Blockchain is starting to deliver on its promise

Ruud Smets, CIO and Managing Partner of Theta Capital, sees interesting developments taking place in blockchain at the moment. He also believes that blockchain technology is a good and ESG-friendly source of diversification in the investment portfolio.

By *Harry Geels*

Has blockchain gradually fulfilled its promise?

'Blockchain networks represent a new era of protocols, creating a 'verification' and 'settlement' layer on top of the existing internet. This is why we often refer to it as the 'internet of value'. These networks enable secure, frictionless transactions between strangers without needing a centralized intermediary. We are moving toward a 'true internet economy', the ultimate evolution of global commerce by offering unparalleled transparency, efficiency, and inclusivity.

Just as information transfer over the internet became seamless, so will the transfer of value. We're still in the early stages, but promising use cases are emerging. For example, stablecoins allow direct dollar transactions without banks or payment systems. In the first quarter of 2024 alone, $ 6.5 trillion in stablecoin transactions occurred –more than Visa, Mastercard, and PayPal combined. Another example is Polymarket, the world's largest prediction market, where over $ 1 billion is currently being wagered on the U.S. presidential election, surpassing traditional platforms by over tenfold due to its global and frictionless nature.

In the coming years, most assets will move 'on-chain', we have seen it begin with dollars, now treasuries and other bonds, and likely equities next.

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BlackRock has already put a treasury fund on-chain. Smart contracts are replacing traditional contracts, presenting blockchain networks with the opportunity to compete against centralized companies – a challenging but exciting prospect. Although regulation and technological adjustments are ongoing, significant progress is being made. Most interfaces are still somewhat techy, but we know how quickly change can occur.

Bill Gates once remarked that people often overestimate what can be achieved in a year but underestimate what can be done in ten. Bitcoin has been around for 15 years, but widespread application of the technology only began around 2019-2020 with Ethereum. So, we are just five years into this journey, and adoption is accelerating with ETFs in Bitcoin and Ether being the fastest-growing ever.'

How does blockchain technology fit into an investment portfolio?

'Blockchain technology is a unique 'diversifier', introducing a disruptive decentralized business model that replaces traditional intermediaries. It can transform banking services, social networks, marketplaces, and more, all on a global scale without borders. Opportunities like these are rare and come once in a generation. This technology is growing so rapidly that as an allocator you can't really afford not to invest in it. Another key diversification point is the private nature of these markets, which are still primarily focused on venture capital investments.'

How are the risks managed?

'Selective investing is crucial as there are a lot of opportunists. We find 98% of startups not worthwhile. However, the technology's broad applicability means numerous investment opportunities remain. Immediate technological risks, such as critical bugs, are low due to open-source systems and the inherent redundancy. Anyone can inspect the software and there are hundreds of thousands of 'nodes' validating all those transactions. Blockchain technology is antifragile. There is a risk that future regulations might centralize control, contradicting the technology's grassroots, inclusive nature. Maintaining decentralization is key while focusing on long-term sustainable use cases.'

Is there an opportunity to incorporate ESG as well?

'Excessive energy consumption is a com-

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mon criticism of blockchain, particularly in Bitcoin mining with its proof-of-work consensus. However, most other protocols use proof-of-stake, significantly reducing energy usage. Ethereum’s switch to proof-of-stake has cut its energy consumption by 99.99%. The banking system uses 92,000 times more energy annually than Ethereum. There is actually a very strong case to be made that blockchain technology should score very highly on ESG criteria. In a similar way as internet protocols, such as the SMTP email protocol, blockchain networks are totally inclusive – they are equally accessible for anyone, to build, to access and to contribute to. Like anyone can build a website or send an email, anyone can use or build a blockchain network, offering a true level playing field. Additionally, blockchain’s decentralized and transparent nature counters centralization, which is quickly becoming a much bigger problem as a result of the proliferation of AI. And in this age of AI, it enables anyone to verify data authenticity at virtually no cost.’

Do you benchmark?

‘Being a young sector, blockchain lacks established benchmarks, but current results are promising compared to traditional VC investments. Across all vintages since 2018, we see much faster deployment, much bigger outcomes and a much faster path to distributions. Blockchain networks are often profitable from day one, with initial liquidity usually achieved within 3 to 4 years. Specialized early investors benefit from current inefficiencies. Our 2018 vintage has already returned six times the investment, with a double-digit overall multiple. And our 2021 vintage recently made its first distribution. Contrary to most investors’ perception, this comes with a substantial margin of safety, due to all the inefficiencies as a result of the complexity and nascency. The technology remains widely misunderstood.’

PHOTO: ARCHIVE THETA CAPITAL

CV

Ruud Smets

Ruud Smets is CIO and Managing Partner at Theta Capital Management. Theta Capital Management was founded in 2001 and is Europe’s largest investor in blockchain venture capital with over $1billion dedicated to the strategy. Ruud joined Theta in 2005 and has led the firm’s investment activities into blockchain technology from inception in 2017. Ruud is a well-known industry specialist and frequent speaker at industry events. He is an LPAC member of several of the leading VC funds in blockchain technology.

What promising trends are coming?

‘Exciting new technologies like shared security and zero-knowledge proofs (ZKP) are emerging. Shared security allows new blockchain networks to leverage the existing security of established networks like Ethereum or Bitcoin, easing the launch of new applications. ZKPs are used to put personal data on-chain in a privacy-preserving manner, speeding up processes like proving qualifications. These innovations will address many current pain points, such as KYC processes, and are key themes for our latest vintage, Theta Blockchain Ventures-IV, which we are currently raising. Finally, we also see more institutional investors entering the space, as they start educating themselves on the technology, something we happily assist with. And as a result more investors are now starting to position themselves for this investment opportunity of a lifetime.’ ■

Legends4Legends 2024:
Unlocking the True Internet Economy.
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