

2.0 Fundamental

Prime Rating Report V2.0

Protocol: Liquity (LQTY & LUSD)

Version: V1

Previous Report: None

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Instructions

Please go to files and make a copy of this template.

Fill in all questions with a written explainer, any relevant links and score per variable. Insert the scores in the scorecard at the end of the report. Please follow the process as laid out in the Medium announcement and submit the report through the form.

Please include your sources into the text (as a link), so others can follow your trail of thought.

1. Value Proposition

The Value Proposition section describes the value a protocol delivers to its users. Based on the proportion of the problem the protocol aims to solve and the potential of the protocol to effectively solve the problem - better than other industry solutions - a Value Proposition rating is created.

a) Novelty of the solution (15 points)

This score evaluates the novelty (uniqueness) of the protocol. Has the protocol introduced any new innovations that help solve user's problems more efficiently? Is the project a fork? To what extent did they copy/fork the original?

Answer: Liquity is a stablecoin project which differentiates itself by having no governance. The protocol is launched with one collateral type (ETH) and that's it. The system from here on out has to work algorithmically. Besides taking away governance, it has 0% interest rates. Instead it only charges borrow and redemption fees, which change with market conditions, increasing and decreasing to guide demand towards the peg. In its essence, stablecoins are not new, and algorithmic stablecoins have been tried plenty. The code is not forked and taking out the governance part was not their first idea, but is one of the first iterations that is live.

Score: 7

b) Market fit/demand (15 points)

This score evaluates the degree to which the protocol satisfies a strong market demand. The market fit evaluates if the protocol is able to satisfy the needs of a specific market (can also be measured by user adoption/ #of users). To what extent has the protocol proven to meet the demand of a specific market? Is the timing of the product right for the market? Is the protocol targeting the right market?

Answer: Stablecoins are a huge part of DeFi now. Liquity took a while to launch, and therefore is not first in the game, by far. It can be considered one of many fighting for the same demand. When you look at [stablecoin metrics](#), LUSD is dwarfed by virtually all other stablecoins out. After the recent crash of 19th of May, LUSD lost its peg sharply, and this was countered by a clear marketing effort, with Liquity being positively mentioned in Bankless, DeFi llama and other outlets. They are also ramping up their integrations. So it might not be a lost cause. However, before it even cracks the top 5 stablecoins, it has a lot of work to do.

Score: 5

c) Target market size? (10 points)

The target market size evaluates the current and future size of the problem the protocol is aiming to solve. The category of the Open Finance solution can be used as a reference to the target market (for example: Lending). Because Open Finance is by definition global, the global market for a specific problem equals the target market size.

Answer: Stablecoins are a huge market, and show no signs of stopping. Their numbers speak for themselves, and are so widely known to be successful, I do not even need to add sources.

Score: 10

d) Competitiveness within market sector(s) (10 points)

This score evaluates the competitiveness of the protocol within the market sector(s) it operates in. This score offers a relative comparison of the protocol and other protocols operating in the same market sector(s).

Answer: Competition within the stablecoin market is murderous. New algorithmic stablecoins are launched every month and the top three (USDT, USDC and BUSD) [are high above](#) all others. Taking out centralized tokens, LUSD still is not even close to the numbers the others do.

Score: 2

e) Integrations & Partnerships (15 points)

Due to crypto's open-source nature, the code of most protocols can easily be forked. This score represents a piece of "unforkable value". Some indicators to look at are the number of applications built on top of the protocol (vertical integration), other entities integrating the protocol's services (horizontal integration) or the number of relevant partnerships (be careful of logo collections/ partnerships without much purpose).

Answer: Even though LUSD is a low level stablecoin when it comes to volumes, Liquity is trying to make up for this with its integrations. Just the [last two weeks](#) included 4 of them. Besides these announcements of integrations, they have an [impressive list](#) of frontend hosts, many of which are run by other DeFi projects. LUSD is nowhere near as ubiquitous as DAI or USDC within DeFi are, but it is making clear efforts to get there.

Score: 11

2. Tokenomics

The Tokenomics section of the review assesses the function of a protocol's token. This includes the token distribution, functionalities of the token, the ability of the token to incentivize positive behavior in the protocol, and the ability of the token to capture a portion of the value created.

a) Is the token sufficiently distributed? (15 points)

The token distribution can be an indicator of a healthy protocol. When the protocol tokens are widely distributed among different stakeholder groups and contributors, this genuinely improves the coordinating capability of the token and strengthens the resiliency of the protocol. Was the initial distribution balanced between relevant stakeholders? Are the tokens distributed over sufficient participants (10, 25, 100 largest addresses)?

Answer: From their [blog](#) (25-3-2021):

"100,000,000 LQTY tokens will be minted at genesis and will be allocated as follows:

- 1. 35.3% to the Liquity Community. 32,000,000 LQTY will be allocated to the LQTY rewards pool. These tokens are earned through Stability Pool deposits and will be rewarded by the protocol to frontends and Stability Providers. 1,333,333 LQTY will be allocated to LPs of the LUSD:ETH Uniswap pool. These tokens are earned by staking LUSD:ETH Uniswap LP tokens and will be distributed by the protocol over the course of 6 weeks. 2,000,000 LQTY will be allocated in the form of a Community Reserve. These tokens are earmarked from the Liquity AG endowment and will be used to fund grants, hackathons, events, and other community-focused efforts.*
- 2. 23.7% to Team and Advisors. 23,664,633 LQTY have been allocated to current (and future) Liquity AG employees and advisors. All LQTY in this category are under a 1 year lockup and are 1/4 vested after 1 year of engagement, then 1/36 every month after.*
- 3. 33.9% to Investors. 33,902,679 LQTY have been allocated to Liquity's early investors who supported our vision and provided the runway necessary for us to succeed long term. All LQTY in this category are under a 1 year lockup.*
- 4. 6.1% to Liquity AG Endowment. 6,063,988 LQTY have been allocated to Liquity AG for use by the company. These tokens are subject to a 1 year lockup.*
- 5. 1% to Service Providers. 1,035,367 LQTY have been allocated to service providers who helped Liquity in various ways before launch. These tokens are subject to a 1 year lockup."*

First reaction is, wow, that is a lot of tokens for team and advisors (63.7%) for a project that supposedly needs no more development, or at least, can't be upgraded. Of course they are still involved with guiding, integrations etc. but is it a good distribution? Liquity has no governance, so in that sense, LQTY is only meant as a revenue sharing token. And most of the revenue will now go to the

team and investors (they hold most of the LQTY that can be staked to earn it). In a traditional sense, this is very reasonable. For now their tokens are locked in vesting schedules. When we look at current holder numbers, there are [4839 holders](#). The token holder supply distribution is not a clear cut case on Etherscan, since the top 30 are framed as contracts (with the top three having 38, 27 and 9.4% respectively). When we look at LUSD, it has fewer holders (you would think otherwise), namely [2491](#). The founder came out [saying](#) around 90% of LUSD is in the stability fund, also saying a couple whales were mostly behind this. All in all far off a perfect DeFi distribution, but due to the nature of the tokenomics, perhaps forgivable.

Score: 6

b) What is the extent of the token's capabilities? (10 points)

Is the token useful within the protocol? Does the token allow the holders to participate in governance or influence the protocol in any way? Does it serve any other purposes?

Answer: LQTY can be [staked](#) to earn revenue made from LUSD minting and redeeming. There are no governance rights, since there is no governance. LQTY is not used within the Stability Fund and staking it has no risks. Which makes it an easy buck for the team and investors when the lock up ends.

Score: 4

c) Is the issuance/distribution model able to improve the coordination of the protocol? (10 points)

To what extent does the issuance of the token support the advancement and function of the protocol? Are the tokens justifiably being issued? Does the issuance model incentivize the right behavior? Are all relevant stakeholders benefiting from the issuance model?

Answer: LQTY is [distributed](#) towards Uniswap LPs, LUSD depositors in the Stability Fund and through grants. The last part is decided upon by Liquity AG, since there is no governance to vote upon the treasury. There are no dev mining, contribution rewards or general LUSD interaction incentives.

Score: 3

d) Is the value capture model able to accrue and distribute value? (10 points)

A value accrual and distribution mechanism can help improve the utility of a token and its ability to be used as an effective coordination mechanism. Does the protocol have mechanisms to distribute some of the value created to the token holders?

Answer: LQTY can be [staked](#) to earn revenue made from LUSD minting and redeeming. This will just go to the stakers, and will not in any way affect future protocol development.

Score: 2

e) Is the token sufficiently liquid to enable active use and trade? (5 points)

Is the token widely available and is there sufficient liquidity available to facilitate all protocol functionalities?

Answer: LQTY has a [\\$23M](#) market cap with \$370k in 24 hour volume. It is available on Uniswap, Quickswap, Curve and Poloniex. LUSD has a [\\$700M](#) market cap and only \$5M in 24 hour trading. With these numbers, it scores quite low.

Score: 2

f) Are there any extrinsic productivity use cases for the token? (10 points)

Besides the protocol's value distribution model as described in 2. d), can the token be used productively on other protocols (e.g. as collateral, for lending, LPing, yield farming, etc.)?

Answer: As described earlier in the integration section, Liquity is actively trying to be integrated with other protocols. Bancor, Curve, Wasabix and similar projects. Most of this is related to yield.

Score: 5

3. Team

The Team section describes the quality of the team behind the protocol. The current version of Prime Rating favors teams that are publicly identifiable. In the case of an anon team, the track record of the specific anons involved can be taken into account

a) Is the team credible and public? (15 points)

Are the identities of the core contributors and team publicly identified? In the case of anon team members, is there any way to track their background/record?

Answer: The company that launched the contracts is publicly known, with address and all. Liquity AG and its team are featured on the [website](#). The team and its advisors are a mixed bag, the founder comes from DFINITY, which can be considered a pump and dump project with vaporware. This might give us some insight on why Liquity's token distribution was so skewed towards the team and investors. Another team member comes from Stellar, which has a [iffy](#) history. But we also have people from Aragon (with its own share of [trouble](#), sure, but still reputable) and Makerdao.

Score: 7

b) Does the team have relevant experience? (10 points)

Are there any documents or trails available to showcase the track record of the team? Do the team members have relevant backgrounds and skill sets?

Answer: As aforementioned, the team does come from within the crypto space and even managed to get an ex-Makerdao (its competitor) on board. If they brought the right set of experience, is to be debated.

Score: 7

c) Does the team participate and help shape the public debate? (5 points)

To what extent do the protocol contributors participate in the public debate around open finance? Are the team members giving presentations, sharing their thoughts and opinions, and do they help raise the collective intelligence of the industry?

Answer: The team is around in the space but is not well known.

Score: 3

d) Is the team able to effectively attract and coordinate resources? (10 points)

How effective is the team at attracting and coordinating resources for the benefit of the protocol? Has the team raised sufficient funding or are there mechanisms in place to attract resources when needed?

Answer: [From EthHub](#) (28-9-2020):

"Raised \$2.4M. The round was led by [Polychain Capital](#), with follow on investments from [a_capital](#), [Lemniscap](#), [1kx](#), [DFINITY Ecosystem Fund](#), [Robot Ventures](#) ([Robert Leshner](#)), and [Alex Pack](#)."

Due to the low level of work the team has ahead (launched and well, no governance adjustments, etc.) and their large share of the token distribution, it can be concluded that the team is funded properly. If this question was about the community, it would have a different answer.

Score: 10

4. Governance

The Governance section evaluates how the protocol is governed and who the governors are. The different governance functionalities and processes are evaluated to determine to what extent the Protocol will be able to self-govern in a way that ensures the development of the protocols while respecting the needs of all current and future stakeholders.

a) Admin Keys (20 points)

Admin Keys allow some critical functionalities of a protocol to be controlled by an admin. This allows the developers to react to potential bugs, but also creates a risk as the developers could potentially misuse the admin keys to exploit the protocol. Does the protocol have admin keys and how are they managed?

Answer: This question assumes the existence of admin keys. And although there are some that were used for deploying, the team stresses it has no control whatsoever. [From DeFi Safety](#) (16-6-2021):

"Admin controls can be found [here](#). All [contracts](#) are [described](#) as immutable. All contracts are automated and immutable upon launch, but no evidence of Pause Control or similar function."

From their [docs](#) (9-7-2021):

"Liquity contracts have no admin keys and will be accessible via multiple interfaces hosted by different [Frontend Operators](#), making it censorship resistant. Liquity has no admin key, and nobody can alter the rules of the system in any way. The smart contract code is completely immutable."

They deserve the highest score here.

Score: 20

b) Extent of Governance capabilities (15 points)

Distributed governance allows the token holders to participate in the governance of open finance protocols. How much influence does the governance mechanism have? Are the votes affecting on-chain changes or do they function solely as signals to the team?

Answer: This is difficult to evaluate. The project has no governance, on purpose. There is a [6.1%](#) allocation towards Liquity AG to distribute through grants and such. Perhaps this could have been done through on-chain governance instead. But it is clear the company did not intend to do any of that sort.

Score: x

c) Active Governance contributors (5 points)

Governance is a process that can be rather resource-intensive if executed well. To ensure good governance is practiced by the protocol, it's important to have a sufficient number of governors allocate resources to the governance process of the protocol. How many individuals participate in the debate around the protocol? How active are voters?

Answer:

Score: x

d) Governance technology/infrastructure (10 points)

The Governance infrastructure relates to the technology, software, and models used by the protocol's

governance. Does the protocol have a reliable and usable voting mechanism? Are there channels for governance debate? Is there sufficient documentation available?

Answer:

Score: x

e) Robustness of Governance process (10 points)

This score requires documentation specifically on the governance process that sets the basic framework in terms of agreements, norms, and language for governing the protocol and to create social consensus. Does the protocol have a formal governance process? How robust is the governance process and does it promote good governance?

Answer:

Score: x

5. Regulatory

The Regulatory section describes the extent and quality of the regulatory environment that affects the Protocol. To be able to guarantee functionality, security, and legality the protocol should comply with regulatory requirements, or limit itself to facilitating services to users who are willing to operate outside of the traditional regulatory environment.

a) Does the protocol have any legal accountability? (15 points)

Does the protocol have any form of legal accountability? Can users and partners hold the protocol accountable in case of a breach of the agreement?

Answer: The company behind Liquity is Liquity AG, it however goes the [extra](#) mile to [tell](#) everyone that they are NOT responsible for anything related to the contracts.

Score: 0

b) What is the quality of the legal jurisdiction? (10 points)

If the protocol has a legal entity, what is the quality of the jurisdiction the entity is established in? Will the jurisdiction be able to facilitate the legal framework for the protocol to expand while remaining accountable.

Answer: If push comes to shove, then Liquity AQ is based in Zug, [Switzerland](#).

Score: 10

Scorecard

1. Value Proposition	Points
a) Novelty of the solution	7 / 15
b) Market fit/demand	5 / 15
c) Target Market Size	10 / 10
d) Competitiveness within market sector(s)	2 / 10
e) Integrations & Partnerships	11 / 15
Total Points - Value Proposition	35 / 65
2. Tokenomics	Points
a) Is the token sufficiently distributed?	6 / 15
b) What is the extent of the token's capabilities?	4 / 10
c) Is the issuance model able to improve the coordination of the protocol?	3 / 10
d) Is the value capture model able to accrue and distribute value?	2 / 10
e) Is the token sufficiently liquid to enable active use and trade?	2 / 5
f) Are there any extrinsic productivity use cases?	5 / 10
Total Points - Tokenomics	22 / 60
3. Team	Points
a) Is the team credible and public? (No, Partly, Yes & Anon , Yes & Public)	7 / 15
b) Does the team have relevant experience?	7 / 10
c) Does the team participate and help shape the public debate?	3 / 5
d) Is the team able to effectively attract and coordinate resources?	10 / 10
Total Points - Team	27 / 40
4. Governance	Points
a) Admin Keys	20 / 20
b) Extent of Governance capabilities	X / 15
c) Active Governance contributors	X / 5
d) Robustness of Governance process	X / 10
e) Governance infrastructure	X / 10
Total Points - Governance	20 / 20

5. Regulatory	Points
a) Does the protocol have any legal accountability?	0 / 15
b) What is the quality of the legal jurisdiction?	10 / 10
Total Points - Regulatory	10 / 25
Total	114 / 250

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