

Information Technology

What is behind the term 'Tokenomics'?

Since Malta has become the first jurisdiction to provide a set of positive regulations on Distributed Ledger Technology (DLT), cryptocurrency exchanges, and Initial Coin Offering (ICO) many companies have seized the opportunity to base in Malta. Among them there are three whale companies with reputable names in the blockchain and crypto exchange world - Binance, BitBay and OKEx.

With the laws passed in parliament on the 3rd of July, Malta became the first country able to assist the development of the new industry which can benefit the island in the future. These laws are expected to come to force some of these days.

Malta is becoming a very ICO friendly island. One of the top priorities that every ICO faces is to raise substantial revenue for the project realisation through its token sales by reaching the soft and hard caps respectively. When the crowdfunding goal achieved, ICOs can start to implement the project following the roadmap written on the whitepaper.

The first wave of consolidation has already started in the cryptocurrency world. Investors are becoming more selective in terms of ICO projects. According to ICS Statist Group 80% of ICOs were scams in 2017 and therefore the trust aspect is crucial. A project trustworthiness should be supported by solid tokenomics and proper expertise in the field chosen for the ICO project.

I sat down with one of E&S Group directors, Karl Schranz, who advises in tokenomics and cryptocurrency, to discuss the meaning and importance of the tokenomics for the ICO sector. He gave me a clear insight of the new topic intriguing many journalists around the world and motivating them to investigate the digital economy.

What is behind the term "Tokenomics"

Tokenomics is the design of the token ecosystem. Correct tokenomics can quite simply make the difference between a successful ICO and one that fails to raise the amount required. Tokenomics is a new art, not older than in a couple of years, and requires the mix of financial, accounting and business skills in combination with experience in the Crypto Economy.

Many so called advisors declare themselves as Tokenomics experts, however few are able to describe what are the main pillars of tokenomics. There are the main areas of consideration when it comes to token design such as soft and hard caps, token type, token price, token quantity, token distribution, fund allocation and lockup options.

Soft and Hard Caps

They are basically fundraising goals of the ICO. A hard cap is the absolute upper limit a team will take and a soft cap is typically a lower limit required for the project realisation. If received donations exceed the hard cap, the funds are immediately returned to investors. If a soft cap isn't reached, funds are sometimes returned as well. Either you try collecting too much, or simply, too little and in both cases your project will suffer, possibly fail.

Type of the Token

There are basically 3 types of the crypto tokens - equity, security and utility.

One of the most promising applications



of smart contracts is the potential for startups to issue equity (or stock) tokens. It will make stock trading more accessible to the average investor and allow shareholders to take a more active role in corporate governance, but due to the current lack of regulatory guidance, few startups have attempted to conduct equity token sales.

A security is a broad classification that refers to any kind of tradable asset. Most tokens are securities by their nature since the majority of ICO participants view crowdsales as investment opportunities. However, a token may fall under the classification of a "utility token", which provides users with access to a product or service.

Token Price

The main concept of tokenomics is to identify the token price. Through this process of verification, financial advisors will then identify the following options to make sure that the token sale is done correctly. Most ICOs create their own tokens to raise money, hence enabling them to

establish the token price. Solid tokenomics obligatory required.

Token Supply and Demand

One of the major things to consider when designing your tokens is the token supply and demand. Creating a token with too much supply will actually backfire. Too much supply, in terms of fiat value, will put off purchasers as demand would be enough to fill the supply. We all know what happens when supply is higher than demand. The value drops. Yet many ICOs seem not to consider this vital part of their tokenomics. The main focus would be on determining the value of the ecosystem as a whole in order to confirm the adequacy of the Soft and Hard caps set and consequently, the price and quantity equilibrium is shaped. It is compared with the value of the ecosystem by evaluating the planned Token Distribution and Fund allocation. This will essentially pave the way for future lockup options to be identified. Additionally, market comparisons are made in order to approve the viability of the whole project.



Token Distribution

Designing the token distribution is vital to achieve your objectives. Token distribution model must assure that you create value for your project, contributors, community and founders in balance. Transparent token distribution answers the question of how many tokens will be distributed in the sale, be kept by the team and go for advisors, community, sponsors, etc.

Fund Allocation

Funds allocation or the allocation of proceeds shows how the received funds will be used in percentage distribution on development, marketing, legal, business development, etc. As for the token Allocation and vesting, it explains what are the criteria for a team to be able to access the tokens they retain in the sale and any vesting or cliff periods to keep incentives aligned.

Life After Tokenomics

Before launching an ICO, founders are to engage investors in supporting the project by starting off a crowd sale. To encourage people to buy and use tokens, one has to put a value to these tokens being issued on the platform. Tokens need to have clear set utility as to what they will be exchanged and used for. Before issuing a token on the platform, ICO founders need to identify the token price, the token quality (or type), the token distribution, how the funds will be allocated, the lockup options and the soft/hard cap to be reached.

Tokenomics is crucially important since it will identify the number of tokens that will be issued during the two stages of token sale and exchange into the services or being traded on the crypto exchanges. It is a critical function undertaken by financial experts with experience in the field and it will definitely pave the way to a successful and fruitful project.

E&S Group has successfully advised 80+ ICOs from their concept stage up to their initial coin offering