Asset and Wealth Management Services: Market Update

Crypto and Digital Assets: Investor curiosity and demand continues to grow

November 2022 - Issue number 4

A fast developing asset class presenting investors with a new risk/return dynamic

Crypto assets offer investors a high potential for returns and at the same time are highly volatile in nature. This combination makes investors reluctantly attracted to this new asset class, as something new to add to their portfolios. As regulation underlying crypto assets improves and well reputed international financial institutions get more actively involved, investor comfort around crypto assets and holding crypto in their portfolio is expected to continue to improve.

The rise of decentralised finance should not be seen as just another wave of digitalisation: blockchain has the potential to significantly disrupt the way businesses operate. With the crypto asset market cap experiencing a ~94 percent CAGR over the period 2013–2021, the crypto ecosystem should no longer be viewed as immature, given it already spans several blockchains and decentralised applications.

What investors find attractive

- Alternative asset class
- High potential for returns
- Something new to add to the portfolio
- Perception of inflation hedging

What investors are most concerned about

- Regulatory concerns
- Too much volatility
- No idea how to value cryptocurrencies
- Lack of easily accessible investment vehicles list ETFs or mutual funds
- Custody concerns/fear of getting hacked/lack of understanding
- Association of crypto assets with criminal activity
- Unsure of where crypto assets fit within an investment portfolio

What is likely to make investors more comfortable to invest

- Better regulation
- Better education
- Launch of ETF type funds
- Better custodial solution
- Easier trading solutions
- Less volatility

Figure 1: A synopsis of how investors view crypto assets

Asset types evolution

Wealth management product and asset types will evolve from current native cryptos to more complex tokens and funds, incorporating tokenization of traditional types of assets. Players will develop an understanding and technology of the different levels of complexity in order to adopt decentralized protocols to mange them.

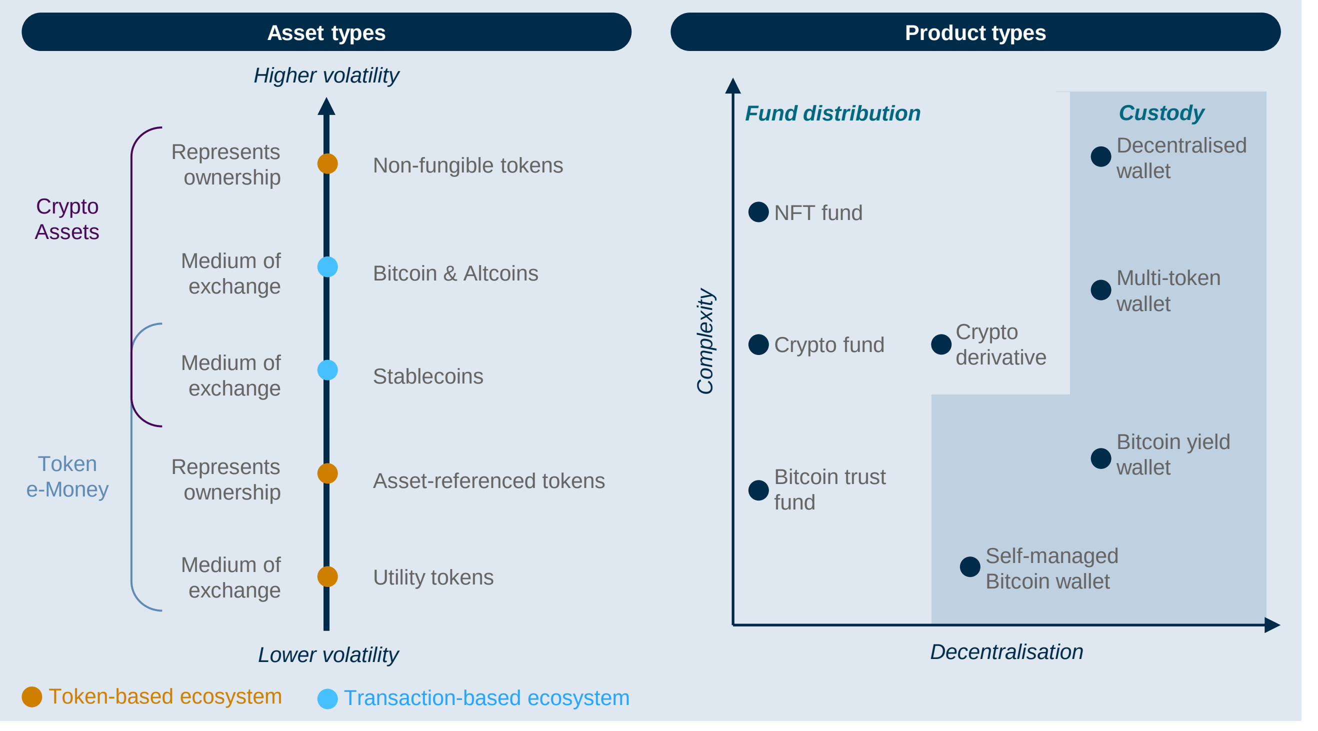


Figure 2: An overview of crypto assets and product types

Regulatory outlook

Regulation of crypto and digital assets will be ongoing and ever-evolving, though its foundations will come from existing capital market regulation at both global and local levels, adapted as required to each asset type.

Although the rise in popularity of crypto assets started in the early 2010s, regulatory responses just started materialising in the late 2010s, with the Digital Currency Governance Consortium only being established in 2020.

At its most basic, the regulatory response is ensuring that the crypto market controls are aligned with global and local existing directives (e.g., AML, MiFID). However, each geography is working on additional requirements specific to the various classes of crypto assets.

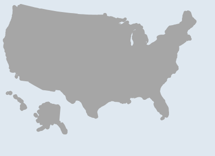
Europe

- EU Council and Parliament agreed on regulatory framework for Markets in Crypto-Assets (MiCA)
- EU AML framework will apply to crypto assets
- Stablecoins issuers to build up a reserve with a 1/1 ratio
- ESMA will require service providers to disclose environmental impacts

UK

- Bank of England and HMT expected to make a decision regarding rolling out a Central Bank digital currency
- Upcoming inclusion of crypto assets in the perimeter of Financial Services and Markets Bill
- Extension of Financial Promotion Order to cover crypto assets and other high-risk investments

USA

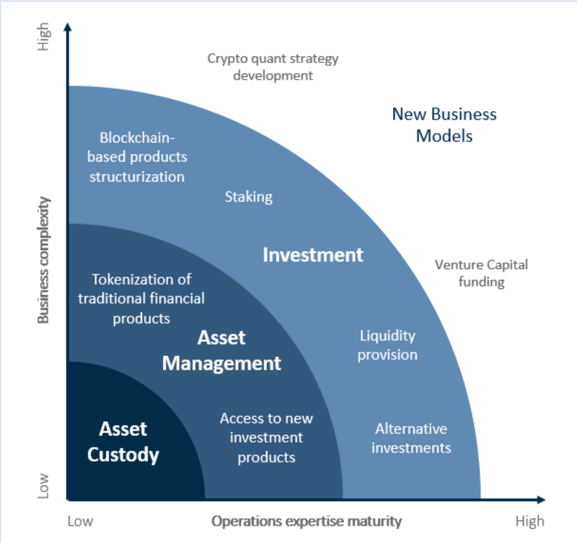


- Cryptocurrency is regulated under the Bank Secrecy Act
- Cryptocurrency exchange service providers must register with FinCEN, implement an AML/CFT programme and report to authorities as required
- Other crypto assets, such as NFTs and stablecoins, are not currently regulated, but this is under review

Figure 3: The evolving regulatory landscape

Embracing cryptocurrency and digital assets

By having a solid foundation and understanding of the basis of blockchain technology and products, increasingly complex solutions and services can be provided without significant operational risk



Asset Custody

- Custody services, related to asset availability and provision of cybersecurity, are the basis on which other digital asset services such as exchanges or blockchain-related developments rely for successful and secure performance.

Asset Management

- Provides access to crypto and digital assets to investors in addition to using the technology to tokenize traditional financial products
- The development of new asset markets with a blockchain base layer provide additional opportunities, leveraging on the operational efficiencies that blockchain technology provides.

Cryptocurrency Investment

- The access to the crypto environment provides access to a set of alternative investment vehicles and financial products leveraged on existing capital markets expertise.
- Besides standard alternative digital asset investment access and the potential to incorporate them to existing products (as a means of diversification), yield earning solutions (such as staking, lending or liquidity provision) provide new products with a varying spectrum of risk.

Figure 4: Business model complexity as products become more sophisticated

Solution development and service implementation

Crypto and blockchain technology implementation into financial institutions occurs in waves of complexity, leveraging operational experience and a more mature core ecosystem for crypto services integration.

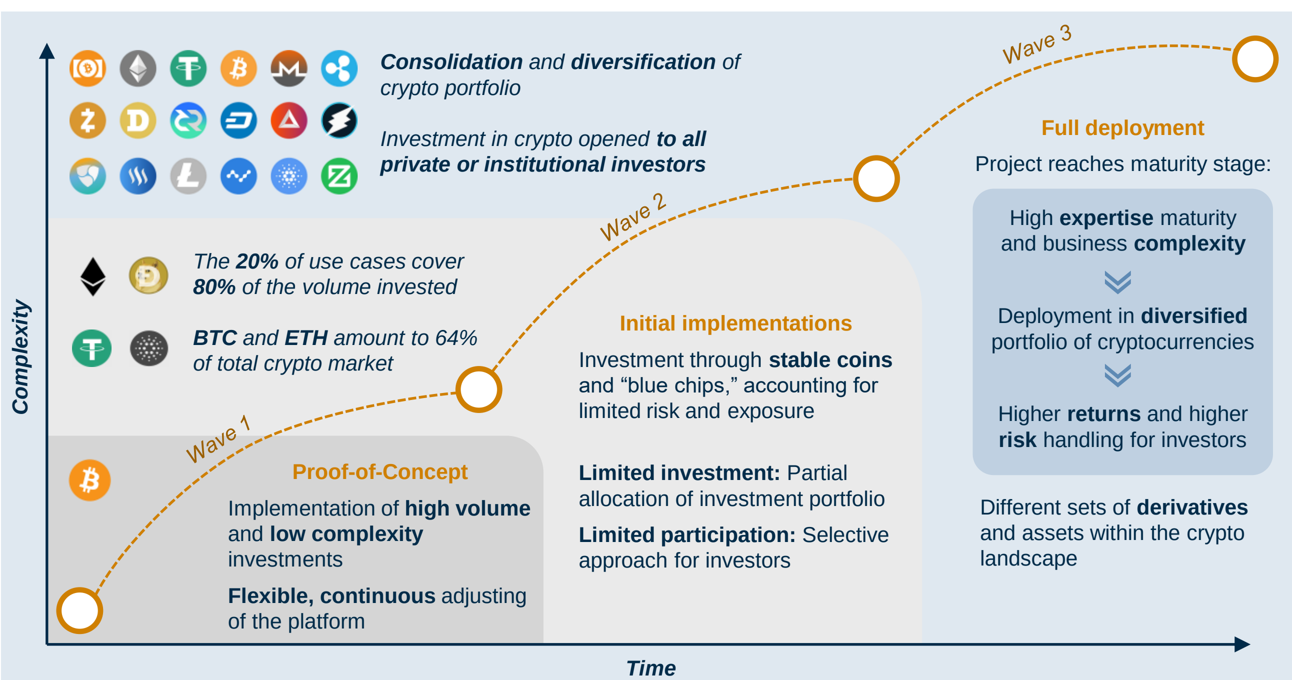


Figure 5: Implementation stages of crypto technology in financial institutions

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