

Changing Client Needs: How Digital Assets will Shape the Financial Market

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This article describes how the needs of clients of financial institutions have changed, especially those of younger generations, and explores how this may relate to the adoption of digital assets in financial institutions. It looks at disruptions in the financial market based on the evolution of digital assets and suggests what financial institutions should consider when including digital assets in their offering.



Key Takeaways



- 1 The financial industry has evolved significantly, with traditional banks transitioning from in-person, manual, paper-based services to digital, automated self-service channels. This transformation was driven by technical progress, product diversification, globalization, regulations, and changing client expectations.

- 2 Younger, tech-savvy generations, such as Millennials and Generation Z, have embraced digital assets, trusting the concept of distributed ledger technology and appreciating the versatility, availability, speed, and global accessibility of its applications. Financial institutions have an opportunity to tap into the growing market of digital assets but need to address regulatory uncertainties and build the necessary capabilities to compete effectively. Additionally, blockchain technology offers efficiency gains and risk reduction in transaction processing between financial institutions, which can revolutionize settlement and other core processes.

- 3 Financial institutions should adopt a gradual approach, starting with specific use cases to gain experience in the digital asset field. They must focus on meeting the needs of their target client populations and regularly evaluate their product and service mix to align with evolving market dynamics. Building a strong positioning in the digital asset market will be crucial to succeed in this business.



Client Needs

Financial institutions have played a pivotal role in the economy for centuries: First banks have been established several hundred years ago. Since then, the general services of banks have not changed. They still centre around safekeeping of assets, processing of payments, facilitation and management of investments, lending and borrowing, exchanging currencies and providing financial advice.

The way that banks have provided services to clients, however, has changed fundamentally: from in-person, manual, paper-based services to digital, automated self-service channels. Drivers for this long journey of change include technical progress, product diversification, increasing globalization, increasing regulations and changes in clients' expectations.



Today's younger generations (Millennials and Generation Z¹) grow up in a digital age with exposure to internet, smart devices, and social media from a young age. Their consumer behaviour is portrayed by a preference for convenience (in terms of access, availability, speed, and ease of use), personalized user journeys and a relation to a good cause (purpose).



Users engage in communities of their interest. Peer reviews and user-generated content are considered trusted sources. The way that products are being used becomes equally important as the products themselves. In short one can say that younger generations value experiences and impact more than possessions.

The Adoption of Digital Assets

Younger, tech-savvy individuals have been early adopters of digital assets. They are more likely to be comfortable with technology, including mobile apps and online platforms, making it easier for them to access and use digital assets.

Digital assets can be broadly defined as any digital representation of value which is recorded on a cryptographically secured distributed ledger. Digital assets include crypto currencies, non-fungible tokens (NFTs), tokenized securities or any other tokenized assets.

Digital assets offer a range of characteristics that are attractive for young, tech-savvy individuals:

- Digital assets can represent a wide range of underlying assets and values, thanks to the versatility of blockchain technology and the concept of tokenization. This opens investment opportunities and applications around asset types like art, music, collectibles, in-game assets, etc.
- Digital assets can be divided into very small units, allowing to invest in fractions of high-value assets.
- Digital asset transactions can be performed with reduced need for intermediaries which allows for increased simplicity and higher transparency compared to the traditional financial market and its complex infrastructure.
- Digital assets operate on a global scale where assets can be accessed across different regions.

In a broader context, the popularity of digital assets among younger generations may be based on other factors as well:

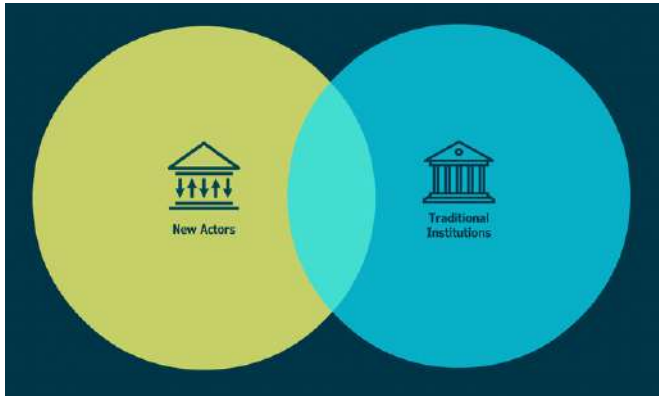
- Peer-to-peer interactions have become widely accepted among younger generations (social media, collaborative economy, online gaming, etc.), which paves the way for digital asset transactions.
- Digital asset enthusiasts form a diverse community, which can create a strong sense of belonging among its participants.
- Organisations that engage with digital assets, often start-ups, apply methods like social media marketing, community building, gamification, integration of educational content, etc. that are effective with younger generations.

Disruptions in the Financial Market

Blockchain technology and digital asset applications have brought extensive technological and business innovations to the financial market. In this context, new market participants have evolved; they introduce exciting new products and services. Crypto banks, digital asset exchanges and brokers, liquidity providers, technology and software providers, and other players have become part of a new digital asset ecosystem.

Traditional financial institutions have started to react and extend their capabilities and offerings. Certain traditional banks now offer crypto currency trading and custody services. Offerings are still limited in scope as they mostly contain passive offerings for some common crypto currencies (without active advice). Services like staking or yield farming have not been adopted by many institutions yet, mostly because of increased complexity and regulatory uncertainties. Some traditional financial institutions do actively seek innovative use cases to leverage blockchain technology for the processing of transactions between financial institutions.

It can clearly be observed that the offerings of the different players in the financial market increasingly converge and overlap. Traditional institutions strive to close the technology gap in order to be able to offer, safekeep, trade and transfer digital assets. Digital asset providers strive to close the security and trust gap, for example by obtaining a regulated status or by extending their offering to traditional assets – for example to accept traditional assets as collateral to grant credit on digital assets.



The digital asset market has been and will continue to be evolving rapidly and possibly turbulent at times. The period with events of insolvencies of digital asset businesses in 2022 has demonstrated this undeniably.

Opportunities for Financial Institutions

With digital assets, opportunities arise for financial institutions to increase assets under management, to gain additional income from digital asset products and services and to attract new client segments. Existing clients might be interested in using digital asset services, which will generate certain benefits. To reach new clients, institutions should consider how the needs of the targeted segments can be met. Is it for example sufficient to incorporate crypto currency trading in existing channels like e-banking, or is it necessary to explore other ways to offer digital asset products and services? As indicated, young, tech-savvy individuals often access digital assets directly by using digital asset exchanges or self-custody solutions. Such individuals will only use financial institutions as providers if they provide a better experience compared to accessing and managing digital assets directly.

The opportunities for financial institutions however reach beyond the offering of digital asset products and service to (end) clients. The blockchain technology bears the potential of revolutionizing the processing of transactions between financial institutions.

Settlement processes for traditional assets, for example, require large efforts and operational diligence to mitigate risks, namely counterparty risks. With digital assets, settlement can take place (nearly) real-time and in an automated manner. The resulting efficiency gains (capital efficiency, resource efficiency) and risk reduction are expected to be significant.

There are a number of barriers and challenges with entering the digital asset market. This includes regulatory uncertainty – although relevant regulators have created a solid regulatory foundation (DLT act in Switzerland, MiCAR in Europe, regulation in Singapore) there are still areas with uncertainties, for example related to staking services. Financial institutions need to be prepared for a changing regulatory environment.

The offering and management of digital assets requires dedicated technology (namely for the safekeeping of private keys, the connection to blockchains and trading venues, etc.). The introduction of such systems and their integration with existing banking infrastructure is highly complex. Moreover, it is essential to build up capabilities beyond technology. This includes the coverage of digital assets in the organizations' product governance and risk management frameworks, the consideration of potential impact for finance (e.g. capital treatment), operational capabilities, the education of all relevant areas in the organization and the development of communication and educational materials for clients.



Traditional financial institutions are well positioned to benefit from the potential of digital assets as they represent trust (regulatory status, robust ownership structure, risk management capabilities, etc.), own strong brands and can build on existing client basis. Considering the dynamics of the digital asset market, it is meaningful to assess the positioning of a financial institution regarding digital assets actively to avoid disadvantages in the competitive market.

Key Considerations

Several financial institutions already include digital assets as part of their offering, and others are in the process of implementation. While such implementation involves many elements that apply for other transformation projects as well, institutions must mind that adding digital assets to their offering means building up a new, evolving business segment. This requires the establishment of comprehensive capabilities – this can be approached gradually.

Financial institutions are suggested to start with a specific use case, for example the trading of crypto currencies or a concrete tokenization case. The focus of such a starting point is mostly about gaining experience in the field of digital assets and not about achieving a projected business case. Ideally, an initial use case involves clients and/or business partners, and it exemplifies real business value.

It may be beneficial that initial implementations are conducted in collaboration with partners that provide specialized technologies, services, or expertise.

Considerations about the offering will need to be made to reach a well-balanced products and services mix – always with a focus to meet the needs of the targeted client population.

Relevant questions may be: Should direct investments in digital assets be offered, or rather indirect investments through funds or structured products that base on digital assets? Should digital assets be offered passively, or should active advice be provided? Is the scope limited to crypto currencies or should other products, like credit, staking, yield farming be offered as well? Can existing distribution channels be leveraged for digital assets or should new ways of client interactions be explored? Such questions need to be evaluated periodically while scaling the digital asset offering. Scaling should include the assessment which capabilities should be established internally, and which ones can be outsourced.

Building a strong positioning with regards to digital assets and refining it continuously will be crucial for financial institutions that want to engage in this growing market.

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