

Markets Update: Cryptocurrency Trading

Jake Siewert: Welcome to our Exchanges at Goldman Sachs Markets Update for Friday March 5th. Each week we check in with a leader across the firm to get a quick take on what they're watching in markets. I'm Jake Siewert, global head of corporate communications here at the firm.

And today we're going to talk about cryptocurrency trading. And to do that we're joined by Matt McDermott, global head of digital assets for Goldman Sachs Global Markets Division. Matt, welcome to the program.

Mathew McDermott: Thank you very much, nice to be here.

Jake Siewert: Well, I predict this will be an interesting session. Matt, you're sitting at the crossroads of a lot of interesting conversations about digital assets in general, but crypto in particular. Must be a very busy time. What are you hearing from the range of clients that we're engaged with?

Mathew McDermott: Yeah, it's certainly a busy time, that's for sure. I mean, in terms of kind of institutional demand, we have seen no signs of that abating. And when we talk about institutional demand, we talk about the whole cross section of the industry sectors. The team have fielded well over 300 conversations. And when I talk about the broad spectrum, I'm referring to hedge funds, to asset managers, to macro funds, to banks, to corporate treasurers, insurance, and pension funds.

And I think it's pretty fair to say that all of our institutional client discussion is really focused around bitcoin. Where the questions are not really, "What is it," thankful. It's more about how can we get exposure, what are the instruments we can transact, and what is Goldman offering today?

And I think what I've found most interesting in the number of conversations I've been part of is the diversity of them. And as you can imagine, the different industry sectors have different perspectives. And they're at different stages of their evolution. So, let's take corporate treasurers, for example, they're interested in two different aspects. Firstly, should they be investing in bitcoin on their balance sheet? And as they think through that, the key drivers from their perspective are negative rates, if they've got cash, you know, on deposit where negative rates are being applied. And then just the general fears around asset devaluation. And so, that's really kind of

driving a lot of thought from that perspective.

And then secondly, they're also thinking about it, particularly in the context of Tesla's announcement. You know, should we consider it as a payment mechanism?

Jake Siewert: Okay, so that's the corporate side, the corporate treasurer side. And obviously, in the wake of that big announcement by Tesla, a lot of interest in the space. How about the hedge fund complex? Some of them have been active for a longer time. What kinds of questions are you hearing from asset managers?

Mathew McDermott: The hedge funds, just taking them first, I mean, yes, they have been active. But I think there's been a reawakening. So, there's a lot of talk. But we've definitely seen a lot more activity across that industry sector over the last three to four months. And then when you look at the macro funds in the asset managers, it's broadly the same, that they've really started to think through all the different investment theses.

And so, from my perspective, talking to those clients, they're much clearer on why they want to invest. Really what they're interested in is broader market behavior. And really identifying what are the most efficient ways for them to get exposure and to think about hedging. To help inform that, our thinking, as well in this space, one of the things that we have thought about and are really keen to share the kind of results with our clients is, what do our clients think? So, we've conducted a survey across our institutional client base, specifically on crypto assets. And we've actually received nearly 300 responses. And found some pretty interesting feedback from that.

Jake Siewert: So, talk a little bit about what you learned from that survey. And was there anything surprising in the findings?

Mathew McDermott: Yeah, good question. What's been particularly interesting of the respondents, 40 percent of the clients currently have exposure to cryptocurrencies. And that could be through a variety of different mediums - the physical through derivatives, through securities products, or other offerings in the market. And so, that seemed actually a little high to me. But I thought that was kind of very reflective of the demand we've seen over the last three to six months.

I thought another interesting stat which really corroborates

what we've mentioned earlier was that 61 percent of the clients expect their digital asset holdings to increase over the next year. And while we're on this, I think it would be a little remiss of me also not to mention, I guess, the demand that we see across our wealth management client base. You know, we see continued appetite both internally and externally through the private banks. So, yes, we see a huge amount of demand institutionally, but we're also seeing that reflected in the private wealth management space as well.

Jake Siewert: This has been an area of focus for Goldman for some time now. How are the client discussions different today than they were four years ago, say, 2017?

Mathew McDermott: I mean plain and simple it's the institutional demand that we see. 2017 was very much a retail-driven market. This time around as mentioned, we've just seen a huge volume of institutional demand across the broad spectrum of different industry types. And as a function, you know, you're seeing incumbent banks now explore ways that they can develop products to satisfy that client demand, enabling them to kind of gain exposure to the different cryptocurrencies. And also, be mindful of what is possible from a regulatory perspective.

At GS, we're exploring a number of different options to facilitate that demand. And as mentioned earlier in the week in the press, we're actually going live with our crypto trading desk, which will be quite narrow initially. But we'll focus on CME features and non-deliverable forwards. And we're also now disseminating bitcoin content to our institutional clients through our Marquee platform.

Jake Siewert: Goldman, as I said, has been in the space for a little while. But some of the big institutions like Goldman have been held back a little bit by some of the regulatory uncertainty around there. What's kept Goldman and others from taking a bigger role in crypto?

Mathew McDermott: Yeah. I think one of the key factors is for the US banks it's the inability to trade the physical. And as we've seen from a lot of demand, particularly kind of with the hedge funds, some of the asset managers in the macro funds, is a desire to get access to the physical. So, that's been something that we've had to think cleverly how we can facilitate that demand in a different way.

In Asia, for example, there are certain jurisdictions where that

is permissible, where you can trade the physical. And we're seeing certain banks look at developing institutional exchanges and other avenues to execute the physical with institutional clients.

Jake Siewert: So, Matt, you mentioned that one of the things holding us back is inability of banks, like ourselves, to trade the physical. What is trading the physical-- we know what trading physical oil means. What does trading a digital asset like bitcoin, the physical asset, what does that look like?

Mathew McDermott: It's actually trading the spot instrument on a blockchain. And so, that's why you'll find with the trading desk we migrate to different products. So, we have the ability to trade derivatives where we cash settle, so we don't trade the physical.

Jake Siewert: So, to close out, any strong conviction from your survey around the price of BTC, where it may be at the end of the year? And more generally, what the future of crypto looks like?

Mathew McDermott: I'll take the last question first then come onto the price. I think this is a fast-evolving landscape where the crypto incumbents have certainly made huge progress over the last couple of years, be it from an institution, a custody, a risk management perspective, you know? And we fully expect them to continue to do so.

But as institutional demands, there is an expectation from clients now that the incumbent banks will develop their offerings to satisfy that demand. And so, I certainly anticipate a certain amount of consolidation across that space. And I think one of the responses in the survey does highlight this. When we talk about top products that clients are interested in, specifically in this marketplace, it is the ability to access spot through their prime brokers.

And the other kind of key fundamental point which I should definitely make is the underlying technology for these markets, private and public blockchains. This represents, you know, a real diverse set of opportunities for the financial industry and something that there's a huge amount of momentum in the market. We know firsthand just given the various different projects we're working on. And we see this as a hugely exciting time exploring the potential of that technology.

In terms of the price action, I think it's very difficult to predict bitcoin. It's not an easy pastime. But the survey was quite insightful in the sense that 76 percent agreed that the price by the end of the year would be between 40 and 100,000. So, hedging their bets somewhat. But 22 percent were predicting over 100,000 dollars. And I was on a similar survey with a private roundtable recently and the results there echoed something quite similar where 33 percent were predicting over 80,000 by the end of the year.

Jake Siewert: All right. Keep in mind, those are not Goldman Sachs predictions. That's from a survey of our clients who are active in the space. But we'll see what the future holds.

Matt, thanks for joining us today.

Mathew McDermott: My pleasure. Thank you for having me.

Jake Siewert: That concludes this episode of Exchanges at Goldman Sachs. Thank you very much for listening. And if you enjoyed this show, we hope you subscribe on Apple Podcasts and leave a rating or a comment.

In case you missed it, check out our other episode this week with Paget MacColl of Goldman Sachs Asset Management and Stefan Strein, CIO of the Cleveland Clinic on how healthcare organizations are investing capital through a public health crisis.

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