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Can cryptocurrencies trade like traditional asset classes?

In the aftermath of the conviction of FTX founder Sam Bankman-Fried, investors want to better understand cryptocurrency transparency and liquidity. This is an executive summary of the *Caution to Confidence: Trusted Access to Cryptocurrencies* webinar hosted at the end of 2023. Listen to the full recording here.

A common misconception is that all cryptocurrencies are alike. Understanding how various digital currencies are managed and valued is key to creating transparency around these assets. For institutional investors to be comfortable allocating time and resources to crypto, they need to know the underlying assets.

Ways to invest

There are four traditional ways to invest in crypto. Often, this is determined by investors' institutional arrangements, fund restrictions and other rules. They can purchase or invest in:

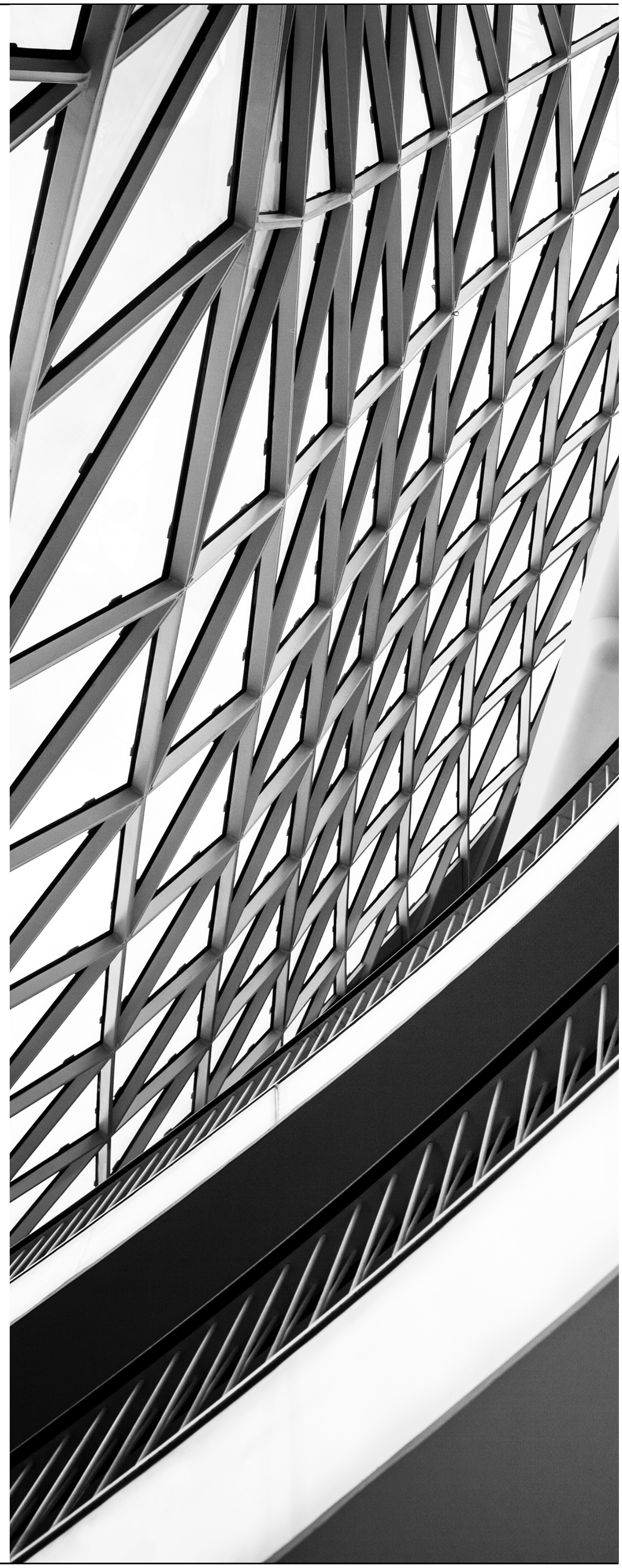
1. **Bitcoin.** At the most basic level, investors can buy bitcoin and Ethereum outright. Then they can decide how to solve for costs, security and other considerations.

2. **Listed exchanges.** Exchange-traded funds, exchange-traded products and trusts can come at premiums or with costs that can make them unattractive for some investors.

3. **Derivatives.** Options or structured products are where most institutional investors are likely to be the most comfortable with cryptocurrency investments. This allows them to allocate money into the space without owning the assets or interacting with the securities.

4. **Proxies.** Listed stocks or miners that trade on the stock exchanges and own crypto offer exposure to the sector without investors having to invest in a set-up to interact with or manage the currencies.

Institutional investors should decide how they plan to invest in the market that is best for their clients, investing structures and governance policies. Investment methods come with their own levels of risk.



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Wide-scale adoption

For the institutional investor community to adopt cryptocurrencies on a wider scale, several elements need to be aligned. One of these is global regulatory clarity so asset managers have a clear understanding of oversight and how to remain compliant.

Look for assets traded on regulated platforms. This ensures access to familiar risk-mitigation tools and provides the benefits of a central counterparty. For example, in 2023, Eurex launched FTSE Bitcoin Index Futures and later extended its offering to include Options on FTSE Bitcoin Index Futures, which is just one product among many in the asset class that helps investors manage risk and sets them apart from other exchanges.

"Investors are increasingly turning to this type of solution where they can trust and they're familiar with the safeguards," said Nicolae Raulet, crypto derivatives product manager at Eurex.

"The focus on risk management really is what's going to drive us forward. Understanding who's interacting in the space, what the markets actually look like, what is the size of the market, and how to do that safely," Raulet said.

"The focus on risk management really is what's going to drive us forward."

Nicolae Raulet, crypto derivatives product manager, Eurex

Because crypto crosses many different disciplines and departments, it can be difficult for companies to onboard. Allocating funds to set up cryptocurrency management is key. Institutional investors and retail brokers have a high standard for market infrastructure in traditional asset classes. To grow and attract more allocations, this also must be the case here.

Yet, "even as the asset class matures, it will probably remain a very volatile space," said Ilan Solot, co-head of digital assets at Marex, a leading provider of custom derivatives and structured products. One of the biggest trends is the "institutionalization of the space and the huge amount of infrastructure being built around digital assets to make it a legitimate asset class," Solot added.

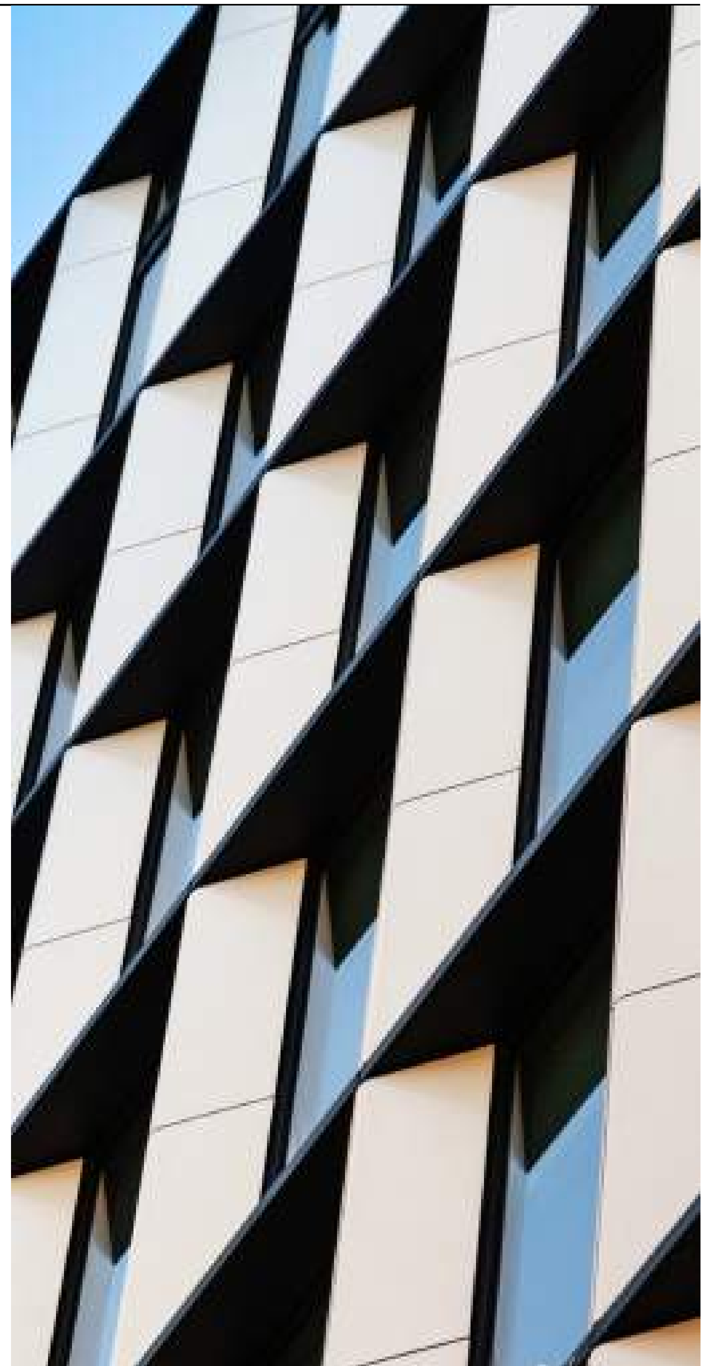
Risk management

The FTSE Digital Asset Indices cover crypto digital assets and were developed in response to investor demand for benchmarks that accurately capture and track the performance of these assets. This allows for integration into traditional portfolio analysis and processes.

Every quarter, FTSE Russell evaluates each of the exchanges to understand the market. They're vetted on qualitative measures such as location, licenses, regulatory oversight and compliance, and proper documentation. On the qualitative side, exchanges are evaluated for the data coming in such as trade volumes, signs of manipulation and other transparency measures.

Exchanges are placed on a list of participants and their trade data are used to calculate the price that drives the FTSE Russell indices. Those on the watchlist are monitored and used to trade a broader list of assets. FTSE DAR Benchmark Assets Reference Price is the underlying pricing methodology designed to capture data from vetted assets and exchanges to meet the requirements of European Union benchmarks.

The FTSE Digital Asset Index Series can be used as a starting universe, performance benchmarks or the basis for index-linked products such as derivatives and ETFs. Creating a transparent pricing methodology is critical to attracting traditional institutional investors to the digital asset space.



"How do we go that extra mile with the asset vetting? We look at things like developer activity, minimum liquidity constraints, how much float in the market and minimum market capitalization parameters. There is a much higher bar for those assets to be [on] an EU BMR-compliant list."

Kristen Mierzwa, head of digital assets — Index Investments Group, FTSE Russell

FTSE Russell is your essential index partner for a changing world. We provide category-defining indices across asset classes and investment objectives to create new possibilities for the global investment community. To learn more about the FTSE Digital Asset Indices, contact us.