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Rick Maeda I Research Analyst
rickm@prestolabs.io

Summary

- Conversations around tokenisation and RWAs dominated the conference as institutional players expressed interest in increasing capital efficiency and reducing costs via this specific application of blockchain technologies.
- The most interesting discussion at the conference was about the latent systemic risks brought about by regulators' insufficient embracing of the new asset class, as well as their tough stance that has deterred large financial institutions from banking companies in this industry.
- Finally, we explore the divide between institutions and "crypto natives". This divide goes beyond sector interest or technological pursuits within crypto; it is fundamental as it strikes at the core values that crypto natives hold dear.

Figure 1: Has the FT flipped to pro-crypto?

Source: FT

Overview

Presto Research recently attended the Financial Times Crypto & Digital Assets Summit in London (08~09May24). In what is possibly the most institutional event in the crypto conference circuit, the vibe was very much “TradFi” as expected. In the third iteration of this conference, speakers ranged from central bankers, regulators, policy makers, funds, broker/market makers, legacy institutions and much more. The regional element probably contributed to the TradFi vibe, but it was also of course the FT’s seemingly indissoluble reputation as an anti-crypto publication. In fact, there was a funny incident on Day 2 during a Q&A where a gentleman in the audience unleashed a scathing criticism on the event hosts, in regards to their integrity around their anti-crypto bias - definitely a standout moment among the rather sluggish energy of this conference. The FT panel moderator tried to comedically brush the incident off but conversations among attendees made it clear that everyone was in full agreement with the gentleman.

Most Discussed Topic(s): Tokenisation (/RWAs)

The top 3 most discussed topics, in order of popularity, were (1) Tokenisation, (2) Tokenisation, and (3) Tokenisation. It’s hard to recall panels where the speakers didn’t steer the conversation back to (yes you guess it) “tokenisation”.

> So… what is tokenisation?

Tokenisation refers to the process of representing real-world assets (or rights) digitally on a blockchain into tokens. “Assets” is a broad term here, and the assets that can be tokenised can include anything from collectibles like sneakers to financial assets to investment vehicles. If you’ve heard someone say “put it on the blockchain”, they are talking about the act of “tokenising” something.

> What are some examples of tokenisation?

Essentially anything can be tokenised, be it a Monet painting or real estate or financial assets such as stocks. The most common example today is a stablecoin, which is a tokenised fiat currency. Tether’s USDT and Circle’s USDC are tokenised U.S. dollars where a token represents one dollar that the company has in its reserves.

> What are the benefits?

A non-exhaustive list of the benefits tokenisation brings:

- Near-instantaneous settlement: instead of the weekday T+n settlement dates of traditional securities, tokenised assets settle 24/7 and as fast as the underlying blockchain allows them to. An example of this attribute given by Marcus Grubb, previously Global Head of Product at State Street and currently Chief Product Officer at IMPB, is of a private bond fund that had to wait 2-months to internally move assets between its GP and LP vehicles - they are now exploring an internal tokenisation project which would make future transfers instantaneous.
- Operational cost reduction: as is often the case with implementing Web3 practices, regulatory compliant smart contracts allow for the removal of “the middleman” - lawyers, brokers, banks, etc. - which means lower costs for existing parties and a lower barrier of entry for new ones. We can continue the previous example of the private bond fund, that can now save recurring costs on its direct distribution platform when externally transferring capital to investors.

Figure 2: Michael Sonnenshein, CEO of Grayscale Investments Source: Presto Research

- Fractionalisation, liquidity, and democratisation: tokens can be divided freely into smaller units, enabling fractional ownership for even physical assets, which could potentially increase liquidity. This allows for a democratisation of access as now a retail investor with $1,000 to invest can participate in the upside of a tokenised PE fund which originally had a minimum ticket of $500k.
- Transparency + trust: ownership history, transaction values, and many more factors that can often be obfuscated in traditional assets, particularly non-public assets, are now easily verifiable. This doesn't necessarily mean a lack of privacy, as blockchains can be private or permissioned. Now you can verify the legitimacy of the Jeff Koons sculpture in front of you and know that your AD is telling the truth when she says she paid $10k for the watch.

A discussion of tokenisation naturally leads to the topic of RWAs ("real world assets"), which are assets that have been tokenised. Fiat-backed stablecoins such as USDT and USDC, as well as tokens that represent real estate, and all the examples mentioned above are RWAs. Here's a sample sentence to tie it all together: "*USDT is an RWA issued by Tether, more specifically a stablecoin which is the result of a tokenised US dollar, that can be exchanged over the blockchain*."

Consequently, RWAs were frequently mentioned (often interchangeably with "tokenisation") at the conference, and with the introduction of asset management behemoths such as BlackRock entering the industry, RWAs have been a bullish topic among the retail crowd as well. With the double-punch of DeFi yields compressing over the last bear market and the US risk-free rate rising, the most active RWA theme has been the tokenisation of USD interest rate yielding assets such as US treasuries and money-market funds. With a widespread adoption of tokenised assets, traditional finance can now have an interoperable, positive carry asset, considered to be cash-equivalent and can be transferred instantly across the blockchain.

Most Interesting Topic: Latent Systemic Risks

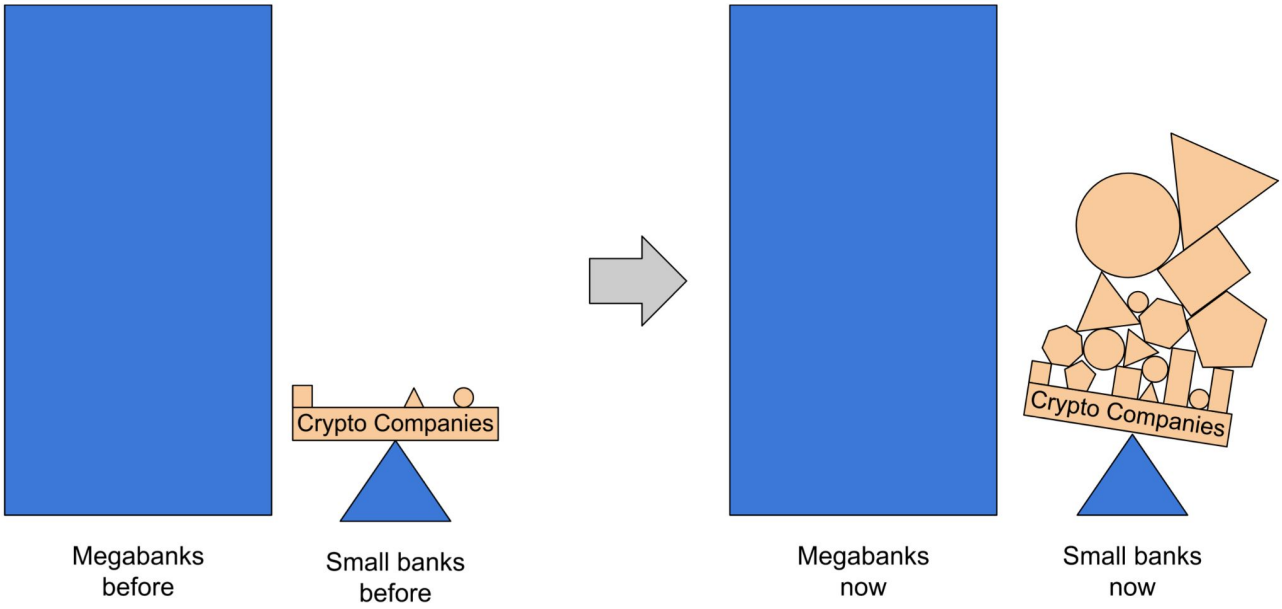
In one of the summit panels, René Michau, Global Head of Digital Assets at Standard Chartered, was asked what regulators could be doing more. In his brief response, he propounded a thought-provoking topic that is currently very much under the radar.

René argued that regulators across jurisdictions have a problematic tendency to take a posture towards banks that discourages them from banking companies in emerging technologies including crypto, and that this creates latent systemic risks in the financial system. The job of a banker when coming across a new asset class is to develop a skill-set to ensure that the organisation understands the risks and moves towards providing banking services to that industry. The story with crypto however, has been that many banks with large balance sheets are getting a free pass for not developing the risk infrastructure to work with such companies.

There's a risk that if you, as a regulator, aren't encouraging - or worse, discouraging - larger balance sheet banks from developing that capability and building out that risk framework, you push higher-risk industries to banks with smaller balance sheets that potentially have a lower capacity to deal with the risks, many of which may still be unknown. This dynamic, which has been prevalent for far too long, needs to be addressed specifically because it's rife even in jurisdictions where regulators are seemingly forward thinking (and also obviously in places where regulators boast "we're tough on crypto, we don't let our banks bank crypto firms" which unfortunately is the majority). It's great that smaller banks have an opportunity to be innovative and capture a new class of clients, but far from diversifying their capital base, these banks end up concentrating their exposure to early industries that tend to be more volatile and unpredictable. Further, the pace at which the crypto industry is growing makes this issue time-critical (Figure 3).

Figure 3: The growing crypto industry is relying on the same banking providers.

Source: Presto Research



There's an argument to be made that this played a substantial role in the March 2023 US banking crisis when Silicon Valley Bank, Silvergate Bank, and Signature Bank all went under within weeks. Mid-tier banks have had an intense concentration to emerging tech companies and funds, often because they were the only ones that accepted bank account applications from non-traditional tech companies. As explored in a personal story in *Appendix 1: Reminiscences of a Crypto Company Operator*, this issue is prevalent in crypto-friendly Singapore as well. As René mentioned, this needs to be explicitly addressed by regulators to disperse the concentration from smaller balance sheet banks and encourage well-capitalised banks to invest in being able to bank firms in emerging tech industries such as crypto.

Main Takeaway: This isn't Satoshi's vision

So far, we've only addressed half of the title ("tokenisation") but not yet the other half; so what does Satoshi's vision have to do with anything?

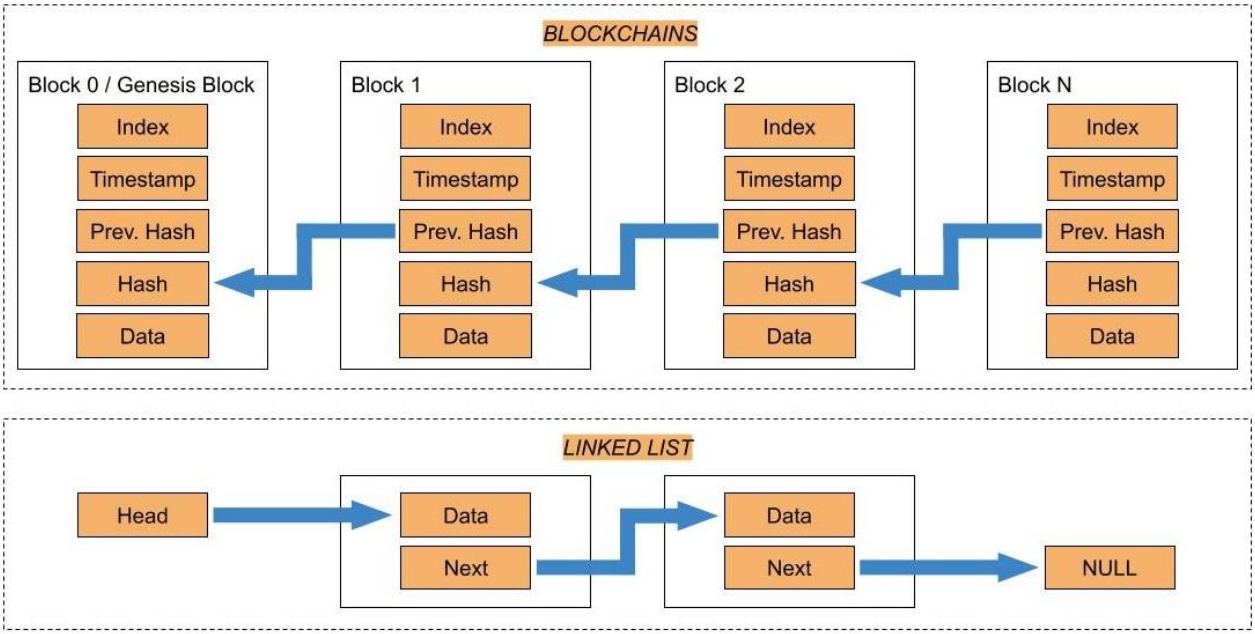
This section discusses the incredible disconnect that was made apparent at this conference, between the "institutional crypto" crowd and the "crypto native" crowd. Crypto native people are individuals with a solid understanding of the concepts and mechanics, as well as being strong proponents of the principles the broader crypto industry has to offer. There is an intellectual curiosity beyond their desire to make money and an active participation in the industry that expands past the "fun times" (i.e. even in bear markets). Many work for "crypto native" firms (purely Web3 companies) and the majority of Gen-Z and millennials who are in this industry professionally belong to this category. On the other hand, people in the institutional crypto crowd, like the attendees of this summit, tend to be a little older and often work in the "digital assets" division of a non-crypto native company.

One question you may have had when reading the "Most Discussed Topic(s)" section is: can't all of these things be done separately from the current "crypto" industry of Bitcoin, Ethereum, etc.? The answer is absolutely yes. The concepts listed in that section, and the majority of the discussions from the conference, could exist entirely outside the scope of what crypto native people would consider the industry to be. In fact, the use cases the institutional crypto people deliberated over would actually work better without many of the values crypto natives consider to be core to this industry such as decentralisation, public transparency, and censorship resistance.

A common example of a "crypto use case" at this summit, and among institutional players in general, was a payment system that can be leveraged to improve asset mobility among financial institutions, central banks, government agencies and other actors. As we discovered in the benefits of tokenisation, this can come with many upsides - however,

Figure 4: Blockchains and linked lists. The latter is taught in introductory computer science classes.

Source: Presto Research

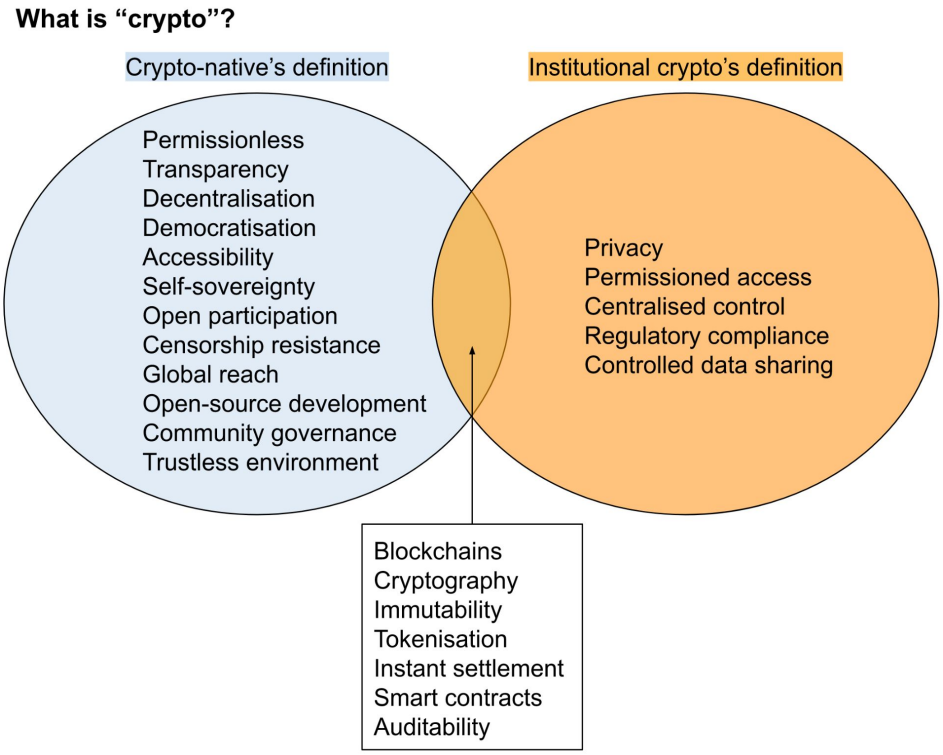


none of those are really “crypto”. The US Treasury can create a tokenisation platform for the clearing and settling of wholesale transactions to allow banks to instantaneously move assets, all on a permissioned blockchain and without relying on any of the public crypto assets as we know today (please see *Appendix 2* on the differences among public, private, and permissioned blockchains). Users of such a platform wouldn't even care to what extent blockchain technology was used, or what assets were tokenised, as long as the UX was an improvement to whatever the legacy system was.

The reality is that the underlying technology, at its core, is incredibly simple: a blockchain is a series of cryptographically linked data points. They are basically immutable, ordered, back-linked lists of transaction blocks, which is a simple enough data structure for even a first year computer science student to understand (Figure 4). And this simplicity allows for the technology to be interoperable across not only use cases but also core objectives. With a fundamental difference in the definition of “crypto” between crypto natives and institutional crypto players, there exists a clear divergence in the end-use cases both sides imagine (Figure 5).

Figure 5: Values and characteristics, crypto natives versus institutional crypto.

Source: Presto Research



Then why do these institutions claim an interest (a market dependant interest at that: there is an endless list of companies that "adopted" crypto and 2021, only to have abandoned it in the bear market) in crypto, instead of just developing their own blockchain-powered platforms that serve their particular use cases? Why do they need to attend these conferences to ramble on about how strongly they believe in the use cases, despite the organisation not having any actionable plan? The impression from a crypto-native person attending this summit was that everyone was just hedging. Companies, particularly public companies, can't ignore what is at the middle of the Overton window at any given time: crypto has an incredible ability to occupy mindshare and like many new shiny things, it maintains positive reflexivity and correlation between its "value" (measured in price for crypto) and social acceptance. CEOs can't be seen missing the current trend and not "investing" in it, because if competitors get ahead by leveraging that trend, it is their heads on the chopping blocks. The apparent lack of belief in crypto's core principles among the speakers

accentuated this feeling that everyone was just playing the role of someone who cared as much as their job forced them to. Had any of the speakers even read Satoshi's Bitcoin whitepaper? The first sentence in the paper's abstract literally references a payment system outside of the current financial system: "without going through a financial institution" (Figure 6).

Figure 6: The Bitcoin whitepaper. The avoidance of financial institutions is a feature not a bug.

Source: bitcoin.org

Bitcoin: A Peer-to-Peer Electronic Cash System

Satoshi Nakamoto
satoshin@gmx.com
www.bitcoin.org

Abstract. A purely peer-to-peer version of electronic cash would allow online payments to be sent directly from one party to another without going through a financial institution. Digital signatures provide part of the solution, but the main benefits are lost if a trusted third party is still required to prevent double-spending. We propose a solution to the double-spending problem using a peer-to-peer network. The network timestamps transactions by hashing them into an ongoing chain of hash-based proof-of-work, forming a record that cannot be changed without redoing the proof-of-work. The longest chain not only serves as proof of the sequence of events witnessed, but proof that it came from the largest pool of CPU power. As long as a majority of CPU power is controlled by nodes that are not cooperating to attack the network, they'll generate the longest chain and outpace attackers. The network itself requires minimal structure. Messages are broadcast on a best effort basis, and nodes can leave and rejoin the network at will, accepting the longest proof-of-work chain as proof of what happened while they were gone.

For many institutional participants, crypto is just an opportunity to integrate a new asset class into their existing business and offer a new product, and this view was reflected in their knowledge and attitudes. Joey Garcia, Head of Public Affairs+Policy+Regulatory Affairs at Xapo Bank, gave an apposite analogy: "it's almost like seeing a cruise liner add wings and say 'now we're massive proponents of aviation as a concept' as they sail across the seas" (Figure 7). There was

single outlier who really pushed the principles of crypto and that was Mr. J. Christopher Giancarlo, former Chairman of the CFTC and a massively popular figure among crypto proponents for his balanced approach to regulate properly without stifling innovation or dismantling crypto's values. Mr. Giancarlo gave a speech on CBDC (Central Bank Digital Currencies), a fairly tough topic for a pro-crypto person, but did so in a hopeful way that integrated the founding ethos of crypto.

However, as evidenced in this summit, not everyone has Mr. Giancarlo's ability to speak the languages of both crypto natives and institutional crypto, so as young crypto-natives start occupying leadership positions in this industry, it's imperative for them to keep the true spirit of crypto alive. Without the effort from their side, regulators will continue to embrace what they *think* is crypto - the version that is missing the core values - and Satoshi's vision will be left behind from the new crypto paradigm.

Figure 7: The institutions have "embraced" crypto.

Source: DALL·E 3

Appendix

Appendix 1: Reminiscences of a Crypto Company Operator

To briefly digress from the first-person plural narrative of this note, I can personally attest to this from my previous job. I will skip the horrors of trying to find a bank for a Cayman Islands domiciled crypto hedge fund and its Singapore-based holding company back in 2021, and also looking for a replacement in March 2023 since we used Signature Bank (one of the few options we had in 2021), because no one will be surprised at how difficult that was. Instead, the story I want to share is from earlier this year (actually still ongoing) when we created a Singapore-based Special Purpose Vehicle (a temporary private limited company) to house a single asset. That asset was a SAFT (Simple Agreement for Future Tokens) which is a legal agreement used to raise funds for cryptocurrency projects, where investors buy the right to receive tokens in the future once the project's tokens are live. The SPV was to be completely inactive until the day we sold the SAFT, at which point we would distribute USD from the SPV's bank account and close the Vehicle thereafter - a very barebones set up and use case. Yet, not a single local bank would open an account for us. This is in Singapore, which is globally considered to be one of the most crypto accepting jurisdictions and this is despite having a local company director with both personal and business accounts at many of the local banks (DBS, UOB, etc.). We're still undecided as our current options are smaller start-up neobanks or more established non-local banks that don't have a banking licence in Singapore, but it's not a stretch to imagine the potential latent systemic risks in many places when this is our experience in crypto-friendly Singapore. Story over, now back to a more professional first-person plural discussion.

Appendix 2: Public vs. Private vs. Permissioned Blockchains

> A *public blockchain* is a decentralised network where anyone can participate and contribute to the process of validating new blocks, with full transparency and no access restrictions (e.g., Bitcoin, Ethereum).

> A *private blockchain* is restricted and its access and participation are controlled by a single organisation or consortium, making it more centralised than public blockchains.

> A *permissioned blockchain*, while potentially open to multiple organisations, restricts participation in the consensus process of validating transactions and blocks to a select group of participants.

About Presto

Presto is a Singapore-based algorithmic trading and financial services firm founded in 2014. Presto focuses on delivering exceptional value for clients through rigorous research-driven approach to investment and trade execution. With more than a 100 million trade executions in a day, Presto is a leading financial services firm in both digital assets and traditional finance markets.

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Authors

Rick Maeda, Research Analyst : X, Telegram, LinkedIn

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