

World Computer vs. Digital Gold

MacroTactical Crypto #20



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Today's note is 2,500 words (10-minute read)

Market and Trade Ideas Update

Lots of weirdness in crypto last week as “The Great Decoupling” captured everyone’s attention. I say “meh”. I’ll discuss that later.

My stop loss in SOL was triggered and that idea is dead. I stuck to the original buy the dip in SOL parameters as laid out months ago in [MTC #11](#) and that cost me.

If you plan to buy a dip, then you recalibrate when spot nears your level, you are most likely reacting emotionally to price action. This is what people on Wall Street jokingly call a “good until close” order. As in, “The order is good until the market gets close to it... But then I will get scared, and panic cancel it.” I try to always stick to my plan, and in this case my plan was wrong. But that’s fine. Being wrong is part of trading.

News flow on Solana hasn’t been amazing with the [shutdown April 30](#), and the recent [clock glitch](#) looking particularly noobish. I will leave it alone for now and move on to other ideas. Solana’s hiccups and Ethereum’s oft-delayed merge and sporadically insane gas fees highlight

in IRL the theoretical tradeoffs between scalability, network stability, cost to transact, security, and centralization.

My bullish BTC view is tiny in the money (30300 entry) but I'm not white-knuckling that since it's more of a swing trade / investment time frame. I want to scale into medium-term BTC longs from 30k down to 20k. Again, this is outlined in MTC #11.

The World Computer vs. Digital Gold

Lately, I have been writing about my preference for BTC over ETH. Here is the reasoning in a nutshell:

- The BTC use case is increasingly clear. It is a liquid hedge against fiat debasement. This use case obviously works in both directions and as the Fed tightens, you would expect BTC to fall. My view is that it will outperform other risky assets from here as underlying demand for what is still a fairly new asset class will be strong and if you wait until the next Fed easing cycle to buy BTC, you're going to be paying \$50,000. Better to scale in on the way down than to chase it back up, in other words.
- The ETH use case is somewhat clear (World Computer), but it has many competitors. The promises of DeFi, Web3, and GameFi are going to be much harder to keep given the complexity of the use cases and the massive level of fraud and grift attached to all these projects. Not to mention the distorted incentive structures (monetize first, build later).
- Crash risk in ETH due to auto-liquidation during times of downside crypto stress is not zero. A majority of DeFi collateral is ETH and the [SBF Magic Box theory](#) looks a bit more on point every day. [MTC #19](#) has a full write-up on why I think ETH has more crash risk than BTC.
- As crypto users age and absorb the lessons of the serial crypto bubbles and bubblettes, they will become less risk-seeking. They are learning that absurd payouts are accompanied by grotesque levels of risk. They will buy fewer lottery tickets, farm less yield, and buy more insurance. ETH is levered to DeFi and altcoins. BTC is not.

There are ways to trade bitcoin dominance on some exchanges via the Bitcoin Dominance Index, but BTC and ETH are such a large part of the crypto ecosystem, it's not really necessary. Together BTC and ETH represent around 65% of crypto (ex-"stable" coins), while coin #3 in the rankings (BNB) is less than 1/10 of BTC's market cap. So, bitcoin dominance is really just a function of the relationship between ETH and BTC. Here's BTCETH vs. bitcoin dominance:

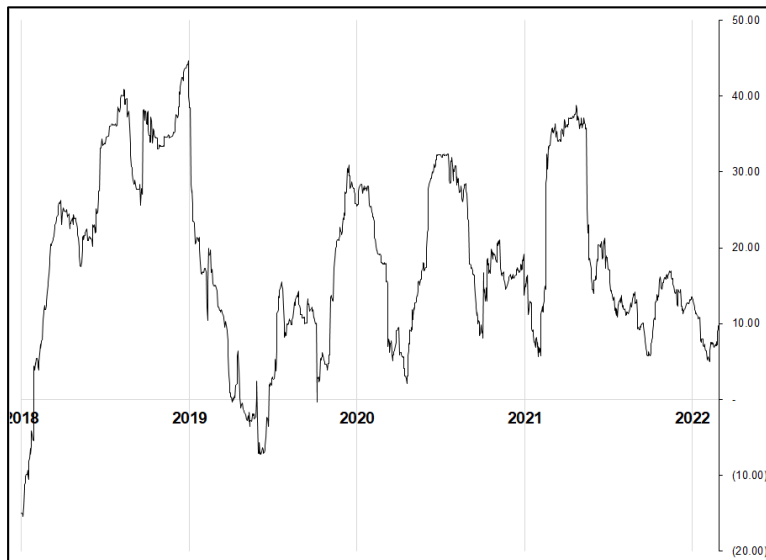
BTCETH vs. Bitcoin dominance (BTC's % of total crypto market cap)



I like short ETHBTC looking for a move back to the 0.33 area. I think this view could work in one of two ways. One, via a crash in ETH, or two, via a much stronger rebound in BTC.

I don't think ETHBTC is as dependent on overall crypto direction as many people seem to think it is. Let me elaborate a bit. ETH is generally more volatile than BTC. For example, 3-month implied at-the-money (ATM) volatility on Deribit right now shows ETH around 78% and BTC around 65%. And if you look at the spread between ETH and BTC realized vol over the last few years, you can see anything close to zero is pretty much the floor. Here's a chart:

ETH 90-day vol minus BTC 90-day vol



Positive number means ETH vol > BTC vol

Sidenote: My goal with MacroTactical Crypto... and in life... is to keep iterating and slowly make things better and better via continuous improvement. In that spirit, and because some readers of this newsletter have >25 years of trading experience while others have <2... Today, I have added a feature called “Explainer Box” to MTC. This will be a box that explains a term or concept for people that are not expert in that thing. If you already know the concept, just skip the Explainer Box. Also, if you have ideas for other MTC features or improvements, please let me know!

Here is an Explainer Box that describes the difference between implied and realized volatility.

Explainer Box
Implied vs. Realized Volatility

First thing to know is: “volatility” and “vol” are used interchangeably. They mean the same thing. “Vol” is just a cooler way of saying “volatility.”

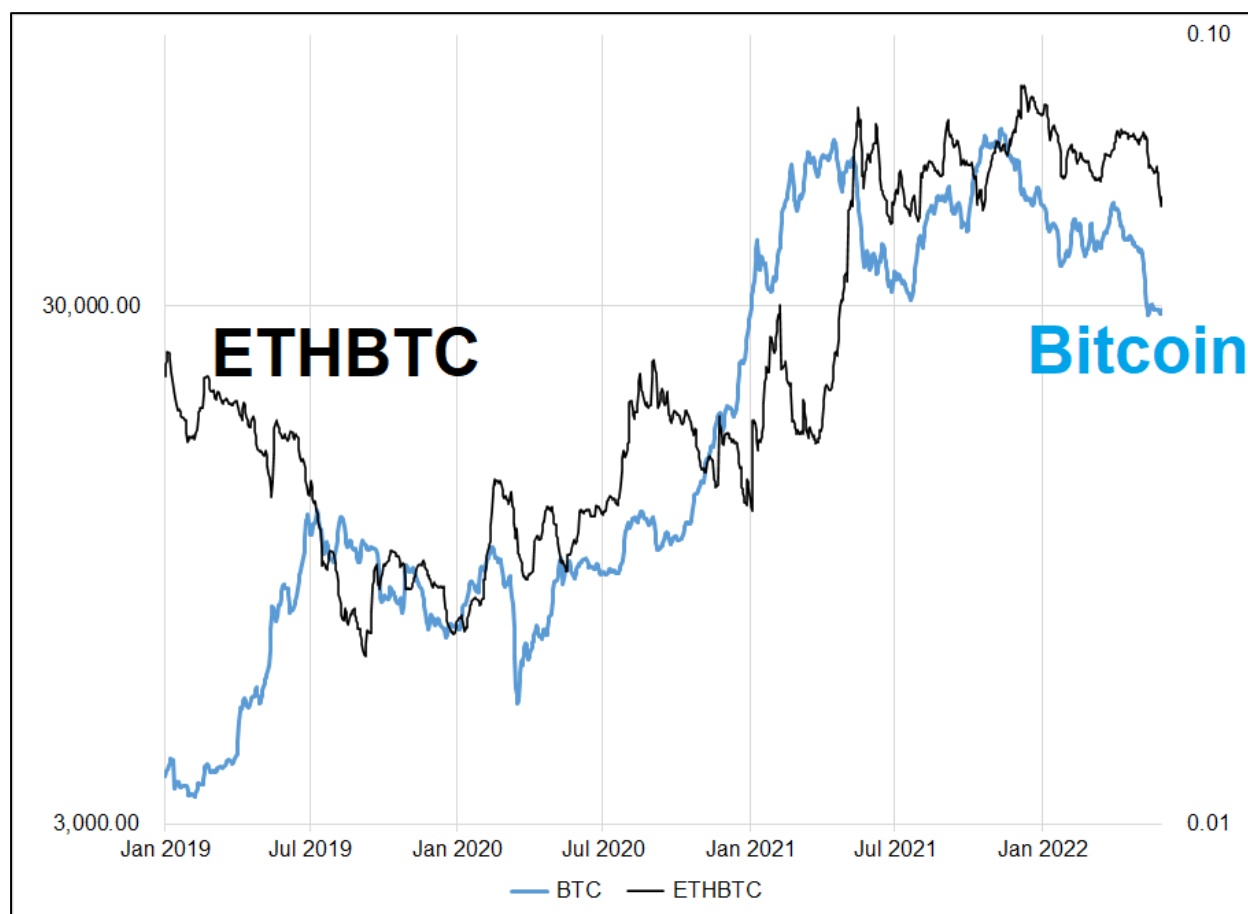
Implied vol is the price of volatility in the market as derived from the price of options. It’s the market’s **forward-looking** estimate of vol... A measure of how *volatile the thing is expected to be in the future.*

Realized vol is **backward-looking**. It is derived from historical data. It’s a measure of *how volatile the thing was in the past.*

Sometimes when people talk about BTC dominance or ETHBTC, the assumption is that because ETH is more volatile than BTC, that means ETH outperforms in bull markets and underperforms in bear markets. Or that ETHBTC is an altcoin season kinda thing (alts happy = ETHBTC up). That’s logical, but it’s not really true all the time.

Here is a chart of ETHBTC and BTCUSD back to 2019.

ETHBTC vs. BTC since 2019



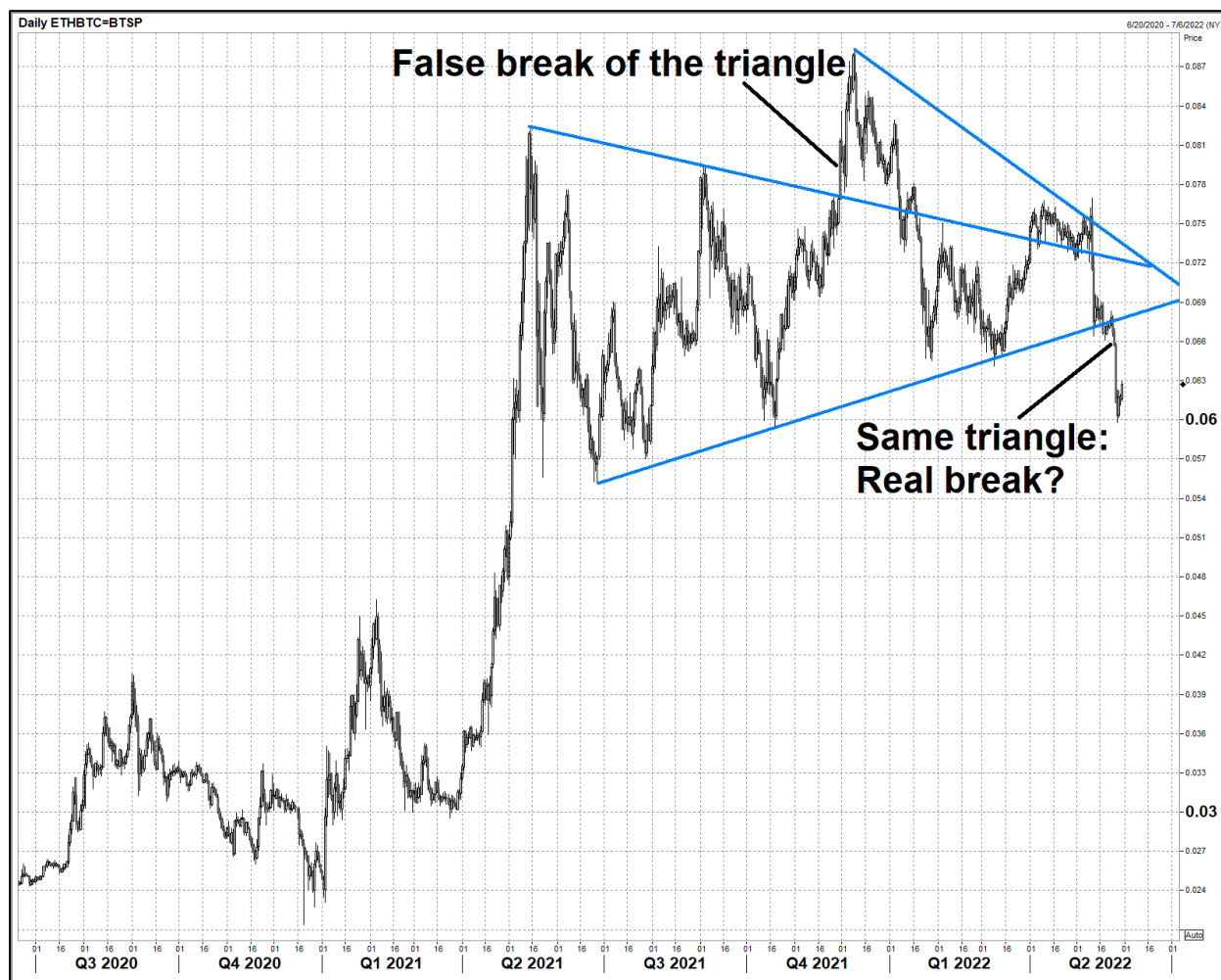
If ETH was just turbo bitcoin, then ETHBTC would go up when bitcoin goes up. But the relationship is not anywhere close to that dependable. You can see there are periods where bitcoin goes up and ETHBTC goes down, particularly the first half of 2019.

My point here is that I think **it's perfectly consistent to be bullish BTC and bearish ETHBTC at the same time**. In January 2021, bitcoin was around 29000, and ETH was 800. ETH has been a massive outperformer for the past two years and I think that outperformance is done. And set to reverse.

I'll keep you up to date on this trade. The parameters are: **Short ETHBTC at 0.061 with a stop at 0.077 and a take profit at 0.033.**

My trades tend to start with narrative, behavioral finance, and global macro thoughts, then use technicals and vol estimates further downstream in the process to narrow in on tactics. The chart of ETHBTC features a huge topside triangle break followed by a rejection and a downside triangle break. I put the stop loss above the broken triangle because if we go back up there, my idea is toast. Here's the chart.

A messy ETHBTC chart breaks both sides of the triangle



When the top of a triangle breaks like this, it often sucks in the last of the FOMO traders to the topside and forces the last of the shorts to stop out. If the break is subsequently rejected (i.e., price heads lower, back through the bottom of the triangle), the market is caught leaning hard the wrong way and progress to the downside is easier. This is similar to the concept of a Slingshot Reversal, [which I explain here](#) in my educational Substack.

I will always track the trade ideas mentioned in here and let you know when I've stopped out or taken profit. None of this is investment advice; my goal is to give you ideas and viewpoints that you can incorporate into your process. Don't copy my ideas. Build your own framework and include the parts of my work that you think make sense... Throw out the parts that don't resonate with you.

Now, let's talk MSTR.

Topside convexity? What do you mean *topside convexity*?

When MSTR falls, bears and Elmer FUDs get riled up about the Saylor Line, or margin calls at \$21,000 or the idea of a Microstrategy board revolt that will force the treasury to sell grillions of bitcoin into a collapsing market. There are some nuggets of truth in the FUD pile but there is a weird and interesting reality that is kind of the opposite story.

Explainer Box
Saylor's all-in bet on bitcoin

In mid-2020, Michael Saylor pivoted his software company to crypto as the treasury of his company, MicroStrategy (NASDAQ: MSTR) bought bitcoin. Since then, MSTR has issued debt to buy more and more bitcoin and the company is now mostly viewed as a levered bitcoin play.

Saylor straddles the genius/madness line for most observers with some thinking he's a messianic visionary while others think he's macadamia nuts. I think he's making a smart all-or-nothing bet with massive upside in one of the greatest moral hazard plays in of all time.

His company was nearly zeroed on fraud charges and the implosion of the tech bubble in 2000 and therefore he feels like he has nothing to lose. I admire his cojones. [Watch him explain it all here](#). Is he opportunistic, strategic, or kookoo for Cocoa Puffs? You decide.

Convexity of MSTR to bitcoin is greater when bitcoin rallies than when it dumps. In other words, if bitcoin has a huge move up, the MSTR rally is larger than the MSTR sell off when bitcoin has a huge move down.

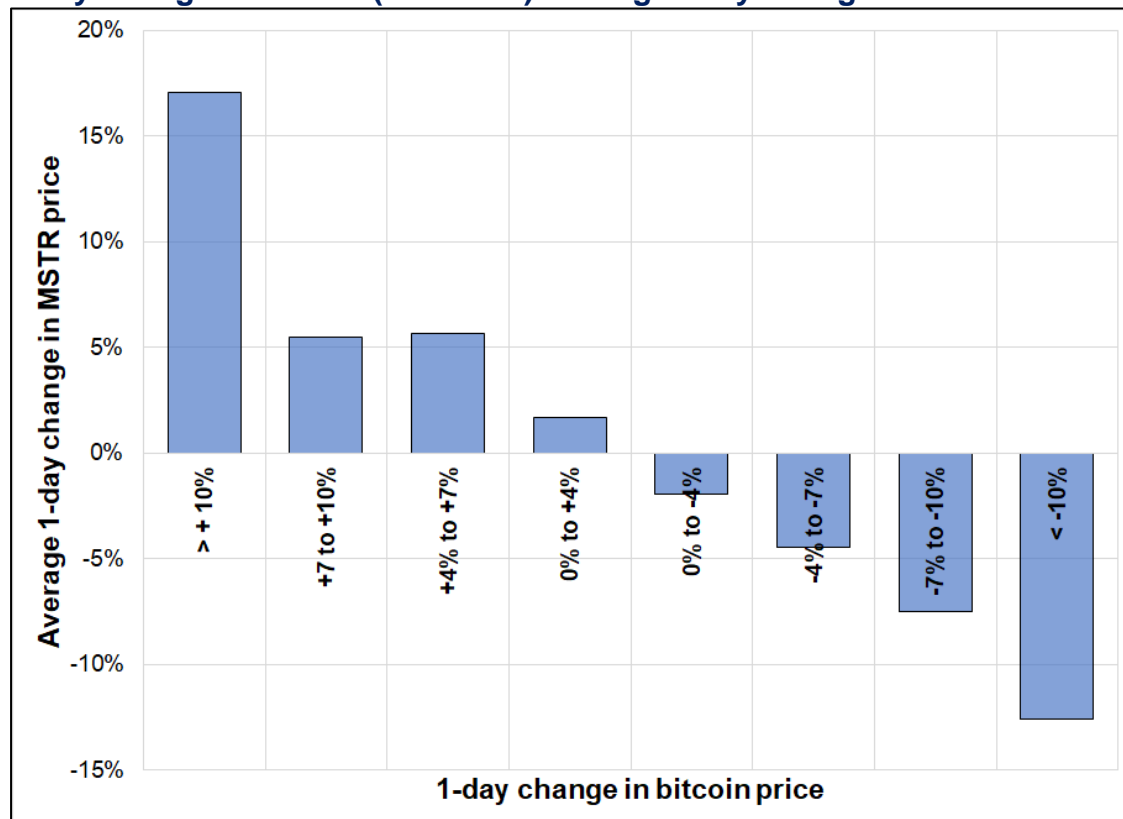
Here's a table:

1-day changes in bitcoin (bucketed) vs. same day average change in MSTR

		MSTR change on day		
		avg	min	max
Bitcoin change on day	> + 10%	17%	5%	29%
	+7 to +10%	5%	-2%	16%
	+4% to +7%	6%	-2%	22%
	0% to +4%	2%	-8%	22%
	0% to -4%	-2%	-14%	9%
	-4% to -7%	-4%	-23%	9%
	-7% to -10%	-7%	-25%	0%
	< -10%	-13%	-26%	-5%

And here's a chart:

1-day change in bitcoin (bucketed) vs. avg. 1-day change in MSTR on those days

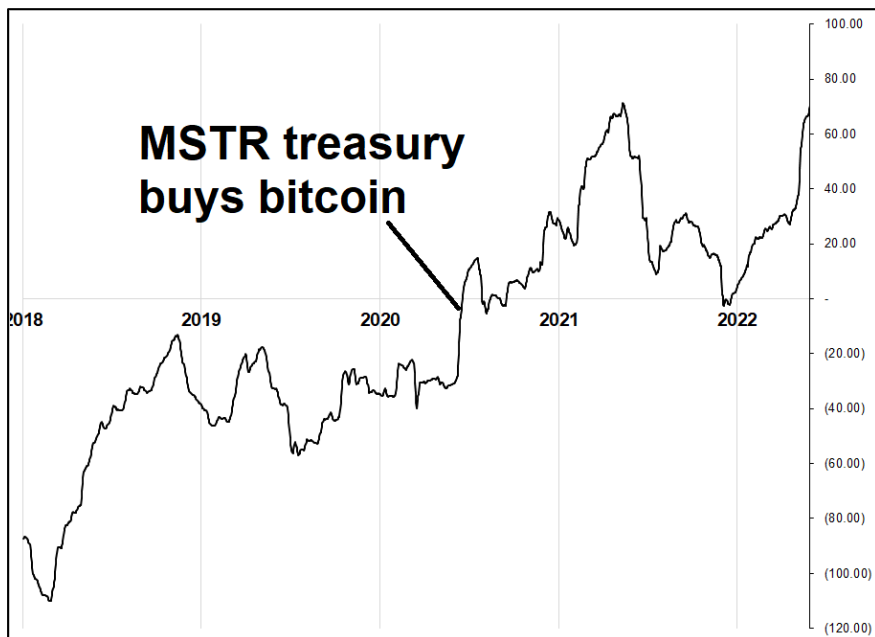


The main takeaway here is that a bitcoin rally of 10% or more sees MSTR up 17% on average while a bitcoin drop of 10% or more leads to a drop of 13% in MSTR, on average. I think that's kind of interesting since it goes against the dominant narrative of downside convexity in MSTR. There are two possible reasons that I can think of for this topside skew:

1. MSTR short interest is 37% of the float. The squeezes are not fun for shorts.
2. The sample size of large bitcoin moves (10% or more in one day) is only 14. Therefore, this result could just be a sample size issue. If you look at bitcoin moves +/-7% (a much larger sample), the convexity disappears and the MSTR reaction is symmetrical.

Either way, MSTR remains a pretty good high-vol bitcoin proxy. If you look at MSTR volatility vs. bitcoin, it's pretty easy to see the day when Saylor started buying bitcoin. MSTR was lower vol than BTC before that and has always been higher vol since. Again, similar to ETH vs. BTC... Zigs toward the zero bound quickly become zags back up.

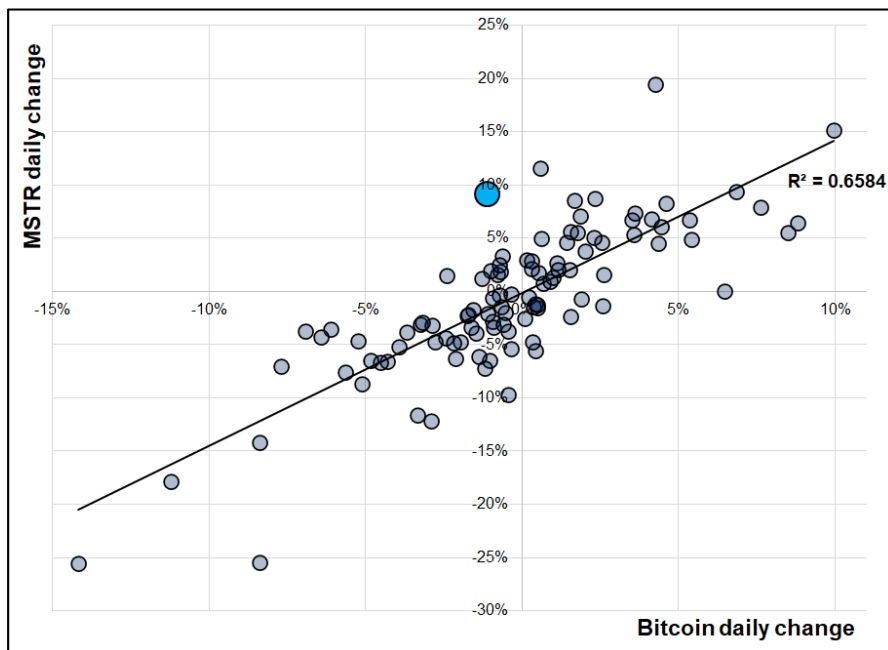
MSTR 90-day realized vol minus bitcoin 90-day realized vol



FWIW, there is no skew for puts in the MSTR options market

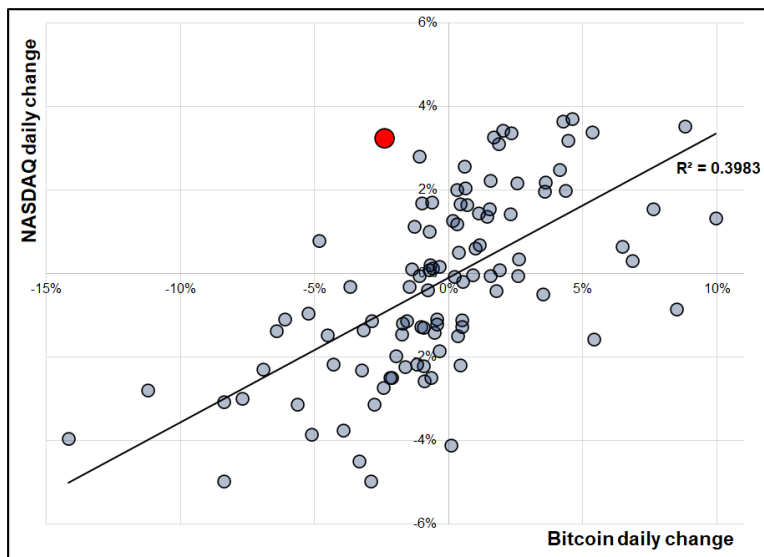
And here's MSTR daily returns vs. BTC in 2022. I marked last Thursday's {BTC down 1% vs. MSTR up 9%} day in blue, just because it's weird.

MSTR daily change vs. bitcoin daily change (August 2020 to now)



The next chart shows the same thing, but BTC vs. NASDAQ. The red dot is Friday's big decouple. Again, weird.

NASDAQ daily change vs. bitcoin daily change (for 2022)

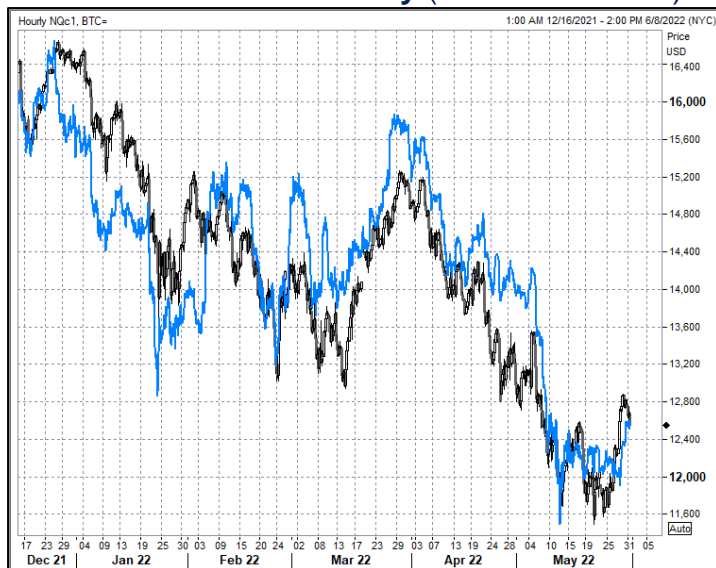


I put linear trendlines on these, but the relationship is not totally linear

People are freaking about that price action last week, but I don't place a ton of weight on a brief decouple between two highly-correlated assets. Very often, there's simply a flow in one market and not in the other on that particular day and the underlying relationship hasn't really changed.

Some dude comes in and buys a shedload of NASDAQ futures as part of a giant rebalancing while some other person across the street is unwinding her crypto fund because of LUNA losses and you get that kind of day. It happens all the time and it doesn't have any forecasting value. Here's the overlay:

NASDAQ vs. bitcoin hourly (late 2021 to now)



It is important to monitor this going forward of course, because the crypto chameleon keeps changing its story and if you want to trade it successfully, you need to know the color of the current narrative. It wasn't always NASDAQ pushing BTC around. And it won't always be NASDAQ pushing BTC around, either.

Final thoughts

The crypto haters are having a field day right now, just as the zealots had many field days in 2021. Mindless, pointless posting of the current level of spot bitcoin on Twitter continues as price travels in both directions.

I still believe (as I often do with many things) that the truth is somewhere in the middle. There is so much grift, fraud, rent-seeking, and generally horrible stuff going on in crypto that it's easy for detractors to pile on, especially when prices are falling.

On the other hand, there is also a ton of innovation going on and that's not going to change, even if the flood of dumb money has dried up for a while. I still think there will be cool blockchain video games, and music applications, and many artists will accrue life-changing benefits, and young people will prefer bitcoin over gold from now all the way to eternity. Try not to get sucked into the bullshit reflexivity argument that bulls used at 65000 and bears use down here.

Markets are wrong a lot. The price is *not* always right. Make up your own mind about crypto and don't just get sucked into the current narrative. Most of the time, **narrative follows price**. This is true in legacy markets but even more true in the hyperbehavioral social experiment called crypto.

Crypto isn't Monetary Jesus come to save that which is lost. But it's not a total fraud or a complete joke either. Crypto is hyperinnovation, fraud, cool technology, scammy rent-seeking manipulation by centralized organizations, a new era of artist/creator empowerment, Ponzi finance, decentralization, and toxic, despicable grift. It's the best and worst of humanity, all wrapped into one big beautiful, stupid, utopian, energy-guzzling, digital package.

Don't follow the crowd. Think for yourself. Stay Bayesian.

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Brent Donnelly

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