



DIGITAL
ASSET
RESEARCH



DAR In Conversation: Q&A with Kyle Downey

Our CEO Doug Schwenk had the chance to speak with Kyle Downey, CEO & Co-Founder of Cloudwall, to ask a few questions about **the risk management of digital assets**.

Click to watch video highlights or scroll down to read the full transcript.

How does risk management for digital assets differ from traditional assets and TradFi?

For traditional key portfolio financial risks, we think about a four-quadrant framework: market risk, liquidity risk, operational risk, and credit risk. In a crypto portfolio, the weightings of those four different quadrants differ. There tends to be a lot of emphasis on operational risk and even more emphasis on liquidity risk.

TradFi's systems are much more mature. There's so much that's been built over time that there's a presumption of good functioning. The same type of infrastructure and safe functioning of said infrastructure doesn't exist in the same way in the crypto space. Crypto is a lot smaller and tends toward Black Swan events. Additionally, you don't see the same type of frequency and intensity in traditional finance. It exists, but often there isn't as much thought put into it.

What are the most common types of risk you have helped clients identify?

We commonly help clients identify risks in the derivatives space. We provide an options and analytics suite, with insights into areas like the term structure of risk. Clients can also break down risks like counterparty risk by factors including self-custody exposure, institutional custodian exposure, and hot wallet exposure.

We utilize models that break risk down into style factors. In combination with a stress-testing tool, we use these models to forecast potential changes from different shocks to those factors. These insights help to quantify the potential effects on a portfolio.

What does digital asset portfolio stress testing look like?

You can stress test a digital asset portfolio based on token returns or factor returns. We focus on both historical and hypothetical scenarios. Clients can look at correlated or non-correlated events to flesh out all these different combinations of how certain events will affect a portfolio. We can also provide explanations around questions like where certain risks exist in VAR models.

Where do you see digital asset risk management going in the future?

We are seeing some interesting early signs of renewed interest around institutional DeFi where the buy side trades peer-to-peer with other market participants on-chain. The evaporation of retail participation combined with institutions stepping back from DeFi has set those protocols back over the past two years. This renewed interest will create demand for more sophisticated DeFi risk management in the future.

Crypto is its own thing. It's not equity. It's not fixed income. It's not a commodity. I think of it like participatory shares in decentralized networks. While it is exposed to many different kinds of risks, ultimately people are going to be managing risk on a diverse portfolio of many types of underliers, including traditional ones. We've seen innovative funds within the past year trade across that range and struggle to deal with the diversity. Properly embracing all those different asset classes in a way that enhances the current generations of risk systems is another direction for digital asset risk management we're excited about.

A few ways to learn more:

- Visit Cloudwall's [website](#)
- Learn about Cloudwall's [Digital Asset Risk Platform](#)
- Explore Cloudwall's [Research](#)