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Analyst Retrospective January 2022

Bitcoin teeters on brink of trendline range

Many investors find that volatility makes for difficult price analysis of Bitcoin. Perhaps this research team can shed some light with a different perspective.

While crypto hardliners continue to stay optimistic by saying "zoom out", the question then becomes by how many years? Investors looking only as far back as 2017-2019 might be biting their nails. In this Copper Analyst Retrospective, we look at multiple indicators and observations over the past year to assess whether or not Bitcoin can turn the corner after dropping nearly 50% from its all-time-high.

Establishing fair value in Bitcoin is one thing. How Bitcoin trades, however, is a completely different story. Bitcoin's price swings seen last year are certainly not for the faint of heart. Investors need an extremely high pain threshold to stay committed. On the flip side, traders, especially those using leverage, are going to need a very small pain thresholds to be able to get in and out as fast as possible when market conditions turn.

While we're not fans of clichés, we will say that the trend is your friend. Not to soften the setback from all-time-highs that Bitcoin is facing, but to actually establish whether or not the cryptocurrency is still trading within its fairly large price range. By observation only, Bitcoin remains within the trading bands (see chart 1).

Despite these swings, it seems that Bitcoin investors might benefit by looking at trends rather than deep price swings. They happen too often and too fast to get a fair market reading. The trend on the other hand seems to be intact – at least for now.

The trendline established was drawn between the low of 2020 and 2021. And had it not been for several confirmations that this line had trading relevance, we would certainly not have highlighted the observation (see table).

Key Trendline events, confirmations between all-time-high cycles

Date	Comment
22-Jan-21	2021 Low
27-Jan-21	Low bounces off Trendline
19-May-21	BTC drops from $43k to $29.8k breaking below Trendline
15-Jun-21	BTC closes on Trendline, continues to drop next day
07-Sep-21	BTC drops from $52.9k to $42k closing on Trendline
01-Oct-21	BTC hits high hitting the Trendline
03-Dec-21	BTC Closes on Trendline
04-Dec-21	BTC Opens on Trendline and drops to low $40k

Should this upward trajectory stay intact, Bitcoin would have to hold above the $38-40k mark based on the drawdown seen in the previous cycle when Bitcoin dropped 32% away from the trendline. As of the start of this year, Bitcoin is already 30% down from the trendline, meaning, either the bottom is now in, or close to potentially breaking the trend entirely.

On the other hand, should Bitcoin continue along this path, accounting for the possible upside of 30% higher than the trendline as seen at its all-time-high, ceteris paribus, the cryptocurrency might very well see the $100k mark toward 3Q22. This research team has asserted the possibility in prior analysis.

But there are other considerations. Many of them.

Top not in?

Bitcoin reserves across all exchanges have now hit a low down 5% from the start of 2021. While that might seem like a small percentage overall, Bitcoin has proved to trade exponentially relative to reserves (see November Analyst Retrospective).

We always like to remind optimists and pessimist alike that Bitcoin is a very pure supply and demand play. Although the mapping of exchange reserves is a difficult task, the data is as transparent as it can be giving fairly good footing as to what is happening on markets.

As things stand, Bitcoin's price has visible upside relative to historical exchange reserves (see chart 2). Should reserves continue their downward trajectory, price might see some significant upside to come comparatively close to previous trends seen in 2021.

Less for sale

Exchange reserves has been a metric favored by this research team. Cryptocurrency reserves indicate the maximum possible available for sale at any given time.

Now, of course, cryptocurrency moves in and out of exchanges and can do so at rapid speed. But, continuing on the theme of this report whereby we look at trends, exchange reserves tell an important story as to the direction markets are taking.

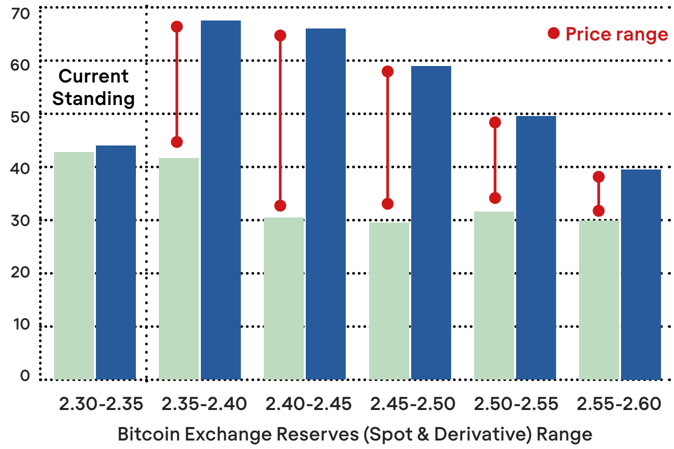
Spot reserves, as we've previously assessed, are a better indicator for market direction than reserves sitting on derivative exchanges.

Traders who are bullish can easily use Bitcoin as collateral on derivative exchanges. This is something we saw happen between November 2020 and May 2021 when reserves increased by 30% as markets rallied to the all-time-high of April last year. As such, derivative reserves can only be used as part of an overview, rather than a definitive market indicator.

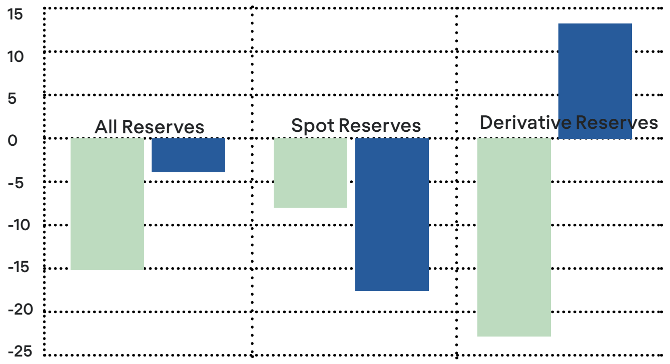
Spot markets on the other hand have been trotting along in a downward trend since March 2020 (see chart 4). January 2021 versus the start of this year saw spot reserves down 18% and 25% down from January 2020.

Meanwhile, stablecoins parked on centralised spot exchanges increased by 410% since last year. Meaning, there is a great deal of gunpowder left on exchanges as market participants wait for some clear direction despite a fair drop in reserves before the end of last year (see chart 5).

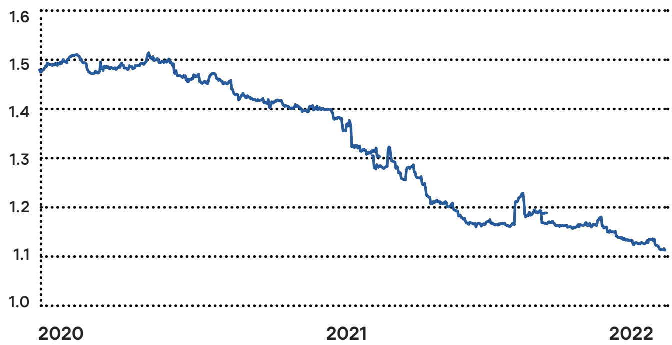
2: Min and Max Bitcoin price based on exchange reserve range ($k)



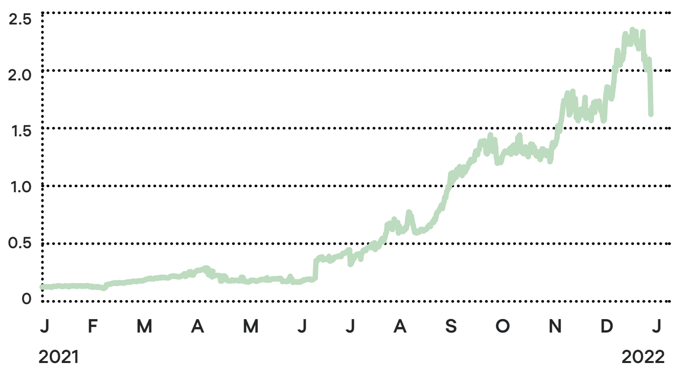
3: % Change in exchange reserves Jan 2020 vs 2021 Jan 2021 vs 2022



4: Bitcoin spot exchange reserves (mn)



5: Spot reserves of Stablecoins (bn)



Retail stacking Sats

The importance of retail cash injection cannot be overstated. Despite a great deal of visible interest from institutions and deep pockets, retail investments continue to be the key market of the industry.

Looking at addresses of only the small holders (0-1BTC) shows that in 2021, investors accumulated nearly 75k Bitcoins over the course of the year. These addresses now crossed the 1mn BTC mark with no year seeing a decline despite price appreciation of the asset (see chart 6).

Over 22% of the new supply, the second highest figure since 2017, was bought up by these small investors alone. Bear in mind, this of course does not (and cannot) account for investments made and held on centralised exchanges.

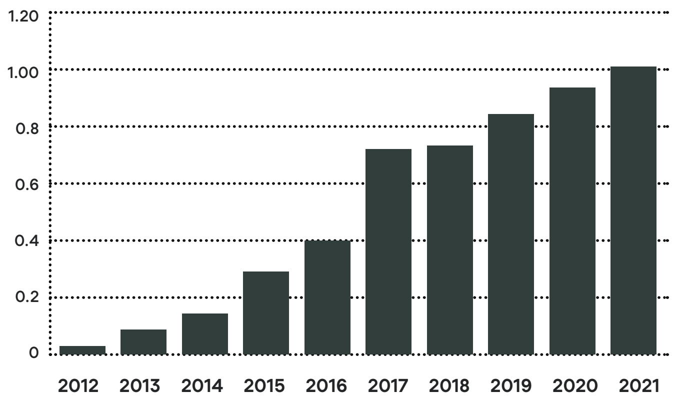
Of course, assessing the percentage of new supply making its way into small investors needs further consideration seeing as every four years Bitcoin's supply gets cut in half. This is why the cost of the acquisition of these holdings at the time they moved into these addresses is of key importance.

Last year saw the cost of the 74k Bitcoins added to these addresses come close to $3.5bn, a record cash inflow beating out 2017 by nearly $1bn (see chart 9). On an annual basis, this would mean an average buy in price of approximately $47k per Bitcoin. This coincides with the average price of the cryptocurrency for 2021. In 2020, both retail cost and price averaged at $11k also. So perhaps not a coincidence at all, but an important indicator of appetite, despite being a fairly small portion of the pie.

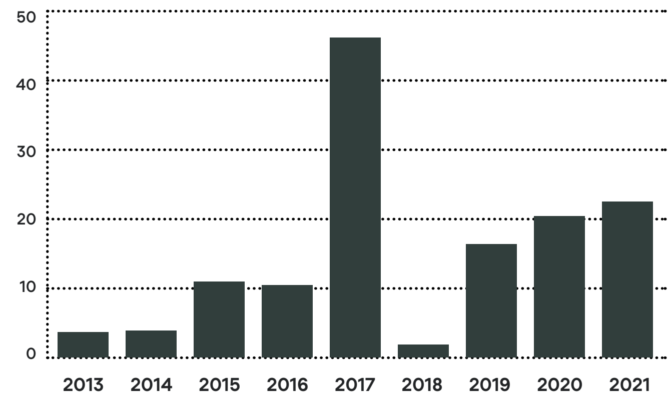
On-chain holdings though represent investors who are comfortable with self-custody. The likelihood is that more retail investors have parked their cryptocurrency on centralised exchanges, with spot markets being a better indicator than traders who Bitcoin that shifts into derivative exchanges.

The differentiation between the two markets is fairly important as it highlights market dynamics of using Bitcoin as collateral in the face of possible liquidations.

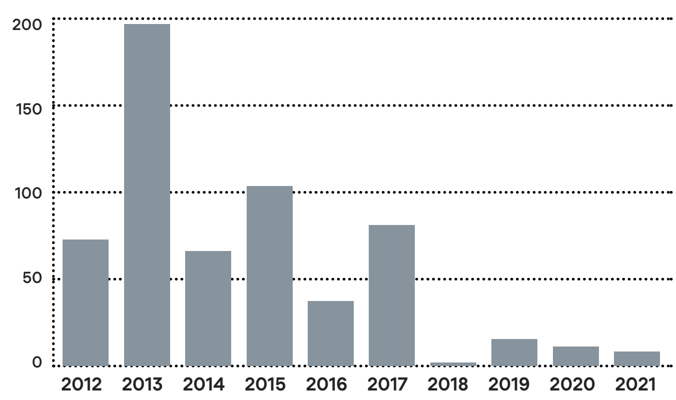
6: 0-1 BTC address holdings total (mn)



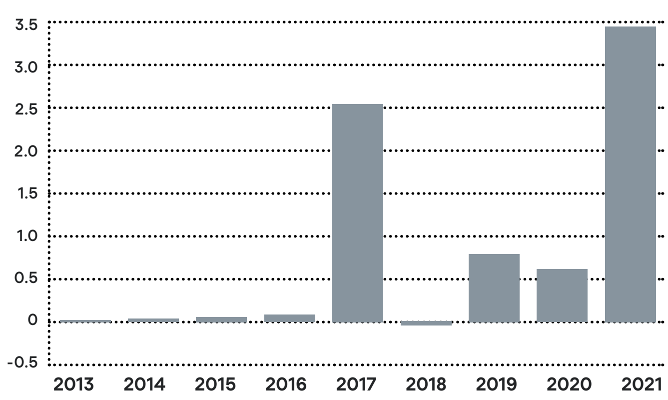
7: % of new Bitcoin supply added in addresses between 0-1 BTC



8: % Increase of Bitcoin in addresses between 0-1 BTC vs previous year



9: Net inflow/outflow cost of acquisition ($bn) in addresses 0-1 BTC



Shorting decline

DeFi markets, well known now to be a primary tool to be able to short markets, offer good insights and correlations to Bitcoin's price.

A quick glance at the outstanding loans for Bitcoin on popular DeFi protocol Compound shows that traders are growing less and less keen on shorting the market (see chart 10).

Also, important to note, however, that outstanding loans for stablecoins are also at a low point, meaning, traders aren't longing the market on decentralised markets either. Still, a useful indicator to gauge market sentiment.

A more traditional indicator is the Relative Strength Index (RSI).

If everyone believes it, is it true?

While we're not incredible fans of technical analysis, there is good merit for their consideration. Reason being, it's a metric that can be seen and assessed by all market participants as they've become standard tools. Everyone can use these metrics for their decision making.

Most popular is the Relative Strength Index that indicates whether markets have been overbought or sold. On the weekly timeframe, Bitcoin often goes into the overbought territory. But on the flipside, it rarely goes below the 30 mark, the number generally used by traders as an indicator that it's time to buy. Last week saw Bitcoin drop to the lowest point since 'Black Thursday' of 2020 (see chart 11).

The institutional paradox

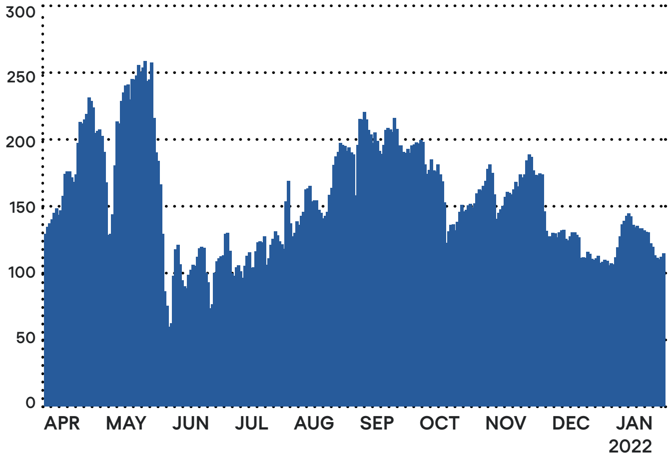
On the one hand, the Federal Open Market Committee (FOMC) meeting held last week that signaled potential quantitative tightening saw global markets - and Bitcoin - dip considerably.

And this week saw that very same policy shift in tone swaying markets right back up (alongside inflation numbers that hit a 40-year high).

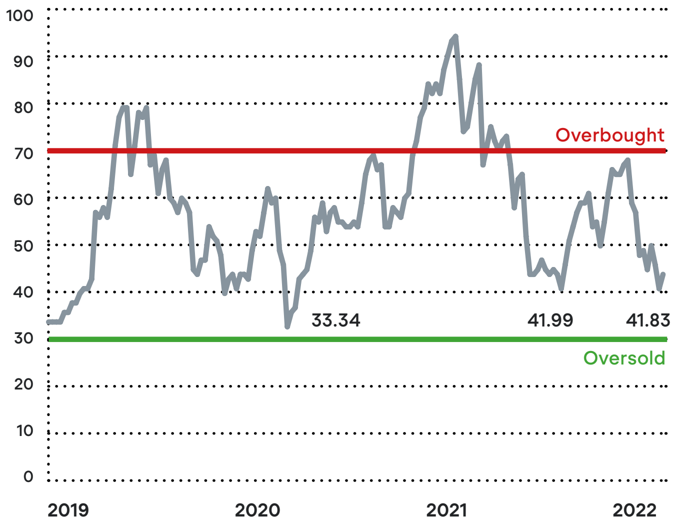
Is Bitcoin now a risk asset that trades alongside traditional stocks? If so, can we finally say that the asset is indeed of institutional class? As far as institutional grade products and treasuries are concerned, one would say that it might not really be the case at all.

Very little has been added since last year. But then again, it hasn't been sold off either at all-time-highs.

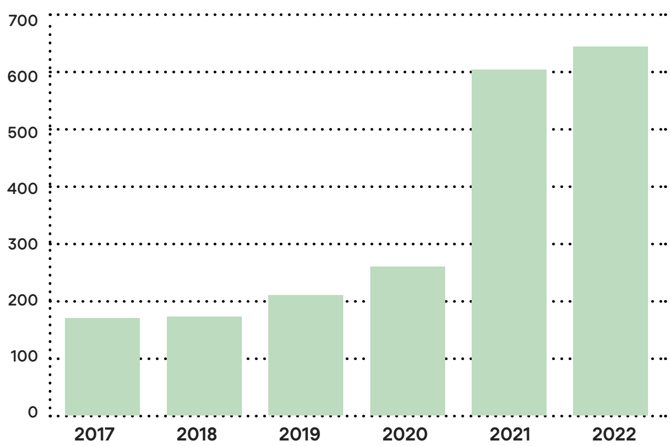
10: Wrapped Bitcoin borrowed on Compound Finance ($mn)



11: Weekly Bitcoin Relative Strength Index (RSI)



12: Grayscale Bitcoin Holdings (k)



Data Sources

Pricing Data:	CoinAPI, TradingView
On-Chain Data:	CryptoQuant, Glassnodes
DeFi:	The Block

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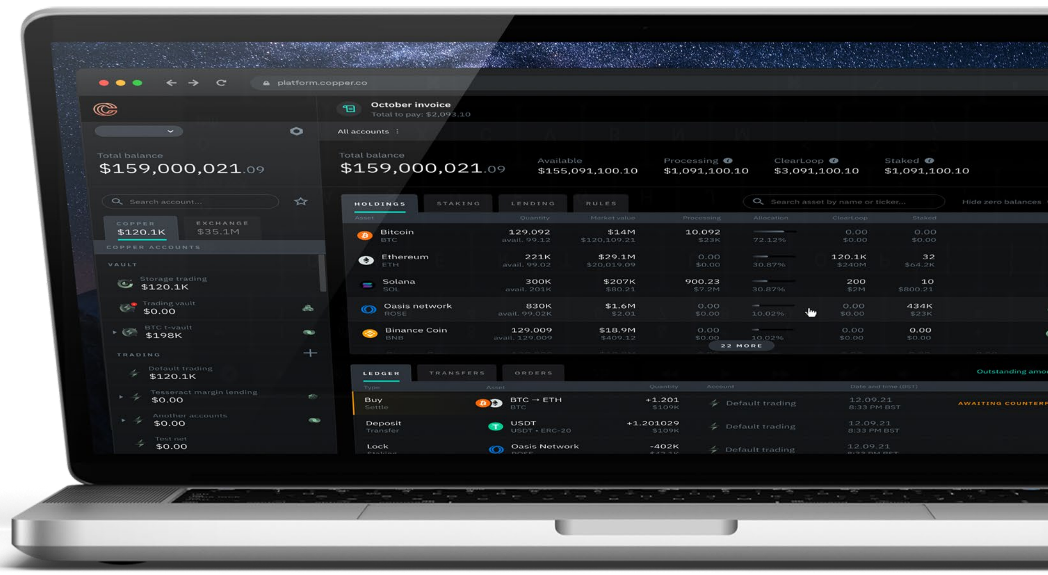

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