ALPHA BOOK

FEBRUARY 2023

THE BIG BOUNCE

MONTHLY MARKET ANALYSIS – READING TIME: 9 MINUTES
By Sander Kok

Figure 1: The base case: BTC spends most of 2023 between $20k-$30k.

Last issue, I suggested the bear market was losing steam, and that several signs were pointing in that direction, while sentiment was still as terrible as ever. We held onto the majority of our BTC longs from $15,900 and onto our ETH longs from $1200, and opened more around the 17k and 20k handles. The reason we added was the sheer power of the breakout. For any breakout to be convincing enough – in crypto, that is – you do not want to see retests of the previously broken resistance, you do not want to see "confirmation", you want to see the train spurt out of the station with only few traders aboard, leaving the majority on the platform with their bags full of fiat, feeling fooled and eager to hop on later. Which is exactly what happened.

How far can this go? Based on the amount of sidelined capital, farther than most will think, although hopping on here does not offer the best risk-to-reward for the short term. The stations at which our train may well turn around lie between $24k and $35k – with $35k as potential resistance on the monthly and $30k-$32k on the weekly. The latter is the more important one. Round numbers like $30k are typically significant in crypto; they tend to get overrun after which price retreats. If BTC were to convincingly break the $25k level, my take-profit level would be around $30k. If, however, the train breaks down and pulls back to the $19k-$20k area, I would feel confident price will go still lower, meaning I would rather be short than long.

But I don't think that will happen anytime soon. We will probably see $30k before $20k. Macro? Yes, it helps if the dollar index continues to weaken (the path of least resistance is up, though), just like it helps if the S&P continues marching up or stays range-bound. But macro playing along is becoming increasingly less important, as it should with crypto still as small as a lemonade stand that only needs a limited number of local customers to be successful.

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BIG WAVES

Bulls were underwater, but they aren't anymore. They are now making waves, dropping more and more stablecoins in exchange for crypto. This month's issue is rather stablecoin-heavy, with no fewer than three articles discussing stablecoin flows. The reason is simple. These flows have been moving the market – they have been and will be.

In our market analysis, Sander Kok discusses the Bitcoin breakout he had forecasted. Will it stick? He thinks so. His string of articles continues with the already mentioned reports on stablecoin flows and ends with a short investigation into why BTC has been breaking out specifically on Fridays. What's that all about? Will it change?

This issue's tech article is an introduction to the layer-2s you've been hearing about. ZK-proofs, optimistic roll-ups, and validiums should help Ethereum scale. What will the layer-2 landscape look like a year from now? Will Ethereum finally become accessible to the teeming millions?

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KEY INSIGHTS

- We remain bullish. The sheer power of BTC's breakout spells continuation. The train left the station with only few traders aboard, leaving the majority on the platform with their bags full of fiat, feeling fooled and eager to hop on later. This means there should be enough sidelined capital to get a shot at $25k-$30k. We expect the $25k resistance level to eventually break, opening up the road to that level. If, however, the train breaks down and pulls back to the $19k-$20k area, we would feel confident price will go lower, meaning we would rather be short than long.

- Macro will remain important to crypto prices, but less so than in 2022. Even the largest crypto, Bitcoin, is still small as a lemonade stand that only needs a limit number of local customers to be successful.

- Last year, many newcomers, including those from traditional finance, moved out of crypto, leaving patronage to natives that are less likely to sell, as was proven by the latter's reluctance to do so under the worst of circumstances in November and December. We remain long-term bullish for the above reason and also for the potential of the deep-pocketed newcomers coming back once macro conditions improve.

- Since the current financial regime and a looming recession are not conducive to risk assets, our base case is for BTC and ETH to stay range-bound in 2023. While the outer limits of the range would be $16k and $32k, with exceptionally good momentum taking the price to the $35k monthly resistance, BTC should spend most of its time between $20k and $30k.

- Our bearish scenario is BTC falling back to the lows, but after seeing its strength at the lows under extreme conditions, we expect it will require a cataclysmic event for these to be broken. Here opens up an asymmetry since the bull scenario is not similarly capped. While new lows require a cataclysmic event, new highs merely require a conducive macro environment. With a looming recession and the threat of persistent inflation, such an environment seems unlikely to materialize at this point. Still, it is not nearly as unlikely as a cataclysmic event.

- Helpful, in this respect, would be gold continuing its impressive reclaim of lost ground into new highs. BTC should continue to benefit if gold keeps running. If that were to happen, Bitcoin would likely get back its lost narrative of digital gold. If this were to play out just as most capital goes short BTC for deeming the run-up merely a bear market rally, we would see these shorts getting squeezed. This would likely lead to more upside as positive price action reflexively feeds the retrieved Bitcoin-as-digital-gold narrative. This scenario seems far away, but it only requires two elements: gold going up and enough "bear rally" shorters.

- Retail investors remaining absent is more helpful than not if you are a long-term BTC or ETH investor. If retail does not stay away, investors would start spreading themselves thin over more retail-friendly (that is, gambler-attractive) projects. In the best and also most probable scenario, retail only returns once BTC's or ETH's all-time highs are broken.

- In the above scenarios, ETH would outperform BTC as its own narratives takes hold, one of which will be "ETH is better than BTC because it is deflationary as well as productive."

- BTC has been breaking out mostly on Fridays in the past month. While the underlying dynamics may have changed by now, the crypto casino that never closes is still appealing to traders from traditional finance who have an itch to scratch as their casino closes. As long as risk assets do well, that itch is more likely than not going to be scratched with longs.

- Liquidity returning, as evidenced by the stablecoin ratio, is good for crypto, and one flow of stablecoin supply may attract other, perhaps truly new flows from those who feel comfortable enough longing crypto in sufficiently liquid conditions.

- The Exchange Flow Monitor shows billions of stablecoin inflow in January, particularly during weekdays and US and European office hours, making this seem like a large western TradFi entity buying (or a large entity returning to market-making).

- ZK-proofs, optimistic roll-ups, and validiums will help make Ethereum accessible. All of these technologies have their advantages and trade-offs. We expect the layer-2 landscape to be more diverse and advanced a year from now, and to be in even higher demand. Value will accrue to both the layer-2 and the main chain, as these will both benefit from each other's success and drive each other's demand. Sharding could kill layer-2s' most important value proposition, as it makes Ethereum cheaper to use, but sharding could also lead to increased demand, making layer-2s more appealing.

PERFORMANCE CHECK: HOW DID WE DO?

Accountability isn't the most poetic of words, but we think crypto needs to hear it more often. Each month, we look back at the calls from our previous issue. So far, we are the only research company to do so, hoping more people in the space will follow.

- We are glad to hold onto most of the BTC we bought at an average of $15,900.
- We were correct to see signs of bear trend exhaustion and happy we did not wait for less uncertain times to place our bets.
- We should not have sold one-third of our position at the top of the range.
- Volatility returned with a vengeance, as we had forecasted. This was indeed, in part, due to news around GrayScale, which did not unwind its funds, as we had predicted. (Also see the image on the right-hand page.)
- The January BTC low was at $16,400, a bit higher than the $15,900 we had expected.
- There were indeed few convinced sellers left. The following turned out correct: "[Bears] are waiting for bad news to hit – which may not happen or may not have as poor consequences as expected, increasing the probability of having to buy back in at a higher price."
- Gold indeed helped Bitcoin as the precious metal outperformed the market, providing tailwind for its digital brother.
- There were no Mt. Gox unlocks on January 10th – we were wrong there. Also, worries about these unlocks have taken a back seat for now.

We published this chart in last month's issue, saying "this chart spells opportunity for options traders." We were right. Just one week after publication, volatility spiked as worries around GrayScale and others alleviated. We also seem to have been right claiming "the next big price move will likely dictate the trend for the coming weeks or months."

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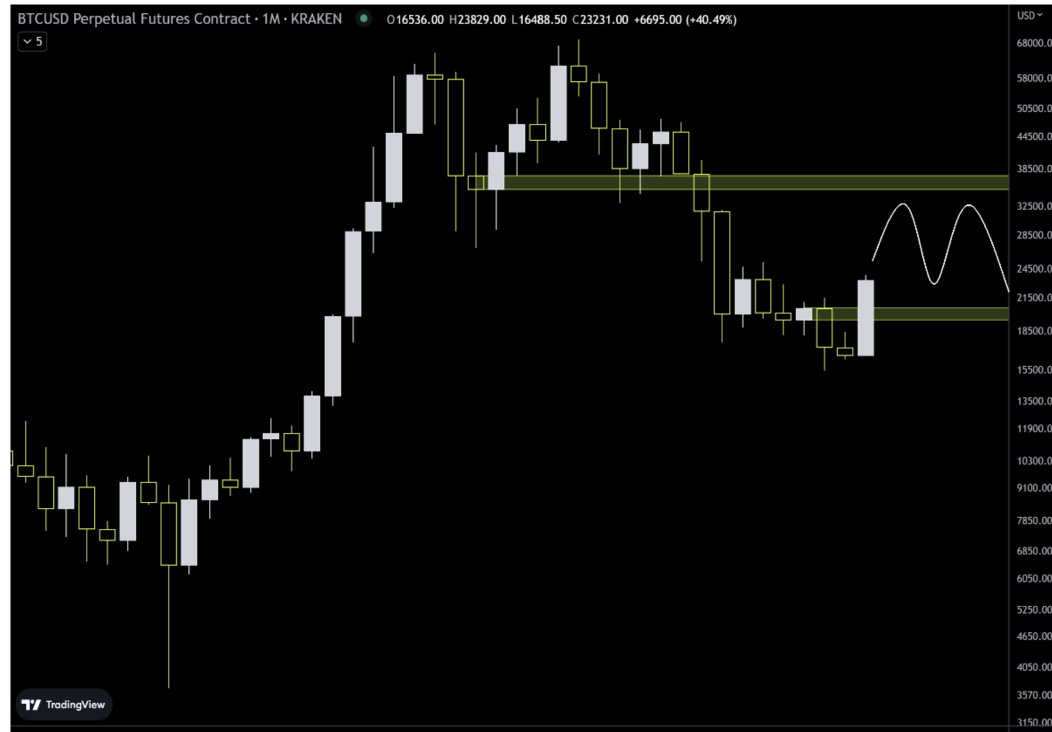


Figure 1: The base case: BTC spends most of 2023 between $20k-$30k.

Last issue, I suggested the bear market was losing steam and that several signs were pointing in that direction, while sentiment was still as terrible as ever. We held onto the majority of our BTC longs from $15,900 and onto our ETH longs from $1200 and opened more around the 17k and 20k handles. The reason we added was the sheer power of the breakout. For any breakout to be convincing enough – in crypto, that is – you do not want to see retests of the previously broken resistance, you do not want to see "confirmation," you want to see the train spurt out of the station with only few traders aboard, leaving the majority on the platform with their bags full of fiat, feeling fooled and eager to hop on later. Which is exactly what happened.

How far can this go? Based on the amount of sidelined capital, farther than most will think, although hopping on here does not offer the best risk-to-reward for the short term. The stations at which our train may well turn around lie between $24k and $35k – with $35k as potential resistance on the monthly and $30k-$32k on the weekly. The latter is the more important one. Round numbers like $30k are typically significant in crypto; they tend to get overrun, after which price retreats. If BTC were to break the $25k level convincingly, my take-profit level would be around $30k. If, however, the train breaks down and pulls back to the $19k-$20k area, I would feel confident price will go still lower, meaning I would rather be short than long.

But I don't think that will happen anytime soon. We will probably see $30k before $20k. Macro? Yes, it helps if the dollar index continues to weaken (the path of least resistance is up, though), just like it helps if the S&P continues marching up or stays range-bound. But macro playing along is becoming increasingly less important, as it should, with crypto still as small as a lemonade stand that only needs a limited number of local customers to be successful.

With institutional adoption in 2020 and 2021, macro became more important to BTC's price than ever, but last year the suits moved out, leaving the lemonade stand with local customers that are less likely to leave. Their reluctance to leave became apparent in November's price action. The theory is as hopeful as it is simple. It explains why BTC's correlation to macro has been dropping off; confirms the bottom may well be in; and, most hopeful, the capital that apparently moved out may well move back in when macro conditions improve, as they eventually will. There is much more potential upside for Bitcoin investors if that vast reservoir of unallocated capital is not yet included in its market cap.

To be clear: macro will remain important to crypto prices. Only less important than in 2022. I remain bullish. Bitcoin's monthly chart is sheer poetry and rhymes with 2015's and 2019's. Let's not get ahead of ourselves, but one cannot help but wonder: could this be it? How often did we not imagine seeing vague traces of that messianic creature called Decoupling in crypto winter's snowy fields? Maybe it finally came. Going by the charts, our poetic friend seems set to give us some more stanzas.

The financial regime has changed, of course. All other Bitcoin bull runs took place in a more conducive monetary environment. So, yes, while hawks have air superiority over doves, the financial landscape looks bleak for Bitcoin bulls. A run to all-time highs remains unlikely until that changes. My base case, therefore, is that the two largest crypto assets, Bitcoin and Ethereum, will remain range-bound for at least another year.

I expect an eventful year for traders and, thus, the range to be wide. Barring surprises – and, to be fair, crypto always surprises – the outer limits lie at around $16k and $32k. BTC would spend most of its time between $20k-$30k. Exceptional momentum would take the price to the $35k monthly

Figure 2: Bitcoin's halvings are a powerful meme that smart investors should take seriously because the moronic multitudes take it seriously.

resistance, while a recession could invite a quick liquidity grab under the lows of $15.5k.

Bitcoin ranging is my base case. What is the bear case? Well, considering Bitcoin's strength in the face of progressively worse news over the past few months, I believe, as mentioned, that the bottom is in. It proved that even in the worst of circumstances, people do not want to part from their Bitcoins at

Figure 3: Old gold's sharp reversal does Bitcoin a service. If gold break all-time highs, BTC should benefit.

a price lower than the current bottom. At this point, I am confident only a cataclysmic event would bring us new lows.

Now, is the upside similarly capped? This is where it gets interesting. The answer is no. Where, in my thesis, exploring new lows requires a cataclysmic event, reaching new all-time highs merely requires a conducive macro environment. With a looming recession and the threat of persistent inflation, such an environment seems unlikely to materialize at this point, but it is not nearly as unlikely as a cataclysmic event. This brings me to a not-that-unlikely scenario.

It is time to dust off the old gold chart (Fig. 3).

After a nearly eight-month sell-off, gold reconquered all lost ground in merely three months. These sharp reversals below all-time highs have a high likelihood of leading to more upside. Now, what happens if gold keeps running? Which crypto might benefit? (Hint: it's orange.)

If this were to happen, Bitcoin finally has a narrative again. After being severely oversold due to macro correlation traders and crypto market-specific fears related to the insolvencies of Three Arrows, Voyager, Celsius, Alameda, FTX, and Genesis, most of the fear has now dispersed. This fear dispersal provided the most important cause for the recent runup, but Bitcoin is still looking for a narrative. What will happen if the last leg of this bear market rally ends just as a new narrative – an old one really: Bitcoin as digital gold – takes hold on the back of gold's success?

What we will get is a growing number of traders going short, as they deem the recent moves to be nothing more than mean reversion. The consensual nature of shorting a bear market rally would mean funding rates will go evermore negative, causing instability to the advantage of long-term bulls and opportunistic stop hunters. When this scenario comes to pass during the early stages of a new narrative, the subsequent short-squeeze will be a joy to behold and likely lead to more upside as positive price action reflexively feeds the retrieved Bitcoin-as-digital-gold narrative.

This scenario may seem far away from where we are standing now, but not much is needed to bring it closer. Bulls just need gold to continue going up

and enough shorters to fuel the necessary squeezes to bring back that strongest of all Bitcoin narratives: that it *always resurrects*. By now, every investor, sidelined or not, knows Bitcoin is the phoenix of finance, and the narrative gets stronger each time it rises from its ashes.

It might actually help that retail is absent. For the above scenario to materialize, we don't want investors spreading themselves thin over other, more retail-friendly (that is, gambler-attractive) projects than Bitcoin and Ethereum. For Bitcoin and Ethereum, and the broader crypto market in the long run, it is best if retail stays away and only returns once the all-time highs get broken, as would be typical retail behavior. The teeming millions will be more interested in the next 100x dog coin anyway, or in zombie layer-1s with skillful marketing teams. Moths and flames. We won't need them this cycle. May the suits walk into the light, though.

Now, what can we expect from ETH in the above scenario? History suggests it would outperform BTC by a large margin, and I see no reason why this time would be different. Granted, ETH would have to beat BTC on the latter's bull narrative, which logically does not make sense. But I think it does if you consider Ethereum's own narratives would begin to take hold in people's minds as BTC makes a run and then redistributes. One of these will be "ETH is better than BTC as it is deflationary as well as productive." Furthermore, all eyes will be on crypto again – on all of crypto – once one of its constituents catches the imagination. Reflexivity will kick in, as it did before. We have seen this play out cycle after cycle.

I am not saying this scenario will materialize anytime soon, but it could, and as I said, not much is needed. It may seem unlikely, but this scenario is much, much less unlikely to materialize than people think. As a trader and investor, I look for asymmetries, and this is, I think, a fine specimen.

ALL ABOUT FRIDAYS

BTC has been all about Fridays this last January (Fig. 4). The positive price action during that day of the week has been far from shallow, with pumps of 2%, 14%, 9%, and 3% from trough to bottom. Continuation during the weekends was not always a given, although one thing has been true – Thursday dips provided excellent buys.

It's anyone's guess if this pattern continues in February. That will mainly depend on whether the month will be as good for bulls as January. We tentatively believe it will. But beware, the reason for the Friday pumps may have changed. While it is still true that, on Friday, TradFi speculators move themselves and their recovered risk-appetite to the global crypto casino that stays open 24/7, we cannot say the same about the short-term risk-to-reward that gamblers seek. (The word "gamblers" is appropriate because if you still have that itch after trading for five days, you likely are one.) Bitcoin, the digital asset TradFi'ers are most likely to touch, had been severely oversold going into January. Now that prices have bounced, we may see less long interest unless other risk assets keep going up, dragging crypto risk-appetite higher. We will see. As long as risk assets do well, it makes sense for TradFi'ers to come get that high beta at the best casino on earth while their pinstripe-suited friends wait for the Monday morning gong. ◆ Sander Kok

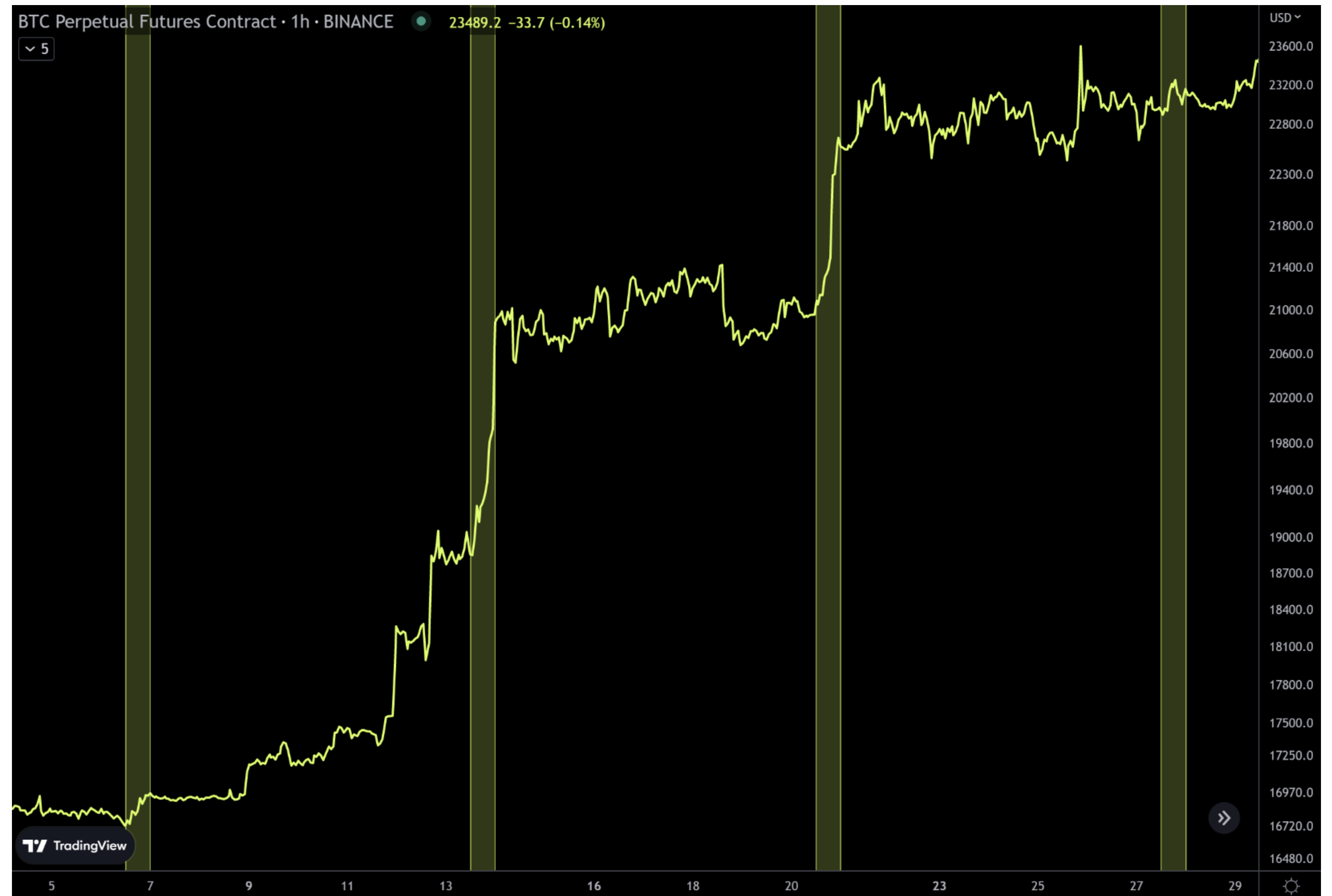


Figure 4: In January, Friday meant up for BTC.

THE STABLECOIN SUPPLY RATIO

One of the more interesting charts right now is the stablecoin supply ratio. This needs to get higher, Twitter analysts say. I disagree. You want this to go lower as that means stables are getting sold for crypto, meaning the ratio goes down due to the cryptos being bought, but you also want to see the exchange supply replenished. That is exactly what has been happening in the past three months (Fig. 5). But we have to be careful: the significant decreases in this ratio over the past 6 months were mainly caused by insolvency fears following the high-profile blowups of Three Arrows Capital, Celsius, Voyager, and FTX, among others (Fig. 6). Market makers feared for their stables and retreated from exchanges. So it only makes sense that this capital comes back once the dust has settled, as it now has, as evidenced by the spikes since November in Fig. 5. But this "new" stablecoin buying power is, first of all, not new, and secondly not going to be used for directional betting; the majority is just old money returning to earn money market-making. That said, liquidity returning is a good thing, and one flow of stablecoin supply may attract other, perhaps truly new flows from those who feel comfortable enough longing crypto in sufficiently liquid conditions. The dynamics are made clear in the chart below (Fig. 6). ◆ Sander Kok

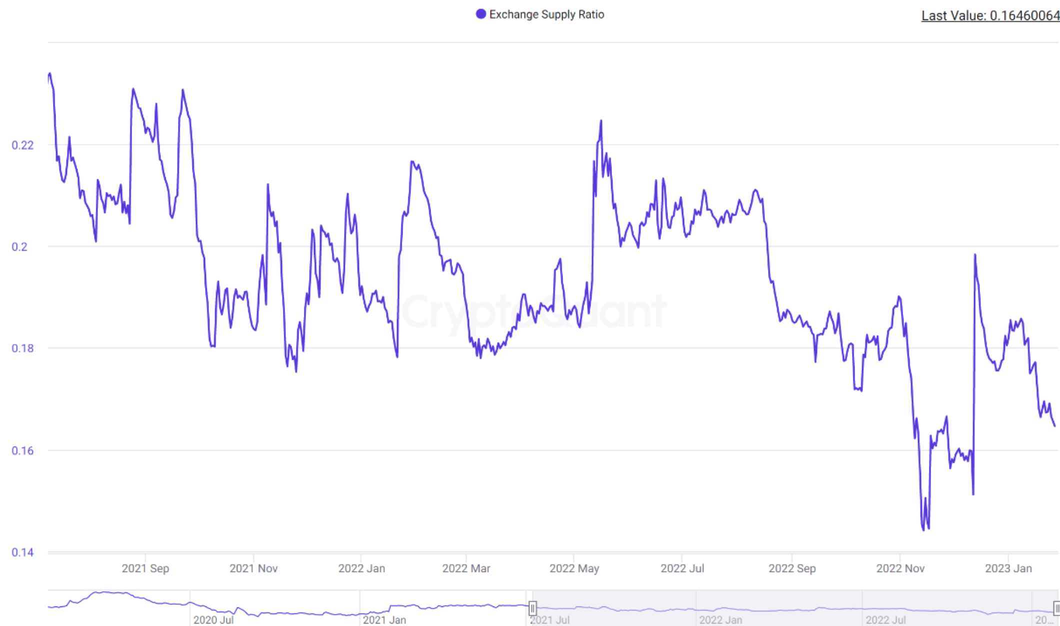


Figure 5: The exchange supply ratio for stablecoins, which is the stablecoin supply on exchanges divided by its total. More stablecoins on exchanges means more buying power, but there are some caveats. (Source material: CryptoQuant.)

Figure 6: An annotated, zoomed out version of the same chart, describing the dynamics of stablecoins on exchanges.

DRY POWDER BEING LOADED?

The chart on the right shows the coin reserve – the total value of all BTC divided by all exchange-held stablecoin reserves. Low numbers mean high buying power.

The chart shows the ratio went up quite a bit in December and the first week of January, while BTC hadn't pumped yet. With the ratio returning to levels not seen since Three Arrows Capital blew up, we have evidence of the market having shaken off most of its worries. This occurred within the space of 6 weeks. Now may not be the best time to climb aboard for traders with a short time horizon, but those waiting for confidence to return may see their patience rewarded as this chart indicates more upside for Bitcoin. The ratio will decrease as BTC has

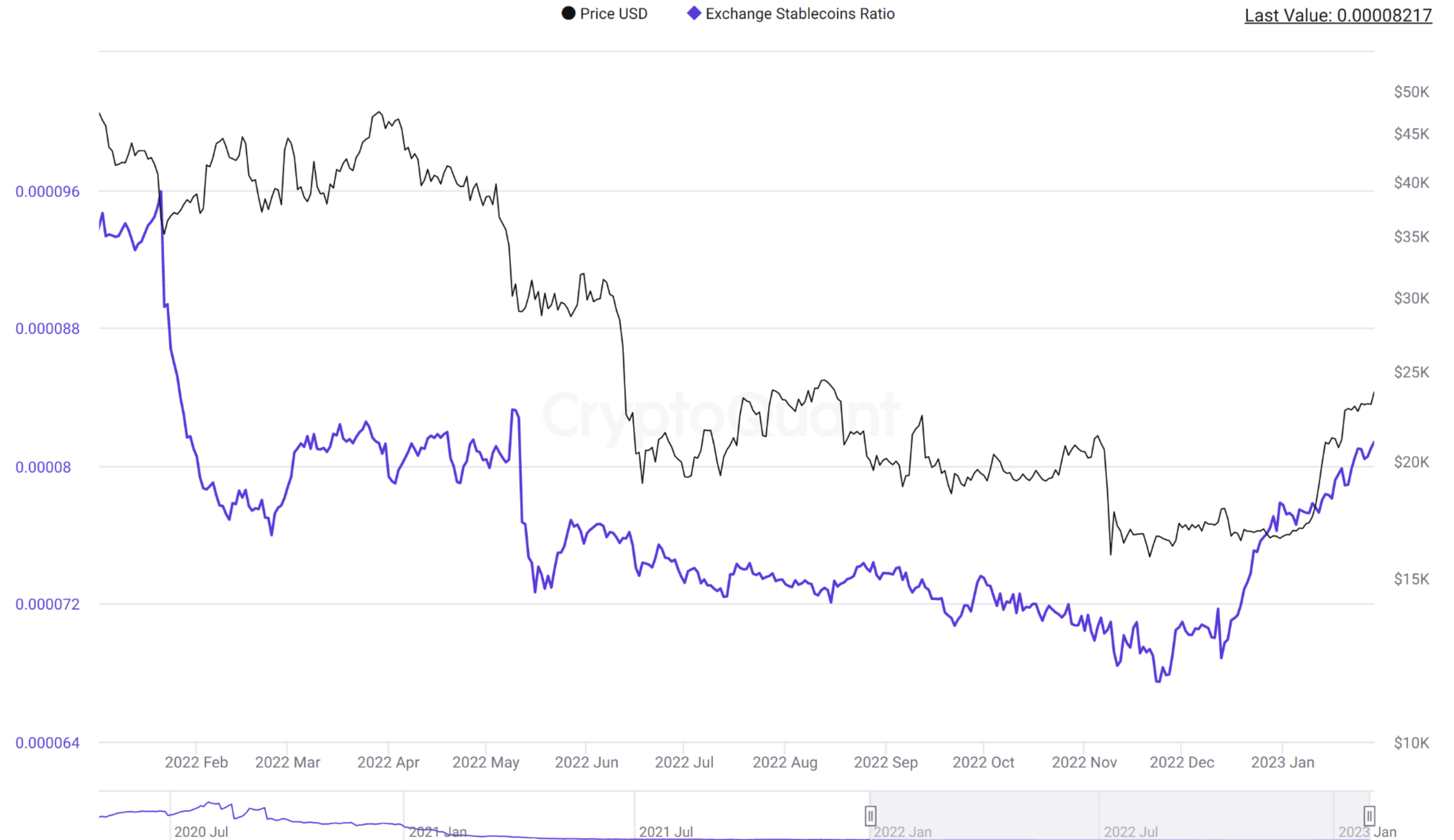


Figure 7: The Exchange Stablecoin Ratio is the total value of BTC divided by all exchange-held stablecoin reserves.

Figure 8: The Exchange Flow Monitor shows no significant stablecoins outflow from exchanges in December and a large inflow only since January – particularly during weekdays and US and European office hours, making this seem like a large western TradFi entity buying.

been putting in higher prices, and stablecoin influx typically follows price increases. This is all the more true when exchange insolvency fears alleviate.

Let me explain with a parable. After years of irrational exuberance, the price of an egg is $1, and there are only 100 million dollars available on egg exchanges around the world. As the macroeconomic climate changes, the egg price collapses to $0.22. At the same time, traders begin to fear that egg exchanges aren't the safest place to put their dollars, so they move them out into their own wallets. (Let's call these exchanges eggs-changes because why not.) There are now fewer dollars on eggs-changes to buy eggs with, even though they have become cheap. But after a while, when bad actors are washed out, traders regain their confidence and move half their initial deposits back. The ratio should therefore go down, but as enough traders view this development as bullish, they

begin to buy eggs, driving the price up. $EGG is now worth $0.44. Due to these dynamics, the ratio did not go down, as you would expect, but went up.

Something similar happened with Bitcoin if you believe the stories. But there is something odd. Why did the ratio skyrocket from mid-December and the first week of January *before* BTC went up? The ratio should have come down as stablecoin reserves flowed back into exchanges while BTC remained range-bound. There is only one explanation: the stablecoin supply actually went down, despite stories of massive influxes during weekdays from what seemed like big entities, looking at their footprint (Fig. 9).

We have gotten so used to analysts apodictically explaining charts, as if, to them, all data is clear-cut and the future is certain. But sometimes it is best to say: "I don't know what caused this inconsistency." Every investor should know that a good question can be much more productive than a good answer. ◆ Sander Kok

Figure 9: An AI-rendered image of Ethereum becoming accessible to the proletariat.

ETHEREUM FOR THE PROLETARIAT

AN INTRODUCTION TO SCALING ETHEREUM

Scaling Ethereum is one of crypto's holy grails. The reason is simple. Blockchain technology remains merely promising for as long as it doesn't scale. We want to be able to use the most popular network in crypto often, and we can't. It is ironic – not to say tragic – that Ethereum's adoption is hampered by its own popularity. Confirmation times increase when the network gets congested, and transaction fees shoot up. Intellectually challenging layer-2 solutions such as ZK-proofs, optimistic roll-ups, and validiums have emerged to address this. In this primer, we will examine these and see what the layer-2 landscape should look like a year from now.

ZK-PROOFS AND OPTIMISTIC ROLL-UPS

ZK-proofs (Zero-Knowledge proofs) are a type of proof that allows verifying a statement without revealing any information beyond the fact that the statement is true. This has important applications in areas such as privacy-preserving transactions, secure multi-party computations, and identity verification since a prover can convince a verifier that a statement is true without revealing any information about the statement itself.

In the context of scaling Ethereum, ZK-proofs are touted as the latest and potentially best solution, and the relevant projects' high valuations in funding rounds reflect this. Ethereum's current architecture is limited in terms of the number of transactions it can process per second, and with the network growing in popularity, as we have established, this limit becomes increasingly problematic. The problem will become smaller with ETH 2.0, but its roadmap

is long, and we are not there yet, so there should be ample time for solutions like ZK-proofs to win market share.

How it works: ZK-proofs prove the validity of a transaction without storing the entire transaction history on the Ethereum blockchain. Instead, a small cryptographic proof is used to verify the transaction's validity, reducing the network's load and allowing for faster and more scalable transactions. The implementation of this technology should increase the number of transactions processed per second and reduce the load on the main network.

How does this relate to optimistic roll-ups, such as Optimism and Arbitrum? Both ZK-proofs and optimistic roll-ups bundle multiple transactions into a single (therefore more efficient) transaction and send it to the Ethereum network. The main difference between the two is that ZK-proofs provide a way to verify the validity of the transactions without revealing any information about the transactions themselves, while optimistic roll-ups bundle transactions for scalability purposes but do not provide the same level of privacy and security. Optimistic roll-ups are also simpler, which is an advantage if you want to be fast.

WHICH ARE BETTER?

Both ZK-proofs and optimistic roll-ups have their own advantages and trade-offs. If privacy and security are top priorities, ZK-proofs seem to offer a better solution, while optimistic roll-ups seem a better choice if scalability is the primary concern. Optimistic roll-ups seem to be the better choice for most projects and users, as they are simpler than ZK-proofs. The latter involves a complex cryptographic process that adds overhead to the verification process. This can slow down the transaction and limit scalability. Optimistic roll-ups, on the other hand, do not have this problem and can process transactions more quickly; thus, they are better for scaling.

Moreover, optimistic roll-ups are more compatible with existing Ethereum infrastructure, making it easier to integrate with existing apps, while ZK-proofs require more specialized infrastructure and may have compatibility issues.

STARKWARE'S VALIDIUMS

A third scaling solution is offered by StarkWare and is called validiums. These are a kind of ZK-proof that, like regular ZK-proofs, do not reveal details about the transactions themselves. Again, whether validiums are better than existing solutions depends on the use case. They have the potential to offer improved scalability, efficiency, and privacy compared to other ZK-proof solutions, but at this point, it is too early to speak with any certainty, as the technology is still relatively young. StarkWare's technology also promises cheaper transactions than its competitors, which may not seem important now that these are already low in price, but this will change when Ethereum becomes popular again.

A YEAR FROM NOW

A year from now, the layer-2 landscape is expected to be more diverse and advanced. The demand for faster and more efficient transactions is typically tied to Ethereum's popularity, which in turn depends on its price as in crypto popularity and price often rise and fall in unison, but the mere availability of cheaper and more private solutions should also drive demand. In 2023, the focus will also be on improving interoperability between different layer-2 solutions, so that seamless movement between them becomes possible, unlocking liquidity that is currently fragmented.

If DeFi, NFTs, or gaming takes off on Ethereum again, we will see layer-2 solutions play a much more significant role than before. We will probably also

see more attention for those that are purpose-built for a certain use case. IMX, for example, uses validiums and is built for gaming and NFTs. If it becomes successful, other purpose-built chains may follow.

WHERE WILL VALUE ACCRUE?

In terms of where the most value will accrue – on the main chain or on the layer-2 – it is likely that both will benefit. The addition of layer-2s can help alleviate some of Ethereum's scalability and cost issues, which in turn can make it a more attractive platform for builders and users, while layer-2s can offer their own value propositions, such as increased privacy or lower transaction costs, which should help drive their growth. As the implementation of ZK-proofs and optimistic roll-ups can bring benefits to both Ethereum and the layer-2, value will likely accrue to both (in different ways).

Now, what about sharding? Shouldn't the cheap transactions promised by the Ethereum Foundation on the ETH 2.0 roadmap kill the various layer-2s' main value proposition? Perhaps, but it is unlikely. While sharding is expected to make transactions cheaper on the Ethereum network and would therefore compete with layer-2s in this area, it may not address all the needs of complex dApps and high-volume decentralized exchanges. These would still benefit from the faster settlement times and improved scalability offered by layer-2s. Also, while sharding lowers the cost of transactions on the Ethereum network, it could also lead to increased demand for decentralized applications, which would drive up the number of transactions and potentially increase the cost of using the network. This increased demand could make layer-2 solutions even more appealing, as they would offer a way to reduce the cost of transactions and improve the user experience. This is, of course, the optimist's story. The pessimist might say that sharding natively competes with layer-2s on their main value proposition – cheap transactions – and perhaps that is enough to make them less useful. How this turns out may depend largely on the order of events. Sharding has begun, but its full implementation will take years. In crypto, a lot can happen in the meantime, as we have seen time and time again, especially when new technology hits the market. ◆ grypto digital team

UPCOMING EVENT RISK FOR FEBRUARY

February 1

FOMC

Federal Open Market Committee: Statement, Rate, and Press Conference

February 3

UNEMPLOYMENT & EARNINGS

US Unemployment Rate Released (previous: 3.5%; expected: 3.6%)
US Average Hourly Earnings m/m (previous: 0.3%; expected: 0.3%)

February 7

JEROME POWELL SPEAKS

The Fed chair speaks at the Economic Club of Washington

February 14

PPI

US Producer Price Index Print (expected: 0.5% m/m; core 0.1% m/m)

February 15

RETAIL SALES

Retail sales (previous: -1.1%; expected: -1.3%)

February 16

PCE

US Core PCE Price Index m/m. This is the Federal Reserve's primary inflation measure (previous: 0.2%; expected: 0.2%)

February 22

FOMC MINUTES

FOMC meeting minutes are disclosed

February 24

PCE

PCE price index (previous: 0.3%; expected: 0.3%)

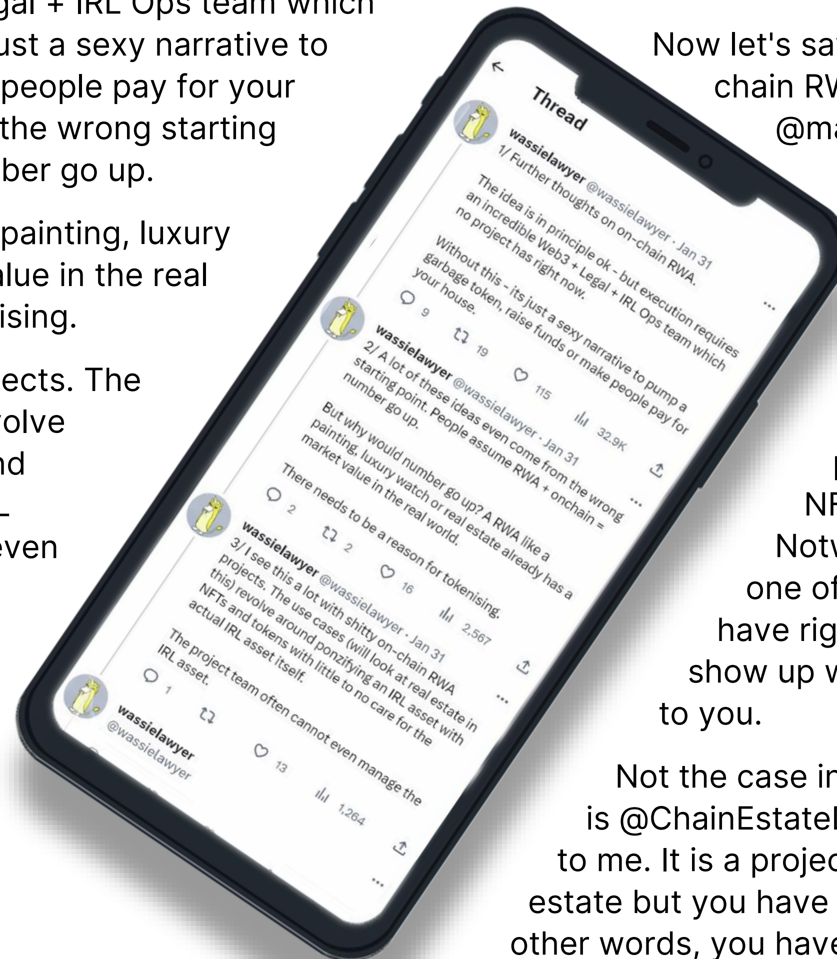
CRYPTO TWITTER SAYS

"Further thoughts on on-chain RWA. The idea is in principle ok - but execution requires an incredible Web3 + Legal + IRL Ops team which no project has right now. Without this - it's just a sexy narrative to pump a garbage token, raise funds or make people pay for your house. A lot of these ideas even come from the wrong starting point. People assume RWA + onchain = number go up.

But why would number go up? A RWA like a painting, luxury watch or real estate already has a market value in the real world. There needs to be a reason for tokenising.

I see this a lot with shitty on-chain RWA projects. The use cases (will look at real estate in this) revolve around ponzifying an IRL asset with NFTs and tokens with little to no care for the actual IRL asset itself. The project team often cannot even manage the IRL asset.

Now let's say you are doing it for the 'right' reason. The reason is normally 'liquidity'. Now there is another issue - why would there be more liquidity? The answer I often get is 'oh because we are fractionalizing it'. This carries securities risk.



Securities risk is easier to manage when you are dealing with fully on-chain assets. How do you think a regulator is going to respond if you start tokenizing say real estate which needs to be registered to an owner? They would say 'Yo this is an unregulated REIT'.

Now let's say you jump through that hurdle. Why is your on-chain RWA better than the IRL version? Take @mattereum for example. Very cool concept and it legally works imo. But in order to jump through the hoops to make it legally work, the benefits of NFT-ing it are reduced. Now don't get me wrong, I am impressed by their asset passport (and how they have 'wrapped' reps and warranties). But when it comes to the piece of land itself, it is simply an option to purchase title. Because it is difficult to turn the NFT into title in a compliant manner. Notwithstanding that, I would consider them to be one of the leaders in this space because you actually have right of recourse against the land itself. I.e. You can show up with the NFT and ask for the title to be transferred to you.

Not the case in many other cases. One example I have looked at is @ChainEstateDAO, because I think a bunch of ads promoted it to me. It is a project that allegedly allows you to 'invest' in real estate but you have zero right of recourse to the real estate itself. In other words, you have given money to the project team to buy

properties in their own name on the basis that they will give you part of the cash flow because 'trust me bro'. No comments on the fact this project literally has a 'buying competition'. So on top of securities risk, you have incredible counterparty risk. You can have a Mattereum style OTP (which has access to asset but doesn't generate yield for holding the NFT) or a Chain Estate style 'trust me bro' 'REIT' that generates yield but has no recourse to asset.

Now what if we blended the two a bit (which I have seen some projects purport to do) where there is a bit of 'trust me bro' and a bit of recourse to assets? Let's pretend securities laws don't exist and you can issue tokens from a 'DAO' that give you cash flow / governance. What actually happens if the DAO votes to have the project team removed and the RWA transferred to 'the DAO'? Is there a right of recourse that the DAO has against the asset holding vehicle (which is often owned in the name of the founders)?

Normally there isn't one. There is no automatic mechanism that compels the transfer of the RWA to another entity (controlled by the DAO) when there is a DAO vote on the matter. You can't do this on-chain, because title transfer requires interaction with legal infrastructure. Hell, even if you had an automatic mechanism that worked, you would need a management company for the asset that is divorced from the asset holding vehicle because who is going to manage the asset if the 'founders' are removed?

So for this to all work, you would need at least (1) an independent custodian that holds the RWA, (2) legal infra which binds the custodian to the token holders, (3) a securities law compliant structure, (4) process for replacing the management company ... It is an issue I have spent many hours meditating and consulting with clients on.."

—wassielawyer (@wassielawyer)
Wassielawyer calls himself "a hentai anime penguin in a suit that once spent another life as a restructuring, insolvency and special situations lawyer."

COLOPHON

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Junior Analyst	Luis H. Borges
Junior Analyst	0xKyle
Junior Analyst	Sven Kamieth
Designer	Ashik Arifa
Intern	Zach Miller

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Role	Name
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CSO	Sander Kok
CTO	Vasile Cojusco
Community Manager	Karsten Lenterman
Marketing Manager	Henry O’Byrne
Blockchain Technical Advisor	Lawrence Ka Chun Hui
Advisor	Bert Rigter

We’re hiring! Shoot a message to sander@captur.fi if you believe you can write the best analyses out there.