IMpact: An investment management podcast series

Episode 10: The transformation of investable assets: Unlocking new investment opportunities in the age of digital innovation

Host:

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Guest:

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Reese Blair: *Hello, everyone. I'm Reese Blair, your host of IMpact, the new investment management podcast series from Deloitte. IMpact brings you hot takes and fresh perspectives from top experts in the industry. Whether we're discussing issues like regulation, recession, or resiliency, we'll take a deep dive into the latest news, trends, and challenges facing investment management professionals. Our mission is to help you focus on investing in what matters. So, tune in, learn something new, and walk away with insights that will help you make an impact on the IM industry and the world around you.*

Welcome back to the IMpact podcast, where we explore the cutting edge of investment management and all the things that are related to this sector. Today, we're diving into a topic that sits at the intersection of innovation and institutional resistance—the transformation of what we consider investible assets in today's digital age.

I am thrilled to welcome Sandy Kaul, a true visionary who has shaped how we think about economic frameworks in financial services. Sandy has spent decades not just observing, but actively theorizing how technological advances reshape our industry's landscape, and timing couldn't be better for this conversation as we're witnessing a fascinating paradox.

While technology is opening doors to entirely new asset classes from intellectual property portfolios to tokenized investments, our industry often finds itself caught between innovation and institutional caution.

Following up on some of our recent conversations around the democratization in investment management, we'll explore how these emerging asset classes might expand beyond institutional walls to reach a broader investor base.

Sandy brings a unique perspective on both the opportunities and challenges this shift presents. From valuation methodologies for intangible assets to the regulatory considerations of wider market access, Sandy, welcome to IMpact.

Sandy Kaul: Thank you so much, Reese. I'm so excited to be here.

Reese Blair: And we are particularly excited for our listeners to hear your thoughts on how we can balance innovation with prudence in this rapidly evolving landscape. So, appreciate your time today.

Sandy Kaul: Great. Let's go.

Reese Blair: Excellent. Sandy, you've spent … well, actually, before we get into the first question, for our audience and for the benefit of our listeners, why don't you share a little bit about your background and sort of what's new and interesting in your world?

Sandy Kaul: Yeah, so I have been in the investment markets in multiple capacities, really, for almost 40 years now. Starting off as a research analyst, then becoming a portfolio manager, then really becoming fascinated with how emerging technologies were changing the delivery model, right when the internet was coming out in the late 1990s. Then I started doing consulting to bring those new technologies into the service model of the industry.

Did work for many years, helping to really shape the hedge fund and the alternative space, the new service models that were coming as we started to incorporate more sophisticated investment techniques into the industry, and then really started writing about the future of the industry in about 2004, 2005. And pretty consistently since then, Reese, every year I've been doing a big survey, typically covering about 50 trillion assets under management and talking to just some of the smartest folks around the world around how they see the industry unfolding and the future unfolding.

And then really thinking about what that means for our own models and our own industry and helping clients, such as Franklin Templeton where I work now, really think about what the future's going to look like and get ready for it. So, I've been working in this space now for a long time. I've seen lots of change myself, and I'm super excited about where we are as an industry and what's coming up ahead of us.

Reese Blair: Well, that is the perfect preamble and tee up for my first question, Sandy. You've obviously, as you've indicated, spent significant time throughout your career developing both thoughtware around various economic frameworks, but also the technological advances within financial services. And so, with that, and everything that you're excited about, as you think broadly across some of the contributions you've made, I'm curious to hear what patterns or trends you've seen over the years.

Sandy Kaul: This is something that I've really spent a lot of time, Reese, thinking about, and what we've really seen is there is this repeating pattern that we see in the industry, which is that new technologies come to the forefront. Initially there's a lot of resistance to using these technologies because they feel very different than what the industry has been used to doing and feels comfortable doing.

But then over time, they begin to get adoption. And as we start to adopt them, they really change our service and our delivery model, and they start to open up new pathways and new behaviors, and then we start to move into a period where the whole model has shifted.

And we've really identified, up until now, three prior phases of this. It really started back in the late 1960s with the advent of commercial computers. Computers had been very much limited to the military and to academia prior to the late 1960s, but that's when commercial adoption of computers really began.

And so, this whole age of automation kicked in, and that really completely foundationally changed our industry and many industries. About 20 years later, that shifted as all the network technologies and all the cryptographic technologies that had been kept as military secrets until the 1970s started being utilized, and we entered an age of digitalization.

And then we're at the tail end of the third wave of what we call virtualization, as we've started to take all of these digital platforms we've built and allow people to directly participate with the platforms.

So, we've all been living in the platform economy for the last, I'd say, 15 to 20 years, and we're coming to the end of this cycle as we start to see the next cycle, which is really about distribution and being able to use protocols. That's what we're coming to as the next wave of evolution. But we've been through these patterns already, and we're entering this new pattern—kind of as we speak—so, it's a very exciting time.

Reese Blair: Indeed. And what this really calls to the fore is the fact that the only thing that remains constant in this universe is change, and you've highlighted that. You've obviously had a front-row seat to all of that change, and with the change, there's always the fear of the unknown.

You started talking about the move from digitalization to virtualization, but let's maybe not get too far ahead of ourselves, Sandy! [laughs] Let's maybe come back just a little bit before we get to the world of virtualization. Let's maybe talk about digitization, but maybe let's talk about it with this concept of fear in the background.

So, taking this concept of fear and the role that it's had when we think about all these advancements that we've had over the decades in our industry, what are some examples that you can maybe bring to the audience's attention, and are we seeing some of that fear creep back in with, again, not as far as virtualization, but maybe with digitization?

Sandy Kaul: When the internet first emerged, there was a lot of people that became very concerned with this idea that individuals could start to have access to information that might be seen as giving them potential to act against their own self-interest.

There was a lot of pushback against this idea of individuals being able to enter their own orders, to make their own decisions about investing, to directly access any types of funds or securities. You saw this same resistance a third time when we started to see cloud technologies begin to be adopted. With the cloud, you had a lot of financial institutions really aggressively saying that they would never use cloud because they had to keep their data secure, and they didn't believe that the security mechanisms around cloud technologies would be sufficient, and therefore they weren't ever going to use them. And we all know today, basically every organization in the world has a tremendous reliance upon cloud technologies to run their day-to-day operations.

So, you've seen this same pattern over and over, this resistance to using new technologies. We saw it in the early days of AI, everything. So, I think that this is a pattern that is your institutional resistance. I really liked how you phrased that. There is this resistance to new technology and change.

Reese Blair: Well stated, Sandy. I want to pivot now. You teased out the notion of the evolution from a platform economy to now this protocol economy. Some of our users may have never heard that term before, and so I'm hoping that you could potentially elaborate a little bit more on what that looks like.

Sandy Kaul: Sure. So, let's just start with the platform economy, because I think that it's become so commonplace that sometimes we don't remember how revolutionary this was. But when internet technologies first came out, what we saw was you would go to a website, and a website was static. It had pages that somebody had programmed in pretty much every word on that page and any pictures that were on the page were static.

There was no such thing as video on a page. It was a very flat experience. We then began to really see a rapid enhancement in how we could interact over the web. And this was because we started to have better broadband, better phone technology, better connectivity. We started to have better programming, more lightweight graphics, more video, and finally we got to the point where we could actually interact with each other over the web.

We started to be able to publish content, we started to be able to consume other people's content, and we really started to move into a world where the web became two ways. The user could do things on the web with other people on the web. The seller could do things with other buyers on the web. We started to really be able to use platforms to do things that we had never been able to do before.

These are all aspects of the platform economy where this platform sits there as a service provider and the service that they're providing is hooking up buyers and sellers, or in the case of social media, the service that they're providing is hooking up users who want to interact with each other.

And so, this is the platform economy: This idea that we are using networks and that there are platforms that are facilitating those networks and that we interact via these platforms, and that this has become so much a part of our day-to-day life that it's hard to remember that this was not a model that anyone had used as recently as 15 years ago.

So if that was the platform economy, we're starting to see some of the limitations of that platform economy today, because the platforms that sit at the middle of it have become very, very powerful.

And it's hard because these platforms are providing all of these services and they have to cover the costs of all of these services with the fees that they charge. So, there's this natural tension that's starting to become obvious in the platform economy, where the costs of running the platform and the need to take fees from portions of the activity that takes place on the platforms, that is coming into conflict with the ability of users to want to use the platforms.

And this is what we really see providing the opportunity to progress the model. And so, let me explain first what a protocol is, because then I think it will make much more sense to people. So, now let's talk about what we mean by the protocol economy. Let's start first—just a real quick explanation of what a protocol is, because it sounds like a kind of scary word, but we use protocols all the time, every day.

In fact, getting onto the web is using a protocol. Every time we type in a webpage address, we see in front of it that little "HTTP"—that's a protocol! That's a communication protocol that allows us to call up websites. And everywhere in the world, it doesn't matter where you are, by typing in that HTTP, your computer is getting the instruction from the code to call up a website. And so we use protocols every day.

And what we're going to be able to do with the protocol economy is that a lot of the functions that we rely upon a platform to provide today, which is a proprietary platform—and they do this as a proprietary service and charge us for it—what we're going to be able to do is individuals are going to be able to initiate those same functions, but they're going to be able to initiate those functions using a new kind of instruction, which is a protocol on the web.

So, I'm going to call for my car to get my car to take me to dinner tonight,. The way I'm going to call my car is going to be via a transportation protocol that I can call up, that my web browser knows is going to be looking for available cars in the area.

And I'm going to do this via an app, and I'm not going to have to pay the app for being able to use the protocol. I might just pay the app for the actual ride. So, it's going to be a more effective way, from a cost perspective, for people to be able to share peer-to-peer activities, services, goods, content. But it's all going to feel very similar to the platform economy, but it's going to be enabled in a very different way.

Reese Blair: Fascinating, fascinating, fascinating, Sandy. So, we're on the Investment Management Impact podcast, and as you were talking about the almost limitless applications for a protocol economy, I couldn't help but think, "Where's the intersection within the investment management industry?" What does this mean for generating ideas for investing and serving clients in this industry?

Sandy Kaul: So, this is where it gets so exciting, Reese, because you're going to be able to do things using these protocols that we've never been able to do before.

That's another way we're going to see it. And then we're going to be able to take our own assets and begin to tokenize them using these protocols because they're creating these, what we call smart contracts, which are basically templates where we just fill in a few details. It's like filling in a form, and by filling in those few details, it creates the code and creates a new asset.

So, I may have equity in my home, and I may want to actually sell part of the equity in my home, and I can go on and I'll be able to create a smart contract that would allow me to actually put my equity of my home into an investment contract that I could sell to people.

So, this is all going to be enabled directly. People are going to be able to go in and directly begin to get these benefits, find these new income sources, find and use these new rewards and benefits, and be able to really think about what assets they have and how to create liquidity around them and create more revenue from sharing their own assets with people.

Reese Blair: You know, Sandy, the intersection, well, multiple intersections as I think about Internet of Things, as you're pulling up to a particular location, as I think about tokens and the rage that was NFTs, that was out there for a while—I mean, there's so many fascinating elements of what you're describing about it. I feel like I'm going to overuse that word fascinating because everything that you're saying is literally blowing my mind.

And the one thing though I'm wondering though is, in our world, cash is king for the most part—and queen—and at the end of the day, there's usually, even though it's electronic, there's still something that physically we know exists. And some of these asset classes that you're talking about, as we think about the evolution of where this protocol economy is going, some of it feels very intangible to me as you're sort of laying this out here.

And so, I'm wondering how would an investor feel value—or even ownership? I know I own equity in my home, but now when somebody else buys a piece of that equity, how does ownership—what does that look like? And even we go down the path of, like you said, platform economy, IP, internet. There's so many elements of this that I'm just wondering how do we think about the intangible nature of all of this?

Sandy Kaul: How does it all really feel like it's real, right? Today, if I'm looking at my bank account, on my bank app, I see some numbers in my bank account, and those numbers represent the amount of money that I should be entitled

to, and I believe that I am entitled to them because the bank is backing it up, the federal government is backing it up, but I don't actually see a pile of cash in an account.

I am believing that that cash is there because I can interact with it, I can instruct it, I can pay bills with it, I can transfer it to my friend. There's things that I can do with that cash; I control it. In essence, it's just a digital asset because I'm just looking at a representation of my cash that's sitting in something that has been arbitrarily assigned to me as an account.

And I trust that the bank underneath it is really going to be doing everything it should be doing to protect me and my money and allocating and administering my money as I desire. So, now think about instead of an account that the bank has, I'm going to have a wallet that I control the keys to, I control the ability to open and close that wallet, and instead of me having to go to the bank to see my money, the bank is going to send my money to my wallet.

So, if I am buying an asset—like I have bought a portion of your home equity, Reese—what I will do is I will see a token that represents my ownership of that portion of your home equity, that token will be deposited into my wallet, and I will be able to open my wallet and see this investment contract. Because the token is an investment contract between you and me, where I am now owning a portion of this property's home equity.

And that contract is something that I will be able to see the terms on. I'm not going to be entitled to telling you what color you need to paint the walls or whether you need to upgrade the appliances; I'm simply going to be entitled to get passive income when you sell your home. I will get X percentage of the value when you sell your home, because that is what owning a piece of your home equity is going to entitle me to.

So, I could see the contract that's embedded in that token, and I will be able to see it in my own wallet to know that I have these rights, and that wallet and that token are going to be held on a blockchain where there are thousands of different nodes who are verifying transactions and making sure that there is no alteration of transactions happening, and making sure that every transaction is a valid transaction and that there can be no fraud. So, it's a much more secure system, actually.

Today, I have to put a tremendous amount of trust in the bank, in the example I was using, but in the future, I am going to be able to go in and see and test the security and know that I have ownership of all these assets because it's going to be in a location that I can really get and see across the entire network.

So, I might have a bank account today with three or four different banks, and I personally have to kind of add up all that money to understand what I own. In the future, each of those banks will have a copy of what I hold with them, but the actual assets are likely to sit in a wallet that I control.

And that's what's going to give us, I think, the confidence in the system: the transparency to be able to see the asset in my wallet, the accessibility to be able to open and look at the contracts that that token provides and the rights and the contracts guarantees that I'm given, and the ability for me to instruct and move assets in that wallet just like I would instruct or move assets in a bank account today.

Reese Blair: And Sandy, just for my own education and for my awareness, is there a key—similar to what you think about, like folks who unfortunately lost their digital key to open their wallet and access their bitcoin—is there a key that would be linked to this digital wallet that, let's just say the unspeakable happens and you lose that key—are you now saying that you who've bought my piece of my equity in my home, you now can't find the key anymore. So, you've now lost that asset. Is that what happens? [laughs]

Sandy Kaul: No, that was definitely a risk, Reese! I know that's a scary concept. That was a risk when this technology was just beginning to be developed. What has happened since is that we have developed much more sophisticated

technologies, and just like today, we trust a custodial bank to hold our securities, or we trust a deposit bank that we've put assets into a safe deposit box.

We are going to trust—we're going to have an intermediary whose job in the future might not be administering the assets, but it's going to be administering the key so that there is always a secure copy of my key. And because of the way that the security on these new cryptographically enabled keys work, no one can actually use the key without me as the owner of the key authenticating it in some way.

So, what's going to happen is I'm not going to have to remember my key, but no one is going to be able to use that key unless I authorize it. And authorizing it could take many different forms, authorizing it could be biometrics, so fingerprints or voiceprints; it could be I own a special identity token, and unless I give you my identity token, you're not allowed to open the wallet.

There's different methodologies that people are exploring, but this whole concept from the early days of the internet, of the early days of blockchain where people talked about, "Oh, I've lost my zip drive with my key on it, and I can't access my $500 million," those days aren't real. That is no longer likely to be the way that this works.

In fact, the commercialization of all of these protocol economy models is going to be completely reliant upon it being as simple and as safe as it is today. No one's going to want to go backwards and have to do things in a more difficult and less safe way. We only want to move forward and have ease of use and trust and that's where we're moving, and that's why the advances in the technology are quickly taking us to this new point in time.

Reese Blair: Got it. So, I was going to ask a question about what some of the challenges are, but it seems as though the technology is evolving as well, and access and safety and the immutable nature of the asset. I mean, all of the things that you would hope to see in a blockchain asset and how would you gain access to that asset, sounds like you've thought about that and there's consideration, quite frankly, with regards to that.

So, I want to start to close out the conversation, Sandy, and as I think about it, I almost want to go back to where we started: this concept of fear. This concept that the more things change, the more they stay the same, but it's also the thing that is also constant, this fact of constant change and with that change there's fear.

And so, I would imagine that some of these investment opportunities that we're discussing are, for some people, radically different than what investors are traditionally used to and so, fear would probably creep in. And so, I'm curious to get your perspective, what you're seeing around the appetite for some of these new opportunities, is there any shifts that are happening in investor preferences?

And then the other side of that would be sort of what does this mean in terms of being available back to that democratization process. Like the fact that things are becoming more available to the masses. What's the appetite look like and are there potential for this to be made available to a broader or larger investor pool?

Sandy Kaul: Yeah, absolutely. So, our belief, Reese, is that the pathway to this is going to go through things that make individuals excited. So, you talked a little bit earlier about the potential of being able to own intellectual property and share in the royalties that come from intellectual property.

This idea of fandom, this idea of cultural assets, things that resonate and would make people feel like, "Wow, that's an exciting part of my life now." That's where we think these investments are going to start.

It's going to start around art collectors being able to own pieces of paintings or sculptures that literally are far outside their price bands to be able to own individually. But being able to own that collectively through tokens and having even a portion of an ownership of a famous painting that you've always loved, or a collection that you really admire, that's going to be a new path to investing.

Having access to music and to artists that matter to people, having access to sports events and teams and sports stars. We're seeing a lot of this happening around soccer teams, particularly in Europe, where each player kind of owns their own IP rights, rather than the team owning the rights. These are all areas that we think this is going to begin.

And so, the pathway is really going to be through the common man, because we think that the first sets of successful investments are going to be those that excite people to own them, and that create that demand and that willingness to put themselves out there to try something new.

Reese Blair: Sandy, it's not hyperbole to say that I could talk to you for hours. [laughs] I always enjoy our conversations, and every time I speak to you, I'm excited. You get my mind racing and so, before we have this go on for much longer, I think we'll bring this plane in for a landing. And with that insight, I should say, about the convergence of traditional and digital asset management, I think we'll wrap up today's episode.

So, Sandy, look, your perspectives on how fear can either paralyze or propel innovation has been incredibly illuminating. I particularly appreciate your practical framework for thinking about intangible assets.

To our listeners, look, whether you're exploring tokenization, developing IP valuation models, or considering how to broaden your investor base, remember that today's challenges and democratizing complex investments are tomorrow's opportunities for industry leadership.

Once again, Sandy, I just want to thank you for sharing your wisdom. Thank you for challenging us to think differently about the future of investment management. As the industry continues to evolve, these conversations become increasingly crucial for all of us.

So, with that, I want to thank you all for tuning in to the IMpact podcast, where we look to not just spend time together but invest time wisely with the best and the brightest in our industry. Sandy, you are one of them. Thank you for facilitating a return on the investment of our listeners time today. Until we meet again, keep questioning, keep learning, and of course, keep making an impact.

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