I believe it is important to understand the differences between these types of strategies and the contribution of such strategies as a lever for growth and long-term value creation for derivatives brokers.

Let’s start by defining what each initiative entails.

A trading competition

usually consists of initiatives that set prizes for the best traders over a period of time. Each competition typically defines specific criteria to rank the results of all traders, with profitability often being one of the most important factors. However, in many cases, criteria such as net trading gains are also included. These criteria are crucial as they can create environments where profitability is paramount in some cases, and where the capital employed is the most important factor in others.

Funding Talented Traders

is an initiative where, based on certain criteria, capital is allocated to the operations of specific traders each period. This capital usually mirrors the trader’s operations, and the trader benefits from a significant portion of the positive results of the strategy. Typically, the trader does not incur a loss of capital if the operations result in negative outcomes.

What are the main differences between both strategies?

Marketing Spend Efficiency

In the case of the trading competition, the cost associated with the initiative is entirely awarded to the winning traders. In the case of Funding Talented Traders, we depend on the performance of the selected traders. It seems unlikely that all traders would lose all the capital employed, and we could even have scenarios where, if the selection identifies talented traders, more capital than initially allocated could be recovered. The variability will be high and will very likely also depend on the type of market.

dYdX Tokens

In a trading competition, awarding dYdX tokens might not lead to a market sale if these users typically hold onto them. In the case of the second initiative, it would be necessary to sell the tokens to provide capital for the operations. This could generate additional pressure on the token. However, if the funding mechanism proves to be more efficient in the long run, it should create less pressure as it would require a smaller budget.

Types of Traders

In a trading competition, the most rational strategy will be to take the highest possible risk with the least amount of capital. It is also common to attempt different strategies to diversify for various possible scenarios. This generally rewards traders who are particularly suited to taking high risks over a period of time, which is usually unsustainable in the long term. In the case of Funding, the focus should be on financing traders who are capable of consistently increasing the capital employed. When deploying capital as investors, what is truly relevant for brokers carrying out these initiatives is the sustainability that allows these investors to continue increasing their capital. In this case, the multi-account strategy does not make sense since the capital is deployed in only one account, and the returns come once that capital has been allocated. The incentive is to achieve good results to maintain it.

What are the main differences between both strategies?

Trader incubators are an excellent strategy and a way to attract the best talent to platforms in the long term. However, brokers typically use competition strategies because they are not interested in traders who are profitable in the long term, as these brokers often take the opposite side of trades against them. I believe dYdX should focus on strategies that seek out professional and sustainable traders for the long term and that are more capital efficient

There are many successful examples of Trader Incubators. The technical challenge would be how to copy these traders or how to assign them capital without allowing them to withdraw it. From Crypto Plaza/Dragon Stake, we could present an alternative to the trading competitions currently held at dYdX.