

Withdrawal of staked Ether and related rewards expected in March 2023

Published 2 March 2023

WisdomTree

Contributor

Unlocking of staked Ether expected to create a benchmark yield for the digital assets industry

Since the Ethereum network underwent a transition in the way it validates transactions from Proof-of-Work (PoW) to Proof-of-Stake (PoS) in September 2022, it has been possible for validators to stake Ether (ETH) in a smart contract but it has not been possible to withdraw the staked ETH or earned rewards yet. A new upgrade to the Ethereum network called the Shanghai Upgrade or Ethereum Improvement Proposal EIP-4895 is expected to change this in March 2023.

We believe this upgrade will be significant for the industry as it creates a yield against which all other token yields can be benchmarked. Although staking and withdrawal of rewards have been enabled by many other tokens, Ethereum remains the most widely adopted smart contract blockchain and has more than double the number of total developers compared with any other blockchain network¹. Because Ethereum accounts for 19% of the total crypto market and has a \$204 billion market cap², the asset is fairly liquid and remains one of the favourite assets to own among institutional investors, along with Bitcoin.

Will unstaking create unusual selling pressure on ETH?

Currently, the amount of ETH that has been staked on the PoS Beacon chain is over 16.7 million ETH or over \$27 billion via over 520,000 validators³. This is only approximately 14% of total ETH in circulation, which is a much lower staking ratio than with many other tokens where the ratio is more typically 40-98%⁴. It is estimated that 65% of staked ETH tokens are already liquid⁵, as many validators have issued staked ETH tokens which can be used for decentralised finance (DeFi) applications etc. The largest ETH validator is a liquid staking pool provider, Lido Finance, with over 30% market share, followed by centralised exchanges Coinbase, Kraken, and Binance⁶. Of centralised exchanges, Coinbase and Binance have offered staked ETH tokens and, hence, liquidity to ETH stakers.

When the Beacon chain came alive in December 2020, an estimated 2 million ETH was staked⁷ on the chain with an average ETH price of \$6008 and these ETH stakers, along with some other early investors, are now in profit. While some of them might be under pressure due to tumultuous crypto price changes last year, we do not expect a significant pricing pressure to come from this group as these investors are likely to be 'true believers' in Ethereum as they took the risk of investing early while not having any firm visibility into when staking rewards could be collected. In addition, we estimate that close to 70% of ETH stakers invested in 2021 and early 2022 and these investors are still underwater. Hence, we do not expect majority of these investors to exit at a loss.

Will unlocking create a situation where one validator could control >50% of Ethereum blockchain transaction validations?

We do not believe so as exiting the Beacon chain will be managed by a staged process. Two types of withdrawals will be possible once withdrawal of ETH and associated staking rewards is enabled. The first option includes a partial withdrawal where a validator withdraws the staking reward but leaves the staked ETH untouched. There is an estimated 1 million ETH in accumulated staking rewards⁹ so far amounting to \$1.7 billion in potential selling pressure at a current ETH price of \$1656¹⁰. Because ETH's daily average volume is about \$13 billion¹¹ we do not think this will be a major threat to ETH's price, particularly considering that this exit flow is likely to take place over days or weeks.

Another type of withdrawal is a full exit where an investor exits both the staking reward and the staked ETH deposit. To counteract potential instability of the network during the exit period, the Ethereum blockchain has imposed limits on these exits. The network is programmed to limit exits to seven validators per epoch, which is 6.4 minutes, and this means that a maximum 1,575 validators can exit the network per day¹². As there are over 520,000 validators in total, we do not anticipate the limited number of daily exits destabilising the blockchain and enabling a malicious attack.

With staking services under threat in the US, should they be considered securities?

In February 2023 Kraken was sued by the Securities and Exchange Commission (SEC) for failing to register the offer and sale of its Staking-as-a-Service program as a security in the US. Kraken chose to settle this charge, end all of its on-chain staking services for US clients, and pay a \$30 million fine. Kraken is the third largest validator of ETH transactions and has approximately 9% market share of the 16.7 million ETH locked in a smart contract network¹³. Kraken's exit from the US will force investors to find an alternative way to stake ETH and we believe this will benefit the liquid staking providers, such as Lido Finance and Rocketpool.

We are inclined to think that not all staking products should be viewed in the same way but, at the moment, there is no clarity on this issue in the US. Recently, SEC's Chairman made several appearances in media arguing that all 'yield', 'earn', 'annual percentage yield', and 'staking' products should probably be treated as securities. As we understand it, Kraken's staking program offered an annual fixed yield, paid twice a week¹⁴, and this was different from the actual yield and frequency of payment made by the underlying

Ethereum protocol. This means that Kraken most probably comingled client assets and actively managed pool liquidity.

If all staking programs are viewed as securities, it will most likely harm Coinbase more as it is the second largest individual ETH validator and derived 11% of its net revenues from staking activities (not just Ether token though) in Q3 2022¹⁵. We believe staking is a high-margin business and, hence, the impact on Coinbase's profitability would be even greater. In fact, Coinbase argues that its staking service should not be viewed as a security as it does not comingle client funds and it pays the same reward as the underlying blockchain minus a transparent fixed fee. Coinbase has also announced it is prepared to go to court to defend its view on the staking service.

1 Source: Electric Capital, Developer Report 2022

2 Source: CoinMarketCap, 17 Feb 2023

3 Source: [Beaconcha.in](https://beaconcha.in), 17 Feb 2023

4 Source: Defi Llama, [Stakingrewards.com](https://stakingrewards.com)

5 Source: Nansen

6 Source: Nansen

7 Source: Cryptoquant

8 Source: Bloomberg

9 Source: [Stakingrewards.com](https://stakingrewards.com)

10 Source: Bloomberg, 17 Feb 2023

11 Bloomberg, 17 Feb 2023

12 Source: [Ethereum.org](https://ethereum.org)

13 Source: Nansen

14 Source: support.kraken.com

15 Source: Coinbase, Q32022 Financials

Related blogs

+ [Ethereum Merge complete. What's changed?](#)

+ [The Ethereum 'merge' and its consequences](#)

Related products

+ [WisdomTree Ethereum \(ETHW/WETH\)](#)

Important Risks Related to this Article

Important Information

Marketing communications issued in the European Economic Area (“EEA”): This document has been issued and approved by WisdomTree Ireland Limited, which is authorised and regulated by the Central Bank of Ireland.

Marketing communications issued in jurisdictions outside of the EEA: This document has been issued and approved by WisdomTree UK Limited, which is authorised and regulated by the United Kingdom Financial Conduct Authority.

WisdomTree Ireland Limited and WisdomTree UK Limited are each referred to as “WisdomTree” (as applicable). Our Conflicts of Interest Policy and Inventory are available on request.

For professional clients only. The information contained in this document is for your general information only and is neither an offer for sale nor a solicitation of an offer to buy securities or shares. This document should not be used as the basis for any investment decision. Investments may go up or down in value and you may lose some or all of the amount invested. Past performance is not necessarily a guide to future performance. Any decision to invest should be based on the information contained in the appropriate prospectus and after seeking independent investment, tax and legal advice.

The application of regulations and tax laws can often lead to a number of different interpretations. Any views or opinions expressed in this communication represent the views of WisdomTree and should not be construed as regulatory, tax or legal advice. WisdomTree makes no warranty or representation as to the accuracy of any of the views or opinions expressed in this communication. Any decision to invest should be based on the information contained in the appropriate prospectus and after seeking independent investment, tax and legal advice.

This document is not, and under no circumstances is to be construed as, an advertisement or any other step in furtherance of a public offering of shares or securities in the United States or any province or territory thereof. Neither this document nor any copy hereof should be taken, transmitted or distributed (directly or indirectly) into the United States.

Although WisdomTree endeavours to ensure the accuracy of the content in this document, WisdomTree does not warrant or guarantee its accuracy or correctness. Where WisdomTree has expressed its own opinions related to product or market activity, these views may change. Neither WisdomTree, nor any affiliate, nor any of their respective officers, directors, partners, or employees accepts any liability whatsoever for any direct or consequential loss arising from any use of this document or its contents.