Is ETH/BTC finally capitulating?

The ETH Report

An overdue update on the Ethereum ecosystem

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January 24, 2025 • Michael Nadeau

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Topics Covered

- ETH vs BTC
- Onchain Fundamentals Update
- ETH vs SOL
- Qualitative Analysis

Hello readers,

It's been a wild week for crypto and a good time to update your priors. I'm not going to cover the Trump memecoin here, but I shared a few thoughts on LinkedIn in case you're interested.

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Instead, this week, we're revisiting ETH and the Ethereum ecosystem with some fresh new data that we're … lves.

Strap in, as we're covering a lot of ground in this one.

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ETH vs BTC

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ETH/BTC *continues* to make new lows. BTC dominance has been relentless — now back to 59.2%. With that said, we'd encourage you to zoom out a bit. The white boxes above show that ETH/BTC was even lower at the same point in the '21 cycle. Bitcoin Maxi's were rejoicing at the time as BTC dominance was 63% back then.

Of course, ETH went on to do a 5x over the next five months — as BTC dominance dropped to 40%.

For some context, if ETH/BTC were to get back to .08 (as it did twice in the last cycle), this would put ETH at $8.2k+ at current BTC levels.

We still think ETH will have its moment.

But I'll admit my conviction is waning a bit.

Something I've been thinking about is the idea that there are still a lot of ETH maxis out there. But I'm also seeing the community fracture a bit. Just this week, we saw several prominent members of the Ethereum community drop their .eth from their X profiles.

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It may be just noise or a bottom indicator. At the same time, you have an interesting setup right now between

1. Ethereum is priced at 3.2x the market cap of Solana but has largely been surpassed by Solana in terms of fundamentals, developer interest, and mind share.
2. ETH maxis are starting to question their allegiance to the chain.
3. Solana continues to capture developer talent and new token launches (Trump memecoin, Pudgy Penguins memecoin)

If you zoom out, you can start to think about what it might take for Solana to flip Ethereum from here. For example, would Solana have to run up 3.2x? Or is it possible that a % of the Ethereum community finally capitulates and swaps a portion of their ETH for SOL?

If it's the latter, a "flippening" could happen faster than people might expect. In this case, ETH would go down while SOL goes up at the same time.

We saw this when Trump launched his memecoin last weekend. Almost all other memes were down immediately as many investors swapped their existing meme holdings for Trump.

It's not my base case (we think most of that rotation has already played out). As noted, it's possible that .eth's denouncing Ethereum is actually the bottom.

Of course, this doesn't mean there is anything deeply wrong with ETH or Ethereum. As far as we can tell, the community is executing on its roadmap. There is still a ton of innovation, developer talent, onchain value, and network effects within Ethereum.

But you don't have to take my word for it. You can study the onchain fundamentals yourself…

In this section I'm going to run through a number of key onchain indicators with some of our new data, sharing a few key takeaways for each.

L1 Fees

Base Fees

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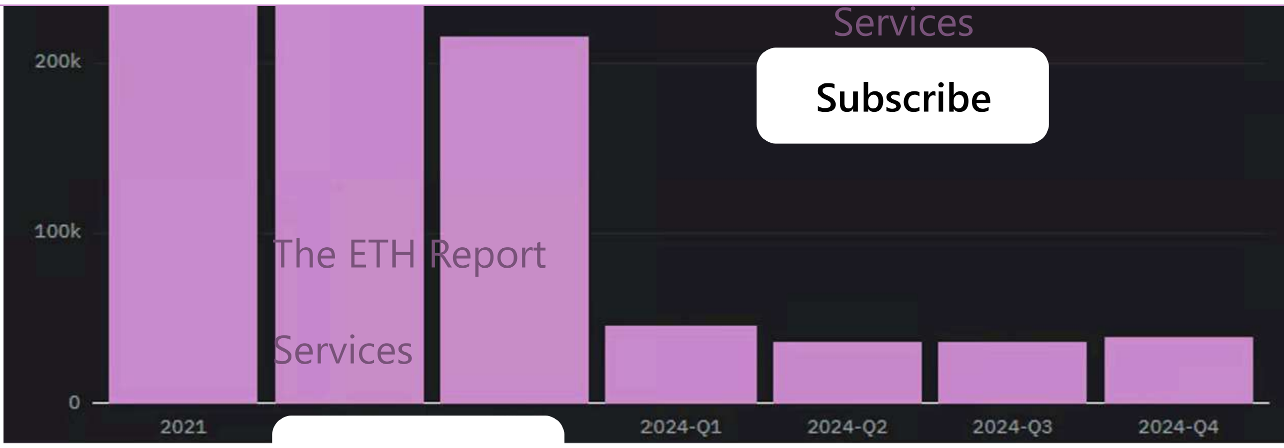
Data: The DeFi Report, Dune

Takeaways:

1. Base fees (which are burned) were up in Q4 for the first quarter since '22 (135% increase over Q3). Still, base fees were down 42% in 2024 compared to 2023.
2. Uniswap, Tether, MEV Bot, Circle, and Banana Gun (Telegram Trading Bot) are currently the top five gas-consuming contracts on the L1.
3. The top contracts reveal how crypto is primarily used today: 1) speculative trading of assets, 2) stablecoins.

Priority Fees



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Takeaways:

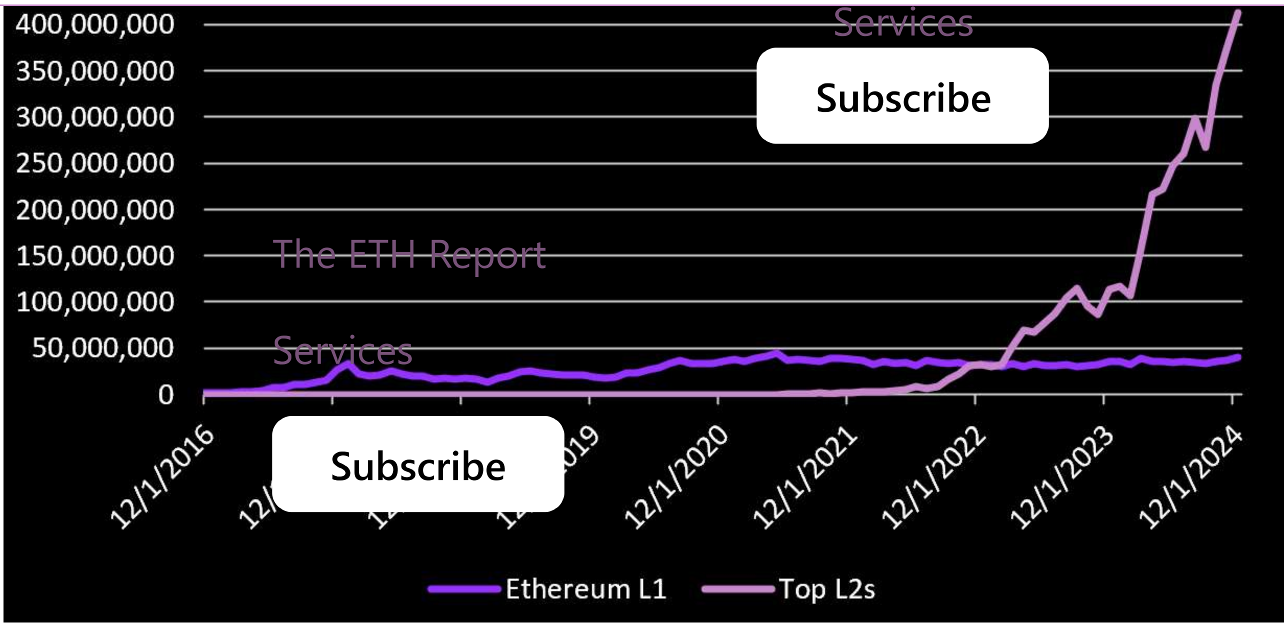
1. Priority Fees (paid to ETH validators and stakers) were up 8% in Q4 but down 21% from Q1. For the year, priority fees were down 26%.
2. Lower priority fees in Q4 vs Q1 is surprising. This means there was less speculative activity on the L1 in Q4 (post-election) than there was at the beginning of the year, pre-ETF announcement.
3. We think there are two primary reasons for this: 1) users are moving to L2s, 2) users are moving to Solana.

L1 vs L2 Transactions

Speaking of L2s. Part of the reason that Ethereum L1 struggled so much last year is due to the EIP4844 network upgrade — which introduced a new type of data on Ethereum called “blobs.” These “blobs” allow L2s to store transaction data on the L1 at very low cost.

This resulted in 1) cheaper L2 fees and 2) no L1 congestion — as L2 transactions no longer compete with regular L1 transactions. Lower congestion on L1 = lower priority fees.

But let’s take a look at user activity at the L2 level. As we noted, users are moving to both L2s (short-term bearish, long-term bullish for ETH) and Solana (short + long-term bearish for ETH).



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Data: The DeFi Report, Token Terminal

Note: L2s included = Base, Arbitrum, OP, zkSync, Blast, Starknet, Immutable, Manta Pacific

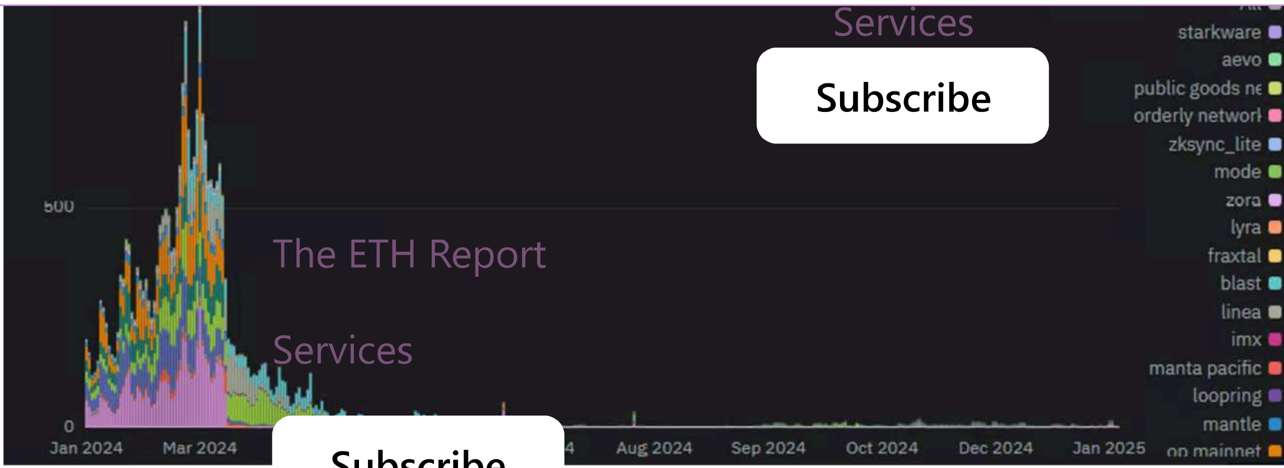
Takeaways:

1. The top L2s are doing 10x the number of transactions as Ethereum L1 today. One year ago the figure was 3x. Two years ago it was 1x.
2. Power laws are playing out on layer 2. Base controlled 64% of the transaction activity in December amongst the top L2s. Arbitrum was #2 at 18%. OP had 7% of the market. Six months ago, Base had 42% market share vs 27% for Arbitrum and 9% for OP.
3. We expect to see the floodgates open for large institutions to enter crypto, with many opting to build their own L2s. Given the current power laws, it will be interesting to see how this plays out. Will institutions launch their own general-purpose L2? Build on Unichain? Build on the OP stack? Time will tell.

But what does all of this mean for value accrual back to Ethereum L1? After all, if L2s are successful, shouldn't this drive demand for ETH (users on L2s need ETH to transact) + increase settlement/accounting fees paid to Ethereum L1?

Let's see what the data says…

L2 fees paid to L1



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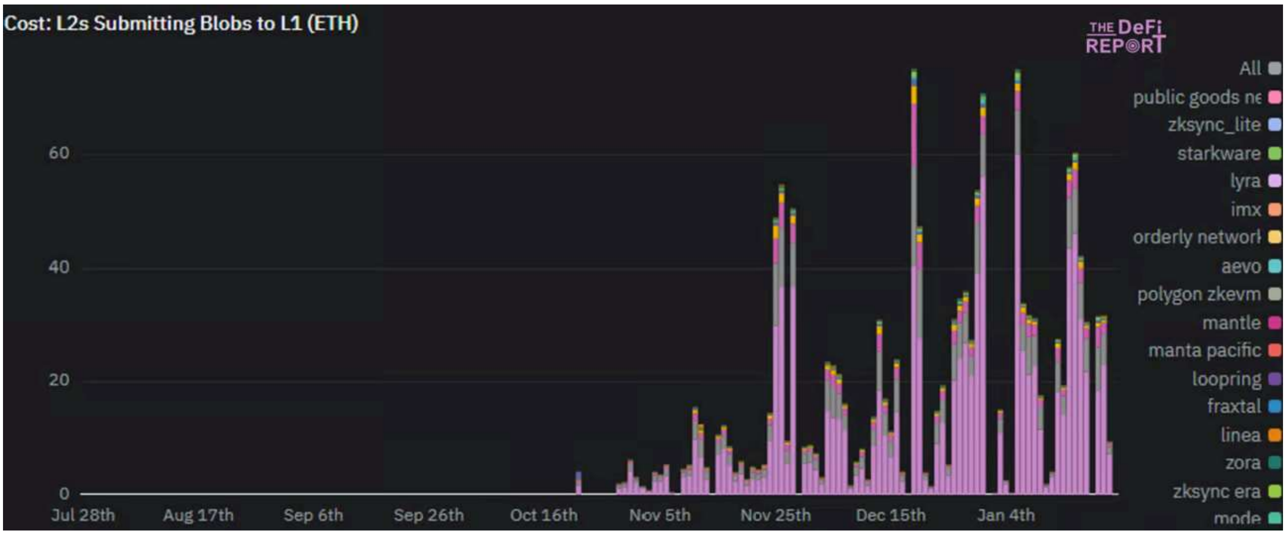
The above chart is showing us the costs that L2s are paying to publish data to Ethereum L1.

Takeaways:

1. The EIP 4844 upgrade occurred in March. The chart shows us the impact: on March 10th, the L2s combined to pay 577 ETH to post data to the L1. Yesterday, they combined to pay 3.6 ETH (99.5% drop) to post data to the L1.
2. Ethereum disrupted itself via EIP4844 so that the network could scale. If it wants to make back those fees, we'll need to see an explosion of L2s and new use cases — which could ultimately backfill the glut of new supply made available via technical upgrades that benefit L2s.

Blob Fees



Data: The DeFi Report, Dune

Takeaways:

1. In the above chart, we can see the increase in blob fees as L2s transition from traditional “call data” and ramp up. Peak activity occurred on 1/6. But only 75 ETH was paid to the L1 ($277k).
2. It took 16.06 million transactions on the L2s to produce the $277k in blob fees ($.017/transaction) on 1/6.
3. Ethereum wa … in L1 fees/day at the peak of the ‘21 cycle. To get back to that level in blob fees, we would need to see transactions on L2s ramp to 4,117,647,058 transactions/day.

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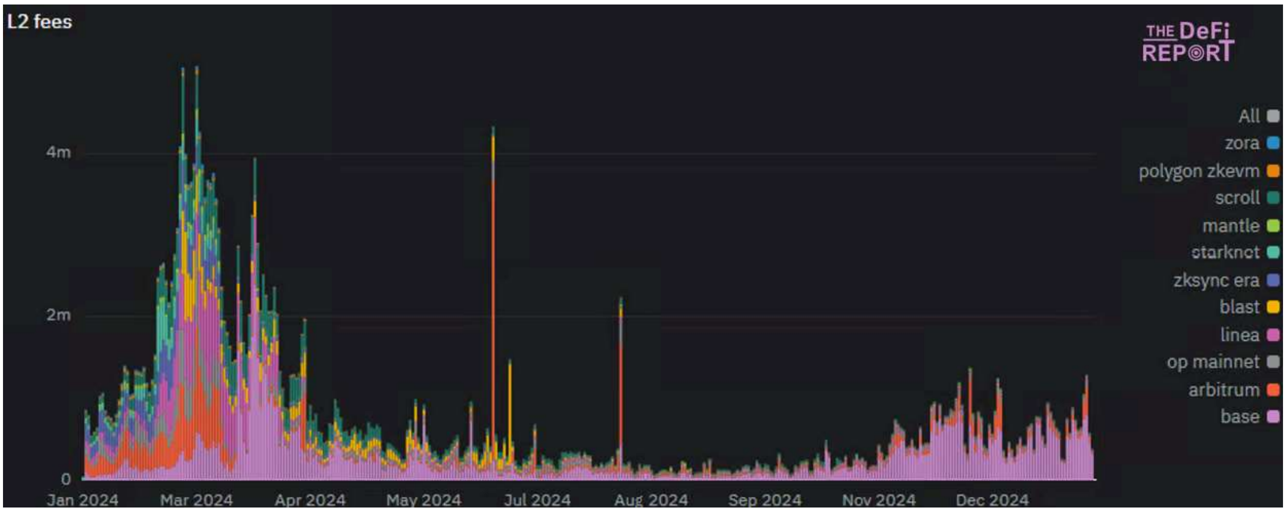
That’s a 256x in terms of combined transactions at the L2 level to get back to peak ‘21 fees for Ethereum L1 (assuming 99% of transactions move to L2).

L2 User Fees

Shifting to *user fees* paid to the L2 (rather than L2 fees paid to L1).



Data: The DeFi Report, Dune

Takeaways:

1. We can see that L2 fees are also way down as a result of EIP 4844.
2. Just before the upgrade was implemented, L2s peaked at about $5m combined user fees per day. Now, they are doing roughly $1m/day.

Arbitrum is number two, with OP the 3rd best L2 in terms of user fees.

L2 User Fees as a % of L1 User Fees

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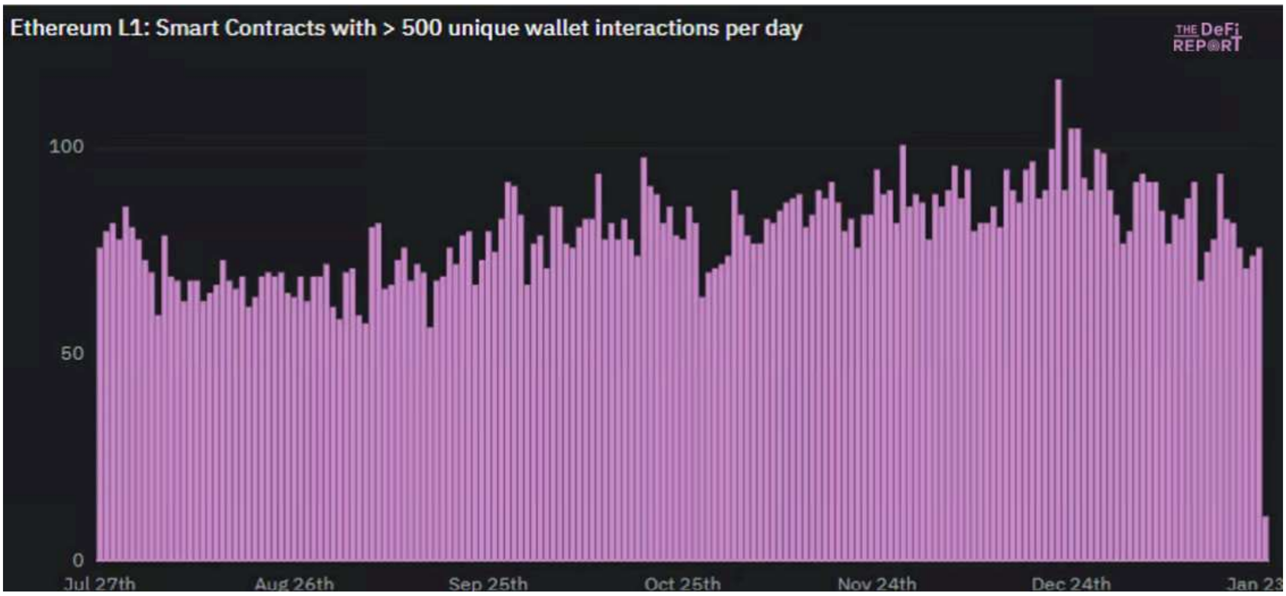
Takeaways:

1. Despite doing 10x the number of transactions of Ethereum L1, the L2s are combining for just 9% of L1 fees currently — revealing persistent demand for L1 block space despite much higher transaction fees.
2. L2 fees as a % of L1 peaked at 24% earlier this year. In the future, we expect 90% + of Ethereum L1s fees to come from the L2s.

Ethereum L1: Smart Contracts with > 500 Interactions per Day



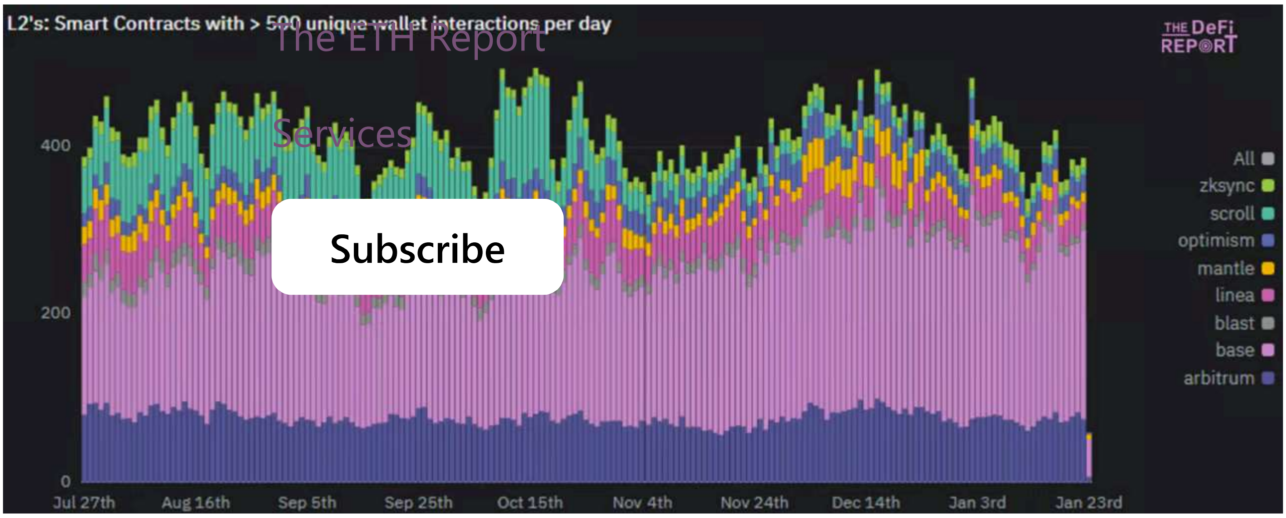
Data: The DeFi Report, Dune

Note: this is a new metric we are introducing as we think it provides a strong signal for relative comparison of L1s and L2s.

Takeaways:

2. The leading contracts are Uniswap, Tether, Circle, MEV bots, Banana Gun, top L2s, and the top DeFi projects.

L2s: Smart Contracts with > 500 Unique Wallet Interactions per Day

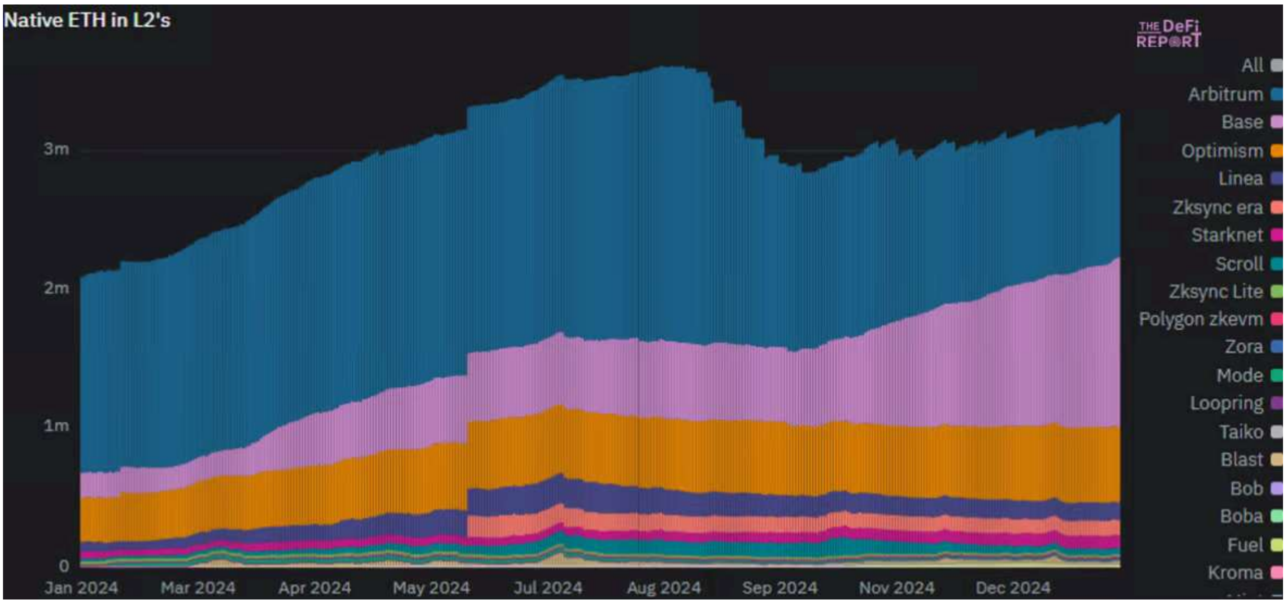


Data: The DeFi Report, Dune

Takeaways:

1. The top L2s are combining for roughly 5x the number of smart contracts with greater than 500 daily unique interactions than Ethereum L1 has.
2. Once again, Base dominates the L2 playing field. It has roughly 55% of all smart contracts with greater than 500 unique interactions per day. Arbitrum is #2 with a roughly 20% market share.

Native ETH in L2s



1. Native ETH (does not include staked or wrappe ... .6 million in July. It's now down to 3.25 million (2.7% of the
2. Base leads with 1.23m ETH. Arbitrum has 1.03m ETH (the above chart tells us that a lot of ETH on Arbitrum left for Base), and OP has 542k. That's 86% of the market right there.

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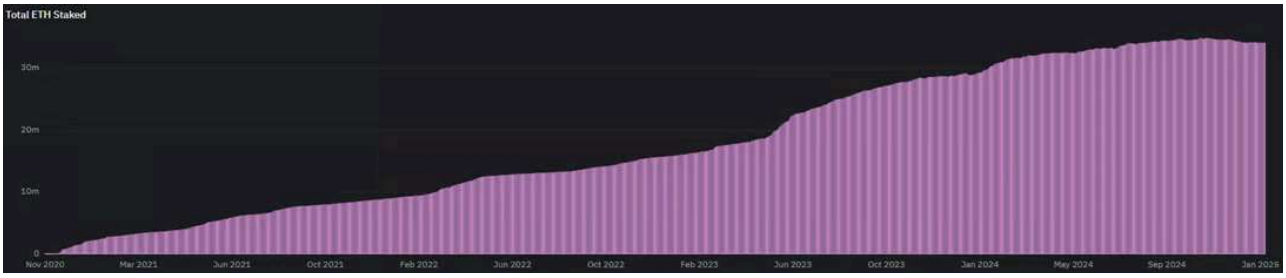
3. 2.7% of ETH having migrated to L2s is surprising to us. It indicates that users *still* do not trust L2 bridging — as 97.3% of ETH currently resides on the L1 (with a small amour
4. If we were tc ... and wrapped ETH, the number would increase to 4.3m ETH on L2s.

ETH Staked

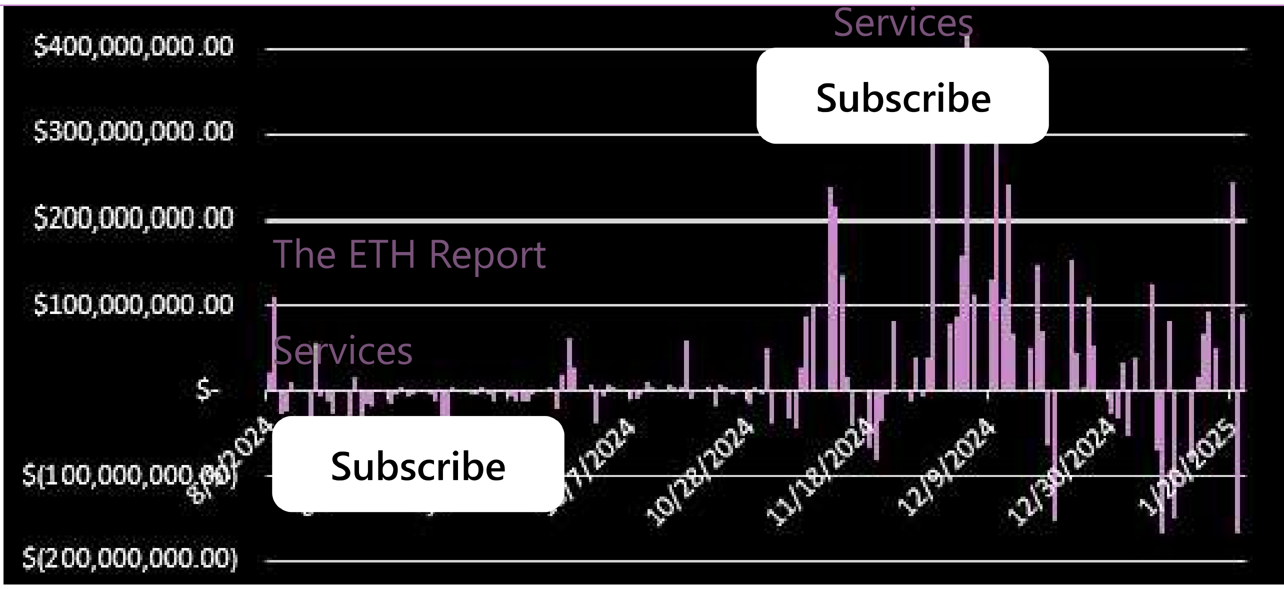


Data: The DeFi Report, Dune

Takeaways:

1. Total ETH staked has dropped in Q4 after peaking at 35m (29% of the circulating supply). It's at 34.17m today.
2. Ethereum staking yields have dropped from 5.5% to roughly 3% over the last few years. The drop is due to a combination of 1) more stakers, 2) lower user fees.
3. If fees continue to increase with total ETH staked leveling off, we could see ETH's staking yield start to move higher.
4. This may surprise you, but in terms of total economic security, Ethereum has $110,984,160,000 of value securing it. Solana has $961,818,000,000 — largely due to a much higher % of SOL staked than ETH on Ethereum. Ethereum's lead as a more secure and decentralized network is fading along with network fundamentals.

ETH ETFs



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Data: Glassnode

Takeaways:

1. The ETH ETFs now hold 3.65m ETH ($11.8b). That's 3% of the circulating supply (more than is held in L2s today). For reference, the BTC ETFs hold 5.8% of the supply ($121b).
2. In terms of net flows, the ETH ETFs have $3.2b today. BTC has $37b of net flows.
3. Given that ETH is about 20% of BTC's market cap, we think the flows could skew toward ETH in the latter stages of the cycle, as ETH only has 9.7% of the BTC ETF holdings today.
4. The ETH ETFs do not return yield to holders today, but we expect this to change. When this occurs, it's possible that the ETH ETF could be more attractive to investors over BTC.

Inflation Rate

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Data: The DeFi Report, Glassnode

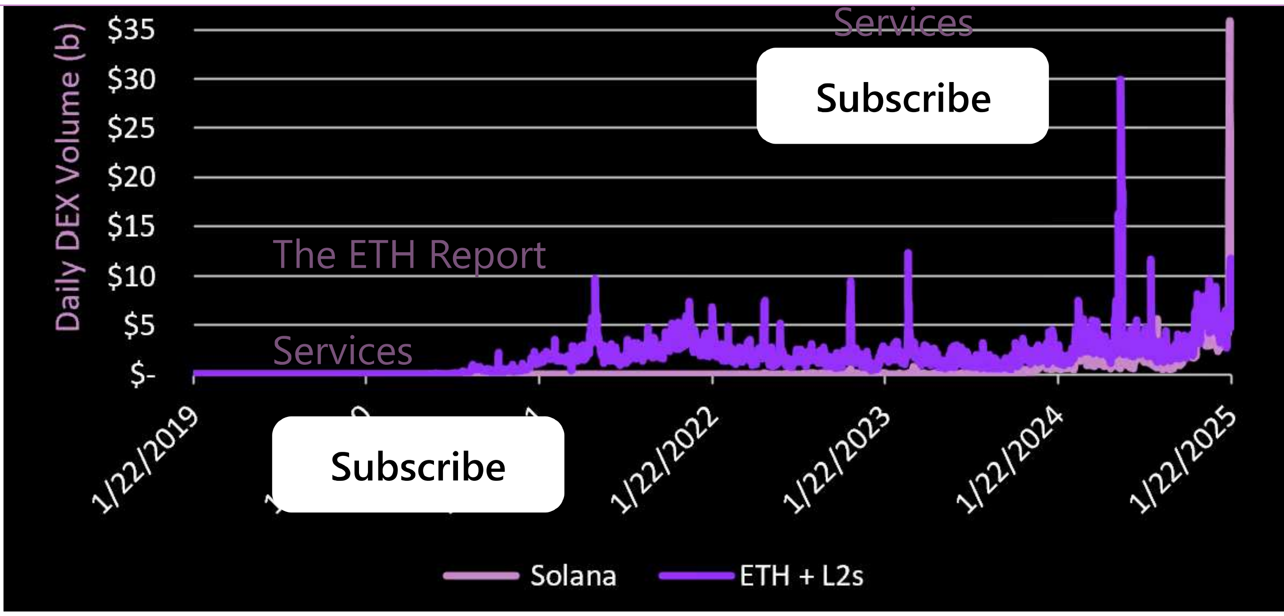
Takeaways:

1. After being deflationary for 2023, ETH supply increased by .10% in 2024.
2. The network was deflationary in Q1 but flipped inflationary in Q2-Q4 after the implementation of EIP4844 in March.
3. Q3 (.11%) and Q4 (.11%) produced the highest levels of inflation.
4. We think it's quite bullish that Ethereum was nearly deflationary in ‘24, given the challenges throughout the year.

ETH vs SOL

We’re going to do a full data-driven breakdown in an upcoming report, so I won’t go into a lot of detail here. But I want to address the most important metric when comparing Ethereum to Solana right now:

DEX Volumes



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Data: The DeFi Report, Artemis

Takeaways:

1. Over the last month, Solana has done $220b in DEX volume vs $172b for Ethereum + the L2s.
2. Last Saturday (TRUMP memecoin first-day trading), Solana did $36b in volume. That's 3x more than Ethereum + the L2s all-time high watermark.
3. For reference, the Nasdaq does roughly $200-$400b per day.
4. We think DEX volumes are the most important metric to track at this stage of crypto adoption. Why? Ultimately, we believe all trading of financial assets will move to public blockchains.
5. The open question for Solana is whether or not institutions like Blackrock will trust it as their home for tokenized equities, bonds, private assets, etc.

Qualitative Analysis

To wrap up, I want to share a few thoughts on what I see from the Ethereum Foundation, community, and overall leadership.

1. I'm growing concerned about Vitalik as the leader. It's not a knock on Vitalik and everything he's built. It's just that Ethereum needs to position itself for the business/institutional community now. Not the cypherpunk crowd. It feels like new leadership is needed for this next stage.

Ethereum needs to see this group step up and serve as BD for institutional use cases.

3. The Ethereum Foundation released its 2024 R ers spending both internally and externally….for 2023. I kid you not. A microcosm of sorts for where Ethereum stands today.

4. It's clear that Solana is moving faster. Has a more aligned community. Is focused on its end users (rather than ideology). And has a technically superior L1 architecture. But that doesn't mean Solana won't run into its own scaling issues that require happening.

In conclusion, Ethereum disrupted itself in 2024 via the EIP4844 network upgrade. Shortly thereafter, it lost momentum. Mindshare. And strategic alignment within the community.

With that said, Ethereum is chugging along. It's executing on its roadmap. We see bright spots throughout the ecosystem, particularly on Base. In some ways, Ethereum feels like it's turning into a value play. The challenge is that crypto markets do not run on value. The run-on *attention*. Speculation. And hype. Therefore, Ethereum needs a major catalyst to bring it back. We think this *could* come in the form of a major announcement from a large TradFi player building an L2, using the playbook that Coinbase has laid out.

Will it be enough to reverse course?

And in the very long run, will any of us remember 2024, EIP4844, and .eth's capitulating?

Time will tell.

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