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Are cryptocurrency markets lagging behind fundamental trends?



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Smart investors take profits. Markets don't simply go up in a straight line. Why should the case be any different with Bitcoin? For cryptocurrency, there is an incredibly bi-polar character with investors either rushing in or rushing out. There might be an outlier, however. Retail investors have been slowly accumulating small amounts of Bitcoin at an extremely steady rate. The absolute numbers might seem small. But they do add up. And reserves on spot exchanges are dropping alarmingly fast. In this in-depth report, Copper delves into retail's accumulation of Bitcoin and assesses the potential market impact of spot markets.

When cryptocurrency analysts looked back at on-chain data for 2020, the fundamentals began adding up. The growth in Bitcoin's price wasn't accidental. It was by and large because supply was being drained off exchanges.

In some ways, Bitcoin's rally to the new all-time high over \$60,000 was perhaps a speculative mania rush. But up until Tesla announced its massive purchase that pushed prices to these levels, the near \$38,000 mark proved to be based on supply fundamentals, not external hype. Granted, there was some muted but keen interest from larger institutions as the price recovered to new highs and government dwarfed all previous monetary expansion schemes.

If one was to look back at this point in time, say five years from now, they might draw parallels between Bitcoin's two largest booms. The soundings from 2017's rally was that "the institutions are coming." They weren't even considering it. And for 2021, the caption read "the institutions are here." While that might be true to some extent, as far as investments in the store-of-value asset, no other major announcement has come the size of Tesla's.

What has changed to be fact is that Bitcoin and other cryptocurrencies have been classified as viable institutional assets already sitting in the treasury of a Fortune 500 company.

More importantly, institutions from banks to government have accepted the new domain money sits in - cryptocurrency and digital trustless assets. It's no longer an if or when, but how this market evolves and where large players will be involved.

Will other large companies partake in investing in Bitcoin? Perhaps. The real question is, should they want to, or inevitably have to, where are they going to find the supply?

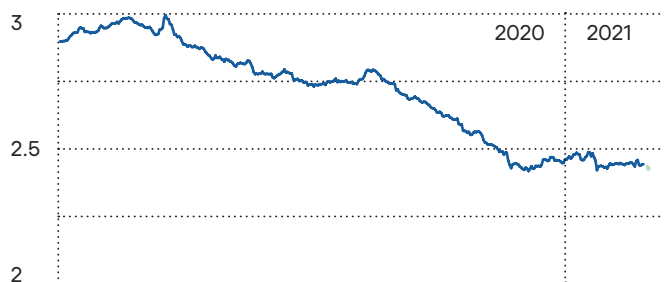
1: 2017-18: The institutions are coming....



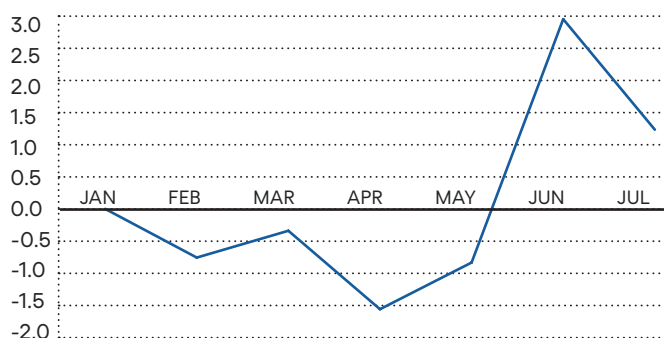
2: 2021: ...The institutions are here?



3: Exchange supply drain from 2020 up until Tesla announcement



4: 2021 All Exchange supply balance (% change vs Jan)





Spot the difference

Hindsight is a beautiful thing. Had investors and analysts been taking note of the declining reserves on exchanges month-on-month since 2020, they would have certainly made incredible returns.

But are there any tell signs for markets moving forward in 2021? Can there be some projection as to trends in supply after Bitcoin rallied only to fall back to month-on-month losses in a row?

It depends where you look. And while Copper isn't one to make projections, some data still stands out and worthy of consideration.

Total exchange reserves have actually increased versus the start of the year (see chart 4 on page 1). What is more interesting is that reserves on spot markets are actually down by nearly 15% from January 2021. Coinbase reserves alone are down by an eye watering 26% (see chart 6).

But since the start of June, spot exchange reserves have seen no change. And while the price of Bitcoin in June and the start of July have seen swings between \$32-38k, the overall average has been \$35k. Markets continue to hobble within this band. Does this indicate potential market equilibrium? Possibly.

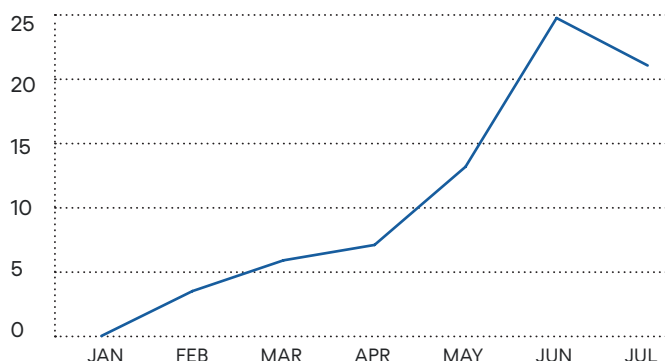
Back of the envelope calculations shows that if the price of Bitcoin from the start of the year increased percentage-wise relative to the reduction in supply on spot exchanges, the price would be around \$35,000. Where it is hovering around today (see chart 7).

Granted, this is an overly simplistic calculation on supply and demand economics with no accounting for traders on the exchanges. But it is an indication that fits at this point in time nonetheless. And the main assumption here is that Bitcoin, at \$29,000 on 1 January was fair value - i.e. before Tesla's purchase announcement was made and where fundamentals predominantly rallied the price of the cryptocurrency.

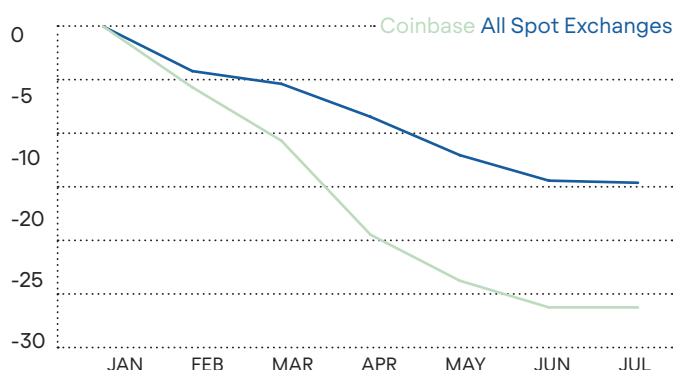
However, let's argue the math is flat out incorrect. The importance of spot exchanges and trends coming from their reserves is of paramount importance regardless. Much like Tesla, large institutions or go-between trading desks will likely tap resources from US spot exchanges, furthering supply pressures.

Of course, there are other considerations. The value in dollar terms of Bitcoin on exchanges is much higher than ever before. The counter argument is that in contrast to 2017, companies weren't laying down \$1.5bn for their own accumulation. The bar is higher in potential cash-flow. But the stock is going down.

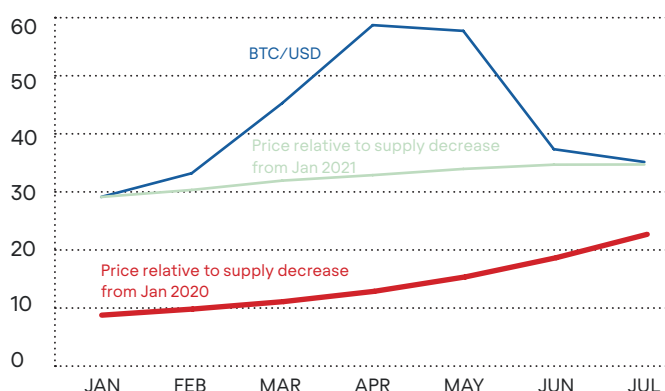
5: 2021 Derivative exchange balance change (% change vs Jan)



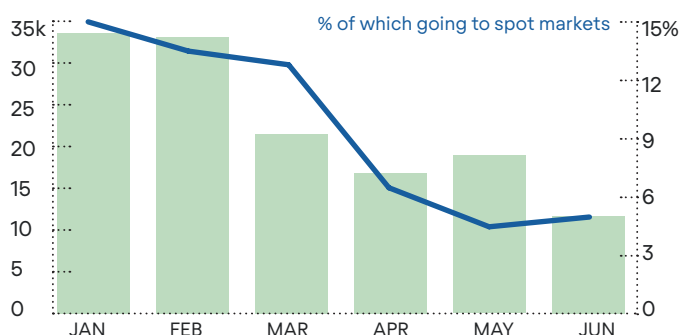
6: 2021 Spot exchange balance change (% change vs Jan)



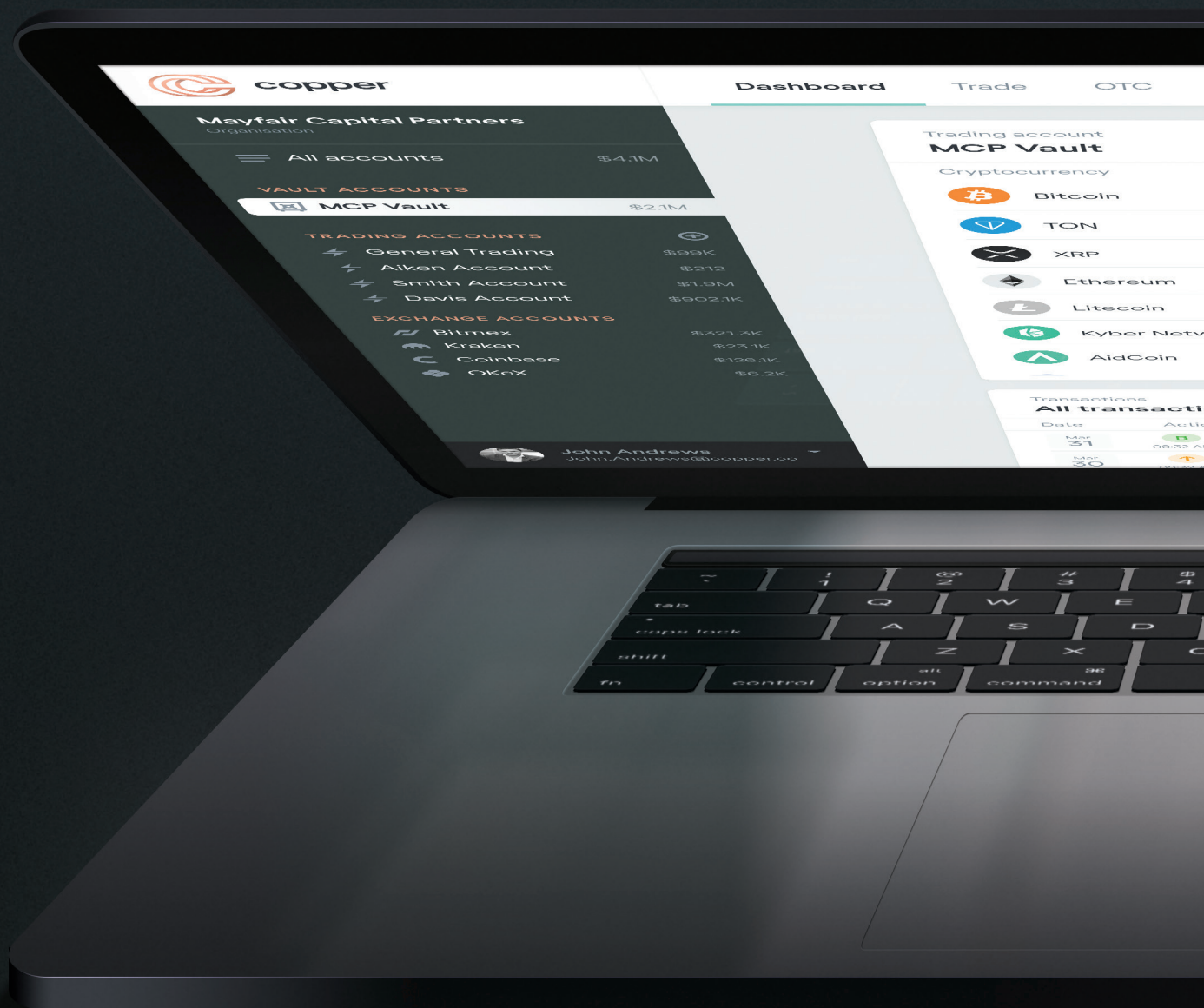
7: Bitcoin Spot Exchange Supply Change Value vs Actual Price



8: Miner Bitcoin flows into exchanges



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