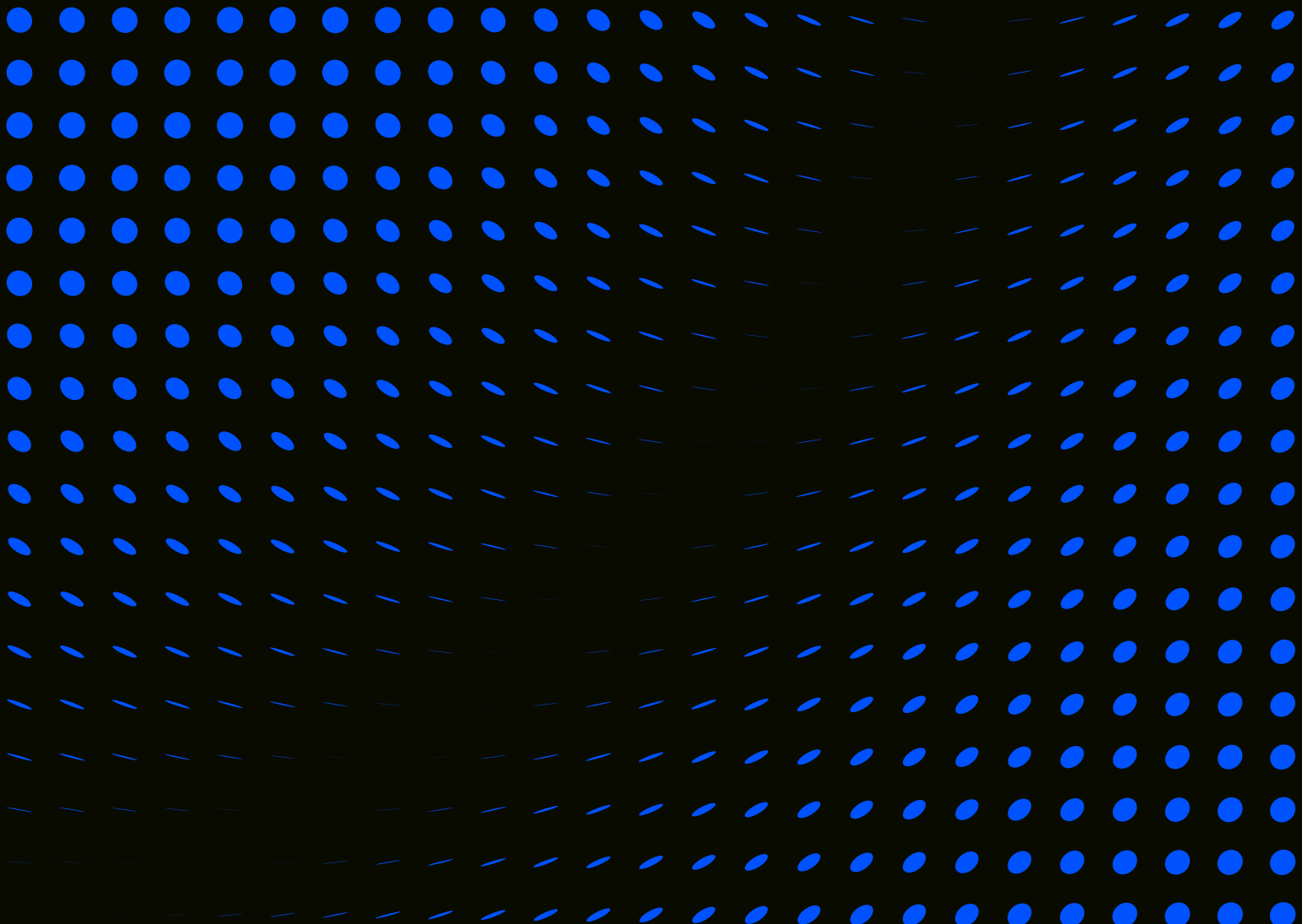


# 2021

## Global fund management report

**coinbase** INSTITUTIONAL





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# Introduction

The Global fund management report provides a broad overview of the crypto fund landscape, including the latest updates on regulatory changes and product trends. Coinbase has witnessed an increase in crypto fund activity to meet demand from investors seeking crypto exposure without buying, holding, and selling these assets directly.

Crypto fund assets continue to increase in aggregate supported by inflows, portfolio performance, as well as new entrants into the space, with more than \$36 billion in assets under management (AUM) at the end of 2020<sup>1</sup>. Coinbase has experienced significant growth through our partnerships with some of the largest financial institutions in the world, with our institutional assets on platform (AOP) reaching \$122 billion at the end of March 2021.

New investment products have continued to hit the market in 2021, with Grayscale Investments, the world's largest crypto asset manager, adding five more investment trusts to its fund family and Osprey Funds launching the Osprey Bitcoin Trust.

Canada continues to hold the spotlight with the launch of three bitcoin exchange-traded funds (ETFs). A number of investment managers in the U.S. are eager to follow, including Fidelity, WisdomTree, and VanEck, who have submitted bitcoin ETF applications with the U.S. Securities and Exchange Commission (SEC), anticipating approval of the first U.S. bitcoin ETF.

In Europe, the European Union has brought forward the MiCA (Regulation on Markets in Crypto Assets) Bill. If the law is passed, digital assets will become regulated financial instruments in the E.U. Australian regulators have also indicated that ETFs could feasibly exist under the Australian Securities Exchange's (ASX) AQUA rules, which govern other types of ETFs in the country.

Our report provides clients' insights on managing crypto investment products with our secure custody, advanced trading platform, and 24/7 support. If you would like to learn more about our solutions for fund managers, please contact us at [institutional@coinbase.com](mailto:institutional@coinbase.com).





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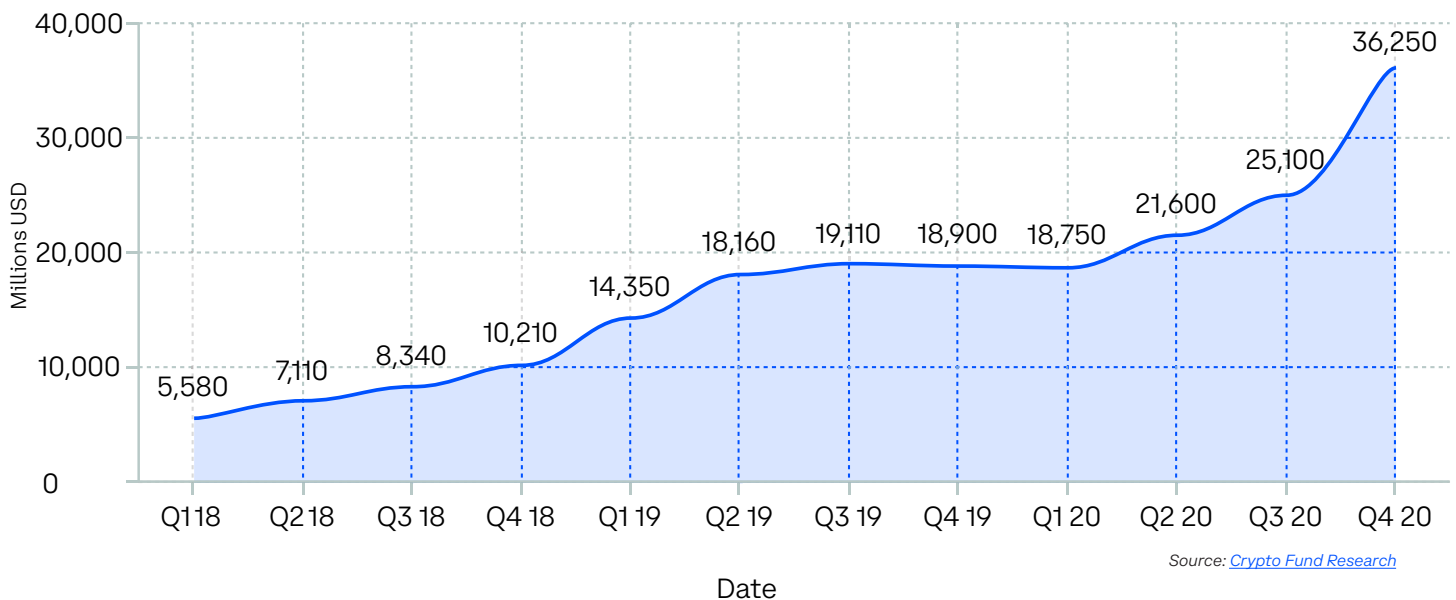
# Crypto fund universe

The crypto fund industry continues to expand as both crypto-native and traditional investment managers launch new strategies to meet investor demand. There are currently estimated to be more than 825 crypto funds globally, including venture capital funds, hedge funds, crypto ETFs, and crypto private equity funds.<sup>2</sup> Only 5% of recorded funds manage more than \$100 million, comprising the majority of assets in this universe.<sup>3</sup>

## Assets under management

The total amount of assets in the crypto fund universe almost doubled YOY, ending 2020 at more than \$36 billion.<sup>4</sup> Major crypto assets created strong performance for these funds, with bitcoin achieving a 321% return in 2020, and continuing to show momentum with an almost 50% YTD return at the end of Q1 2021.

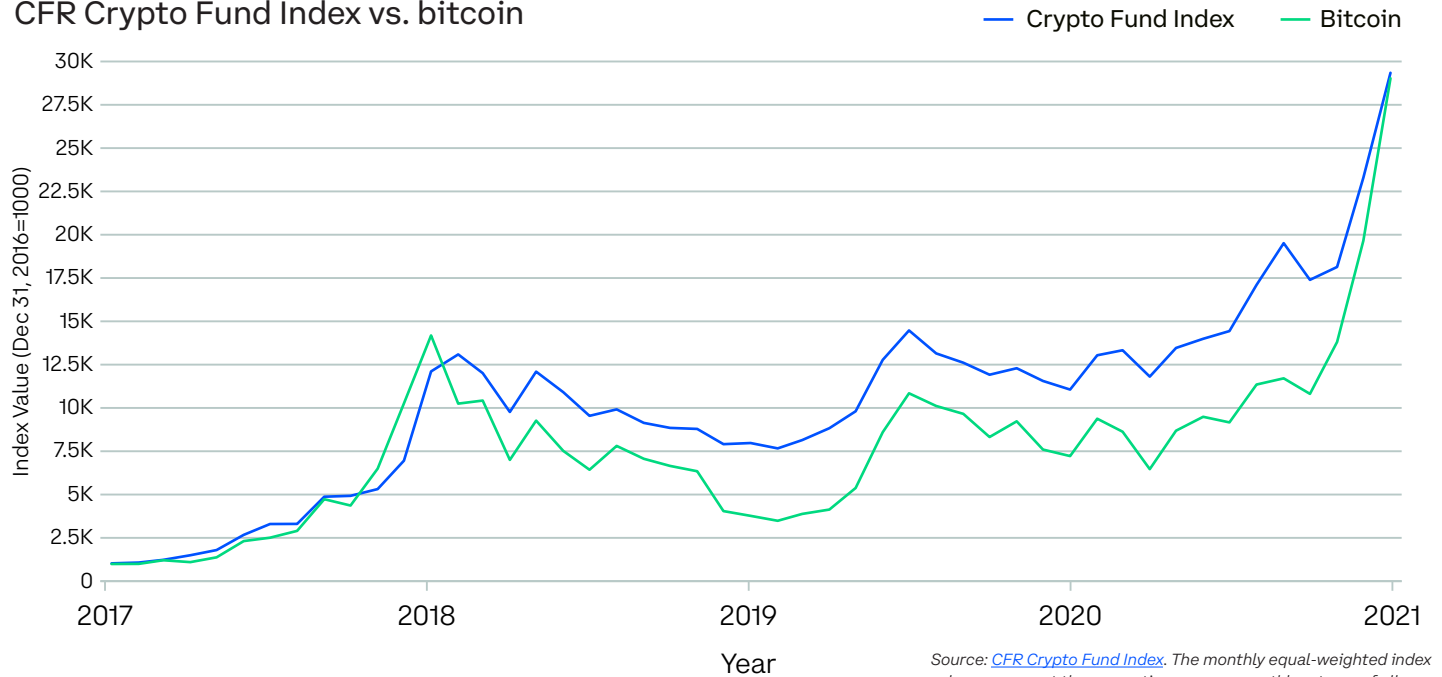
### Total crypto fund AUM



## Crypto fund performance

Crypto funds have outperformed bitcoin and most other cryptocurrencies since 2016, according to Crypto Fund Research, which maintains a global crypto fund performance database. The data suggest that crypto funds have historically underperformed cryptocurrencies in bull markets, but often outperform in more bearish markets, most remarkably during the “crypto winter” of early 2018.<sup>5</sup>

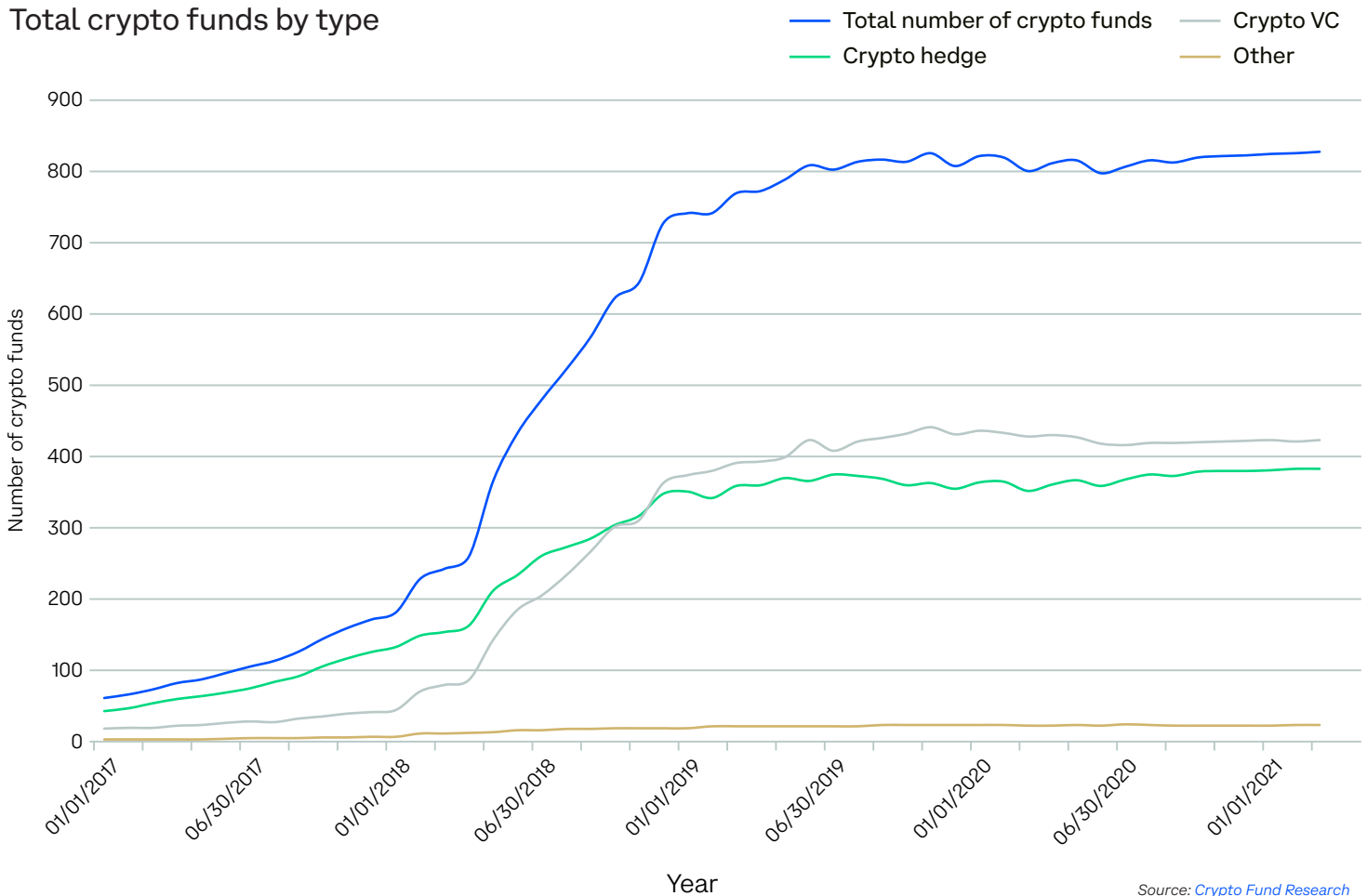
CFR Crypto Fund Index vs. bitcoin



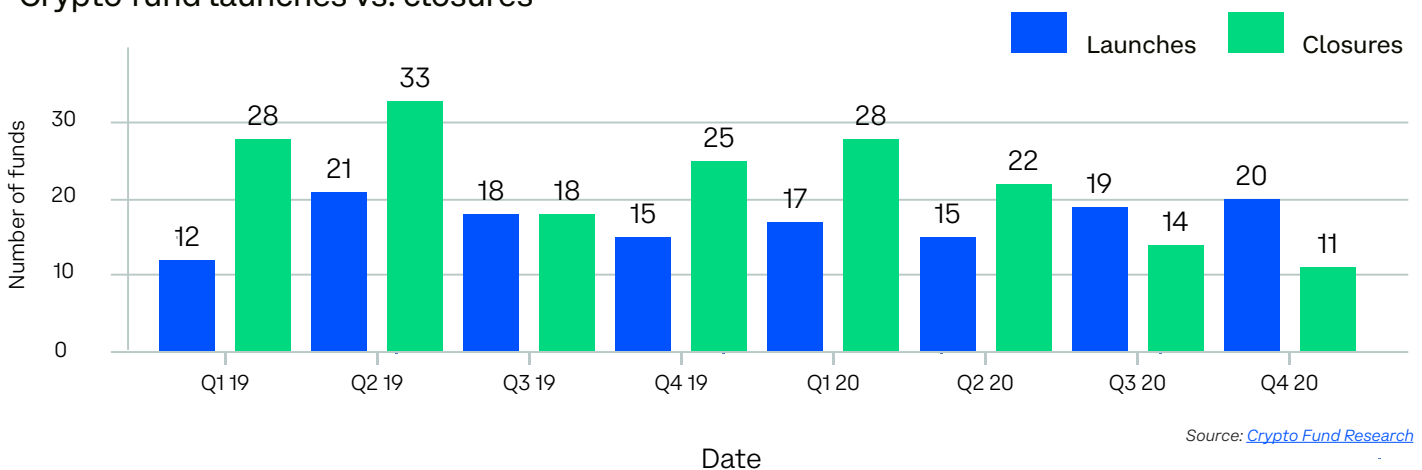
## A growing universe

The total number of crypto funds has grown by more than 800% in the past five years, driven primarily by the launch of VC and crypto hedge funds in 2017-2018. The pace of new crypto fund launches began to pick up again in the second half of 2020 after six quarters of limited growth, with the latest bull market likely to encourage more launches in the coming months.<sup>6</sup> While ETFs and other public fund vehicles make up the minority of the current fund universe, we expect this number to increase as regulatory challenges are addressed.

### Total crypto funds by type



### Crypto fund launches vs. closures



# Evolution of crypto fund regulation

## Timeline of first-movers

**9/2013**

**Grayscale** Bitcoin Trust (GBTC)<sup>8</sup> launches as the Bitcoin Investment Trust

**5/2015**

Bitcoin Tracker One lists on **NASDAQ/OMX** in Stockholm, becoming first bitcoin-based security available on a regulated exchange<sup>7</sup>

**11/2017**

**Bitwise** launches 10 Crypto Index fund (BITW)<sup>9</sup>



**12/2017**

**Grayscale** Ethereum Trust (ETH) launches<sup>10</sup>



**2/2018**

**Ontario Securities Commission** approves Canada's first blockchain fund – **Blockchain Technologies ETF**<sup>11</sup>

Cryptocurrency has matured and is now beginning to be successfully integrated into the wider financial world. A good example of this maturity is the development of crypto funds, and in some parts of the world, a developing regulatory environment that protects investors from security and manipulation risks.

There have been no specific laws preventing the launch of private funds – witness the early proliferation of crypto hedge funds, for example. Instead, concerns around the volatility of the asset class, constrained liquidity, market manipulation, crime, and security have been top of mind for regulators in North America, Europe, and the Asia-Pacific region.

The lack of regulatory clarity around digital assets means that, until now, the choices in front of both retail and institutional investors for gaining regulated exposure to the asset class have been limited. Mutual funds, for instance, are required to invest in regulated products and therefore cannot hold bitcoin directly.

## Canada at the center of fund action

Canada's securities regulator, Canadian Securities Administrators (CSA), recently approved three bitcoin ETFs. The first is the Purpose Bitcoin ETF (BTCC), which began trading on February 12. BTCC generated volumes of \$165 million on its first day and now has more than \$500 million in assets under management.

We believe Canada's approval of bitcoin ETFs will nudge along regulators elsewhere as part of the initiatives to bring crypto into the financial landscape fully. It will impose market surveillance, custody, and auditing requirements on the industry, offering a safer route into the space for retail and institutional investors.

**"We are excited to announce that Coinbase is now qualified to offer custody services in Canada for ETFs and public funds, and look forward to expanding our current relationships to provide a seamless trading execution and custody solution."**

**Steven Capozza** *Senior Manager, Institutional Sales*





### Timeline of first-movers

11/2018

**Amun**, now 21Shares, launches digital asset basket ETP (HODL) on Swiss stock exchange<sup>13</sup>

2/2019

**21Shares** Bitcoin ETP becomes the world's first physically backed bitcoin ETP to start trading<sup>12</sup>

3/2019

**21Shares** Ethereum ETP debuts, the world's first physically backed ethereum ETP<sup>14</sup>

**21SHARES**

6/2019

**G20** Financial Action Task Force recommends a standards framework for VASP

11/2019

**German Parliament** passes a bill that allows banks to store and sell bitcoin from January 1, 2020

### U.S. trails in retail crypto funds

The U.S. SEC, the regulatory body overseeing fund issuances, has numerous crypto ETF registration statements to consider. As of April 2021, it is reviewing the fourth effort from investment manager VanEck, which first filed a bitcoin ETF proposal with the SEC in 2016. All prior proposals from VanEck were rejected. In April 2021 the SEC also began to review a second application, from WisdomTree. So far these are the only two crypto ETFs that have also filed the necessary listing exchange filings. The listing exchange filing is important because it starts the clock for regulatory review and is also the stage where all prior attempts of a crypto ETF have previously been rejected.

New leadership at the SEC may create new opportunities to revisit crypto ETF approval in the U.S. The green light for these products would likely mean a trade-off in terms of stricter regulation of the crypto space, which we believe will ultimately benefit the current best-in-class offerings in digital asset custody and prime brokerage.

Gary Gensler, who has recently been confirmed as the next chairman of the SEC, is thought to be more sympathetic to the deeper integration of crypto into the financial system. SEC Commissioner Hester Peirce – known for her dissenting opinions in favor of approving a bitcoin ETF – may soon have more support to explore the potential of the crypto asset class.



## Timeline of first-movers

11/2019

**WisdomTree** bitcoin ETP lists on Swiss stock exchange<sup>17</sup>



1/2020

**21Shares** launches the world's only listed crypto inverse ETP, Short Bitcoin ETP.

4/2020

**3iQ Digital Asset Management's** The Bitcoin Fund starts trading on Toronto Stock Exchange<sup>16</sup>



6/2020

**ETC Group** launches bitcoin ETP BTCetc on Deutsche Börse's **XETRA**<sup>18</sup>



7/2020

**15 FiCAS** Active Crypto ETP is the world's first actively managed ETP with crypto as the underlying asset class<sup>19</sup>

9/2020

**EU** proposes a full regulatory framework for crypto



In Europe, rules around the legal structure of funds made it difficult for bitcoin exchange-traded products (ETPs) to operate as ETFs. UCITS (Undertakings for Collective Investment in Transferable Securities) is a European Union regulation dating from 1985 that lays out the legal requirements for mutual funds, money market funds, and ETFs. Because UCITS bars commodities from eligibility, the regulatory framework for crypto in Europe remains a gray area.

Additionally, the European Union's Markets In Financial Instruments Directive (MiFID) II regulatory framework tightened up on key investor information documents (KiID) requirements. This led Grayscale Bitcoin Trust (GBTC), for example, to become inaccessible to many U.K. and E.U.-based investors, even though it remained listed on many investment platforms.

It was not until February 2019 that the first physically backed ETP was launched in Switzerland by Amun, whose crypto funds now come under the 21Shares brand.

In June 2019, the G20's Financial Action Task Force recommended a standards framework for Virtual Asset Service Providers (VASPs), giving a lead to sovereigns to begin the rollout of legally aligned regulations for crypto.<sup>15</sup>

In November 2019, the German parliament passed a bill that allowed banks to store and sell bitcoin from January 1, 2020. By September 2020, the E.U. had proposed a full regulatory framework for crypto. The European Commission – the E.U.'s executive arm – stated that digital assets must become a regulated financial instrument, and has brought forward the MiCA (Regulation on Markets in Crypto Assets) Bill. If the law is passed, digital assets will become regulated financial instruments in the E.U.

**“Even in the current environment, the U.S. continues to launch more crypto funds than anywhere else in the world. We’re passionate about helping our clients build out infrastructure to manage these funds as regulators work to ensure the correct protections are in place for investors.”**

**Lauren Abendschein** *Director, Institutional Sales, U.S. and Americas*

# Product development: from trusts to ETFs

One by-product of the nervousness of regulators around digital asset funds has been that few regulated entities have been established, creating a substantial early-mover advantage.

In this context, the Grayscale Bitcoin Trust (GBTC) became the dominant conduit for institutional funds seeking exposure to bitcoin. However, the competitive landscape is changing.

There is consensus in the finance industry that the launch of a bitcoin ETF in the U.S., given its pivotal role in the global financial system, would be a groundbreaking moment for the crypto asset class. Crypto ETFs can provide retail investors with relatively low-cost exposure to bitcoin and other digital assets, while curtailing their worries about security, custody or liquidity.

ETPs are a popular form of collective investment vehicle because they are easy to access and reasonably priced. Globally, this fund structure comprised \$7.7 trillion in assets under management in 2020.<sup>20</sup>

ETPs typically track the price of an underlying asset that is either physically held or synthetically derived through use of derivatives products, such as swaps and futures. However, not all exchange-traded products are exchange-traded funds, and the confusion is further compounded by the fact that the terms ETF and ETP are sometimes used interchangeably.

## Not all ETPs are equal

Many of the earliest ETPs listed on European stock exchanges were not ETFs but debt securities known as exchange-traded notes (ETNs), which potentially expose investors to greater counter-party risk than ETFs because they are unsecured debt instruments. Exchange-traded commodities (ETCs) are another ETP variant still, and are similar to ETNs in that they are also debt instruments. It is worth noting that ETNs were recently banned for sale to retail by the U.K. Financial Conduct Authority (FCA).

Unlike investment trusts such as those available from Grayscale, ETPs of any type are open-ended products, which means that there is no limit to the capital size of the instrument. In order to liquidate a holding, an investor must sell the units back to the fund issuer through its redemption mechanism.

Although the GBTC has proven a key route for institutions to gain regulated exposure to crypto, its closed-ended structure means that it either trades at a premium or discount to its net asset value. The advent of the Canadian ETFs already appears to be providing competition for this exposure, as investors can now buy into a bitcoin ETF that always trades at its net asset value.

# History of crypto fund managers

## Timeline of first-movers

**12/2020**

**3iQ** Digital Asset Management follows its Bitcoin Fund with the Ether Fund.<sup>39</sup> **Valkyrie** launches Valkyrie Bitcoin Trust

**1/21**

CoinShares lists physically backed bitcoin ETP, **CoinShares** Physical Bitcoin (BITC)<sup>37</sup>



**1/21**

**Ninepoint** launches its Bitcoin trust in an CAD\$270 million initial public offering, plans to convert to an ETF in May 2021<sup>40</sup>

**2/21**

**Ontario Securities Commission** approves bitcoin ETFs<sup>41</sup>



**2/21**

**Purpose** Bitcoin ETF starts trading on Toronto Stock Exchange, becoming the world's first bitcoin ETF<sup>38</sup>

**2/21**

**Osprey Funds** launches the Osprey Bitcoin Trust<sup>42</sup>



## U.S.

Until a few years ago, there was little choice of investment vehicles for investors looking to gain exposure to bitcoin and other digital assets. But in the U.S. Grayscale has been a pioneer in this space, launching GBTC, the world's largest publicly traded bitcoin fund, in 2013. GBTC saw its assets grow to \$38.4 billion at the end of Q1, amid growing investor demand for crypto, helping Grayscale's total AUM swell to \$45.2 billion.<sup>21</sup> Grayscale offers a range of other trust products containing digital assets, including Ethereum (ETHE) and Bitcoin cash (BHCG), which are both SEC-reporting. It has recently announced the launch of five more digital currency investment trusts, citing growing global demand for these types of products.<sup>22</sup> Grayscale's products can be traded over the counter (OTC), in traditional brokerages, and in tax-advantaged accounts.

Another pure bitcoin play was launched recently by Osprey Funds. The Osprey Bitcoin Trust listed in February 2021 and is available through a brokerage account or individual retirement accounts.<sup>23</sup> In April 2021, Osprey Funds announced the launch of the Osprey Polkadot Trust, available through the OTCQX market.<sup>24</sup>

Other U.S. asset managers are also looking to attract funds from the brokerage channel, while the ETF route is still uncertain. San Francisco-based Bitwise Investments, which offers a range of index and fund products, opened up its Bitwise 10 Crypto Index Fund (BITW) for trading in traditional brokerages in December 2020. The index includes a market-cap-weighted basket of the 10 largest digital assets, which is automatically rebalanced.

Significantly, Fidelity Digital Assets, the crypto arm of fund management company Fidelity, launched the Wise Origin Bitcoin Index Fund to accredited investors and institutions in August 2020. At the end of 2020, IDX launched risk-managed indexes priced by S&P Dow Jones, which underpin IDX's Risk-Managed Bitcoin and Risk-Managed Ethereum trusts. In April 2021, Brazil-based Hashdex, in partnership with NASDAQ, launched its Crypto Index ETF on Brazil's B3 and Bermuda's BSX exchanges. The fund tracks the NASDAQ Crypto Index.

## Europe

Europe has helped lead the way in recent years in the crypto ETP space. The world's first bitcoin ETP – XBT Provider Bitcoin Tracker One – was launched in April 2015 by U.K.-based CoinShares and its XBT Provider brand. The ETN is listed on the NASDAQ/OMX exchange in Stockholm and has \$1.29 billion assets under management. This earliest of bitcoin ETPs does not hold physical bitcoin but instead takes a synthetic replication approach using certificates.

Products that physically replicate the underlying asset class have appeared in the past three years – for example the Amun Crypto Basket ETP (HODL), which was launched on the Swiss SIX stock exchange in November 2018. This was the



# 4.1

## Timeline of first-movers

2/21

**Evolve** Bitcoin ETF becomes second bitcoin ETF to list on a major exchange<sup>43</sup>

3/21

**Ninepoint Partners** announces plans to convert its Bitcoin Trust to an ETF in May<sup>44</sup>

3/21

**CI Galaxy** Bitcoin ETF becomes third Canadian bitcoin ETF to start trading.<sup>45</sup> **ETC Group** lists Ethereum ETP on Deutsche Börse's Xetra<sup>46</sup>

3/21

**Grayscale** launches five new digital currency investment trusts

4/21

**Purpose Investments** and **CI Global Asset Management** both receives approval to launch Ether-based ETFs

4/21

**Iconic** receives regulatory approval for a physically backed Bitcoin ETP to list on the Frankfurt Stock Exchange

first product exposed to a basket of crypto assets, where investors could gain access to 75% of the crypto market through one investment, with protection from the volatility of the asset class.

In February 2019, 21Shares (formerly Amun) launched the world's first physically backed bitcoin ETP, also on SIX. The 21Shares Bitcoin ETP (ABTC) listed on the Deutsche Börse in July 2020 and had \$319 million in assets under management as of March 18, 2021. In addition to ABTC, 21Shares now has a further six ETPs tracking digital assets such as Ethereum and Polkadot, and three more index funds alongside its HODL product. In February 2020, 21Shares also launched the world's only listed crypto inverse ETP, Short Bitcoin ETP (SBTC).

WisdomTree is another key player in the growing crypto ETP market in Europe. Its bitcoin ETP was listed in November 2019 and had accumulated \$371 million in AUM as of mid-March 2021.<sup>25</sup> London-based ETC Group has also had success with its BTCE Bitcoin ETP, which joined Deutsche Börse's XETRA in June 2020 and has amassed over \$1 billion in AUM. It listed an ethereum ETP on the same stock exchange in March 2021.<sup>26</sup>

CoinShares has added to its product offering this year with the launch of CoinShares Physical Bitcoin on the SIX Swiss Stock Exchange in January<sup>27</sup> and a physically backed ethererum ETP, CoinShares Physical Ethereum, in February.<sup>28</sup> In April, Iconic received regulatory approval in Germany for a physically backed Bitcoin ETP to list on the Frankfurt Stock Exchange.<sup>29</sup>

## Canada

Much attention in the crypto fund management industry has been on Canada in recent months, where new bitcoin ETFs have gathered significant assets under management in a short amount of time and driven high trading volumes.

The Purpose Bitcoin ETF became the world's first bitcoin ETF when it listed on Toronto Stock Exchange in February 2021.<sup>30</sup> Nearly 10 million shares in the ETF changed hands on the first day of trading,<sup>31</sup> and it exceeded USD \$1 billion assets under management a month after launch.<sup>32</sup> Evolve ETF followed close behind, also listing in February,<sup>33</sup> followed by CI Galaxy Bitcoin ETF in March.<sup>34</sup> In April, Purpose Investments and CI Global Asset Management both received approval to launch Ether-based ETFs.

Even before this, other Canadian fund managers have seen strong growth in their digital asset products. 3iQ Digital Asset Management's Bitcoin Fund, launched in April 2020 on the Toronto Stock Exchange, saw its market capitalization exceed CAD\$1 billion in January.<sup>35</sup> 3iQ followed its Bitcoin Fund with a similar product for ethereum: the Ether Fund began trading in December 2020.

Canadian investment firm Ninepoint Partners launched a Bitcoin Trust in January in a CAD\$230 million initial public offering. It has since announced it plans to convert the fund to an ETF in May.<sup>36</sup>

**"Europe has led the way in the exchange-traded product space thanks to developments in Switzerland and now Germany, and we are pleased to provide world-class custody services for several of the leading fund providers in the region."**

**Drew Robinson** *Senior Manager, Institutional Sales, EMEA Lead*

# Coinbase solutions for fund providers

Coinbase works closely with asset managers, supporting them with our secure custodial infrastructure and advanced trading capabilities. Coinbase's integrated prime brokerage solution offers fund providers the services you would expect from a traditional prime broker, built for the specific requirements of digital assets. The offering brings together our multi-venue trading platform and custody services with round-the-clock support from our experienced trading, coverage, and client services teams.

## Trading

There are a number of ways to trade with Coinbase. Our OTC desk provides a white-glove service and takes orders by voice, encrypted chat, or email. Our trading, coverage, and client-services teams help asset managers plan and execute big trades. Clients can also manage their trades through our web application, or alternatively they can trade via our REST and FIX APIs, which is the approach often chosen by frequently trading clients.

Our smart order routing provides deep, multi-venue liquidity. It pools liquidity from Coinbase's own exchange and other vetted third-party exchanges, directing orders algorithmically to find the best price available.<sup>47</sup> The same diversified liquidity pool can be accessed through both our professional trading platform and OTC desk. Our advanced execution algorithms give fund providers a powerful toolkit that includes TWAP (time-weighted average price), "float" orders that optimize for execution price, and "opportunistic" orders. We also access a network of principal OTC desks to source competitive quotes based on common index and NAV benchmarks.

Transparent post-transaction cost analysis shows precisely how orders are split, routed, and filled across venues. We operate an agency only model, which means that we never trade against our clients. Our interests are aligned and we work hard to find the best available price in the market for our clients. We are also able to post-settle trades and offer short-term trading credit to allow ETF providers to more easily manage their cash flow.

**"The next 12 months will be a critical time for crypto fund managers to position themselves in this market, and it has become a major focus for our team to provide these clients with superior technology to support their vision."**

**Greg Tusar** *VP Institutional Product for Coinbase*

### Coinbase currently serves the following fund providers:

#### U.S.

Hashdex  
Grayscale  
Bitwise  
Pantera  
One River  
Valkyrie  
IDX  
Osprey  
Castle Funds  
Skybridge

#### Canada

Purpose Bitcoin ETF  
3iQ Bitcoin Fund  
Ninepoint Bitcoin Trust  
CI Galaxy

#### EMEA

WisdomTree Bitcoin ETP  
21Shares Bitcoin ETP  
Iconic Bitcoin ETP

## Custody

We are one of the largest digital asset custodians, offering fund providers peace of mind that their assets are secure. Coinbase Custody's offline cold storage provides maximum security, using battle-tested cold storage infrastructure that has never lost client funds. Our industry-leading insurance policy protects offline and online assets across all our products. Coinbase's institutional assets on platform (AOP) reached \$122 billion at the end of March 2021.

Our U.S. custodial entity, Coinbase Custody Trust Company LLC, is a fiduciary under New York State banking law. Coinbase also operates a Dublin, Ireland-based custodial entity, Coinbase Custody International, which services many of our overseas clients. Coinbase Custody Trust Company LLC has been audited by Deloitte & Touche LLP as of and for the period ended December 31, 2020. Deloitte & Touche LLP also completed two System and Organization Controls (SOC) examinations (a SOC 1 Type 2 and a SOC 2 Type 2 examination) for Coinbase Custody Trust Company LLC, for the period of January 1, 2020 to September 30, 2020. You can learn more about the countries where Coinbase and affiliated companies are registered [here](#).

Coinbase Custody supports more than 108 assets across 15 different blockchains as of March 31, 2021. This breadth of asset support has helped drive growth in our introducing-broker segment. We balance safekeeping of assets with easy online client access to holdings, allowing clients to get the most out of their assets securely and actively.

Asset managers who use Coinbase benefit from key features for certain assets, such as staking and active governance from safe, online storage of assets. This allows our clients to earn rewards through staking activities and to vote without having to put their funds at risk.

**"There is incredible potential for financial institutions who are expanding access to the cryptoeconomy through these fund structures. We are excited to partner with these clients as public interest and demand for these offerings grows."**

**Brett Tejpaul** *Head of Institutional Sales, Trading, Custody and Prime Services*



# Grayscale Investments case study

Grayscale Investments is the world's largest digital currency asset manager, offering a wide range of digital asset investment products available to institutional and accredited investors through private placements and the public markets.

## The challenge

Grayscale was looking for a qualified custodian that provided world-class security and a high-quality service, as well as the flexibility to devise solutions to Grayscale's range of needs and plans to grow.

## Choosing Coinbase Custody

Grayscale selected Coinbase Custody in 2019 after a thorough review of the market. It compared 10 different custody options, taking into account a number of key factors including security, insurance coverage, regulatory compliance, and the overall ability of its potential custody partner to scale with the business. Coinbase provided the best solution when it came to both security standards and asset coverage, which was important for Grayscale's growing suite of products and assets under management.

## Coinbase's advantages

Grayscale has found Coinbase to be extremely responsive to its suggestions and willing to work together on improvements to the user interface, and efficiently implement any changes. The process is streamlined and transparent, which makes clients feel as if they're a part of the process rather than outside of it. Coinbase has also been able to explain its processes and demonstrate its robust security framework, broad service offering, and quality assurance to Grayscale's partners including auditors, institutional investors, and key stakeholders.

**"As the world's largest digital currency asset manager, we're laser focused on providing only the best products and most secure experience for our investors. That means working with other leading firms in our industry who have a proven reputation and share the same commitment to quality as we do. Coinbase is at the top of that list."**

**Michael Sonnenshein** *CEO Grayscale Investments*

## Custody for Grayscale

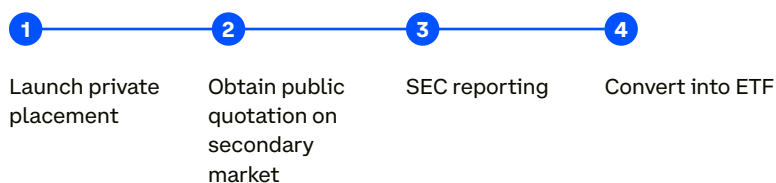
Coinbase serves as custodian for Grayscale's single-asset investment products and their underlying digital assets, such as Grayscale Bitcoin Trust, Grayscale Ethereum Trust, and Grayscale Ethereum Classic Trust. Coinbase is also the custodian for the underlying digital assets in Grayscale's Digital Large Cap fund, which provides exposure to the top digital currencies by market cap.

## The path to ETFs

Coinbase also provides custody to Grayscale's five new digital currency investment trusts, which were launched in March 2021 in response to increasing global demand for these types of investment product. The new trusts, which take Grayscale's offering to 14 products, offer investors exposure to five digital currencies – Basic Attention Token (BAT), Chainlink (LINK), Decentraland (MANA), Filecoin (FIL), and Livepeer (LPT).

They operate in the same way as Grayscale's other single-asset investment trusts. Grayscale intends (with no guarantee) for shares in these products to be quoted on a secondary market<sup>48</sup> and ultimately converted into fully-regulated ETFs.

### Lifecycle of a Grayscale product



# An interview with WisdomTree

**WisdomTree, a newer entrant to the space, shares its outlook and experience launching crypto ETFs with traditional investment management expertise**

**What is your perspective on entering the crypto ETF space as a traditional asset manager? What was your initial vision for developing these products?**

It's been an educational process for us entering the crypto space, one which started in late 2017. Despite the price fall in bitcoin at the time, there was so much excitement about the potential for reorganising the financial ecosystem. However, we had to go on a journey to satisfy ourselves this wasn't just hype.

We left the process with two conclusions: 1) digital assets are here to stay, and 2) there is a huge gap between the traditional finance and crypto native worlds. Our initial vision was focused on bridging that gap.

**What was the tipping point that gave you confidence in digital assets as an investment strategy?**

There wasn't a tipping point per se. I think everyone who has a traditional finance background comes to the digital asset or crypto space with the same reservations or criticisms but as you spend time digging into these, they start to fall away. At WisdomTree, we pride ourselves on being innovative and forward-thinking. As we did our research, it became clear that we should put our name behind digital asset products, and help our clients use them to achieve their investment goals.

**What are some of the macro drivers that you're monitoring to inform your strategy? What will drive digital asset adoption in 2021 and beyond?**

Since the global financial crisis, cross-asset correlations have been increasing across the board. Bitcoin and other digital assets have historically shown returns uncorrelated with other assets. While these correlations may increase over time with greater institutional adoption of digital assets, we think low correlations will generally persist, given the differing investment theses of these assets. Also, the unprecedented fiscal and monetary stimulus in the past year has made inflation hedges top of mind for investors, and we see a scarce, structurally deflationary asset, like bitcoin, as having a lot of salience in this environment.

Regarding adoption, or the potential for adoption, the major driver we look at is what we call "real world" use cases; examples of where digital assets make financial experiences better for people or where we see them presented as adding value to a product offering. This might be cross-border remittance, sources of stability, escrow, trade financing, payments, companies looking at crypto as a way of accessing new markets.



2020/2021 has seen major announcements about bitcoin with large companies such as Visa, PayPal, and Tesla all looking to integrate bitcoin into their business. We think we'll continue to see more of these announcements in the future, and businesses and consumers will continue to incorporate digital assets and blockchain into more areas.

**Why was Coinbase Institutional ultimately chosen as your partner in this space? What was the due diligence process like?**

We're very excited about the partnership with Coinbase. Their experience in the space has given them the expertise to offer an institutional platform we can be confident in. We finished the due diligence process impressed not only with the custody solution, the people involved and their commitment, but also with the building of a better ecosystem for digital assets.

**What Coinbase offerings are you currently using to help manage your products? Can you tell us about your experience working directly with Coinbase?**

We use the Coinbase Custody solution for our European exchange-traded bitcoin product which leverages the same cold storage architecture that underpins Coinbase's custody of crypto assets for its retail customers. In addition to greater security, Coinbase Custody offers the industry's leading insurance policy, providing further reassurance for our investors. It's still early days for us but it has been an overwhelmingly positive experience and we've been impressed with the level of partnership shown.

We also have set up a Coinbase Prime account as part of our initiative to incorporate digital assets into the model portfolios we make available to financial advisors. The API connectivity Coinbase offers has made the connectivity on pricing and performance tracking easy.

The workflows associated with physically backed, exchange-traded products have some intricacies compared with other structures in the fund space. The Coinbase team worked hard to ensure the platform was tailored to deliver what we needed.

**"It is clear to WisdomTree that bitcoin, digital assets, and blockchain technology will be increasingly important in financial services going forward. Our clients – both institutional and retail – are looking to better understand and access this asset class through investor-friendly means. Coinbase Institutional has been a great partner to WisdomTree as we've grown our leading bitcoin ETP in Europe and developed new products. We are excited to continue working with them to increase engagement with this new asset class for investors around the world."**

**Jonathan Steinberg** *CEO and Founder, WisdomTree*

Cryptocurrency collective vehicles such as exchange-traded products are likely to see a dramatic shift in gear this year. The approval of ETFs in North America, Australia, Europe (where there are already a number of ETPs), and the Asia-Pacific region could offer a significant increase for fund flows into the sector.

### **A greater shift to ETFs**

The success of the bitcoin ETFs in Canada has raised hopes that the U.S. SEC, which has in the past rejected all bitcoin ETF applications, will follow suit.

There has been a wave of companies lodging applications for a bitcoin ETF in the U.S. this year. For example, Valkyrie Digital Assets, a subsidiary of Dallas-based Valkyrie, filed a bitcoin ETF application in January and a second application in March for an ETF that would invest mainly in companies that have bitcoin on their balance sheets or are otherwise connected to the digital asset.<sup>49</sup> Elsewhere, NYDIG and SkyBridge Capital have also filed for bitcoin ETFs with the SEC.<sup>50</sup> WisdomTree has additionally submitted a crypto ETF proposal. Grayscale has also confirmed it is committed to converting its GBTC to an ETF when possible.

All eyes are now on the U.S. regulator to see whether Canada's recent approval of three bitcoin ETFs and the evident demand for these types of investment products will encourage a change of approach in this jurisdiction.

### **Crypto funds leading product development**

We expect to see accelerated expansion in the range of crypto fund products available to investors. The appetite for digital asset allocation from both retail and institutional players may still be largely untapped, which is why there is so much anticipation around the prospect of the U.S. SEC approving a bitcoin ETF.

The development of physically backed ETFs in the crypto space has allowed for exposure to the market with the opportunity to smooth out volatility. We see this as a growing space and we expect to see further development in these types of products.

Further, if an ETF is approved for trading on U.S. markets, it may shift discussion to questions about the design and access of the entire fund industry, including how the efficiency advantages of blockchain technology could be extended to how funds are traded.

On the mutual fund side, for example, back-office platform Calastone launched its Distributed Market Infrastructure for trading mutual funds two years ago, helping its 1,800 client companies save almost \$4 billion annually by moving certain transactions on blockchain, which removes incidences of manual reconciliation.

We continue to expect current digital asset funds, prime brokerage, and custody leaders to be at the forefront of leading-edge trade innovation.

## Regulatory clarity driving further fund launches

The strengthening regulatory oversight of the digital asset class underpins the growing belief that crypto markets are mature and suitable for investment from a wide range of investors.

Regulators in Europe and Canada have taken a series of actions that have helped bring clarity to the definition and regulation of digital assets, and in some cases helped to drive product development. Europe's legislative proposals also intend to introduce custody and capital requirements as well as a regulatory sandbox approach to foster innovation and development.

Australia is on the cusp of allowing bitcoin ETFs, indicating they are open to the idea as long as investors have appropriate protection commensurate with any associated risks. Following the rejection of an application from Cosmos Capital for a bitcoin ETF, the Australian Securities and Investments Commission (ASIC) qualified their position, stating that ETFs could feasibly exist under the Australian Securities Exchange's (ASX) AQUA rules, which govern other types of ETFs in the country. Fund managers are anticipating greater regulatory clarity this year, with proposals from VanEck, Australian-based issuer BetaShares and ETF Securities pending approval with the ASIC.

While the U.S. SEC has to date declined to approve a bitcoin ETF, given the recent change in administration and the further development of the asset's market and market structure, the path towards approval seems to be nearing. That being said, approval is contingent upon thorough engagement with the SEC, along with a thoughtful submission which differentiates a new proposal from those previously disapproved.

Importantly, the U.S. Office of the Comptroller of the Currency (OCC) signaled last year that stablecoins would be allowed to deposit fiat reserves at banks, and banks could engage in digital assets custody.

We believe that clearer regulatory guidance will help propel product issuance plans from fund managers in the U.S., Europe, and Asia-Pacific – and we look forward to supporting our clients' success in this growing industry.

**"You see these more nimble fund providers jumping in at earlier stages as Australia potentially allows a bitcoin ETF for the first time. We are dedicated to providing best-in-class execution capabilities to help these players take off in this region."**

**Kayvon Pirestani** *Director, Institutional Sales, APAC Lead*





## About Coinbase Institutional

Coinbase Institutional provides integrated solutions that marry our custody, advanced trading platform, and prime services. Coinbase Prime, our unified investing experience, has the tools sophisticated investors need to execute large and complex trades, complemented by a diverse pool of liquidity. Because our institutional business works on an agency basis, our interests are aligned with those of our clients as we seek the best prices in our network. Once trading is complete, Coinbase Custody is one of the safest places to store digital assets.

### **Contact us**

To learn more about Coinbase Institutional, please email us at [institutional@coinbase.com](mailto:institutional@coinbase.com).

**Sign up** for Coinbase Institutional product [here](#).

### **We're hiring**

Learn about Coinbase careers [here](#).

# Endnotes

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