

Crypto Market Update - sometimes it only needs a spark to lid a fire_____

There has been a lot of talk about crypto winter and Bitcoin collapsing and disappearing in nirvana. While the recent market sell-off is indeed painful it is my desire to share some interesting feedback and thoughts with you.

We all remember when the first Bitcon ETF (BITO) got launched in October of last year. It was well covered on all social media platforms since BITO attracted more than \$1bn in the first two trading days – the most successful launch in the history of the ETF industry.

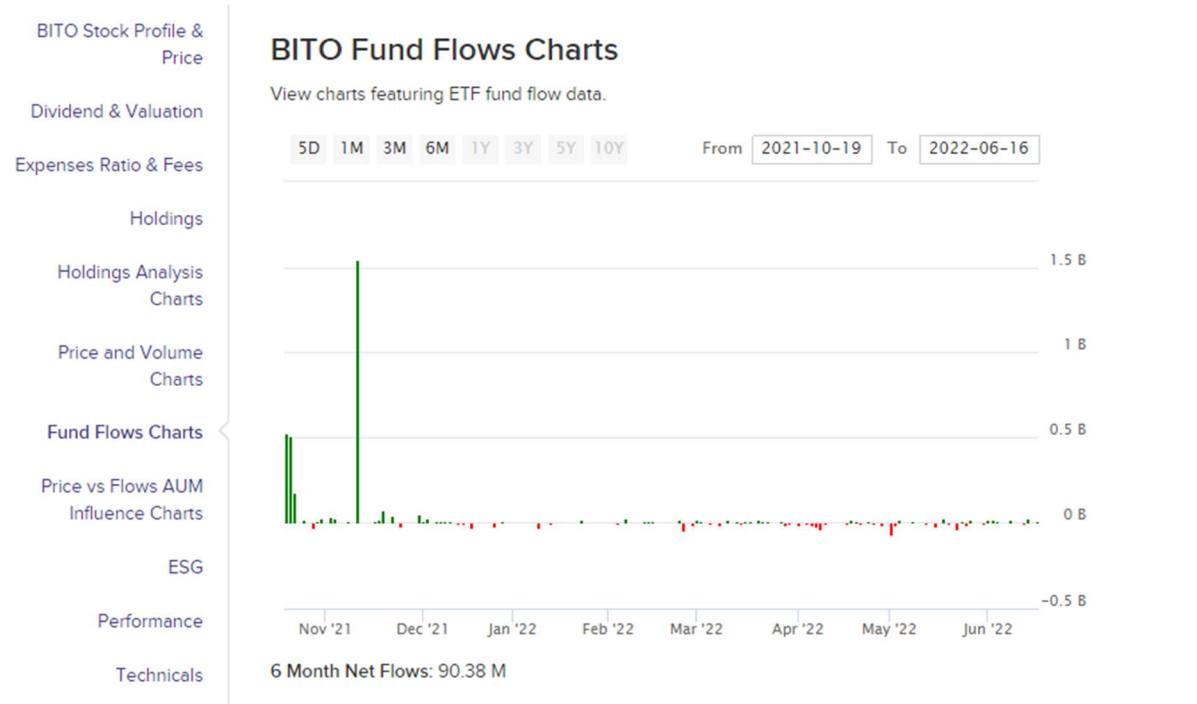
In the hype of the ETF launch Bitcoin reached its all-time high just a few days later on November 10th 2021 at \$68’991.85. Just on the same day BITO saw a significant inflow of \$1.5bn on one day! (see chart below). Good news, right? More Bitcoin price appreciation to come?

An ETF can issue new units in various ways. If new money flows into an ETF the market maker issues new units which can then be freely traded. However, if someone what’s to short an ETF but there is no paper available new units will be created too, in a process called “create-to-lead”. In the latter case new units are being issued but the investor’s intention is to sells those units short. This is what happened on Nov. 10th 2021 when one big investor or a small group of investors shorted BITO worth \$1.5bn. Please remember this happened at the top of the Bitcoin hype. Someone took a huge risk to short the hell out of Bitcoin.

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BITO ProShares Bitcoin Strategy ETF

Price: \$12.95 ↑
Change: \$0.23 (1.81%)
Category: Currency
Last Updated: Jun 17, 2022



Source: etfdb.com and SerMont AM

June 2022

Only shortly thereafter the price of Bitcoin sold off to the levels before the news about the launch of BITO in September 2021. As things went on and the price of bitcoin weakened the self-fulfilling prophecy started. Momentum traders, CTAs, Hedge Funds, Algo trading programs etc. discovered the weak momentum and start selling too. Sometimes it only needs a spark to lid a fire. Please see Bloomberg chart below.



Source: Bloomberg, SerMont AM

Since the newly launched BITO ETF is buying future contracts and not bitcoin token there is one more thing to consider. Usually, commodity futures are trading in contango which means prices for contracts farther in the future are more expensive than shorter term contracts. BITO is buying the first and the second month contract and shortly before they expire, they are being rolled in the new more expensive contracts. In the process a negative roll-yield is being generated which was about 10% p.a. when BITO got launched in October 2021.

If an investor, however, sells the ETF short the negative roll yield works in his or her favor generating a positive contribution. In addition, if the contract size is large enough it can move the spot price of bitcoin as the experience has shown.



The Bitcoin Futures used in the BITO ETF are trading on the Chicago Mercantile Exchange CME. Using current data, the ETF has the following holdings:

Holdings as of 6/21/2022

Weight	Ticker	Description	Exposure Value (Notional + GL)	Market Value	Shares/Contracts
--	--	TREASURY BILL	--	\$299,339,751.00	300,000,000
--	--	NET OTHER ASSETS (LIABILITIES)	--	\$365,242,805.10	365,242,805
10.91%	--	CME BITCOIN FUT NON-EQUITY INDEX 26/AUG/2022 BTCQ2 CURRENCY	72,536,250	--	690
29.43%	--	CME BITCOIN FUT NON-EQUITY INDEX 24/JUN/2022 BTCM2 CURRENCY	195,562,500	--	1,875
59.64%	--	CME BITCOIN FUT NON-EQUITY INDEX 29/JUL/2022 BTCN2 CURRENCY	396,358,800	--	3,792

Source: proshares.com

Comparing this data to the open interest on CME reveals the following...

Description	Last	Chg	Settle	Time	Bid	Ask	Open Int	Volume
1) Spot				6/21				
2) Jun22	↑20395	-465		15:21	20380	20390	6403	4043
3) Jul22	20395	-510		15:21	20390	20415	5945	1864
4) Aug22	20380	-645		15:19	20430	20490	835	108
5) Sep22				6/21	20485	20540	228	

Source: Bloomberg BTCX1

The future holdings off the BITO ETF are making up 2/3 of all “open interest” in the 2nd month contract and about 1/3 of all “open interest” in the front month contract. These are huge numbers and suggest that in the future investors will have to keep a close eye on the holdings of the BITO ETF since the underlying futures can move the Bitcoin spot price in one or the other direction. Size matters in the futures market.

The recent crypto market’s woes have also been linked to idiosyncratic risks such as the failure of the Terra stable coin which was supposed to be pegged 1:1 to the USD. Shortly thereafter the Celsius network, a platform which offered high rates of return for cryptocurrency deposits stopped customer withdrawals. Just for the record, our **Alteritas Blockchain SONICCX Fund did not have any exposure to the forementioned token.**

While we think that the higher than usual market volatility will continue for the next weeks and maybe months, we are encouraged to see what is being built on Bitcoin through the lightning network - a layer 2 protocol allowing for faster transactions between participants. The same goes for the smart contract

platforms Ethereum and Cardano just to name two protocols. Further, Ethereum is planning to switch from its energy intensive proof of work to proof of stake consensus mechanism in August which is expected to save 98% of energy.

Within our Alteritas SONICCX fund we have eliminated Solana because of two outages in May. It seems the protocol has grown to fast too quickly. A solid blockchain network needs not only to be fast and cheap but also decentralized, reliable, and stable for great user experience. In addition, we have increased our cash position to 30% in April due to unfavorable market environment. The money will be deployed again carefully over the next few months.

Thank you for your attention and the trust you have placed in us.

Kind Regards,

Volker Zaworka