

Long Term Performance Remains High

Takeaways

- On average, performance was negative across equities, bonds and alternatives for the quarter and year, triggering a drawdown of a magnitude not seen by investors since the Global Financial Crisis and the 1970s (Appendix Exhibit A).
- Despite the recent drawdown, long-term performance remains high. The 10-year portfolio returns are well above long-term averages on an absolute and risk-adjusted basis.
- Alternatives, an asset class that's often held to diversify portfolios, did little to improve investor outcomes. Hedge fund returns tracked public equities, while private capital fund returns were muted.
- There were two notable exceptions. First, investors skilled in manager selection in private markets achieved some diversification by generating excess alpha. Second, investors with long-term or outsized allocations to commodities stocks and funds, and in particular energy, relatively outperformed peers.

Introduction

Addepar is a leading wealth management platform. 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 this mission, we established Addepar Research to carry out research on investment organizations—their governance, management, operations and decision-making—leveraging the power of the Addepar network to improve collective performance.

The platform natively supports all ownable asset categories, with a particular focus on alternative asset classes such as hedge funds and private equity. In this analysis, we focus on assets of independent registered investment advisors (RIAs) and single family offices (SFOs). This subset represents more than 275,000 portfolios with almost \$4 trillion in assets (see Exhibit 1).

Exhibit 1

RIA and SFO Assets Reported on Addepar USD

\$, Billions^{1,2}



The unique breadth and depth of the dataset generated by the Addepar platform offers transparency into the investment themes and trends of sophisticated high-net-worth (HNW) investors. Particularly for investors with a significant allocation to less-traditional investments, we hope to provide a relevant point of comparison that complements other benchmarking analyses.

¹ All analyses shown in the report exclude individual investments that exceed \$1 billion in value, along with very small and very large portfolios. This avoids introducing significant skew into the results.

² All values displayed are as of the end of Q2 in each year.

The goal of this particular report is to provide transparency into portfolio performance across the platform. We also regularly publish companion pieces that focus on asset allocation.

Q3 2022 performance

Let's first examine performance quartiles for the major asset classes (see Exhibit 2) for Q3 2022.

Exhibit 2

Aggregate Performance Quartiles by Asset Class

Percent, Q3 2022



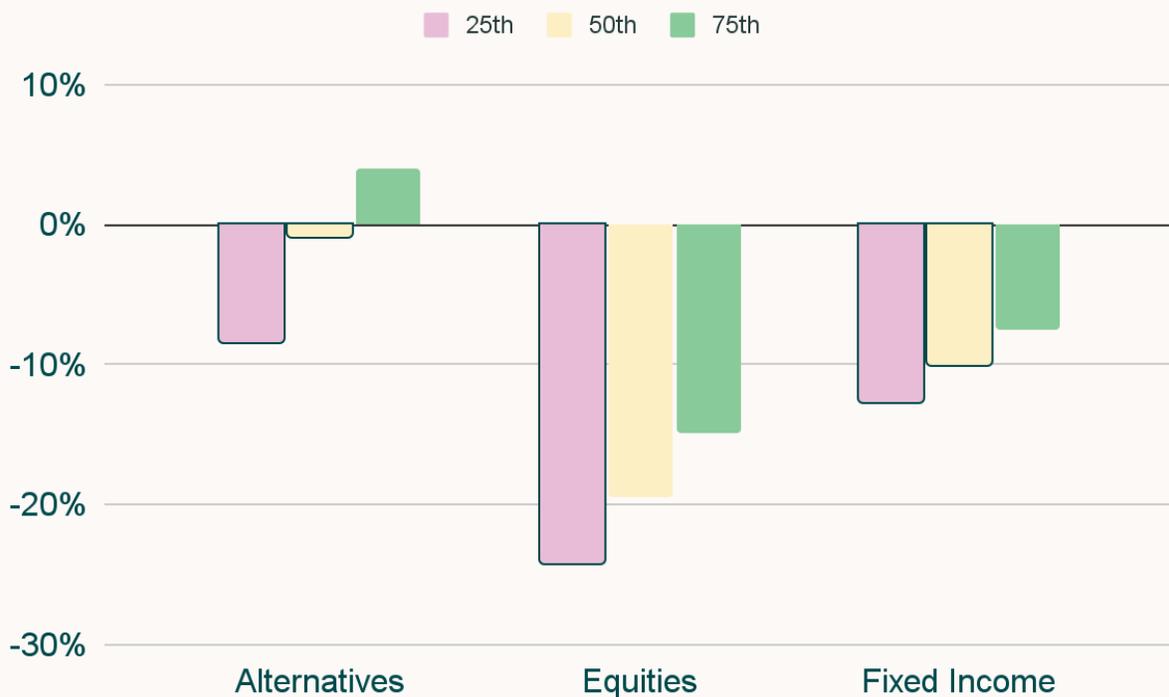
In the third quarter, portfolios had negative returns in each major asset class³. The median portfolio earned -6.7% in equities compared to -5.3% for the S&P 500. Fixed income portfolios

³ Major asset classes comprise more than 90% of asset allocations.

earned a median return of -3.2% compared to -7.6% in WGBI⁴. Median alternative returns were flat for the quarter. Unabating inflation prints flowed through to increases in expectations of Fed tightening and an economic slowdown—ultimately weighing down valuations of most assets.

Exhibit 3

Aggregate Performance by Asset Class
Percent, Q4 2021–Q3 2022



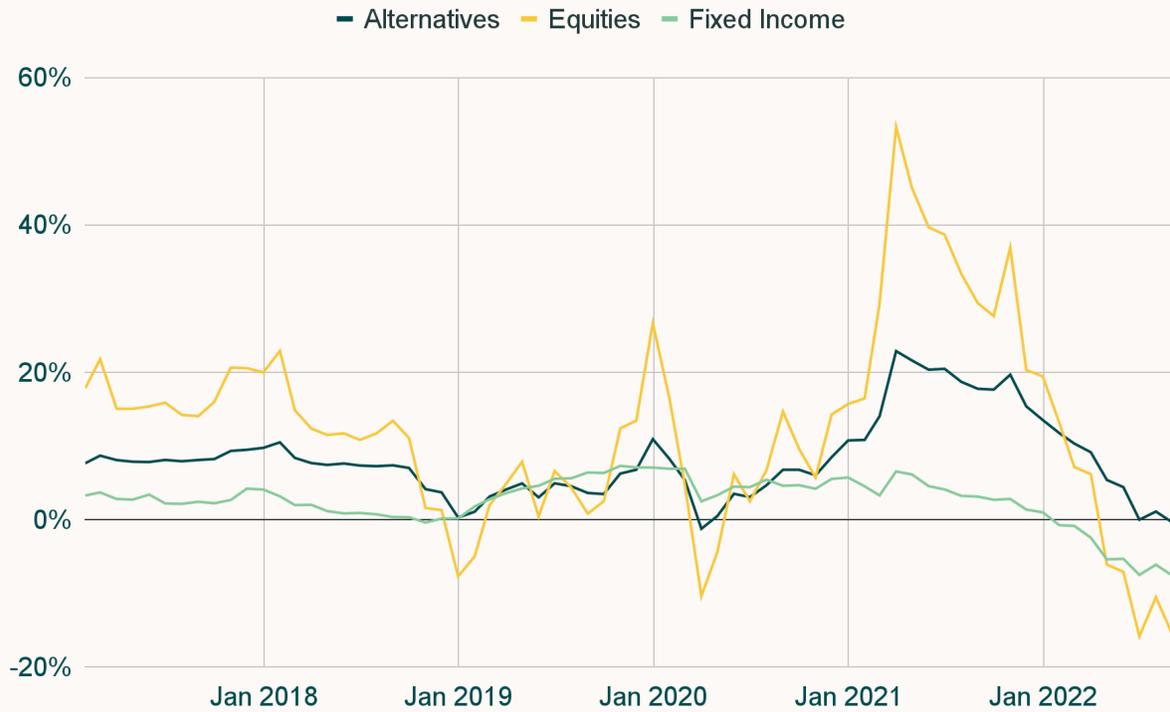
Third quarter performance contributed to all major asset classes experiencing negative returns over the previous year. **As Exhibit 4 shows, this is the first time in recent memory that, on average, clients have experienced simultaneous losses in equities, fixed income and alternative assets over the past year.**

⁴ World Government Bond Index

Exhibit 4

Aggregate Performance by Asset Class

Mean Cumulative 1-Year Rolling Returns by Asset Class



The downturn has negatively impacted long-term risk-adjusted returns, which remain comparable across asset classes. As Exhibit 5 shows, long-term Sharpe ratios have declined to approximately 0.25.

Exhibit 5

Median Portfolio's Asset Class Sharpe Ratio
Q1 2016 through Q3 2021 and Q3 2022

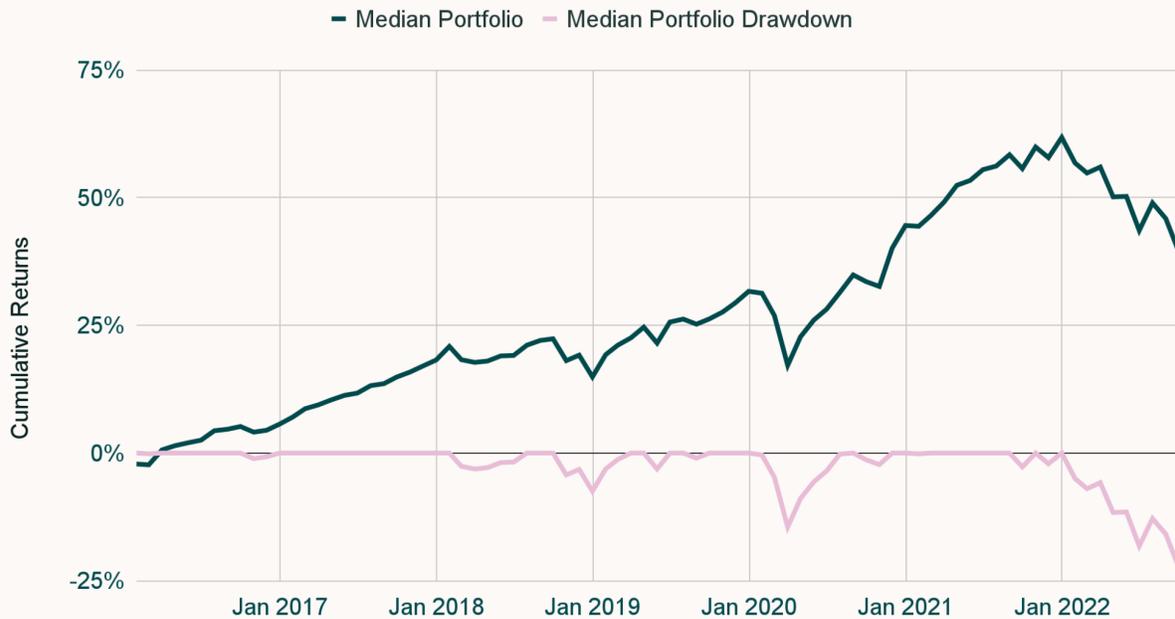


Performance across time

Investors have benefited from strong performance across asset classes over the long term. **Per Exhibit 6, at the aggregate portfolio level, long-term cumulative performance remains solid despite the 2022 drawdown, which is now longer and deeper than the drawdown at the onset of the pandemic in 2020.**

Exhibit 6

Cumulative Performance Q1 2016–Q3 2022

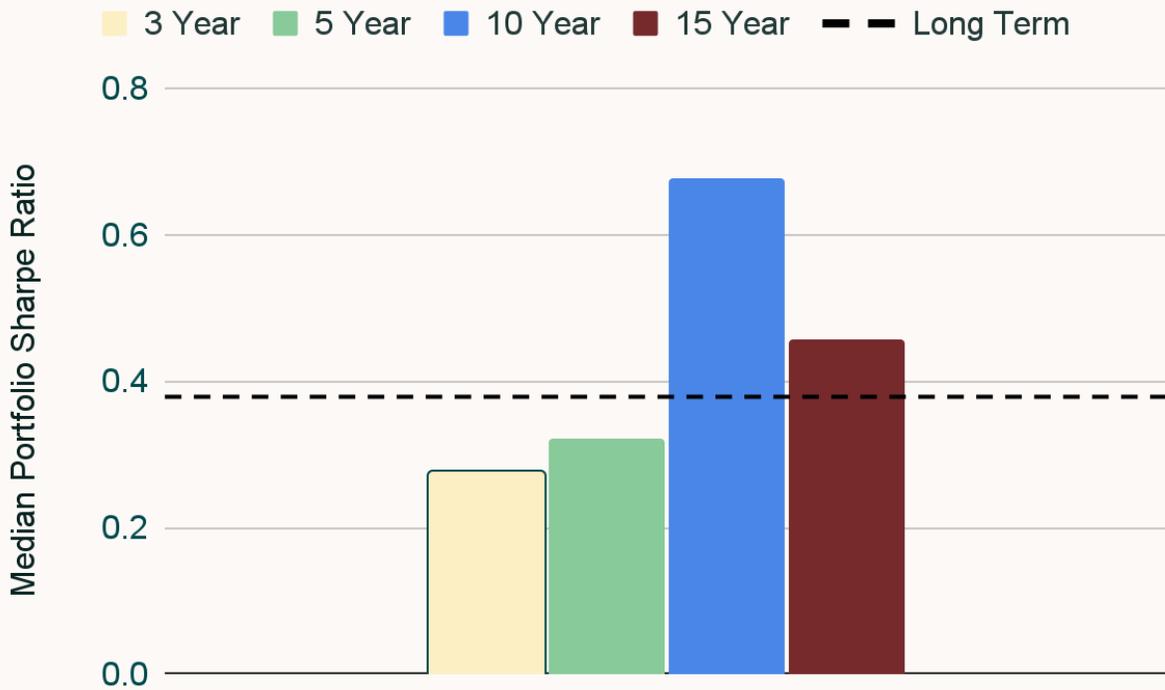


Although cumulative performance has recently declined, risk-adjusted performance continues to be significantly higher than the long-term average. **This means that for investors, a buy-and-hold strategy with a long-term perspective has continued to outperform historical norms.** Our Q3 2022 Asset Allocation Research Note shows relatively consistent asset allocations over time and minor derisking, indicating that portfolios generally remain positioned for the long term.

Exhibit 7

Risk-Adjusted Performance

Historical Sharpe Ratios as of Q3 2022



The above chart presents median portfolio Sharpe ratios⁵ over various time periods ending in Q3 2022. Sharpe ratios are muted over the past three to five years relative to 10, 15 or more years.

Portfolio and asset-class performance

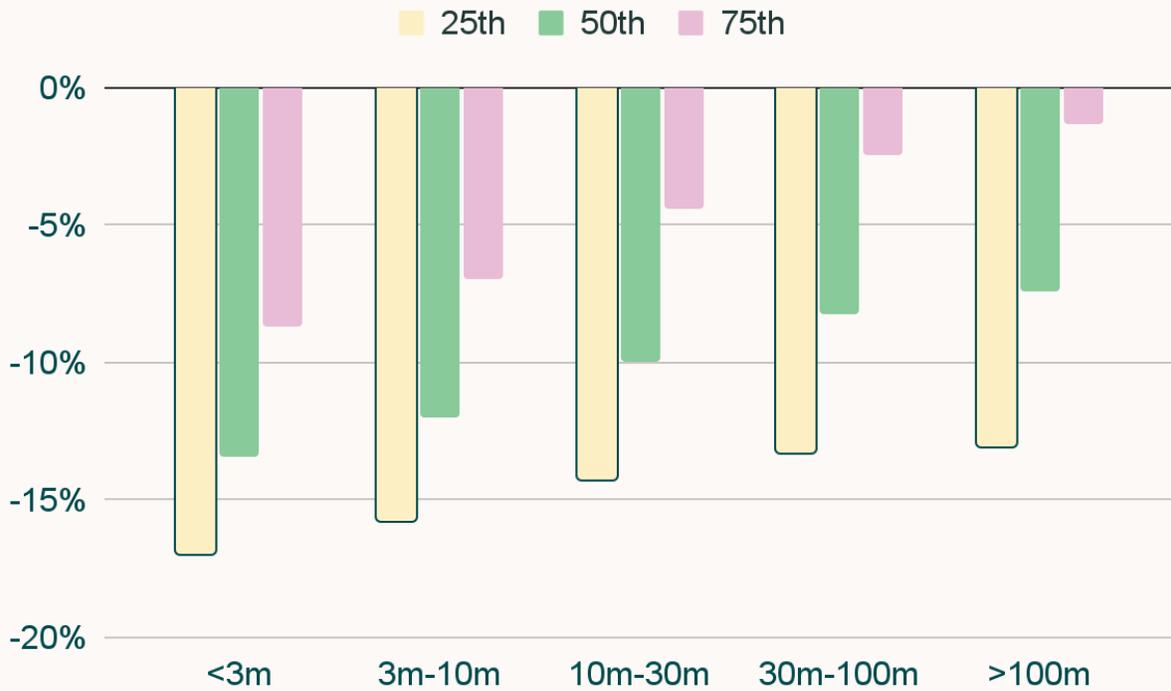
In general, the very largest portfolios tended to outperform. This pattern is particularly pronounced at the 75th percentile.

⁵ Median portfolio return of all portfolios that have been in our dataset from January 2016 through Q3 2022. Prior to Q1 2016, we used the 60/40 portfolio's returns employing the S&P 500 and U.S. Government Bond indices. Long-term Sharpe ratio is based on returns from 1970 to present.

Exhibit 8

Aggregate Performance by Portfolio Size⁶

Cumulative Return, Q4 2021– Q3 2022



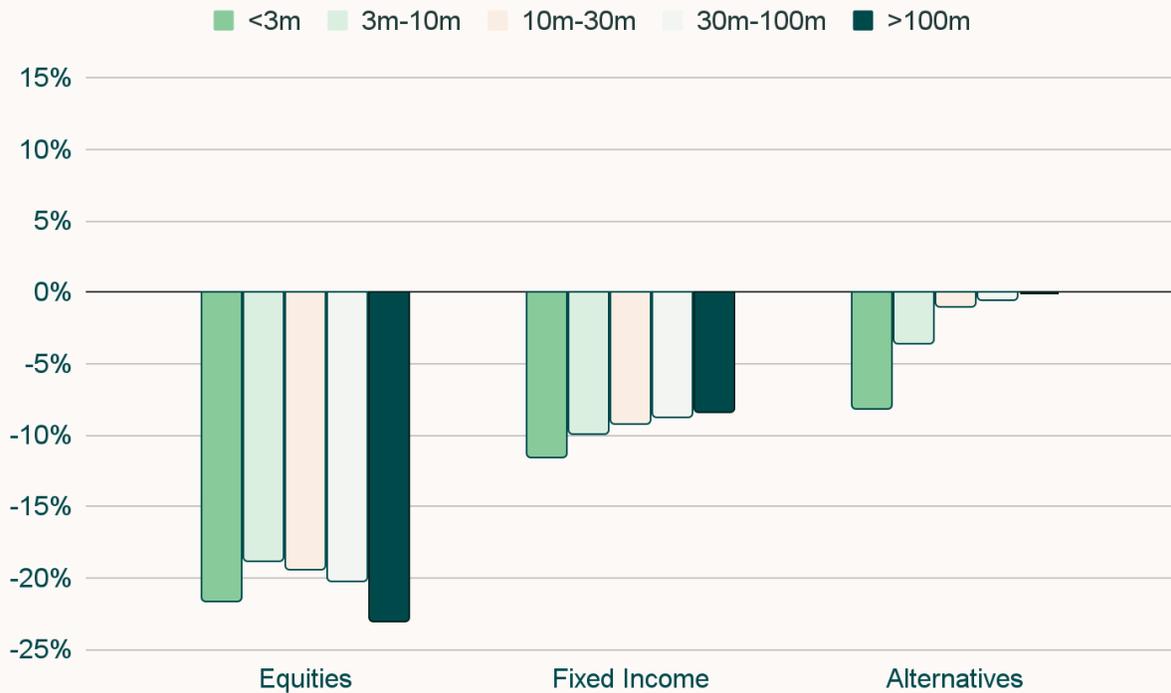
Outperformance of larger portfolios is primarily due to higher allocation of alternatives and better returns in alternatives investments.

⁶ Portfolios grouped by size include RIA and FO client assets.

Exhibit 9

Asset Class Performance by Portfolio Size

Cumulative Return, Q4 2021–Q3 2022

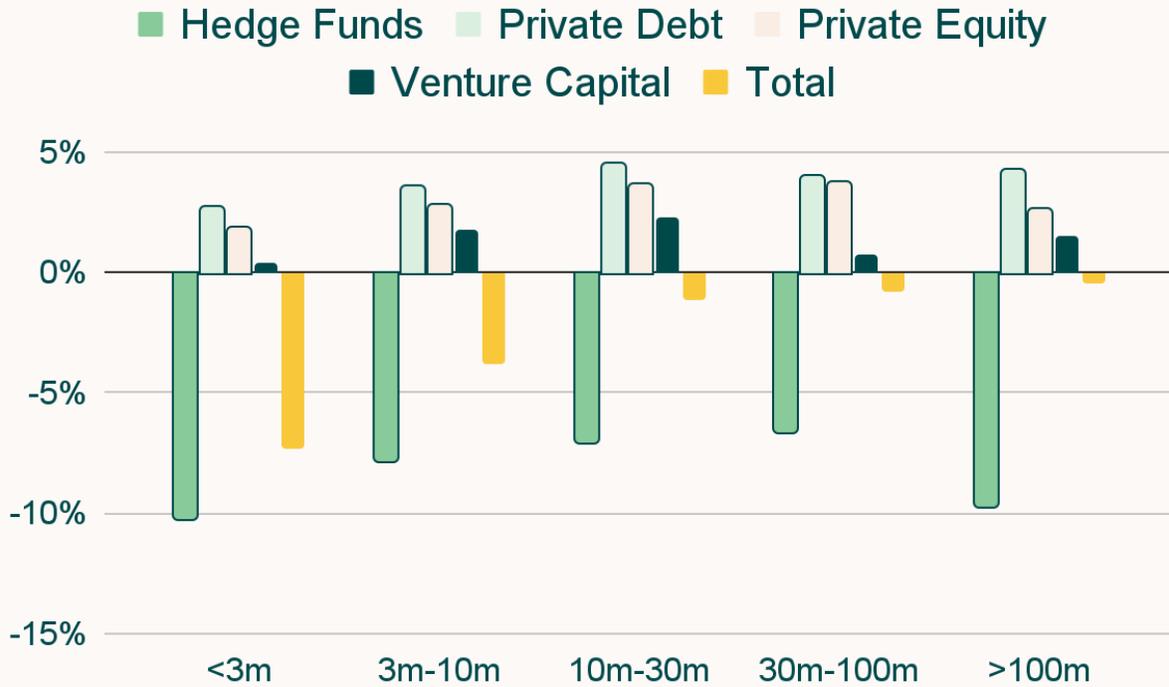


Alternatives:

In aggregate, alternatives returns for the year ending Q3 2022 are negative for the average investor. This is primarily due to hedge funds dragging down returns within the asset class. Also, as previously noted, larger portfolios are generally producing higher returns in alternatives. This can be attributed to the larger portfolios' smaller allocations to hedge funds (see Asset Allocation Research Note).

Exhibit 10

Performance of Alternatives by Portfolio Size
Percent, Q4 2021–Q3 2022



The negative hedge fund returns are unsurprising because median hedge fund returns generally track equity markets (correlations are 0.85). Exhibit 11 presents the six-month cumulative rolling average of the median HNW investors' equity and median portfolio hedge fund⁷ returns from Q2 2017 through Q3 2022. The hedge fund returns closely track the returns of equities, largely due to equity beta packaged into hedge funds.

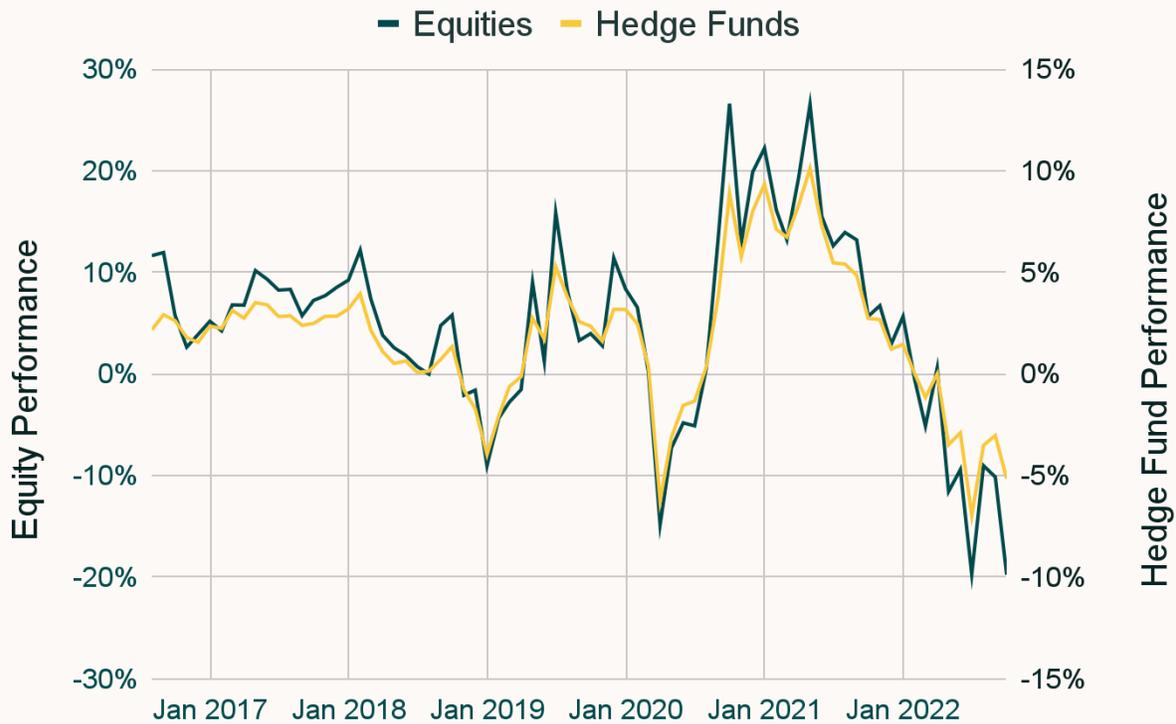
When aggregating returns across hedge funds, the idiosyncratic risk in individual funds is effectively diversified across all hedge fund investments. Therefore, aggregate hedge funds

⁷ Note that the median hedge fund is not the same each period. It's sampled independently from the set of hedge fund returns for individual time periods.

effectively achieve an equity-like return. A similar phenomenon can be observed with hedge fund indices such as the HFRI (see Appendix Exhibit B).

Exhibit 11

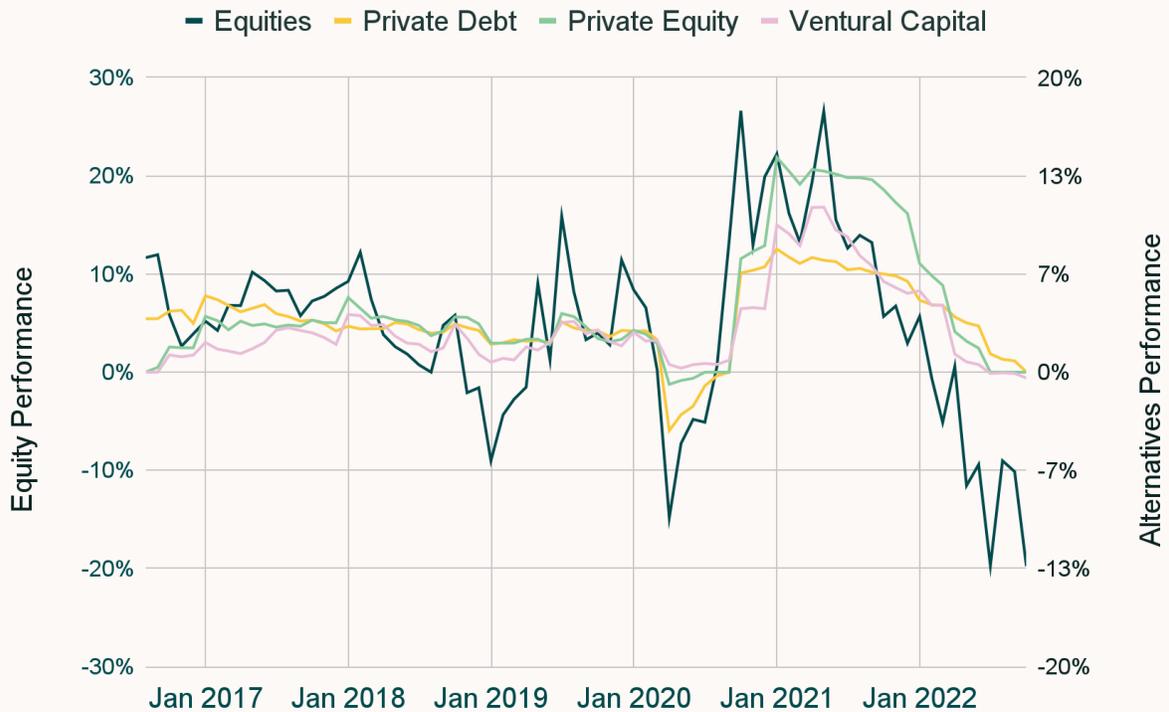
Median HNW Equity and Hedge Fund Returns
6-Month Cumulative Return Rolling Average



While median hedge funds have depressed returns for alternatives in aggregate, returns on other private capital investments such as private equity and venture capital have fallen to near zero. As illustrated in Exhibit 12 and examined in depth in our PE Benchmarking Addepar Research Brief, aggregate private equity returns track smoothed and lagged public-market equity returns. **If history bears this out and public markets continue their drawdown, we may see some negative private equity returns in the near future.**

Exhibit 12

Mean Equity and Private Capital Returns on Platform 6-Month Cumulative Return Rolling Average



Although aggregate returns in alternatives have historically tracked public market equivalents, they remain a popular asset class due to the alpha potential in manager selection. As shown, skilled investors who are able to identify and select high-quality managers, may be able to generate ample alpha returns.

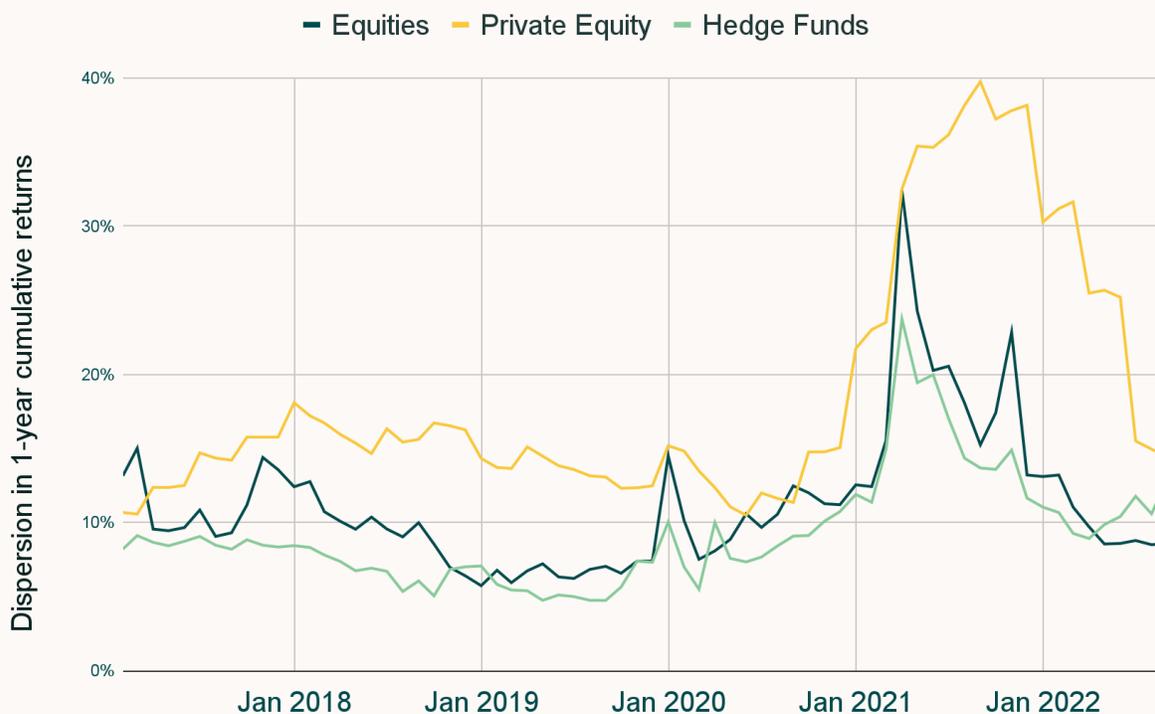
Below, we highlight the amount of dispersion in 1-year cumulative returns in public equity, private equity and hedge fund investments from Q1 2017 through Q3 2022. We measure dispersion by subtracting the 25th percentile cumulative return for each asset class from the 75th percentile cumulative return for that asset class. We see that over time, HNW investors have experienced

similar dispersion in equities and hedge funds—with higher dispersion in their private equity investments.

Notably, median equity returns have shown twice the volatility as hedge funds, and yet they have the same dispersion, which implies that in a relative sense (or risk-adjusted sense), hedge funds have more dispersion than equities. On the other hand, private equity has twice the dispersion of public equity, while having half the volatility around the median. Therefore, alts (and private equity in particular) show roughly two to three times the dispersion of public equities on a risk-adjusted basis over the past six years. **HNW investors who are skilled at choosing private capital managers have done well by investing in private equities and hedge funds because there's been more room for them to achieve excess alpha returns above what's attainable in public markets.**

Exhibit 13

Dispersion in 1-Year Cumulative Returns
75th Percentile–25th Percentile Cumulative Rolling Returns

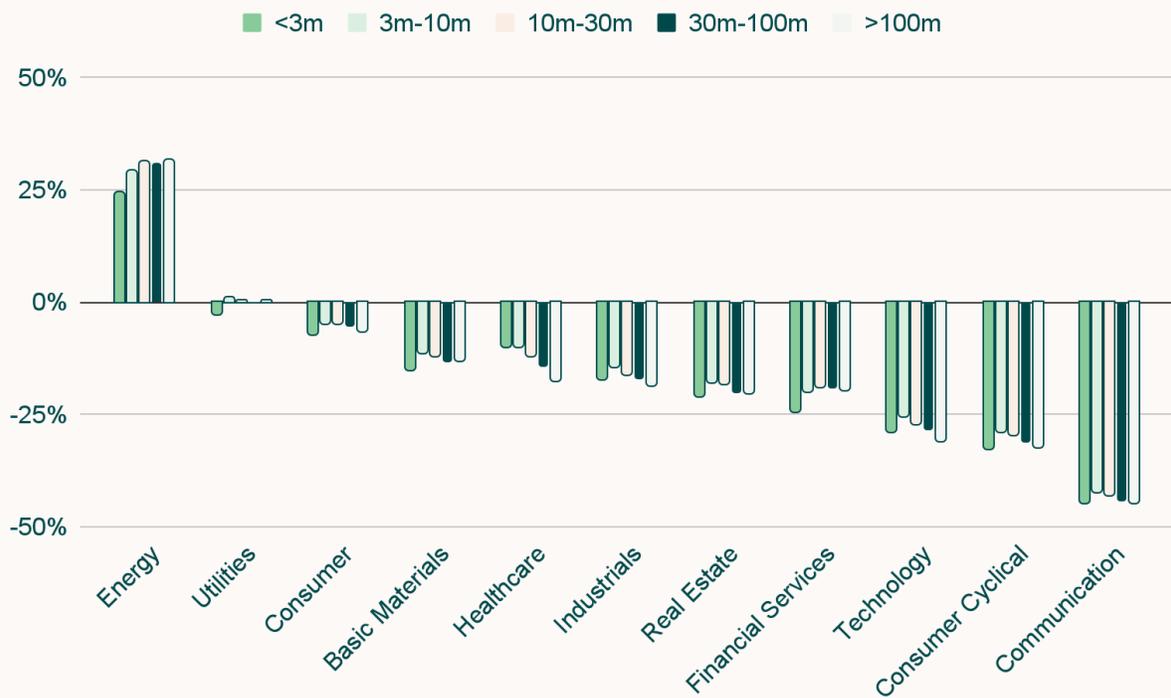


Equities:

In equity markets, 10 of 11 sectors had negative returns. The past year's rising energy prices buoyed the energy sector, while sectors with more growth-oriented stocks such as communications, cyclicals and technology underperformed. Due to the longer cash flow duration of growth stocks, these were more heavily impacted by rising discount rates and more recently, by concerns over decreased earnings as the economy slows.

Exhibit 14

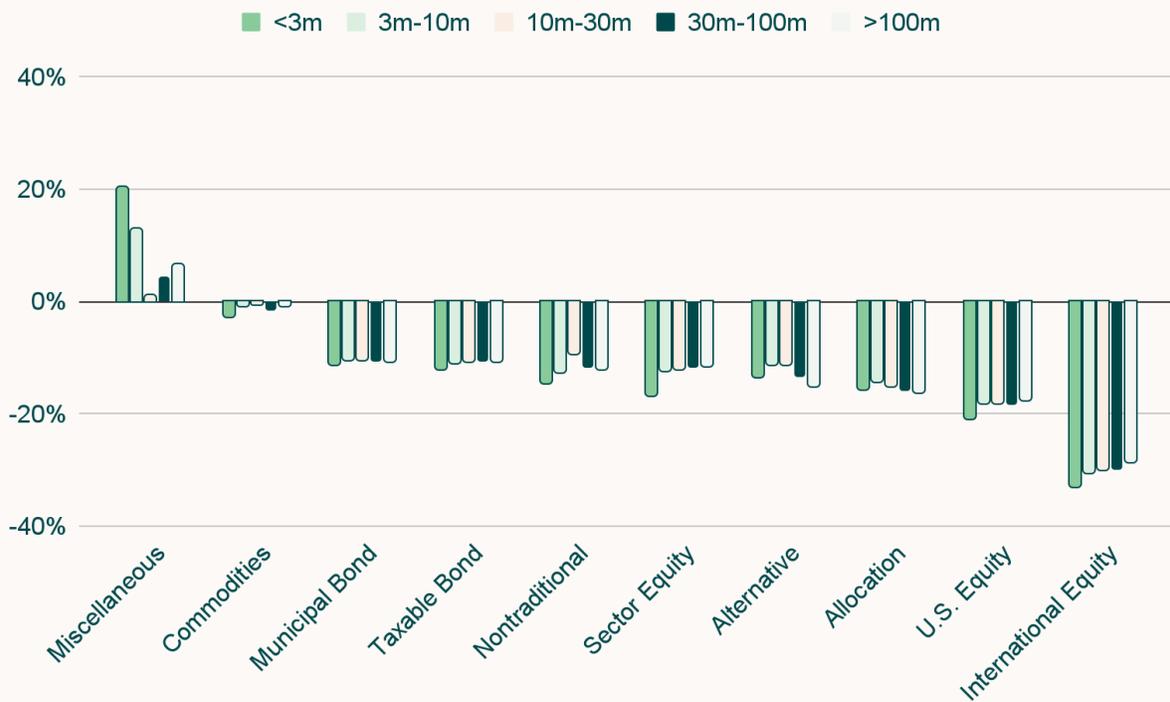
Equity Returns by Sector and Portfolio Size
Percent, Q4 2021–Q3 2022



Among funds, all but the miscellaneous category had negative returns. Largely due to energy, commodity funds provided flat returns, while U.S. and international equity funds fell into bear market territory.

Exhibit 15

Mutual Fund and ETF Returns
Percent, Q4 2021–Q3 2022



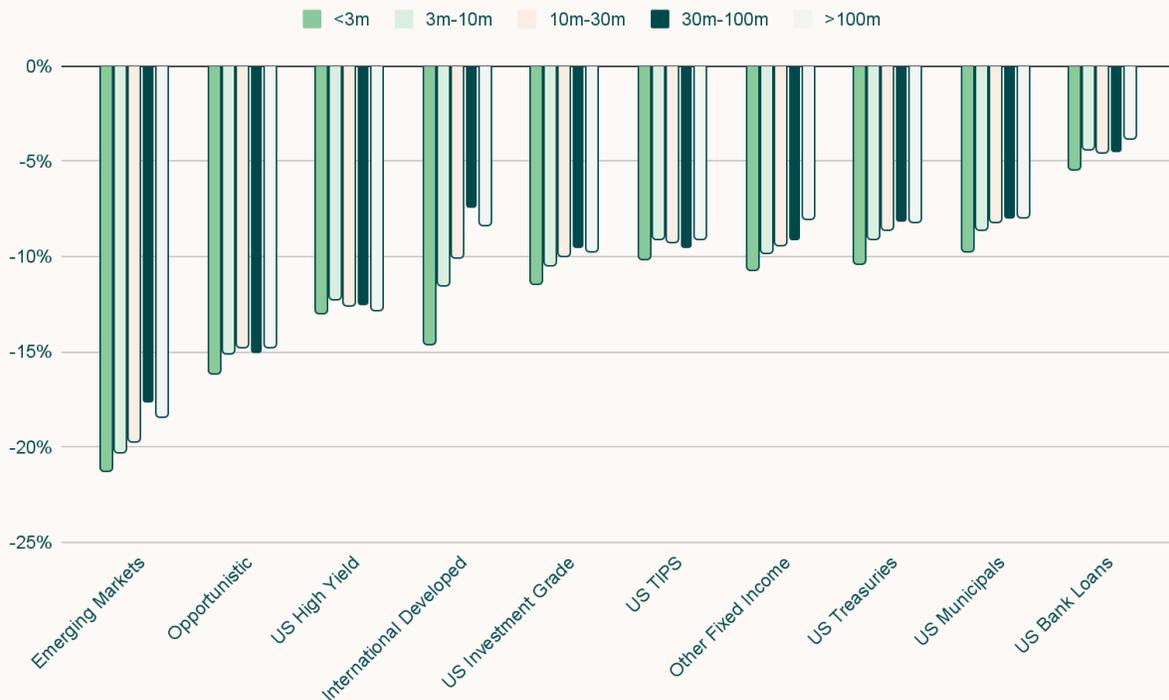
Fixed income:

The following figure shows returns for fixed income instruments over the past year, broken out by portfolio size. **Fixed income performance was negative year over year across every sub-asset class we track.** Both rates and spreads have sold off, leading to the worst performance in the highest-risk asset classes such as emerging markets and high-yield instruments. In the most recent quarter, rates continued to sell off strongly, while spreads were slightly wider—leading to

more even losses across the sub-asset classes.

Exhibit 16

Fixed Income Returns by Instrument Type and Portfolio Size
Percent, Q4 2021–Q3 2022



Conclusion

We've provided a range of views and transparency into the performance of portfolios represented on the Addepar platform. We continue to publish updates to these views on a quarterly basis, and also invite you to review our companion piece on Q3 2022 portfolio positioning.

Please email research@addepar.com if you have any questions or suggestions for how this publication can be improved.

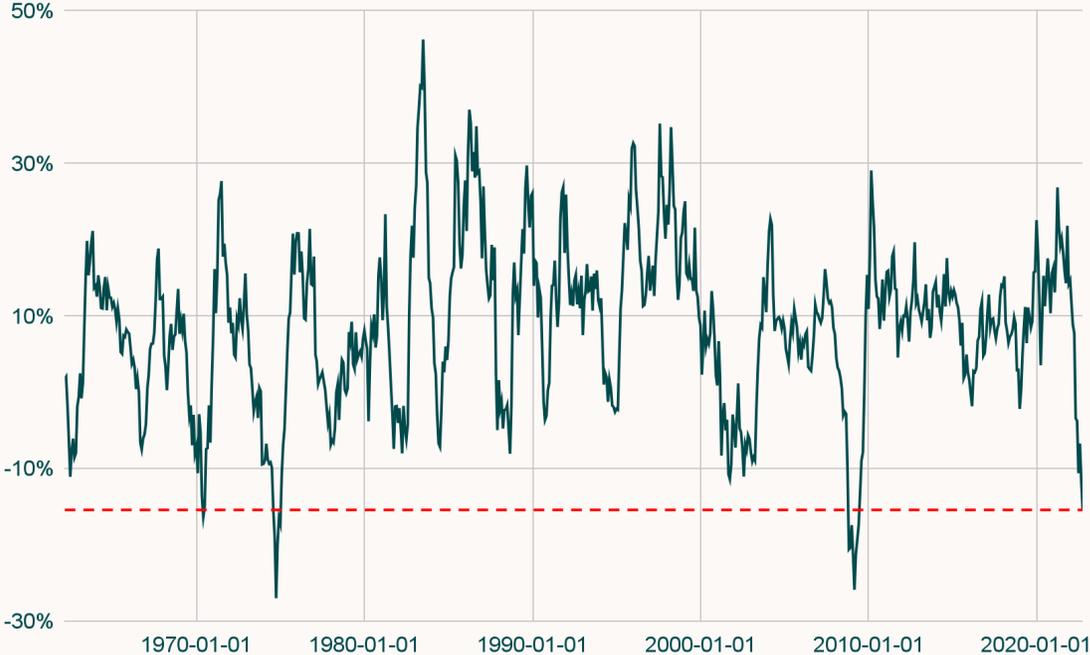
Appendix

Asset Classifications

| Asset class | Sub-asset class |
|---------------------------|---|
| Cash | Cash Cash equivalents |
| Fixed income | U.S. Treasuries and Agencies U.S. TIPS U.S. investment-grade credit U.S. high yield U.S. bank loans International developed markets Emerging markets Opportunistic Other fixed income Unknown fixed income U.S. municipals/tax exempt |
| Equities | U.S. equities Global equities Developed markets–Americas Developed markets–EMEA Developed markets–Asia Pacific Emerging and frontier markets Other equities Concentrated equity positions Unknown equities |
| Mixed allocation | Asset allocation vehicles Held-away accounts |
| Alternatives | Hedge funds Concentrated alts positions Private equity & venture Real estate funds Other alts Unknown alts |
| Private business | Direct private companies |
| Direct real estate | Direct real estate |
| Other | Collectibles Direct loans Unknown Liability |

Exhibit A

60/40 Portfolio's Return
1-Year Rolling Average, Q1 1962 - Q3 2022

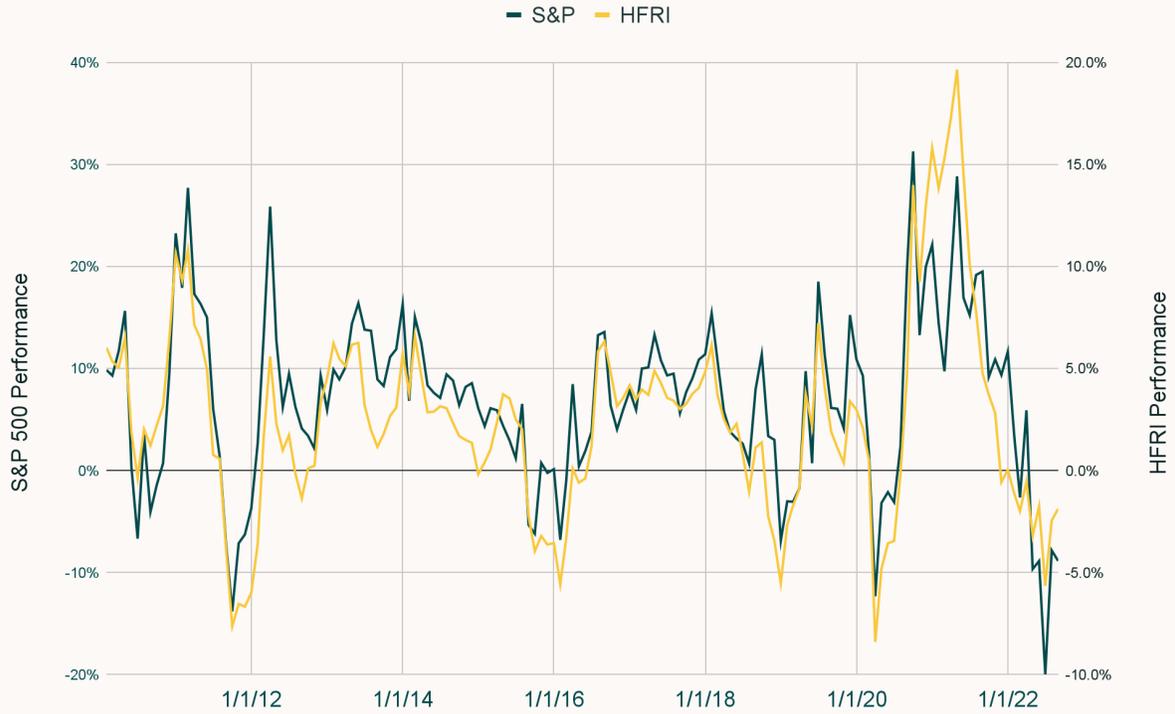


Source: Thomson Reuters

Exhibit B

HFRX Equal Weighted Strategies Index vs. S&P 500 Returns

6-Month Rolling Returns, Q1 2010–Q3 2022



Source: Thomson Reuters

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