COMMENTARY

Why investors need legal certainty before they pile into NFTs

A recent ruling helped clear some issues up, but institutional appetite is still held back by a lack of clarity

In the never-ending search for yield, it is easy to see why asset managers are looking to invest in alternative asset types such as NFTs, which should, in theory, deliver higher yields

By Bourn Collier

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Bourn Collier is a director at consultancy Truva Corp

Anyone else get the feeling that the Treasury requesting the Royal Mint to create a non-fungible token is no more than political theatre? For all the talk on government-led expansion of digital assets, this has yet to result in action.

If the UK as a financial centre is to be a leader in innovating and growing the use of digital assets, we will need more than a sovereign NFT. Ask anyone working in the crypto industry at the moment, and the main thing they will say is that due to the fact that the Financial Conduct Authority has not approved anyone as a provider of cryptoassets, the UK crypto market is essentially frozen.

In contrast, other jurisdictions such as Malta, Bermuda and Gibraltar already have fully established cryptoasset regimes.

When most people think of NFTs, they immediately look to artwork and sometimes music or videos, where NFTs represent the original of something digital, as opposed to something tangible that would interest an investor. Currently, institutional investors are limited in the ways that they can benefit from NFTs. But institutional adoption is crucial to integrating crypto and NFTs into the UK financial system.

The challenge here is that most of these products don't have clearly understood structures with a sufficient link between digital interests and the underlying asset, deterring their use in funds and financial product creation.

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Progress is being made though, as the UK's High Court has recognised NFTs as property in a potentially groundbreaking case involving NFT marketplace OpenSea and a UK fintech entrepreneur seeking recovery of misappropriated tokens. The decision recognises rights to holders of these assets in the instance that they are lost or stolen, providing new protections. While this is encouraging, the OpenSea case could go further to satisfy the investment community.

There is somewhat of a barrier to asset managers who have never been under greater pressure from investors to find alternative ways to provide returns. In the never-ending search for yield, it is easy to see why asset managers are looking to invest in alternative asset types such as NFTs, which should, in theory, deliver higher yields.

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NFTs certainly present an attractive proposition to those on the hunt for high yield. According to a DappRadar report, the market generated more than $23bn in trading volume during last year. And in January alone, the NFT market as a whole topped $7bn in trading volume – well on its way to setting another record-breaking year. France-based asset manager Amundi is even considering entering the NFT market and offering its clients the ability to invest in them.

While this level of interest from the institutional investor community can only be seen as positive, asset managers will look to refine investment structures to protect their investments in NFTs.

The Treasury announcement is a good start, but why is the government only looking to have one NFT, as opposed to a number of them? After all, doesn't everyone want to have an NFT with a picture of the Queen on it?

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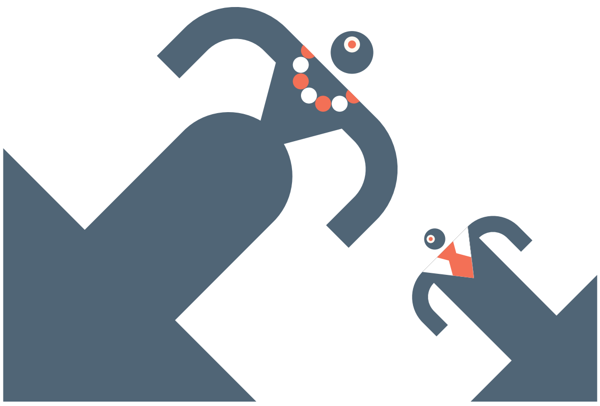

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