

Simple Summary

A proposal to decrease the vault spread parameter from 100 basis points down to 30 basis points.

Introduction

Hey dYdX community! I'm Max, and I've worked on-and-off on dYdX research topics since the early days of dYdX V3 governance. I'm now working with the dYdX Ecosystem Development Program to help research dYdX LP vaults. With this research, I aim to provide the community with an understanding of the benefits and drawbacks of LP vaults, as well as provide an initial recommendation for the quoting parameters that should be put in place for the vaults. This particular proposal addresses the vault spread parameter, which I believe should be changed from 100 bps to 30 bps.

Motivation

The [dYdX Chain v5.0 upgrade](#) included the initial version of protocol-enshrined vaults. Note, LP vaults were introduced in the [dYdX Chain v5.0 upgrade](#) for testing purposes only. These vaults enable passive liquidity provision, similar to how users can provide liquidity on AMMs like Uniswap (read more about vaults [here](#)). Each vault is associated with a single market, where the vault places orders that sit on the orderbook as resting bids and offers. The vault has certain dYdX Chain governance controlled parameters that control the prices for those bids and offers, one of which is the spread parameter. A large value for the spread parameter means that the vault is more protected against short-term price movements, since users must cross a larger spread to take liquidity against the vault. However, this protection for the vault comes at the expense of liquidity for traders, so the spread parameter must not be so large that traders don't want to cross the vault's bid-offer spread. For this parameter, the best way to optimize it is to set a reasonable value at first, then observe its empirical performance, then iterate on the parameter value.

I believe that a 30bp (0.3%) spread parameter would be much more reasonable than a 100bp (1%) spread parameter. For comparison, traders on dYdX V4 today can often trade BTC or ETH for ≤ 1 bp of spread. Even Uniswap V2's default LP pools effectively charge a 30bp spread.

Furthermore, it is better to bias in favor of a lower spread parameter rather than a high spread parameter when testing vaults. This is because a lower spread parameter is expected to lead to more fills, which would give us more data to understand how vaults perform. In the case where I am wrong, and that 30bps is too low, we can always adjust the parameter back up to 100 bps with another governance proposal.

Specification

Lower the [spread_min_ppm](#) parameter to 3000 (i.e., 30bps).

Implementation

This proposal simply requires a parameter change on dYdX Chain mainnet.

This proposal was successfully tested on [dYdX Chain testnet](#).

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Next Steps

I will submit the mainnet proposal on June 10, 2024.