



## Digital tokens backed by gold

### Introduction

Banking giant HSBC has just embarked on the tokenisation of gold, enabling the precious metal to be invested and traded digitally.

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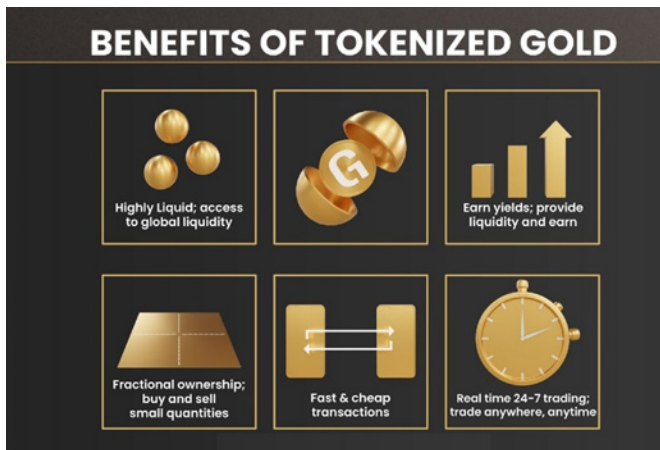
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HSBC has launched a token that represents a pre-determined fixed quantity of physical gold, providing a digital means of accessing and trading the precious metal.

HSBC's tokenisation of gold is in and of itself a minor revolution. Not just for the British bank, but for the financial industry as a whole. Indeed, the move is part of a wider trend towards digital transformation across the industry. By tokenising gold, HSBC is bridging the gap between traditional and digital finance. This initiative could potentially revolutionise the way gold is managed, traded and integrated into financial portfolios.

HSBC is not the first institution to attempt this experiment, as the blockchain platform "Tether" has long offered Tether Gold (XAUt), its digital token backed by physical gold, with a market capitalisation in excess of \$550 million. Pax Gold (PAXG) is a gold-backed crypto-currency issued by Paxos, a regulated blockchain infrastructure. The Paxos gold token has a capitalisation of \$435 million. Unlike Tether Gold and Pax Gold, HSBC's token is currently only available to the bank's customers.

The implications of gold tokenisation are considerable for investors and the banking sector as a whole.



Source: Aurus.io

For investors, gold tokenisation reduces barriers to entry (via fractionalisation) and increases market liquidity, opening up new opportunities for portfolio diversification.

Tokenisation also makes it possible to generate returns on physical gold.

## Gold-Backed PAXG Token Spikes to \$2.9K Amid Geopolitical Tensions

By Omkar Godbole | Apr 14, 2024 at 7:46 p.m. | Updated Apr 15, 2024 at 6:18 a.m.



Source: Yahoo! Finance

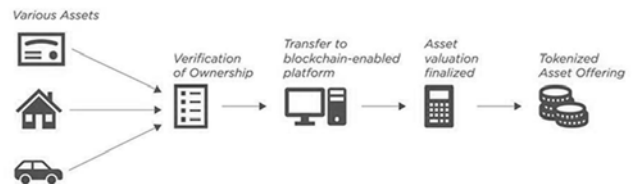
Above all, it enables gold to be traded on a 24/7 basis. As a reminder, during the Iranian drone attack on Israel, the digital gold tokens already available on the market (e.g., Tether Gold and Pax Gold) had reached a value equivalent to \$2.900 per ounce of gold by Saturday night. Physical gold prices and the prices of gold ETFs had not fluctuated, since traditional stock exchanges are, of course, closed at weekends.

For the banking sector, this means a step forward in the adoption of blockchain technology and the creation of new financial products. These developments could very well reshape the global financial market, as tokenised assets enable transparent global transactions, with reduced costs and increased efficiency.

## Understanding tokenisation

Tokenisation is the process of converting real assets into digital representations on a blockchain. This process enables assets to be exchanged, transferred, and managed digitally. These tokens constitute a digital representation of ownership, with each token corresponding to a specific asset, whether gold, real estate or other commodities.

### ASSET TOKENIZATION PROCESS

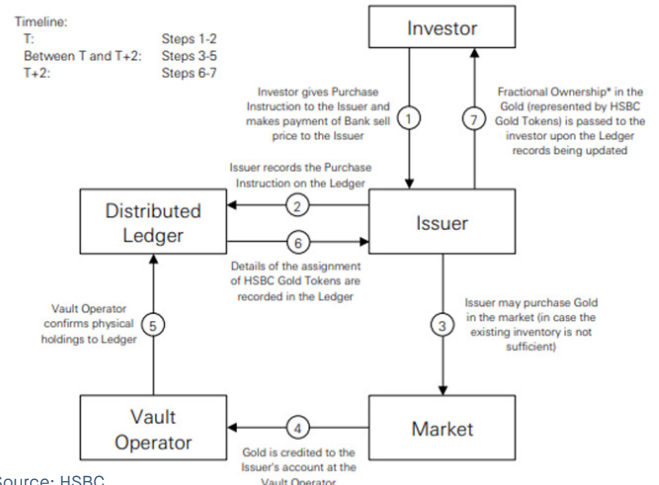


Source: HSBC

We're talking about fractional ownership here, which means that a gold bar represented by HSBC gold tokens can be held simultaneously by more than one investor. In this case, the unit of exchange is the troy ounce, with each HSBC gold token representing the fractional ownership record of 0.001 troy ounces, or approximately 0.03 grams.

Blockchain technology enables this tokenisation process. It is essentially a decentralised digital ledger that securely records transactions. These blockchains run on a network of computers, ensuring that no single entity controls the data. The blockchain is an ideal platform for managing tokenised assets because of its decentralised structure, which enables transactions to be recorded transparently and immutably. For HSBC, all gold tokens will be recorded on an internal private ledger using distributed ledger technology operated by the platform operator (also HSBC).

### Diagram 1 – Settlement of a Purchase Instruction



Source: HSBC

Tokenisation offers several key advantages, the most obvious of them is liquidity. Assets such as gold, real estate and other traditionally illiquid assets can now be traded more quickly and openly. Thanks to tokenisation, assets can be represented by millions or billions of digital tokens, making it easier for investors to buy and sell these assets on a variety of easily accessible exchanges, thereby increasing market liquidity. This also broadens the pool of potential buyers and eliminates the need for costly transactional intermediaries.

Another key advantage is accessibility. Due to regulatory or financial restrictions, many assets with the greatest upside potential are not accessible to individual investors. Investing in high-end art, collecting sports cars that appreciate in value, or buying and leasing apartment buildings are just a few examples of investments with high performance potential but difficult access. Tokenisation makes this type of investment accessible to a wide audience.

In addition, a common problem with high-value assets is the lack of easily accessible and reliable data on returns, ownership, sale, and other important criteria that investors need to know in order to make informed financial decisions. Given that many blockchains are public, tokenisation has the advantage of enabling all this past information to be traced. For some, this is even the most attractive attribute of blockchain technology. A recent proponent of the use of blockchain technology is independent presidential candidate Robert F. Kennedy Jr. who recently declared, "I'm going to put the entire budget of the United States on blockchain so that every American - every American - can look at every line item in the entire budget at any time, 24 hours a day." Following the logic of the "smart contract", tokenisation allows users to view an asset's ownership history (in addition to past performance or returns).

### HSBC's bet on digital assets

HSBC's interest in digital transformation is not new, as HSBC has already publicly recognised the potential of digital assets and blockchain technology. The bank has regularly invested in projects aimed at using blockchain that can revolutionise financial services such as international trade finance and securities transactions.

With this strategic step forward, the bank aims to position itself at the forefront of digital innovation, diversifying its portfolio of financial products and simultaneously creating seamless access to gold trading for its customers.

Other major banks are also exploring the possibilities offered by digital assets. For example, JP Morgan launched its JPM Coin in 2019, which facilitates cross-border payments using blockchain technology.

These initiatives are representative of the industry's recognition of blockchain's ability to streamline traditional financial systems by making them more efficient and accessible. Asset management giant BlackRock is another industry leader that has recently been in the news about tokenisation. In March, BlackRock unveiled a new real-world asset (RWA) tokenisation fund, called BUIDL, on the Ethereum network. BlackRock's BUIDL has become the largest tokenised cash fund with over \$375 million in assets under management, surpassing Franklin Templeton's OnChain U.S. Government Money Fund.

### Gold tokenisation

Gold tokenisation involves a multi-stage process that combines technology and finance. It starts with the supply and storage of gold. HSBC ensures that physical gold is secured in its vaults in England and Wales, with each unit of gold having a corresponding digital token representing ownership.

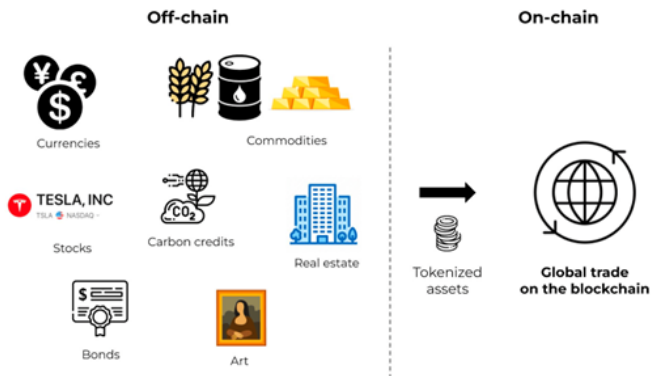
Given the newness of this industry, regulatory considerations are crucial when tokenising gold. The financial sector must ensure compliance with constantly evolving global regulations, including anti-money laundering (AML) and know-your-customer (KYC) requirements. These measures help prevent illicit activities and ensure the legitimacy of tokenised gold markets. It also means that regulators are responsible for creating frameworks that take into account the specific aspects of blockchain and digital assets, striking the right balance between innovation and investor and market protection.

Market acceptance is one of the main obstacles to the mass adoption of digital assets. Despite the growing popularity of digital assets, scepticism remains high among investors and traditional markets. Surveys by the Pew Research Center show that 75% of Americans who have heard of cryptocurrencies lack confidence in their security and reliability, with 39% saying they don't trust them at all. At the other end of the spectrum, only 6% said they were very/extremely confident in the reliability and security of cryptocurrencies. To overcome this, HSBC needs to build confidence in its tokenised gold offering and demonstrate its legitimacy and value to potential investors. These efforts will probably have to include educational initiatives to inform customers about the benefits of tokenisation and how the technology works.

Technical issues are another potential obstacle. As blockchain technology is still evolving, scaling its infrastructure while maintaining security is no mean feat. HSBC needs to ensure that its tokenised gold offering is secure, reliable and can handle growing demand without compromising performance.

## Conclusion

Tokenised assets are set to play an important role in global finance, extending beyond gold to encompass a variety of asset classes, with some even predicting a future in which all stocks, bonds, funds and real assets are tokenised. Major banks and financial institutions are playing a crucial role in shaping the future of tokenised assets. As institutions increasingly embrace blockchain technology and integrate it into their offerings, they bring stability to this emerging market and, above all, legitimacy. What's more, their involvement is helping to establish regulatory frameworks and industry standards, thereby guaranteeing the security and reliability of tokenised assets.



Source: Halborn

## For further information

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