

# The Weekly Update

Week 36, 2022



Provided by **arcane**  
research

1

## Market Update

- Bitcoin has seen a strong recovery of 8% over the last seven days, outperforming the rest of the crypto market and regaining some of its market dominance as we approach the long-awaited Ethereum merge.
- As the Ethereum merge approaches, the proof of work-based Ethereum hard fork seems to be losing interest while Ethereum Classic maintains its strength.
- ETF traders are unwinding short exposure in BTC ETFs, eyeing potential upside, leading CME basis to recover.
- MicroStrategy's everlasting quest to grow its BTC treasuries continues as the company seeks to issue class A stocks to purchase \$500m worth of BTC.

2

## Valuation

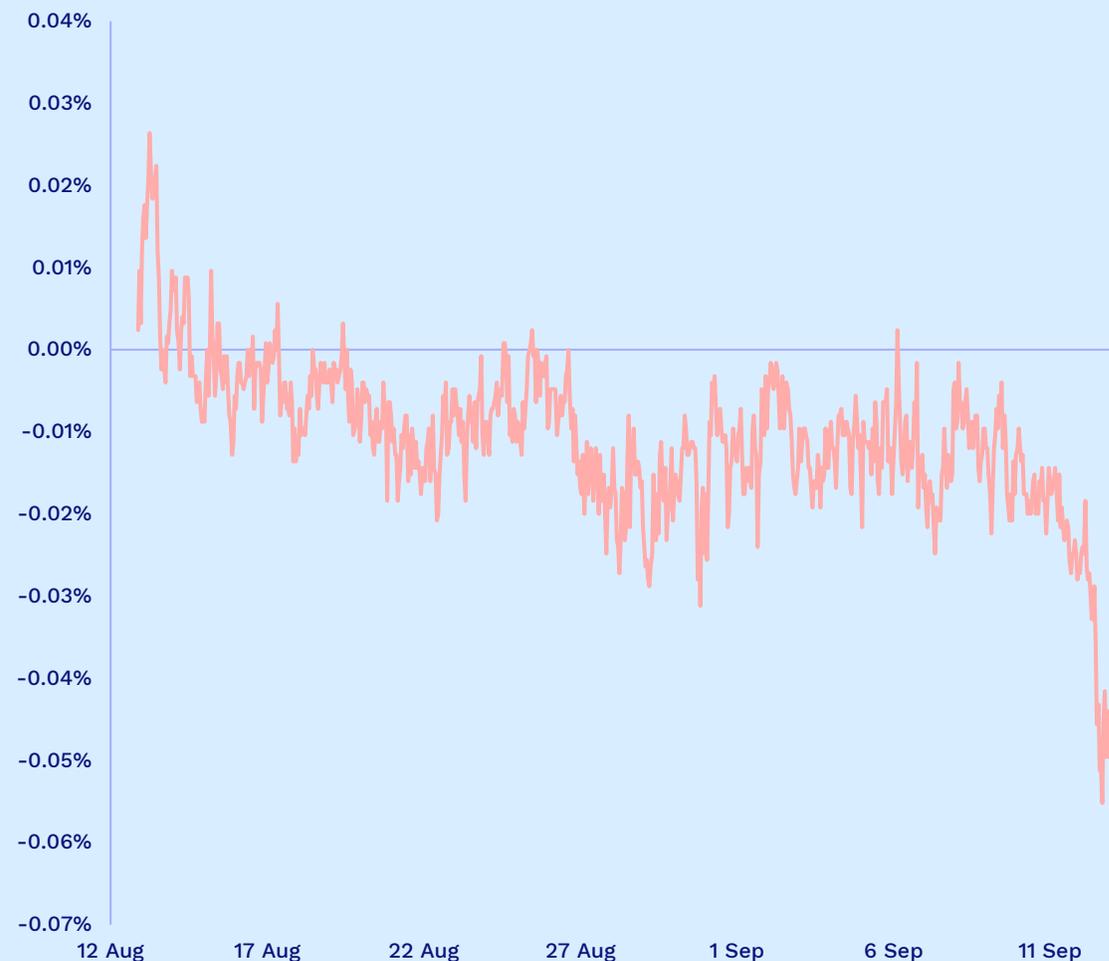
- Bitcoin just broke out of the narrow range it has been trading in for several weeks and is now attempting to break the \$22.5k resistance.
- CME's period in backwardation ended last week, driven by ETF traders reducing their downside exposure in anticipation of potential upside in BTC.
- Ethereum perps are seeing a massive plunge in funding rates as traders actively seek to hedge ahead of the merge, a buy-the-news story in the making?

3

## Blockchain Activity

- Bitcoin's 7-day average hashrate has surged to an all-time high as the public mining companies plug in their new machines.
- The soon-to-be-obsolete ETH miners are looking for alternative cryptocurrencies to mine. One of these is ETC, whose hashrate has more than doubled since July.

Ethereum (ETH) Funding Rate: FTX



Source: : Skew

# Bitcoin regaining market share as Ethereum merge nears

- Bitcoin has seen a strong recovery of 8% over the last seven days, outperforming the rest of the crypto market and regaining some of its market dominance as we approach the long-awaited Ethereum merge.
- This will be a huge week in crypto. The Ethereum merge is scheduled to occur on September 15<sup>th</sup>, and market participants are hedging like never before. Relative to BTC, ETH has underperformed in the last week, falling from a peak of 0.085 ETHBTC to 0.077 today, while the ETHBTC correlation has declined in a relatively volatile environment.
- In addition, we've seen subtle hints of BTC decoupling from broad financial markets, most recently with BTC's strong push Friday morning while financial indexes mostly traded in a flat environment.
- Nonetheless, certain events and scenarios generate a high correlation. Today's U.S. YoY CPI print of 8.3% is one such example. The market expected a MoM print of -0.1%, but we got yet another negative inflation shock, with a slightly positive MoM print of 0.1%. Bitcoin immediately plunged by 5.5% in the following minute from \$22,700 to \$21,400, while Nasdaq futures dropped by 3.2% as market participants brace for yet another substantial rate hike on the September 21<sup>st</sup> FOMC.

## Last week of top 50 by market capitalization

Best Performing	Price	Last week	Last month	YTD
Cosmos Hub	15.89	25.5%	33.3%	-59%
ApeCoin	5.77	21.4%	-13.3%	-53%
Solana	38.34	19.0%	-17.8%	-75%
Worst Performing	Price	Last week	Last month	YTD
Lido DAO	1.97	-3.1%	-32.6%	-33%
Ethereum Classic	38.55	-2.6%	-12.0%	-11%
LEO Token	4.98	-1.6%	2.1%	-31%

Source: CoinGecko, messari.io

## Bitcoin Correlation:

90-day correlation (weekly change included)	ETH	GOLD	S&P500
<b>BTC</b>	0.869	-0.039	0.246
	-0.089	0.614	-0.002

Source: CoinMetrics

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



Source: Tradingview (Coinbase, Binance US)



# Traders are rotating into bitcoin ahead of the merge

**The BTC dominance is down at levels not seen since 2018 as ETH gains favor among crypto investors ahead of the merge.**

- September started with bitcoin significantly underperforming the rest of the crypto market. Bitcoin's weak performance ended last Friday as the price began soaring. As we approach mid-September, bitcoin is the second-best performer among our indexes, with a 12% gain. The best performer is the Mid Cap index, which saw a solid start to the month.
- Bitcoin's outperformance has led the bitcoin dominance to soar by 1.8% over the past seven days. It's currently sitting above 40% for the first time in almost one month.
- In late August and early September, the rest of the crypto market, particularly ETH, managed to steal market share from the underperforming BTC. The ETH dominance fell by 0.7% over the past seven days but is still close to its highest level since December 2021.
- Big happenings like the merge sometimes lead to a "sell-the-news" event caused by traders over-positioning themselves ahead of the event. ETH's underperformance ahead of the merge indicates that some traders attempt to front run a potential "sell-the-news" event. Still, whether or not the merge will turn out to be a "sell-the-news" event remains to be seen.

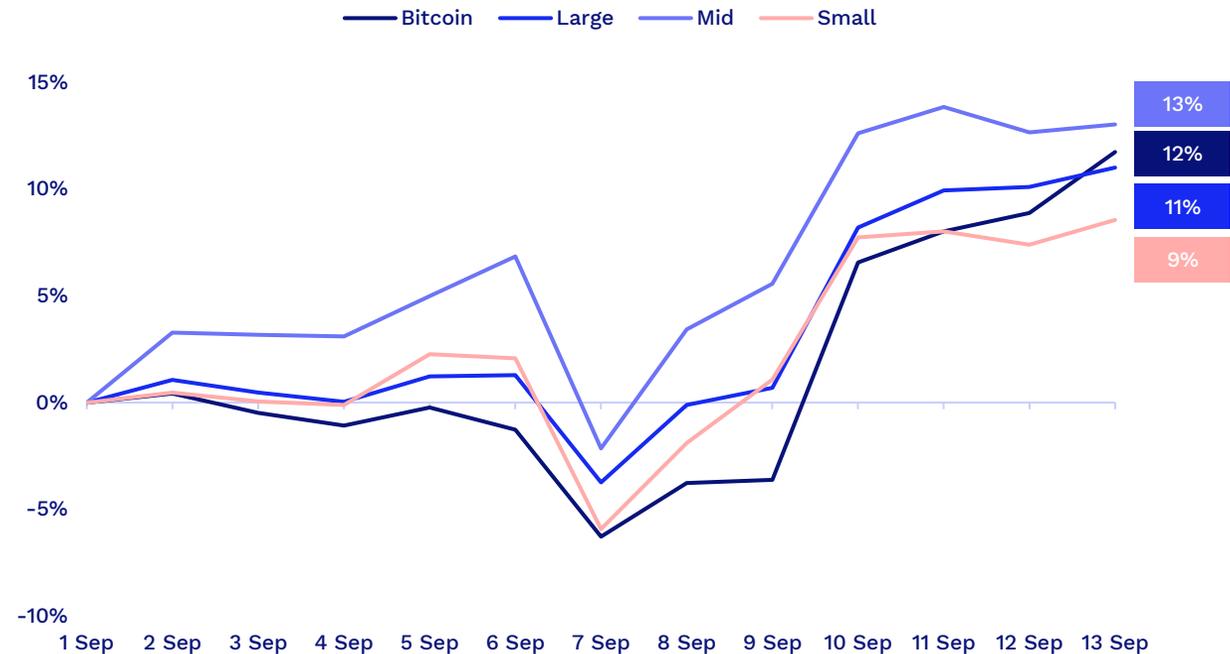
Percentage of Total Market Capitalization

	BTC	ETH	USDT	USDC	BNB	BUSD	XRP	ADA	SOL	DOT
Market Share	40.07%	19.68%	6.35%	4.83%	4.45%	1.89%	1.67%	1.61%	1.28%	0.80%
Weekly Change	1.81%	-0.67%	-0.44%	-0.37%	-0.10%	-0.07%	0.01%	-0.12%	0.12%	-0.05%

\* Weekly change in percentage points

Source: CoinMarketCap

Monthly Performance of Market Cap-Weighted Indexes



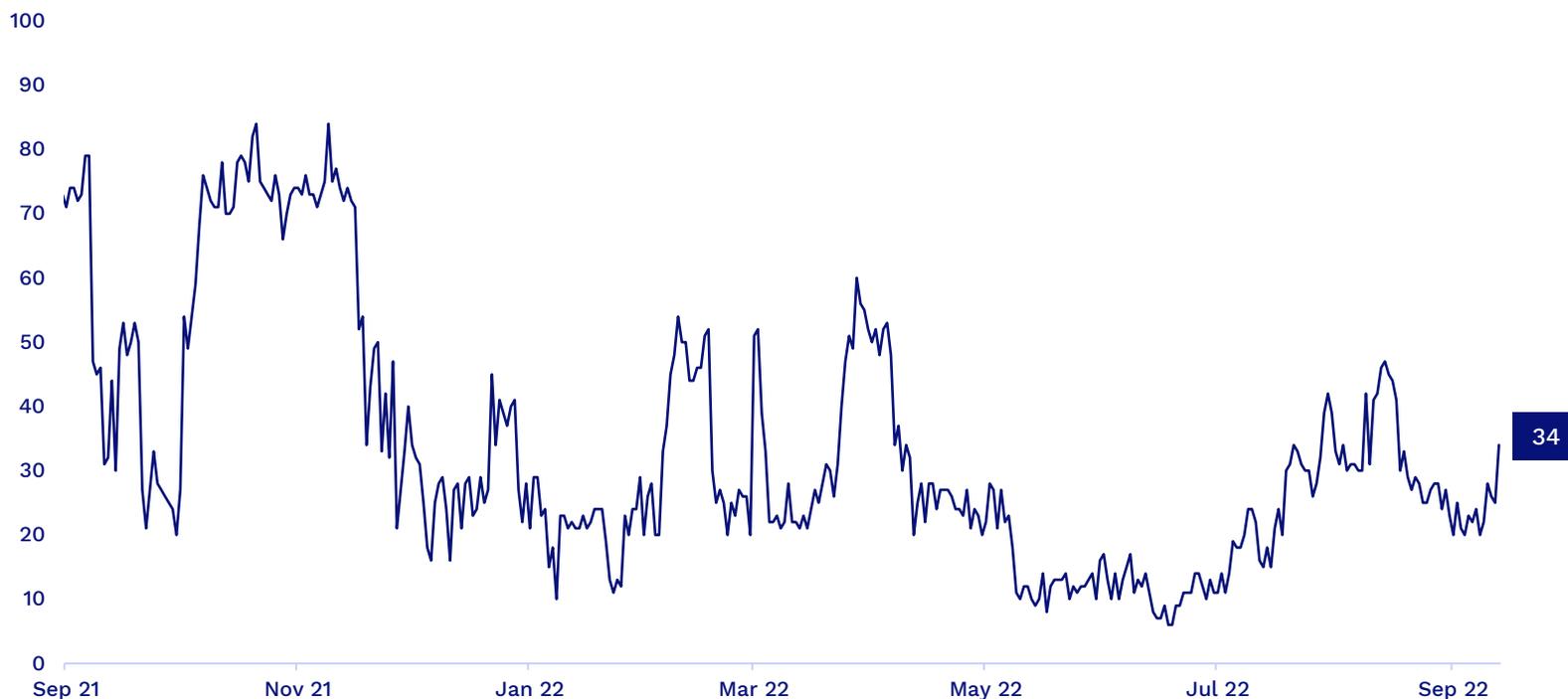
Source: Bletchley Indexes, Tradingview (Coinbase)



# The market sentiment is improving, but traders are still cautious

The Fear and Greed Index has managed to climb out from the 'extreme fear' area. A significant component of the index calculation is market momentum and volume, and recently we have seen growing spot volumes in a positive market. The index still signals 'fear', reminding us that investors still don't believe the seemingly never-ending bear market to be over.

Fear and Greed Index



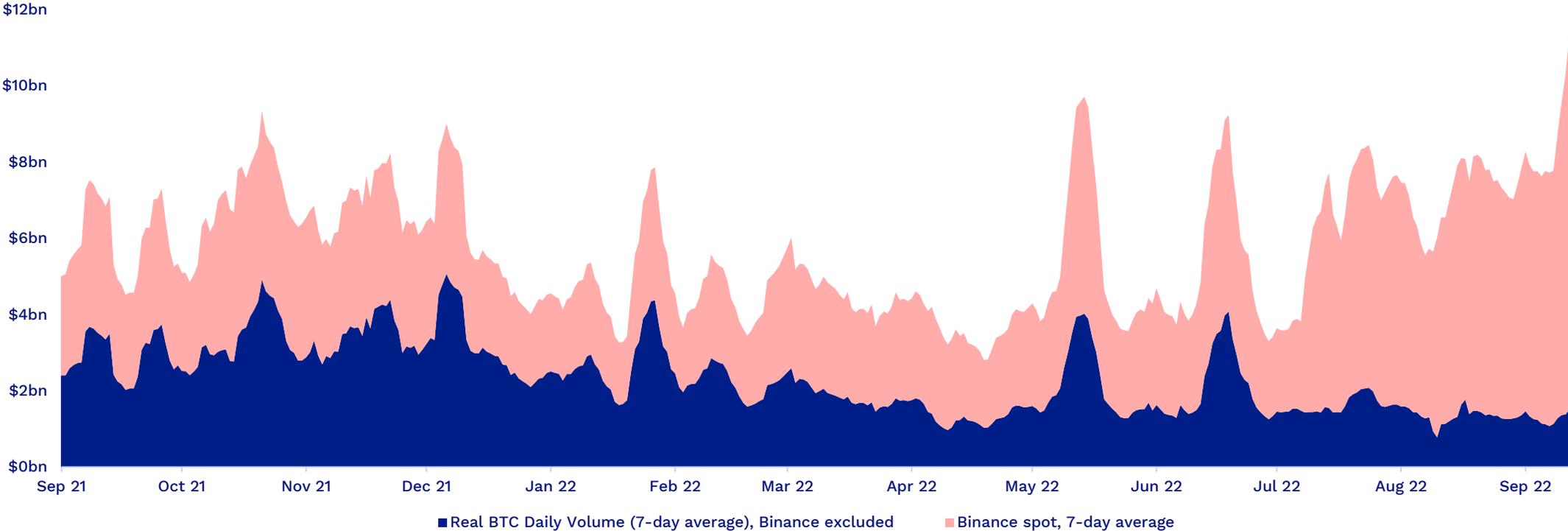
Source: Alternative.me



# The bitcoin spot volume surges to yearly highs

The 7-day average bitcoin spot volume has surged to a yearly high of \$11.4 billion. Most of this trading activity happened on Binance, which has completely taken over the bitcoin spot market due to its fee removal this summer. Binance's zero-trading fee policy has made new high-frequency trading strategies profitable and attracted these types of traders to Binance's bitcoin pairs. The 7-day average spot volume on Binance is currently 87% of bitcoin's total spot volume.

Real BTC Daily Volume\* (7-day average)



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

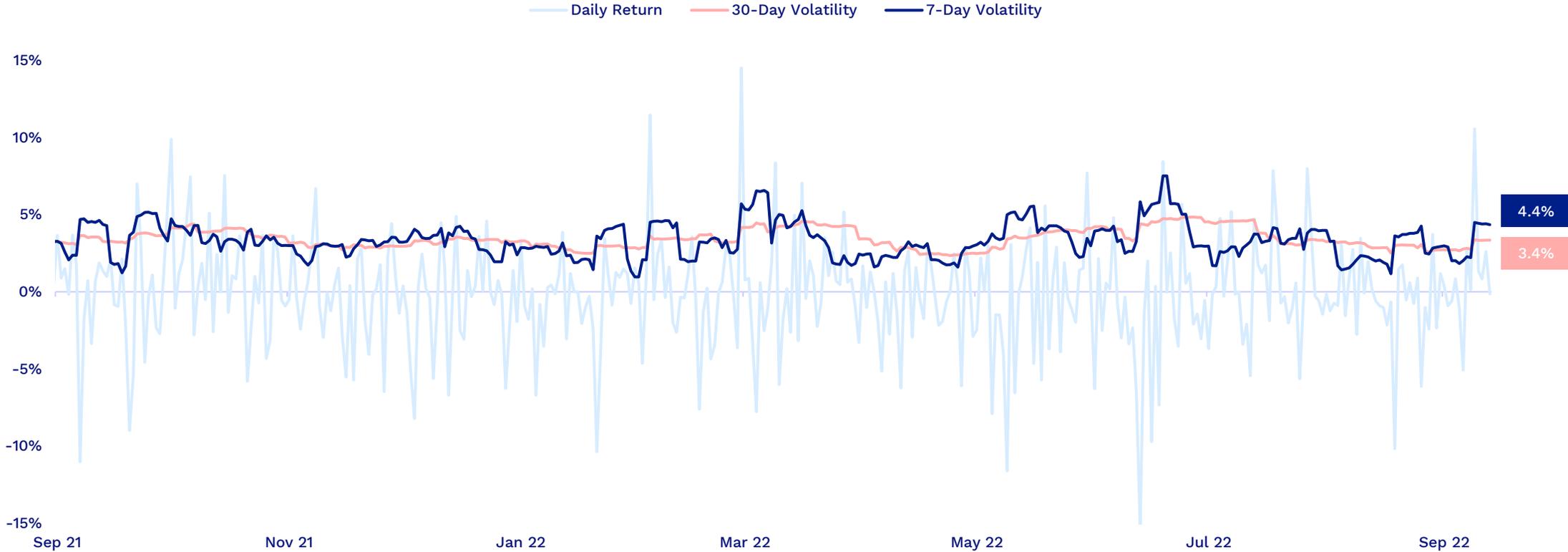
\*Includes Bitwise 10 exchanges, LMAX, FTX



# Bitcoin's third highest daily return in 2022 leads volatility to grow

Over the past weeks, bitcoin's volatility has been unusually low as the price stabilized around \$20k. This calm period ended last Wednesday as the price dropped to a bottom of \$18.6k and suddenly made a massive rebound up to \$22.3k over just a few days. Most of these gains came last Friday when the price soared by 10.6%. The high volatility will likely continue over the following days as the merge may significantly increase trading activity.

### BTC-USD Volatility



Source: Tradingview (Coinbase)



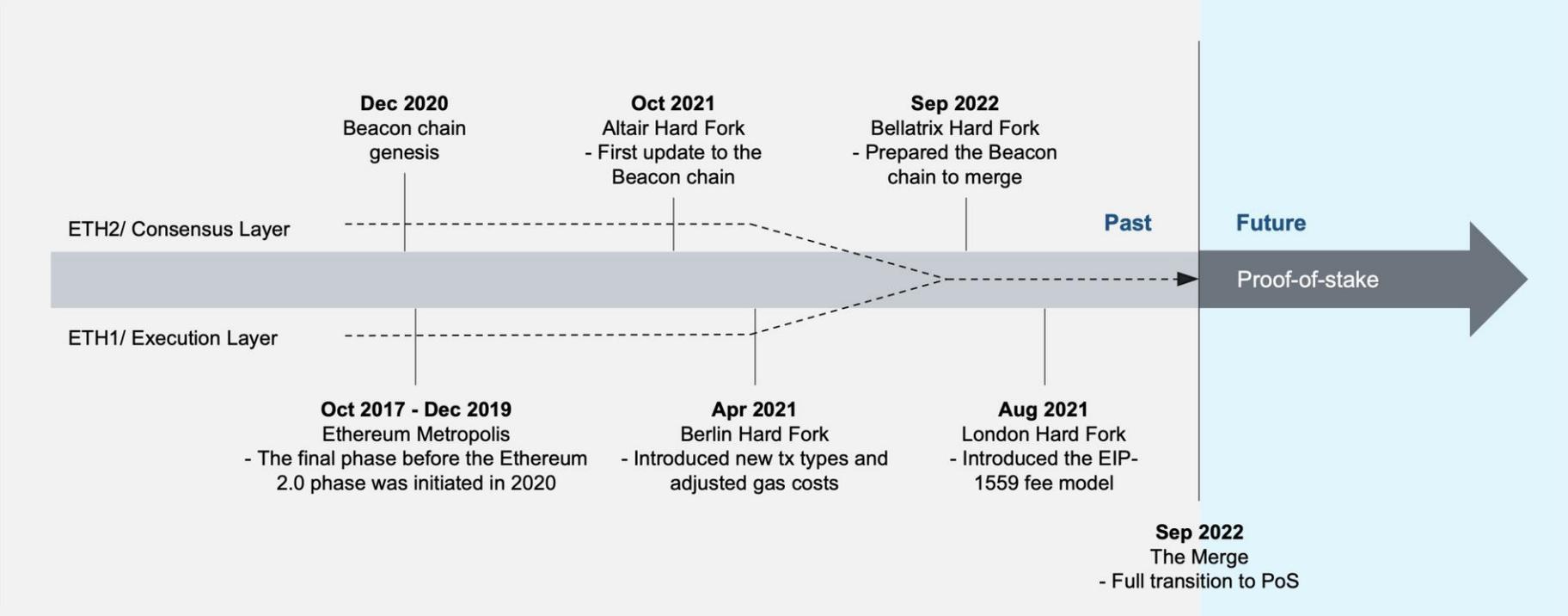
# The calm before The Merge

Ethereum, the second biggest cryptocurrency by market cap, is expected to complete its transition from Proof of Work (PoW) to Proof of Stake (PoS) around September 15, 2022. Last week, Bellatrix was activated—the last major update before the merge—and enables Ethereum consensus layer clients to execute transactions on the Beacon chain.

**A brief on what the merge will mean in practice:**

It *will*: 1) Immediately reduce Ethereum’s energy demand by 99.95%, 2) Allow for future upgrades that will make it faster and more scalable, and 3) Reduce ETH issuance by ~90%\*. It *will not*: 1) Create another blockchain called “Ethereum 2.0”, 2) Create a new Ethereum token called “ETH2”, or 3) Lower the cost of ETH transactions.

Ethereum’s journey from Proof-of-Work to Proof-of-Stake



\*estimate

Source: Ethereum Foundation



# ETHPOW hard fork struggling to maintain its momentum

**As the Ethereum merge approaches, the proof of work-based Ethereum hard fork seems to be losing interest while Ethereum Classic maintains its strength.**

- Ethereum Classic has had a rock solid year, outperforming most of the market. ETC started the year with a market cap size of approximately 1% the size of Ethereum's but has, over the last nine months, seen its market cap relative to ETH grow to 2.5%.
- The strength of Ethereum Classic is most likely driven by the ETH miner. Once the merge finalizes and Ethereum mining becomes obsolete, ETH miners have very few viable alternative chains to migrate to.
- Nevertheless, while the price action has been strong, and the security on ETC will strengthen with growing hashrate, it's worthwhile assessing the actual usage of ETC. As of writing, Ethereum Classic has shallow economic activity.
- Per DeFiLlama, Ethereum Classic has a total value locked of less than \$1m and is the 120<sup>th</sup> largest layer-1 measured by TVL. ETC could thus face difficulty garnering any meaningful economic activity after the merge. Most of the strength in recent months seems to rather relate to Ethereum Classic representing an important ideological bastion for some investors following the infamous DAO hack and ETC being one of few alternative chains for Ethereum miners to migrate to.
- Thus, in order to potentially reap the benefits of some of the infrastructure and usage of Ethereum's vibrant DeFi ecosystem, a group of miners has attempted to push for a hard fork at the merge, which would lead to a chain-split at the merge, as we've previously explained.
- Nevertheless, as of writing, ETHW and ETHPOW, which are derivatives based on the potential hard fork, have seen dwindling activity. On Bitfinex, ETHW has seen a substantial decline. ETHW is priced at 1.14% of the value of ETH, while it traded at 3% of the price of ETH at launch. This is well below the ETC price relative to ETH, and it might suggest that the old dame ETC is currently viewed as the more appealing continuation case for proof-of-work based Ethereum activity.

Market cap relative to Ethereum: Ethereum Classic, ETHW (Bitfinex)



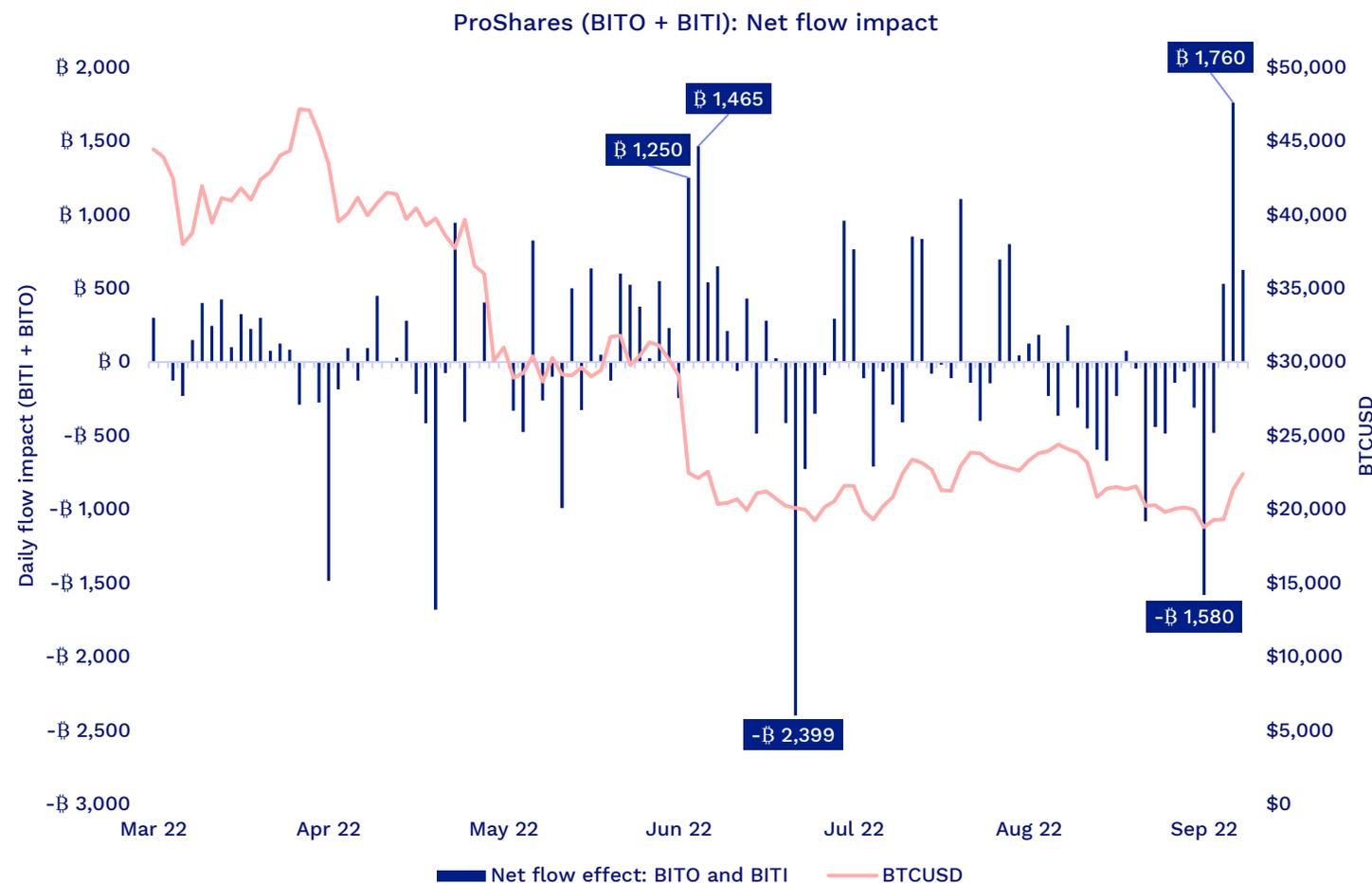
Source: Coinmetrics, Tradingview (Bitfinex)



# Positive flows to BTC ETFs after a month of downside focus

## ETF traders are unwinding short exposure in BTC ETFs, eyeing potential upside, leading CME basis to recover.

- Thursday and Friday last week showed promising signs in ETFs after a month of near-constant net negative flows to ProShares BTC ETFs.
- In the last three trading days, BITO has experienced consecutive inflows, equivalent to a growth in BTC exposure of 1650 BTC.
- Meanwhile, BITI, the short ETF, saw substantial outflows, amounting to 1,060 BTC on Friday. This is the largest BTC equivalent outflow from BITI since launch, and it suggests reduced conviction from traders betting on a further downfall.
- Outflows continued on Monday, as BITI experienced outflows equivalent to 425 BTC. Following these outflows, BITI's short exposure has declined to an equivalent of 3,850 BTC. This is on par with the peak short exposure reached in June and July, implying that there still is a solid demand for betting on BTC downside.
- The Friday outflow of 1,060 BTC from BITI and inflow of 700 BTC to BITO combined contributed to a net positive directional impact equivalent to 1,760 BTC in the ProShares ETFs. This makes the Friday flows the strongest day in terms of ProShares' flows since October 21st, 2021. These flows have likely contributed to sending CME's futures back into contango.
- While the daily flows on Friday in isolation suggest a growing bullish sentiment in ETFs, it's worth noting that BITI's BTC equivalent exposure sits on par with June and July highs, while BITO's BTC exposure has declined to a three-month low.



Source: ProShares, Tradingview (Coinbase)



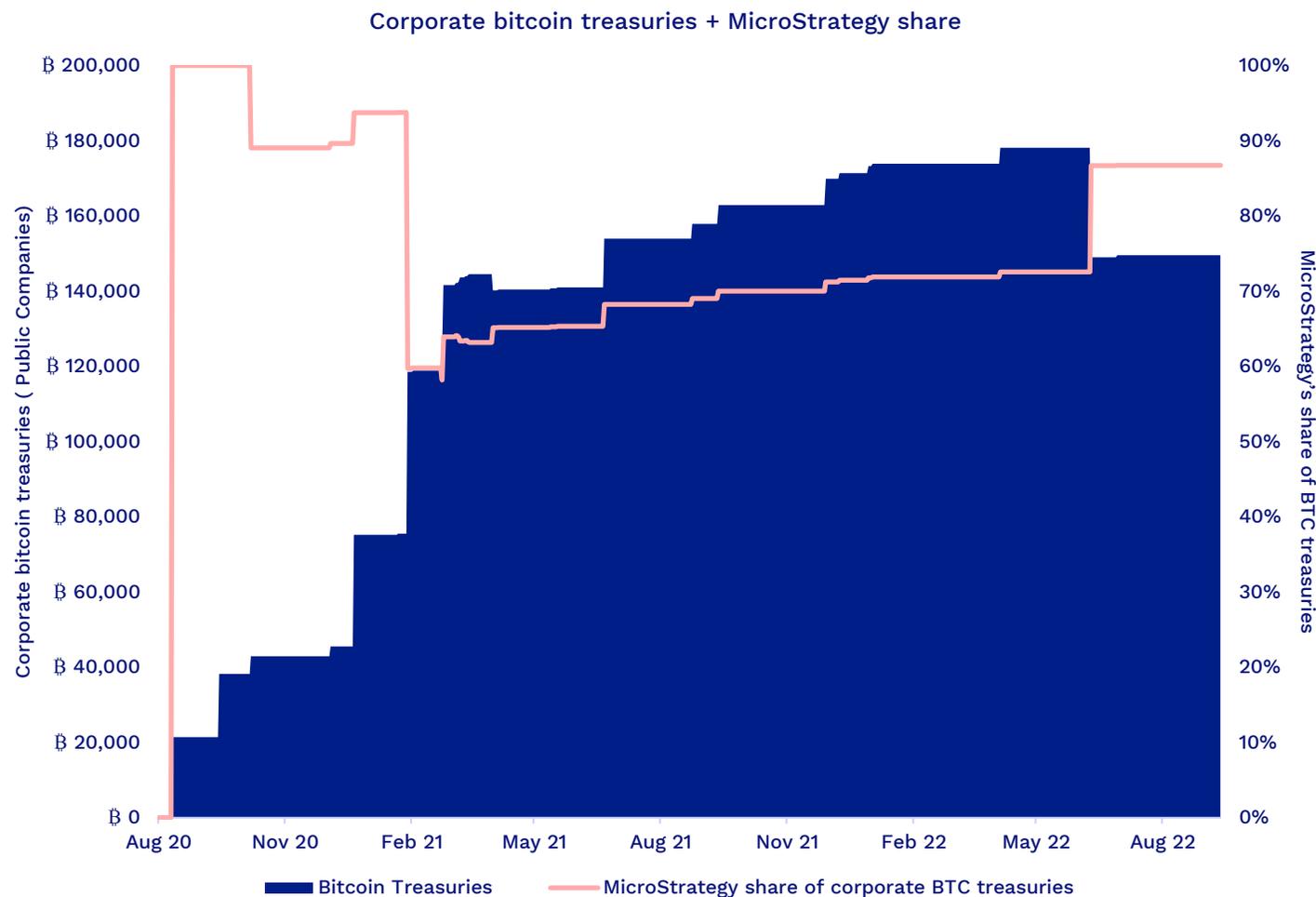
# Saylor Texas hedging: MicroStrategy to accumulate more bitcoin

**MicroStrategy's everlasting quest to grow its BTC treasuries continues as the company seeks to issue class A stocks to purchase \$500m worth of BTC.**

- MicroStrategy currently holds 129,700 BTC and seeks to buy more BTC by selling up to \$500m in class A stock.
- Last summer, MicroStrategy pulled off a similar stunt by launching an at-the-market security offering on June 14th, 2021, to sell up to \$1 billion of its class A stock aiming to buy BTC with the proceeds. Then MicroStrategy purchased \$1bn worth of BTC over an extended period, with the first purchase being announced two months after the offering announcement.

Date	BTC Purchased	\$ Spent
8/24/2021	฿ 3,907	\$177m
9/13/2021	฿ 5,050	\$243m
11/29/2021	฿ 7,002	\$414m
12/9/2021	฿ 1,434	\$82m
12/30/2021	฿ 1,914	\$94m
<b>Sum</b>	<b>฿19,307</b>	<b>\$1bn</b>

- At current prices, \$500m equals 22,500 BTC. This would increase the BTC balance of MicroStrategy to 152,000 BTC, representing 88.5% of the BTC held by public companies.
- In 2020 and 2021, MicroStrategy also purchased BTC through note offerings. These purchases were pre-announced, allowing the market to react to MSTR's purchases. The class A stock purchases last year came in more surprising increments, this will likely be the case today as well, and investors should be prepared for various MicroStrategy purchase announcements in the coming months.



Source: MicroStrategy, Square, Tesla, Meitu, Aker





# Valuation



# Bitcoin breaking out from its narrow range - \$25k next?

**Bitcoin just broke out of the narrow range it has been trading in for several weeks and is now attempting to break the \$22.5k resistance.**

- Bitcoin is currently trading just below an important resistance level at \$22.5k, which served as support in August and local tops in June and July.
- If bitcoin manages to power through \$22.5k, the next resistance level is in the \$25k area. This area has proved to be a strong resistance for bitcoin on multiple occasions lately, marking the local peak during this bear market.
- Above \$25k the horizon is open until \$30k, which is both an important psychological level and served as a vital support level for bitcoin in May and June.
- Towards the downside, bitcoin has strong support in the range between \$19.5k and \$20.k.
- Further downwards, an extremely important support level is at \$17.5k, which has marked the bottom of this bear market.



Source: Tradingview (Coinbase)

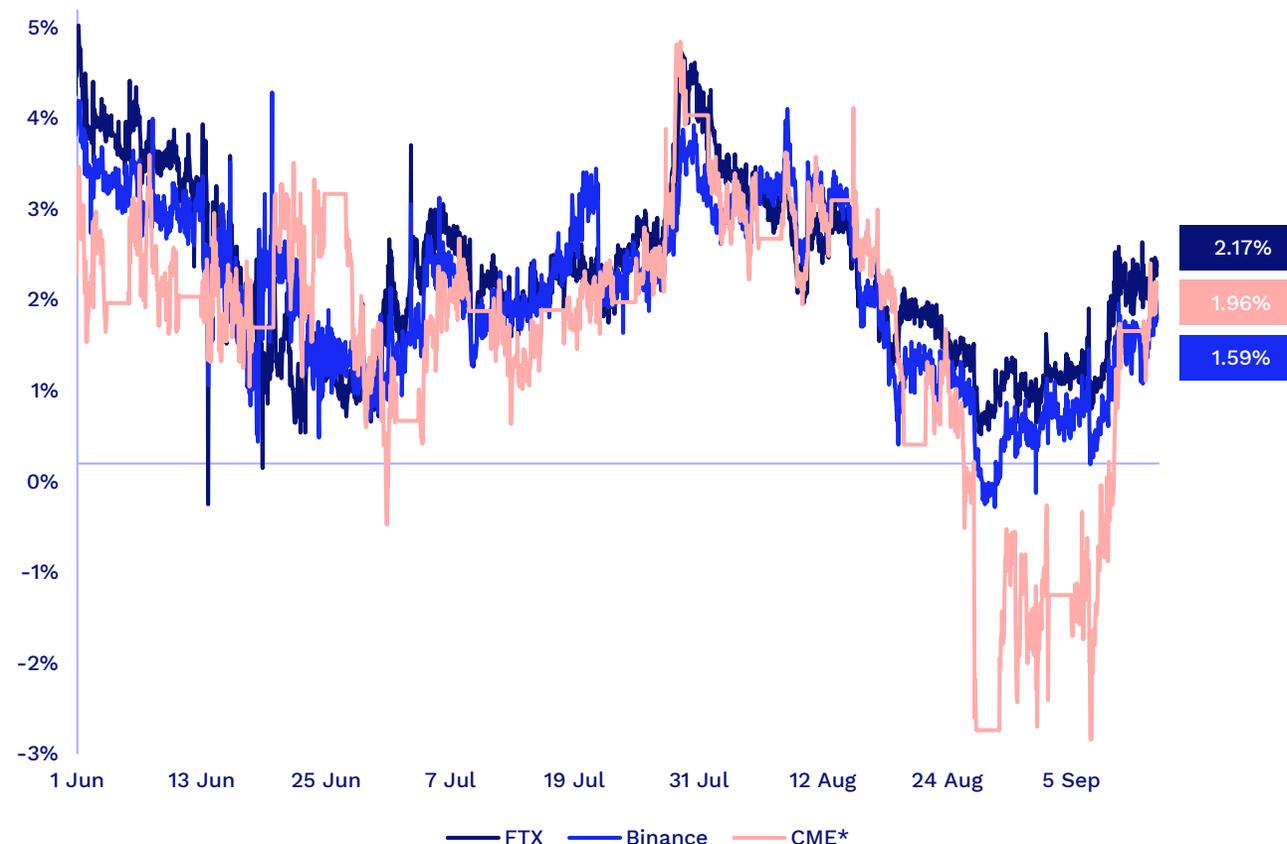


# CME basis recovers

**CME's period in backwardation ended last week, driven by ETF traders reducing their downside exposure in anticipation of potential upside in BTC.**

- Bitcoin futures has seen an uplifting trend in the last days following BTC's recovery from range lows, with the futures basis climbing to 2% across all venues.
- CME has seen the strongest recovery, with its futures no longer trading at a discount to spot. The key source behind this recovery is likely the ETF flows, as addressed earlier, with short-covering having a positive impact on CME's basis.
- After CME's recovery, the CME basis now aligns with the offshore basis. In addition, CME's front-month futures currently trade at a premium to other offshore venues for the first time since early August.
- The basis offshore has also recovered over the last seven days. Currently, the basis has climbed to mid-July levels.
- While the climbing basis suggests a more optimistic outlook from BTC futures traders, a 2% annualized basis is low through historical lenses. Overall, traders still seem to be cautiously positioned, with a considerable willingness to protect for further downside.
- Nevertheless, the recovery suggests a breath of optimism in the market and coincides with BTC strengthening, both versus Nasdaq and versus ETH, amid a very interesting macro and crypto week.

Bitcoin Futures Annualized Rolling 3-Month Basis



Source: Skew, Laevidas, Tradingview, CME

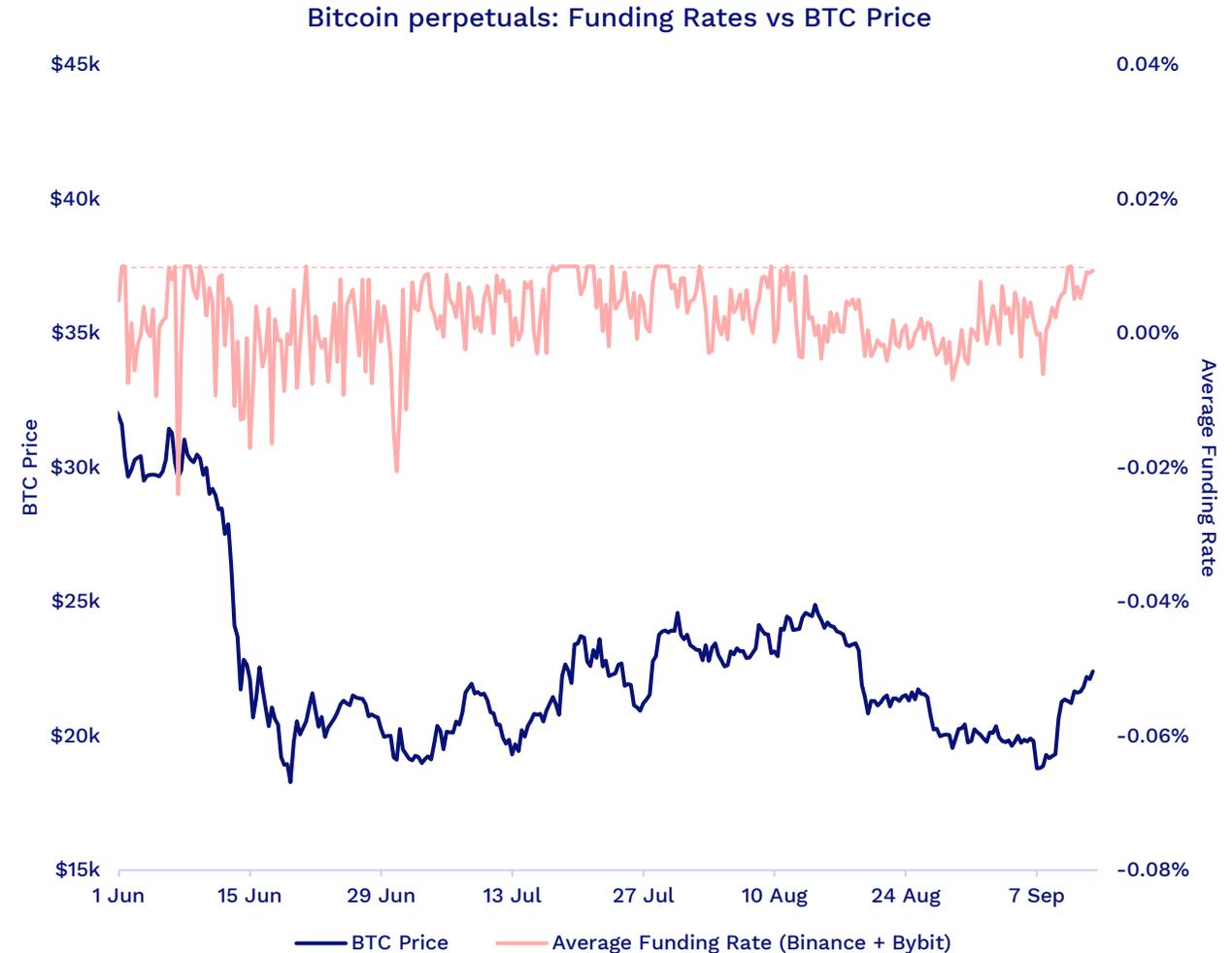
\*Closed Saturday - Sunday



# Funding rates climbing to neutral levels

**Funding rates also recovered over the last few days amid brewing optimism as BTC recovers.**

- Funding rates reached neutral levels amid BTC's Friday recovery.
- We saw a short squeeze in BTC perps leading to the funding rate recovery on Friday as \$130m worth of shorts got liquidated. This is the largest short liquidation volume seen in BTC since June 13<sup>th</sup> but is still negligible in size compared to previous squeezes.
- This short squeeze had a minor impact on open interest, which remains high, as illustrated in the next slide.
- Funding rates have since declined slightly but remain higher than prior to the Friday recovery, suggesting a fairly balanced demand to enter longs and shorts in BTC.
- Still, while funding rates have recovered to neutral terrain, the extended periods of funding rates below or at neutral prevails. December 3<sup>rd</sup> is the last time funding rates climbed above neutral levels.



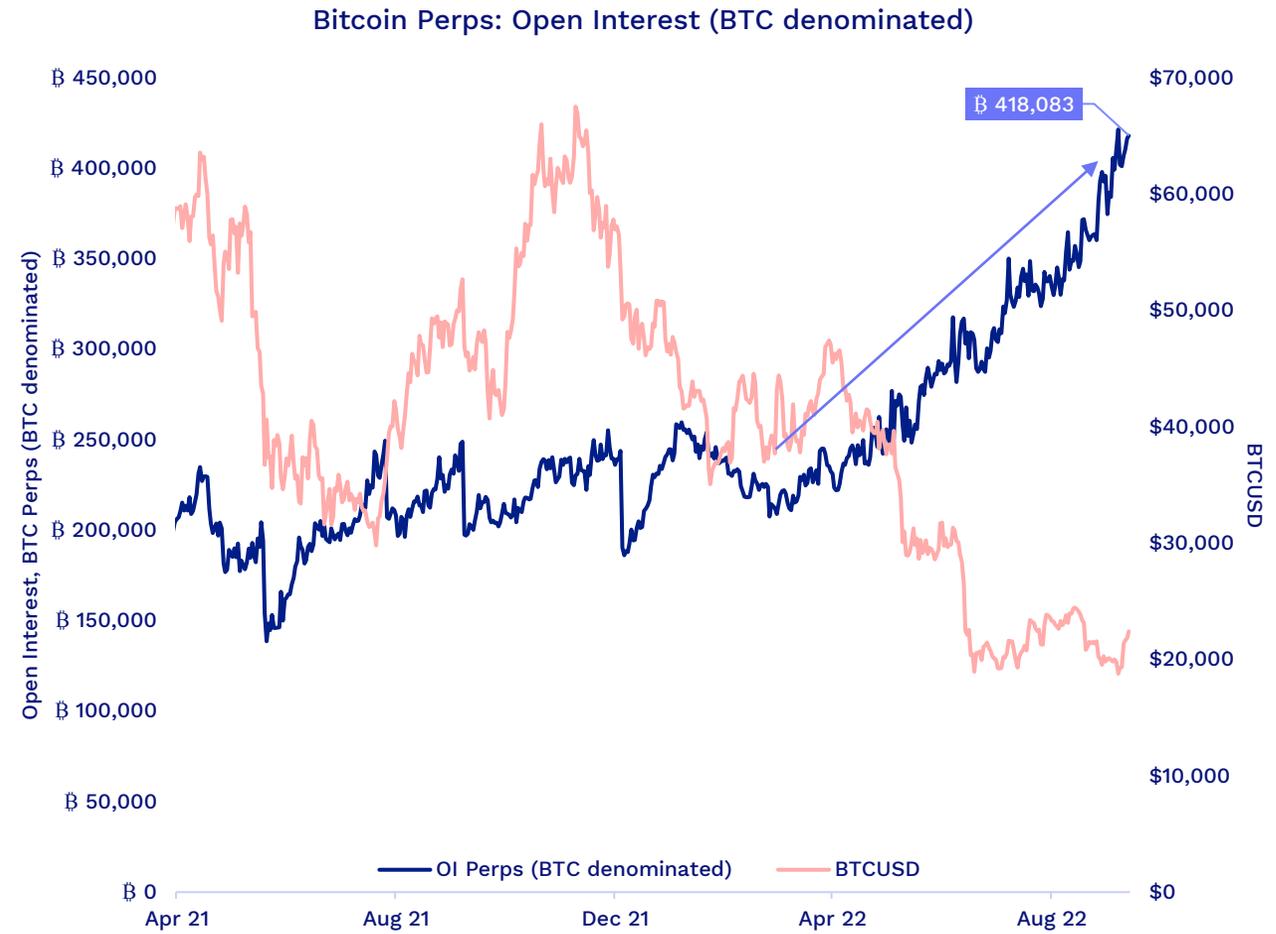
Source: Skew, Bybit, Binance



# BTC denominated open interest at all-time high

## Open interest in perps sees further growth – now sitting at 418,000 BTC.

- BTC denominated open interest in perps stays high and reached a new all-time high last Wednesday of 421,000 BTC before experiencing a minor setback amid the Friday short squeeze.
- As noted previously, the open interest has not been heavily impacted by BTC crashes, suggesting that longs are conservatively leveraged in BTC derivatives.
- By illustrating the open interest in notional value, we get a sense of the relative degree of leverage in the market, removing noise introduced by BTC's inherent volatility.
- On Wednesday, the combined open interest in BTC perps and futures reached a new all-time high, surpassing the previous February 2020 peak.
- In February 2020, the growth was accompanied by an elevated futures basis and positive funding rates. Then, leverage was more concentrated on upside bets, leading to the cataclysmic days of March 12<sup>th</sup>. Now, the growth has occurred amid a prolonged depressed sentiment, and it's fair to assume that the market is less exposed to a March 12<sup>th</sup>-like crash.
- Open interest may remain high for extended periods, but this new paradigm is unlikely to last. Allocation into derivatives involves funding costs, and positions are bound to unwind somewhere down the line. The strong constant growth in OI, with negligible declines during the Luna and 3AC collapses, suggests that shorts have been at the wheel throughout the rise.
- Once uncertainty is lifted from the market related to the pressuring macro backdrop, regulation, and the Ethereum merge, it's certainly plausible that hedges will be unwound, which may have positive implications for the BTC price.



Source: Laevidas



# ETH perps seeing massively negative basis

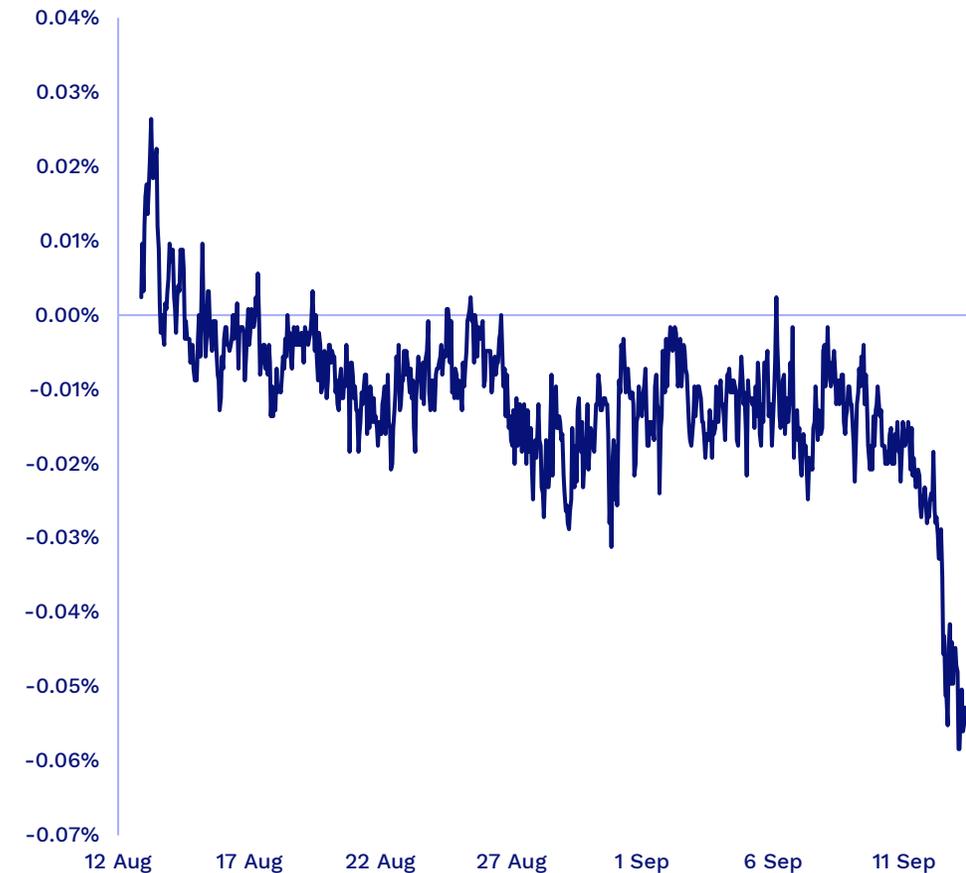
**Ethereum perps are seeing a massive plunge in funding rates as traders actively seek to hedge ahead of the merge, a buy-the-news story in the making?**

- Yesterday, the accumulated funding rate on FTX's ETH perp reached -0.94%, meaning that shorts had to pay 0.94% in daily compensation to longs to hedge ahead of the merge.
- FTX's funding rates update at an hourly interval. If the current funding rate regime of approximately -0.06% per hour until the Merge, shorts will pay approximately 2.4% in fees to longs.

## Three strategies may fuel the aggressive shorting:

1. Cash neutral exposure, with a 1:1 allocation of ETH spot vs. ETH shorts. If the funding rate remains as low as now, and such a short is held until the merge, hedgers will pay 2.4% in fees for an airdrop token which is currently valued at 1% of the ETH market cap.
  2. Hedging a failed merge. If the merge succeeds, shorts may unwind. Prices may react positively to this flow if spot positions are maintained.
  3. Downright bearish bets on Ethereum, either due to a failed merge or a classic sell-the-news event.
- Ethereum has weakened versus BTC in the last week, falling from a high of 0.085 ETHBTC to 0.077 ETHBTC, suggesting that some have already rotated to BTC ahead of the merge.
  - Crypto has a rich history of known positive events becoming sell-the-news-events. In bitcoin, more or less all known massive events in newer history have coincided with the typical sell-the-news reaction. This occurred during the CME futures launch in 2017, the ICE futures launch in 2019, Coinbase's IPO in 2021, El Salvador's BTC adoption day, and the spot ETF verdict.
  - Still, all these sell-the-news events saw vastly different derivatives activity, with derivatives traders then punting long exposure. This time, derivatives are in a vastly different state, with a huge focus on hedging. In the likely event of a successful merge, we might be in for a rare buy-the-news event in crypto as traders unwind hedges, having a positive impact on the overall market.

Ethereum (ETH) Funding Rate: FTX



Source: Skew





# Blockchain Activity



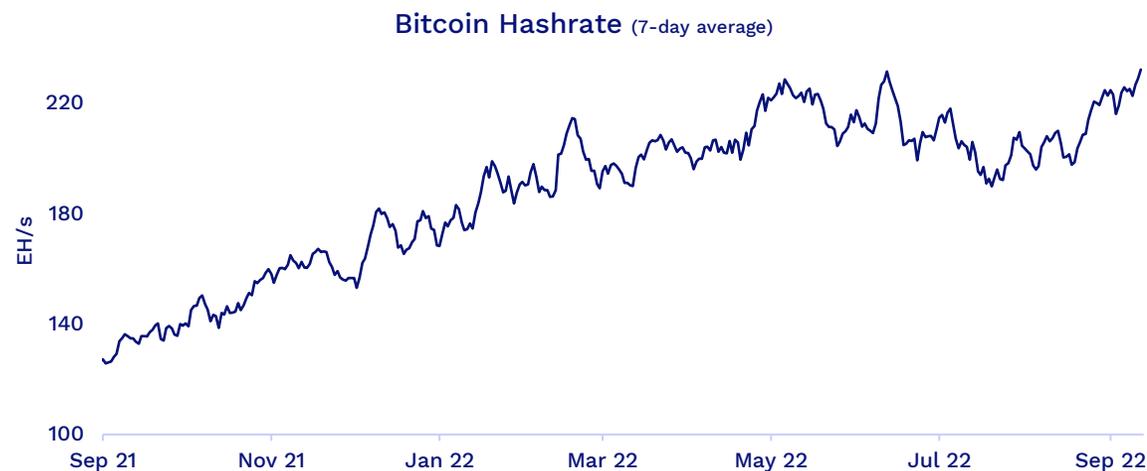
# Bitcoin's hashrate reaches all-time high

Bitcoin's 7-day average hashrate has surged to an all-time high as the public mining companies plug in their new machines.

- The hashrate's prior all-time high was in early June after a slow and steady growth since the summer of 2021. The hashrate suddenly started falling in June as miners unplugged their machines due to a heatwave in the U.S. that led to soaring electricity demand. The U.S. currently hosts around 40% of Bitcoin's hashrate.
- The public bitcoin mining companies are awaiting enormous deliveries of mining rigs in the coming months. Some of them, like Marathon, already have thousands of mining rigs in storage waiting for hosting space and aim to plug in 6.9 EH/s over the next three months. Riot Blockchain has plans to plug in an additional 4.5 EH/s in 2022, while Core Scientific plans to deploy around 4.4 EH/s.
- Due to the enormous hashrate growth plans of the public mining companies, we expect the hashrate at the end of this year to stand close to 245 EH/s. This estimate is, of course, very dependent on the bitcoin price development. If the bitcoin price keeps increasing towards \$30k, we might see some older generation mining rigs coming online again, which could lead the hashrate to reach 260 EH/s.
- A symptom of the rapid hashrate growth is the high block production rate. Over the past seven days, miners have churned out 6.28 blocks per hour, significantly above the target of 6. The Bitcoin network will likely increase its difficulty by 3.2% later today, in the fourth upwards difficulty adjustment in a row.
- All these upwards difficulty adjustments pressures miners' profit margins. With difficulty sitting at an all-time high, bitcoin miners are severely vulnerable to a significant drop in the bitcoin price, particularly those with the least liquid balance sheets.

Powered by:		Bitcoin Network Data			
BYTETREE		9/12/2022	7d prior	7d Change	30d Trend
Network	Daily Miner Revenues	\$ 19,839,495	\$ 18,836,336	5.33%	
	Fees per day	\$ 289,494	\$ 276,780	4.59%	
	Fees % Revenues	1.46%	1.47%	-0.01%	
	Daily TX Volume (\$M)	\$ 3,680	\$ 3,455	6.50%	
	Transactions per day	259,763	251,256	3.39%	
Utility	Avg TX value \$	\$ 14,167	\$ 13,753	3.01%	
	# Blocks per hour	6.28	6.21	1.15%	
	Avg. # TX per block	1,724	1,667	3.39%	

Source: Bytetrete



Source: Blockchain.com



# Ethereum miners are migrating to Ethereum Classic

**The soon-to-be-obsolete ETH miners are looking for alternative cryptocurrencies to mine. One of these is ETC, whose hashrate has more than doubled since July.**

- Ethereum mining is a significant industry. The total industry revenue was \$18 billion in 2021, more than bitcoin mining's \$17 billion.
- If everything goes according to the plan, the merge will take place on Wednesday evening/Thursday morning and replace ETH miners with validators. ETH miners have invested billions of dollars in GPU mining rigs. These rigs can't mine bitcoin, so the soon-to-be-obsolete ETH miners are looking for other tasks to direct their rigs' computing power to.
- One of the biggest alternative cryptocurrencies ETH miners migrate to is Ethereum Classic (ETC). It has seen a 150% increase in its hashrate since July.
- The price of ETC has also pumped by 171% since July, as traders seem to speculate that ETH miners will attempt to pump the prices of other GPU mineable coins when they get kicked off the Ethereum network.
- Other significant cryptocurrencies that ETH may switch to include Ravencoin, which has also seen a significant increase in both its hashrate and price as the merge got closer.
- Still, these alternative cryptocurrencies are too small to absorb a significant share of the ETH hashrate. Hashrate Index estimated that alternative cryptocurrencies could only take on 15% of ETH's hashrate before rendering mining unprofitable.



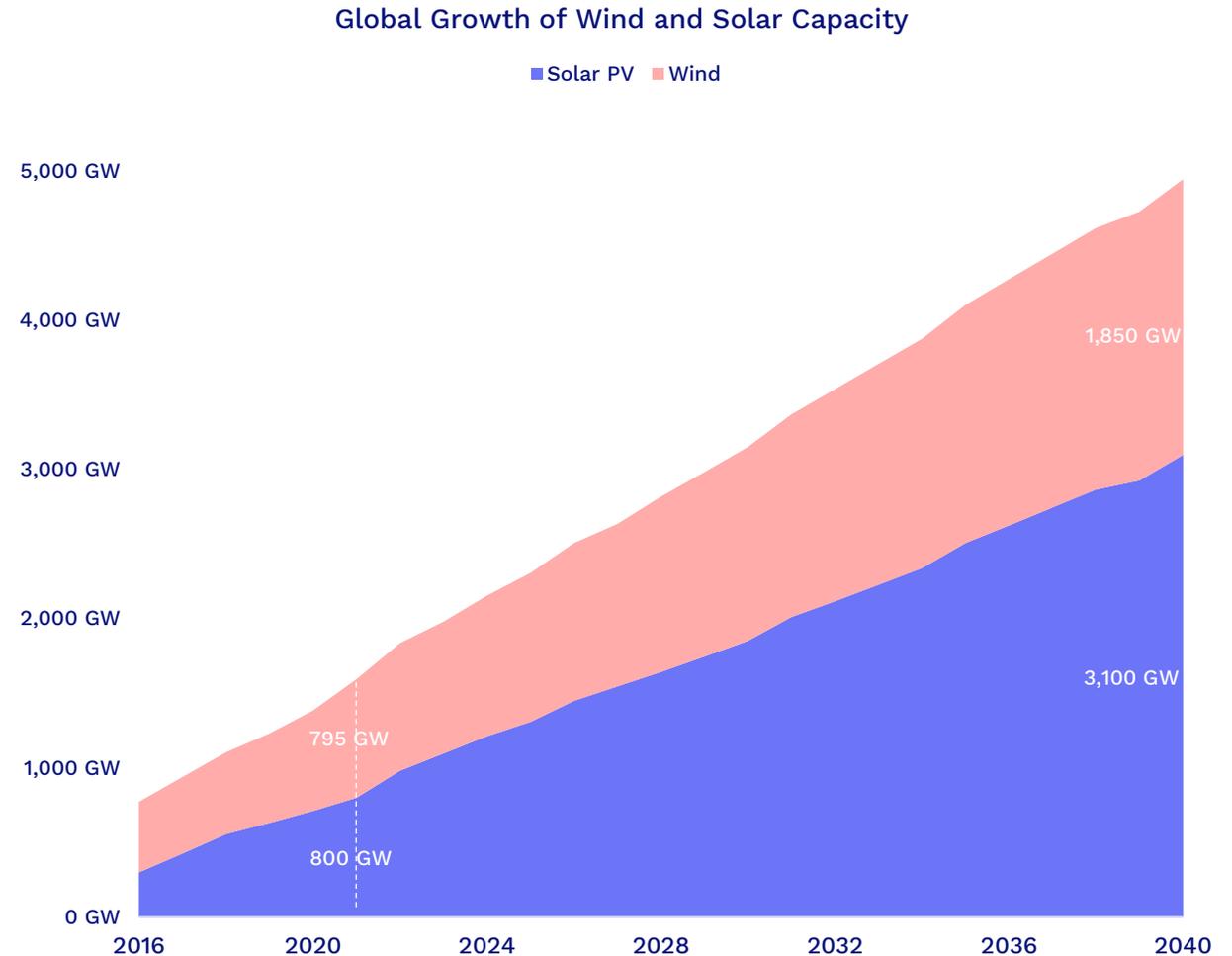
Source: Coinmetrics



# Bitcoin mining improves the economics of renewable energy

**Wind and solar are variable energy sources that sometimes produce more energy than the grid needs, leading to energy waste. Bitcoin miners are uniquely flexible energy consumers that can monetize previously wasted wind and solar energy.**

- The global generation capacities of wind and solar power have seen massive growth over the past years. In its Sustainable Development Scenario, the IEA estimates that wind and solar generation capacities will keep growing rapidly.
- The growing share of wind and solar power will lead to more wasted energy due to the variable nature of renewable energy production. Energy waste is an economic challenge that, if left unmitigated, can threaten renewable energy economics, thus limiting its growth.
- Since wind and solar generators have marginal production costs of \$0, they will always bid their energy into the market for \$0 per MWh. Therefore, we often see high price volatility in electricity markets with high shares of wind and solar. The electricity price is very low or even negative at times of high wind and solar production and very high when wind and solar don't produce.
- Bitcoin miners can help reduce curtailment and mitigate the frequency of negative electricity prices by strategically locating themselves close to the wind and solar plants to offtake their excess energy. This is achieved by exploiting the interruptibility of bitcoin mining, so that wind and solar producers can alternate between delivering power to the grid and bitcoin miners depending on the power prices.
- Learn more about how bitcoin mining improves the economics of renewable energy in Arcane's new report "[How Bitcoin Mining Can Transform the Energy Industry](#)".



Source: IEA (Sustainable Development Scenario)



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