Bitcoin Suisse | Decrypt

August 13, 2019 | Season 1 Episode 4

Is Bitcoin a “Safe Haven”?

We live in a world where a single tweet can have wide-reaching effects on the global economy and markets. Future-proof stores of value are in dire need. Can cryptocurrencies – and Bitcoin in particular – fulfill this role?

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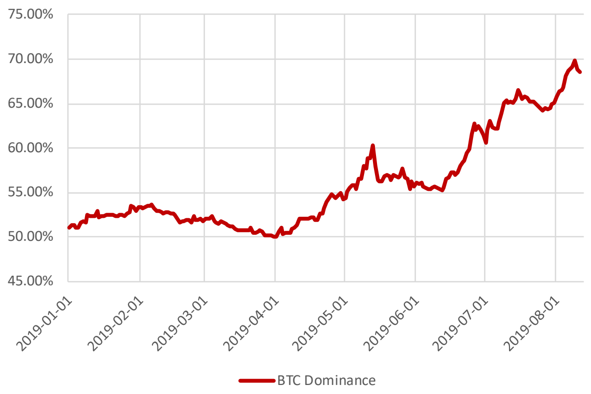
While state-issued currencies and government bonds are the most common liquid store of value, their future purchasing power heavily depends on central banks and monetary policies. Investors trying to escape low and negative interest rate levels have mainly been flocking into stocks and equities during the past decade. In times of economic fear, uncertainty, and doubt, the suitable instruments for wealth preservation could start changing. Non-inflatable, alternative monetary assets might become increasingly appealing in a downturn which is once more met with more central bank interventions.

Both Bitcoin and gold fulfill this criterion. Gold has been an integral part of the monetary system for the majority of the 19th and 20th centuries and is widely accepted as valuable across borders since ancient times. Bitcoin shares many characteristics with gold, such as fungibility, durability and scarcity, and is therefore often called “digital gold”. Like gold, Bitcoin does not pay interest – but it is inherently deflationary contrary to the current debt based monetary system.

Ultimately, Bitcoin as a store of value seeks to remove the need for trust in counterparties, like governments or banks. In that regard, Bitcoin’s risk is limited to complete network failure – however, as per the *Lindy effect*, the chances of network survival increase with every day that passes by. This makes Bitcoin, the oldest successful cryptocurrency, unique among the more than 2’000 cryptocurrencies in existence today and solidifies its leading position as a digital store of value.

Indeed, Bitcoin’s share of the total cryptocurrency market capitalization, the Bitcoin dominance, has recently been on the rise. Starting at 50% in April, it has increased to almost 70% in August. Unlike 2017, where a rising tide (Bitcoin price) has lifted all boats (altcoin prices), divergences between crypto-to-crypto correlations become more apparent in this year.

Illustration 1: Bitcoin dominance year-to-date. The dominance has increased significantly since April.



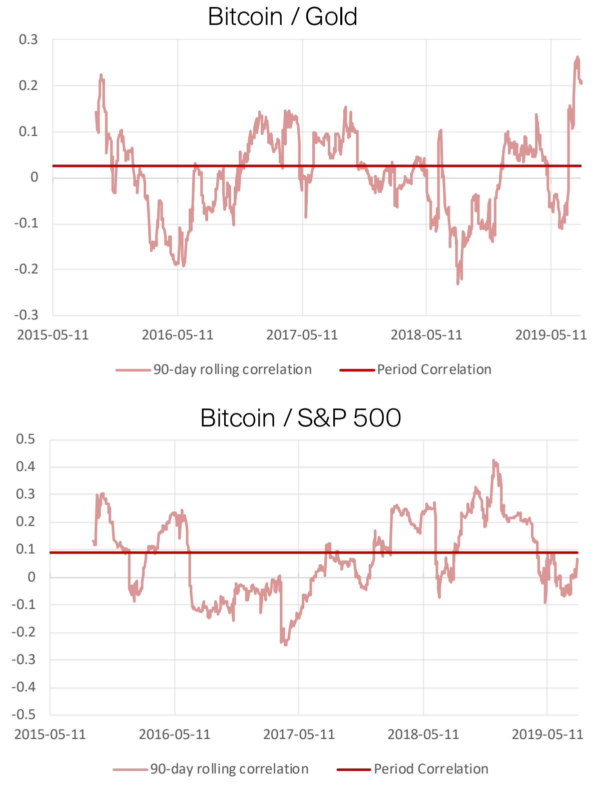
Source: coinmarketcap.com, Bitcoin Suisse Research.

> *“They use [Bitcoin] more as an alternative to gold really. It’s a store of value, it’s a speculative store of value, like gold.”*
> *– Jerome Powell*

Especially the smaller altcoins or tokens, remnants of the 2017 ICO craze, suffer from the current market conditions. Valuations were overblown, and many projects failed to live up to their promises until now.

Possibly, this increase in Bitcoin dominance paints a picture of a new group of cryptocurrency investors of 2019. Instead of trying to cherry-pick a long-term winner, their investment hypothesis is to look for an asset class that is decorrelated to the rest of their portfolio and, potentially, a bet on a future store of value. An overview of the correlations between Bitcoin and gold as well as the S&P 500 index since 2015 is given in Illustration 2.

Illustration 2: Correlation between Bitcoin (GBTC), gold (GLD), and the S&P 500 (SPY). 90-Day rolling correlations based on daily returns.



Source: Yahoo Finance, Bitcoin Suisse Research.

The overall correlation of Bitcoin to equities (with the S&P 500 as proxy) and gold are low at <0.1 period correlations. However, in the last few months, the correlation between Bitcoin and gold has been increasing and currently sits at 0.21 for the last 90 days. This further bolsters the claim that the perception of **Bitcoin could gradually transition from a high-risk, speculative investment to a “safe haven” asset similar to gold in times of economic turmoil**.

Trade War, Currency War, and a Global Plunge in Bond Yields

Since Bitcoin’s birth, we have not experienced a global recession. For the first time in history, every person with a smartphone has access to a digital asset that is not tied to any country. Bitcoin may turn out to be a great option for investors that want a part of their portfolio protected against the government’s unpredictable manipulation of financial markets, especially during time of war. Switzerland’s neutrality during WWI and WWII has attracted tons of capital to flow into this geographic safe haven. Like Switzerland, Bitcoin is also neutral during wars, and may become a digital safe haven for global financial assets.

A major corner stone of President Trump’s administration is to make the US economy great again. Deficit-financed tax cuts boosted US equities and extended the current bull market to one of the longest in US history. Being up for re-election in 16 months’ time, Trump has a huge incentive to keep the stock market booming until November 2020. He is pressuring the Federal Reserve to cut rates, which may be one reason the Fed cut US rates from 2.5 % to 2.25 % last week.

Trump recently announced on Twitter that he will be imposing an additional 10 % tariff on all Chinese imports to the US beginning on September 1st. The Trump administration is also challenging trade agreements that the US has with Mexico and the European Union. Provoking a trade war may have also been intended to pressurize the Fed into lowering rates more aggressively. As mentioned in the first episode of Bitcoin Suisse Decrypt, **cutting rates inflates asset prices**. When the stock market is high, people can feel a false illusion of prosperity. If Trump is able to extinguish the fire he started by striking a deal with China and if the economy is humming along because of injections of cheap money, voting ballots will be cast for Trump.

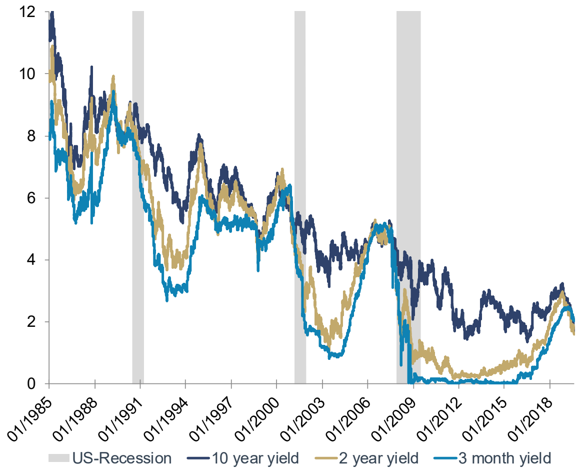
However, that is just one possible scenario. The more likely scenario is what one of JP Morgan's investment advisors outlined last week: "The US dollar is at risk of losing its status as the world's dominant currency." This week, China responded to Trump by suspending purchases of US agricultural crops, and the Chinese yuan's exchange rate with the dollar depreciated to the lowest it has been in the past decade. This will make Chinese products cheaper and will allow China to reduce its dependence on US trade and attract new trading partners. Also, China has increased its gold reserves for 8 straight months now, which can be interpreted as a vote against the US dollar. All of this adds up to less demand for US dollars.

> *"With the yuan over 7.0, an FX war, instability in HKG and the beginnings of capital flight, BTC rally could have real legs"*
> *– Michael Novogratz*

We are in a phase of weak global currencies, and we may enter a full-blown currency war. No country wants to hold another's hot potato. The biggest economic powers are trying to push off the negative effects of inflating their domestic currency onto their trade partners. In response, their trade partners either have to devalue their currency, which wipes out the household savings of millions, or let their currency appreciate, which forces exporters out of business. This emerging fear of currency war, trade war, and economic instability has been triggering another spectacular plunge in global bond yields during the past few weeks.

Gold and Bitcoin are having phenomenal rallies in response to the madness. Gold breached its six-year high of $1,500, and Bitcoin surpassed $12,000. The major news station in the US, CNBC, had two commenters this week claiming that **capital is flowing into Bitcoin because we are entering a global recession**. There are more and more red flags that signal a recession is imminent: e. g., the Federal Reserve lowering interest rates, inverted yield curves, and a spike in percentage of loan defaults. We have already witnessed two out of the three criteria...

Illustration 3: Bond yields are dropping around recessions.



Source: Federal Reserve Bank of St. Louis, Incrementum AG.

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