease in four years.

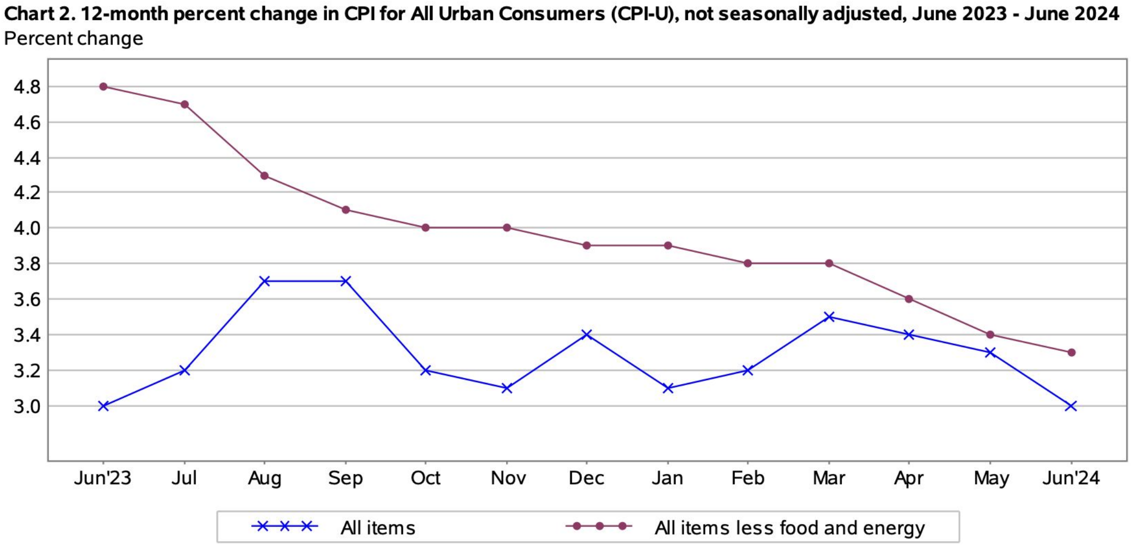

Figure 9. 12-Month Percent Change for Headline and Core CPI (Source: Bureau of Labor Statistics)

Headline inflation came in down 0.1 percent, bringing the annual inflation rate to 3 percent. The consensus forecast for monthly and annual headline inflation was for a 0.1 percent and 3.1 percent increase respectively. Core inflation, which excludes volatile food and energy prices, also rose by just 0.1 percent for the month, marking a 3.3 percent increase year-on-year. The consensus forecast was for a 0.2 percent increase from the previous month and a 3.4 percent increase from a year ago. We have come a long way from the 9.1 percent year-on-year inflation reported in June 2022.

We anticipate that this moderation in Consumer Price Index data will be similarly reflected in the forthcoming Personal Consumption Expenditure price index, which next reports on July 26th, and which the Federal Reserve closely monitors to set monetary policy.

While Fed Chair Jerome Powell has urged caution, he stated that the trend is promising, though more consistent data is needed before declaring victory over inflation. We are increasingly confident that inflation is on the right track to return to the Fed's two percent target.

Given the current economic data, there is a high probability that the Fed will start reducing its federal funds rate in September. Moreover, further easing in the labour market, as suggested by recent testimony from Powell, might warrant an additional rate cut in December. In his recent speech to the US Congress, Powell said that "in the labour market, a broad set of indicators suggests that conditions have returned to about where they stood on the eve of the pandemic: strong, but not overheated."

US Producer Prices Rise Slightly in June

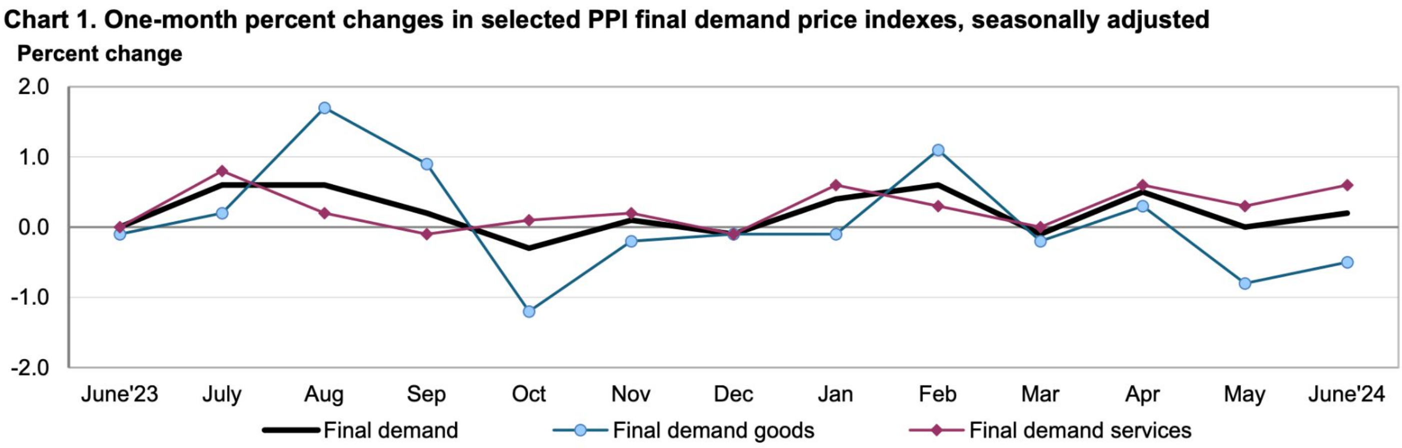

Figure 10. One-Month Percent Changes in Producer Price Index (PPI)

In June, US producer prices rose modestly, mainly driven by rising service costs. Producer Price Index (PPI) data for final demand rose by 0.2 percent in June, following stagnant growth in May. The latest PPI figures surpassed the consensus forecast of a 0.1 percent rise.

The Producer Price Index measures the selling prices 'received' by domestic producers for their output over time. PPI was up 2.6 percent for the 12 months ending in June, marking the highest year-on-year gain since March 2023 and slightly above the 2.4 percent increase observed in May. A notable 0.6 percent rise in service prices was a significant contributor to this increase, with trade service margins experiencing a 1.9 percent surge.

Excluding volatile components such as food and energy, goods prices remained unchanged after a 0.2 percent rise in May. The core PPI, which excludes food, energy, and trade services, also held steady in June—the lowest reading since May 2023—following a 0.2 percent gain in the previous month. On an annual basis, the core PPI rose by 3.1 percent, down from 3.3 percent in May.

It is important to note that the PPI report does not account for shelter costs, which was a key factor in the June Consumer Price Index report.

The rise in PPI might appear to be a source of concern for the US economy, however, the components responsible for the increase are historically volatile. We note in particular, the notable rise in final demand services, particularly trade services margins, which jumped by 1.9 percent from May, and was the largest monthly increase since March 2022. The increase is widespread among wholesalers and retailers of fuel, autos and other goods. Services can be influenced by a wide range of factors, such as seasonal demand, changes in consumer preferences, and fluctuations in economic conditions. This data tends to be volatile and frequently revised.

June Sees Uptick in Small Business Optimism Amidst Lingering Challenges

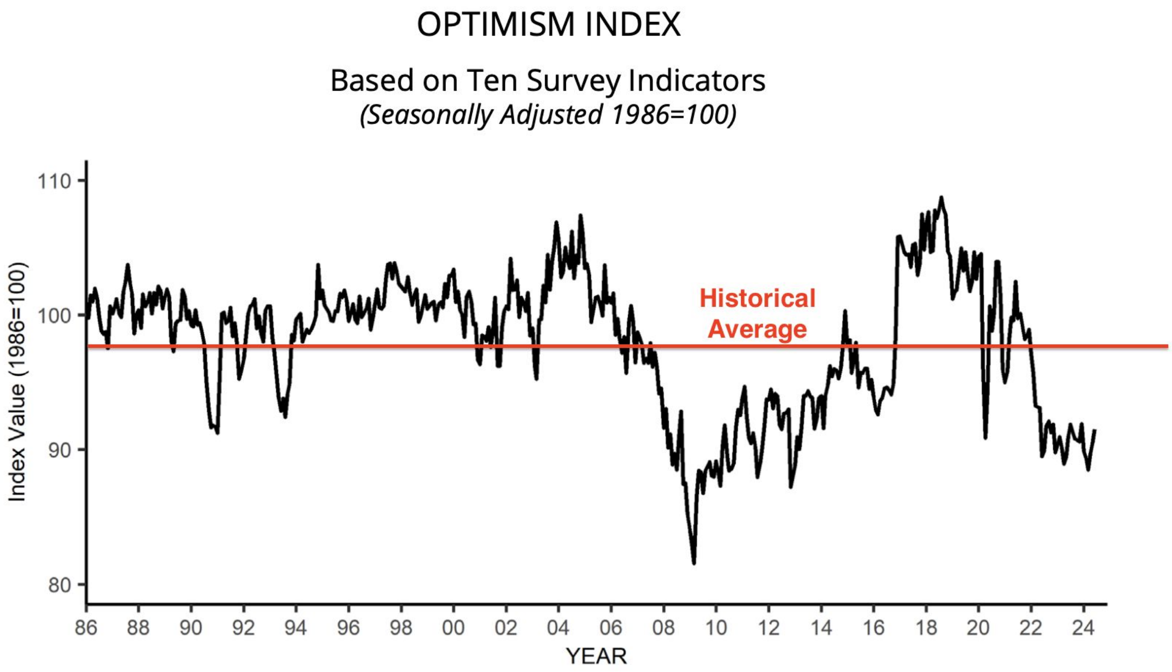

Figure 11. Small Business Optimism Index
(Source: The National Federation of Independent Business, NFIB)

The Small Business Optimism Index climbed to 91.5 in June, the highest reading of the year and a one-point increase from May. It is the most optimistic the index has been since December 2023, when it reached 91.9.

However, it still falls short of the historical average of 98, marking the 30th consecutive month below this benchmark. Inflation remains the predominant concern for small businesses, with 21 percent of owners identifying it as their most significant challenge, albeit this is a slight decrease from May.

In the monthly jobs report, 37 percent of small business owners reported having job openings they could not fill, a decrease of five points from May. Capital expenditures also declined, with 52 percent of owners reporting capital outlays in the past six months, down six points from May and the lowest since August 2022. Looking ahead, 23 percent of business owners plan capital outlays in the next six months, consistent with May's figures.

Reported sales figures were also bleak. Over the past three months, 12 percent more business owners reported a decrease in sales than those who reported an increase. Additionally, when it comes to future sales, 13 percent more owners expect sales to decline rather than increase.

The Optimism Index remains tightly bound around 90, well below the 50-year average of 98. Inflation persists as the top business concern, compounded by record-high mortgage rates affecting housing affordability. Small business owners face significant uncertainty and closely monitor economic developments and the Fed's upcoming decisions.

US Consumer Borrowing and Its Economic Implications

According to the Fed's latest consumer credit report, US consumer borrowing saw its most significant increase in three months in May, driven primarily by a surge in credit-card balances. Total credit outstanding rose by $11.4 billion in May, following a revised $6.5 billion gain in April. This increase surpassed consensus forecasts of $8.9 billion. It is important to note that these figures are not adjusted for inflation.

Revolving credit, which encompasses credit cards, increased by $7 billion, marking the largest rise in three months. Additionally, non-revolving credit, including vehicle and education loans, grew by $4.4 billion.

The data suggests that Americans are relying more on credit cards and other forms of payment to satisfy their consumption requirements, which reflects the depletion of savings accumulated during the pandemic. This dependency, combined with rising living costs, is putting further strain on household finances and indicates a potential slowdown in consumer spending. This situation may also explain the stagnation in retail sales in May and the downward revisions of previous months' data.

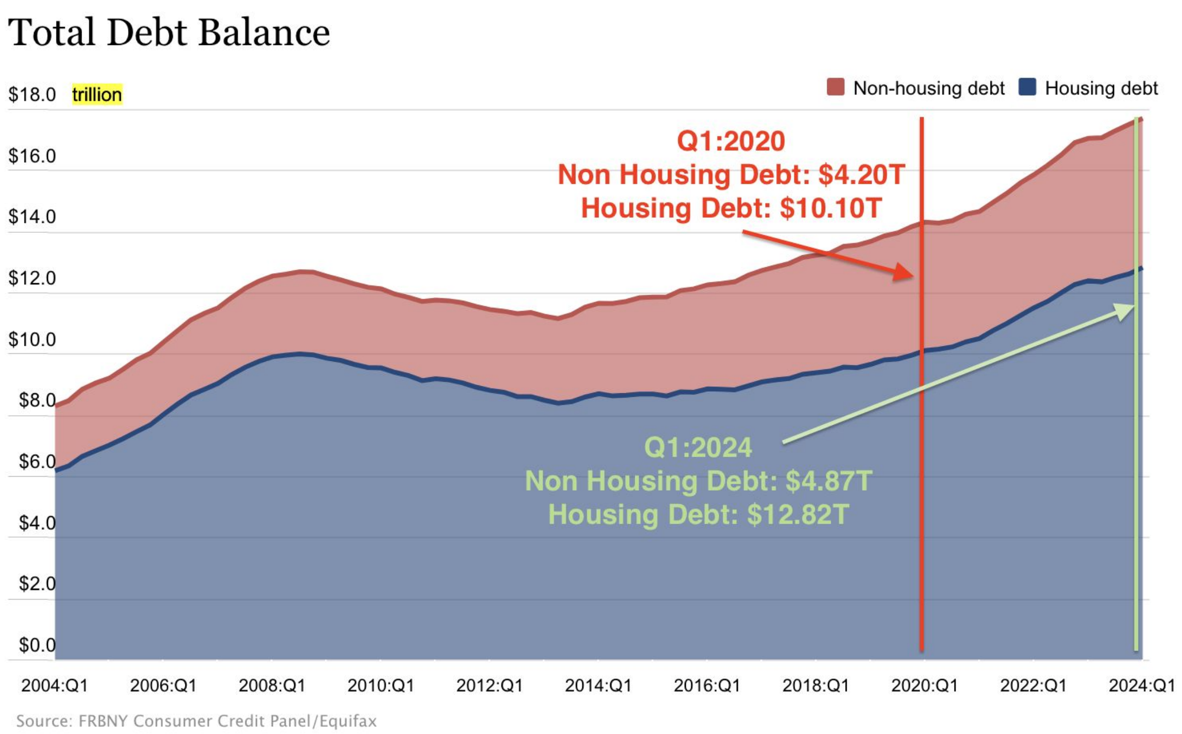

Figure 12. US Consumers Total Debt Balance (Source: Federal Reserve Bank of New York)

Since the pandemic began, consumers have added $3.4 trillion in debt, with borrowing over the past few years occurring at significantly higher interest rates. With consumer debt at record levels and much of it carrying high interest rates, maintaining high rates for an extended period could exacerbate the financial strain on households. This strain could lead to reduced consumer spending, ultimately slowing economic growth. Hence, we believe the Fed must avoid keeping rates too high for too long to prevent further financial stress on consumers and support sustained economic recovery.

NEWS FROM THE CRYPTO-SPHERE

Germany's Bitcoin Wallet Has Gone to Near Zero

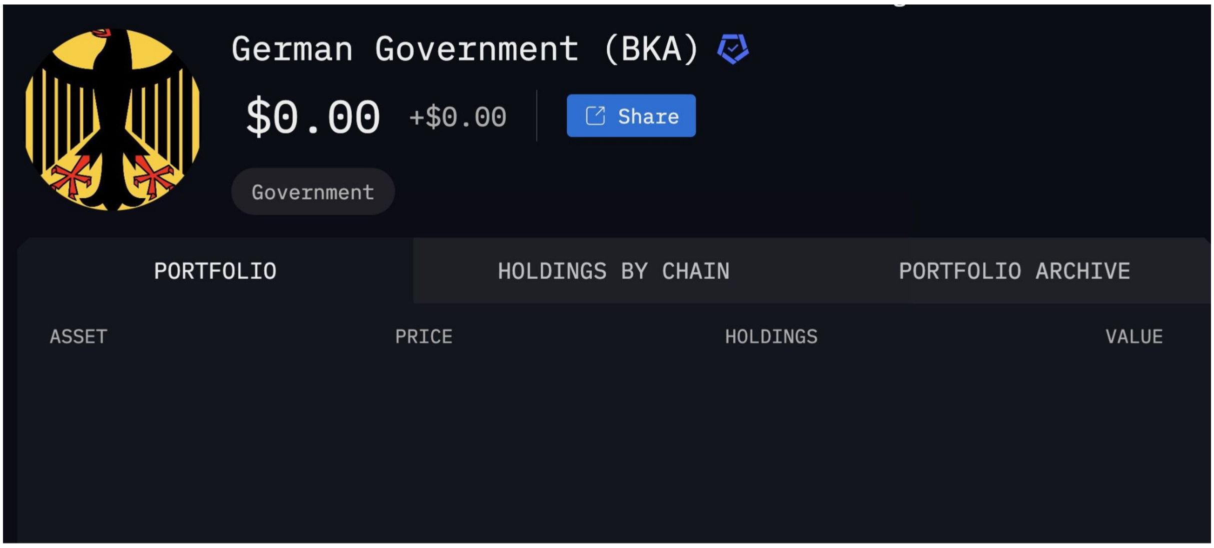

Figure 13. Germany's Bitcoin Wallet Has Gone to Near Zero

- **Germany has been liquidating seized bitcoin through staggered transfers to various exchanges and market makers**
- **The country's bitcoin wallet is now almost at zero, recording only a marginal balance of $289 as of Sunday July 14th, according to Arkham Intelligence**

Germany has been transferring thousands of bitcoins to various exchanges and market makers, indicating an effort to liquidate the cryptocurrency it seized earlier this year. This series of transactions has resulted in the country's bitcoin wallet reaching a near zero balance as of Sunday, July 14th, as reported by Arkham Intelligence.

Indeed last Friday, July 12th, the balance had hit zero after the wallet saw a transfer of 500 BTC (valued at $28.6 million) to the wallet address "bc1qu," believed to be associated with an OTC service institutional deposit. Shortly afterwards, 400 BTC (worth $22.9 million) were sent to some centralised exchanges, with another1,000 BTC (equivalent to $57.3 million) transferred to a wallet address identified by Arkham as linked to B2C2 Group.

We believe that any residual amounts transferred back to the German Government wallet is simply 'dust' from hot wallets at the various exchanges and OTC desks that have been dealing on their behalf.

These transactions are part of the German government's sell-down of 50,000 BTC it confiscated from Movie2K, a defunct film piracy website. When seized, the Bitcoins were valued at over $2 billion.

The US Securities and Exchange Commission Drops its Probe Into Hiro Systems PBC and Paxos

Figure 14. The US Securities and Exchange Commission drops its probe into Hiro Systems PBC and Paxos

- **The US Securities and Exchange Commission (SEC) has wrapped up its three-year investigation into Hiro Systems, which developed the Stacks blockchain**
- **Paxos also announced receipt of formal termination notice of SEC's investigation of BUSD**

The US Securities and Exchange Commission (SEC) has concluded its three-year investigation into Hiro Systems, a blockchain software company, which raised $70 million through token sales between 2017 and 2019. This development is the latest in terminated investigations in various crypto projects including Ripple last year, which was ended following a court ruling, and Consensys last month.

Last Friday, July 12th, the SEC's Division of Enforcement released a filing addressed to Hiro, stating, "based on the information known to the staff as of that date, the staff does not intend to recommend an enforcement action by the SEC against Hiro."

While this notice signifies a positive outcome for Hiro, it also included a standard disclaimer. The SEC cautioned that the notice should not be interpreted as an exoneration or a guarantee that no future action will be taken based on the investigation's findings.

Also last week, Paxos announced that the SEC ended its investigation after examining the stablecoin Binance USD (BUSD). Paxos announced that on July 9th, it received a "formal termination notice," indicating that the SEC would not pursue enforcement actions against the company regarding the BUSD investigation. The US Securities and Exchange Commission issued a notice to Paxos in February last year over its involvement in the Binance USD stablecoin, alleging that the stablecoin is an unregistered security.

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US House Falls Short in Attempt to Override Biden's Veto on Resolution to Overturn SAB 121

Figure 15. US House Falls Short in Attempt to Override Biden's Veto on Resolution to Overturn SAB 121

- **US lawmakers' attempt to override President Biden's veto of a measure to overturn SEC's SAB 121 fell short of the needed two-thirds majority in the House**
- **SAB 121 requires banks to list crypto holdings as liabilities, preventing them from offering digital asset custody services, a move opposed by industry groups like the Blockchain Association**

US lawmakers voted 228-184 last Thursday, July 11th, in a failed attempt to override President Joe Biden's veto of a legislative measure to overturn SEC Staff Accounting Bulletin No. 121.

SAB 121 is an SEC accounting bulletin that aims to prevent banks from offering digital asset custody services. Both the House and Senate had previously voted to rescind SAB 121, but the President vetoed their resolution, leaving the custody restriction in place. "The Administration strongly opposes passage of H.J. Res. 109, which would disrupt the Securities and Exchange Commission's work to protect investors in crypto-asset markets and to safeguard the broader financial system," the White House said in a statement of Administration policy in May. The House scheduled a vote to override the veto, which required a two-thirds majority - but failed to do so last Thursday

SAB 121, has been controversial within the crypto industry over the past year due to fears it could hinder banks from being able to custody digital assets. The bulletin mandates that firms holding crypto on behalf of customers must list these holdings as liabilities on their balance sheets.

Despite the failure to override, the fight is not over for some. US Representative Mike Flood said that he will continue to "pursue other pathways to end SAB 121 so that we can get government out of the way of growing our digital financial future". Reps. Mike Flood, R-Neb., together with Wiley Nickel, D-N.C, introduced the resolution to overturn the bulletin in February.

The Blockchain Association and the American Banking Association are also against it. Even the American Banking Association noted its a support for overturning SAB 121: "SAB 121 precludes banks from offering digital asset custody at scale, limiting bank adoption of Bitcoin ETFs and tokenization".

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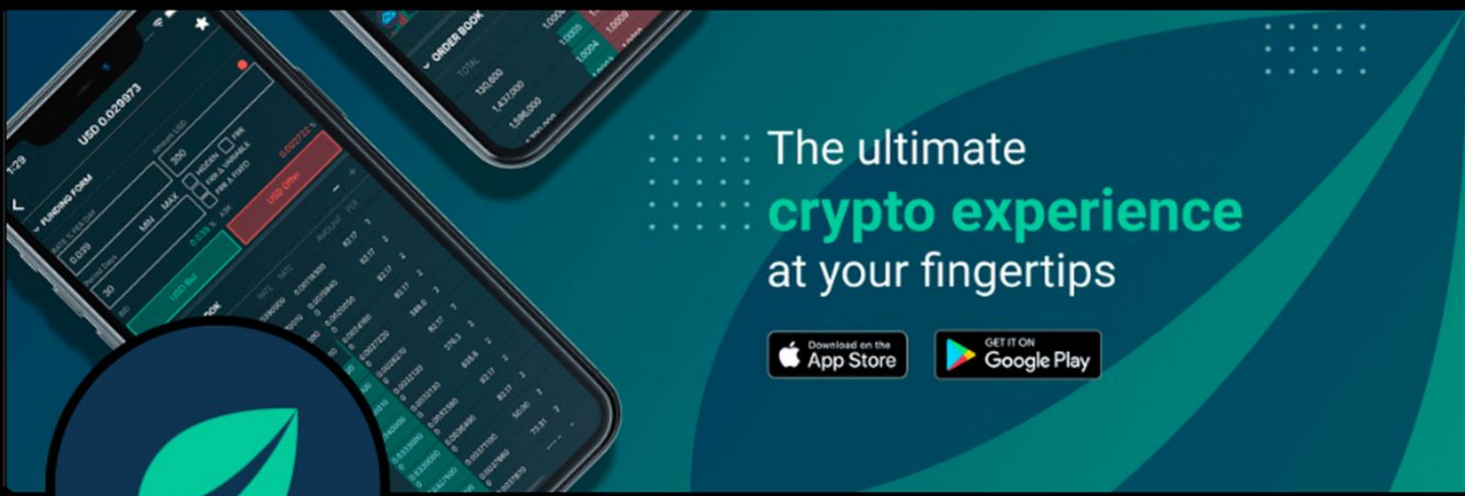
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