



## Decentralized Finance Is Coming

technology payments

**Summary:** Decentralized finance (DeFi) is in its early stages. So, do community financial institutions need to follow this new trend? Yes. One big bank has dipped its toe into these waters and more are likely to follow. Not only that, but also DeFi is seen as a viable funding option for SMBs and the unbanked. Here is what you should know.

The term, decentralized finance (DeFi) was first coined in August 2018 between the Ethereum developers and entrepreneurs according to coinmarketcap.com. Other terms they considered included: Open Horizon, Lattice Network, and Open Financial Protocols. But, these innovators liked the idea of DeFi or “defy.” Is this a threat or an opportunity for bankers?

While it is too early to answer that question, DeFi is certainly gaining some momentum. According to an article in Forbes, around \$20.5B has been invested in DeFi as of January 2021.

**DeFi 101.** DeFi in its most basic form is essentially the circulation of peer-to-peer funding through a blockchain network completely independent from traditional banks or brokerage firms. Utilizing blockchain software that incorporates security and accountability, DeFi enables borrowers and lenders to transact directly using cryptocurrencies. This broadens the marketplace for lending and has benefits such as faster transaction times and more simplified processes. As cryptocurrencies keep gathering momentum and credibility, DeFi acceptance should follow. Stablecoins are crypto coins that are *“always equal in value to a central bank currency such as the US dollar and that have centralized issuers.”* As it is now, stablecoin growth is climbing and reached \$1T in transaction volumes in 2020, according to The Block Research.

**Traditional FI interest.** Ernst & Young’s global blockchain expert recently predicted that traditional [FIs will begin offering various DeFi services by the end of 2021](#). Sure enough, Societe Generale, a global investment bank, recently used DeFi to refinance \$20MM worth of bonds, initially issued as security tokens through an Ethereum blockchain. The firm is using this as a test, as it is planning to offer such DeFi refinancing options to its customers beginning in 2022. Other big banks may follow.

**Big risks.** While the idea of a speedier, simpler method for executing financial transactions is appealing, it is not without risks.

- DeFi falls outside of regulatory oversight. Therefore, these transactions don’t have the same security and recourse if your account gets hacked.
- There is no FDIC insurance supporting these funds.
- There are often massive valuation swings for cryptocurrencies (although stablecoin is more reliable).
- Based on software platforms, bugs or program errors could cause delivery issues or even allow cyberthieves access.

**Keep DeFi on your radar.** DeFi is still in its early stages. Yet, it is definitely something to keep watching. The technology will likely advance quickly. As the economy ramps up further, SMBs will need funding. In 2020, according to the World Trade Organization, there was a [lack of financing for SMBs to the tune of \\$5T globally](#). DeFi may be one place that these businesses turn to.

Furthermore, this technology is seen as a way to help unbanked communities. As the founder and CEO of a de novo in WY said, *"I think it's really important that a bank stay on top of this, because there are new payment systems coming that offer better, faster, cheaper solutions, and that is an opportunity for [bankers]. But to the extent that they fight [DeFi] or ignore it, instead of understanding the opportunity for them to plug into these new networks, they may be on the losing end of this."*

We will keep you informed of the developments on DeFi as they evolve.

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## ECONOMY & RATES

Rates As Of: 11/15/2021 12:31PM (GMT-0700)

Treasury	Yields	MTD Chg	YTD Chg
3M	0.05	0.00	-0.04
6M	0.07	0.00	-0.02
1Y	0.17	0.02	0.06
2Y	0.53	0.03	0.41
5Y	1.26	0.07	0.89
10Y	1.62	0.06	0.70
30Y	2.00	0.07	0.36
FF Market	FF Disc		IORR
0.08	0.25		0.15
SOFR	Prime		OBFR
0.05	3.25		0.07

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