

Q2 2023

Kaiko Research

Quarterly Market Report

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Q2 Timeline

April

April 11

BTC hits \$30k for the first time in nearly a year

April 12

Ethereum completes Shapella upgrade

April 17

SEC files charges against Bittrex

April 20

EU Parliament passes MiCA

April 25

Binance withdraws \$1bn offer for Voyager

May

May 1

TUSD trades at a premium

May 7

Binance halts BTC withdrawals as fees surge

May 12

Bakkt delists 25 of 36 tokens because of regulatory pressure

May 21

Gemini says DCG missed \$630mn loan payment

June

June 1

Hong Kong opens retail trading

June 5

SEC files charges against Binance and Binance CEO CZ

June 6

SEC files charges against Coinbase

June 12

Aave considers freezing CRV markets because of \$60mn loan

June 15

Tether depegs, BlackRock files for spot BTC ETF

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Analyst Commentary



Clara Medalie

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Stablecoin Volatility is Concerning

Stablecoins are systemically important in cryptocurrency markets, so even the slightest depeg can cause mass market contagion. As such, it is concerning that stablecoins were particularly volatile in Q2: TUSD wobbled amid Prime Trust concerns, USDT depegged for mysterious reasons, BUSD traded at a discount as Binance came under fire, and USDC crashed during the March banking crisis.

While each stablecoin moved for unique reasons, the volatility highlights a bigger problem: crypto markets are dependent on highly centralized stablecoins that often lack transparency around reserves. While Circle has made huge efforts to improve USDC transparency and even Tether has shown some willingness to improve, the relatively unknown TUSD is today posing the biggest risk. In just a few months, it has become the second largest stablecoin, almost entirely due to Binance's zero-fee promotion.

While TUSD is not yet systemically important, Binance is an extremely important exchange, so any activity on it should be scrutinized. TUSD is the least transparent stablecoin of the bunch, and for the sake of crypto market integrity, I hope this can change.



Dessislava Aubert

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BTC and Macro Have Decorrelated

Despite the U.S. Federal Reserve pausing rate hikes in June for the first time in more than a year, the overall macro liquidity outlook has worsened in Q2 relative to the previous quarter. Following the debt ceiling deal in early June, increased debt issuance by the U.S. Treasury could further drain liquidity from the market and negatively impact risk appetite in the coming months.

Yet, despite the tough macro conditions, bitcoin has remained resilient, attracting institutional inflows and closing the quarter up more than 8%. Not only that, the asset seems to be further distancing itself from traditional assets as crypto-specific factors take the lead in driving market conditions.

BTC's correlation with the tech-heavy Nasdaq just dropped to a two-year low of 1% while its historically negative correlation with the U.S. Dollar weakened significantly from -60% to -8%. There is a growing divergence between bitcoin, which is maturing as an asset, and altcoins, which have been hit hard by the worsening regulatory environment and challenges in banking infrastructure. Overall, the end-of-quarter rally was undeniably led by BTC.

Analyst Commentary



Riyad Carey

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It's Impossible to Ignore DeFi

Even as USDT's market cap grew to all-time highs this quarter, the stablecoin became more vulnerable to depegs because of shrinking liquidity in the Curve 3pool. An \$80bn stablecoin relies on a \$300mn TVL pool on a DeFi protocol with a \$650mn market cap. DeFi protocols have more pricing power than ever, creating interactions between centralized and decentralized markets that are unprecedented in traditional finance.

This also means that the governance of various DeFi protocols must remain informed on changes on centralized exchanges. For example, alarm bells were raised at Aave this quarter when a risk manager noticed that CRV's off-chain liquidity had fallen by half in recent months (discussed on page 13). All of Avi Eisenberg's exploits and attempted exploits involved both centralized and decentralized markets.

DeFi has become so influential that all market participants need a full view of DEXes. On the flipside, DeFi protocols need to better understand the importance of centralized exchanges and be proactive in adjusting risk. This is more important than ever because of the increase in decentralized futures exchanges.



Conor Ryder, CFA

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2023: The Year the U.S Lost Crypto?

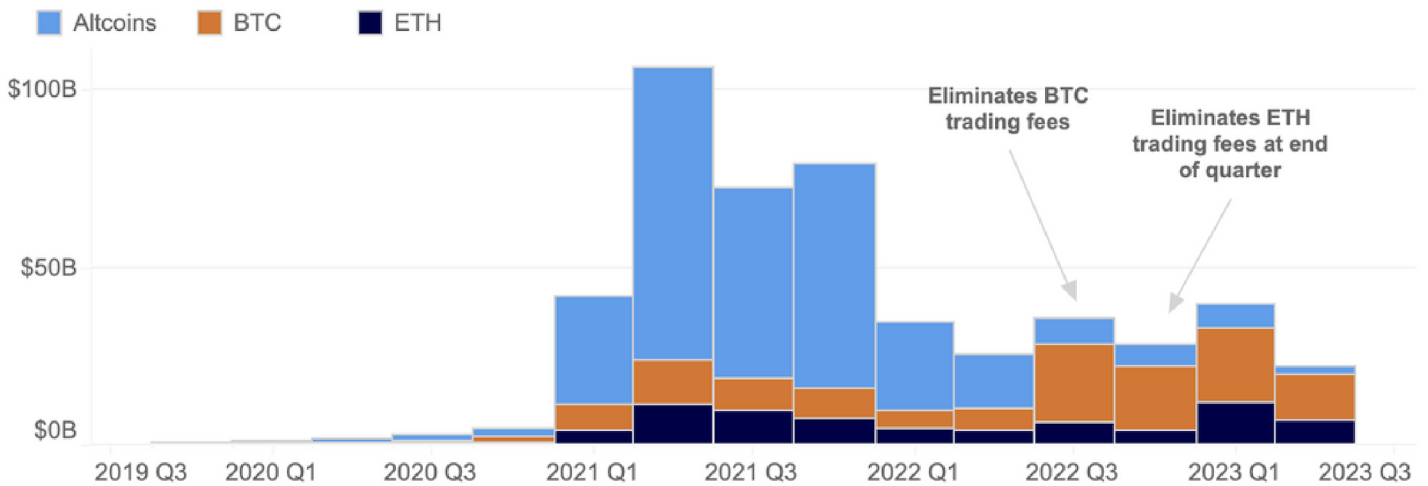
The reality is we could very easily look back on 2023 as the year the U.S lost out on crypto. Personally I want to see the U.S lead crypto innovation, as they have done with tech, but its looking more and more like they are starting to fall behind. The dominance of Tether and Binance are clear indicators that regulatory enforcement in the U.S is pushing crypto overseas. USDC market cap has fallen from \$45bn at the start of the year to just \$28bn today. Coinbase and Binance.US have lost volume share and liquidity since the start of the year versus their overseas counterparts.

The good news is that the last couple of weeks have seen a renewed interest from institutions in the U.S in the form of Blackrock, Fidelity and others applying for spot Bitcoin ETFs. It's clear that these institutions don't want to fall victim to crypto moving overseas, and look to now apply some pressure on the SEC. The stablecoin bill next month should also provide some much-needed regulatory clarity. The combination of this bill and an approval of the ETF applications could see the U.S regain a foothold in the crypto industry. Any other outcome and 2023 will be seen as the year the U.S drove crypto overseas.

SEC Charges Binance and Coinbase

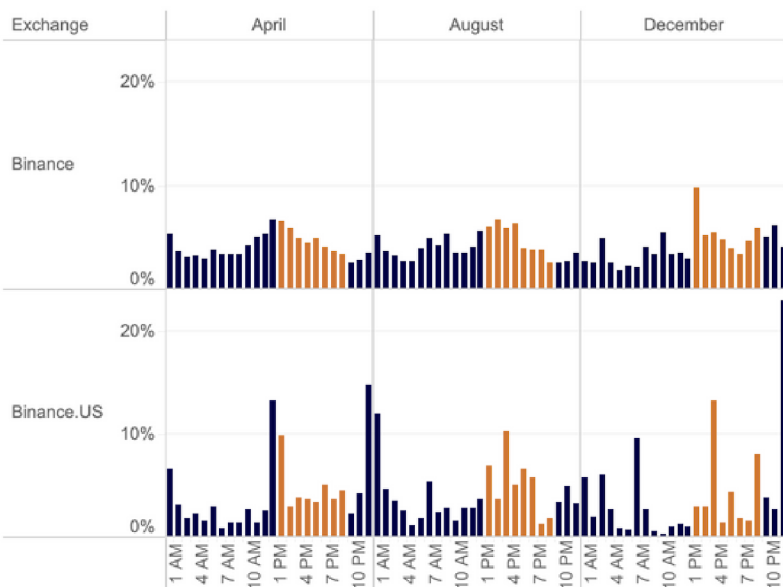
Alleges Wash Trading on Binance.US

Binance.US Quarterly Volume



The SEC made waves in June when it first filed charges against Binance, Binance.US, and Binance CEO CZ, alleging they were operating an unregistered securities exchange, broker-dealer, and clearing agency. One of the more eye-catching allegations was that a trading firm/market maker owned by CZ had been wash trading on Binance.US, especially in advance of its seed funding in September 2021. Shown above, the growth in quarterly volumes was astonishing, jumping from \$5bn to \$42bn to \$106bn in just three quarters. Notably, altcoin volume was greater than BTC and ETH volume combined for the entirety of the bull run, which is highly unusual for U.S. exchanges.

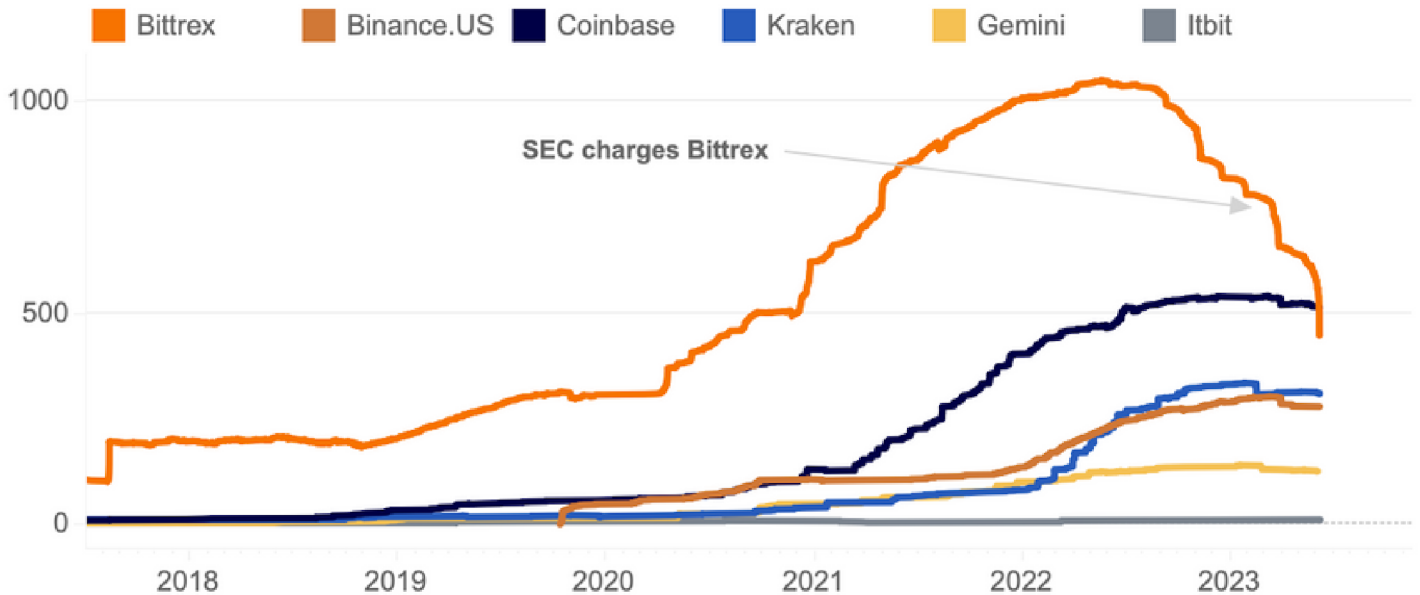
COTI Hourly Volume Distribution in 2022



The SEC pointed to the altcoin COTI as an example of wash trading on Binance.US, claiming that CZ's trading firm Sigma Chain was responsible for up to 35% of the token's volume. As shown below, its hourly distribution of volume in 2022 was strange, showing spikes in seemingly random hours in different months. Meanwhile, other exchanges show a smooth distribution that usually peaks in the morning in the U.S.

SEC States Certain Tokens Are Securities

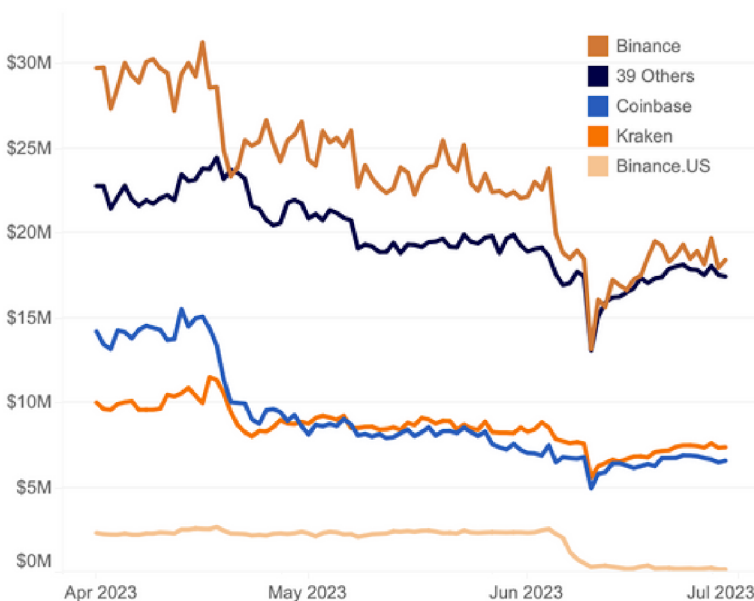
Number of Active Spot Trading Instruments on U.S. Exchanges



The SEC alleged that Binance, Binance.US, and Coinbase have all offered trading of unregistered securities, naming about 20 tokens that it considers securities, including SOL, ADA, and FIL. Regarding Coinbase, it also named NEXO, a token that is only available on DEXes through Coinbase Wallet.

However, the first set of charges this quarter came against Bittrex, also for offering trading of unregistered securities. When examining the number of actively traded spot instruments it's clear why: Bittrex was by far the most aggressive U.S. exchange in terms of new tokens, while Coinbase became more aggressive in 2021.

SEC-Identified Token Liquidity Combined 1% Market Depth of Tokens

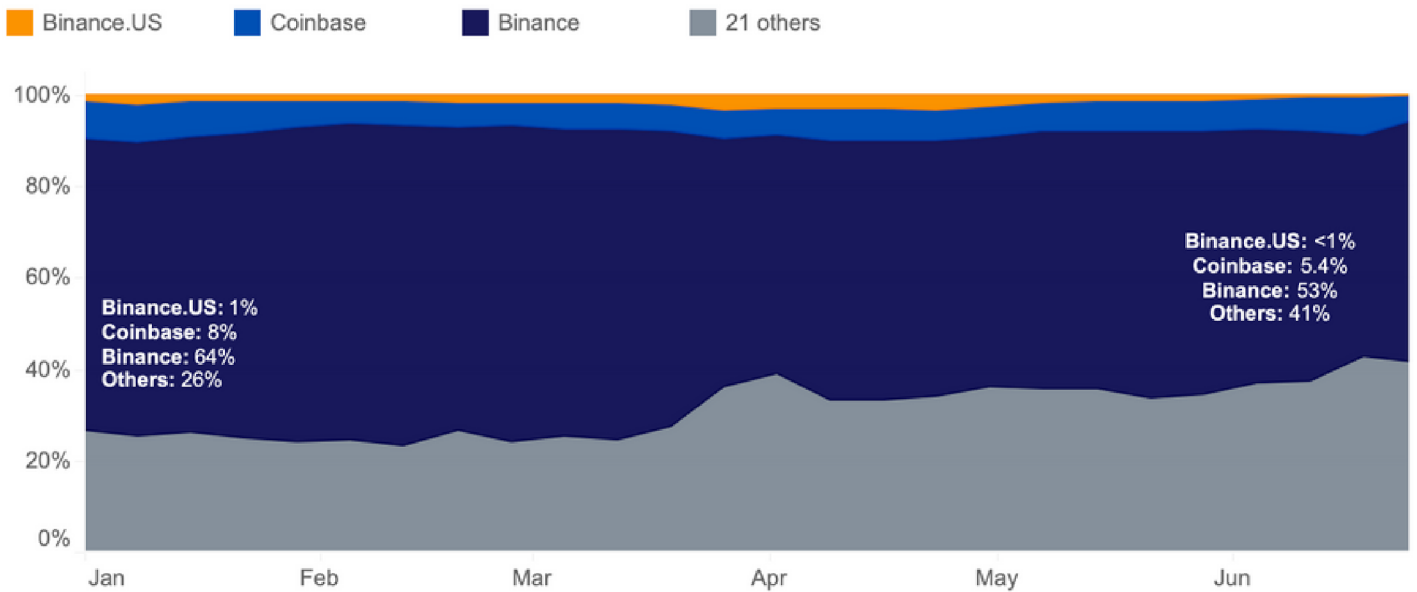


The charges had significant effects on liquidity, especially on the liquidity of tokens identified as securities by the SEC. Coinbase's liquidity for these tokens suffered most following the Bittrex lawsuit, dropping from \$15mn to \$10mn in a matter of days. However, the sharpest dips were on Binance and Binance.US after charges were filed against them. Binance's liquidity has largely recovered while Binance.US's has continued to decline as market makers left the exchange, standing at under \$200k at the end of the quarter.

Binance's Market Share Takes a Hit

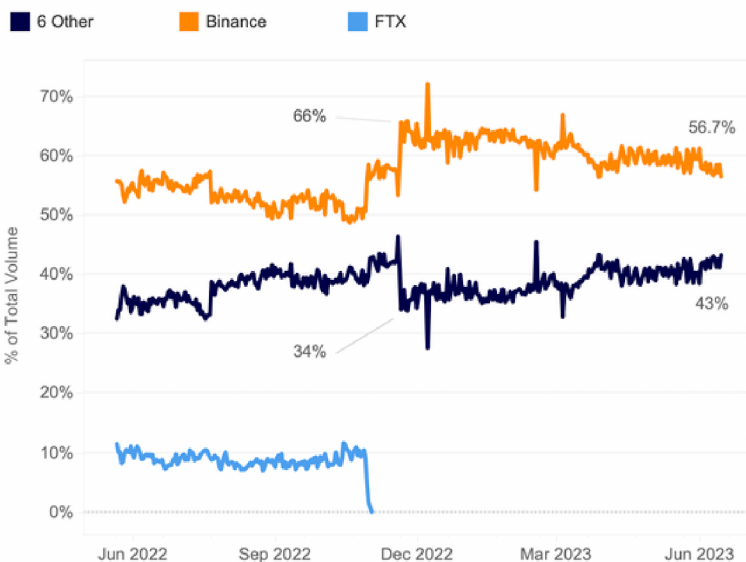
Binance Ends Most Zero-Fee Trading

Spot Volume Market Share



Binance closed out the previous quarter by reinstating trading fees for BTC-USDT and BTC-BUSD spot pairs. This, combined with some major lawsuits from the SEC and CFTC, has contributed to Binance's market share of spot volumes dropping from 64% to 53%. Binance's share has gone to a variety of exchanges, with Bybit and OKX faring best, in what is arguably a healthier market structure for exchange competition. Meanwhile, Coinbase's market share fell from 8% to 5.4%.

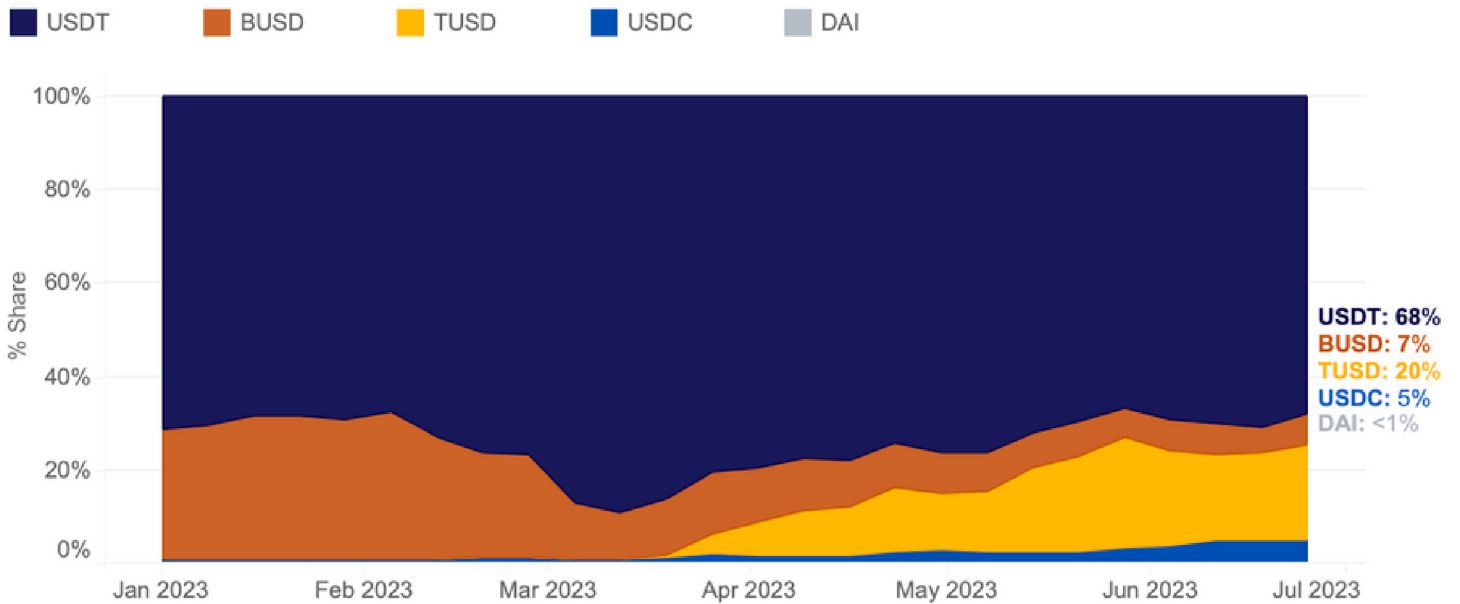
Market Share of Perpetual Futures Volume



Binance's share of derivatives volume has also been on a steady decline in 2023. Since the CFTC took up a case against Binance futures markets, the exchange has struggled to capture the same market share it did towards the end of last year. Starting the year at 66% of perpetual volumes, Binance has lost nearly 10% market share year to date, clocking in at 56% today.

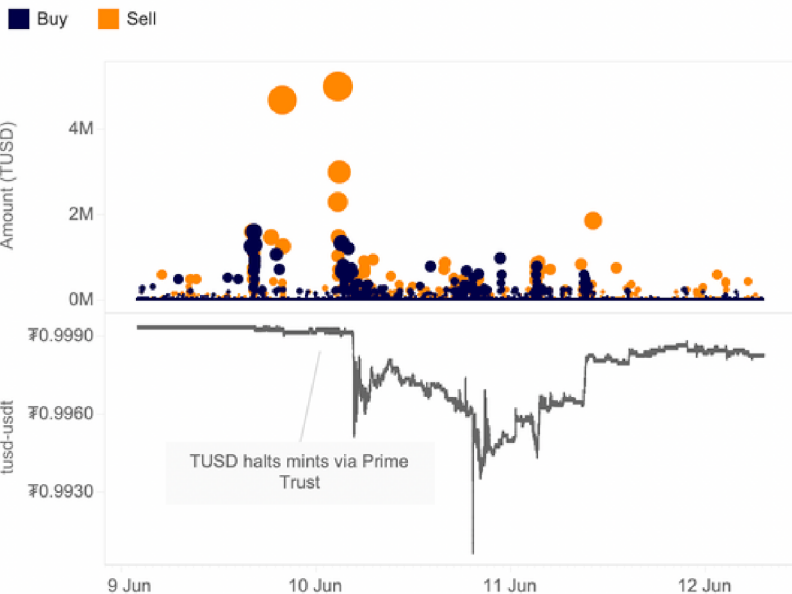
TUSD Gains Market Share Amid Depogs

Stablecoin Volume Market Share on CEXs



TUSD’s market cap and trade volume have soared ever since Binance promoted the stablecoin by eliminating fees for the BTC-TUSD pair. The pair has since overtaken BTC-USDT as the most traded BTC market in crypto and currently accounts for 61% of all BTC volume on Binance. Overall, TUSD pairs account for 20% of volumes across all exchanges. However, while trade volumes have surged, liquidity as measured by order book depth has lagged, which suggests market makers are cautious about providing liquidity for the stablecoin. In the last few days, Binance has removed trading fees on more TUSD pairs, likely leading to another surge in TUSD market share and market cap.

TUSD Depogs

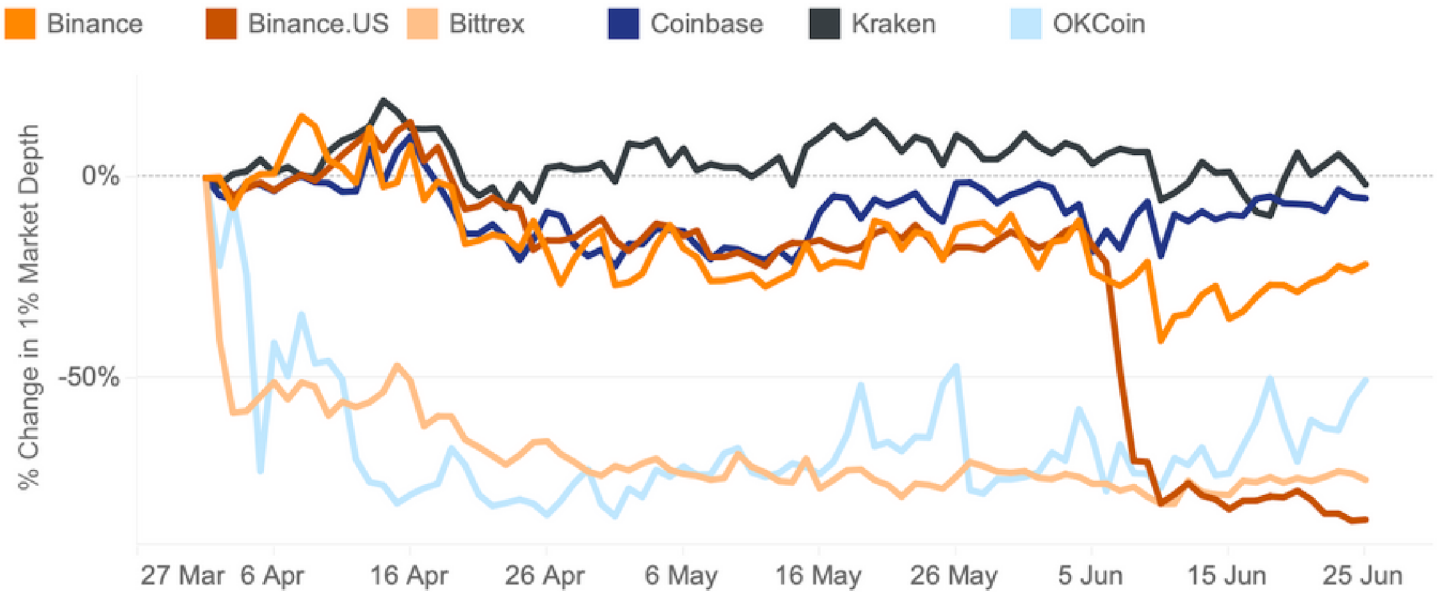


In the early hours of June 10, TUSD fell to its lowest level against USDT since March, hitting 0.994 following a wave of large sell orders on Binance. The selling started after news [broke](#) that one of the stablecoin’s partners, Prime Trust, would temporarily halt minting. Nevada regulators have since asked a federal court to impound the company’s assets, alleging that it purchased crypto with customer funds.

Liquidity's Slow Recovery

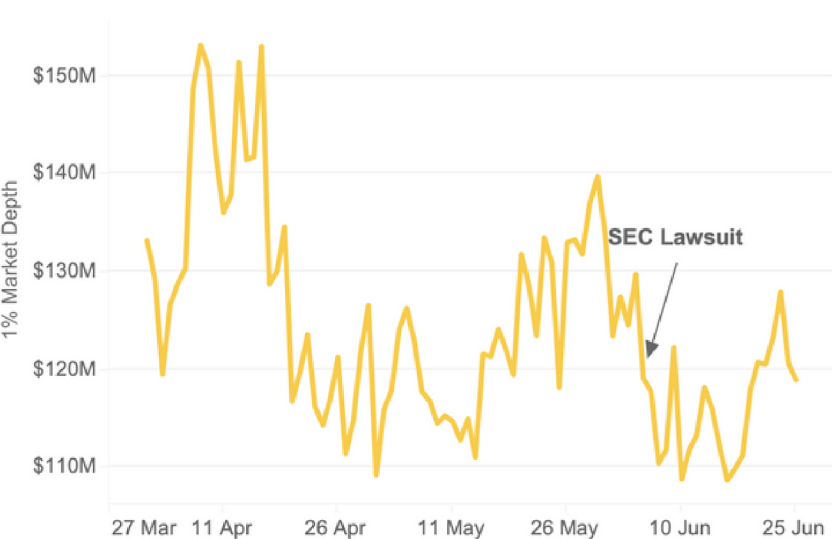
SEC Charges Cause Market Depth Drop

% Change in Market Depth, Top 10 Assets



Some exchanges are feeling the brunt of SEC enforcement from a liquidity standpoint. Bittrex, Binance.US and OKCoin have seen their market depth drop the most for the top 10 tokens, with Bittrex depth down 68%, while Binance.US and OKCoin are both down 85% year to date. OKCoin suspended their USD deposits after the banking crisis in March. The suspension was only supposed to be temporary but a lack of alternatives has meant the suspension is still in place, hampering liquidity on the exchange as a result.

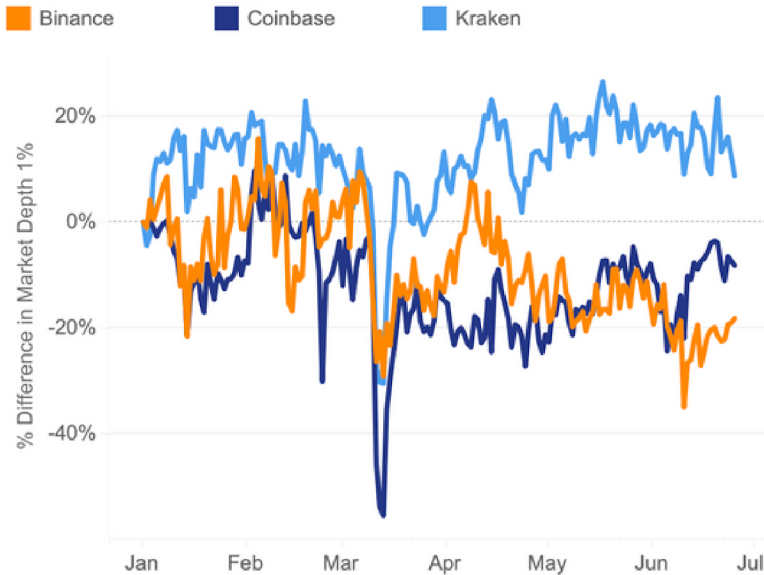
BTC 1% Market Depth,



Global BTC liquidity has been grinding lower throughout the quarter, down over \$10mn. Two significant market makers, Jane Street and Jump, announced they were winding down their liquidity operations in the U.S. and there has been no recovery in BTC market depth since. The SEC lawsuits against Binance and Coinbase caused another dip in depth, though this has since recovered amid the latest rally.

Kraken's Liquidity Holds Strong

1% Market Depth of Top 10 Tokens

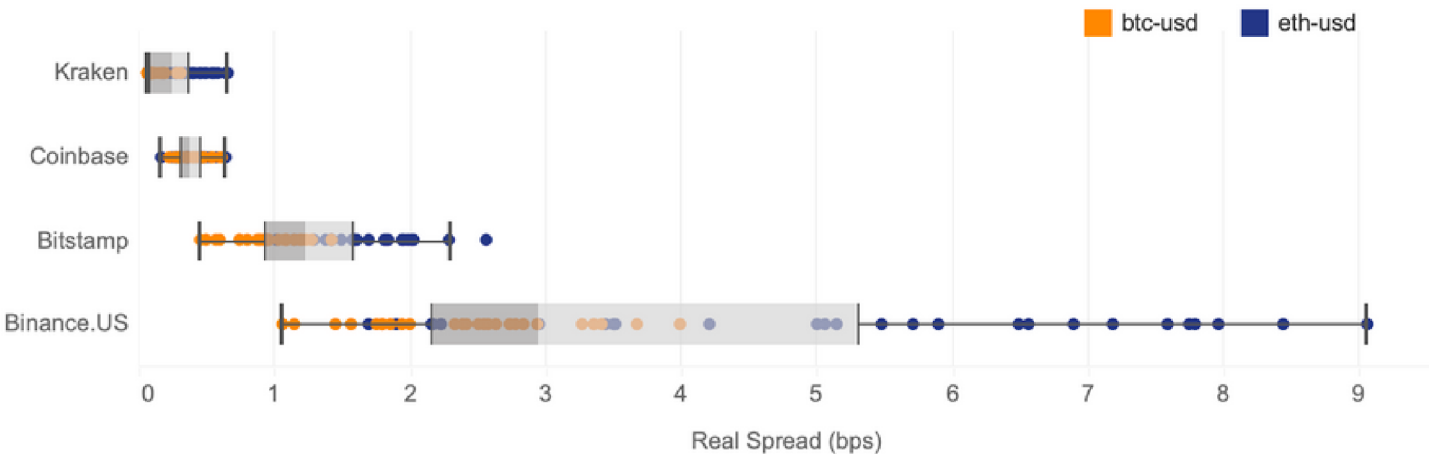


Kraken's liquidity has been remarkably resilient. It was one of the only exchanges we cover that has increased market depth since the start of the year. Liquidity on Coinbase and Binance is generally good proxy for the overall market, with Coinbase liquidity improving to end the quarter, down 7% since January compared to Binance's 20% loss.

Kraken's spreads are tighter than Coinbase's and currently the best in the U.S. Meanwhile, Binance.US is struggling.

Kraken Spreads Tightest as Binance.US Suffers From Wider Dispersion

Real Spreads for month of June



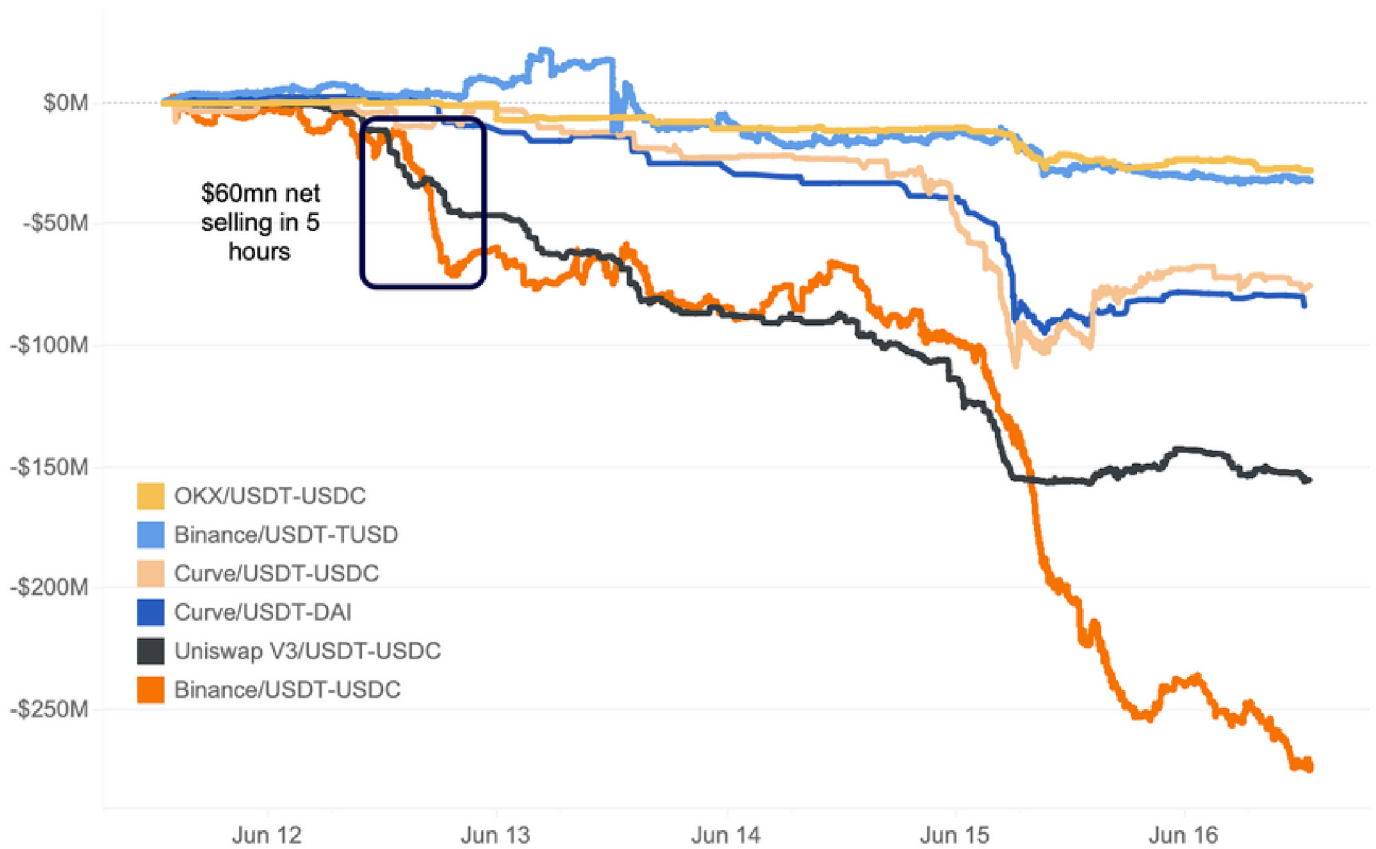
Liquidity disproportionately suffering in the U.S.

Liquidity falling in the U.S. is now a significant trend that has impacted prices on Binance.US and Coinbase throughout the quarter; with less liquidity, prices have less support to both the upside and the downside. It is also possible that U.S. exchanges will lose market share to their overseas counterparts in the short term. However, Kraken looks quite strong from a liquidity standpoint, while overseas exchanges like OKX have grown both market share and liquidity, at the expense of Binance.

Tether Depegs

Cumulative Volume Delta for Major USDT Pairs

Negative indicates net selling of USDT



USDT briefly depegged down to \$0.995 in mid-June ahead of stories from CoinDesk and Bloomberg detailing the stablecoin's backing in 2021, showing that some funds were in commercial paper issued by Chinese financial institutions. The chart above shows Cumulative Volume Delta (CVD) for major USDT pairs, including those on DEXes. It indicates that there was significant USDT selling on Binance roughly four days before the story was released and three days before USDT actually depegged, suggesting larger holders may have been aware of the coming stories.

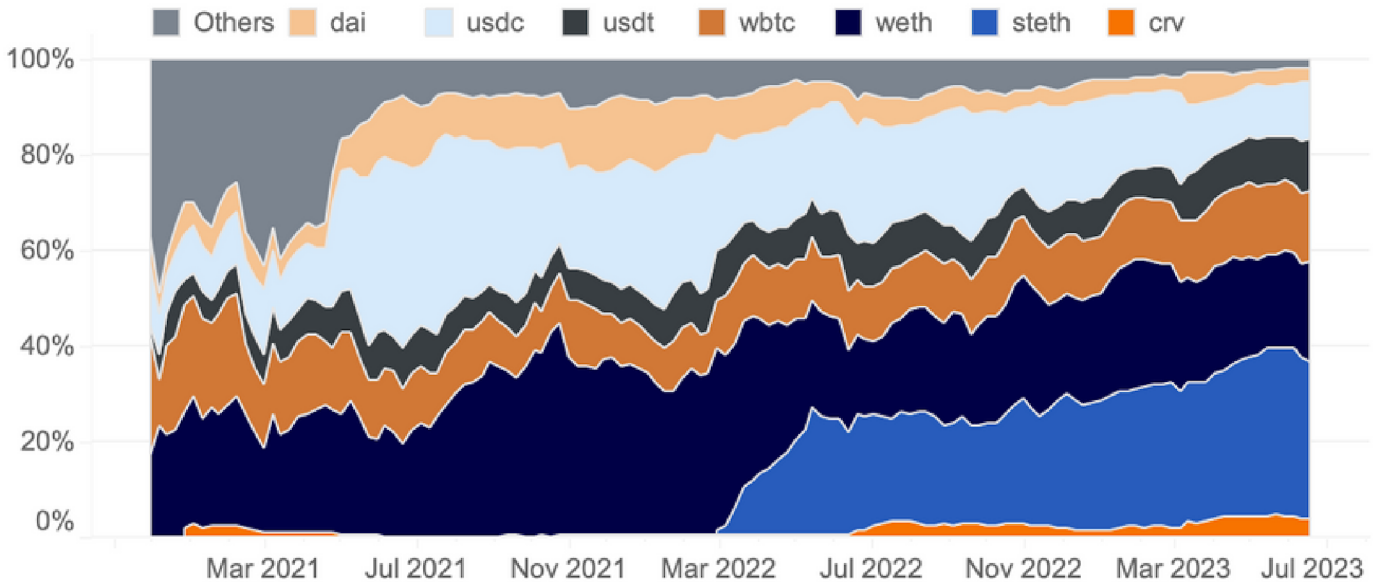
DEXs, too, accounted for significant selling, with Uniswap V3 facilitating \$150mn net selling, while Curve's 3pool accounted for \$150mn net selling, split roughly evenly between USDT-USDC and USDT-DAI.

Depegging risks remain in the crypto industry.

We've already established that liquidity has remained low this year, which raises risks for stablecoins. USDT is particularly vulnerable to minor depegging events because of its fees and minimums: 0.1% with a minimum redemption of \$100k. In some cases, it may be economically rational for large USDT holders to simply sell their USDT on the open market rather than incur the fee. Additionally, retail users will likely not meet the minimum redemption requirement, again creating a barrier to reducing supply.

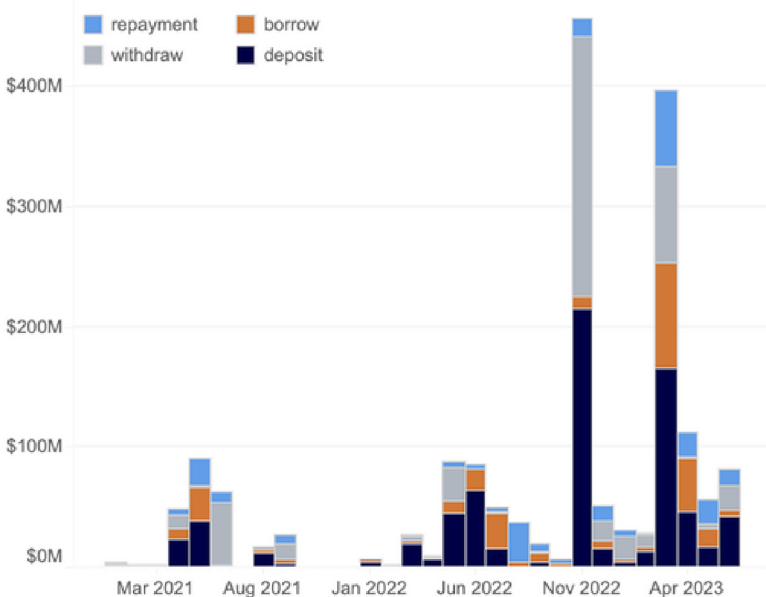
Aave Reconsiders Risk Management

Aave V2 Deposits Share



Concerns were raised in the Aave governance forum after a risk manager noticed that Aave V2's CRV market had continued to grow even as CRV liquidity has suffered alongside other altcoins. Nearly all of the CRV that has been deposited to Aave V2 belongs to Michael Egorov, the CEO and founder of Curve Finance. Currently, his position stands at nearly \$200mn CRV deposited and \$65mn USDT borrowed. Notably, this is the same position that Avi Eisenberg targeted in his attempted exploit of Aave, though at the time Egorov had under \$50mn of CRV deposited. Shown above, CRV has come to represent an increasing share of all Aave V2 deposits as its value has increased and other altcoin markets have been mothballed.

Curve CEO's Aave V2 Activity



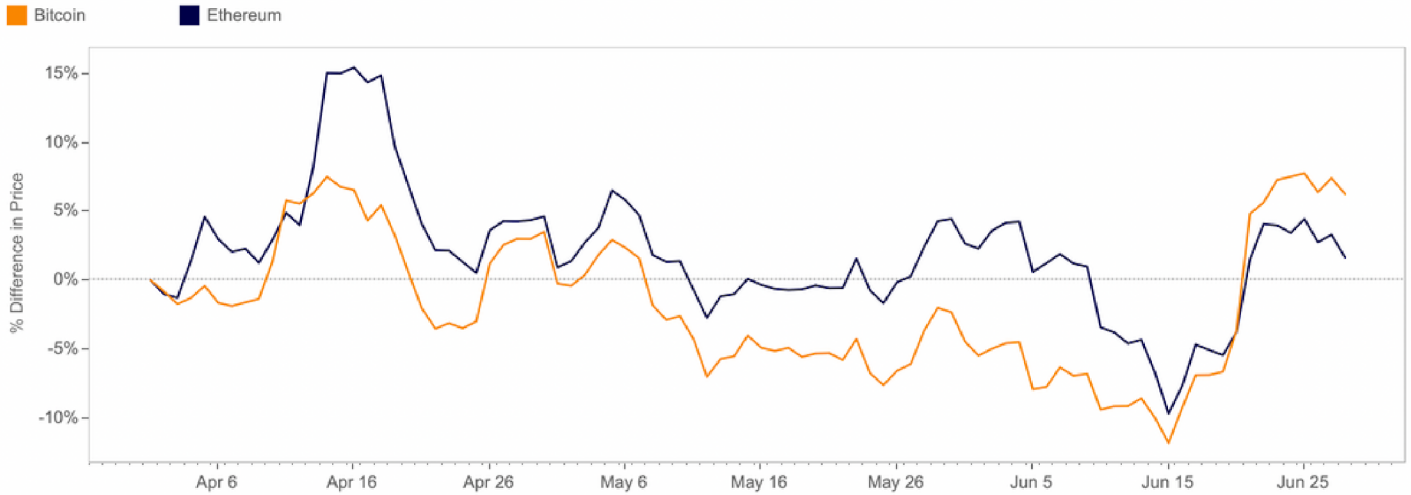
To the left is shown all of Egorov's transactions on Aave V2, aggregated monthly. His activity has been higher in recent months, but still has not surpassed November 2022's level. This was the month of Eisenberg's attempted exploit, and Egorov made significant deposits to protect his loan's health.

If this position were to be liquidated, Aave would almost certainly be left with significant amounts of bad debt because of a lack of CRV liquidity, as explained in our Deep Dive.

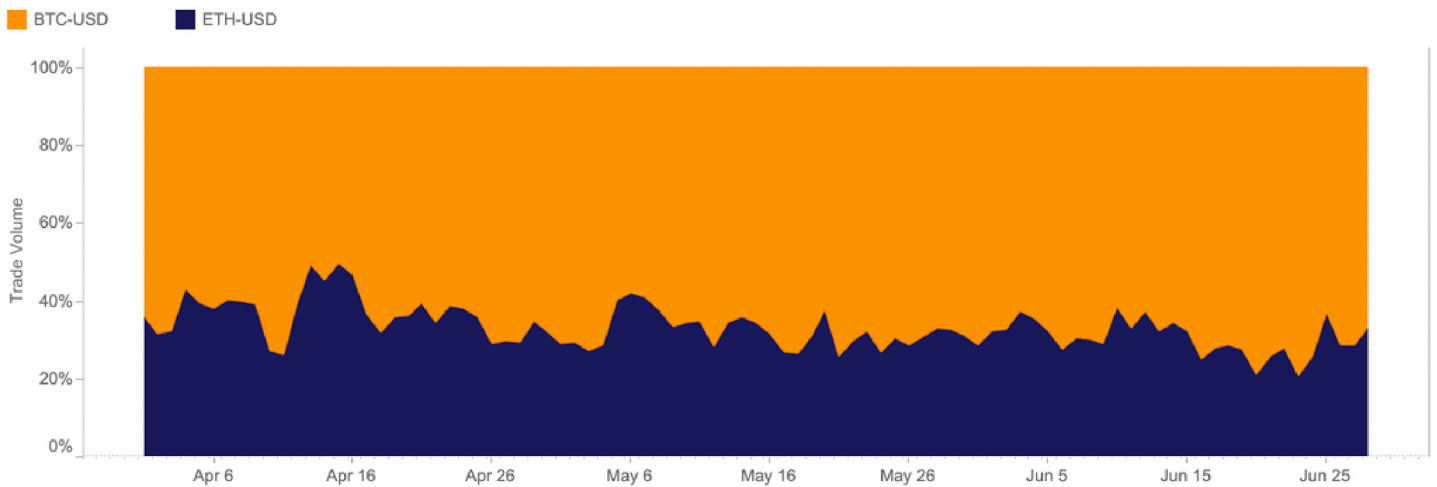
Q2 Chartbook

Price, Volumes, & Liquidity

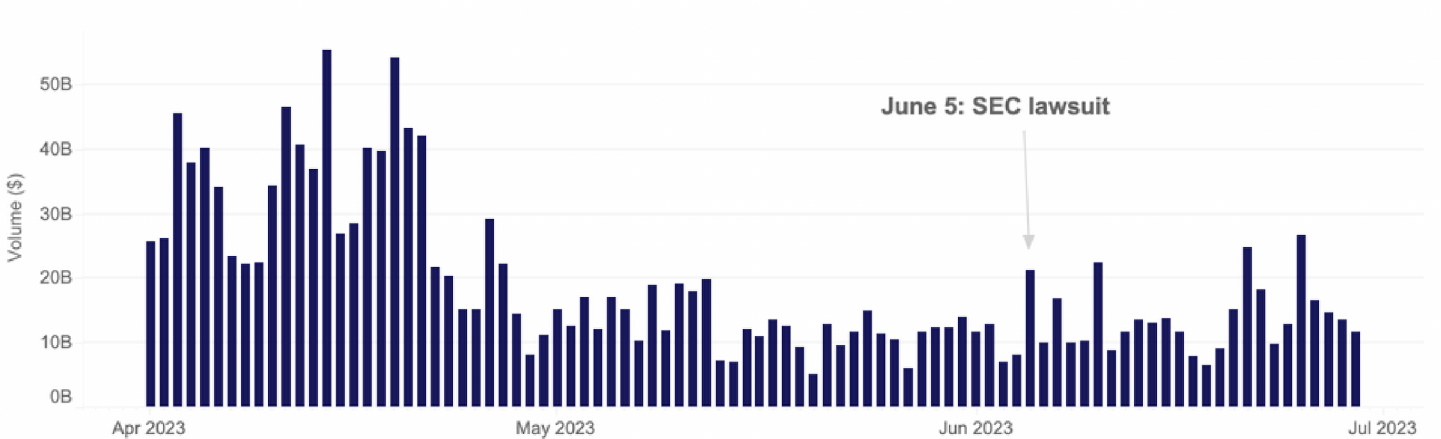
Quarterly Returns



BTC to ETH Spot Volume Ratio

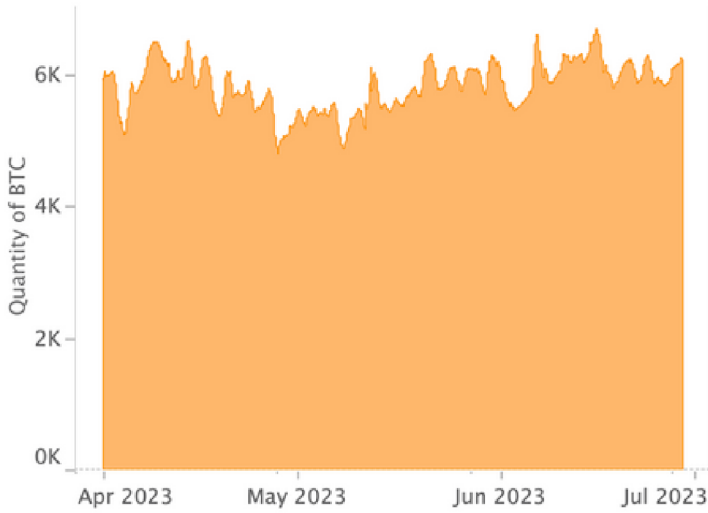


Daily CEX Spot Volume

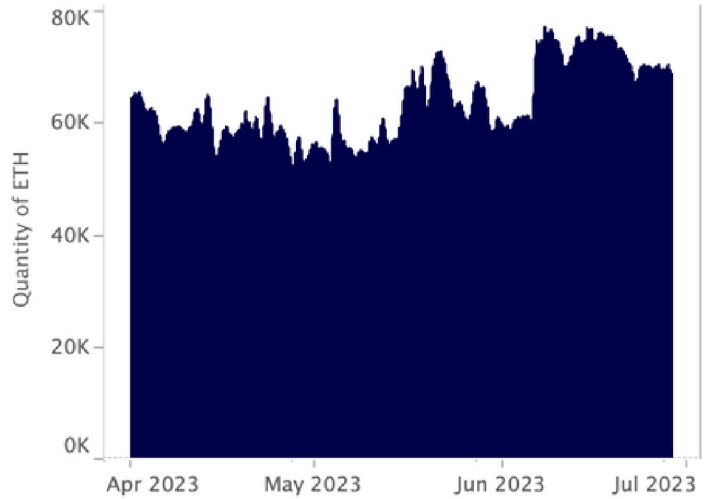


Aggregated 2% Market Depth

BTC-USD(T)



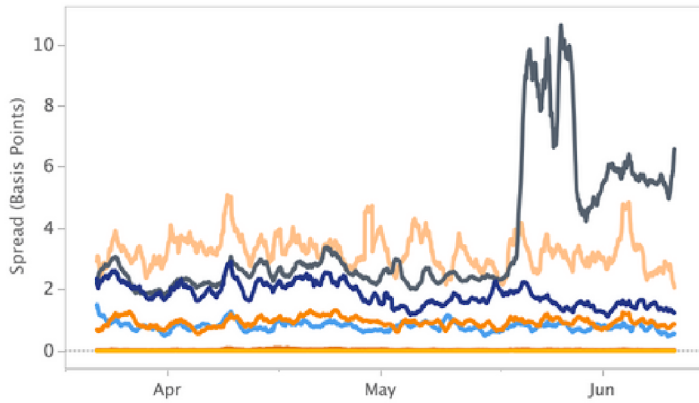
ETH-USD(T)



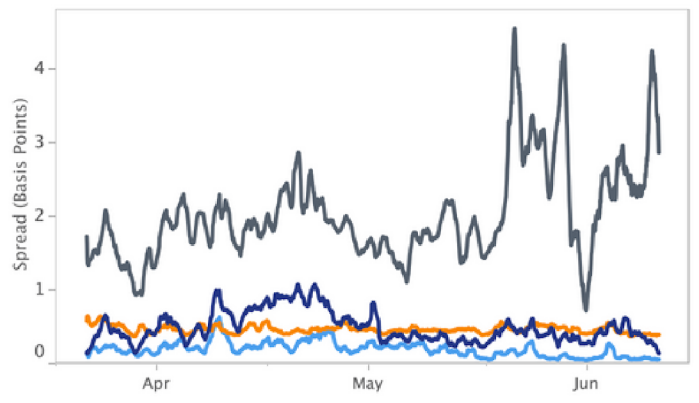
Bid-Ask Spread

- Coinbase
- Kraken
- Binance
- Poloniex
- Bitfinex
- Binance US
- OKX

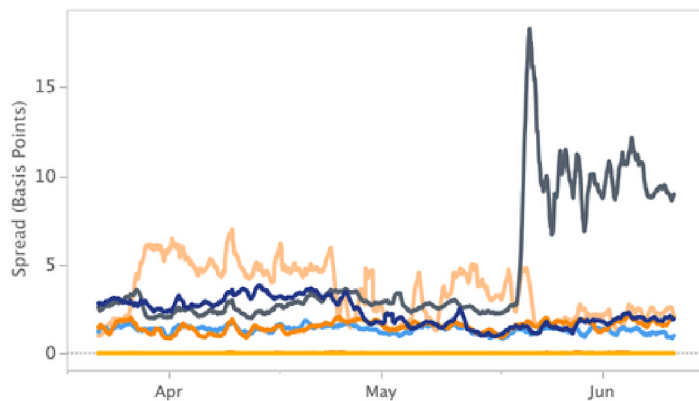
BTC-USDT



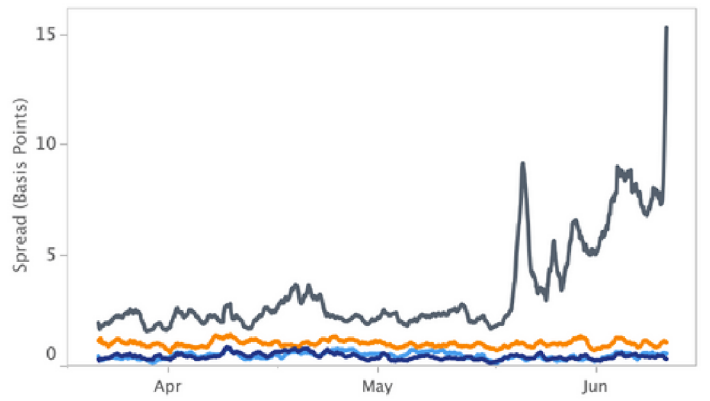
BTC-USD



ETH-USDT

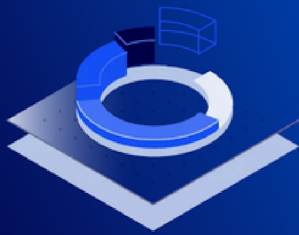


ETH-USD



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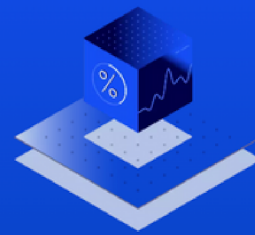
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