# MULTICOIN CAPITAL

# HUOBI TOKEN ($HT)
## Analysis and Valuation

By Mable Jiang & Spencer Applebaum

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# Executive Summary

Exchange tokens are currently the most interesting sector in crypto because they sit at the intersection of where there is demand today and where there will be opportunities tomorrow. We have previously expressed a thesis that exchange tokens are the best way to get exposure to open finance and that there is tremendous growth potential. There are significant barriers to scaling which give incumbents a clear competitive advantage. This has been confirmed by the horizontal integration of products by the biggest exchanges. We previously saw pure-play, specialty exchanges focused on a specific subset of derivatives (BitMEX, Deribit, CME) but have now seen futures integrated into the existing exchanges with great success (Huobi, OKEx, and Binance have all usurped BitMEX's dominance in futures).

Exchanges are also able to be nimble with token economics and introduce new use cases to their tokens over time. We've seen this with virtually all exchange operators, whereby they add new products and integrations to offer token holders advantages over other users. Some examples include Binance's Launchpad offering and Huobi's Lock & Mining program.

We track the exchange token market closely (as noted in our Binance reports here and here; we also still hold a large long BNB position), and through our ongoing analysis of the space we noticed that there is a divergence between the fundamentals of Huobi and the current valuation of Huobi Token ($HT). After digging deeper, we believe that Huobi is misunderstood by the market and that $HT is undervalued at current prices, primarily because of information asymmetries that exist between the East and the West.

We are long $HT for a number of reasons, and because there are several near-term, compelling catalysts:

1. Huobi is the best way to get broad exposure to increased blockchain and crypto excitement in China, which is now a national priority. Huobi OTC is the most liquid among all the CNY on/off ramp exchanges and is the most recognized brand for new Chinese users to get exposure to Bitcoin and other major cryptocurrencies.

2. Contrary to a widely held Western opinion, Huobi's volumes today are in fact very real, and they custody more BTC than every other exchange except Coinbase. Furthermore, Huobi is ranked second globally in spot volume (behind Binance), second in derivatives volume (behind Binance Futures), and second in derivatives open interest (behind BitMEX).

3. Huobi appears to be making a commitment toward more transparency, which could help close the information asymmetry between East and West.

4. Huobi has expanded their product offerings significantly in the past two years, most notably into derivatives trading (for details see the section below). We expect Huobi to continue

innovating and adding other types of financial products, including options, staking, etc.

5. Huobi recently open sourced the code for Huobi Chain, an initiative backed by the world-class team at Nervos and will be the first “compliant” exchange-chain in the world.

6. $HT currently has the highest buyback ratio of any exchange token on the market at 17.8%. In fact, $HT’s buyback ratio is 4.4x higher than the exchange token industry average. We believe that it is mispriced and the buyback ratio should trade closer in-line with Huobi’s peers. For example, based on LTM burn metrics, that would imply a $HT market cap of $4.3B, representing as much as 345% upside from today’s price.

In this report we explore the current operations of Huobi, detail the history of its products and operations, its tight-knit relationship with the government, and its trading volume (with a specific focus on its peer-to-peer OTC trading and expiry and perpetual contracts). We also explore Huobi’s recent effort to become a financial infrastructure provider in China by building Huobi Chain, which uses Nervos Muta SDK as its technology provider. With the fundamental support of steady growing trading volumes, attractive token economics, relative mispricing by the market, and a perceived blessing by the Chinese government, we believe that $HT is one of the best risk-adjusted investment opportunities in the cryptocurrency space.

# An Overview of Huobi

## HUOBI’S HISTORY

Huobi was one of the first cryptocurrency exchanges to launch in China. The first syllable “Huo” means fire in Chinese, and “bi” means token.

Huobi has an eventful history, but one not well known. Like a phoenix, it battled through trial by fire and emerged from the ashes stronger. It survived multiple regulatory crackdowns, including the infamous “September 4th” crackdown by the Chinese government in 2017 and the November 22, 2019 probe by the People’s Bank of China (PBoC) into Chinese crypto exchanges.

Since then, Huobi has become one of the largest and most successful crypto exchanges in the world, with the vast majority of its users in China. It allows traders to easily swap digital assets and trade crypto derivatives.

The company, Huobi Group, was founded in early 2013 by Leon Li, who is still the CEO today. He launched the first version of the trading platform on September 1, 2013, which became China’s largest digital currency exchange by December 2013, and by mid-2014—directly following the spectacular collapse of Mt. Gox— amassed >60% global market share of Bitcoin trading volume (see chart 2). During this time, Huobi was the most liquid exchange in the world.

In November 2013, during Huobi's explosive rise, the company raised an angel round from Dai Zhikang and Zhen Fund. Huobi then raised a $10M Series A round in April 2014 from Sequoia China. The exchange continued to expand rapidly, reaching 300 employees by 2017.

In January 2017, following a surge of crypto trading in the country (RMB exchanges accounted for 98% of global Bitcoin volume in parts of 2016), the Chinese government cracked down on crypto exchanges across the country. People's Bank of China (PBoC) officials met with management teams of all of the major crypto companies in China. They pressured the two leading exchanges—OKCoin and Huobi—to enforce stricter anti-money laundering rules on customers. Per chart 1, global trading volume was dominated by CNY pairs at the time:

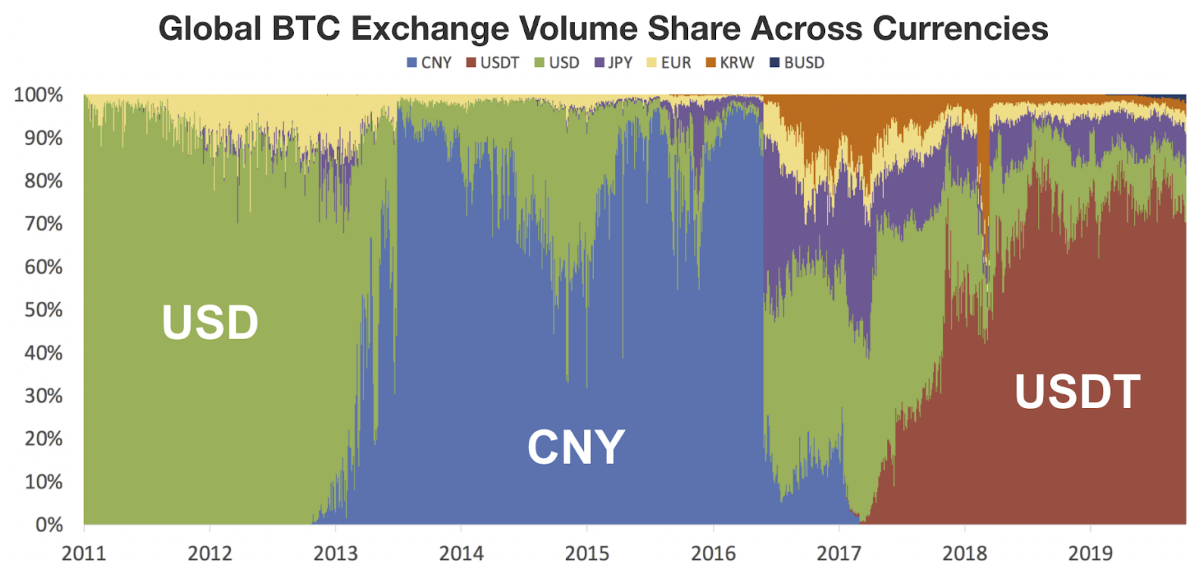


*Chart 1: Source - [CryptoCompare]*

In response to the action, both OKCoin and Huobi halted withdrawals; BTC China, the 3rd-largest exchange operating at the time, also announced a 72-hour review period for all withdrawals. Chart 2 below clearly illustrates the impact of the enforcement action on the Chinese exchanges. Global market share of RMB exchanges fell from 96% in January 2017 to 24% in February 2017.

Then, on September 4, 2017, the Chinese government released the announcement that it would ban Bitcoin exchanges directly following its ban on ICOs. Three days later, BTC China announced that it would cease operations at the end of the month. Huobi and OKCoin announced that they would halt trading by the end of October. This ban is referred to as the "September 4th Event."

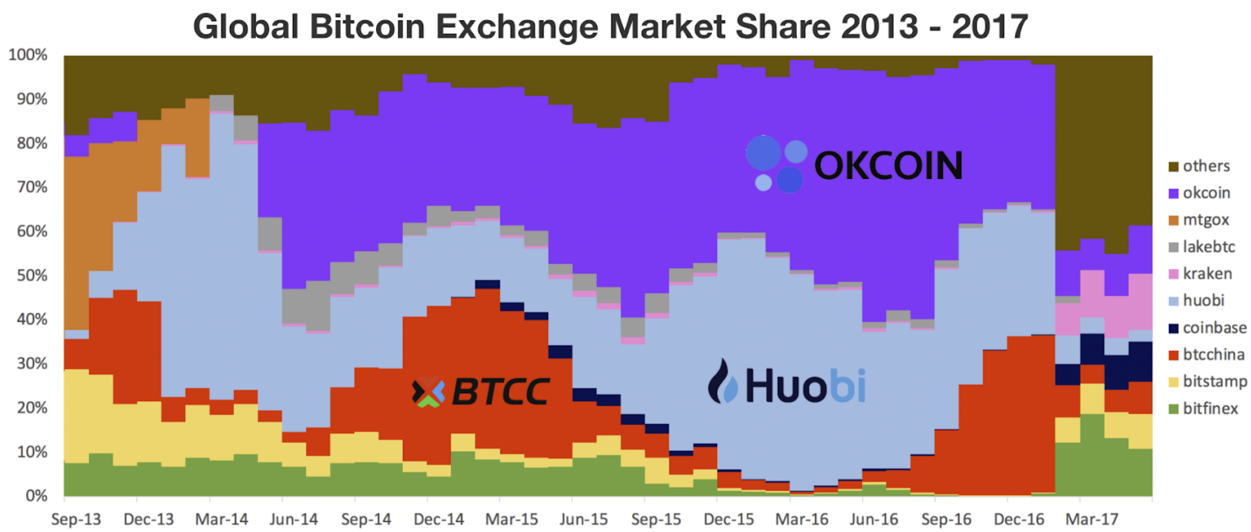


*Chart 2: Source - [Bitcoinity Data]*

Up until the "September 4th Event," Huobi only offered fiatRMB-to-crypto services. The ban forced Huobi to adjust its strategy and pivot into a "global institution of digital asset and financial technology," a (admittedly loose at the time) vision set by Leon Li, the CEO of Huobi Group. In November 2017, Huobi launched a peer-to-peer (P2P), over-the-counter (OTC) trading platform (instead of fiat-to-crypto trading on the exchange itself). Both this peer-to-peer OTC platform and the crypto-to-crypto spot trading platform rolled up under Huobi Pro, which is now named Huobi Global.


*Chart 3: Source - [Huobi Group]*

At the same time, Huobi actively attained licenses in different jurisdictions, such as Japan, Gibraltar, and Thailand, and acquired an offshore entity in Hong Kong, to become compliant in several regions globally. While Huobi Global was able to keep its technology stack in China, it opened offices in Seoul, Singapore, and Tokyo by the end of 2017. Over the next three years, Huobi went on to launch seven new business lines distributed all around the world. Instead of allowing a single door to close on them and end their business, they chose to open other doors.

Still, with China as its primary market, Huobi understands the importance of being close with local regulators. In September 2018, Huobi China (separate from Huobi Global) moved its headquarters to "Hainan Resort Software Community," to which the government later issued a "Blockchain Experiment District of the Hainan Free Trade Zone" license. As a founding co-organizer of the Hainan Free Trade Zone, Huobi Group claimed that it aimed to help China "build a global financial infrastructure with blockchain and digital finance" through Huobi Chain and Huobi China, a subsidiary that positioned itself as an one-stop platform to offer blockchain industry consulting and training services to Chinese enterprises and the local government.

The relationship maintenance was clearly well received. In their seminal Financial Stability Report (2019), the PBoC noted that "*173 Chinese virtual-currency trading and token issuing platforms have all exited without risk*." Yet, Huobi was one of the few platforms (including Binance and OKEx) that managed to continue operating in China and serving traders, including Chinese traders.

We highlight the above stories because they not only show that Huobi is resilient and flexible in the face of adversity, but also because it has managed to maintain its foothold before regulators formally legitimize its existence, just like how Alipay survived for 8 years before getting an official license to operate.

Today, Huobi Group operates a diversified global business:

1. *Huobi Global* - Spot / Margin / Huobi Derivatives Market / OTC
2. *Huobi Pool* - Hash market / PoW pool / Staking service
3. *Huobi OTC* - China's leading P2P OTC onboarding application
4. *Huobi Chain* - Layer 1 chain that will use Huobi Token as the native staking asset
5. *Huobi Cloud* - White label tech solution that allows entrepreneurs to launch localized exchanges across the globe; Argentina, Russia, and Thailand.
6. *Huobi Capital* - The investment arm of Huobi Group
7. *Huobi China* - A research and development group that assists enterprise companies in China with blockchain

## HUOBI TOKEN ($HT) OVERVIEW

In February 2018, Huobi introduced Huobi Token ($HT).

300M $HT were initially exchanged for "Huobi Point Cards," prepaid cards that let people trade on Huobi with discounts. Huobi management's intention with $HT was to share the growth of Huobi exchange with their customers. During the first two quarters after launching, Huobi used 20% of revenues from the operation of Huobi Global to buy back $HT, and these $HT were injected into an insurance fund for emergencies. By Q3 2018, the insurance fund had accumulated close to 50M $HT.

In Q3 2018, Huobi changed its policy to buy back $HT with 20% of its quarterly revenue and airdrop these $HT to existing token holders, effectively giving buyers a lower implied price per token. Then, in Q4 2018, the community expressed their willingness to change the $HT rule from an airdrop to a burn. Based on the community voting results, in Q1 2019 Huobi changed its operation to use its quarterly revenue, which expanded because they added income from futures trading, to buy back and burn $HT. The buyback-and-burn rule was well received as it created deflationary pressure. Furthermore, because of the potential risk of the team's vested $HT unlocking (creating downward price pressure), in Q1 2020 Huobi changed the rule to use 15% of their revenue to buy back and burn the circulating $HT, and rely on the team's vested $HT for the other 5%. Other unvested team tokens will no longer flow into the secondary market.

$HT can be used for discounts on Huobi Global, voting on new project listings, and more. Additionally, Huobi will soon move $HT from Ethereum to Huobi Chain. Below is an overview of $HT's primary use cases:

1. **Token Burn** - 20% of all revenues generated on Huobi and Huobi derivatives are used for an $HT burn each month. Of the 20%, 15% is from a buyback from the liquid float and 5% is from team treasury tokens. Thus far, Huobi has bought and burned 52.9M $HT tokens over 8 quarters since they launched the repurchase program. Additionally, they've burned 1.6M $HT from their FastTrack program (token listing fee) and 274K $HT from their Prime program (IEO platform).

2. **Discounted fees** - Customers who hold a certain amount of $HT are eligible to receive discounted fees on the Huobi exchange, including a discount on margin loan interest and spot and derivatives fees. The more $HT an investor holds, the higher discount the investor receives. This increases demand for Huobi tokens and provides a nice velocity sink.

3. **Huobi Prime** - Huobi previously had a platform called Huobi Prime, that utilized $HT. All project tokens were purchased using $HT. Generally speaking, all users needed was a fully-verified Huobi Global account and an average daily holding of 500 or more Huobi Tokens in the 30 days leading up to a launch.

4. **Lock & Mining** - Users who lock $HT tokens receive daily Huobi Pool Token ($HPT) airdrops. Once users have $HPT, they're then entitled to real cash flows from Huobi Pool PoS operations, including tokens such as EOS, TRX, and ATOM. Specific airdrop quantity depends on lock option period selected, quantity locked, and Huobi Pool's mining hash power and daily float.

   Huobi Pool currently has 5% global market share of Bitcoin mining. On top of that, Huobi Pool's y/y revenues grew 218% from $2.5M in 2018 to $6.3M in 2019 (in large part to PoS and

DPoS operations, likely leveraging Huobi exchange deposits).

5. **Collateral** - Users can post $HT as collateral for margin trading and futures trading. In addition, OTC sellers are allowed to deposit $HT as their margin to provide P2P OTC services on Huobi's platform.

6. **Governance** - Token holders can use their $HT to vote for projects to be directly listed through FastTrack.

7. **Gas for Huobi Chain** - HT will power Huobi's new native smart contract blockchain.

8. **External use cases** - In addition to the in-platform use cases, users can also use $HT to pay with external ecosystem partners. This is similar to other exchange tokens. A few examples:
    a. Travala.com: a travel booking site
    b. FomoHunt: an e-commerce and crypto news platform (users can buy NFT arts, event tickets, garment, and hardware)
    c. C5game: In-game assets exchange platform

## HUOBI'S POSITION IN CHINA

Huobi is currently the most dominant exchange in China (along with OKEx) — a country that is emphatically embracing blockchain as a national priority, per President Xi's comments in October 2019, the recently announced Blockchain Service Network (BSN), and the forthcoming DC/EP system (discussed more in-depth below). Several factors impact the dominance of an exchange in China, including governmental resources, execution, spot and derivatives trading volume, BTC/ETH reserves held on exchange, and the management team's vision and corporate strategy. We can clearly see from trading volume and user distribution data, which will be discussed in detail below, that Huobi commands a dominant position in China.

Anyone who has experience running a business in China understands that there are unimaginable complications and nuances in terms of the official policies versus actual enforcement. The Chinese government, since Deng Xiaoping initiated the "Open the Door" policy, has been known for its hand-holding style in terms of managing both the private and public sectors. What does that mean? It means that companies in a nascent private sector will operate cautiously in the gray without clear guidelines from the government, and try to stick around longer than competitors and aim to be blessed by regulators as the industry matures.

Alipay is the quintessential example of this. Alipay operated in the gray for years before getting a license from the government. Now, it is one of the biggest payments platforms in the world in large part because the Chinese government supports them.

Today, Huobi is in this very situation, where the Chinese government has already publicly expressed its interest in embracing blockchain technology, but is still ambiguous about cryptocurrencies (note: despite the government's proclamations about "blockchain, not crypto," the real enforcement is ambivalent).

Local users and observers can easily deduce that Huobi has essentially been "blessed" by regulators in China. Additionally, it's also clear that the Chinese government has progressively softened its stance on blockchain and crypto since President Xi's speech in October 2019:

1. Officials in China's Sichuan province (the mining capital of China) sped up mining legalization (whereas before it was legally gray), and the industry has since been encouraged by a former Chairman of the Securities Regulatory Commission (the Chinese SEC).

2. The Blockchain Service Network, a consortium blockchain project led by the State Information Center, a government agency under the National Development and Reform Commission, recently launched.

3. Development of DC/EP, China's digital fiat currency project, has accelerated. Recently, the media discovered and reported on a screenshot of a beta of the application out in the wild.

4. The Ministry of Education of China recently gave a greenlight to Chengdu University of Information Technology (CUIT) to open China's first blockchain engineering major.

President Xi's remarks opened the floodgates to awareness, investment, and education around blockchain. Giving a green light to the second largest economy in the world and 1+ billion people is tremendously positive for the crypto industry, and the market reacted accordingly. Following the speech it was clear the market was looking to get exposure to the "Long China Crypto" thesis (based on blockchain stock performance in China and the launch of FTX's dragon index). We will discuss China's blockchain initiative in-depth later in this paper.

## HUOBI'S VOLUMES AND MARKET SHARE

In March 2019, Bitwise shared their seminal market infrastructure report with the SEC, claiming that only 10 crypto exchanges have real volumes. Huobi was notably excluded from that list. Since then, we have found that most Western-based audiences ignore Huobi (and thus $HT), believing the exchange's volumes are fake.

Contrary to that belief, recent market activity suggests otherwise. To confirm or disprove these findings we consulted with several trusted counterparties, all of which independently confirmed that Huobi is actually one of the *most* liquid exchanges in crypto. Following discussions with these market participants, we conducted additional research and diligence to further verify these claims, which included:

1. Analyzing Huobi's market share of BTC exchange deposits (BTC under custody), as depicted in Chart 4 below (a strong indicator of real trading volume, or at least a real business). Note that Coinbase has the most BTC under custody (whereas Huobi has the 2nd most of any exchange globally), but Coinbase is not accounted for in the chart below due to the scale of the chart.

2. Examining historical order book depths and futures open interest across Huobi and other major crypto exchanges (both spot and derivatives).

3. Speaking with a wide array of market makers and OTC desks, such as Three Arrows and Kronos Research.

4. Verifying that the company employs more than 1,100 people.

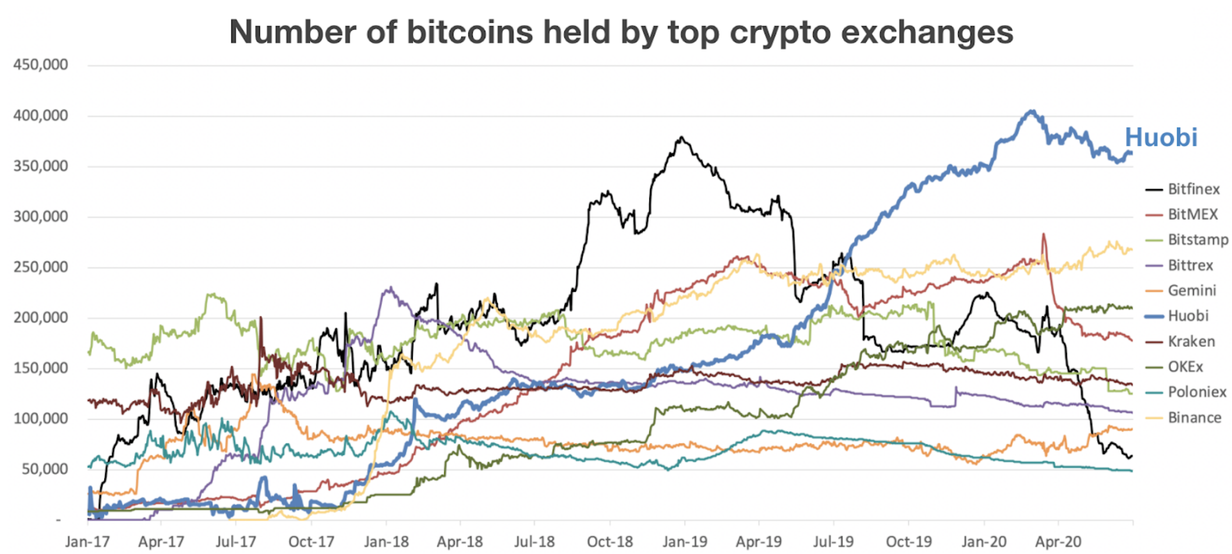


*Chart 4: Source - [Glassnode](#) (Coinbase excluded)*

While it is impossible to completely eliminate the possibility of wash trading from exchange platforms, there is abundant evidence to suggest that Huobi is as liquid as every other top exchange. For example, Huobi has the 3rd highest open interest of any BTC futures exchange. As some knowledgeable people have noted, open interest is harder to fake than volumes.

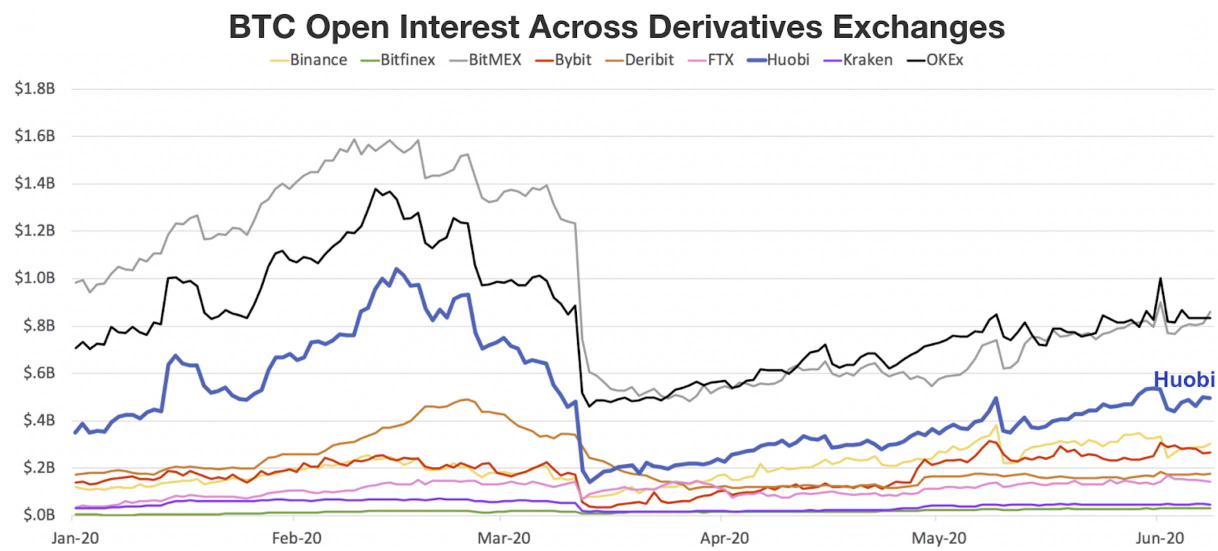


*Chart 5: Source - Skew*

Huobi is the most trusted brand in China and users are willing to pay more to trade and custody their assets with them. While the party line might be that trading has been discouraged or prohibited since the "September 4th Event" in 2017, it is obvious that Chinese traders, both retail and professional, are still deeply involved in crypto. And because there's no official crypto-RMB exchange anymore (following the government crackdown in 2017), most traders are happy to trade fiat for crypto using Huobi OTC.

So if Huobi's volumes are in fact real, then the question is how does their market share stack up against exchanges included in the Bitwise Real 10? The color scale table below helps answer that question:

## Monthly Spot Exchange Volumes

| Volumes (blns) | Binance | Bitfinex | BitFlyer | Bitstamp | Bittrex | Coinbase | Gemini | Huobi Pro | itBit | Kraken | Poloniex |
|---|---|---|---|---|---|---|---|---|---|---|---|
| Jan-19 | $19.24 | $4.84 | $0.57 | $1.46 | $0.85 | $2.45 | $0.46 | $9.70 | $0.31 | $2.75 | $0.42 |
| Feb-19 | $20.76 | $4.56 | $0.44 | $1.53 | $0.76 | $2.33 | $0.36 | $11.49 | $0.24 | $2.34 | $0.34 |
| Mar-19 | $26.61 | $3.27 | $0.33 | $1.24 | $1.49 | $2.08 | $0.28 | $17.49 | $0.18 | $1.86 | $0.34 |
| Apr-19 | $34.83 | $6.97 | $0.81 | $2.90 | $1.84 | $5.21 | $0.63 | $27.63 | $0.42 | $4.09 | $0.75 |
| May-19 | $58.90 | $9.75 | $1.86 | $5.31 | $2.27 | $11.72 | $1.05 | $42.31 | $0.61 | $8.40 | $1.29 |
| Jun-19 | $67.73 | $11.73 | $2.64 | $5.81 | $2.38 | $14.11 | $1.14 | $49.40 | $0.57 | $10.37 | $1.32 |
| Jul-19 | $52.37 | $9.95 | $3.12 | $5.97 | $1.70 | $13.91 | $1.17 | $43.18 | $0.55 | $9.72 | $0.99 |
| Aug-19 | $31.42 | $5.21 | $1.74 | $3.88 | $0.91 | $7.96 | $0.75 | $30.56 | $0.44 | $6.06 | $0.61 |
| Sep-19 | $28.57 | $4.12 | $1.11 | $3.24 | $0.71 | $6.06 | $0.57 | $23.45 | $0.24 | $4.79 | $0.55 |
| Oct-19 | $32.13 | $3.33 | $1.32 | $3.39 | $0.61 | $5.58 | $0.44 | $23.00 | $0.28 | $4.37 | $0.76 |
| Nov-19 | $29.33 | $2.62 | $1.07 | $2.32 | $0.38 | $4.53 | $0.29 | $26.98 | $0.19 | $3.52 | $0.77 |
| Dec-19 | $23.98 | $2.14 | $0.83 | $1.66 | $0.30 | $3.64 | $0.23 | $18.74 | $0.16 | $2.77 | $1.21 |
| Jan-20 | $37.56 | $4.09 | $1.39 | $2.91 | $0.62 | $6.39 | $0.40 | $35.12 | $0.20 | $4.29 | $2.20 |
| Feb-20 | $59.80 | $5.34 | $1.88 | $3.61 | $0.87 | $9.28 | $0.53 | $44.55 | $0.18 | $5.35 | $2.68 |
| Mar-20 | $66.90 | $7.65 | $2.30 | $5.71 | $0.98 | $13.46 | $1.21 | $43.79 | $0.16 | $7.50 | $1.80 |
| Apr-20 | $47.34 | $4.25 | $1.71 | $4.48 | $0.84 | $9.24 | $0.71 | $33.43 | $0.11 | $7.36 | $1.66 |
| May-20 | $57.68 | $4.63 | $1.94 | $6.62 | $1.20 | $13.80 | $0.83 | $30.70 | $0.23 | $7.03 | $1.99 |
| June-20 | $43.30 | $2.95 | $1.34 | $3.74 | $1.04 | $7.71 | $0.70 | $25.30 | $0.16 | $4.85 | $1.03 |
| **Grand Total** | **$1,390.21** | **$188.81** | **$50.01** | **$124.02** | **$37.35** | **$263.42** | **$22.01** | **$1,022.93** | **$10.05** | **$185.02** | **$19.70** |

*Chart 6: Sources - CoinAPI, CryptoCompare*

It is clear that Binance and Huobi are both dominant, and based on this data that Huobi is a top 2-3 spot exchange globally.

# Huobi's Expansion Beyond Spot Trading

## HUOBI OTC

Over time, Huobi's peer-to-peer OTC app has become one of the most liquid markets for traders to acquire BTC with fiat in China. Despite the fact that there is no public data about the peer-to-peer OTC volumes, within various WeChat traders groups, the number of "Huobi OTC" mentions is significantly higher than any OTC run by other centralized exchanges. Flex Yang, the CEO at Babel Finance, a HongKong/Beijing-based cryptoasset management platform that has approximately $350M of loans outstanding and assets-under-management of 8,000 BTC, 3,000 ETH, and $18M of stablecoins, suggested that Huobi peer-to-peer OTC is their clients' first choice when they need to exchange for fiat. Also, according to two different China-based wallet operators (both are among the largest in the world), Huobi's peer-to-peer OTC platform regularly processes over $100M of volume per day.

21% of the main Huobi.com website traffic comes from their peer-to-peer fiat-to-crypto OTC platform. Huobi has proven effective at using this as a customer acquisition strategy by funneling OTC traders to the main Huobi Global crypto-to-crypto exchange, and then offer them additional services once they have onboarded. Therefore, even though Huobi peer-to-peer OTC revenues do not directly flow to the $HT burning schedule, the volume of the peer-to-peer OTC platform has an indirect impact on the spot volume of major cryptocurrencies traded on Huobi Global.

## HUOBI DERIVATIVES MARKET (HUOBI FUTURES)

On December 10, 2018, Huobi Derivatives Market (Huobi Futures) was launched as part of Huobi Global.

The trading volume of the expiry contracts at Huobi quadrupled year over year from April 2019 to April 2020. During the past 12 months, the peak monthly volume of the expiry contract reached $154M in February 2020. In April, Huobi's perpetual swap volume reached $503M, despite only rolling out the product in late March. By launching new products carefully, Huobi has earned a reputation for being a platform that prioritizes asset security and risk management for retail and professional traders.

Huobi Future's market share today of BTC Futures is 23%, ranked 2nd globally only behind Binance Futures (though the rankings generally change every month). Huobi Futures was able to expand its market share for a few reasons:

1. **Risk control as the internal No. 1 priority:** abnormal transaction and liquidation risk monitoring 24/7 with proactive communications through multiple channels; allowing partial liquidation and preventing clawbacks (charges at the profitable accounts during the extreme market situation after the insurance fund runs out) when the balance in the insurance fund is still positive.

2. **Improvement in user experience**: the tech team iterated its web, app, and API ends multiple times. In March 2020, the system went through an upgrade to improve its TPS up to 6,000 transactions per second and shorten the response time.

3. **Diversified product offering:** gradually launched multiple types of orders, and enhanced liquidation protection.

4. **User retention and customized customer services:** team hosted a series of trading competitions with big awards (e.g. Maserati, yacht) to attract big traders and correspondingly offered differentiated VIP client services. Huobi understands how to entice big traders and market makers to onboard to the platform.

Over the past year, Huobi has upgraded its technology infrastructure and its product offerings in derivatives trading, which now makes up the majority of Huobi's revenues.

According to several firms that trade on Huobi, such as Su Zhu at Three Arrows, the platform was able to operate normally and provide emergency VIP support during the Black Thursday market crash on March 12, 2020. Huobi's robustness during the extremely volatile situation is one proof point that explains why it's able to command the Chinese market and attract brand loyalty.

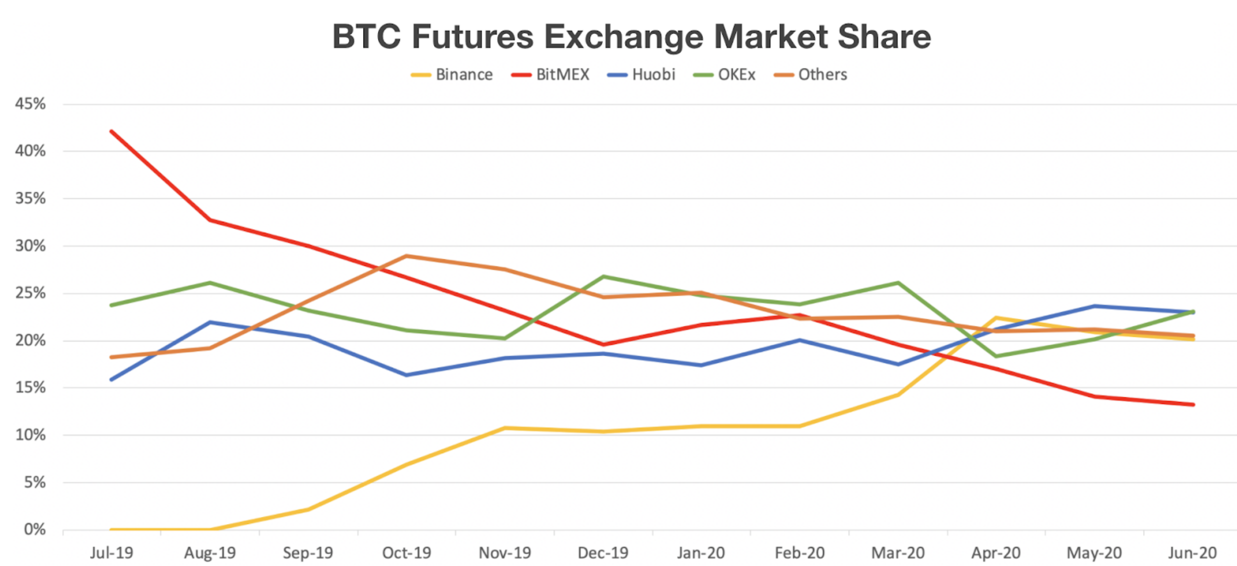

*Chart 7: Source - Skew*

With momentum mounting, there are several tailwinds at Huobi's back, including the secular decline of BitMEX's dominance. On the surface, it appears that BitMEX had a very strong 2019. Arthur Hayes (BitMEX's CEO) reported on Twitter in July 2019 that the exchange reached $1T of trailing 12 month volume. When BTC hit $13K in late June, BitMEX facilitated a record-breaking $16B of volume on its perp swap contracts. However, since then, the company has been bleeding market share to competitors (see chart 7 above, BitMEX is red).

With the rising opportunity, Huobi Futures plans to focus on two strategies going forward: globalization and product diversification. On March 27, 2020, Huobi launched its inverse perpetual swaps that support 10 different tokens. In 2020, the derivatives market will launch more products including vanilla perps and options. Huobi Futures's geographic focus will include Singapore, Great Britain, Korea Vietnam, and Russia, all of which have historically driven offshore exchange volumes. Furthermore, the company will continue to support the "shared-VIP" plan, which will allow professional trading teams in traditional markets to receive VIP services at Huobi Futures.

In summary, Huobi Futures is growing derivatives market share, and stands to gain from BitMEX's recent struggles (i.e., user email leak, CFTC investigation, bleeding market share, index price attacks, March 12 circuit breaker, etc). If the trend continues, it's reasonable to expect BitMEX to continue forfeiting market share to Huobi, OKEx, FTX, Deribit, and Binance.

## HUOBI CHAIN: THE FIRST OPEN SOURCE EXCHANGE-CHAIN

On June 6, 2018, Huobi kicked off the Huobi Chain project by announcing that they would partner with a global leader for the development of a blockchain. After a year and a half of development, in November 2019, Huobi's native blockchain was open-sourced, becoming the first exchange chain to open-source its code. The "global leader" that Huobi chose turned out to be the Nervos team (disclosure: Multicoin Capital owns Nervos's $CKB token). The SDK that Huobi Chain deployed is called Muta, which uses Nervos's Overlord consensus.

A few months later, in March 2020, the Huobi Chain team launched its public beta testnet. The partnership with the Nervos team is reciprocal: Huobi benefits from the infrastructure technology expertise that the Nervos team offers, and the Nervos team is able to have its first test run of the Muta SDK with a big enterprise partner like Huobi. By adopting a cross-chain model, the assets issued on Huobi Chain could rely on the layer 1 security of the Nervos CKB blockchain and have a gateway to a compliant instance.

We believe the market currently underappreciates the vision of Huobi Chain. It's easy to look at it on the surface as a regulated exchange-chain. Similar to Binance Chain, Huobi will start with its own decentralized exchange; however, Huobi Chain is differentiating by supporting arbitrary smart contracts from launch. This enables third-party developers to build DeFi applications on top of the protocol. The implication behind a KYC-enabled exchange-chain is extremely powerful: Huobi Chain makes it possible to create regulatory-compliant liquidity (i.e., blockchain-based CBDC) using DeFi protocols built on top of the chain.

| | Huobi Chain (Public Testnet) | Binance Smart Chain | Binance Chain (Live on Mainnet) | OKChain (Public Testnet) |
|---|---|---|---|---|
| **Infrastructure dev** | Nervos Muta | Ethereum Virtual Machine | Cosmos SDK | Cosmos SDK |
| **Consensus** | Overlord | PoS Authority | Tendermint | Tendermint |
| **Supports Smart Contract** | Yes | Yes | No | Yes (But users cannot deploy directly yet) |
| **Virtual Machine** | CKB VM / RISC-V VM gcc/gdb/llvm compatible | EVM-Compatible | No | WASM |
| **Open sourced?** | Yes | Yes | No | Yes |
| **Language** | Rust | Solidity | Golang | Golang |

*Chart 8: Source - Nervos WeChat Public Account*

Huobi understands that in order to operate in China, financial services providers must be compliant and work closely with regulators. That's why Huobi decided to enable a regulator node on Huobi Chain. If Huobi had tried to build it without one (and ignore Chinese lawmakers), it's likely that they wouldn't have been able to launch it.

In the months leading up to the launch of Huobi Chain, Huobi has already dedicated a significant amount of time and resources to accelerate the DeFi movement in China: it is the first exchange that launched its own stablecoin, $HUSD, and custodial ERC-20 form of Bitcoin, $HBTC.

Today, while Huobi is the primary platform for users to trade $HBTC and $HUSD, some third-party platforms like Stable Asset Swap by dForce have added support for $HUSD (and will support $HBTC soon). $HBTC and $HUSD are increasingly becoming the bridge between centralized exchanges and the DeFi world in China. As a result, the next move for Huobi Chain since its public testnet went live will be migrating $HBTC and $HUSD over to Huobi Chain, followed by the Huobi decentralized exchange (Huobi DEX).

The native token for Huobi Chain is the same as the currently traded exchange token, $HT (unlike OKEx and $OKB). Thus, the value created from on-chain activity will accrue to the token.

# Huobi Token ($HT) Pricing Framework

The most common relative pricing technique used for exchange tokens is the buyback ratio. For example, if a token's fully diluted market cap is $100M, and the team is buying and burning $10M of tokens each year, its buyback ratio would be 10%. Exchange tokens are generally purchased on the open market with revenues (or profits in the case of Binance and KuCoin), and as such we've created a chart to show all of the relevant quarterly exchange profits/revenues over time:

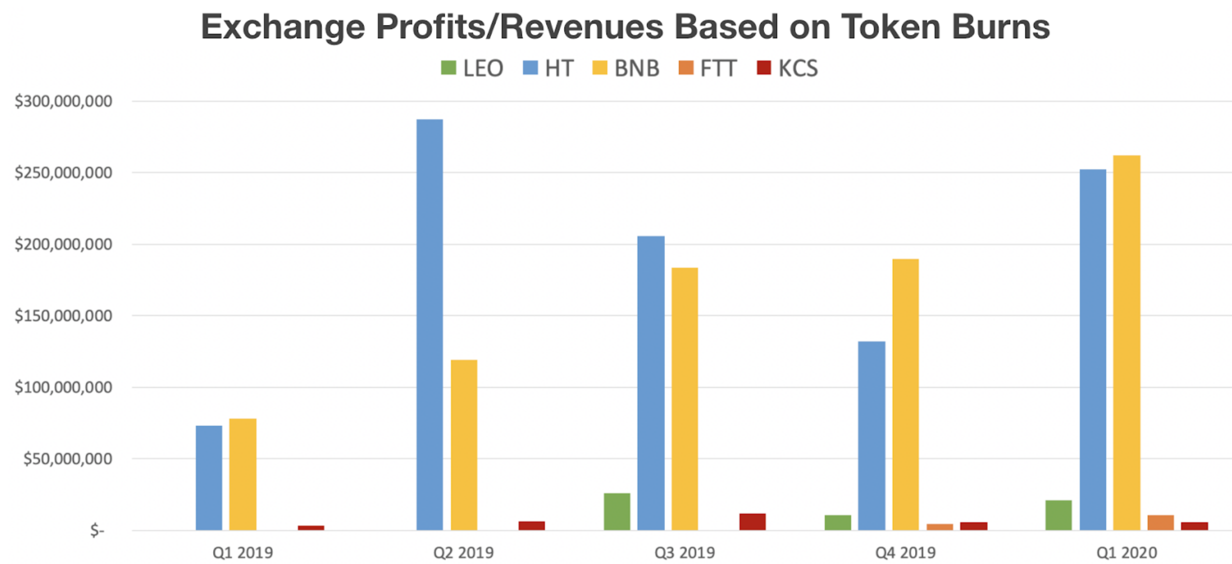


*Chart 9: Sources - Exchange Websites, Etherscan*

As mentioned above, after spreading the comps in the exchange token sector, we can see that Huobi's buyback ratio is materially high relative to competitors. Today, $HT's buyback ratio is 17.8% (higher than all others on a fully-diluted basis and liquid float basis). That means Huobi (at current revenue run rate and $HT valuation) will buy back every single token over the next 6 years. We believe this alone has the opportunity to push up the price over the next few years. As a result, we find $HT's token economics to be quite compelling.

| **Exchange Token Comp Analysis** | | | **mm tokens** | | **%** | **Fully Diluted** | **Floating Mkt** | **Trailing 12 month** | **Fully Diluted** | **Floating** |
|---|---|---|---|---|---|---|---|---|---|---|
| **Token** | **Platform** | **Last Px** | **Fully Diluted** | **Float** | **Floating** | **Mkt Cap (mm)** | **Cap (mm)** | **burn (mm)** | **Buyback Ratio** | **Buyback Ratio** |
| FTT | FTX | $3.05 | 344.97 | 115.93 | 33.60% | $1,052.16 | $353.57 | $10.97 | 1.04% | 3.10% |
| BNB | Binance | $17.67 | 179.88 | 147.88 | 82.21% | $3,178.48 | $2,613.04 | $151.00 | 4.75% | 5.78% |
| OKB | OKEx | $5.06 | 300.00 | 279.33 | 93.11% | $1,518.00 | $1,413.40 | $69.15 | 4.56% | 4.89% |
| LEO | Bitfinex | $1.14 | 985.24 | 978.13 | 99.28% | $1,123.17 | $1,115.07 | $17.43 | 1.55% | 1.56% |
| KCS | KuCoin | $0.78 | 171.25 | 81.25 | 47.45% | $134.20 | $63.67 | $2.97 | 2.21% | 4.66% |
| **Comparable Company Averages** | | | | | **71.13%** | **$1,401.20** | **$1,111.75** | **$50.30** | **2.82%** | **4.00%** |
| HT | Huobi | $4.22 | 290.99 | 233.37 | 80.20% | $1,227.98 | $984.82 | $175.50 | 14.29% | 17.82% |
| **Huobi's Burn Premium Over Sector Average** | | | | | | | | | **5.06x** | **4.45x** |

*Chart 10: Sources - Exchange websites, Maple Leaf Capital, CoinGecko, (for assets that started burning within the last 12 months, we took the full history and prorated out to 12 months)*

Cryptocurrencies are priced against each other, they are not valued. As a result, the logical conclusion from the above table is that either *all* of the exchange tokens excluding $HT are overpriced, or $HT is significantly underpriced. In our view, $HT is misunderstood by the market in a few key areas, and as such, is materially underpriced against other exchange tokens. We think that the three bullet points below explain the pricing discrepancy between $HT and comps:

1. **Regulatory risk:** China cracked down on crypto exchanges in 2017, and so the Western community thinks they are operating in a grey area. But we believe regulatory risk is mitigated because Huobi seems to be blessed by regulators and is still operating. Now, blockchain is a big national priority in China which is a positive for Huobi.

2. **Wash trading:** Huobi is not included in Bitwise's Real 10 but we believe this risk is mitigated by on-chain assets under custody increasing to 2nd globally behind Coinbase, spreads tightening, and volume sizing experiments showing minimal slippage, indicating volume on Huobi is in fact real. We've also spoken with several large OTC desks and market makers, who have all confirmed that they can trade large size at good prices on Huobi, and that it's as liquid as any other big exchange in crypto.

3. **Cultural/language barriers:** It's a Chinese company and doesn't explicitly cater to Western customers. This is mitigated by a renewed push into Western markets, more clearly defined strategy updates, a clear commitment to transparency with the new burn metrics page, etc. We acknowledge that this is still a challenge for Huobi, and we are actively engaging with them to help in this area.

We think that, at relative exchange token prices, $HT is a compelling risk-adjusted investment opportunity. For HT's buyback ratio to come in line with the rest of the exchange token sector, which we think it should given that the aforementioned risks are overstated by the market, the price of $HT would need to capture 4x upside from current prices.

# Betting on China

## THREE CRYPTO MARKETS: USA, CHINA, AND EVERYWHERE ELSE

Over the past 24 months, global liquidity in crypto has fragmented rather than consolidated. Liquidity is fragmented across regulated vs. unregulated venues, jurisdictions, different kinds of products (spot, perps, options, futures), assets, and more. Ambitious entrepreneurs are launching new exchanges on a regular cadence (to the tune of 45 per year according to CoinMarketCap data), and we expect this trend to continue for the foreseeable future.

Notably, most of the new trading platforms are derivatives exchanges. Most challenger exchanges are focusing on derivatives for one simple reason: it's really hard to compete for retail spot liquidity. Whereas a derivatives exchange can successfully compete by offering new innovative products, carving out a niche, or making markets on their own exchange (FTX move contracts, CoinFLEX physically delivered futures, Deribit options, etc), there is not as much room to innovate in offering fiat-BTC spot trading. Liquidity, UX, and brand trust are the predominant vectors of competition.

Today, there are three primary spot markets in crypto:

1. USA: dominated by Coinbase, and to a lesser extent Kraken, Gemini, and CME.
2. China: dominated by Huobi, and to a lesser extent OKEx and Binance.
3. The Rest of the World: dominated by Binance, and to a lesser extent hyper-localized exchanges (Bitso in Mexico, Indodax in Indonesia, Luno in South Africa, etc).

Globally, just a handful of exchanges dominate spot trading. Given the cultural, regulatory, and brand moats that these major exchanges have developed over the years, it is unlikely that new players will be able to compete for fiat onramp volume. All of these incumbents operate at massive scale, and thus can offer the lowest fees possible. These companies have significant brand awareness and trust, which is extremely difficult to replicate.

In China, Huobi and OKEx have clear structural advantages in the form of regulatory capture. BTC China was forced to shut down in 2017 while Huobi and OKEx only temporarily paused trading, but were effectively allowed to continue operations. Similar to BTC China, BISS, another Chinese exchange, was shut down by authorities in Beijing, who deemed it an illegal fundraising fraud. As the market shrank due to closures, Huobi and OKEx amassed market share by simply keeping the lights on.

## CHINA'S BLOCKCHAIN INITIATIVE

On October 24, 2019, Chinese President Xi Jinping made a landmark speech in which he emphasized the national strategic importance of blockchain technology to China. He went on to reiterate that China should accelerate development, investment, and innovation around distributed ledger technology as a national priority. Some highlights from the speech include:

1. **Increased Investment**: Investment firms should accelerate their investments in the space
2. **Leading the Standard Setting in the World**: Chinese firms and individuals should lead global discussions around setting the industry standards
3. **Strengthening the Industry Talent Pool:** Universities and enterprises will provide more relevant courses so that more strong talents can go into the sector
4. **Financing Loans for SMEs** - SMEs may be able to take advantage of the progress of DeFi
5. **Integration of Credit Information / Data**: Personal data and credit information on chain to be associated with real world identity; China could potentially deploy a mass-scale on-chain identity network
6. **"Blockchain+"**: The government encourages large enterprises to incorporate blockchain technology into their product / production process (e.g., a "consortium chain"), so that people would start to interact with blockchain tech in their daily lives

7. **Strengthening the Guidance and Exploring the Regulation**: China will still enact some regulations, but will remain hands off in order to encourage innovation.

Shortly following President Xi's speech, Li Wei, the head of technology at the PBoC, echoed President Xi's comments by suggesting banks should step up their applications of blockchain technology and embrace digital finance.

Since then, officials in China's Sichuan province (the mining capital of China) sped up mining legalization (whereas before it was legally gray), and it has since been encouraged by a former Chairman of the Securities Regulatory Commission (the Chinese SEC). Additionally, the Blockchain Service Network, a consortium blockchain project led by the State Information Center, a government agency under the National Development and Reform Commission, also recently launched.

In the months since then, we have observed that interest in blockchain has been steadily increasing and permeating all facets of society: supply chain management, intellectual property protection, digital invoice issuance, lottery drawing transparency, and fraud detection.

Furthermore, a few days after Xi's speech, Qifan Huang, the Vice-Chairman China Center for International Economic Exchanges, announced the launch of Digital Currency Electronic Payment (or "DC/EP"), the Chinese Central Bank's Digital Currency (CBDC). While this concept remains obscure and obtuse to most, its significance to the world cannot be overstated.

Although the final technology infrastructure for DC/EP is yet to be finalized, it is almost certain that it will be deployed on a consortium blockchain, with the Central Bank being a "supernode" that has the power to overrule. The details of transactions that take place on DC/EP will not be accessible to anyone other than the Central Bank. In other words, the Chinese government aims to leverage the unique features of blockchain to tackle money laundering and protect user privacy against malicious third parties. It's a stroke of genius: it allows the Central Bank to retain the control and oversight they need, but improves on the existing legacy payment rails which are fragmented, slow, and expensive.

During the 13th National People's Congress (NPC) and the Chinese People's Political Consultative Conference (CPPCC) that started in Beijing on May 21, the CEO of Huobi Global, Leon Li, was invited to speak at a panel discussion hosted by the Journal of People's Political Consultative Conference, during which he proposed how blockchain could help finance SMEs and improve information transparency within enterprises. Li's presence at this government-run program during one of the most politically significant conferences in China implicitly implies Huobi's strategic importance to Chinese policy makers.


*Chart 11: Leon Li (left) on the panel with other representatives of People's Congress, Source - [Securities Daily]*

As the government grows awareness of crypto, the first place that local Chinese traders are likely to visit to purchase crypto is Huobi. As a result, Huobi Token ($HT) provides novel backdoor exposure to the increasing interest in blockchain and crypto in China that would otherwise be off limits to outsiders. For example, retail traders cannot invest in the DC/EP system nor in the BSN network.

We believe there is currently insufficient information to pick a market-winning token in China—we do not know whether Chinese investors will buy the top 10 market cap assets, Chinese-native tokens (like NEO, OTM, QTUM), or gamble on small-cap assets that have a history of running up idiosyncratically. While it is too early to build strong conviction in one particular asset or another, we do know that Huobi is—and will be—the primary retail exchange in China because it quietly operates the most liquid RMB on-ramp.

Thus, owning $HT allows investors to get exposure to China's burgeoning ecosystem—and the customary speculation that accompanies it—without taking on idiosyncratic price risk with any one particular asset. All else being equal, Huobi should do well as a company if Chinese retail investors onboard into the distributed ledger ecosystem.

With more than 1.3B people in China, Huobi's market opportunity is massive.

# Conclusion

It is hard to be an early bird. And it is considerably harder to be an early bird that lasts. Huobi is this lasting early bird. After weathering the storm through multiple bull and bear markets, Huobi has consistently been able to capture several market opportunities, grow market share, and improve its business to maintain its edge as the dominant exchange in China.

Huobi has done this all while many new crypto exchanges have launched, bringing a flurry of new competition for the company. However, the increasing competition has not hurt Huobi's market position. In fact, the data tells us that the spot exchange incumbents are so entrenched that entrepreneurs are now starting to realize it's extremely difficult to compete. As chart 12 below shows, exchange launches have significantly slowed down this year, even though prices, volumes, and exchange revenues are skyrocketing. And of those new exchanges, many are derivatives exchanges that aim to offer some novel product that existing exchanges don't offer.

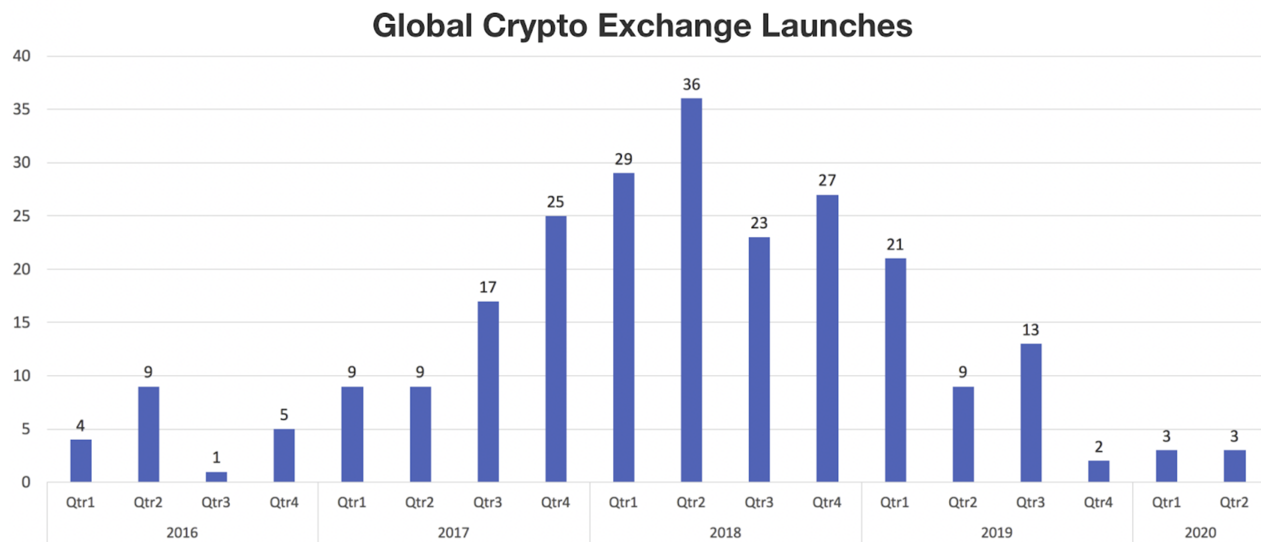


*Chart 12: Source - [CoinMarketCap]*

Huobi's significant investments in risk management, system performance upgrades, and marketing campaigns have helped the company retain existing retail clients, attract more professional traders all over the world, and grow trading volumes and revenues. These actions sufficiently justify why Huobi has become a market leader within the exchange space. But on top of that, the fast execution on Huobi Chain and the partnership with Nervos Muta has shown that they are also willing to expand outside of the exchange business into DeFi, which is a massive growth market opportunity that has yet to be fully explored.

China is a fast-growing hub for crypto innovation right now. Consequently, it's not surprising that investors are seeking novel ways to get exposure to the growing awareness of crypto in China. However, because there are few credible vehicles to invest in without taking on too much idiosyncratic risk, we believe $HT presents the best risk-adjusted way for intrigued investors to get quantifiable exposure to crypto in China. On top of capturing upside on the "China crypto" thesis, $HT's token economics are very attractive relative to peers.

For all of the reasons outlined in this paper, we are very bullish on $HT at current prices and believe that $HT will outperform the broader cryptoasset market over the next 1-2 years. The market capitalization of $HT is currently $985M, and it is ranked #20 on CoinMarketCap.