



# CRYPTO PRAGMATIST PRO

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<b>Name</b>	Velodrome Finance
<b>Market Cap</b>	\$11,150,000
<b>Fully Diluted Market Cap</b>	\$528,200,000 (Terminal supply of 2b tokens)
<b>Executive Summary</b>	<p>Velodrome Finance is an automated market maker (AMM) built on Optimism. The project was launched June 2nd, 2022. The team behind Velodrome previously launched <a href="#">veDAO</a>, which was tightly integrated with the <a href="#">infamous Fantom AMM, Solidly</a>, built by famed DeFi founder Andre Cronje.</p> <p>Solidly, and thus Velodrome, are AMMs designed to align protocol emissions with fees generated. As such, the necessary background knowledge is heavily related to veTokens (mainly Curve's).</p> <p>Velodrome is the largest AMM on the Optimism network in terms of TVL at \$61.5 million (16.22% of Optimism's total \$379 million).</p>
<b>Problem Solved</b>	<p>As an AMM, Velodrome is a place for users to trade both <b>stable</b> and <b>volatile</b> asset pairs with market leading low fees and low slippage.</p> <p>We have detailed in <a href="#">previous reports</a> the importance that token liquidity plays for projects in DeFi. The problem associated with this is that people will not provide liquidity with their capital for free, thus protocols, in one way or another, need to incentivize the liquidity of their token. This happens in a few ways:</p> <ul style="list-style-type: none"> <li>• Pool2 emissions (Pool2 requires exposure to the token being farmed, ie. native token) are costly, inflate token supply, and simply lead to 'farm and dump' strategies.</li> <li>• Protocol owned liquidity (POL) is not always needed and requires a large amount of upfront capital.</li> <li>• Bribes for \$CVX/\$CRV are becoming less 'arbitragable' for protocols, and may eventually be a winner-take-all game for whichever protocol can pay the most.</li> </ul> <p>Velodrome tightly aligns rewards with emissions, and benefits protocols that decide to lock their \$VELO tokens and play into</p>

	<p>the long term sustainability of the project. You can think of it as a refined Curve with both stable and volatile pairs.</p>
<b>Tokens</b>	<p>There are two main tokens for the protocol:</p> <p><b>\$VELO:</b> The ERC-20 utility token for the protocol is used as a rewards token for liquidity providers.</p> <p><b>\$veVELO:</b> The governance token takes the form of an ERC-721/NFT. Users can lock up their \$VELO for up to 4 years, with a longer lock period corresponding to more \$veVELO.</p> <p>\$veVELO holders receive the lion's share of incentives from the protocol: fees, bribes, anti-dilutive rebases, and governance rights. This incentivizes protocols and liquidity providers alike to lock up tokens.</p>
<b>Terminology</b>	<p>On top of the mechanics mentioned above regarding Curve's vote-escrowed tokens, Velodrome indirectly leans on some of the (3,3) game theory <a href="#">popularized by Olympus DAO</a>.</p> <p>The main incentive here is to align the interests of those who are providing liquidity with the long-term \$veVELO holders, creating a flywheel that prioritizes volume and fees.</p>
<b>Founders</b>	<p>There are a lot of people behind the project (including Andre Cronje and Daniele Sesta for the OG codebase), but some of the core team members today are:</p> <p><a href="#">Jack Anorak</a>, <a href="#">alexcutler.eth</a>, and <a href="#">Gabagool</a></p>
<b>Backing/Funding</b>	<p>The project was backed by an incubator DAO, Information Token. They have a 10% stake vested over 24 months, the Optimism team has a 5% stake vested over the same amount of time.</p>
<b>Risks</b>	<p>DeFi exchange tokens have many risks, and looking at them as long term investments can be a risky play. Protocols like Uniswap and SushiSwap have cemented the fact that many of these are simply 'farm and dump' tokens, providing no use to the long term holder and a steady bleed of token value over time.</p>

	<p>Essentially, these protocols pay for liquidity by diluting ‘equity’ holders. Velodrome’s bet is that they’ll be able to create a flywheel that overcomes this equity bleed. Although Velodrome’s clear goal is to do the opposite of this, it is something to be aware of.</p> <p>Of course, there will always be the risk of smart contract exploits, and the value at risk (VaR) for AMMs is significantly higher because of the high TVL required for trading volume. This <a href="#">recent incident</a> put the protocol bribes at risk of being compromised, but was quickly resolved.</p>
<b>Competitors</b>	<p>Velodrome is attempting to disrupt arguably the most competitive area of DeFi: exchanges. Uniswap will be its largest competitor on Optimism, however so far \$VELO is winning the race by liquidity.</p> <p>With roughly 16.22% of all TVL on Optimism, Velodrome cleanly outpaces Uniswap which accounts for just 11%.</p> <p>On Mainnet Ethereum itself, Uniswap (by FAR the largest dex on Ethereum), only holds about 10% of all TVL on the network. Clearly Velodrome has entered as a serious competitor to command the largest share of assets on Optimism.</p>
<b>Documentation</b>	<a href="https://docs.velodrome.finance/">https://docs.velodrome.finance/</a>
<b>Code Repository</b>	<p>The protocol is a fork of Solidly, with some minor changes that are detailed in the documentation.</p> <p>Solidly codebase: <a href="https://github.com/solidlyexchange/">https://github.com/solidlyexchange/</a></p>
<b>Site</b>	<a href="https://app.velodrome.finance/">https://app.velodrome.finance/</a>
<b>Social Media</b>	<a href="#">Discord</a> <a href="#">Twitter</a>

## Intro

Back in the glorious frothy market in early 2022, Andre Cronje was one of DeFi’s best-known names. It came as no surprise, then, when he announced the launch of a groundbreaking Fantom (\$FTM) AMM. Collaborating with another DeFi counterpart, Daniele Sesta, it was touted to be one of the biggest projects in DeFi. Images like this contributed to the hype:



Well, some will remember that the launch of Solidly was a total mess. There was lots of confusion and uncertainty, DAOs were popping up trying to front-run emissions, and there were some bugs in the code and front end that made the user experience horrible. Despite all of this, the protocol took in **massive** inflows and reached a peak of nearly \$2.3 billion in TVL.

The Solidly story ended shortly thereafter. For one reason or another, Andre famously “left the space”, deactivated his Twitter, shutting down the majority of his DeFi projects, and has not worked in the DeFi space since.

 **Anton Nell**  
@AntonNellCrypto 

Andre and I have decided that we are closing the chapter of contributing to the defi/crypto space. There are around ~25 apps and services that we are terminating on 03 April 2022.  
1/3

10:38 AM · Mar 6, 2022 

 [Read the full conversation on Twitter](#)

One of the largest DAOs that was playing the long-term game to control emissions on various Solidly aggregators was veDAO (\$WEVE). After being closely involved with the disaster of

Solidly and seeing the value of the DAO *if* Solidly had been successful, the team decided to fix some of the original problems and develop their own version of the AMM.

### Liquidity Incentivization

Almost like a broken record at this point, we have looked at various methods for how protocols attract and *retain* liquidity. The most rudimentary model can be seen in Uniswap: distributing protocol tokens to the LPs. As we know, this facilitates a farm and dump strategy and creates a price chart that looks like this:



There is no incentive to hold the \$UNI token, so LPs create consistent selling pressure to realize their rewards from being the lifeblood of the protocol.

And then there is Curve. While the incentive is inherently the same (liquidity providers earn \$CRV emissions, which they can and should dump for a profit/earnings), Curve adds the twist of **vote escrow**. This created Convex, StakeDAO, and a whole bunch of other creative ways for protocols to incentivize liquidity.

The difference between Uniswap and Curve is that within Curve there are only tightly correlated assets, also known as stablepairs (often \$1-pegged stablecoins). This reduces impermanent loss exposure for LPs and means that the incentive structure can look different to that of Uniswap: Curve can offer very low trading fees and low slippage.

Velodrome is somewhat of a marriage of these two projects: expanding farther on the mechanics of a vote-escrow token, and offering the benefits to volatile pairs of assets.

## Velodrome

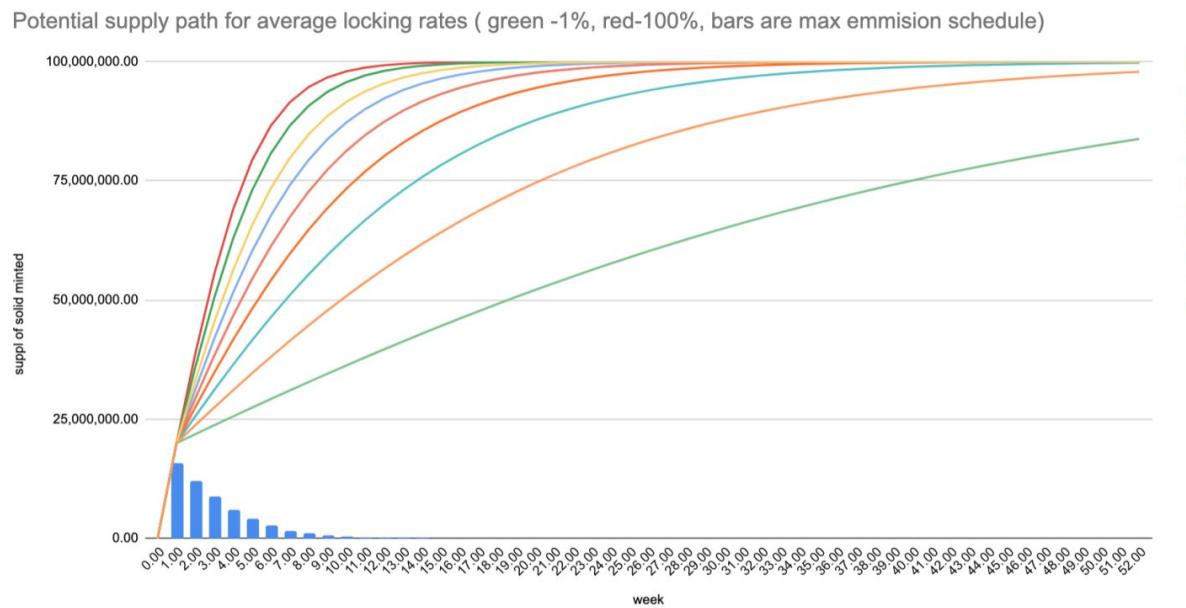
The Velodrome team took the best parts of Solidly and did away with the worst. By using a more thoughtful long-term approach to building the AMM, we are hopeful that the improvements will make a meaningful impact on Velodrome's success over time.

## Improvements on Solidly

Solidly had many issues beyond the bugs. Whether a product of being rushed to market in the high-flying bull market or simply incompetence, the project seemed minimally thought out compared to Velodrome. In the docs and previous veDAO blog posts, the team summarizes the improvements made over the original Solidly AMM. They are:

### 1) Prolonged Emission Decay

The first of the list is the flawed emissions schedule. Many newcomers were eager to be on the starting block for the next big thing, yet the unique emissions schedule seemed to take many by surprise.



The emissions rate schedule was highly inflationary in the initial weeks and then quickly fell off a cliff, emitting only \$SOLID dust after week 10. This created a situation where the first incumbents would receive the largest portion of \$SOLID, and thus control the largest share of voting power.

As a fix, Velodrome created an emissions schedule that **decayed at a slower rate**, meaning protocols joining in the future still had value to unlock with \$VELO. Early lockers will receive

anti-dilutive rebases like Solidly, but again at a lower rate than its predecessor. We will go into more detail on the emissions schedule in the tokenomics section below.

## 2) Eliminated Unproductive Gauges

One notable issue with Solidly was when large \$SOLID holders started directing emissions towards their private pools. The most memorable of this was the Batman-Spider pool, in which only certain people could mint those tokens and thus receive the emission rewards.

To combat this, Velodrome has a whitelisting process for the pool proposals, as well as a multisig team that can strike down any pool that seems unproductive to the future of the protocol:

Signer	Affiliation	Address
Gabagool	Velodrome	0xe9b80b4cf85d7709583dff27c1f51b289cd1e152
Jack Anorak	Velodrome	0x9eBd10B46B43351097caB2D3c03Ccf440957A2a9
pooltypes	Velodrome	0xc0DE1436C4E247F8652476A0B9ff55699801e1d0
Nick	Velodrome	0x53e0b897eae600b2f6855fce4a42482e9229d2c2
vfat	Hundred Finance	0xF0Ca09fbf9a5f61E657Fb208b46b8685c1d4766
0xHamZ	DeFi Independent	0x698c3619f9ecB540cEc21E056ae4A900Bca1649C
Optimism	Optimism	TBD

*Multisig signers, called the Commissaire*

## 3) Tying Rewards with Emissions

Potentially the biggest flaw in Solidly was the fact that voters were able to receive their bribe rewards before they actually directed the emissions.

For example, let's say that an external project, FRAX, wants to bribe for its FRAX-USDC pool on Velodrome. In the case of Solidly, users were able to take the following action:

- a. Cast their votes for FRAX-USDC pool
- b. Claim rewards
- c. Switch their vote, directing emissions to a different pool before the voting period ended

In this scenario, the bribes pretty much just became free money for people with voting power, and didn't actually require specific action. The simple fix from Velodrome now only allows voters to make one voting action per period. Easy enough, right?

#### 4) Ongoing Project Support

Finally, another achilles heel to the Fantom AMM was the fact that there was no team to help with future development. No DAO, no discord, and no documentation meant that the bugs that were so damaging to the validity of Solidly, couldn't be fixed. Although immutable code can often be a good thing (no tampering), in Solidly's case, it created a permanently broken protocol.

Velodrome established all of the community aspects that Solidly was missing.

With the above improvements, Velodrome takes the stance that the underlying mechanism of the veNFT voting system seen in Curve is extremely productive in incentivizing liquidity. Let's go a little deeper into **why** the solution proposed by Velodrom is viable in the long term.

##### The Token

The token model is simple and quite similar to that of curve Curve, with a native token and vote-escrowed version of that token. Let's look at \$VELO first.

**\$VELO** is the ERC-20 standard token for the protocol that incentivizes/rewards liquidity providers via emissions. Think of this like any other DEX token that is distributed to LPs.

**\$veVELO** can be locked on a similar linear schedule as \$CRV. The whole purpose of \$veVELO is to reduce the consistent selling pressure that \$VELO would otherwise face. Locking \$VELO will return a specific amount of the NFT wrapper, depending on the length of the lock period:

- a. Locking 10 \$VELO for 1 year generates 2.5 \$veVELO
- b. Locking \$VELO for 4 years generates 10 \$veVELO

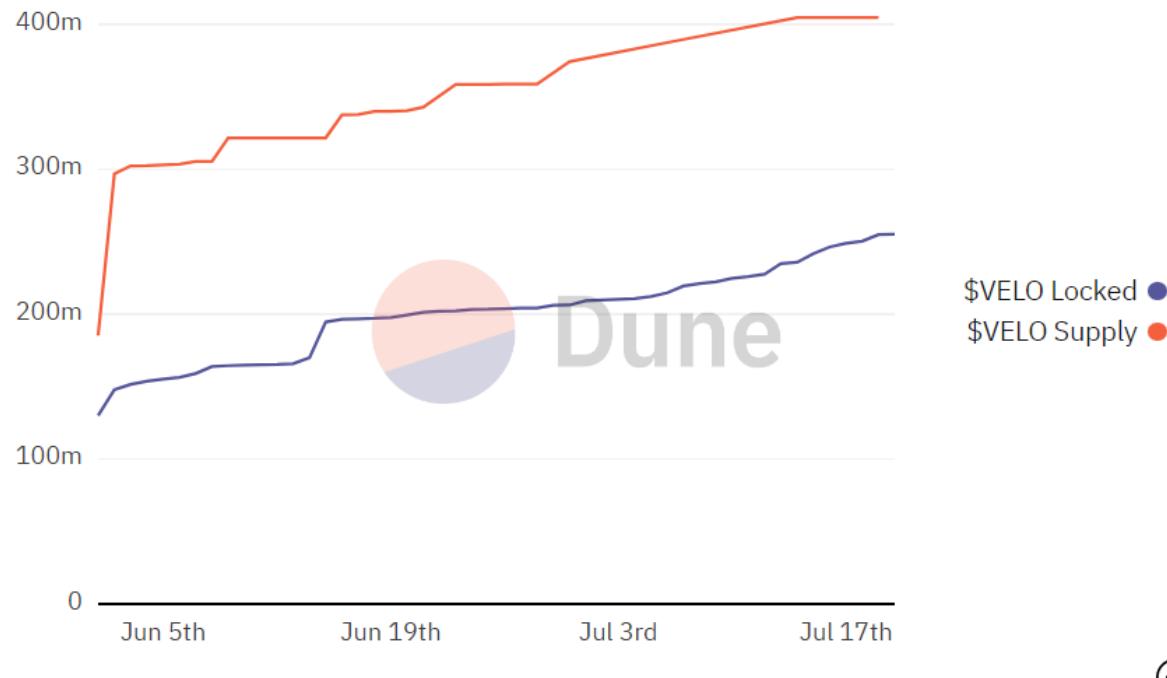
Voters hold the main power and thus earn the rewards by receiving protocol fees, bribes, and rebases. Bribes/fees are described as either 'internal' or 'external' by the team.

- Internal fees: Trading fees for different pools. Voters that cast their vote for the \$ETH-USDC pool would receive their proportionate share of all trading fees within that pool.
- External bribes: The same as those provided to \$veCRV holders or \$vICVX holders. Outside projects will offer payment to be distributed between the voters of a given pool.

The flywheel effect here is that LPs would be better off by locking and compounding their rewards rather than dumping their emissions received. Since launch, we can see that the locking rate is outpacing the \$VELO emissions rate:

## Velodrome Finance \$VELO Supply/Locked

 @Marcov



### Airdrop and Farming Yields

Let's take a look at how you can actually earn money by using Velodrome, and what seems most promising at the moment.

First is the yields provided by LPing. Remember, these are in the form of \$VELO emissions, so take the high APRs with a grain of salt as they can fluctuate based on token price.

#### Volatile Pools:

Pair	APR	Liquidity
OP-USDC	76%	\$ 6,458,704
WETH-USDC	31%	\$ 5,653,175
VELO-USDC	237%	\$ 2,475,838
FRAX-USDC	18%	\$ 1,513,418
VELO-OP	110%	\$ 276,631

The two highest yielding pools are both exposed to \$VELO: one paired against \$USDC and one against \$OP. These APRs sit in such a high range because 10M of the founder \$VELO supply

(2.5% of initial supply) was locked and constantly directing their vote power to these pairs, which are essential to the project success in the short term.

The obvious risk with these pools is impermanent loss, and with the case of \$VELO pairs, the tokens sitting in the pool **do not accrue any rebases** and will become diluted from emissions over time.

### Stable Pools

The stable pair pools have some juicy APRs on offer as well:

Pair	APR	Liquidity
USDC-DAI	9.4%	\$ 17,472,117
USDC-sUSD	15.0%	\$ 14,996,548
WETH-sETH	20.8%	\$ 5,926,288
FRAX-USDC	13.3%	\$ 4,100,813
USDC-LUSD	24.1%	\$ 3,762,188

Again, the reward token here is \$VELO, so to realize an APR listed above would require constant selling of all \$VELO rewards at the current market price. Over the long term, however, users and especially protocols seeking liquidity would be better off by locking rewards and participating in the flywheel.

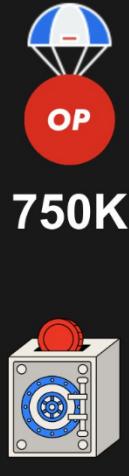
### Airdrop

A significant portion of total token supply has been sidelined for future incentive programs that encourage the continued growth and use of the protocol. One of those events is happening right now:



## veVELO Locking Incentives

Rewards	Eligibility	Distribution
Early Lockers 50K \$OP	<ul style="list-style-type: none"><li>Locked 10k+ veVELO <b>before 7/14</b></li></ul>	<ul style="list-style-type: none"><li>Proportional to veVELO balance</li><li>Snapshot 7/13 midnight UTC</li></ul>
Bonus 125K \$OP	<ul style="list-style-type: none"><li>Qualified as <b>Early Locker</b></li><li>Locked 10k+ additional veVELO <b>before 7/28</b></li></ul>	<ul style="list-style-type: none"><li>Proportional to veVELO increase</li><li>Snapshot 7/27 midnight UTC</li></ul>
New Lockers 75K \$OP	<ul style="list-style-type: none"><li>Not Early Locker</li><li>Locked 10k+ veVELO <b>before 7/28</b></li></ul>	<ul style="list-style-type: none"><li>Proportional to veVELO balance</li><li>Snapshot 7/27 midnight UTC</li></ul>
Ongoing 500K \$OP	<ul style="list-style-type: none"><li>Locked 10k+ veVELO <b>any time after 7/28</b> for next 20 weeks</li><li>Ongoing rewards at avg of 50K \$OP every 2 weeks</li></ul>	<ul style="list-style-type: none"><li>Proportional to veVELO increase</li><li>Snapshot every 2 weeks</li></ul>



Unfortunately, the ability to be an ‘early locker’ has passed as of 7/14. But, the 75k \$OP airdrop can be picked up as long as users lock before the 28th. And in the last section, locking 10k \$VELO (~\$250) every 2 weeks will make you eligible for a 50k \$OP airdrop.

Right now, early lockers that are eligible for the first airdrop have locked only 3.1M of \$veVELO, so the airdrop is going to be pretty solid for the early users. The project has seen a spike in attention recently, so this ‘new locker’ airdrop will likely be less fruitful, but still should be a good bonus.

As far as math goes, each dollar locked will make you immediately eligible for \$1.33 in Optimism rewards.

### Extra Bribes

Velodrome started a “public goods” program where they are topping up on some of the bribes for certain pools:



Velodrome (VELO)  
@VelodromeFi

...

## 1. Public Good Bribe Program (1.25M \$OP)

At a rate of ~30k \$OP / week, Velodrome will bribe critical ecosystem pairs such as:

\$WETH - \$USDC

\$OP - \$USDC

\$OP - \$WETH

\$VELO - \$USDC

\$sUSD - \$USDC

Rewarding \$veVELO voters who vote for deep liquidity on critical ecosystem pairs.

Let's assume an average price of \$1 for OP for simplistic purposes (as of writing, it's trading at ~\$0.75) This would mean roughly every week for the next 6-9 months (length of the program), there is an additional \$30k in bribes across the protocol's most important pools.

By comparison, this is minimal compared to the bribes to \$vlCVX holders, which have gone well into the 10's of millions. But for a protocol on a smaller scale it is a significant boost to the voting incentives.

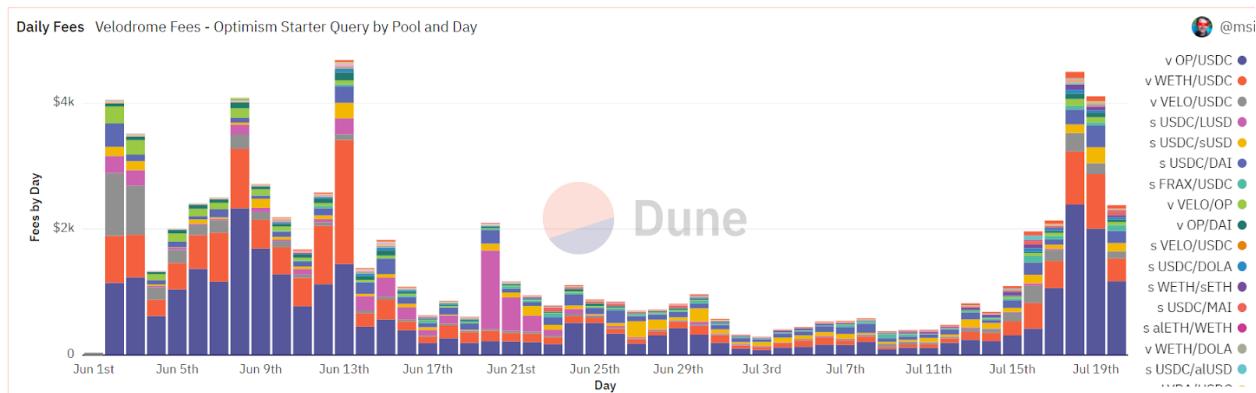
### Fees and Rebases

When thinking about APRs in the form of \$VELO rebases, the *best* practice would be to ignore the effect on total APR. The rebase is in place to reduce incentive for people to sell and encourage long term participation. There are two reasons for omitting the APR:

- 1) If the rebase rewards are sold to realize the earnings, APRs on other earnings in the protocol will decrease over time because of the dilution.
- 2) While technically increasing the \$VELO amount in your wallet, the rebases do not have any intrinsic value other than anti-dilutive effect, and should be locked to maintain other earnings.

Often times, high APRs can get new users unreasonably excited about a protocol without fully understanding the details of the return numbers. Rebases seem to have potential for this effect, and should be **wholly ignored when looking at the desired return** for Velodrome.

In regards to fees (the protocol calls them ‘internal bribes’), the APRs have increased significantly the past week due to increased usage in the protocol. [This dune dashboard](#) provides all the necessary info on trading fees generated:



Remember: fees for trading can only be earned on the pools you vote for. This creates a positive feedback loop where voters will vote for the highest volume pools - which directs emissions towards those pools, incentivizing LPs to put their capital there and offering deep liquidity for traders. Another example of the flywheel in effect.

Here is a closer look at some of the top pools in terms of trading fees and their respective APRs:

Pool	7-Day Fees	# Votes	Vote APR (Projected)
vAMM-OP/USDC	\$7,415.13	36.32m	36.4%
vAMM-WETH/USDC	\$3,170.07	12.94m	43.6%
sAMM-USDC/DAI	\$1,204.84	8.19m	26.2%
vAMM-VELO/USDC	\$1,198.65	44.26m	4.8%
sAMM-USDC/sUSD	\$852.80	19.10m	8.0%
sAMM-FRAX/USDC	\$410.82	3.30m	22.2%
vAMM-VELO/OP	\$355.39	5.06m	12.5%

## Putting it All Together

Made clear above, things can get complicated quickly when trying to calculate potential rewards for locking and voting for given pools. Given that the protocol is so new, protocol wide trading fees and bribe amounts are extremely volatile. The dollar amounts may seem low in revenue, but everything should be observed with taking into consideration the scale of the market cap and token price.

The highest APRs available right now are through bribe incentives with voting pools. There is an art to it in finding the pools with a smaller amount of votes but still sufficient dollar amount in bribes.

### **Tokenomic Deep Dive**

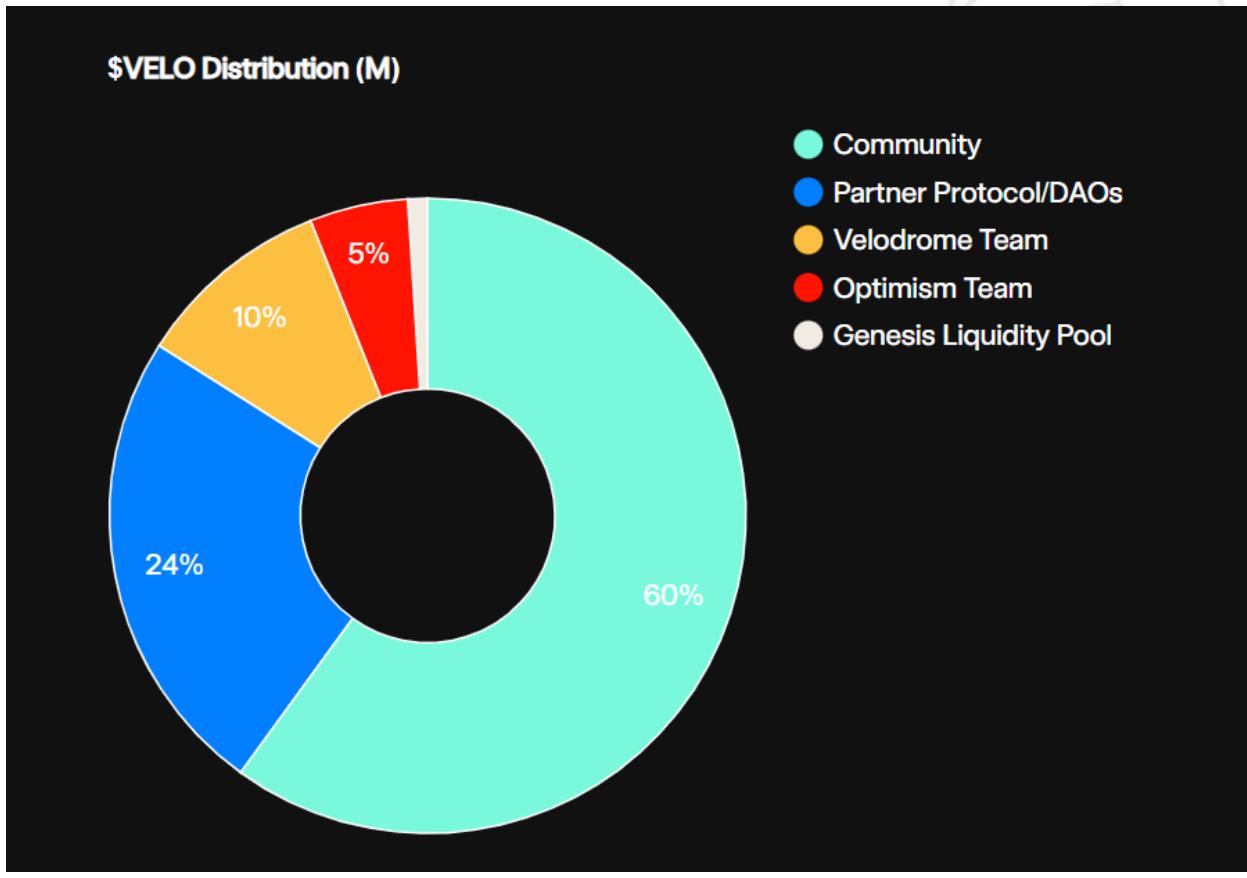
As we touched on, the Solidly tokenomic model was flawed in the sense that it was aggressively inflationary. While Velodrome takes the same protocol design as Solidly, the adjusted emissions schedule and baked-in (3,3) game theory should alleviate the inflationary pressure on the token.

That's the idea, at least, and these highly-inflationary tokenomic models have come under criticism in recent months. Velodrome clearly thinks that their tokenomic flywheel will be able to overcome inflation—it remains to be seen. We think it faces an uphill battle, but aren't completely skeptical of the project's viability. It definitely remains to be seen, though, especially compared to some other more 'blue-chip' projects and competitors.

### **Initial Distribution**

The initial distribution was slated more towards retail users by creating a fair airdrop allocation. This combated the initial race for DAOs to acquire TVL that was seen in the case of Solidly, mostly Solidex and 0xDAO (which made them eligible for the airdrop), to control future emissions and thus the direction of the protocol.

Here is the token distribution, which we will reference throughout this section:



*Velodrome*

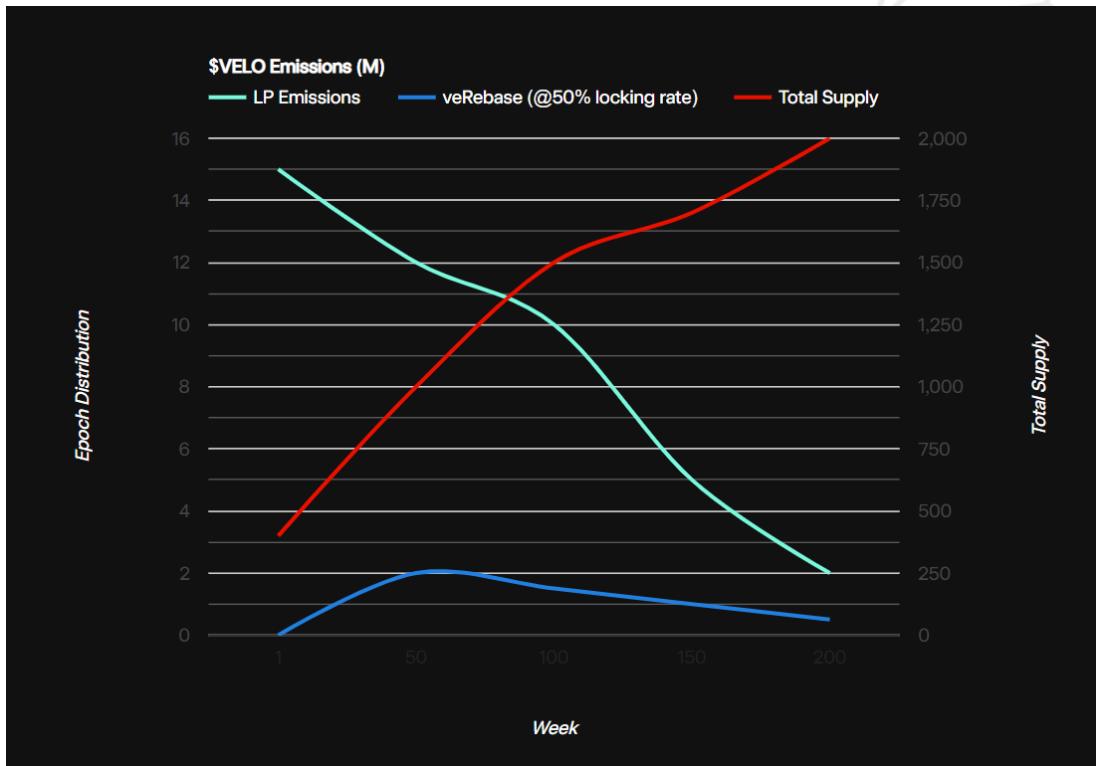
The community allocation is clearly the majority of tokens. 27% and 18% of the 240M were distributed to \$WEVE holders and \$OP network users respectively. The rest of the community portion was given to various users or protocols that have a track record of participating in long-term governance, including \$veCRV lockers with 1,450 day minimum lock and \$vICVX lockers since new contract deployment.

By weeding out any exploitative users, Velodrome can be confident that users will buy into the long term incentives of the protocol, which is necessary for the flywheel to take effect.

18% of the total 24% for partner protocols/DAOs was given to protocols most likely to contribute to Optimism and Velodrome's success, with 6% reserved for future grants to partner protocols.

#### Emissions Schedule

Weekly \$VELO emissions are the backbone to the protocol, incentivizing LPs to leave their capital in Velodrome. The emissions start at 15M and decay at 1% per week.



Because of the inflationary effect, \$veVELO holders are compensated with rebases. Without this, there would be minimal incentive to lock the \$VELO because over time \$veVELO holders' equity value of their token would get diluted by emissions.

### Team Allocation

Total allocation for the team is 40M, or 10% of the initial supply. 25% of this is \$veVELO and will be used for voting 'in perpetuity', so the amount of token supply we should be concerned with is reduced to 30M.

Half of this is vested over 12 months, with the first 6-months as \$veVELO and the subsequent 6 months on a linear unlock period. This is shorter than what we would typically like to see, but given the market conditions, it can be justified. The remaining amount is vested on the similar schedule, but over a 2 year period.

3.5% of emissions will be going to the team address for anti-dilutive purposes and to cover ongoing expenses.

### Competitive Analysis

The long term thesis here is that protocols will be eager to participate in Velodrome in order to maximize their capital efficiency. Here is anecdote from early this week on Synthetix tapping into the liquidity on Velodrome:



Velodrome (VELO, \$sETH)  
@VelodromeFi

...

This week, the [@synthetix\\_io](#) made their first bribe on Velodrome with \$2,000 for [\\$sETH](#).

How'd it go?

That bribe (+our boost) netted them an addition 4M in votes and \$11k in emissions.

A 5.5x ROI that brought in 3.75M in TVL.

Talk about capital efficiency!

Essentially, it is significantly cheaper for protocols to bribe rather than incentivize pools on Uniswap or another AMM. This is nothing new, and was (still is) the same with Convex being a place for protocols to unlock capital efficiency. This is a good sign for Velodrome, however, as it means that the product they're selling (liquidity) remains at a discount and highly in demand.

The turning point will be when protocols decide to start farming these emissions as well, locking into \$veVELO, and replace their bribes with just voting for emissions towards their own desired pools.

As protocols with deeper pockets and treasuries seek to accumulate vote power on Velodrome, the protocol turns into a freight train you don't want to stand in front of. With low fees and low slippage, Velodrome should be the desirable protocol for anyone looking to swap.

### Weaknesses

The claim that protocols unlock capital efficiency by bribing voters rather than ponying up for their own incentives holds under *certain conditions*. As we have seen with Convex, the dollar value in emissions per \$vICVX vote (a proxy for \$veCRV, which is comparable to \$veVELO in our report) has fluctuated over time.

We can determine that the dollar amount in emissions is a function of the following:

## 1) The amount of other bribes.

For example, a total bribe pool of \$100k and emissions are worth \$200k, then protocols will unlock \$2 in emissions per \$1 in bribe. As more protocols step in to bribe, this bribe arbitrage goes away and \$1 spent on bribes approaches \$1 in emissions.

## 2) The dollar value of emissions.

This fluctuates based on price and benefits from the locking and game theory behind vote-escrow. Yet, there is constant downward pressure as the emission schedule approaches zero.

Keep in mind, this is **strictly** looking at the bribe marketplace on Velodrome, which is only one portion of its service as an AMM. Currently, protocols unlock roughly 2-5x in emissions for each dollar spent on bribes, which is clearly beneficial:



Velodrome (.velo, .velo)  
@VelodromeFi

...

Bribing increases the incentives for **\$veVELO** lockers, while attracting liquidity to critical ecosystem pairs.

Bribing protocols can yield a 2-5x return in emission value per bribe value, acting as a capital efficient liquidity catalyst for new and existing players.

7:46 PM · Jul 15, 2022 · Twitter Web App

We can continue with the above framework to find the optimal state for Velodrome.

Ideally, there would be enough bribe flows from protocols to be profitable for voters, but not too much to the point where the “emissions arbitrage” goes away. Theoretically, the emissions arbitrage does not need to be significant, and even \$1.05 provides capital efficient liquidity for a protocol. But as we have seen with \$vICVX, the dollar in emissions per dollar in bribe never goes too far below \$2.

Continuing to look at the amount of emission value per bribe value will be telling to see when protocols may stop utilizing Velodrome. As an innovative and somewhat unfamiliar AMM, protocols may rather pony up the cash to just incentivize liquidity in a different way rather than bribing with Velodrome.

## Emission Reduction Over Time

The incentive for LPs to provide liquidity is not trading fees, but the \$VELO emissions. Although the protocol is designed for LPs to lock their \$VELO, over time the emissions are reduced, and APRs will fall. In theory, the LPs would have enough \$veVELO to receive compensation from the trading fees of the pools, but all situations must be considered.

Emissions do not reach zero until 4 years from now, so it is not a present day problem. But, with the basis of the protocol revolving around LPs being compensated for the opportunity cost of storing their capital elsewhere, it is hard to conceptualize what the next move would be.

## Valuing Velodrome

As a small-cap project, valuing the protocol is difficult. One of the issues that arises is due to the constant fluctuation in price and market cap because trading volume is comparatively low. However, we can take a simple P/S metric with the above data on trading fees (revenues).

A total of roughly \$76,000 for the 7 weeks of operation would forecast yearly revenue at \$570,000. At a current (fluctuating) market cap of \$11.1M, this brings us **near a P/S of 20**. If we account for dilutive effects of emissions, P/S is **105.2**. This is significantly higher than all other major dexes on Ethereum.

Project	Price	Diluted Market Cap	30 days Total Revenue ↓	P/S ratio (30 days avg)
Uniswap	\$5.3	\$5,327,200,199	\$61,000,377	6.36
dydx	\$1.8	\$1,795,124,574	\$19,035,046	6.07
PancakeSwap	\$3.2	\$2,363,808,268	\$13,998,965	3.82
Synthetix	\$2.6	\$717,700,687	\$10,431,702	19.39
Curve	\$1.0	\$3,233,617,769	\$6,181,589	35.76
Sushiswap	\$1.1	\$282,161,712	\$6,144,219	3.30
Balancer	\$4.9	\$468,059,187	\$2,891,960	14.67

[source](#)

However, taking a look at Market Cap/TVL does not necessarily show that the protocol is *that* overvalued:

Token	Market Cap	TVL	Mcap/TVL
UNI	\$ 3,389,246,423	\$ 5,790,000,000	58.54%
CURVE	\$ 3,854,521,306	\$ 5,340,000,000	72.18%
VELO*	\$ 60,000,000	\$ 74,678,000	80.34%

\*using a price of \$.03 and terminal supply of 2B

Circulating market cap will fluctuate every week based on emissions, so it is a difficult metric to use for any valuation purposes. Comparing Velodrome on these metrics highlights that we need to be extremely considerate of the impact that emissions will have.

Although the incentives in place should create the necessary locking to reduce impact of an increasing token supply, this type of extreme token inflation is a new model.

### Conclusion

Velodrome took advantage of a unique and innovative protocol design in Solidly while making sure that all the errors were eradicated. Bringing the protocol to one of Ethereum's rollups leaves the door open for massive network effects to take place as the protocol continues to grow.

Right now, we are most looking forward to a bribe interface, similar to Llama Airforce for Convex. This will allow us to take a more critical eye to the earnings paid out to voters and figure out what the most profitable pools are. The team is planning on fixing the UI for their app as well, which should help clear up some of the questions

As the bulk of emissions are released in the earlier portion of the protocol's life, it is critical that strong DeFi protocols seek to accrue voting power as early as possible. Synthetix showing a desire to stack \$VELO is a great start, and we would like to see this continue. The key question to us is if DAOs and protocols stack \$VELO: if so, it could be very bullish for the protocol, but if not, token inflation might crush any positive price appreciation.

All in all, we see \$VELO as something worth keeping a close eye on, as things can change rapidly. The feedback loop that occurs as more protocols utilize and lock \$VELO, the farther things can run. Despite the reduction in emissions schedule, it seems challenging to overcome such rapid inflation. Additionally, we would like to see protocols incorporate something along the sorts of liquid wrappers or DAO accumulation specifically targeting \$veVELO. These positive network effects are fully possible and could trigger a wild runup in price,