The Weekly Update

Week 31, 2022

luno

Provided by arcane research

1 Market Update

- Bitcoin has been stable over the past seven days, hovering between $22,500 and $24,500 and is up 2% over the past seven days.
- The market shares of bitcoin and stablecoins continue falling as traders seem more comfortable with risk exposure. Meanwhile, ETH has increased its market share as the merge is nearing.
- Share prices of bitcoin miners, crypto holding companies, and crypto exchanges have all surged in July.
- Instruments for trading the upcoming Ethereum merge and potential proof of work chain split are getting launched as trading strategies amid possible arbitrage opportunities emerge.

2 Valuation

- The technical trend for bitcoin continues, with another higher low printed last week. The resistance in the lower $24k area was once again tested yesterday. Will it break this week?
- Futures premiums in bitcoin saw a decline over the last week as bitcoin ranged but stays higher than July levels. Meanwhile, we note all-time low ETH futures prices compared to spot as delta neutral strategies ahead of the merge see growing traction.

3 Blockchain Activity

- The Bitcoin miner revenues have seen solid growth lately, but it's slowing down as the bitcoin price stabilizes and the mining difficulty increases.
- Last week, Chinese Ethereum miner Chandler Guo launched a campaign to hard fork the Ethereum blockchain at the Merge, to enable a PoW based Ethereum chain to continue after the Merge.
- Riot generated $9.5 million worth of power credits in July, significantly more than their bitcoin production this month of 318 BTC.

Source: Skew

Renewed crypto market optimism as the Ethereum merge nears

- The crypto market continues its recovery process after the dreadful start to the summer. While altcoins keep rallying, bitcoin has established a solid consolidation range in the $22,500 to $24,500 area and is up 2% over the past seven days.
- Market sentiment has improved and is at the highest level since April, as measured by the Fear and Greed Index. This renewed risk appetite has led altcoins to outperform bitcoin. BNB has increased 14% over the past seven days, while ETH is up 8%.
- Part of the market sentiment improvement might be caused by hopefulness regarding Ethereum's upcoming merge.
- With crypto prices slowly grinding upwards, volatility has been remarkably low lately. Wednesday's release of the July CPI numbers might be a catalyst for increased volatility.
- The crypto rally started with the larger coins around two weeks ago, but now traders have moved to smaller ones. Of the top 50 coins by market cap, Flow is the best performer with a 47% gain, followed by NEAR, which increased by 24%.

Last week of top 50 by market capitalization

Best Performing	Price	Last week	Last month	YTD
Flow	2.99	46.8%	76.1%	-64%
NEAR Protocol	5.34	24.4%	40.1%	-66%
Quant	126.16	21.3%	47.5%	-30%

Worst Performing	Price	Last week	Last month	YTD
LEO Token	4.79	-7.7%	-16.3%	-27%
Filecoin	8.64	-1.4%	48.8%	-74%
Internet Computer	8.24	-1.3%	17.5%	-73%

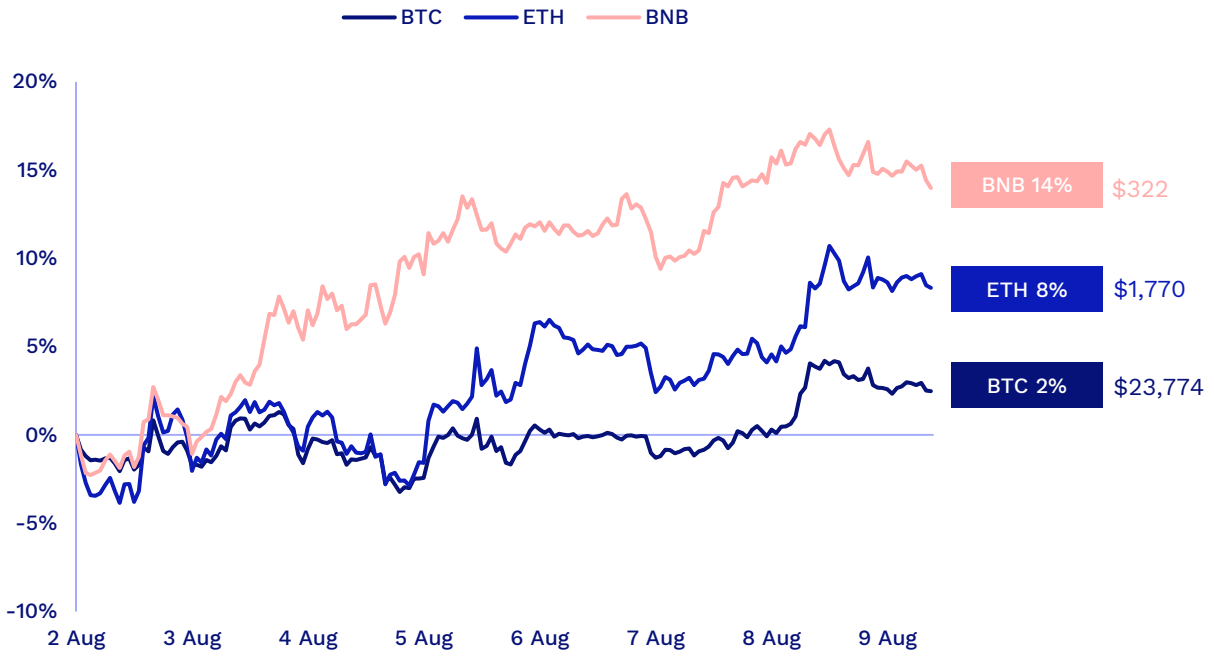
Source: CoinGecko, messari.io

Bitcoin Correlation:

90-day correlation (weekly change included)	ETH		GOLD		S&P500	
BTC	0.893	-0.003	0.218	-0.071	0.645	-0.005

Source: CoinMetrics

Top 3 by Market Cap: Percentage Change in Price Over the Last Week



Source: Tradingview (Coinbase, Binance US)

Traders rotating from bitcoin and stablecoins to altcoins

The market shares of bitcoin and stablecoins continue falling as traders seem more comfortable with risk exposure.

- All indexes have seen positive returns in August, with the Small Cap Index leading the pack with a 9% increase. Mid Caps (+7%) and Large Caps (+5%) follow closely behind, while bitcoin (+2%) has seen the least gains.
- With bitcoin underperforming relative to altcoins, the bitcoin dominance has plummeted from a peak of 47% in the middle of June to 40.5% now. As the market sentiment has improved (next slide), traders have been more interested in getting exposure to altcoins than bitcoin.
- Most notably, we see ETH increasing its market share by 0.89 percentage points over the past seven days, while BTC's market share is down 0.96 percentage points.
- As the market has gotten hungrier for risk, we also see the market shares of stablecoins plummeting. Since the middle of June, USDT's market share has fallen from 8.1% to 5.9%.

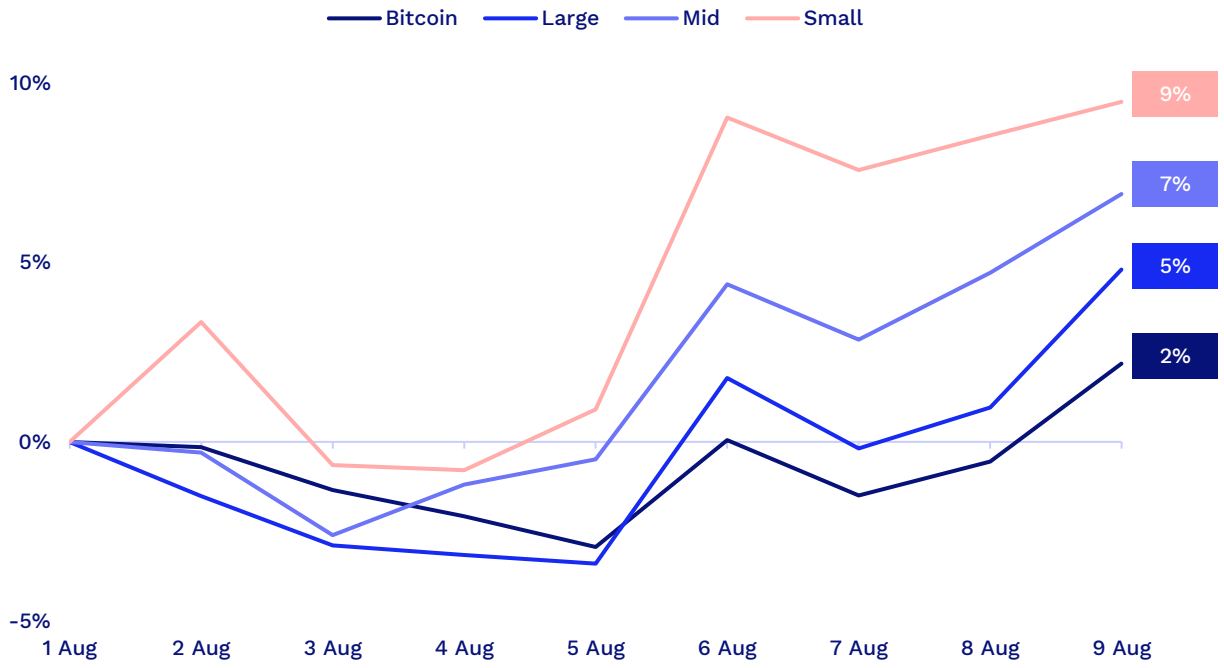
Percentage of Total Market Capitalization

	BTC	ETH	USDT	USDC	BNB	XRP	ADA	BUSD	SOL	DOT
Market Share	40.52%	19.20%	5.92%	4.83%	4.62%	1.62%	1.61%	1.59%	1.31%	0.89%
Weekly Change	-0.96%	0.89%	-0.40%	-0.37%	0.36%	-0.09%	0.03%	-0.12%	-0.02%	0.16%

* Weekly change in percentage points

Source: CoinMarketCap

Monthly Performance of Market Cap-Weighted Indexes

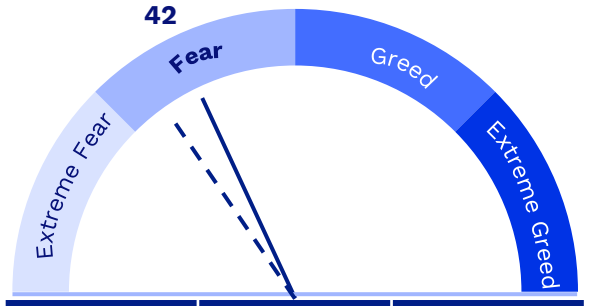


Source: Bletchley Indexes, Tradingview (Coinbase)

Market participants don’t want to declare a bull market yet

The Fear and Greed Index sits at 42 – the highest since April. The market sentiment has been steadily improving since the bottom in the middle of June. Even after this market sentiment improvement, the Fear and Greed Index still hasn't climbed out of the fearful territory. In addition, the slow growth of the index indicates an inherent fear among market participants that the crypto market's recent rebound could be short-lived.

Source: Alternative.me

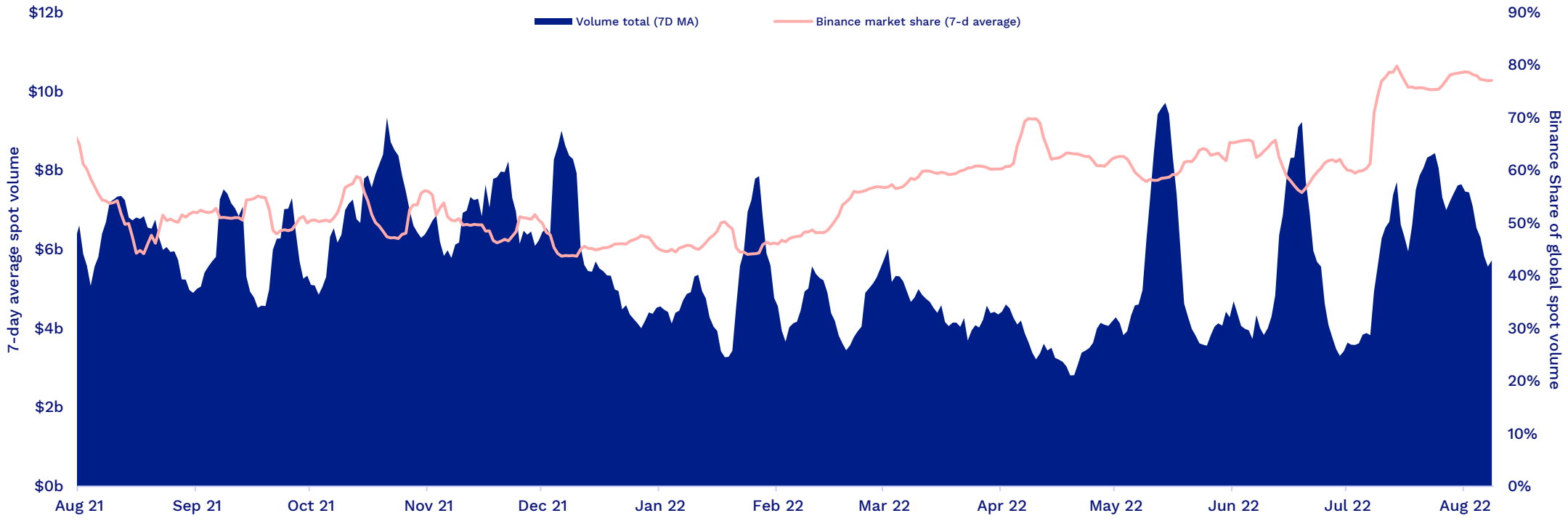


Now	Last week	Last month
Fear (42)	Fear (31)	Extreme Fear (22)

Bitcoin's spot volumes are declining after the July surge

The bitcoin spot volume is on the way down after reaching close to one-year highs in July. Binance is still the venue for almost 80% of spot trading activity, as the exchange behemoth's fee removal for several BTC pairs one month ago successfully helped it eat up even more of the bitcoin spot market. Trading activity remains muted across all other venues.

Real BTC Daily Volume* (7-day average)

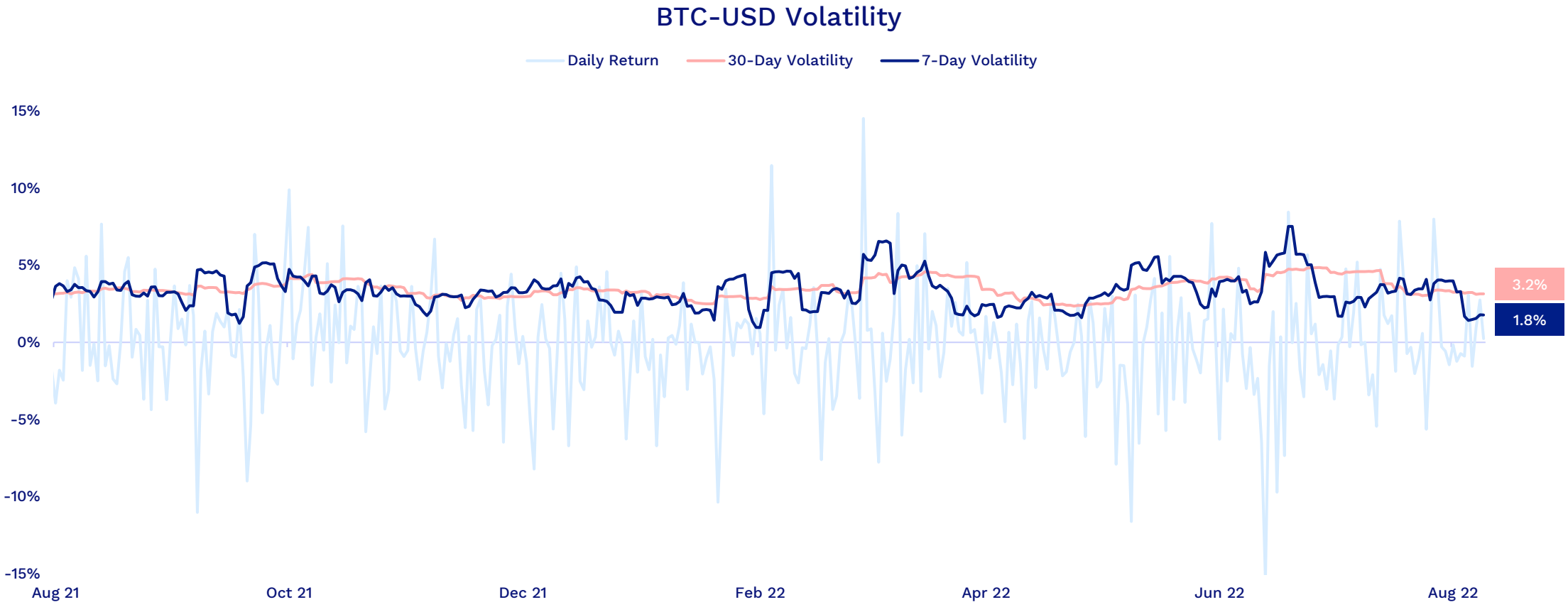


Source: Skew, Tradingview (Binance, Binance US, Bitfinex)

*Includes Bitwise 10 exchanges, LMAX, FTX

Bitcoin's 7-day volatility falling towards a yearly low

Bitcoin has been remarkably stable over the past seven days, hovering between $22,500 and $24,000. This price stability has caused bitcoin's 7-day volatility to fall to 1.8% - among the lowest in one year. Over the past seven days, there have been no fundamental catalysts for price movements. Could Wednesday's release of the July CPI be the catalyst for higher volatility?

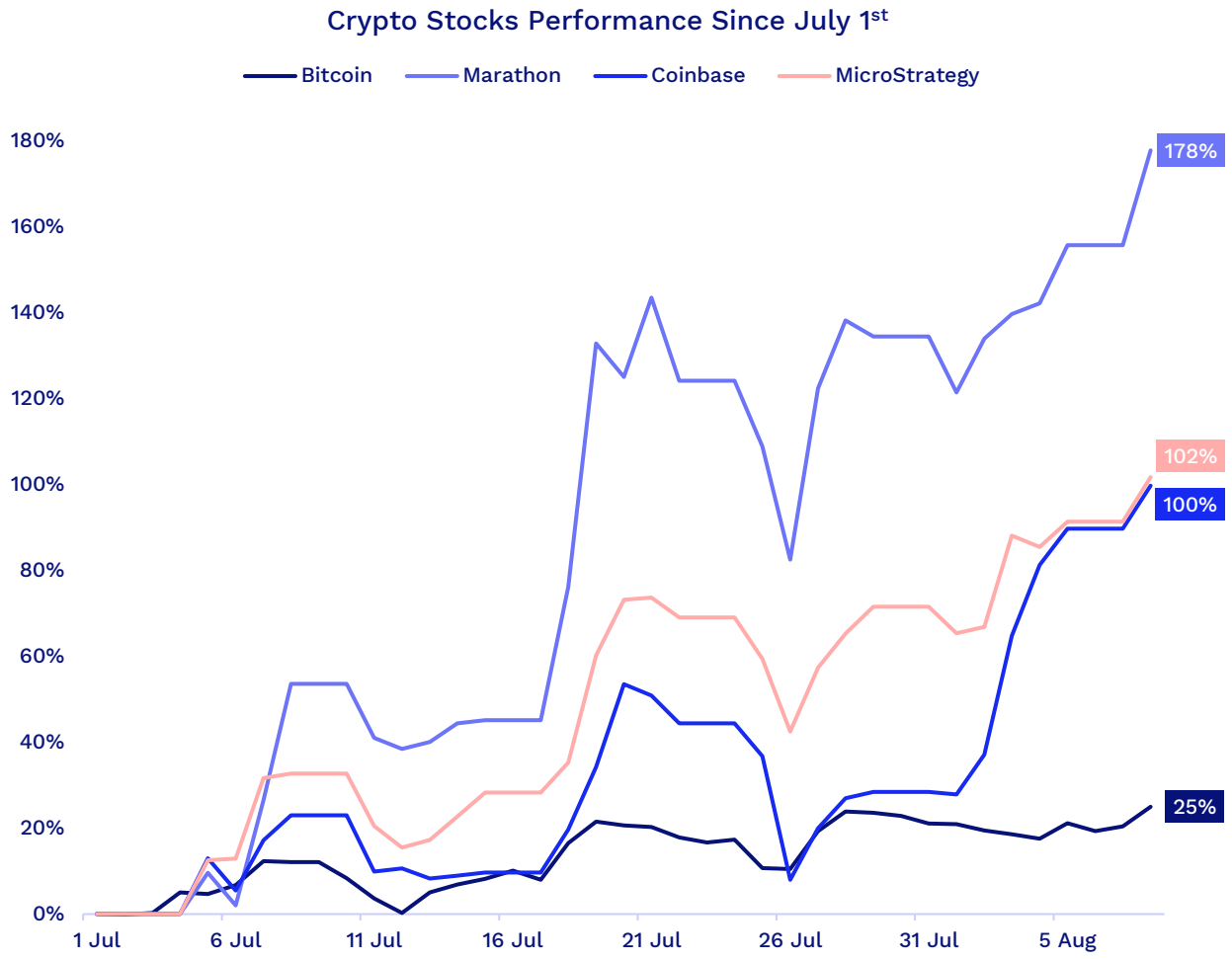


Source: Tradingview (Coinbase)

The bitcoin rebound fuels a crypto stock surge

Share prices of bitcoin miners, crypto holding companies, and crypto exchanges have all surged in July.

- There are several crypto stocks from various sectors in the crypto ecosystem, such as bitcoin miners, crypto holding companies, and crypto exchanges.
- Crypto stocks have tended to follow the bitcoin price, albeit with a higher beta, meaning that they amplify bitcoin's price movements both to the upside and the downside. Looking at the chart, we can see how correlated these stocks are, resulting from their high correlation to the bitcoin price.
- As the bitcoin price has declined by 49% in 2022, crypto stocks have naturally also seen a poor first half of the year. Bitcoin holder MicroStrategy is down 38%, bitcoin miner Marathon has fallen 55%, while crypto exchange Coinbase has seen 60% of its share price shaved off in 2022.
- Still, these stocks would have been down much more if not for their strong rebound during the last month, fueled by bitcoin's recent solid performance. Since July 1st, Marathon has soared 178%, MicroStrategy 102%, and Coinbase 100%. Nothing fundamentally changed at Marathon or MicroStrategy that should have caused these price increases, but they are both heavily affected by the bitcoin price. A large share of Coinbase's returns came on August 4th when the crypto exchange announced that Blackrock – the world's largest asset manager- will let institutional clients trade crypto through a Coinbase integration.
- Crypto stocks offer risk-tolerant investors the opportunity to take a levered bet on the crypto ecosystem. Knowing these stocks will only keep performing well if the crypto market keeps recovering is essential.



Source: Tradingview

New trading strategies emerges as Ethereum approaches merge

Instruments for trading the upcoming Ethereum merge and potential proof of work chain split are getting launched as trading strategies amid possible arbitrage opportunities emerge.

- In a series of threads, Galois Capital has made a case for trading a potential chain split in Ethereum following the Ethereum merge, and now a movement initiated by a large Ether miner for ETHW (Ethereum PoW) has gained traction.

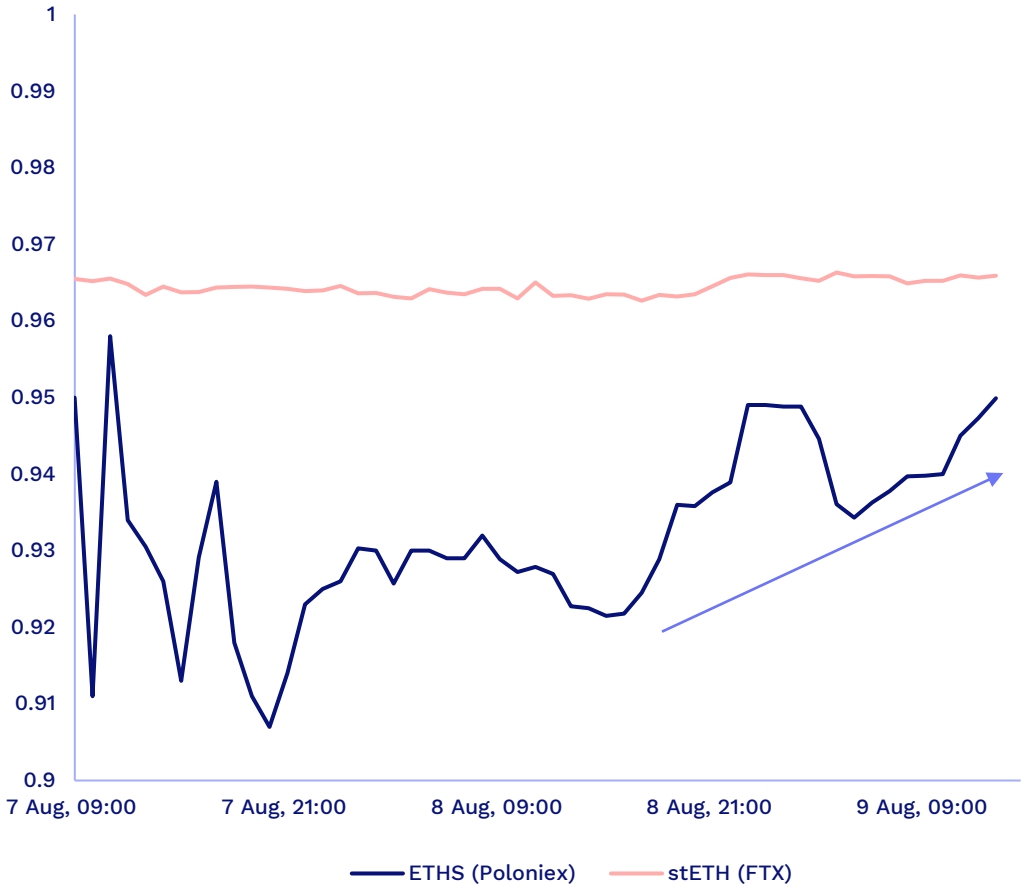
- Galois is trading the merge, and a potential chain split through a delta neutral strategy, holding spot and shorting quarterly futures at equal size. Since announcing its trade, a discount to the spot market has emerged in quarterly ETH futures. This trade enables exposure to a potential chain split and is based on the assumption that ETHPOW will accrue a share of the current value of ETH.

- Both Poloniex and BitMEX have launched instruments to trade ETHPOW, with Poloniex launching an instrument for trading PoS ETH (ETHS) simultaneous to launching the ETHW alternative. ETHW at Poloniex currently trades at 0.06 ETH while ETHS trade at a substantial discount to stETH, albeit at low volumes. Nevertheless, a well of arbitrage opportunities seems to be erupting for traders as the situation develops.

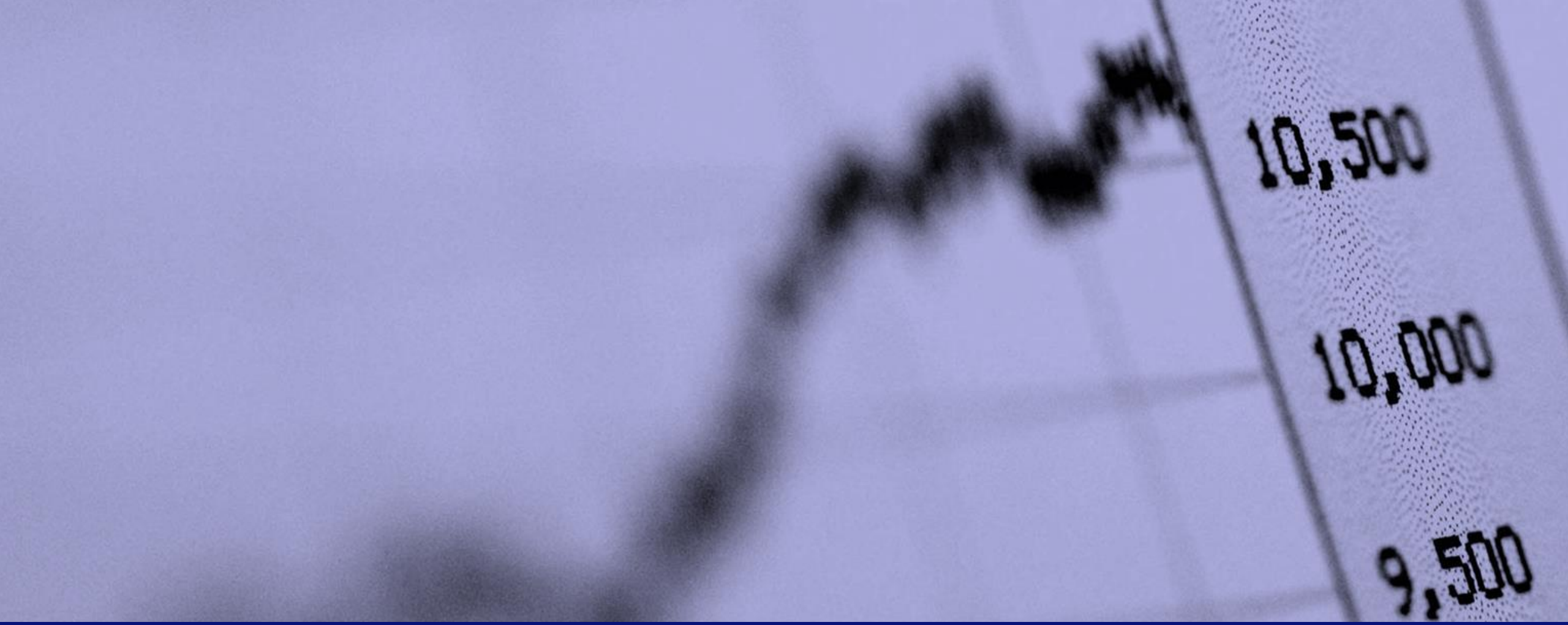
- A ETHPOW alternative following a potential chain split will meet several challenges, in particular related to Ethereum's "Ice Age Difficulty Bomb", which will slow down the block discovery rate by increasing the complexity of PoW calculations. The potential ETHW split will likely have to hard fork its client and permanently remove the ice age feature to be viable in the long run.

- The case in favor of ETHPOW versus the already established Ethereum proof of work alternative Ethereum Classic, a fork that occurred following Ethereum's infamous DAO hack in 2016, is that ETHPOW will launch with more infrastructure and contracts on chain than ETC. Nevertheless, ETHPOW will likely suffer from lacking support from stablecoin issuers such as Circle and Tether, in addition to WBTC. This could create a dicey environment in the ETHPOW DeFi ecosystem in the event of a launch. BitMEX Research has proposed a different strategy to take advantage of a potential split based on stablecoin exposure featuring a more complex execution.

Aug 7th-9th: stETH/ETH (FTX) vs ETHS (Poloniex)



Source: Tradingview (Poloniex, FTX)



Valuation

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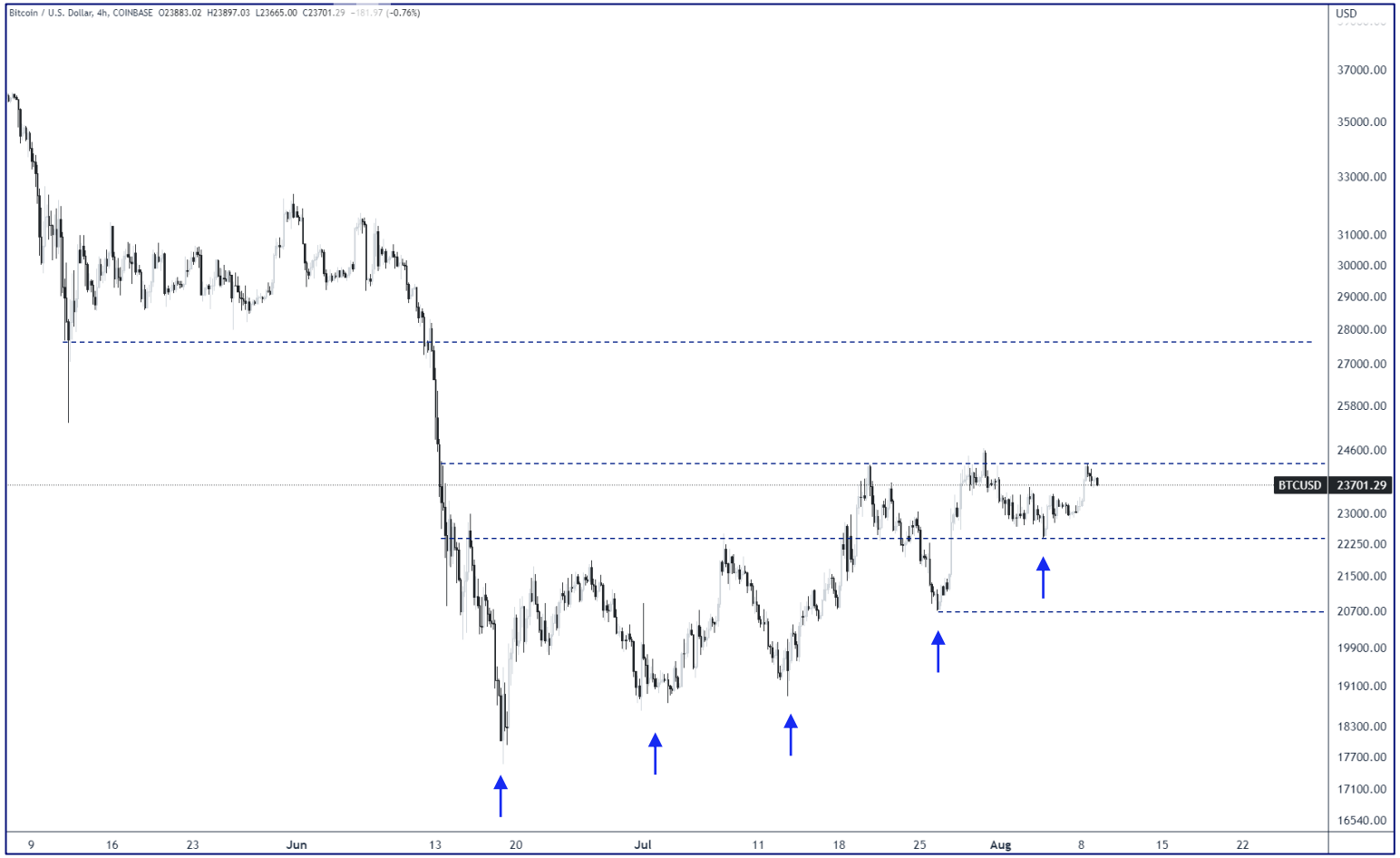
Another higher low for bitcoin last week

The technical trend for bitcoin continues, with another higher low printed last week. The resistance in the lower $24k area was once again tested yesterday. Will it break this week?

- Bitcoin's steady climb continues. The price bottomed at ~$22,400, which marked another higher low and the bullish technical trend for bitcoin continues.
- As suggested last week, this July resistance level could now have been flipped to support.
- The resistance in the lower $24k area still holds and was tested for the third time yesterday.
- A tight range between ~$22.5k-$24k could now have been established. The direction out of this range will be telling for the short-term outlook for bitcoin.
- As mentioned last week, a break up above the $24k resistance level could see us move towards the $27k-$28k level.

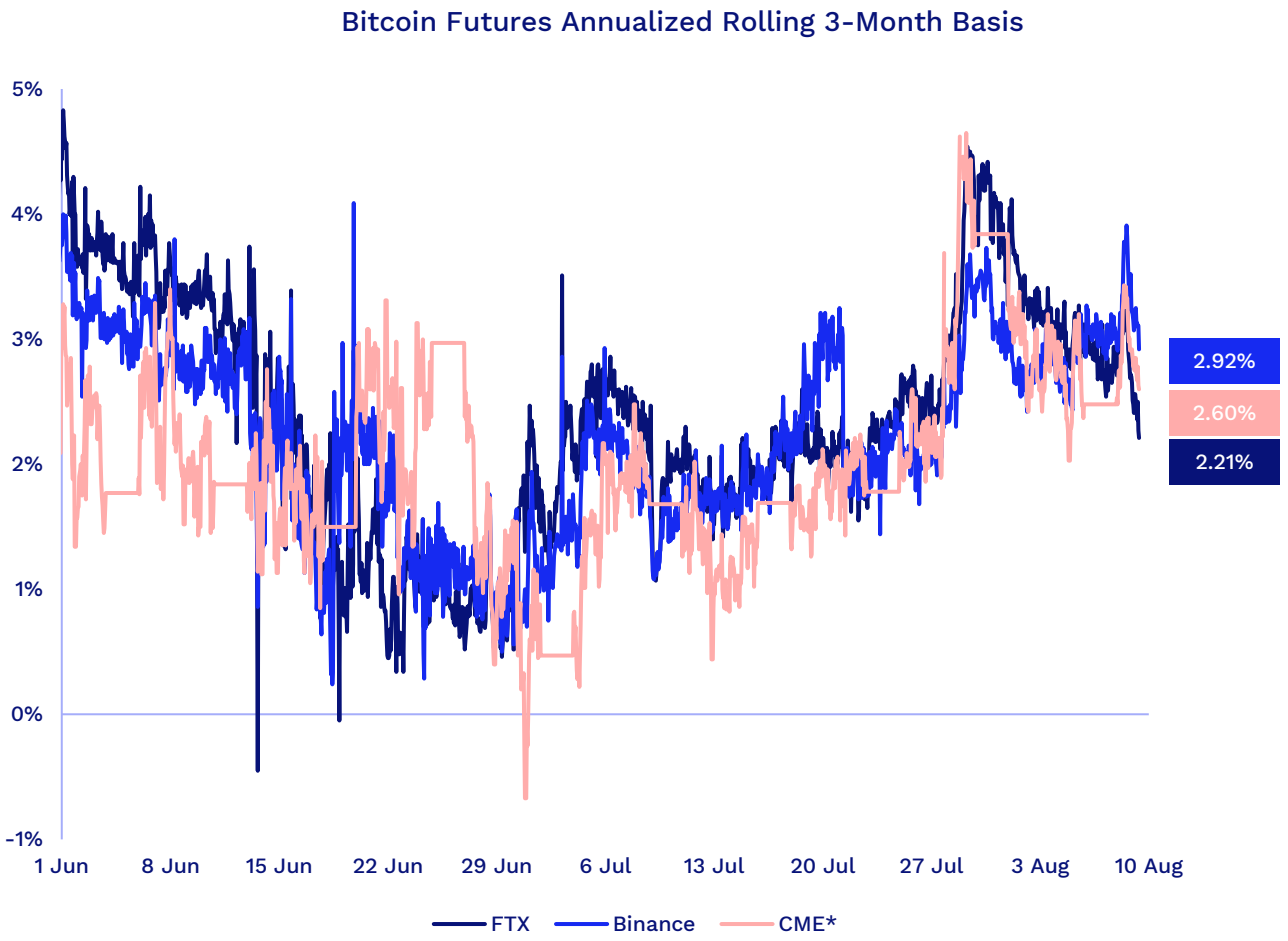


Source: Tradingview (Coinbase)

Futures premiums declines but remains higher than July levels

Futures premiums saw a decline over the last week as bitcoin ranged but stays higher than July levels.

- The futures premiums have declined below 3% in the bitcoin futures market after touching 2-month highs last week of 5%.
- Still, the current 3-month basis remains higher than what we've seen since contagion created havoc in the market in June.
- There are no noteworthy deviations in the premiums of offshore exchanges and CME. While FTX saw the highest premiums last week, FTX futures have since flipped to trade below the rest of the market.
- CME's relatively high basis might be helped by outflows from the short bitcoin ETF BITI. BITI's short exposure currently sits at a BTC equivalent of 2490 BTC, the lowest BITI exposure since June 28th, suggesting an improving sentiment overall in the market.
- The current decline in futures premiums might be caused by more conservative positioning ahead of Wednesday's U.S. CPI release, which might impact the overall risk sentiment in the coming month.
- While Bitcoin futures trade above the mid-June to late July levels, Ethereum futures currently trade at an all-time high discount.



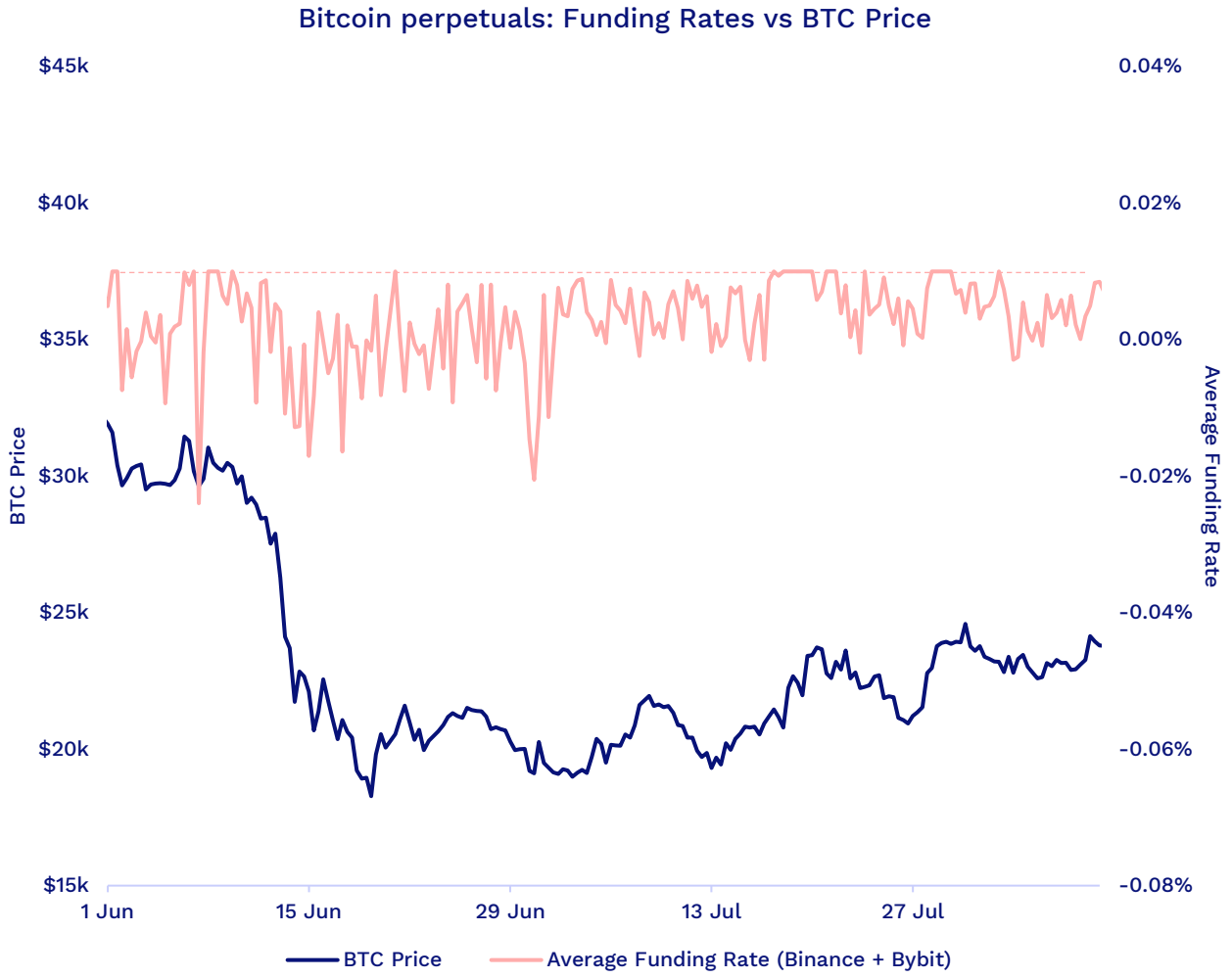
Source: Skew

*Closed Saturday - Sunday

Funding rates still tumbling below neutral levels

Funding rates still struggle to reach neutral levels as perps continue to trade at slight discounts to the spot market.

- Funding rates have trailed below neutral territory as BTC has spent most of the week ranging between $23,000-$24,000.
- We noted neutral funding rates amid BTC's push last week, but following a rather uneventful week in BTC, perps have again resumed trailing below the spot market.
- It's now more than 8 months since Binance and Bybit saw funding rates above the neutral level.
- As perps continue to see funding rates below neutral levels, open interest has seen further growth. Mid-day Monday saw BTC denominated open interest in perps push towards yet another all-time high of 369,000 BTC driven by a sharp growth on Binance.



Source: Skew, Bybit

Ether futures prices at all-time lows relative to Ether spot

While bitcoin futures trade at a premium to the spot market, Ether futures have started trading at all-time lows relative to the spot market, likely caused by the upcoming merge and a potential chain split on the horizon.

- Ether futures are trading at all-time lows relative to the spot market. Binance saw a massive 5% discount on average on Monday, a clear all-time low for the Binance ETH futures.
- The Ether futures discount is far from isolated to Binance. FTX's discount is also at an all-time low, pushing below the discounts seen in the aftermath of the stETH crash following Celsius and 3AC's implosions.
- CME is trading at a more conservative discount but also sees its futures trading below spot for the first time since its launch in February 2021.
- Overall, Ether futures have traded at low premiums throughout the summer, but nowhere near the current low levels. The discounts are accompanied by a rise in open interest, currently sitting near all-time highs (next slide).
- The discounts are likely a result of trading strategies ahead of the long-awaited Ethereum transition to PoS. The market is bracing for the possibility of a hard fork leading to the birth of a PoS ETH alternative and a PoW ETH alternative. In slide 10, we explain the Galois trade, shorting quarterlies, and longing spot through delta neutral exposure. This is likely the key catalyst behind the futures discount.
- Interestingly, we saw similar dynamics unfold back in August 2017 ahead of the Bitcoin Cash fork, with BTC futures trading at an annualized basis of -9% on Okcoin. As the fork occurred, the basis again normalized. Similar effects might come into fruition as we approach the Ethereum merge.

Ether futures: 3mth annualized basis (24h MA)

Source: Skew

Open interest in Ethereum near all-time highs in notional terms

Open interest in notional terms in Ether futures and perps nears new all-time highs as the Ethereum futures basis decline to all-time lows.

- The ETH denominated open interest in ETH futures and perps has climbed to near 4.2m ETH.
- This is the second highest ETH denominated open interest recorded ever, only beaten by the 4.21m highs of July 14th this year. The open interest peak in July was caused by massive hedging, likely motivated by the promising arbitrage opportunity related to Celsius' bankruptcy and corresponding large holdings of stETH trading at a large discount to ETH.
- The current peak, however, is likely caused by the delta neutral trading strategy explained in the previous slide and slide 9.
- While ballooning open interest amid extreme discounts in futures may foreshadow a short squeeze, a majority of the recent surge in leverage is likely caused by more conservative risk management, affiliated with low leverage and delta-neutral exposure. Thus, the likelihood of a sizeable short squeeze in ETH is less potent in the current market climate.

Ether Futures and Perps: Ether denominated open interest

Source: Skew

Blockchain Activity

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Stagnating growth in bitcoin miner revenues

The Bitcoin miner revenues have seen solid growth lately, but it's slowing down as the bitcoin price stabilizes and the mining difficulty increases.

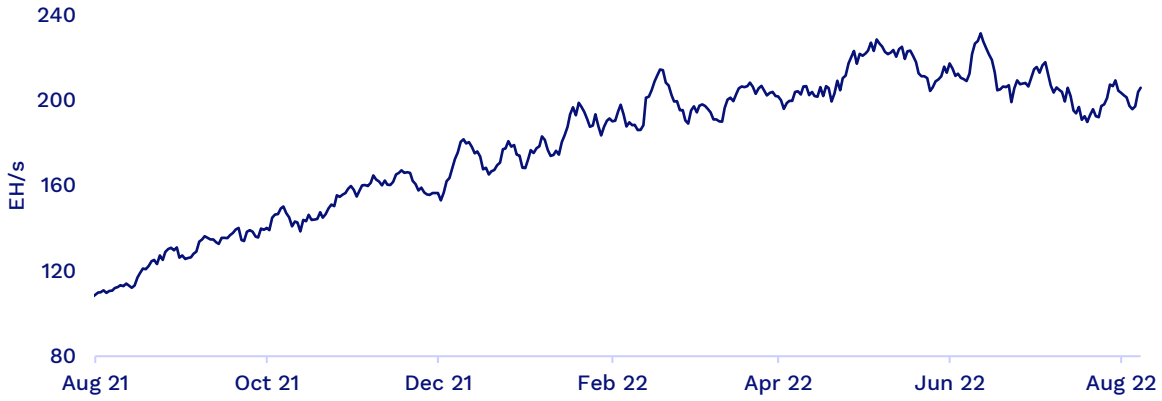
- Daily miner revenues increased from a bottom of only $17 million on July 17th to $21.8 million on July 29th. Since then, the growth has slowed, and daily miner revenues over the past seven days were only marginally higher at $21.9 million.
- The recent bitcoin price stabilization mainly caused the slowing growth in daily miner revenues, but the increasing mining difficulty also had a small impact.
- The Bitcoin network increased its mining difficulty by 1.7% last Thursday. This was the first upwards difficulty adjustment since June 8th, following three consecutive downwards adjustments.
- The difficulty is increasing as the hashrate is coming back online. In July, the hashrate fell to its lowest level since March as the bitcoin price decrease squeezed out some of the miners with the highest bitcoin production cost.
- The low July hashrate was also, to a minor degree, caused by American miners powering down their machines in response to surging electricity demand following a heatwave.
- Other than that, we see no significant changes in on-chain activity, except for a larger drop in average transaction value. The number of daily active addresses has slightly increased from the bottom in June and is now at 900k.

Powered by: BYTETREE

	Bitcoin Network Data				
		8/8/2022	7d prior	7d Change	30d Trend
Network	Daily Miner Revenues	$ 21,893,359	$ 21,552,018	1.58%	
	Fees per day	$ 355,579	$ 317,246	12.08%	
	Fees % Revenues	1.62%	1.47%	0.15%	
	Daily TX Volume ($M)	$ 3,287	$ 3,883	-15.34%	
	Transactions per day	254,717	254,429	0.11%	
Utility	Avg TX value $	$ 12,905	$ 15,260	-15.43%	
	# Blocks per hour	6.21	6.13	1.46%	
	Avg. # TX per block	1,708	1,706	0.11%	

Source: Bytetree

Bitcoin Hashrate (7-day average)

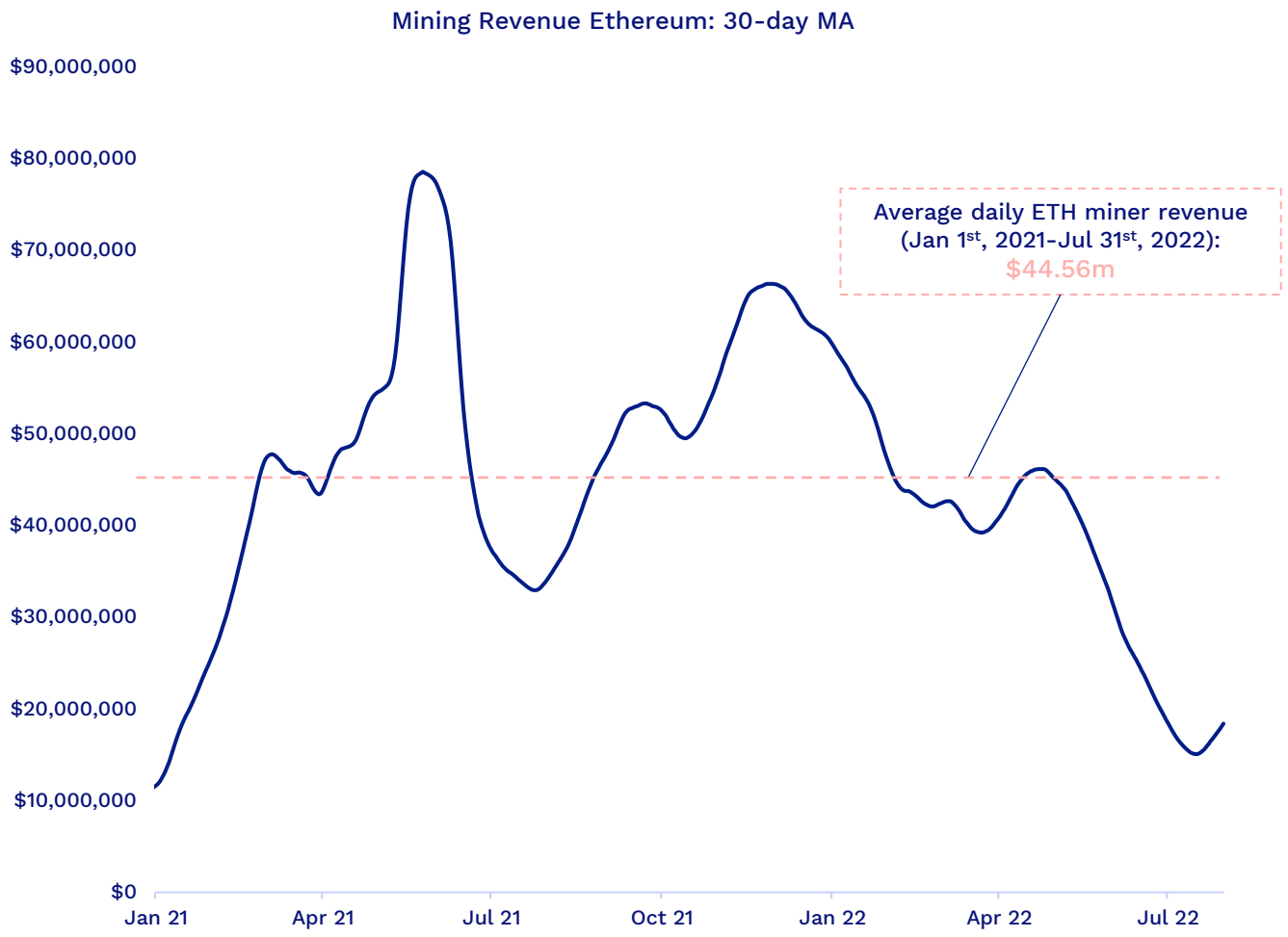


Source: Blockchain.com

ETHPoW and ETH2: The story of miners vs. social consensus

Last week we gave a brief on the Merge: the switch from Proof-of-work (PoW) to Proof-of-stake (PoS) consensus on the Ethereum blockchain. However, not everyone welcomes the switch, and ETHPoW—representing the token for the PoW chain that might continue to exist— is getting increasing attention.

- Last week, Chinese Ethereum miner Chandler Guo launched a campaign to hard fork the Ethereum blockchain. In the beginning, both chains would be identical, duplicating any holdings. However, although the network can be technically duplicated, the value cannot.
- There will be 2 USDC/USDT for 1 USD held by Circle/Tether. Stablecoin issuers will have to choose which chain stores the actual value, so in theory, they could decide which chain becomes the new Ethereum. However, doing anything against social consensus would be bad for business, and the Ethereum community has decided to switch to PoS.
- If stablecoins are worthless on the PoW chain, DeFi on PoW crumbles. But some exchanges will list ETHPoW, causing speculation on the asset and a race to extract as much ETHPoW from the dead ecosystem as possible. TL;DR: the trade is already becoming crowded.
- There is no community behind ETHPoW, and interestingly, the list of ETHPoW supporters consists of either mining pools or exchanges. Ethereum mining is bigger than bitcoin mining based on revenue (see chart), so miners clearly have financial incentives to support an ETHPoW chain.
- However, no dApps or infrastructure providers have publicly supported the fork. And if everyone plans to sell ETHPoW after the Merge, it is yet to be known where the bids will come from.

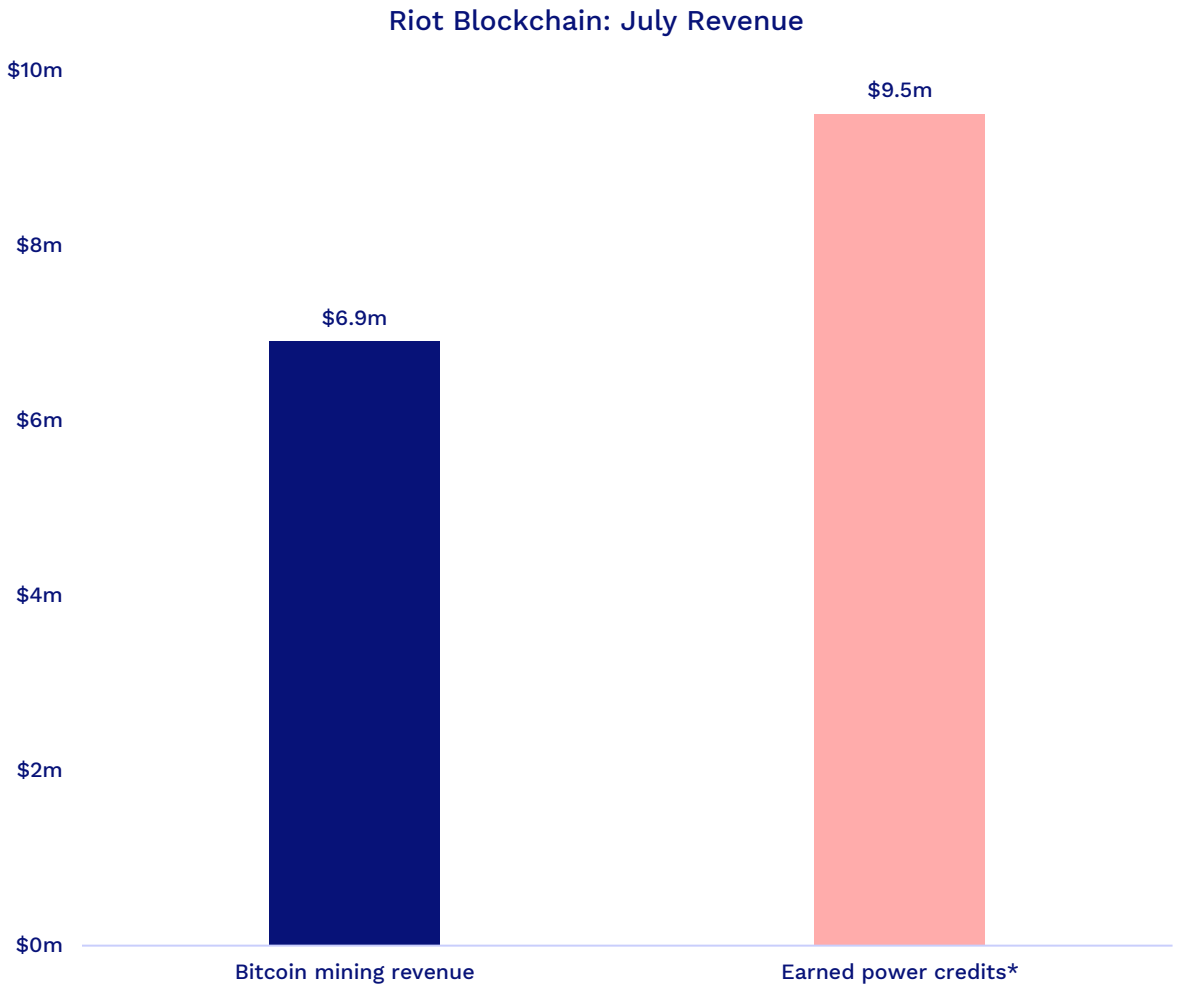


Source: Coinmetrics

Bitcoin miners are paid to strengthen the electricity grid

Texas' electricity demand soared to critical levels in July as a heatwave hit the state, and the grid operator paid flexible consumers to reduce their electricity usage. One of these was bitcoin miner Riot, earning $9.5 million by turning off its machines.

- Riot generated $9.5 million worth of power credits in July, significantly more than their bitcoin production this month of 318 BTC, worth $6.9 million at the average July BTC price of $21,634.
- Riot has a complex power strategy that lets them take advantage of the unique interruptibility of bitcoin mining as an electricity-consuming process. By adjusting its facility's electricity consumption based on grid conditions, Riot strengthens Texas' electric grid and is paid handsomely for providing these energy services.
- To earn these power credits, Riot curtailed 8,468 MWh in July. That means that they earned $1,122 per MWh of energy curtailed. If they had directed this energy to mining bitcoin instead, they would have earned only about $140 per MWh, making them heavily financially incentivized to curtail production.
- These power credits and other demand response payouts give Riot an industry-leading estimated electricity price of $29 per MWh. Other industrial electricity consumers can't achieve such low electricity rates, proving bitcoin miners' unmatched value to the grid.
- Why do bitcoin miners have the opportunity to provide these demand response services to the grid? Bitcoin mining is an energy-intensive and stable load that can be rapidly adjusted up or down with extreme precision at no extra cost. These factors make it the most flexible electricity-consuming process that exists.



Source: Riot Blockchain (July production update)

*Unaudited, estimated and pro-forma

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