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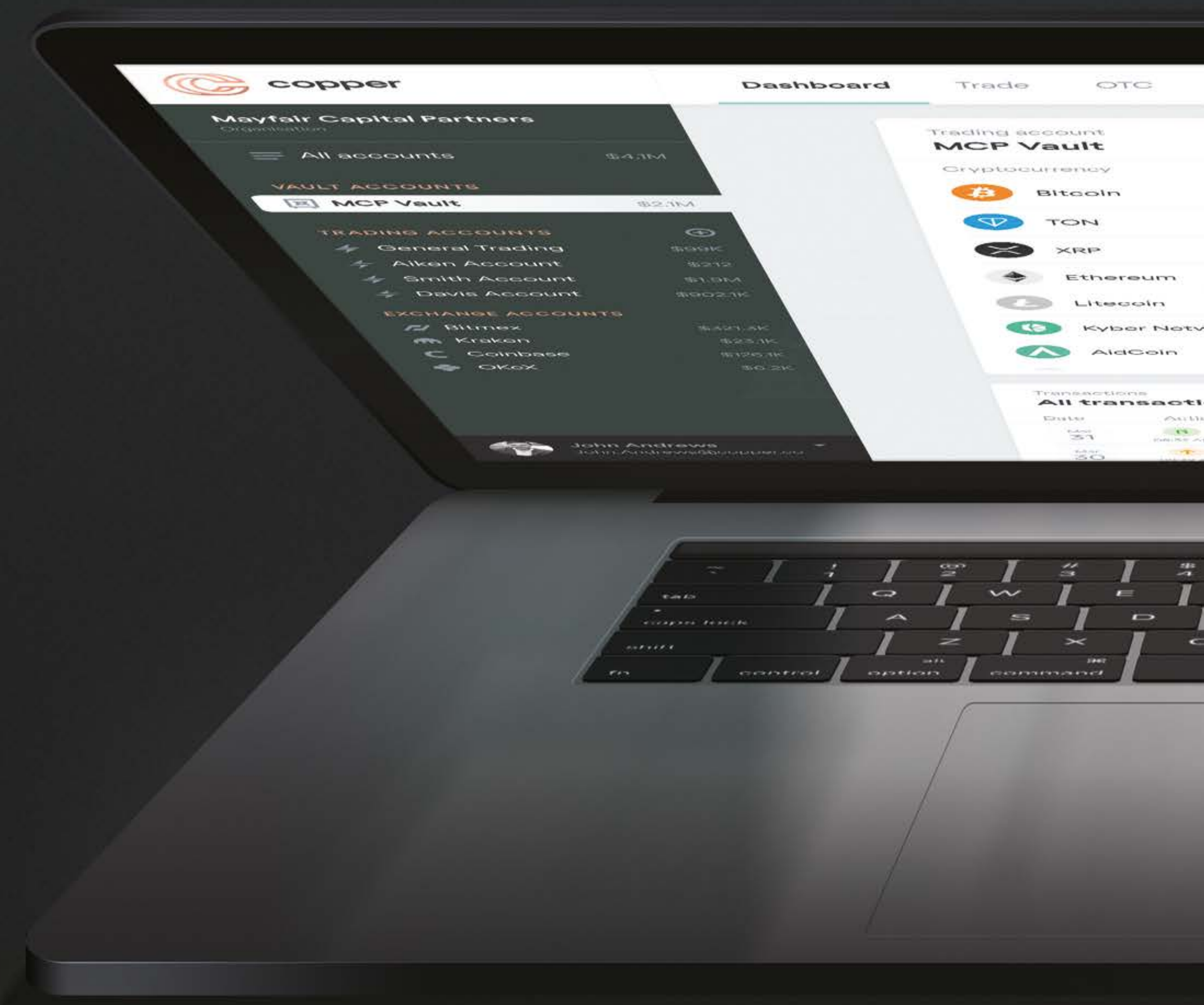

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Routes to institutional growth in digital assets

By A. Paris

The institutionalisation and maturing of the cryptocurrency and digital assets world is taking place – at present this is primarily happening through investment professionals moving from traditional finance and setting up their own cryptocurrency funds. But increased allocations from institutional investors are also expected to follow as the long-term outlook for the sector looks robust, volatility notwithstanding.

Niclas Sandstrom, CEO & co-founder of Hilbert Capital, assesses the development of the industry through people moves: "Many of my colleagues, myself included, came from traditional finance, hedge funds or investment banks. This movement is a good thing because, although there are also people coming from a purely technology background in crypto and funds, you can't overstate the importance of having managed money and risk before and having been in that environment. The truth is that the infrastructure around these assets is not as strong yet, so having that experience in traditional finance is helpful. Having people migrate from traditional finance into the digital assets space definitely accelerates the maturity process."

Dmitry Tokarev, CEO of Copper, has also seen this development: "People move from traditional finance to the crypto space everyday. Our clients are not all crypto native fund managers – they are former private bankers or portfolio managers of global macro funds, long short funds, etc."

Alex Batlin, founder and CEO of Trustology, agrees: "We are seeing the gradual institutionalisation of the crypto world which is happening through people movement rather than traditional organisations committing large chunks of capital to these assets."

This maturing of the industry can be seen to support the argument for greater flows of institutional money into cryptocurrency and digital assets. Having experienced money managers running cryptocurrency funds can give traditional institutional investors more confidence in allocating money to such assets.

According to Tokarev: "Capital allocators are the ultimate goal and we're likely to see more funds appearing and being made available. There is also an element of time and certain decisions you cannot make without taking the view for the next 20 to 30 years. This asset class hasn't been around for this long yet so it's not unreasonable that they're not investing yet."

> *Although there are also people coming from a purely technology background in crypto and funds, you can't overstate the importance of having managed money and risk before and having been in that environment.*

Niclas Sandstrom, Hilbert Capital

Pierre Maliczak, CEO of Altarius, comments on the outlook for institutional flows into digital assets: "Currently, the institutional money allocated to this asset class represents about 10% of the market. To be recognised as a real asset class, the allocation needs to increase drastically. Now, more than ever, I think such investors will be considering investing into cryptocurrencies. The amount of debt issued recently by the central banks does raise serious questions about fiat currency valuation. China, with the announcement of the creation of its own digital currency, challenging the supremacy of the US dollar will add instability too."

Sandstrom at Hillbert makes a similar forecast: "This central bank crisis has seen them printing so much money and with interest rates being so low for such a long time, digital assets are a good hedge against this. If you invest long term, digital assets are safe from inflation, or hyper inflation, and are not correlated with gold or stocks. So cryptocurrency is looking a lot more appealing from that point of view."

Batlin notes the industry has been talking about traditional institutions coming into the digital space for a long time but it hasn't happened en masse yet: "We haven't yet seen traditional institutions putting a large chunk of their allocation into crypto."

However, according to Sandstrom institutional investors are coming around to the idea of having a digital assets allocation: "People are starting to understand that although cryptocurrency means a lot of volatility it also generates enormous return. This doesn't mean they should put all their money into digital or crypto but they should make an allocation - for some 2% of net assets is the right allocation, for others it might be 10% or more."

"At the moment I think it's irresponsible not to have any exposure to digital assets or Bitcoin at least. It's a genie you can't put back in the bottle – the more it exists the less likely it is to go away," adds Tokarev.

Bridging the gap

Maliczak at Altarius says there are still serious obstacles holding institutional allocation back: "What the investor needs is a clear international regulatory framework and proper bank custody services to safeguard the assets. It is moving but it will take time."

However, according to Batlin, the reason for low take-up from institutional investors, particularly pension funds, is not driven by the lack of traditional custody banks. He says: "Fidelity offers custody but this has still not encouraged pension funds to allocate. They are cautious by nature and so they should be. The lack of demand on their behalf is driven by the notion of the asset class still being too risky and not deep enough. Although the infrastructure is a factor, it is not one that's keeping them from allocating."

Sandstrom speaks of the importance of having traditional players offering custody of digital assets, alongside the new, more tech-based players: "It's important that traditional players come on board because it lends trust. Having a firm like Fidelity is great for adoption because people trust Fidelity. On the other hand, the newcomers have more innovative ideas. They have more freedom and in that freedom new exciting technologies will be born that a traditional player like Fidelity wouldn't go near. So, it's important that both exist in parallel."

"The traditional banking sector does already face many challenges in dealing with this new asset class and the new technologies attached to it (competition with neo-banks, KYC, digital onboarding and so on). It's going to require them to re-think their whole business model. But they have no choice if they want to survive," says Maliczak.

Sandstrom however acknowledges that having so-called household names offering custody will not automatically lead to greater allocations: "I think it will just take time. Institutions, especially pension funds, are quite conservative – rightly so. But we have seen investors like university endowments – MIT, Harvard, Chicago – who have been allocating for some time."

Batlin believes insurance funds will be the next big institutional player to allocate to the digital space: "They're geared towards graduated risk. Part of what they do is take different risks and bets so I can see that they may choose to go down this route a lot more in the near future."

Maliczak outlines another trend: "We've also seen recently clients investing heavily into young start-up companies they identify as being potential market disruptors in very specific spaces. The view is to get access to new technologies for their own business and leverage on investment opportunities with high diversified potential returns. The risk is higher, but looking at the current market conditions, it does make sense."

Although Tokarev at Copper concedes this could be a way to bridge the gap; he notes: "You can do this but it's a double bet – you're long the sector but also long the execution so it's a double or nothing bet. If you believe in the sector then you should put 1-5% directly into Bitcoin." ■

Institutional calibre custody solutions and connectivity

Interview with Paolo Ardoino, Hugh Hughes & James Banister

Bitfinex, a state-of-the-art digital asset exchange, is leading the way in driving mass institutional participation in the crypto trading market. Through strategic partnerships, Bitfinex has created an institutional calibre offering, providing hedge fund managers with a robust infrastructure to enable them to offer digital asset trading to clients.

Its partnership with Koine, a London-based digital asset custody provider and FCA authorised EMI, pushes boundaries in providing an institutionally oriented post-trade service, enabling investors to mitigate counterparty risk and use private keys in the clearing and settlement of cryptocurrencies.

Koine's secure, bank grade infrastructure and governance provide a true separation of duties for the custody and settlement of digital assets. Its unique security model, using Digital Airlocks™, replaces the cold store and hot wallet model which exposes private keys to humans and results in poor operational scalability. By combining this new digital asset security model with fiat custody and DvP settlement, Koine provides a post-trade solution that is suitable for traditional capital markets.

According to Paolo Ardoino, CTO at Bitfinex, the exchange's partnership with Koine "is critical in driving uptake of digital asset trading amongst hedge fund managers worldwide, mitigating counterparty, insolvency and credit risks of trading on exchanges."

Ardoino added that it is part of the exchange's ongoing strategy of building a service fit for institutional trading, which began around two years ago when it selected Market Synergy to build a bespoke network for the exchange to address a gap in the market. "We are now at the forefront of delivering robust, high performance connectivity for institutional clients," said Ardoino.

Market Synergy GmbH is a Swiss-based organisation which offers institutional standard cryptocurrency connectivity for hedge funds, banks and brokers through a highly secure, reliable network which is monitored and supported 24x7. Any institution wanting to trade cryptocurrencies can connect with Market Synergy via a FIX feed or ISP link and access Bitfinex's wide selection of digital assets. Market Synergy also offers colocation services to any Bitfinex institutional clients.

James Banister, CEO, Market Synergy adds, "Market Synergy is part of the FXecosystem group of companies and we have over a decade of experience in outstourced connectivity for institutional clients. We have applied the same high standards to our digital asset infrastructure that we use in the FX market. Being secure, robust and reliable is a priority at all times but never more so than now. During recent periods of extreme volatility, our network was able to process digital asset volumes exceeding $2 billion in a single day which is a significant achievement.

"Since launching our joint offering with Bitfinex, we have built an impressive worldwide client base including hedge funds, specialist crypto funds, professional traders and brokers. We are confident that Bitfinex's latest development, through its partnership with Koine, will result in a surge in clients as having access to a professional custody solution for handling digital assets provides financial institutions with increased confidence in the digital asset sector."

Hugh Hughes, Chairman and CEO at Koine concludes, "Since the early days of digital assets, it's been clear that, in order to attract algorithmic funds managers, a traditional market structure was essential. And this is what we have created; a post-trade environment that, alongside leading exchanges like Bitfinex, meets the custodial and settlement needs of institutional capital." ■

Paolo Ardoino
CTO, Bitfinex

Paolo Ardoino joined Bitfinex in early 2015 and now serves as CTO, developing and managing core parts of the Bitfinex backend architecture. Paolo has been building valuable tools and infrastructure for financial innovation for the past 15 years.

Hugh Hughes
Chairman & CEO, Koine

Hugh Hughes is an experienced CEO who has been responsible for brokering several large-scale mergers and acquisitions, including the sale of Fixnetix to CSC (now DXC Technology). Hugh was CEO of Societe Generale Securities for nearly 10 years.

James Banister
CEO, Market Synergy

James Banister founded Market Synergy GmbH in 2018 to complement the FXecosystem group of companies. Market Synergy provides institutional-grade connectivity to the digital asset market place. James has been involved in the FX industry for 25 years.

Digital Asset Custody

We make it safer, faster & easier

Trustology's vision is to create the most compelling digital assets company of the 21st century. We believe in accelerating the crypto economy by pioneering new ways of generating value for everyone on the blockchain.

Utilising our highly-skilled and innovative people, well-designed processes and superior technology, we're delivering best-in-class digital assets custody solutions.

Our first focus has been securing and managing cryptoassets for individual and institutional investors with our TrustVault platform technology—on-chain, on-exchange and now when working with decentralised finance protocols.

Make the move.
Open a TrustVault account today.

Eliminating credit risk will lead to increased flows into digital

Interview with Dmitry Tokarev

Capital inflow into digital assets from active asset managers is expected to increase in the near future. Investor concerns regarding exposure to credit risk from exchange venues are being overcome as a result of new infrastructure developments.

"The elimination of credit risk signifies considerable progress in this area. The biggest thing it does is that it unlocks the capital due to arrive into the space. So far, this factor has been a major deterrent, according to most of our client feedback," explains Dmitry Tokarev, CEO at Copper.

He says the firm's recently launched tool – ClearLoop – does just this: "We built a clearing network to resolve the issue of investors and traders having collateral sitting at the venue. If one of those venues disappears, as has happened in the past, then all that money would be lost. Our tool, however, allows investors to face the exchange directly, get better pricing and settle trades instantly."

This means investors can bypass the exchange's hot wallets and settle trades off-exchange, allowing them to be more agile given they have full control over their response to market movements and pricing changes.

The way it works is that ClearLoop ensures both the client and the exchange have enough assets to cover any position submitted by a trader before it is opened. Copper then settles fiat and crypto trades instantly between parties after the trade has taken place.

Tokarev discusses the impact such infrastructure will have on the value proposition of crypto from the perspective of institutional investors: "The crypto space offers plenty of trading opportunity as there are many inefficiencies there to exploit. Also, the funds are returning 5% per month, which is attractive especially given the return in many other areas has dried up. But the risks have often outweighed the appeal of the sector. If you eliminate some of those risks, such as the credit risk to exchanges, then it becomes a more attractive value proposition, thus improving investors' willingness to allocate to these assets."

Essentially, Copper is driven by the guiding principle that the problems its clients face can be solved efficiently, collaboratively, and securely to the benefit of the entire digital asset ecosystem.

Asked about volatility in the digital space, Tokarev points out: "Volatility is a trader's best friend and an investor's worst enemy. The industry is still young and is still developing so the volatility is expected and is not a problem. Once people understand the value proposition I don't think anyone can do the research and come away thinking it's all smoke and mirrors. If you understand the math and the money I don't see how this can not make sense on a longer term horizon."

Beyond crypto

Copper's aims as a firm go beyond the crypto and digital assets market. Tokarev outlines his ambition to have the infrastructure the firm is building be applied to traditional finance: "Many of us come from a traditional capital markets background and we know the difficulties back and middle office professionals face in dealing with a system which is archaic and has not changed in the last 30 to 40 years."

Although there are characteristics which differentiate a digital assets fund from a traditional active fund, Tokarev details how from a fund management standpoint, the two differ very little: "We're talking about the exact same structure as any other fund. They have a structure, a manager, a PMS system. They go to the same lawyers to put together a prospectus and a DDQ, they have an administrator and auditor to onboard LPs and receive subscriptions, custodians, etc. Ultimately you can be in a situation where your digital assets funds can have the exact same structure as in the traditional space."

He acknowledges legacy systems which underlie trillions in assets are hard to change and integration can take longer. However, Tokarev believes this change, should it be undertaken, would revamp work practices: "It would improve life for people working in back and middle office functions. So the next generation of CTOs can work more efficiently.

"It's about giving tools to the middle and back office to allow buyside players to operate more efficiently, more transparently. Using such infrastructure would allow them to work faster and generate more value for their investors by doing what they do best which is manage funds."

Lessons from B2C

Tokarev also describes how within traditional finance, there is no single source of truth of information, which is a problem blockchain can solve: "Blockchain is the most secure database in the world because it is driven by a central source of information. Blockchain is the only system where that central database is immutable and cannot be modified. But, critically, it can be accessed by everyone. This offers a secure central source of information, as opposed to traditional markets which rely on disparate databases belonging to asset managers, prime brokers, custodians, exchanges, clearing houses, etc, all trying to execute and settle the same trade. At the end of the day, financial markets are driven by data about who has what."

He also says this technology can lead to the end of T+2 settlement: "Different assets can live on blockchain and people can trade them in a trustless environment, in seconds rather than in days. Technically, T+2 settlement, which is the norm, can be abolished. There is no physical reason for T+2 to exist. With blockchain you can settle instantly and in such a way that it will be verified and proved – It will not only prove the entry exists but also that the entry is not forged and is correct. It's robust recording keeping and its free."

The goal of embedding this technology in the business to business world is bold but the potential makes it a worthwhile undertaking, especially if lessons are learnt from the B2C market. "If B2C fintech is a Ferrari, B2B is still very much a cart being pulled by a cow. However, we would like to create the infrastructure which traditional financial services will use because B2B fintech is 50 times larger than B2C fintech, and could operate more efficiently if given half a chance." Tokarev says. ■

Dmitry Tokarev
CEO, Copper

Dmitry Tokarev started his career as a Quant, having graduated from Imperial College, London, with a Distinction in Risk Management and Financial Engineering. He later helped to build an asset management firm as its CTO and as a partner, which currently oversees c. USD5 billion in assets. It was there he observed a gap in the market for Copper, as he found there were no feasible options available to institutional investors in the Crypto space that allowed for the necessary security, control and speed of storing crypto assets.

Operational support gains ground as crypto develops

Interview with Alex Batlin

The digital asset space has expanded to include multiple cryptoasset types, blockchains and a variety of centralised and decentralised exchanges – the administrative burden of which has grown exponentially for investors. As larger investors such as asset managers and family offices look to increase their trading activity in the digital space and diversify their portfolio, services provided by third parties to support their efforts are gaining importance.

When Bitcoin first came to market in 2009, it was the only crypto asset available and investors were not focused on trading it as such. Due to it being new, they took a buy and hold approach and the go-to insured private key custody solution at the time was cold storage – a physical offline vault.

The market has since developed dramatically. Alex Batlin Founder and CEO of Trustology discusses: "As the crypto winter passed, investors wanted to make money on Bitcoin beyond capital growth. This meant the inclusion of borrowing, lending and hedging mechanisms. People also wanted to increase their trading activity through margin calls – trading Bitcoin either on spot or through derivative contracts."

For this to happen, assets needed to be transferred at speed – something which previously was not a priority. "Before, you had 48 hours to ask your cold custodian to transfer assets as few wanted to actively trade it. Now, however, you need to trade a lot more quickly to make those margin calls and fund positions on exchanges with digital currencies. All these things require velocity and capacity to execute transactions much more quickly," Batlin explains.

He goes on to outline the further evolution which has seen the proliferation of asset types and trading venues: "There are now thousands of different coins on tons of different networks. The variety is huge and investors need to worry about managing all of them as each one has a slightly different wallet that's native to that platform and usually the user experience is poor."

In addition, there are now several venues for trading, lending and borrowing. As yet, no single venue has enough liquidity to support large trading volumes, therefore managers need to trade on multiple exchanges. Further, as the market matures, the assets increase in value and may become prey for hackers.

These developments mean the crypto market is growing, and asset managers have more opportunity to generate alpha. However, they also result in a greater administrative burden, which managers are often not trained to handle or lack the technical expertise to navigate. The market is, therefore, seeing the emergence of crypto custody service providers like Trustology, offering the security and operational support needed in managing private keys for asset managers looking to actively trade in digital assets.

"We've created a secure, segregated key and transaction management system which allows managers to generate multiple wallets and work with assets on-exchange, on-chain and across decentralised finance (DeFi) protocols. With on-chain assets, we safeguard private keys on the client's behalf. For on-exchange assets, we manage all client withdrawals and transfers and allow clients to create controlled environments ("walled gardens") across exchanges using enforced multisig and whitelist controls."

"Working with us allows asset managers to raise more capital from investors because it raises investor confidence in the manager's operational capabilities i.e. mitigating holding and fiduciary risks. Also, their time is precious and instead of managing manual and cumbersome tasks, they can focus on what matters – generating alpha," Batlin concludes. ■

Alex Batlin
Founder & CEO, Trustology

Alex Batlin is the CEO and Founder of Trustology. A self-confessed technology geek, Alex is an entrepreneur at heart with extensive banking and blockchain experience and tenure. Previously, at BNY Mellon, Alex was Blockchain Lead and Founding Head of the Emerging Business & Technology team. At UBS, Alex was founding head of a blockchain-focused FinTech Innovation Lab in the UK's Level 39 accelerator. Alex co-founded Utility Settlement Coin, Enterprise Ethereum Alliance and the Trusted IoT consortia, and was featured in the 2015 FinTech Finance35 and 2016 FinTech 40 lists.

BITFINEX

Founded in 2012, Bitfinex is a digital asset trading platform offering state-of-the-art services for digital token traders and global liquidity providers. In addition to a suite of advanced trading features and charting tools, Bitfinex provides access to peer-to-peer financing, an OTC market and financed trading for a wide selection of digital assets. Bitfinex's strategy focuses on providing unparalleled support, tools, and innovation for experienced traders and liquidity providers around the world. Visit our website to learn more.

Contact: press@bitfinex.com

www.bitfinex.com

COPPER

Copper.co is an institutional cryptocurrency custody and prime brokerage firm, headquartered in London. Founded in 2018, Copper provides the infrastructure to acquire, store and trade digital assets, in a manner which satisfies global investors and regulatory standards. Copper's products are unique in the cryptocurrency space. While there are other infrastructure providers, often they charge for withdrawals, lack clarity in trading locations and offer poor security. Copper is different. By leveraging MPC safeguarding protocols, Copper ensures that its clients - ranging from funds, financial institutions, and high-net-worth individuals - have complete certainty that their capital is never at risk of theft. Copper is also one of the few digital asset custody solutions to be insured against crime, including theft of fiat or digital assets, with a comprehensive policy brokered by Aon in London.

Contact: info@copper.co | +44 (0)20 7101 9455

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KOINE

Koine offers segregated, institutional custody & settlement of digital assets, providing essential Financial Market Infrastructure (FMI). This brings together the full suite of governance, compliance, risk management and audit of real-world asset trading to the digital asset ecosystem for the first time. Institutional clients can engage with digital assets while fully adhering to regulated market practices. Koine's 'Digital Air Lock™' technology embeds 'EAL7+' military-grade security to secure digital assets and prevent them being compromised. Its ground-up architecture, team, governance and systems make it the only choice for the professional trading community, delivering a truly institutional service for all trading styles, from passive holding to high-frequency trading, across multiple venues with real-time gross settlement.

Contact: Jason Mochine | jason.mochine@koine.com | +44 (0)20 7072 0955 / (0)7990 565040

www.koine.com

MARKET SYNERGY

Founded in 2018, Swiss-based Market Synergy provides institutional-standard robust and secure cryptocurrency connectivity to the digital asset market place. Customers include hedge funds, brokers and traders. Any institution wanting to trade cryptocurrencies can connect with Market Synergy to access a wide selection of digital assets. It also offers a FIX feed and ISP link to Bitfinex's digital asset gateway, giving trading firms the means to trade this asset class. Market Synergy is part of the FXecosystem group, whose wealth of expertise in building and maintaining secure networks for institutional clients underpins Market Synergy's ability to provide digital asset pricing though a proven infrastructure, monitored around the clock by our dedicated NOC team.

Contact: Jonathan Baile | +41 (43) 588 02 58 | jbaile@marketsynergy.ch

www.marketsynergy.ch

TRUSTOLOGY

Trustology was created to help accelerate the crypto economy by enabling the adoption of cryptoassets on a global scale. We build solutions to address the very real concerns that stand in the way of widespread blockchain adoption, now and in the future. This extends to safeguarding digital assets which we prioritised addressing.

That's why we built TrustVault – a fast, user-friendly and highly secure custodial wallet service designed to address the security and ownership shortcomings of existing custody solutions, hardware wallets and cold storage options today, whilst also providing the same level of speed, flexibility and access we've come to expect from traditional assets and account services.

Contact: Mia Mohamed | mia.mohamed@trustology.io

www.trustology.io