

Strategist's Corner
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When Competition Returns

Why the Low-Competition Era May Be Ending

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In Brief

- The 2010s muted competition, allowing dominant firms to sustain high profits and market concentration.
- AI lowers the cost of challenging incumbents, while renewed investment expands rival capacity.
- As competition returns, scarce advantages and stock selection should matter more.

In a Strategist's Corner from August titled [Why Index Concentration Will End](#), I argued that today's market concentration reflects concentrated profits and investors' belief in their durability, rather than merely passive flows. An index records the profit takers, but it doesn't create their customers, margins, or returns on capital.

In this piece, I follow up by asking why those profits became so durable and, more importantly, what might bring that durability to an end. Spoiler alert: we think the catalyst is AI.

That answer may sound obvious, but what is less obvious is why AI may affect corporate economics very differently from Internet 2.0. Internet 2.0, with its focus on cloud computing, user-generated content, and two-way interaction, often strengthened incumbents through network effects. AI, or what we are calling "Internet 3.0," may give new challengers the tools to compete.

That Distinction Matters

To be clear, I'm not so bold as to suggest that AI will rewrite the laws of economics. Quite the opposite. I'm suggesting that it may reactivate forces that have been present for centuries.

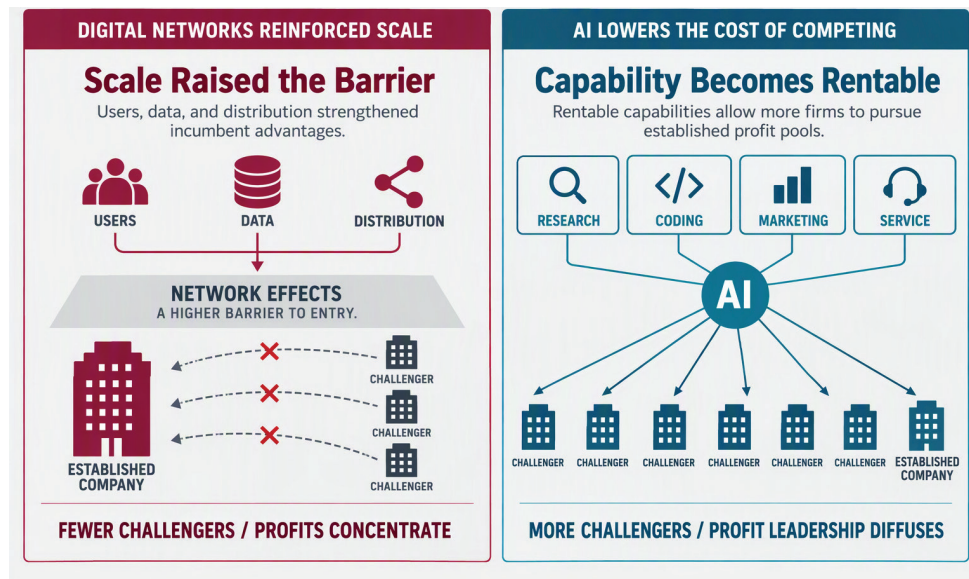
Long before investors were counting ad clicks in the 2010s or comparing tokens per watt today, capitalism had developed a remarkably reliable habit of turning extraordinary profits into an invitation for competition.

The process is usually straightforward. First, something new appears, demand exceeds supply, and returns rise. Those returns then attract entrepreneurs and capital. New supply follows, customers gain alternatives, and pricing power weakens. As profits fall, less efficient competitors fail. Finally, supply and demand move back toward equilibrium, and economic returns normalize.

We saw this with railroads, automobiles, radio, telecommunications, and personal computers. While the products have changed over time, capitalism's response has not.

Capitalism is persistent, but it is not always punctual. Case in point: the last market cycle. As Exhibit 1 illustrates, Internet 2.0 produced "winner-take-most" economics in several large industries, while Internet 3.0 may make sophisticated capabilities available to more challengers.

Exhibit 1: Internet 2.0 vs. Internet 3.0



Two different competitive cycles

Why Competition Was Muted

From 2009 through 2021, two forces slowed capitalism's response to high returns. First, less capital was directed toward rival supply. Asset-light models and offshoring reduced the need for new productive capacity, while more cash was returned to shareholders or deployed into acquisitions. Second, Internet 2.0 made some leading businesses harder to challenge as they grew. More users generated more data, attracted advertisers, strengthened distribution, and raised switching costs.

Less rival capacity was being built as digital barriers rose. Profit margins and returns on capital stayed elevated, investors treated those profits as durable, and valuation multiples expanded.

The 2010s didn't repeal capitalism, but they did subdue it.

The Return of Competition

Both conditions are now changing. Reshoring, supply-chain resilience, trade fragmentation, and infrastructure needs are pulling investment back into the cost base.

AI is changing the competitive architecture. Basic model capabilities are becoming more abundant, accessible, and substitutable. AI is also making once-expensive functions such as research, coding, marketing, customer service, and administration increasingly rentable.

Put simply, AI is capital intensive to build but increasingly capital light to use. That lowers the minimum scale and cost required to try to compete. Startups, adjacent incumbents, and even customers can attack established profit pools without recreating an incumbent's entire organization.

AI does not guarantee success, but it lowers the cost of trying. Incumbents need not disappear for their economics to weaken. They only need to capture less incremental profit, spend more to defend their position, lose pricing power, or earn lower returns on new investment.

What Changes for Investors?

The investment question is not simply who adopts AI; nearly every company will. It is whether a business earns above its cost of capital today, can compound by reinvesting at attractive incremental returns, and can keep the gains after customers and competitors respond.



Durable advantages will remain, but they are more likely to reside in what stays scarce and difficult to replicate, including physical capacity, proprietary context, trusted distribution, permissions, switching costs, and customer relationships.

The prior cycle rewarded exposure to established profit pools. The emerging cycle should instead reward selectivity. A capitalization-weighted benchmark adjusts after prices move, but fundamental investors can assess whether the economics are changing before the index does.

Renewed investment and AI are restarting the capital cycle, and when competition returns, stock selection should matter more than it has in some time. ▲

Keep in mind that all investments carry a certain amount of risk, including the possible loss of the principal amount invested.

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