

The ABCs of Asset Backed Cryptocurrency

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Blockchain technology has many uses in commercial real estate. This brief focuses on cryptocurrency backed by CRE as the underlying asset. The process of representing a fractional ownership interest in an asset with a blockchain digital token is called tokenization. Each digital token represents direct ownership of an asset, such as a real property, a share in a company owning real estate, an interest in a real estate investment fund, an allocation of property income, or any combination these rights. Tokenization offers issuers greater efficiency, lower costs, and access to a broader investor base for the issuers. For investors, real estate tokens may offer greater opportunities in a variety of otherwise costly property assets, greater liquidity over secondary exchanges and enhanced information transparency.

There are five basic steps in the tokenization process:

1. Identification, acquisition, and financing of a real estate asset.
2. Creation of a smart contract and compliance with applicable securities laws.
3. Selection of an exchange platform and deciding how many tokens will be issued.
4. Listing tokens on the exchange through a security token offering (STO) and advertising the offering.
5. Providing investor support and administering payments or profits.

In its [Real Estate STO Whitepaper 2021](#), Deloitte identified benefits of the adoption of an STO:

- With fractionalization, STOs can lower the high minimum investment thresholds for private real estate investments, providing greater access to a larger number of investors.
- A token can be customized to offer special features such as access or usage rights in one product.
- An exchange listed token has enhanced liquidity through secondary exchanges and can be traded 24/7 and settled within hours.
- Smart contracts, utilized for tokenization, can lower transaction costs, and automate management functions such as dividend payments, thereby increasing efficiency.
- Records on the blockchain are intended to be secure, transparent, and immutable.

While the potential of tokenization is great in CRE, it remains a nascent technology with low public awareness. Stakeholders have only just begun to develop the exchange platforms, custody services, user communities and, most importantly, political, and institutional support. Further, security regulations on the formation of an STO and on trading in secondary markets can vary significantly from jurisdiction to jurisdiction. No international regulatory framework currently exists.

Major projects using tokenization include:

- **November 2018:** Factora tokenized a luxury East Village condominium in Manhattan with 12 units and a total appraised value of \$36 million.
- **August 2019:** Smartlands closed a STO involving a £12.06 million student housing complex in Nottingham, United Kingdom.
- **February 2020:** Red Swan, in partnership with tokenization platform Polymath, tokenized over \$2.2 billion in real estate assets, representing 16 commercial properties, including mid-rise and high-rise apartments in California, New York, and Texas, as well as a 150-acre hemp farm in Ontario, Canada.
- **July 2020:** KlickOwn AG completed a €1.5 million initial bond offering for Historisches Lüneburg, located in Lüneburg, Germany, conducted exclusively via tokenization.
- **August 2020:** MountX Real Estate Capital licensed the Vertalo platform to design and launch 15+ digital real estate projects in Mexico and Canada. In November 2020, they completed the first tokenization of real estate in Mexico including two apartments for a total price of \$5.2 million Pesos.
- **September 2020:** REINNO launched a marketplace for tokenized CRE, including five offerings worth over \$237 million in aggregate available to accredited investors.
- **March 2021:** Mapletree Europe Income Trust Tokens were issued, representing an indirect ownership interest in Mapletree Europe Income Trust that holds interests in office assets in European growth cities.
- **October 2021:** MarketSpace Capital tokened \$6.5 million in equity on a 250-unit active adult living (55+) apartment building in Dallas.

While these projects are the initial ventures into real estate backed cryptocurrencies, what is the future market potential of this technology? The global real estate investment market sits at over \$10 trillion as reported in the [MSCI Real Estate Market Size Report 2021](#), which may represent the upper limit of the potential market for real estate backed tokens. However, much of the income producing real estate held worldwide is controlled by large corporations or high net worth individuals and is rarely traded. Therefore, aggregate transaction volume may be a more realistic measure of the potential for tokenization. [CBRE estimates](#) global CRE investment reached a record annual total of \$1.3 trillion in 2021, up by 55% from 2020. At this point, we do not know how quickly these transactions will be tokenized.

Matt Andelman, CEO & Co-Founder of ABC Tokens and ABC Fintech, believes that education and marketing are key to increased adoption of asset backed tokens. "If we are going to build this from scratch, why wouldn't we build it on the blockchain?" As issuers and investors begin to understand the benefits of this technology, it is likely that the real estate digitization market could be poised for exponential growth in the coming years.