

## 2.0 Fundamental

### Prime Rating Report V2.0

**Protocol: Compound**

**Version: 2**

**Previous Report:** [Link to previous report](#)

**Date: June 13, 2021**

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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.

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## 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:** Compound is one of the first and [leading](#) DeFi protocols that has introduced many novelties and innovations to the ecosystem. Compound was the first protocol offering permissionless lending pools, where users can earn an interest rate on their deposits and borrowers can borrow capital via over-collateralization.

Compound can also be credited as the first protocol offering liquidity incentives (better known as yield farming), thus kick-starting DeFi summer 2020. Furthermore, they created an on-chain [governance module \(governor alpha\)](#) which has been forked by many other protocols and developed a second version [governor bravo](#). With the advent of side-chains and L2 solutions, Compound is again one of the first-movers (although in a different direction than most) by developing their own semi-permissionless [blockchain solution](#), which aims to solve interoperability and scaling issues, including their own interest-bearing stable coin solution CASH.

In summary, Compound is one of the main pillars of DeFi and they have introduced many important money legos to the ecosystem.

**Score: 15**

## **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:** Compound used to be the leading lending/borrowing protocol in DeFi for most of 2020 (closely followed by Aave). However, with the introduction of their own liquidity incentives, Aave has surpassed Compound in terms of [TVL](#). However, the two projects (together with Maker) are still neck-to-neck in terms of the more relevant metric "[outstanding loans](#)", and are leading the market by a large margin.

**Score: 15**

## **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:** The market for lending and borrowing is already a billion-dollar market that is expected to grow substantially with more adaptation and better access to DeFi services. In comparison, the global lending market in TradFi is worth [trillions](#).

**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:** As indicated above, Compound is one of the leading protocols in DeFi and used to be the benchmark in the lending market segment for most of 2020. At the time of writing, however, Aave has positioned itself as the [market leader](#) in terms of TVL and loans, although by a small margin. On the other hand, Compound still has over 5-times more users than Aave.

**Score: 9**

## 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:** As mentioned in the beginning, Compound is one of the major DeFi money legos that several other protocols have build upon (e.g. [InstaDapp](#), [yearn.finance](#), [Barnbridge](#) or Index Coop's [FLI products](#)) and integrated with (e.g. Zerion and Zapper).

Compound is not known for having many official partnerships with other DeFi protocols. They do, however, have a few mentionable [partnerships](#) with companies active in the wider crypto ecosystem (e.g. Coinbase Custody, BitGo and Ledger).

**Score: 13**

## 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:** Although Compound does have a high number of token holders (over [170k](#) at the time of writing), most of the tokens are in the hands of a few individuals/ groups. The [initial token distribution](#) is rather skewed towards a small group of people, with over 46% of all tokens going to investors and the founding team. Just a little over 50% were reserved for the community, with a majority going to users of the protocol via liquidity incentives (~42%).

Two researchers from the University of Basel found that the top 50 wallets hold [86.75%](#) of all COMP tokens. Further, they used the GINI coefficient as a proxy-measure for decentralization, and Compound (with over 90%) had one of the worst decentralization ratios. It has to be said though, that this study is from September 2020, and things might look a little different in the meantime. Nonetheless, the initial token distribution won't change.

**Score: 7**

## 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:** The COMP token is a governance token first and foremost. It is used to participate in governance votes, and in order to be able to submit a proposal, one must have 65k COMP tokens (used to be 100k, but was changed with [proposal 052](#)). An address can also lock 100 COMP to create an [Autonomous Proposal](#), which then needs to get 65k delegated to go live for voting.

Furthermore, the token is used to incentivize usage of the protocol. As mentioned earlier, Compound was the first protocol introducing a liquidity mining program to reward lenders and borrowers with the native governance token.

The token can be used within the protocol itself to earn interest. However, the protocol does not have a revenue stream yet. Compound only has a reserve factor, subtracting a percentage of the interests paid, into a reserve fund to protect against borrower default or liquidation malfunction.

**Score: 7**

## 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:** While some tokens were allocated (and vested) to early investors and the team, 42% of all tokens are reserved to incentivize usage of the protocol.

As mentioned above, the token is required to participate in governance. 7.75% of the tokens are reserved for community contributors. However, contributing to Compound requires technical skills or very deep knowledge of the space, excluding most average users, but it seems to have attracted some very skilled contributors.. Contributor Grants need to be approved by governance ([example](#)).

**Score: 9**

## 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:** There is a value accrual mechanism (reserve factor) which is similar to a fee. At the time of writing, the reserve factor for [USDC](#) is 7% for example. And there's currently over 6M in USDC reserves for that market alone. However, Compound does not have a value distribution mechanism, meaning there's no dividend-like function for passive token holders to receive some of the protocol's revenues.

Score: 7

### 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:** Yes, the token is available on most centralized exchanges (e.g. Coinbase, Binance, Kraken, etc.) and has highly liquid pairs on DEXes such as Sushiswap and Uniswap V2 and V3.

Score: 5

### 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:** The COMP token can be used on most major DeFi protocols. For example, it can be deposited on [Maker](#) to borrow Dai, deposited into a [Yearn](#) to earn interests, or put into a liquidity pool on major DEXes.

Score: 9

## 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:** Founder [Rober Leshner](#) and Co-founder [Geoffry Hayes](#) are well-known figures in the DeFi ecosystem. Robert acts as multi-sig holder to other protocols such as Sushiswap or CREAM Finance and has been an investor in several other [projects](#). Thus concluding that they are highly credible individuals. Further, there is a [team page](#) on the website listing all employees of Compound Labs.

**Score: 15**

## **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:** Yes, the team is full of highly capable individuals and that they have the required skills is evident through the success of the protocol.

**Score: 10**

## **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:** Yes, at least founder [Robert Leshner](#) is one of the most active DeFi people on Crypto Twitter and regularly participates in conferences or interviews. Furthermore, he's also very approachable and usually replies on the forum or to DMs quite swiftly.

**Score: 5**

## **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:** The team attracted many reputable VCs such as Coinbase Ventures, a16z, Polychain Capital or BainCapital Ventures.

They also initiated a liquidity incentive program to reward community contributors and usage of the protocol. The protocol has attracted many highly capable people and entities within the DeFi ecosystem to become active participants and contributors to Compound (e.g. [Getty Hill](#), [Monet Supply](#), [Gauntlet](#), [Arr00](#) or University blockchain clubs from [Berkley](#), [Michigan](#) or [MIT](#)).

**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:** As indicated earlier, Governor Bravo is the on-chain governance module used by Compound. In other words, Compound is fully decentralized (technically) and only a governance vote can effectively implement changes to the protocols smart contracts. There's also a 2 day delay before any changes are activated.

From their [docs](#):

"When a governance proposal is created, it enters a 2 day review period, after which voting weights are recorded and voting begins. Voting lasts for 3 days; if a majority, and at least 400,000 votes are cast for the proposal, it is queued in the Timelock, and can be implemented 2 days later. In total, any change to the protocol takes at least one week."

**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:** Through [Governor Bravo](#), participants of Compound governance do have the ability to change or add many updates to the protocol. It's not just a signal to the team, but effective on-chain changes. For instance update smart contract parameters, adding new markets (i.e. new tokens), changing parameters of the markets, etc. However, in order to create such a proposal, one needs to be able to code in solidity.

**Score: 15**

### 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:** The Discord as well as the forum are full with active discussion and community members. However, due to the high level of technical skills required to create changes, effective contributions are limited to a few people.

**Score: 4**

## 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:** As mentioned a few times already, Compound built their own infrastructure (previously governor alpha, now governor bravo), which were copied by many other protocols. Furthermore, there is an active Discord chat and the [forum](#) is used to discuss proposals and potential improvements to the protocol.

**Score: 10**

## 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:** The process is clearly documented and very robust. Compound offers some [guidelines](#) on their website here, and there's also an [article](#) explaining how to contribute.

**Score: 10**

# 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:** Yes, Compound Labs Inc. which is one of the main token holders and the creator of the protocol is a company [registered](#) in the United States in San Francisco. Public information about the company (e.g. [SEC report](#)) is available and easy to find through a Google search.

**Score: 15**

## **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:** Compound Labs Inc is a legal entity registered in San Francisco, United States.

**Score: 10**

## Scorecard

1. Value Proposition	Points
a) Novelty of the solution	15 / 15
b) Market fit/demand	15 / 15
c) Target Market Size	10 / 10
d) Competitiveness within market sector(s)	9 / 10
e) Integrations & Partnerships	13 / 15
<b>Total Points - Value Proposition</b>	<b>62 / 65</b>
2. Tokenomics	Points
a) Is the token sufficiently distributed?	7 / 15
b) What is the extent of the token's capabilities?	7 / 10
c) Is the issuance model able to improve the coordination of the protocol?	9 / 10
d) Is the value capture model able to accrue and distribute value?	7 / 10
e) Is the token sufficiently liquid to enable active use and trade?	5 / 5
f) Are there any extrinsic productivity use cases?	9 / 10
<b>Total Points - Tokenomics</b>	<b>44 / 60</b>
3. Team	Points
a) Is the team credible and public? (No, Partly, Yes & Anon , Yes & Public)	15 / 15
b) Does the team have relevant experience?	10 / 10
c) Does the team participate and help shape the public debate?	5 / 5
d) Is the team able to effectively attract and coordinate resources?	10 / 10
<b>Total Points - Team</b>	<b>40 / 40</b>
4. Governance	Points
a) Admin Keys	20 / 20
b) Extent of Governance capabilities	15 / 15
c) Active Governance contributors	4 / 5
d) Robustness of Governance process	10 / 10
e) Governance infrastructure	10 / 10
<b>Total Points - Governance</b>	<b>59 / 60</b>

<b>5. Regulatory</b>	<b>Points</b>
a) Does the protocol have any legal accountability?	<b>15 / 15</b>
b) What is the quality of the legal jurisdiction?	<b>10 / 10</b>
<b>Total Points - Regulatory</b>	<b>25 / 25</b>
<b>Total</b>	<b>230 / 250</b>

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