21 YEARS OPALESQUE

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Small Managers - BIG ALPHA - Report 99

VanEck Digital Assets Strategy's risk-reward-based approach pays off

B. G., Opalesque Geneva:

VanEck, a large ETF house, has a firm hold on the digital assets space. Nowadays, the firm manages $1.89bn in digital assets through 19 strategies. One of its products is Digital Assets Alpha Strategy (DAA), a long-biased liquid token strategy that aims to generate alpha through token selection and risk management.

Pranav Kanade is the portfolio manager. Before joining VanEck two years ago, he served as a credit portfolio manager at Millennium Management and head of research for liquid credit investing at Angelo, Gordon & Co. He will speak at the **Small Managers - Big Alpha Episode 15** webinar on Tuesday 9 July (details below).

VanEck, a family-owned investment management firm headquartered in New York and founded in 1955, manages about $101.9bn (as of March 2024) through ETFs, mutual funds, institutional funds, SMAs and UCITS. It pioneered investing in foreign growth stocks and gold. The firm made multiple attempts, since 2021, to launch a spot Bitcoin ETF, until the SEC authorised it, along with 10 other applicants, in January this year.

VanEck Digital Assets Alpha Strategy

Within the digital asset fund universe, those strategies opting for a liquid and active strategy can choose between arbitrage, liquidity provision, trading and fundamental. DAA is using the latter, with a long-biased edge.

Fundamental analysis involves examining a company's financial statements and broader economic indicators to uncover a security's intrinsic value. VanEck first identifies projects through qualitative analysis, then identifies the key KPIs (key performance indicators) that drive the token of the security value, and makes assumptions and forecasts those KPIs to build a DCF (discounted cash flow) model. The manager then determines the valuation and decides on the positioning.

The Strategy owns and actively manages 10 to 30 digital asset tokens and securities. It takes a risk-reward-based approach, with the flexibility to adjust for adverse market conditions. The net long exposure is 80-100% (but could be as low as 35-50%). The size limit for individual positions is 10% of NAV. The manager employs quantifiable downside hedging via selling to go into cash or options.

According to VanEck, the investible universe includes more than 24,000 tokens and roughly $2.67tln in market cap. The universe of digital asset securities includes 20 publicly traded global equities and $147bn in total market cap. The Strategy takes from both universes through a thesis-driven approach, a focus on cash flow and valuations, and positioning dictated by the macro environment.

The token is not the product, it's the accelerant for a great product, according to VanEck.

Unlike equity investments which offer ownership and voting rights in a company, token investments, especially utility tokens, focus on specific utilities within a network and might not grant ownership or voting power. Token investments have gained traction with the rise of blockchain technology and decentralised finance (DeFi), explains Wowsummit.net. Tokens can represent various digital assets, including cryptocurrencies, utility tokens, and security tokens.

The manager anticipates the $2.82tln global digital asset market to take a share from the $239tln global bond and equity market in the coming decade. Furthermore, they believe that less than 1% of the liquid token projects will generate over 99% of the returns. In other words, “most tokens will be worth nothing and will lose value but a small subset will accumulate a lot of value,” says Pranav Kanade.

The five key investible themes include:

1. Core infrastructure (of blockchains, bridges and oracles…); according to VanEck, it is “the connective tissue between millions of developers and billions of users.”

2. DeFi building blocks (including decentralised exchanges (e.g. Uniswap), liquid staking platforms (e.g. Lido), and more); “the core primitives forming the foundation of the on-chain economy.”

3. Upgrading TradFi Rails: “Building the familiar TradFi experience on top of crypto rails represents an opportunity to upgrade the financial system.”

4. Web3 & the Creator Economy, “adding an open and composable layer to the web2 internet & unlocking frictionless new experiences”.

5. Decentralised physical infra (DePIN), “a new paradigm in bootstrapping and maintaining physical networks and competing against incumbent networks.” Opportunities include wireless networks (e.g. Helium), mapping and road analytics (e.g. Hivemapper), and more.

Two investment examples are Lido, a liquid staking solution for Ethereum and other proof of stake chains, and Render Network, which offers a decentralised alternative to cloud computing services that have become prohibitively expensive.

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