

RIVEMONT

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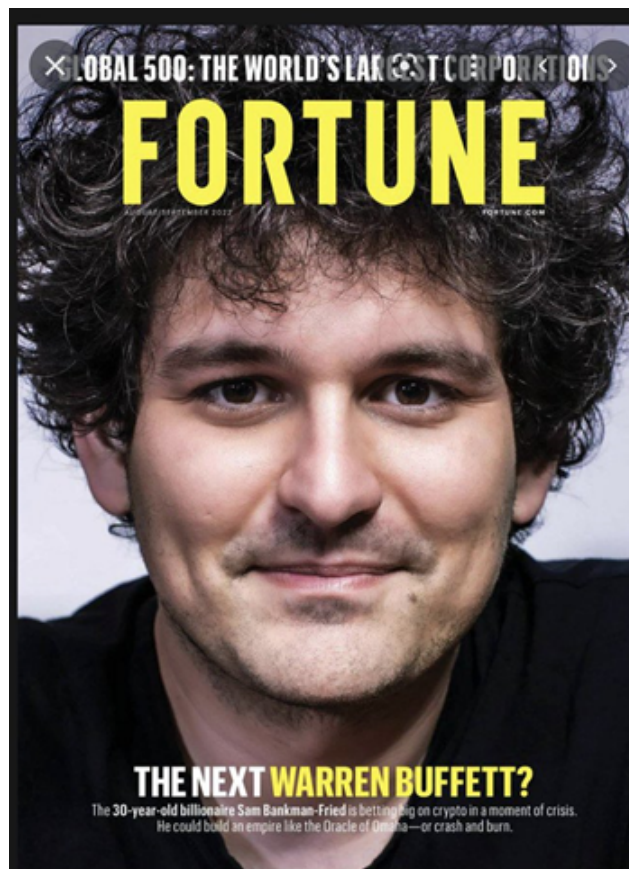
Rivemont is the portfolio manager responsible for the investment decisions of the Rivemont Crypto Fund.

For a rare time this year, this letter will not begin with a contextualization with macro elements affecting the markets as a whole in a specific direction. Instead, it was a new crisis entirely specific to cryptocurrencies that rocked the markets yesterday. As cryptocurrencies continued their gradual rebound alongside the stock markets, it was a saga involving the massive Sam Bankman-Fried (SBF) FTX exchange - a crisis that might have made the LUNA and Celsius ones seem secondary in comparison - that pushed the markets over the precipice. Let's reserve that communication to explain exactly what happened. While the story is certainly worrisome for investors in the short term, it is nonetheless fascinating from a business perspective despite the large and unpleasant

financial impact.

Let's first put things in context. Binance is by far the most popular and profitable exchange in the cryptocurrency market. Its closest competition, however, was FTX, a multi-billion dollar company. It was these two titans that rubbed shoulders this week.

Binance predates FTX's existence. Several years ago, Binance was an early investor in the FTX startup. However, Bankman-Fried's growth strategies quickly paid off in a favorable market, with the exchange growing at a rapid pace to become the 2nd largest in market shares and consequently the direct competitor of Binance. During the most recent crises, SBF always seems to be involved, trying to buy out the failing entities. Only a few months ago, he was seen as the possible savior of the industry. Fortune magazine even called him a possible future Warren Buffett, no less.



In this context where the two exchanges were now direct competitors, Binance decided to sell its shares in FTX. Under the terms of the deal, Binance agreed to receive the equivalent of \$2 billion in FTT tokens, the native token of FTX. This token was still worth \$22 as of early yesterday. Now, it is important to know that FTT does not have the trading volume of a token like BNB (Binance's native token).

Then, two days ago, Binance's CEO Changpeng Zhao (CZ) publicly stated that SBF was speaking ill of him to the various regulators, attempting to "tamp down" his competitor to the possible detriment of the health of the industry in general. As a result, he announced to his 7M followers on Twitter that he was about to sell his entire \$2 billion worth of FTT tokens on the open market. The message to the token holders could not be clearer and more disturbing. Such

selling pressure for a token at such volume and in a climate of uncertainty was likely to completely crush its price. Panic gripped the markets. Everyone wanted to sell their FTTs, but with no buyers lining up at the doors. The price, unsurprisingly, fell back greatly.

Along comes Alameda, a parent firm of FTX and owned by SBF. It is a market maker that officially holds \$12 billion in assets and \$7 billion in liabilities. However, half of the assets are composed of FTT tokens whose price is crashing and whose market offers no liquidity. Overnight, the firm appears in mortal danger. Alameda offers to buy all of Binance's FTT tokens at \$22 apiece, but CZ doesn't intend to take it that way, responding that he prefers to use free market forces instead. If Alameda is suddenly facing such a risk, what about FTX, the very firm behind the FTT token? SBF may be sending out a message that everything is okay and client assets are safe, but investors remember the recent sagas all too well. They are scrambling at the gates to withdraw all of their crypto assets from FTX. The exchange is facing over \$1 billion in withdrawals. A true liquidity crush. A modern day run to the bank.

Rather than reassure exchange members, FTX instead announces a freeze on withdrawals. The panic reached its peak. It was soon learned that there were no bitcoin left to withdraw from FTX's reserves.

Then, suddenly, an announcement that would have been unimaginable just a few days ago dropped. Binance buys FTX to get them out of trouble and ensure the safety of customer assets. The markets applauded the news for a moment with a strong rebound, before the dust settled. The worst-case scenario seems to have been averted for now. Nevertheless, the price of an FTT token is now only \$4.20, a drop of over 80% in 24 hours. All those who use it as collateral are suddenly facing a critical situation, having to sell other of their assets like BTC and ETH. Once again, the leverage of some market players suddenly in crisis creates a downward pressure on prices. In addition, we find ourselves with a suddenly highly centralized exchange market. The agreement for Binance to purchase FTX has not yet been signed either and is subject to a due diligence review. CZ is the only driver now. What will he do? The death of FTX is not yet

completely impossible. As we know, markets hate uncertainty.

If you like the raw forces of capitalism, this is a story to marvel at, despite its passing consequences on prices. In the space of a few days, Binance launched a rumor, made a public threat, which led to the purchase of its biggest rival for possibly pennies on the dollar. A true hostile takeover between the industry giants.

Note that the acquisition only affects the non-US operations, FTX.com. FTX.us will remain independent of Binance. However, according to an audit conducted in 2021, the U.S. portion of FTX accounted for only 5% of revenue.

Later Tuesday, CZ tweeted that he believes "all cryptocurrency exchanges should use merkle-tree proof of reserves." In the same tweet, he added that if banks operate with fractional reserves, crypto exchanges should not. Zhao also later said that Binance has never used BNB as collateral and that he believes no exchange should use its native token as such. History has shown us this three times rather than once already in 2022...

For Sam Bankman-Fried, this is what could be sarcastically described as a bad day at the office. In 24 hours, the FTX CEO lost about \$14.6 billion, or nearly 94 percent of his total wealth, according to the Bloomberg Billionaires Index. In fact, he's no longer on that list. SBF, 30, said last year that his company would be big enough to buy Goldman Sachs. He can forget about that. The 94% loss is the biggest one-day collapse ever among billionaires.



Needless to say, this saga continues to drive the markets. The price of bitcoin, which was doing well just last week, has painted a new annual low. Will this transaction quickly put this crisis behind us and allow the process to rebound to the level of the past few weeks? After all, the fundamental value of bitcoin and ether has certainly not changed. It is the level of uncertainty that has risen. Instead, will more pages of this story be written, with consequences that are impossible to predict today? As one popular analyst put it: "Stocks are doing well. A Black Swan event ruined the price action for cryptos, but once that taste is out of people's mouths, we should see \$BTC and \$ETH put on a small rally. Once again, the problem is not with the assets themselves."

Volatility will certainly be with us for some time to come. Tomorrow was already forecast as such with the October US Consumer Price Index data.

As for the fund, we were overweight in ETH at the beginning of the current crisis, which certainly did not help. However, we reacted quickly to move these assets into BTC in the first wave of selling, and then raised cash in the second wave. We estimate our losses in the last 24 hours to be equivalent to those of BTC, despite our initial position in ETH. We are therefore currently positioned defensively with a higher level of liquidity.

Rivemont Investments, manager of the Rivemont Crypto Fund.

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