Strategist's Corner
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Virtual Investing? Really?

Observations on Web 3.0 and the metaverse

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To listen to the full conversation.

What is Web 3.0?

- Web 1.0, the original Internet, was a repository of information. Internet users could add, search, navigate and consume information by going to different servers and Web pages.
- Web 2.0 is about transactions and the creation of information and content used, for example, to drive advertising and to share through social media platforms. Users can also buy items from websites run on centralized platforms.
- Web 3.0 is based on a decentralized, peer-to-peer model that incorporates security, transactions, payments and administration. Crucially, users creating data own that data, which fundamentally changes how the data are used.

Capital market disruptions caused by Web 3.0

- The vast majority — maybe even 75% — of Web 2.0 companies didn't exist on Web 1.0; the scale of the opportunity and risk set as we transition to the next model will likely be similar.
- This is consistent with the S-curve changes seen over the past century across cars, electricity, radios, computers and electric vehicles; the Internet has multiple S-curves as it transforms.
- Negative disruptions include social and search. As they are built on centralized platforms and monetize based on user data, the ground is shifting beneath them. This could be an opportunity depending on how they respond.
- Positive disruptions can be seen across these areas:
  - IT services companies, as they will be in greater demand, and new models of hardware as well as software as a service
  - Financials that face the risk of disintermediation at the hands of distributed finance platforms
  - Media distribution with alternative services that allow content creators to get paid more of the economics
  - New payments built into Web 3.0 and platforms that move transactions away from current networks

What is the metaverse?

- The metaverse is an application of Web 3.0. You can build a metaverse on Web 3.0 but Web 3.0 is not the metaverse.
- A shared, virtual world that is independent of the user, so it exists and continues to play like a movie behind the scenes when users log out. It's immersive, so virtual or augmented reality headsets can be used to interact with it.
- Shopping, education, entertainment and virtual real estate already exist in this virtual world, with younger generations already spending time there.

Capital market disruptions caused by the metaverse

- Likely beneficiaries include these:
  - Semiconductors, as more servers and more storage are required
  - Electronic sports (e-sports), as the metaverse originated in gaming and is rooted in it
  - IT services, as there will be more things to fix, migrate to and do.
- Likely losers from the disruption may be found in these areas:
  - Retail, given the disruption of brick and mortar business caused by e-commerce; this will be e-commerce on steroids, with virtual stores in the metaverse where people can try on clothes, for example; these virtual stores will be built on virtual land already being bought and sold on these platforms
  - Social and search, which, again, will see changes to how they monetize users

Implications for investors

- The transition from the current world to one where Web 3.0 and the metaverse are fully operational will take several years, perhaps longer. The journey from here to there will be fraught with risk, but there will be substantial opportunity along the way. Many companies with meaningful market caps are investing ahead of this theme, and investors need to understand why they're doing that. Where are they going? What does it mean to their economics and returns?
- These investments and the moves investors are making will have a meaningful effect on the fundamentals for these companies. It might take 10 years, but the changes and the implications drive stock prices today, so it's important to stay active in the space and understand it ahead of the actual realization of these themes.
- What hasn't changed is that investing remains a discounting mechanism of future cash flows, as it has always been. Even as science changes things, it's still ultimately about figuring out which companies have the commercial application and ability to monetize the science and which don't.

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