Following up on the previous [text proposal](#) to relaunch the Incentive Program, we propose to change the Incentive Program significantly. As such, we are sharing this proposal and plan to launch a new text proposal.

Aligning with the state of the dYdX Chain and the up-coming launch of dYdX Unlimited, Chaos Labs proposes the following incentive structure to bring maximum impact to the upcoming dYdX Unlimited upgrade.

We have carefully analyzed each aspect of this proposal, designing it using community feedback and learnings from the 9 month Launch Incentive Program.

Detailed Proposal

The proposed rewards will continue to be earned as points over each one month season. As before these will be split into dedicated allocations for traders, and market makers to incentivize these activities separately.

Liquidity on the dYdX Chain has been discussed in depth, and with permissionless markets launching, deep, thick orderbooks will be needed to allow traders the freedom to trade across the wide range of markets. To achieve this goal, 60% of rewards are being directed towards market maker incentives, with the remaining 40% earmarked for traders.

To better size the incentive program for this liquidity focus, we propose reducing the overall size to $6m in DYDX, over 4 months (1.5M per month) to allow for an impact analysis before committing further tokens.

Proposed Incentive Structure for Traders

Trading points are being simplified for the dYdX Unlimited relaunch to make them easier for traders to understand and optimize for, while rewarding them for performing the activity most beneficial for their segment to the dYdX Chain, paying fees.

A traders trading points are proposed to be represented as their fees paid with a 2x boost for fees in non top-5 markets.

This is multiplied by the trading points multiplier to arrive at a final points number. The multiplier is constant across markets.

Proposed Incentive Structure for Market Makers

The value provided by market makers can be measured across different dimensions. It is important that market maker rewards approximate the positive impact that market makers provide to the dYdX Chain ecosystem. This aligns the rewards-maximizing strategy most closely with positive outcomes for the dYdX Chain.

It is also important that the rewards formula is simple and easy for market makers to optimize for. To meet these two objectives of aligning rewards with value provided, while remaining simple and easy to optimize for, the market maker rewards will focus on differentiated incentives across three dimensions:

- Maker volume satisfied:

The total volume of maker volume over each period.

- Orderbook liquidity provided:

Orderbook liquidity plays a crucial role in enabling larger trades and liquidations to clear. This will be measured by randomly sampling the orderbook at different depths.

- Long-tail market serviced:

To simplify the definition of long-tail and align with the trading rewards methodology, we will define long tail as all markets other than the top 5 by volume. These top 5 by volume will be announced at the beginning of each season, measured as the 5 highest volume markets of the previous season.

Proposed Methodology

We propose measuring the value provided by market makers using the two-factor Cobb-Douglas production function. This function widely used to represent the technological relationship between the amounts of two or more inputs and the amount of output that can be produced by those inputs.

α and β in this case represent the output elasticities of volume and liquidity which are in the process of being calibrated, while κ represents a multiplier boost for long-tail markets. They should be measured and calibrated in a way that best incentivizes behaviors beneficial to dYdX.

A benefit of measuring market maker contributions like this is that the formula can be thought of as measuring the volume weighted liquidity provided. The volume weighting will naturally upweight liquidity provided in more active markets, and over

more active periods, tying the value of the liquidity to its utilization to an extent.

The volume score and the liquidity score should be measured over a defined period in each market. At the end of the period, the Q score should be computed in each market, and summed across markets for an overall value. This will provide protection against excessive liquidity being provided in markets that do not require it as the low volume scores there will weight this liquidity low because of the product formula.

The proposed measure of liquidity is to track the sum of liquidity at 25bps (L_{25}

) and 50bps (L_{50}

) and weight this by the inverse square of the spread to value tighter liquidity more:

The final Q score is multiplied by the market maker points multiplier to arrive at the final market maker points score.

To limit this rewards segment to market makers providing a dedicated service to the dYdX Chain, only makers doing over 0.25% of maker volume over a season are eligible for maker rewards.

Summary of the Revised Proposal

- The duration of this iteration of the program is proposed to be reduced to 4 months.

- The total size of this iteration of the program is proposed to be $6m in DYDX, with $1.5m allocated to each 1 month season.

- 60% of each season's rewards allocated to improving liquidity through market maker incentives making up $900k per month.

- Market maker incentives to add a liquidity component to the current volume-based formula.

- 40% of each season's rewards allocated to trader incentives, making up $600k per month.

- Trader incentives will be fee weighted, with a 2x multiplier for fees paid in non-top 5 markets. The top 5 markets will be announced at the beginning of each season as the highest volume markets from the previous season.

- There will be a deeper integration with the trading front ends with APIs being built to track metrics associated with user rewards.

There will no longer be trading leagues in the incentives re-launch.

Next Steps

In the absence of strong dissent, we will submit an on-chain proposal on November 7, 2024 to ratify this proposed incentive structure for the dYdX Unlimited launch.