

Crypto asset hubs

By Lawrence Au

Regulators work to balance risk while positioning for the opportunities

Financial centres across the world are stepping up efforts to establish themselves as crypto asset hubs as mainstream adoption gathers pace. Global crypto-themed funds attracted US\$9.3 billion of inflows last year, up from \$6.8 billion in 2020, according to data from digital asset manager CoinShares.

As of end-2021, crypto investment managers had \$62.5 billion of assets under management. There were 132 investment products in the market, including 37 launched in 2021 and 24 in 2020, reflective of growing demand and popularity.

Last year also saw the debut of the world's first exchange-traded fund backed by physically settled bitcoin. The Purpose Bitcoin ETF began trading on the Toronto Stock Exchange on February 18, 2021, and amassed \$1 billion of assets after one month, underscoring investors' eagerness for an easy way to get exposure to bitcoin.

Meanwhile, the first US bitcoin-linked ETF bowed in on the New York Stock Exchange on October 19. The ProShares Bitcoin Strategy ETF tracks bitcoin prices through futures contracts traded on the Chicago Mercantile Exchange. It was one of the most heavily traded ETFs in market history on the day of debut.

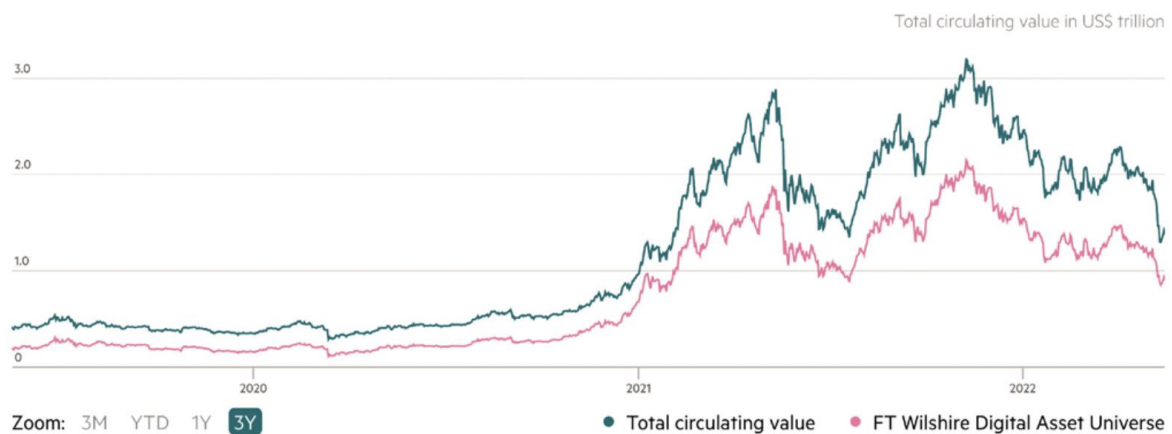
Trading volumes of crypto currencies broke all records in 2021. Crypto research firm The Block Research reported more than \$14 trillion in trading volume from centralised crypto exchanges, which hold customers' private keys, unlike decentralised exchanges. That figure was almost seven times higher than in 2020.

Overall market conditions have taken a drastic downturn this year. Prices of both traditional and crypto assets have plummeted. As of May 12, the price of bitcoin had plunged around 60% to \$27,908 from a peak of around \$68,000 last November. The aggregate circulating value of the ten largest crypto coins tracked by the FT Wilshire Digital Asset Universe fell to \$926.96 billion. But that is still larger than the gross domestic product of the Netherlands, which, at \$913.86 billion last year, was the 17th largest economy in the world.



Aggregated view of the FT Wilshire Digital Asset Universe

Circulating value



More metrics

Circulating value	\$926.9bn
Universe coverage	67%
Number of assets covered	10

*As of May 12, 2022
Source: Financial Times

About this view

FT Wilshire Indexes have a strict eligibility on which exchanges can contribute. The total circulating value represented here is the aggregate circulating value of eligible digital assets trading on the eligible exchanges. This circulating value will differ from similar figures quoted elsewhere.

The regulatory landscape

As institutional and retail capital pour into crypto assets and new types of blockchain-based securities and exchanges continue to emerge, nations are working on regulations to prevent risk as well as to position themselves for the financial opportunities that come with these assets.

The US is home to the largest number of crypto investors, exchanges, trading platforms, crypto mining firms and investment funds. However, its rules and regulations are often ad hoc and reactionary. Different government agencies, including the Securities and Exchange Commission (SEC), the US Treasury, the Federal Reserve, and the Commodity Futures Trading Commission, have issued their own differing interpretations and guidance.

This March, the White House issued an executive order directing government agencies to coordinate their efforts to create a regulatory framework for crypto assets. Apart from ensuring consumer protection and financial stability and mitigating illicit use, it aims to give the US a competitive edge in crypto development.

In the European Union, the Markets in Crypto-assets Regulation introduced in 2020 provides a legal framework for the development of crypto asset markets within the bloc. It clearly defines the regulatory treatment of crypto assets that are not covered by existing financial services legislation.

Last December, the European Parliament and the Council of the European Union reached an agreement on the Distributed Ledger Technology (DLT) Pilot Regime Regulation. The regulation



lays down the conditions for acquiring permission to operate a DLT market infrastructure, defines which DLT financial instruments can be traded, and details the cooperation between DLT operators, national authorities and the European Securities Markets Authority.

This April, the UK government announced initiatives designed to make the country a global hub for crypto asset technology. The move includes bringing stablecoins into the ambit of UK regulation with a view to their being used as a recognised form of payment; legislating for a financial market infrastructure sandbox to help firms innovate; working with the Royal Mint on proposals for issuing a non-fungible token; and an engagement group to work more closely with industry.

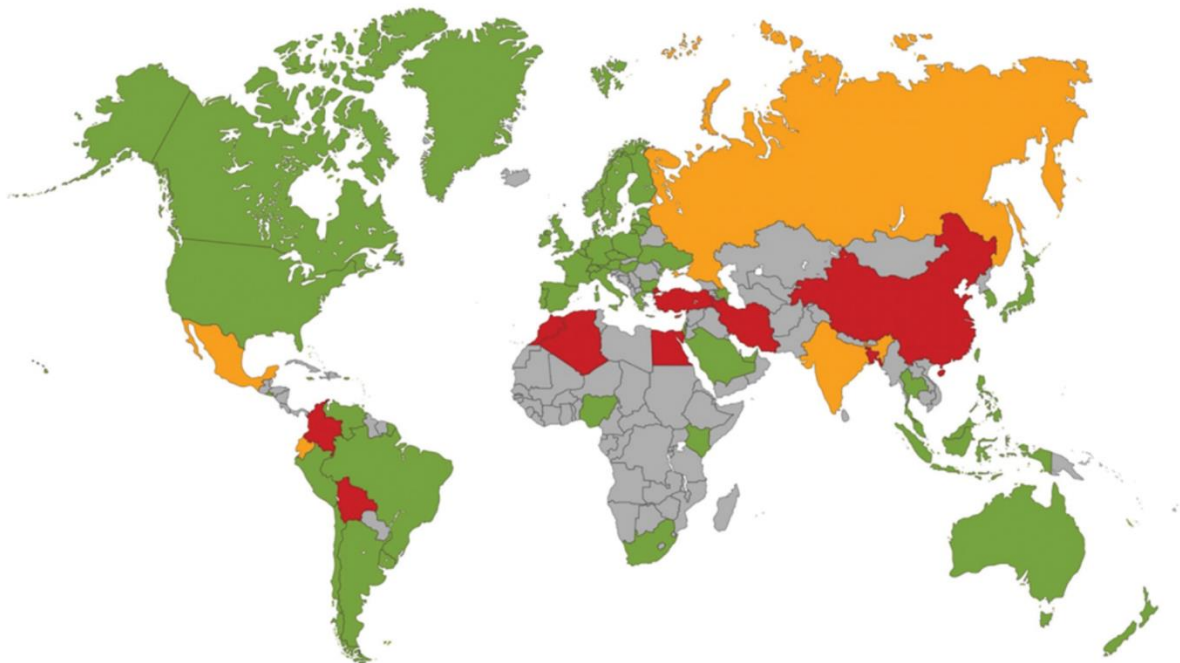
It is Switzerland, however, that is leading the pack in Europe in the crypto space. Following the initial coin offering boom and turmoil in 2017, it introduced a framework that classified digital assets so that they could be regulated in the same way as existing financial markets.

In September 2020, Switzerland introduced the Distributed Ledger Technology Act, which enables the introduction of blockchain-based securities with the same functionality and protection as other securities. It also allows multilateral trading of these securities by non-professional investors by introducing a new type of financial market infrastructure authorisation. The country has been hailed for showcasing some of the best practices in regulated crypto markets.

Over 1,100 blockchain and crypto companies have now set up home in the Alpine State's so-called Crypto Valley, and 14 of them reached unicorn status at the end of 2021. The combined value of the 50 largest companies has grown to \$611.8 billion, according to a report published on the government's Swissinfo.ch platform in January.

Cryptocurrency regulations by country

■ Mostly legal
 ■ Some significant concerns
 ■ Mostly illegal



Source: Thomson Reuters 2022

Asia Pacific leads growth

The Asia Pacific is the fastest growing region for crypto assets. Research firm Chainalysis estimates that Asian markets accounted for 43% of global cryptocurrency activity, with \$296 billion of transactions between June 2020 and June 2021.

Japan was the first developed country in the world that formally legalised payment with cryptocurrencies and introduced a regulatory framework for crypto exchanges. However, its crypto industry's development was tainted by the high-profile collapse in 2014 of Mt. Gox, which once handled 80% of global bitcoin trading, and the headline-grabbing \$500 million hack on Coincheck in 2018.

In April 2020, the government formed two self-regulatory bodies, the Japanese Virtual Currency Exchange Association and the Japan Security Token Offering Association, to promote regulatory compliance and public confidence. With a strengthened regulatory framework along with a massive clean-up, the industry has restored much of its shine. The trading value of cryptocurrencies in Japan last year was over \$1 trillion, and the country is now home to 31 exchanges and over 450 blockchain companies.

China was the first cryptocurrency superpower in the Asia Pacific region. At one stage, it had a massive number of individuals invested in the cryptocurrency space, the largest bitcoin transaction volumes, and many companies and organisations exploring blockchain



and cryptocurrencies. But Beijing banned all cryptocurrency transactions in September 2021, driving all the players and their activities offshore.

Hong Kong's approach to crypto businesses has been fragmented. The Securities and Futures Commission announced in November 2019 a regulatory framework for virtual asset trading platforms riding on existing rules and regulations. The following August, OSL was given approval in principle for virtual asset automated trading and brokerage licences. However, there is still a lack of regulatory clarity. Digital asset firms find it difficult to open or maintain bank accounts in Hong Kong, and often have their accounts suspended for any transactions related to digital assets.

This January, the Hong Kong Monetary Authority issued a discussion paper setting out its thinking on the approach to crypto assets, particularly on payment-related stablecoins, taking into consideration international recommendations, the market and the regulatory landscape. It is seeking the views of the industry and the public on the regulatory approach.

Singapore has been very proactive in creating a separate and comprehensive framework on crypto and digital assets to address the unique complexity of these assets. The Payment Services Act of 2019 clearly defines the treatment of these assets as digital payment tokens (DPT) and licensing exchanges as DPT service providers, and puts crypto custodians under the Securities and Futures Act.

More than 170 firms, including some of the world's biggest crypto exchanges such as Gemini, Coinbase, Circle, and Crypto.com, have applied for operating licences since the Monetary Authority of Singapore opened applications in January 2020. But they soon realised that they were subject to the toughest screening and verification process. Crypto platform Bitcoin.com reported in December that over 100 companies have been rejected or had withdrawn their applications.

"The licensing process is stringent because we want to be a responsible global crypto hub, with innovative players but also with strong risk management capabilities," MAS Managing Director Ravi Menon said in a speech at the Financial Times Crypto and Digital Assets Summit on April 27. "We only approve applicants with strong governance structures, fit and proper board and management, and we go through their track record."

As of April, only three exchanges have been licensed to operate in the city state, although some have been allowed to service clients while waiting for approval. Some applicants who are frustrated with the lack of progress are now looking to set up shop in Dubai, which has been issuing licences to virtual assets service providers since March this year.

The Singapore government has also limited crypto activities only to accredited investors. In January, MAS published guidelines to discourage cryptocurrency trading by the general public. It prohibits bitcoin ATMs and clamps down on public advertisements and engaging third parties like social media influencers for promotion.



The Securities Services Advisory Group

Australia is the latest in the Asia Pacific region to announce ambitions to become a crypto hub. In March, the Senate Committee for Australia as a Technology and Financial Centre released a 168-page report containing 12 key recommendations to achieve this goal. Time will tell whether this initiative will gather momentum to push ahead.

As the fast-growing crypto industry evolves and countries vie to become crypto asset hubs, the key challenge is how to toe the line between innovation and regulation.

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