Making sense of the growing interest in Ether

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Ethereum has been on a massive run this year; despite the recent crypto market pull back ether (ETH) is up over 250% YTD[1] at the time of writing. Interestingly, it is also up over 200% vs Bitcoin which shows its increasing size and importance within the crypto universe. Given these moves we thought it was worth examining some of the drivers:

Excitement over ETH 2.0

There is a great deal of excitement in the space around proposed future developments to the Ethereum network that many are lauding as the next big thing to drive the ecosystem forward. There are wide ranging changes planned, but the two major developments are, firstly, the move to Proof of Stake (POS) from Proof of Work (POW) as a consensus mechanism and, secondly, the development of “layer 2” solutions to help with network scaling. There is speculation that these changes will help propel the usage of the Ethereum network bringing more users and more projects on to the platform.

Additionally, the potential change to POS is tapping into a raging debate in the crypto sphere: Energy usage. POS is much less energy intensive than POW and, as such, some speculate that this could be a tailwind for the platform’s adoption.

Another interesting element of ETH 2.0 is changing the gas fee mechanics which will result in a portion of the ETH used to run a smart contract being destroyed in the process. This adds a structural deflationary element to ETH and there are many out there speculating that would allow the protocol to tap into the limited supply/store of value narrative that has been big a driver of investments in Bitcoin.

Decentralised Finance (DeFi) developments

One of the most innovative deployments of the smart contracts has been the rapid growth of DeFi which has mostly occurred on the Ethereum network. This is essentially using decentralised technology to automate the way value is transferred, a role historically done by big institutions and one that that has been very profitable. There are DeFi products which are aimed at replacing exchanges, disrupting lending, innovating bond issuance and the list goes on. For example, the LINK and Uniswap DeFi projects on Ethereum have attracted large amounts of capital and are showing huge potential. If Ethereum can maintain its dominance in this space it should continue to drive demand for ether.

Cyclical rotation from Bitcoin as prices trend sideways

Bitcoin is still the most ubiquitous cryptocurrency. Its bull runs generate the most attention in media and it is by far the most common entry point for new money entering the market. But we all know that market

moves come in cycles so, as the steam comes out of bitcoin, we see investors looking to take profits and rotate into something else and ether is often their next choice. This isn't a new phenomenon and is followed by crypto pundits who talk about the market following a trend from BTC to ETH to large cap Altcoins[2] and DeFi and finally to the micro-cap projects.This was a pattern observed in the 2017 market and something we saw playing out prior to the crypto wide market pullback in May. Interestingly, this cycle seems to be picking back up where it left off with ETH and Altcoins leading the recovery.

Ethereum has always been an incredibly interesting innovation of the technology introduced by Bitcoin and the power of the smart contracts run on the network is being proven by the exciting projects being built on it. There is competition in this space with alternative projects launching to challenge Ethereum on various technical perspectives or limitations of the protocol (perceived or otherwise). However, the Ethereum development community are not resting on their laurels and are actively looking to address bottlenecks to wider adoption as can be seen in the ambitious upgrades planned. Additionally, as with anything that thrives on network, there is a hearts and minds battle at play. Ethereum has a huge head start on any competition; unseating Ethereum as the dominant smart contract or DeFi platform will take some doing.

[1] Source: Coinbase as at 7th of June 2021

[2] An Altcoin is an alternative digital currency to Bitcoin

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