AAVE (AAVE) - Investment Memo

Category: Decentralized Finance
Sector: Lending & Borrowing
Position Type: Core Allocation (Target: 5 to 7%)
Current Price: $287 (June 16, 2025)
Market Cap: 4.36B | FDV: $4.60B | Circulating Supply: 15.16M AAVE | Max Supply: 16M AAVE

Overview

Aave remains the liquidity hub of DeFi lending, spanning 18 networks and accounting for roughly two-thirds of all on-chain borrow liquidity. Its multi-asset collateral model, tiered risk framework and battle-tested governance have created high switching costs for the > 79k monthly active users who rely on it for leverage, yield strategies and real-world-asset vaults. Net deposits surpassed the 2021 cycle peak in January 2025 and TVL continues to trend higher alongside record transaction counts, pushing transfer activity to levels last seen in mid-2021.

Investment Thesis

1. Aave's more than $25 billion in total value locked—over six times the next-largest lender—anchors liquidity, oracle integrations, and governance participation, giving the protocol durable network effects.

2. The forthcoming V4 upgrade will merge collateral pools across leading Layer-1 and Layer-2 networks into a single liquidity layer, letting users borrow in one transaction without bridges once the phased rollout begins in mid-2025.

3. Two independent fee engines, core lending fees now running about $46 million over the last 30 days (annualized) and the GHO stablecoin supply of roughly $219 million, provide recurring revenue that will be reinforced by a built-in savings rate after V4.

4. Permissioned Aave Arc pools, Lens-integrated social-credit lines, and real-world-asset vaults expand the addressable market beyond crypto-native leverage demand and diversify fee streams toward institutional treasuries and fintech borrowers.

5. On-chain risk feeds from Gauntlet and Chaos Labs will soon automate updates to loan-to-value limits and interest curves, strengthening risk controls and aligning the protocol with institutional standards.

Key Catalysts

- A major software upgrade (called "v4") goes live later this year. It pulls liquidity from 10+ blockchains into one shared pool, so users won't have to juggle bridges or multiple wallets. Simpler UX and deeper liquidity usually translate into higher volumes and fees.

- Aave's own stablecoin, GHO, will soon offer a built-in savings rate. Think of it like the protocol paying interest on its house currency: it attracts more holders, and the interest payments flow straight back to the Aave treasury.

- "Permissioned pools" are coming for banks, fintech lenders, and real-world-asset deals. These pools run KYC checks and accept off-chain collateral, opening the door to borrowers who can't or won't touch fully permissionless DeFi today. Bigger borrower universe = more fees.

- Risk settings (loan-to-value ratios, interest rate curves, etc.) will update automatically based on live market data from Gauntlet and Chaos Labs. Faster, data-driven adjustments reduce blow-up risk and make the system feel more institutional-grade.

Risks

- Lean competitors (Morpho Blue, Spark Lend, Compound III) offer lower base rates and could peel off blue-chip collateral.
- Regulatory scrutiny of a USD-pegged stablecoin may constrain GHO listings in key jurisdictions.
- Governance power is concentrated (> 45 % voting share among whales and service providers), creating capture risk.
- Long-tail asset listings still drive a non-trivial share of revenue and increase liquidity-crunch exposure.

Valuation Framework

Phase 1 ('25-'26) – V4's cross-chain pool collapses fragmented liquidity; if protocol revenue lifts from today's $85M run-rate to ~$180M and 40% is shared with stakers, an 18× cash-flow multiple underpins $190-$220 per token; creating a solid base from which AAVE can compound higher.

Phase 2 ('27-'28) – GHO float expands toward $1B with a savings rate, and steady institutional adoption drives revenue to $250M; a 50% fee split raises token-aligned cash flow to $125M; a 22× multiple supports the $320-$380 bracket.

Phase 3 ('29-'30) – Permissioned pools and RWA vaults mature, pushing revenue toward $400M; capturing 50% of that at a 25× infrastructure multiple yields $5.0B in equity value, or roughly $450-$500 per AAVE on a projected 15.5M float.

Positioning Rationale

AAVE serves as our core DeFi infrastructure holding (5-7% allocation), functioning as the liquidity backbone that enables most other DeFi protocols to operate effectively. Its dominant market position creates a defensive floor while the V4 upgrade and institutional expansion provide meaningful upside optionality over a 3-5 year horizon.

The allocation size reflects AAVE's dual nature: it's both a mature, cash-flow generating protocol ($85M+ annual fees) and a growth story with clear catalysts (cross-chain unification, GHO adoption, TradFi integration). This balance makes it suitable as a core holding rather than a smaller tactical position.

We pair AAVE with oracle infrastructure (LINK, PYTH) because lending protocols are critically dependent on reliable price feeds—this creates portfolio synergies while diversifying across complementary DeFi primitives. AAVE's three-cycle track record and battle-tested risk management also provide stability that newer lending protocols lack, making it an anchor position as we allocate to higher-beta infrastructure plays elsewhere in the portfolio.

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