Covid-19 ‘net positive’ for crypto-currencies

The market cap of crypto is many times smaller than that of the stock market in terms of traded volume. Still, the crypto-currency market appears to have benefited from the outflow in capital from traditional financial markets, at least in the short term according to billionaire Zhao Changpeng, founder and chief executive of Binance, the world’s biggest crypto-currency exchange by trading volume.

While traditional financial markets crashed during the Covid-19 pandemic, Binance estimated its earnings at US $262.5 million in the first quarter, mainly from transaction fees. It also saw a 47.4% rise in the number of new institutional investors in the first quarter of this year compared to the previous quarter.

“It think Covid-19 has probably been a net positive for crypto-currencies,” said Zhao. “Covid-19 has overall caused a lot of stress in the traditional financial markets, and some of the measures that people have taken are actually pushing people into crypto-currencies.”

However, Zhao also said that until the crypto-currency market grows significantly, it will always, to an extent, correlate with stock market performance. “When people are hurting financially in one market, they will get cash from other markets” including by liquidating their crypto-currency investments, he explained.

The Covid-19 pandemic and resulting containment measures have had a huge impact on retailers, restaurants, and tourism globally. The US economy contracted at a 4.8% annualised rate in the first quarter, its sharpest decline since the Great Recession between 2007 and 2009. Meanwhile, China’s economy contracted by 6.8% in the first quarter of 2020 compared to a year earlier.

Binance, however, does not have all its eggs in one basket. No country contributes more than 10% to its revenue, explained Zhao, and they have plans to further spread out operations. The company applied to operate in Singapore in February and announced in June that it will soon launch a UK trading platform.

This expansion is not without its challenges though. In many countries, unclear regulation regarding crypto-currency is also a major problem, according to Zhao, who said that when in doubt Binance tries to follow common sense, “We’re living in a world where unless there’s a law forbidding you from doing something, then it’s assumed it’s legal,” he added.

The company was among four crypto-currency exchanges and seven crypto-currency issuers, applying to their regulatory framework, according to the chief executive. “Even within the Binance team, no one can penetrate our access point.”

According to analysts, Bitcoin and the S&P 500 are both correlated and co-integrated, with the pair’s R squared value at 95%. Such a large correlation suggests that Bitcoin, as a dependent variable, is extremely susceptible to movements on the S&P 500.

The situation is complicated by Covid-19 related measures such as quantitative easing, which inflates the money supply, boosting both stocks and Bitcoin. At the same time, stock markets are seeing increasing intervention in the form of artificial competition from central banks buying worthless shares. This has led to suspicions from commentators who suggest that the bull run of the past several months is long due for a correction.

Bitcoin, then, remains far from ‘decoupling’ from macro forces. The real test is a stress situation, Covid-19 is certainly providing this and it is likely to continue until the pandemic subsides.