Dear Woodstock Family

“We are in a structural bull run punctuated by short-term healthy price discovery and reality check events. At Woodstock, we are unmoved as digital assets have been accepted as an asset class both at the institutional and retail levels. In the short term, influencers can sway markets, but the fundamental activity cannot be undermined by knee-jerk price action. We will see tremendous growth in this space in the next few years.”

~ Pranav Sharma, Founding Partner, Woodstock Fund

De-Mystifying the Price Correction

The digital assets market that seemed to be defying gravity corrected swiftly on the back of the selling pressure due to regulatory crackdowns, environmental concerns, and heightened tax scrutiny. Between 12th May - 19th May 2021, the Bitcoin market experienced the largest drop event since the March 2020 sell-off. The market traded down by over 47%, from the weekly high of US$ 57,929 to lows of US$ 29,965. This weekly candle is now the single largest drop in the price range in history, a whopping US$ 27,964 candle.
A Breakdown of the Drop

Analysis of Events Driving Bitcoin’s Price

This price action was caused due to external factors which had almost nothing to do with the fundamentals of Bitcoin or Blockchain Technology. In addition, such corrections are commonplace in a nascent asset class, and below is a chart that shows historical BTC price movement, most of which were also triggered by news and announcements –

In Apr ’13, Bitcoin saw the markets fluctuate, post which Mt. Gox, a major digital currency exchange of the time, suspended trading for a day which caused the market to correct further. Then in Mar ’17, the SEC rejected two BTC ETF applications which sent the prices tumbling down from US$ 1,300 to US$ 1060 in 2 days. A year later, in Jan ‘18, Chinese officials ordered Bitcoin mining operations to ‘close’. This news combined with the ICO mania caused a 56% correction in 46 days.

2018 to early 2020 was a relatively stable time for Bitcoin when we saw projects building strong foundations for the 2020 bull run. The key takeaway here is that Bitcoin’s price corrections have been news driven in the past.
The Likely Drivers of the May ’21 Drop

Three significant events appear to have impacted the recent price movement:

1. Tesla Chief, Elon Musk, showed his concern on Bitcoin Network’s power consumption trend and said the company would no longer accept Bitcoin as payment.
2. China announced a ban on crypto-related activities including trading, mining, lending, settlement services, etc. They have asked institutions and exchanges to stop providing any digital asset trading solutions of any form.
3. US Fed seemed to be contemplating increasing interest rates to hold on rising inflation and control the overheated economy. Although, recent reports have shunned the possibility of the same in the foreseeable future.

After a few months of a strong upside rally across the market and the open interest in derivatives markets at all-time highs, the marginally higher highs on the Bitcoin price action suggested that the momentum was slowing down, we had the wyckoff distribution phase in play, and the events shared above acted as a catalyst that resulted in a significant correction across the board.

On-Chain Metrics Analysis

Swift corrections are commonplace in this market. However, an interesting on-chain metric analysis on capitulation sell-off showed that the majority of sellers who sold their BTC were short-term holders (1m – 6m old coins) (i). Whereas, most of the long-term holders (1yr – 3yr) who sold their positions had done so prior to this correction, possibly rotating them into other digital assets such as Ethereum. This suggests that old hands did not panic sell nor rush for the exits. (ii)
Let’s move onto analyzing some metrics on the world’s two biggest exchanges, Binance and Coinbase. Recent price action saw different behavior on both the exchanges. Binance, which is the preferred exchange for new entrants due to its low fees and less stringent KYC policies, observed an increase in BTC deposits.(iii) Conversely, Coinbase, which has a US native user base, saw a steady increase in the net BTC withdrawals over this period. Coinbase is the preferred venue for US institutional investors, and such high daily withdrawal rates (10k – 20k BTC/Day) appears to indicate that larger buyers still remain in the accumulation phase during this entire price correction.(iv)
Regulation – An Adoption Catalyst

In 2021 we witnessed a wide array of events in the blockchain ecosystem which indicated that governments, financial institutions, and retail investors are developing a thesis around digital assets.
In this newsletter, we discuss the role of regulations as an adoption catalyst, the recent developments in the global regulatory landscape for digital assets, and how different financial institutions have responded to regulatory clarity.

**The Requirement for Regulation**

The primary purpose of regulatory frameworks is to protect investors from scams and fraudulent schemes. Digital asset markets, like all financial markets, will benefit from rules to ensure fair trading and sufficient risk disclosure.

The United States is a popular capital market as the investors are well protected from bad actors.

Greater regulatory clarity will provide comfort to larger institutional investors who only operate in regulated products, and this will improve the stature of the industry as a whole as well as attract more liquidity and funding into it.

**The Marquee Regulator**

The United States is an important thought leader in the policy-making world. As a result of the government’s effort to understand this asset class better, there has been an interesting interplay between blockchain experts joining regulatory offices and ex-regulators joining boards of large digital asset players:
<table>
<thead>
<tr>
<th>Blockchain to Government</th>
<th>Government to Blockchain</th>
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<tbody>
<tr>
<td>• Gary Gensler, who taught a class on blockchain at MIT, was appointed as the Chairman of the SEC</td>
<td>• Jay Clayton, former SEC Chair, joins the advisory board of asset management firm One River</td>
</tr>
<tr>
<td>• Cynthia Lummis, a Bitcoin supporter, joined the Senate Banking Committee</td>
<td>• Brian Brooks, ex-Comptroller of Currency (acting) joined Binance US as its CEO.</td>
</tr>
<tr>
<td>• Sunayna Tuteja, ex-head of digital assets at TD Ameritrade, now works at the Federal Reserve’s Chief Innovation Office</td>
<td>• Max Baucus, an ex-US Senator, also joined Binance US as an advisor</td>
</tr>
<tr>
<td>• Brett Redfearn, the former SEC official, joined Coinbase as its VP of capital markets</td>
<td>• Brett Redfearn, the former SEC official, joined Binance US as an advisor</td>
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These appointments instil further confidence in the digital assets space and they will help create sustainable policies that will enable the citizens to enjoy the benefits of decentralized finance.

At this point, it would be remiss to ignore the demand from politicians to ‘crackdown on illicit activities’. Janet Yellen, US treasury secretary, recently raised concerns around “money laundering, Bank Secrecy Act, use of digital currencies for illicit payments, consumer protection and the like”. However, these remarks only highlight the need for awareness and conversations around blockchain technology, and through regulatory hiring, setting up panels, and participating in conferences the US government is demonstrating a strong appetite for learning about the same. We are confident that they will come up with fair rules which will allow residents to participate in the blockchain ecosystem while protecting such investors’ interests.

**Global Regulations**

Because of the decentralized nature of digital tokens, every government is looking to create a framework for their citizen’s participation in this ecosystem.

**Singapore**

The Monetary Authority of Singapore (MAS) has proactively taken measures to stop bad actors without curbing blockchain’s technological innovation. They engage with leaders of the blockchain industry to understand the sector better and they even run a FinTech Regulatory Sandbox to provide companies a safe space to experiment with the
technology. Recently Propine, an end-to-end digital securities services firm, graduated from this accelerator.

Further, Tharman Shanmugaratnam, Senior Minister and chairman of MAS responded to parliamentary questions on the digital asset markets on 5–Apr–21. The answers highlight the regulator’s understanding of the technology and their aim is to mitigate risks associated with cryptocurrencies through:

- Prudent AML/CFT requirements for entities providing digital asset services
- Observation of the network to identify suspicious activities
- Raising public awareness on the risk of investing in digital tokens

These steps are being taken to provide a stable and benign trading environment in Singapore. MAS continues to be a trendsetter when it comes to FinTech regulation.

India

In Apr ‘18, the Reserve Bank of India (RBI) prohibited its banking and related entities from dealing with crypto-currencies. However, this move was not backed by public consultation or independent research. Subsequently, the Supreme Court of India overturned RBI’s April 2018 circular. This exercise reflected the power of the people in the world’s largest democracy.

RBI on 31–May–21 has reinforced and asked banks, NBFCs, and payment system providers not to refer to its earlier virtual currencies-related circular, which was issued in April 2018 and later aside by the Supreme Court, in their communications to customers.

Currently, the government is taking active steps to understand this space better and on 19–May–21, the Economic Times recently reported that the central authorities are looking to set up a panel to study crypto regulations. Lastly, to address the ‘Indian government is planning to ban crypto again’ rumor, in Mar ‘21, the Finance Minister, Nirmala Sitharaman said that “the government has always been clear that it will not shut off all options, and will allow for cryptocurrency experiments in
fintech”. She went on to elaborate that the ministry is working with start-ups to promote innovations in the blockchain space.

**China**

The Republic of China has had a tumultuous history with Bitcoin which began in **2013** with the central bank barring financial institutions from handling Bitcoin transactions. Then in **2017**, China declared ICOs as illegal. A reiteration of this ban was picked up by Reuters recently and then on **21st May** “China vowed to crack down on bitcoin mining, trading activities”.

We are still waiting to see how this clampdown on mining will pan out, however, a clear silver lining from the mining ban could be a wider geographical distribution of Bitcoin miners across the world. Reports indicate that miners are either selling equipment or moving to nearby locations to continue being a part of the blockchain ecosystem.

**Institutional Investments in Digital Assets**

Progressive regulation and sustained quantitative easing have propelled the adoption of decentralized digital currencies. Microstrategy, Square, and Tesla* were early adopters of the Bitcoin buying trend and have added a substantial amount of Bitcoin on their balance sheets. They were joined by BlackRock, J.P Morgan, SkyBridge, Goldman Sachs, BNY Mellon, Mastercard, Morgan Stanley, Visa, and PayPal, all of whom are either trading, investing, or providing digital asset support in 2021.
Newsflow of institutional adoption has been extremely positive and even when Bitcoin recently dipped, wallets linked with Over-The-Counter (OTC) desks registered large outflows of $BTC. Large investors usually make investments via OTC desks to avoid influencing asset prices on public exchanges. Thus, $BTC moving from these desks is widely taken to represent institutional buying.

**Conclusion**

In 2021, the rise of Bitcoin’s price and the recent correction has given new market participants a masterclass in risk management. However, on zooming out, we see:

<table>
<thead>
<tr>
<th>27-May-21</th>
<th>01-Jan-21</th>
<th>01-Jan-20</th>
<th>01-Jan-18</th>
<th>01-Jan-16</th>
</tr>
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Data Source: [Yahoo Finance](https://finance.yahoo.com)

These prices give the following return for Bitcoin:

<table>
<thead>
<tr>
<th>YTD</th>
<th>1 Year Return</th>
<th>3 Years Return</th>
<th>5 Years Return</th>
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<tr>
<td>16%</td>
<td>31%</td>
<td>276%</td>
<td>10,317%</td>
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In order to fairly compare Bitcoin’s return with other assets, we turn to Willy Woo’s chart of risk-adjusted returns of Bitcoin versus Gold, US Stocks, US Real Estate, Bonds and Emerging Currencies:
Bitcoin massively outperforms other assets. Both institutional and retail investors are learning how to incorporate digital assets into their portfolios. These assets have historically been more volatile than most other investment instruments, however, value investors must not get shaken up by short-term volatility and focus on the long-term performance of the technology.

Moreover, the recent price fluctuations have brought more regulatory attention to space and at Woodstock, we see this as a positive sign. Policymakers are engaging in conversations with blockchain experts and trying to educate themselves to come up with intelligent regulations. This is the key to mainstream adoption.

Note: Tesla stopped accepting Bitcoin as payment, however, it continues to hold the token in its balance sheet.

**Woodstock in the News**

1. Near Protocol has organized an India Accelerator and we are happy to support them as investment partners
2. These are the new additions to our portfolio:
   1. **Arterra**, a digital collectible hub with a hyperfocus on eSports
2. Nayms, a digital insurance marketplace for regulated brokers and underwriters
3. Read our views on quadratic funding
4. Our thoughts about digital asset markets and influencers were covered in an article by DKoding
5. Read our Investment Thesis on Covalent

You can find the previous month’s newsletter here.

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Questions? Feedback? We’d love to hear from you! Simply reach out to us at contact@woodstockfund.com

Warm Regards,
Woodstock Team