Friday, November 26, 2021

MacroTactical Crypto #5
Nobody will ever tell you to sell

A mistake that traders and investors often make is the failure to analyze or understand both cyclical and structural drivers of markets. People get caught up in the structural narrative and forget the cyclical one. In a structural bull market, you can still have eye-watering down cycles that bankrupt many bulls. Traders and investors that are solely focused on structural bull or bear factors will tend to miss the trees for the forest.

This was an epic problem in 1999 as the market focused on the structural bull internet story and failed to see the cyclical risks. It manifests in many other markets too. Another example is that many investors have a permabear stance on the Canadian dollar because of the structural problems in the Canadian economy, but they fail to recognize that in the reflationary and monetary policy up cycles, the Canadian dollar performs very, very well. The best trades are when cyclical and structural factors align, like crypto in 2020/2021.

But not crypto in 2022. Sure, the structural bull story is intact, but **the cyclical factors driving crypto higher since March 2020 have now turned bearish**.

It feels rude right now to even utter something bearish about crypto because so many people have become so intellectually, financially, and philosophically committed to the space. I feel naughty, or even mean-spirited being bearish. Still, I am trying to ignore those feelings as I think there should be more agnostics focusing on the fact we are in a bad part of the cycle for crypto here and the corrections could be epic. I'm not a hater—I'm happy to be bullish or bearish price in crypto—and I'm structurally bullish crypto and Web3, just like you probably are.

If you're a maxi with a 10-year time horizon, cycles don't matter, but if you want to sidestep Crypto Winter 2, you could do worse than reducing risk as the halving cycle and the monetary policy cycles both turn bearish.

Halving cycle is bearish

Every ~1200 days, the reward for mining bitcoin transactions is cut in half. Each halving has been followed by an epic bull run, then a super cold period, then another bull run in anticipation of the next halving cycle. Chart:

Bitcoin performance over the three halving cycles

The BTC and crypto hype machine is 10X more powerful than the 1999/2000 internet hype machine. Nobody is ever going to tell you when to sell. It is borderline verboten for anyone in crypto to even utter a bearish word. Keep that in the back of your mind. Every story you ever hear is going to be bullish.

Make sure you can survive winter.

Note in the chart on the last page that each bull run is less impressive than the one before. As market cap rises, it becomes impossible for the next wave to outperform the last. This is why the Plan B model residual keeps getting bigger. The halvings are mathematically less important (lower overall impact) and the law of large numbers kicks in. It's easier to grow from 3 billion to 3 trillion than it is to grow from 3 trillion to 3 quadrillion. Obviously.

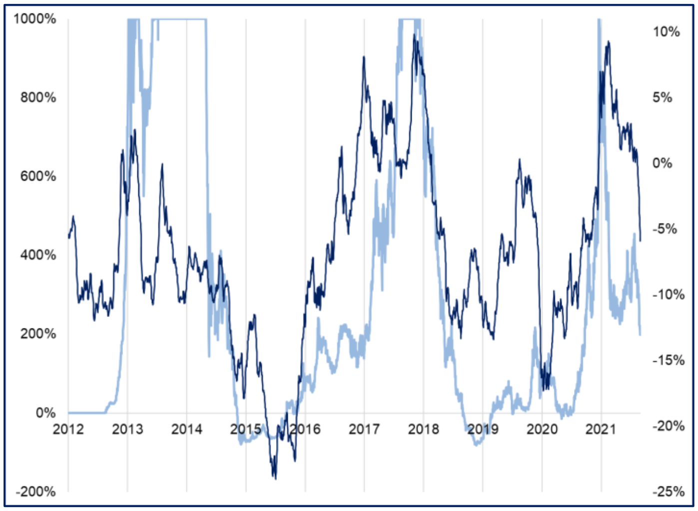
Fed cycle is bearish

One of the big reasons Paul Tudor Jones and many others were screaming from the rooftops about bitcoin in mid-2020 was because the US just embarked on the greatest monetary policy experiment in modern history. That was the start of a massive bullish cyclical environment for crypto. Now, the experiment is either over, or its on a prolonged pause. The dollar debasement story is dead for now as USD moons, the Fed accelerates taper, and global central banks slow printing.

I have no doubt that the next round of money printing will be more ludicrous than the last and that will probably take crypto to new all-time highs at some point in 2023 or whatever… But for now, one of the biggest inputs into the bull crypto thesis is on hold. And all those new TradFi types that have just bet their careers on crypto will not be able to ignore the turn in the Fed cycle as easily as non-macro crypto maxis.

The most understandable way for me to show the Fed cycle and its impact on crypto is to show EM currency performance vs. BTC. When the Fed turns hawkish, the USD rallies fastest and most aggressively against emerging markets. Here is the YoY performance of bitcoin vs. EM currencies:

BTC YoY performance vs. JP EMFX Currency basket YoY



Left y-axis is bitcoin, I capped it at 1000% so the chart remains legible. Right y-axis is JP Morgan EM FX index

Obviously, I could be wrong. The nu variant could lead to another massive round of money printing, for example. More likely, though, $69k BTC was a major maximum for crypto prices and some sort of winter is around the corner. I doubt it will be as bad as the last winter, but you never know.

Thanks for reading. Click here to sign up for crypto updates (free) or my macro daily ($490/year) or both.

Current trade (From MTC#4):

Short ETH at 4210. Take profit 3010. Stop loss 4902.

I will track the trade ideas and report on performance once per quarter.

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