



# 2023 RIA Investment Trends

January 2024

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Addepar's dataset reveals insights into timely investment trends. It serves as a unique point of comparison, especially for those with substantial allocations to alternative investments.

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**Confidential**

# Overview

Addepar is a multi-product software and data platform for even the most complex investment portfolios. When the company was founded in 2009, one of the most pressing challenges in financial services was a lack of transparency. Addepar was built with the mission of unlocking the power of informed, data-driven investing and advice. In keeping with that mission, we established Addepar Research to carry out research on investment organizations — their governance, management, operations and decision-making — by leveraging the power of the Addepar platform to understand and help improve collective performance.

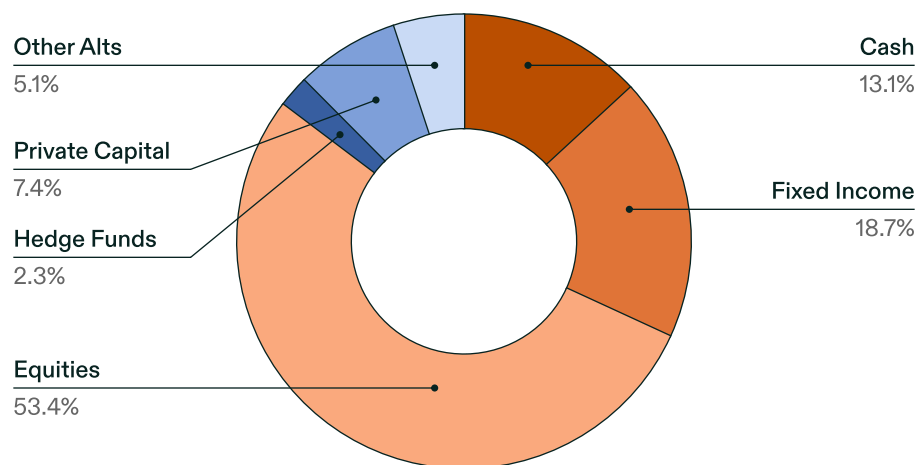
Year end is a time when most investment managers look ahead and make predictions. Yet, combining such forward outlooks with deeper analysis of what investors are doing with their portfolios *right now* can provide more holistic insights. Our findings are derived from the aggregated position and flow-level data from \$3.9 trillion on-platform assets. This analysis enables you to bridge between what is happening today and expectations regarding the next 12 months at the aggregate and asset-class levels.

There are two sections of this report: highlights of allocation trends across major asset classes and a spotlight on equities, the largest asset class for most portfolios. Our findings are largely consistent with studies on passive investment; however, these commonsense points are not as commonly applied as one might think.

To begin, we show the average portfolio asset allocation. Equities is the largest allocation at 53%. Alternative assets (e.g., hedge funds, private equity, venture, private credit, real estate) are an increasingly prominent feature of portfolio allocations, comprising 14% of a typical portfolio.

## Asset Allocation

December 31, 2023

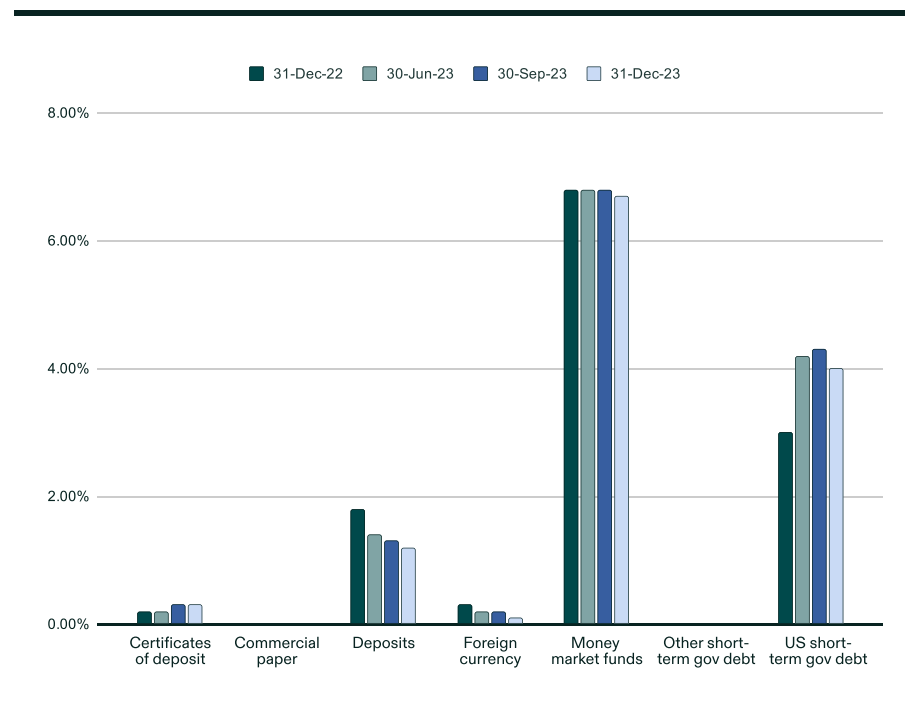


*Private Capital includes Private Equity, Venture Capital, and Private Debt. Other Alternatives includes mixed allocation fund of funds, other collective vehicles, commodities, collectibles, direct venture, and real estate.*

# Asset class allocation trends

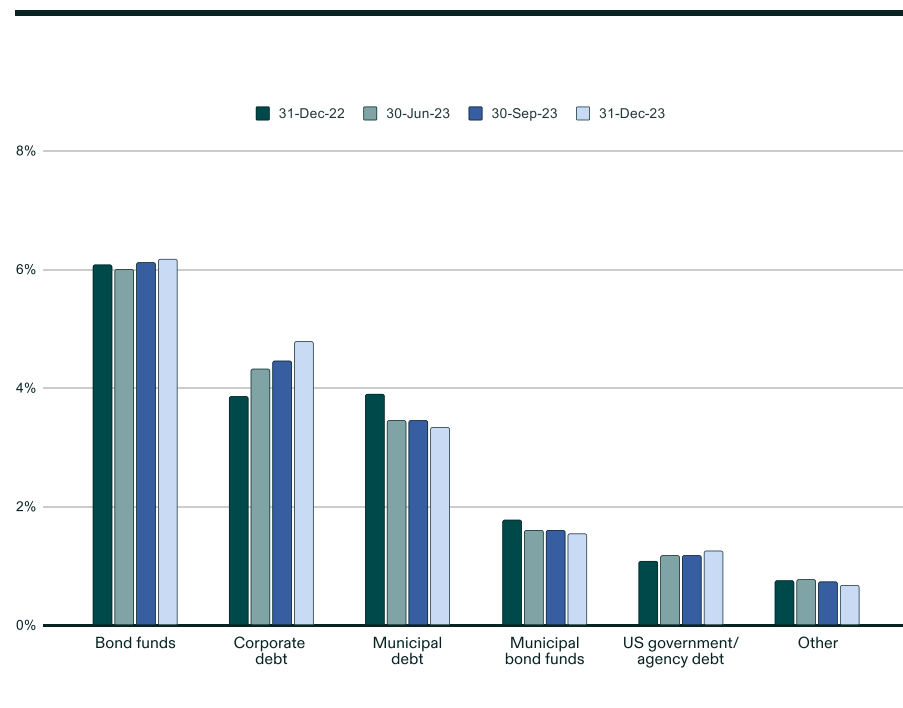
## Cash: High allocations and rotation from deposits to Treasury bills

Overall cash allocations are at their highest level since 2020. Portfolios modestly rotated from deposits to Treasury bills over the year.



## Fixed income: Increasing allocations to corporates

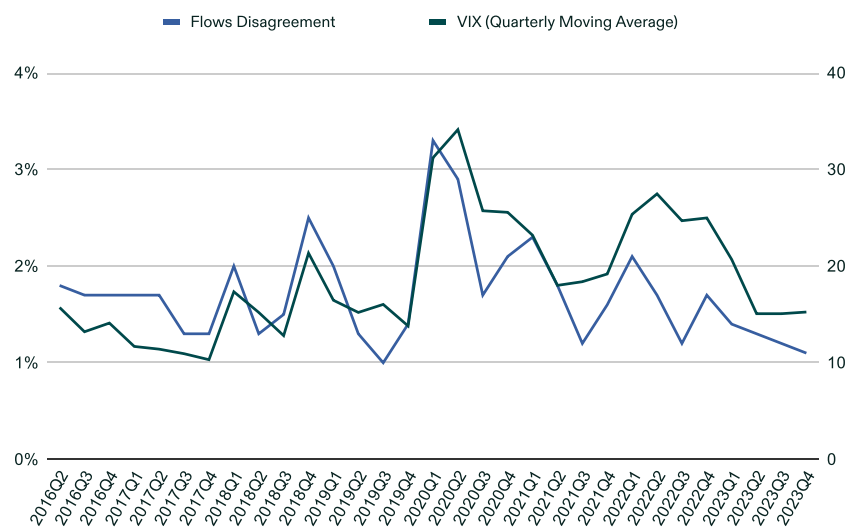
While holding overall allocations broadly consistent, portfolios added approximately 1% to corporate debt exposure on average over the course of the year.



*\*Other includes structured debt, international government, ABS/MBS, and agencies.*

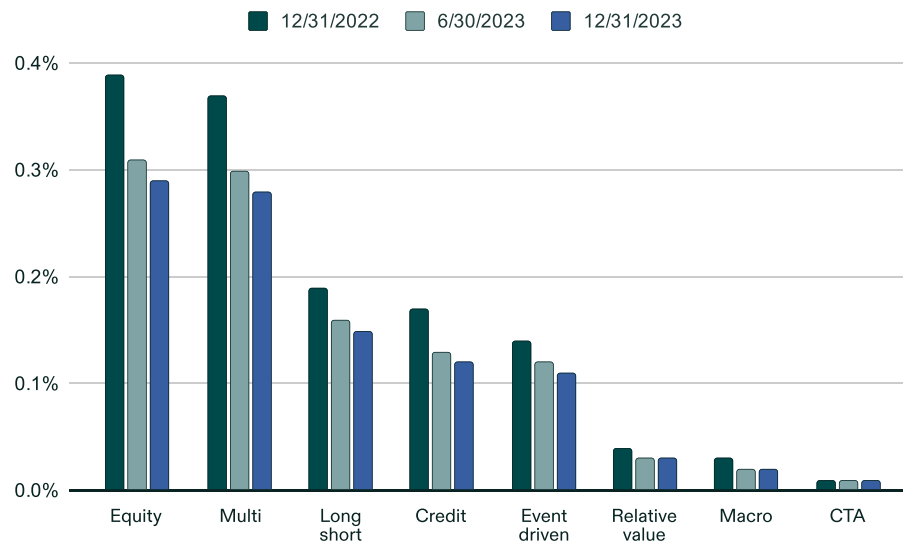
## Equities: Flows disagreement at its lowest level since 2016

Flows disagreement measures lack of consensus in direction of equity trading based on the magnitude of equity purchases relative to total portfolio sizes. On a historical basis, correlation is very high (.65) relative to VIX, a market measure of volatility. Broad-based economic strength, tempered inflation and consensus around a soft landing is manifesting in one of the lowest levels of flows disagreement since 2016.



## Hedge funds: Despite desire for diversification, allocations remain small and secularly declining

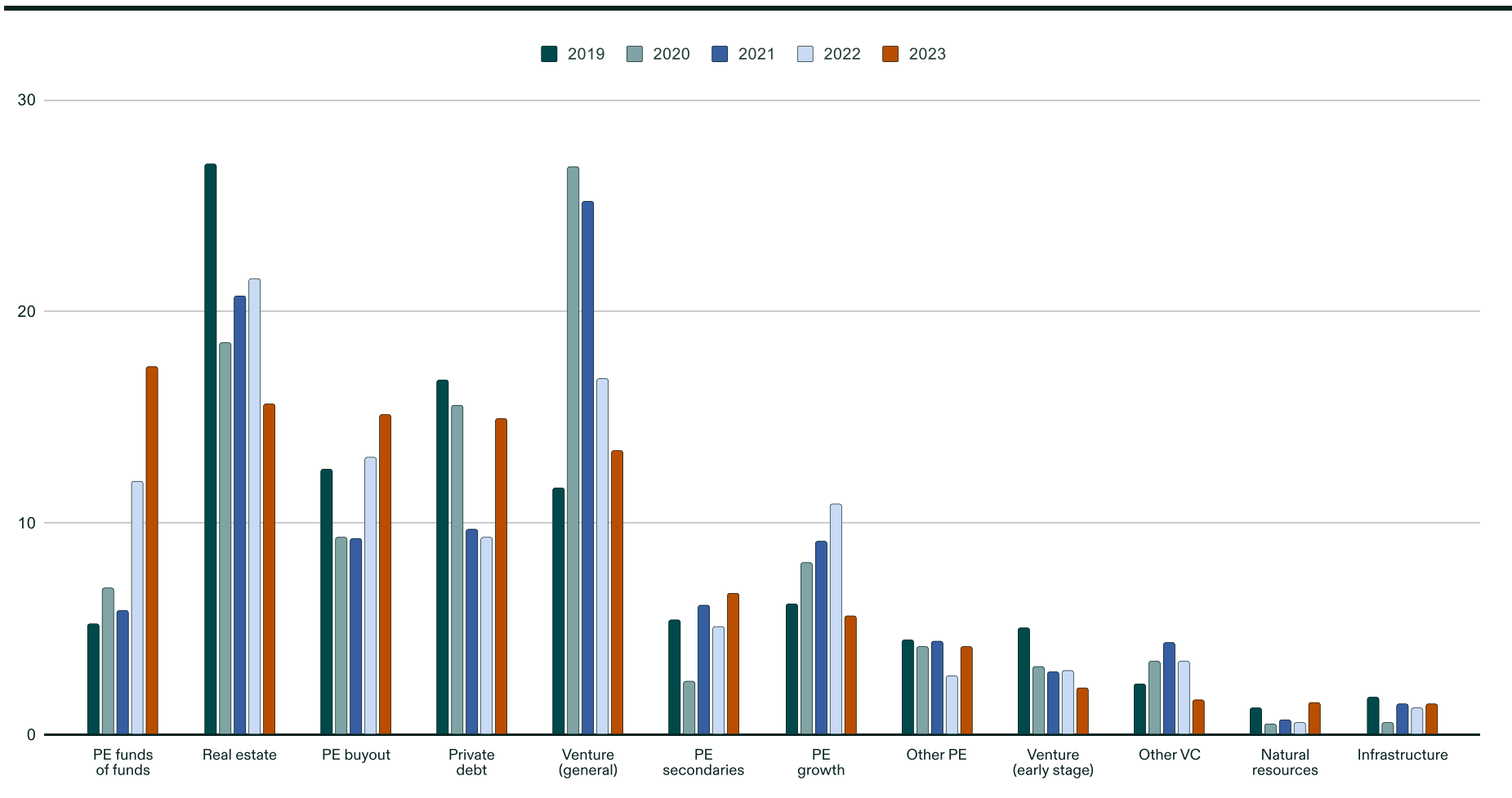
Coming into 2023, diversification through hedge funds (and other asset classes) was a significant area of discussion. Despite all the discussion, total allocations to hedge funds remain generally very small and continue to secularly decline across all strategies.



<sup>1</sup> Flows are measured as net cash flows over a portfolio's NAV. Flows disagreement measures the interquartile range of flows

## Private capital: Buyout commitments spike while venture declines

Venture and growth saw spikes in commitments in 2020 and 2021, with subsequent declines. Fund of funds, buyout and private debt had peaks in 2023.





# Spotlight

Warren Buffet, the ultimate proponent of passive investment, famously advised investors, “When trillions of dollars are managed by Wall Streeters charging high fees, it will usually be the managers who reap outsized profits, not the clients. Both large and small investors should stick with low-cost index funds.”<sup>2</sup>

In this spotlight, we share evidence that supports this claim by applying a classic factor modeling<sup>3</sup> technique to the Addepar dataset. This approach assesses the degree to which highly available return streams like the equity market explain a portfolio’s return. Our analysis covers portfolios with more than \$100,000 in portfolio value with more than two years of data comprising 67,000 portfolios.<sup>4</sup> Data is since January 2016.

Our analysis shows that a high proportion of portfolios are underperforming a passive strategy. At the same time, a relatively large number of investors are systematically generating positive alpha (returns from active management).<sup>5</sup>

The accompanying chart classifies portfolios along two dimensions: passive model fit<sup>6</sup> and alpha. Each quadrant<sup>7</sup> shows the percentage of portfolios ( $p$ ) and average alpha ( $\mu$ ). Overall, 71% of portfolios show high model fit. While this may seem high, previous studies on active mutual funds show even higher proportions. Some of this is due to concentrated positions held by owners/founders. Portfolios with low alphas comprise 60% of portfolios, which is slightly less than 50/50 odds, a pattern documented in many studies on active management. Each quadrant in this chart encapsulates a rich set of (over/under) performance stories, which we now describe.

<sup>2</sup> 2016 Berkshire Hathaway investor letter

<sup>3</sup> Three factor Fama-French. Analysis focuses on U.S. Equities, typically > 90% allocation for most equity portfolios

<sup>4</sup> Model results are not sensitive to the degree the panel is balanced

<sup>5</sup> Calculated at the equity portfolio level which is typically net of fees

<sup>6</sup> Measured by  $r^2$  of the regression

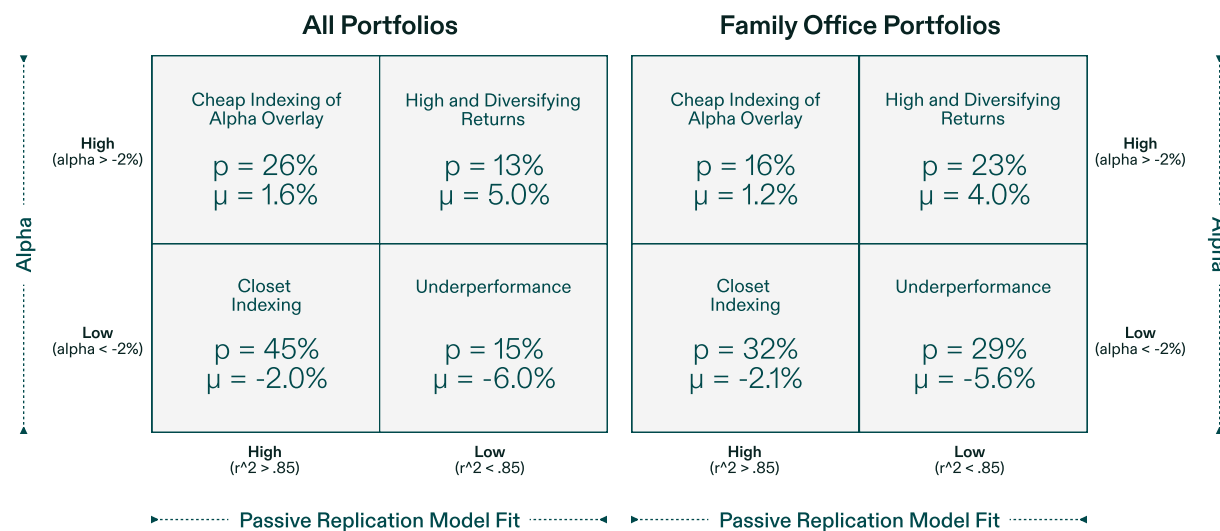
<sup>7</sup> Qualitative conclusions of this analysis are not dependent on thresholds set for each 4-box quadrant

**Closet indexing:** This is the quadrant occupied by a majority of investors, where, on average, portfolios are generating -2% of alpha using strategies that could instead have been replicated by passive market exposure. One of the simpler actions that could be taken to improve the returns of these portfolios is to transition to a passive replication strategy with low-cost index funds (i.e., move upward to the “High–High” quadrant).

**Cheap indexing or alpha overlay:** Approximately one-quarter of portfolios have generated a high alpha return and significant passive market exposure. If one has access, this quadrant is a great option for many investors.

**Underperformance:** While studies suggest that past performance is a very unreliable predictor of future performance, these return streams can have an outsized impact (given the magnitude of alphas).

**High and diversifying returns:** These are relatively desirable return streams due to their potential diversification impact, which depends on their level of correlation to equities. The fact that such a high proportion of high and diversifying return streams are represented in all portfolios, will be the topic of future spotlights.



Please reach out to us at [research@addepar.com](mailto:research@addepar.com) for deeper analysis and information on diagnosing your portfolios.

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