Digital Asset Opportunity Index: Taking the ETF Revolution Digital

The forthcoming academic paper *Digital Asset Opportunity Index: Taking the ETF Revolution Digital* provides the theoretical framework for the PlannerDAO Digital Asset Opportunity Index. This paper introduces the Three Pillar Index methodology, which defines the criteria necessary for mass adoption of a digital asset index.

Pillar One: Broad-Market Implementation

Financial indices did not have the widespread recognition they have today prior to the advent of index funds and ETF investing. Until an investor can purchase the potential upside of an index in their own account, the price-tracking feature of an index remains theoretical and does not affect the everyday investor.

Only when an investor could match their portfolio to the rewards and risks of the S&P 500 price they saw on a ticker did indexing enter the public consciousness.

The primary limitation of recent crypto indices is the lack of solutions for an investor to purchase the index in a single transaction. Whereas an investor can buy an ETF with the ticker SPY and have an economic interest in the price movements of the S&P 500, this solution only exists in specific corners of the market for digital assets.

Pillar Two: Zero Management Fees

As the price of ETFs and index funds have decreased steadily over time, it is likely fees for digital asset indices will do the same. The leading on-chain provider of crypto indices, Index Coop, has fees on their products ranging from 95 basis points to 195 basis points.

This tradeoff of high fees for easy accessibility is easily compared to the arrival of index funds. Low fees were not the initial feature of index investing, it's primary appeal was the ease of implementation. By allowing an investor to own a complete investing strategy with a single trade, indexes as an investment strategy were born.

The arrival of ETFs and their low fees (sometimes even zero fees) made index mutual funds virtually obsolete, and digital asset investing will likely follow a similar path. Mass adoption of a cryptocurrency index will require a solution offered to the general product for zero fees above blockchain costs that cannot be avoided.

Pillar Three: Transparent Governance

Whether used as a measure of price movement, or as an investment strategy, index creators and managers must be transparent in their methodology and management. Financial indices have a long history of publishing their methodology and keeping the public aware of any changes as the index evolves.

Where many index providers fall short is transparency in how their governors are appointed. Organizations that are privately controlled may have conflicts of interest with potential investments that are under consideration by the index.

Non-profit or decentralized organizations have an easier path to eliminating conflicts, but if they are charging a fee for use of the strategy the incentive remains to add more recognizable names to the index. This would give the index increased credibility as well as introduce them to a potential partner for the marketing and distribution of their product.

The safest route to ensuring transparent governance of an index is management by a team of fiduciaries without compensation tied directly or indirectly to the underlying assets.

Building a Three Pillar Index

The remainder of this paper focuses on how to build a Three Pillar Index in the digital asset space that is specifically designed for use as an investment strategy by the end investor.

The methodology used will explain how index components can be screened to account for the first pillar of broad-market implementation. By focusing on the end-investor, index rules can be created to facilitate the index creation process.

Implementation of the resulting index will cover the second pillar of zero management fees. We explore different methods of adding a crypto index to a portfolio and determine the most efficient way for an investor to implement it.

Process for Three Pillar Digital Asset Index Adoption:

1. Sector Classification
2. Sector Weighting
3. Security Screening
4. Asset Selection
5. Index Maintenance
6. Governance