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Analyst Retrospective April 2022

Bitcoin price action disconnected from on-chain demand signals

How to value Bitcoin continues to be a seriously debated topic despite on-chain metrics showing a clear direction in demand. Small and medium investors have upped their take of the supply and exchange balances continue to drop. Decentralised Finance markets are showing more parked wrapped Bitcoin and less borrowing of the cryptocurrency too. But, cash and carry plays are only showing lukewarm returns and funding rates remain flat. Copper ties things together in this report.

Volatility makes Bitcoin seem like a complex asset to assess when in reality, it's a pure supply and demand play. There are no cashflows. Its ability to be used in transaction settlement outside of moving in and out of exchanges is a tiny portion still. It ultimately boils down to whether or not there are more enthusiastic long-term buyers than short-term sellers.

On-chain data gives investors a better picture. Traders, on the other hand, are creating copy/paste bots with the most obvious technical analysis metrics. Some win, some lose.

Sharp rise in accumulation

The sharpest visible rise in holdings has happened with medium size investors holding 1-10 Bitcoins. For the first time since 2020, markets have not taken account the increase in holdings (see chart). This begs the question whether markets have new information on the price of Bitcoin outside demand, or there is a significant lag in accounting for reduced supply. Due to US equity market correlation, it's more plausible that it's the latter.

Since the start of February 2022, the addresses increased their size by a whopping 51k Bitcoins in less than three months at the fastest rate and most accumulation seen since the end of 2020, when Bitcoin was still at the $10k mark (see chart). The on-chain cost of these holdings averages to $47k per Bitcoin. This was also the average cost seen by small retail investors in 2021 (see Copper In-Depth Report #18).

In essence, these addresses alone have siphoned off over 89% of the new Bitcoin supply for the period of 1 February till 6 April 2022, when investors began to buy in heavily (see table). And these investors are opportunistic. Observable is that they are more price sensitive and begin to exit before a new price top is formed.

Their current direction and thesis are crystal clear. And these on-chain investors haven't been the only consistent buyers either.

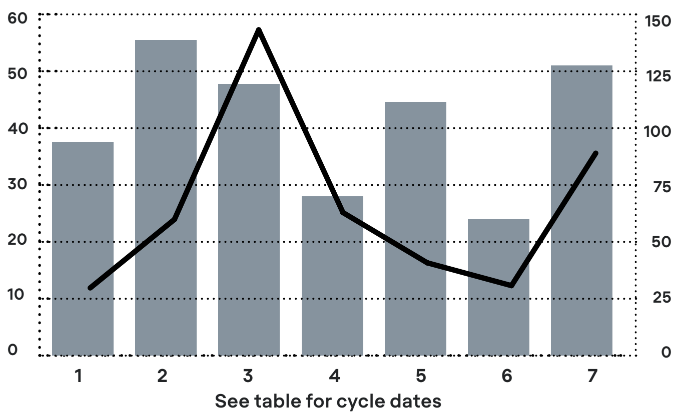
1: 1-10 BTC addresses near all-time-high total (mn BTC)

Cycles where 1-10 BTC addresses increased their position

#	From	To	Increase	Days	% New Supply
1	01-Jan-20	10-Mar-20	37573	69	30%
2	15-Mar-20	05-May-20	55489	51	60%
3	28-Sep-20	04-Nov-20	47779	37	143%
4	21-Nov-20	09-Jan-21	27950	49	63%
5	15-Jun-21	13-Oct-21	44595	120	41%
6	26-Oct-21	19-Jan-22	23914	85	31%
7	01-Feb-22	06-Apr-22	51045	64	89%

#	From	To	Price Start	Price End	Price Change
1	01-Jan-20	10-Mar-20	7,166	7,935	11%
2	15-Mar-20	05-May-20	5,161	8,888	72%
3	28-Sep-20	04-Nov-20	10,779	14,034	30%
4	21-Nov-20	09-Jan-21	18,678	40,642	118%
5	15-Jun-21	13-Oct-21	40,538	56,005	38%
6	26-Oct-21	19-Jan-22	63,082	42,372	-33%
7	01-Feb-22	06-Apr-22	38,493	45,510	18%

2: Accumulation cycles for 1-10 BTC and percentage of new supply absorbed - k BTC (LH-Axis) - % of new supply (RH-Axis)



Adding up, bit by bit

There are numbers of players within the Bitcoin investment space, but none other than small retail holders who self-custody have been so consistent in demand with a long-term perspective.

Since the start of the year, 0-1 BTC addresses increased by nearly 40k Bitcoins. That alone would be 47% of the new supply this year. However, readers of Copper's research already knew this from our previous Analyst Retrospective.

Average daily accumulation from small retail investors kicked off 2Q22 in grand style, hitting a new high of 0.06% (see chart 3).

At average growth rates, and into the next Bitcoin halving estimated in May 2024, current prices would simply imply very little new supply overhang would be left just from these small retail investors. Even at a 0.03% daily change, which compounds quickly, would see retail investors siphon off all of the new supply (see chart 4).

It would be very difficult not to see prices increase. Bitcoin doesn't break supply and demand economics into new theories; it adheres to the most classic of equations. Price volatility, of course, is a different story and still a riddle to traders and investors alike.

But what we can say for certain is that 90% equivalent of the new Bitcoin supply minted in 2022 has gone on-chain to addresses holding 0-10 BTC. There is little new supply overhang from small and medium investors alone.

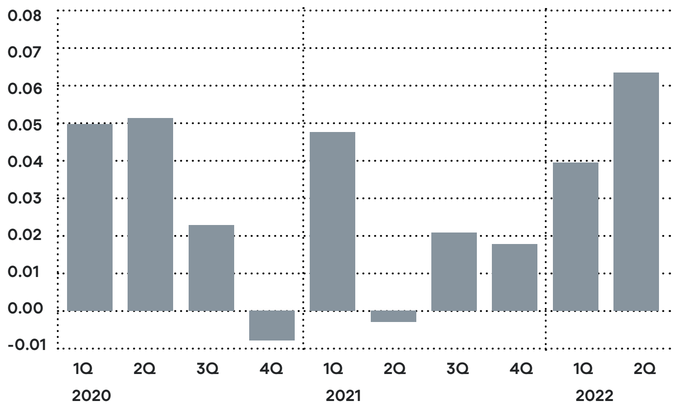
DeFi short sellers take pause

Another metric to keep a close eye on is supply changes on DeFi protocols. The most utility in borrowing wrapped Bitcoin is really to short it on decentralised exchanges. But there has been a growing shift in supply and demand dynamics on popular protocol Compound Finance (see chart 5).

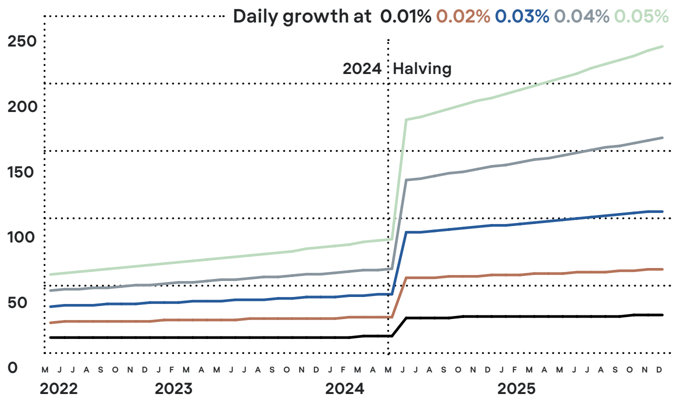
Lending utilisation for wBTC on Compound hit a new low of just 3%. More Bitcoin is making its way into the supply side, while demand has dropped more than four times seen at different cycles during 2021. And it's not that the returns are great by any stretch of the imagination with annual yields standing at less than a 0.01%. The expectation is clearly value appreciation.

Meanwhile, as always, Copper mentions exchange balances in our analyst retrospectives. But as we continuously delve into this topic, so this time we let the numbers speak for themselves (see chart 6).

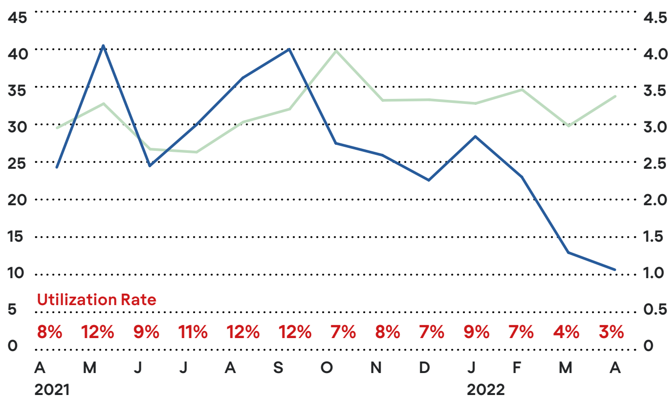
3: Daily average growth rate in addresses holding 0-1 BTC (%)



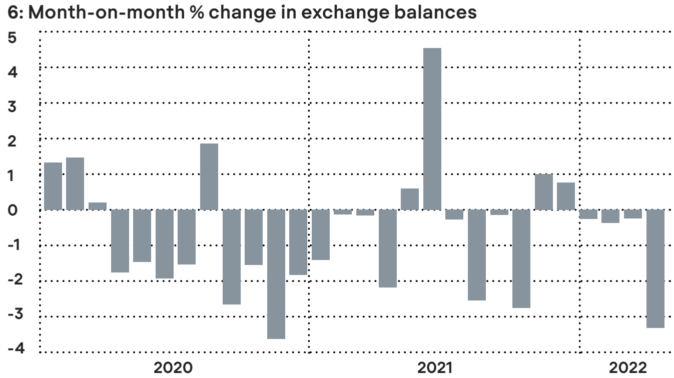
4: 0-1 BTC address accumulation % of new supply



5: Supply vs Borrow of wBTC on Compound.Finance (k)



6: Month-on-month % change in exchange balances



Raw on-chain data source for this report was from Glassnode

State of play: Regulators, cryptoassets and CBDC

Regulators are working together in tackling systematic issues like KYC/AML at a global level. Different implementations of Financial Action Task Force (FATF) guidelines by regulators affect Virtual Asset Service Providers (VASP) the most. Rules like identifying destination wallets, and lowering reporting thresholds for transactions, accompanied by overbroad definitions of VASPs will not only hurt privacy but compliance success.

Crypto companies have arbitraged jurisdictional differences to grow their bases and service a global customer ecosystem. But regulators are coming together to implement global policies. By creating a uniform set of regulations, watchdogs effectively decrease the flexibility of VASPs for domicile.

Central Bank Digital Currencies (CBDC) are a major way for regulators to interact with the blockchain space. Implementing a CBDC comes with various issues like maintaining privacy, wholesale vs retail distribution, ease of implementing sanctions, and interoperability with current financial systems. 87 countries, who account for over 90% of global GDP are exploring a CBDC. The recent US Presidential executive order requesting research into CBDC viability has improved the position of the US. Still EU and smaller countries are ahead of the US in this area. Companies like Consensys and Paxos are leading the charge in working with regulators to create and deploy CBDCs.

Regulators have a two developed a two-pronged approach to cryptoasset regulation. Narratives like energy and environmental cost of Bitcoin mining, and a long list of hacks and exploits set the scene for tighter restrictions on cryptoassets. However, creating a compliance framework in the face of Decentralised Finance (DeFi) won’t be a walk in the park.

Date	Jurisdiction	Event	Description
Mar-22	EU	MiCA passed without PoW Ban	Rules for taxation, Compliance with KYC/AML
Feb-22	Italy	Compliance with FATF and 5AML	VASP should have local entity
Feb-22	Canada	Compliance with Ma-reva Injunction	Asks VASPs to freeze assets
Feb-22	US	Stablecoin Reserves	Stablecoins to have 100% reserves
Feb-22	India	Crypto Tax	Capital gains tax on crypto set at 30%
Jan-22	Russia	PoW Mining Ban	proposed ban on mining and use of cryptocurrencies
Jan-22	UK	Address misleading crypto advertisements	Promotion of qualified cryptoassets are subject to FCA
Jan-22	US-Arizona	Legal Tender	Senator introduces a bill to make Bitcoin legal tender in Arizona
Jan-22	Jamaica	CBDC Pilot	Bank of Jamaica completes first CBDC pilot.
Dec-21	Iran	Mining Halted for En-ergy	Authorized mining is halted to save energy in winter
Dec-21	India	Blanket Crypto Ban Floated	RBI floats blanket crypto ban
Dec-21	France	CBDC Trial	Banque de France completes first phase of CBDC trial
Dec-21	Australia	Licensing for VASP	Crypto regulations to be included in payments overhaul
Nov-21	Finland	Marketing Restrictions	Only registered VASPs can market crypto assets
Nov-21	UK	Taxes on Crypto Assets	HMRC rules updated to include 2% digital services tax
Nov-21	US	Infrastructure bill includes restrictions on crypto assets	Transactions that are more $10,000 to be reported to the IRS
Nov-21	Israel	Licensing for VASP	requires local fintech companies and virtual currency service providers (VASP) to obtain an operating license
Sep-21	El Salvador	Bitcoin is made legal tender	Government makes Bitcoin legal tender, buys 200BTC and creates Bitcoin bonds
Sep-21	US	Lending regulation	SEC issues wells notice for Coinbase’s lending product
Aug-21	UK	Crypto Fraud and As-set Recovery network is formed	Global network to share best practices around asset recovery and fraud
Aug-21	Netherlands	Dutch CB warns against Binance	Dutch CB says Binance is not compliant with local regulation
Aug-21	Canada	Tether trade prohibit-ed	Ontario Security Commission prohibits trading in USDT
Jul-21	Global	IMF warns against crypto	IMF warns against use of crypto as national currency
Jul-21	EU	ECB launches Digital Euro	ECB wants to implement a digital euro that is more efficient than Bitcoin

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