



2023 Family Office Investment Trends

January 2024

Addepar's dataset reveals insights into timely family office 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.

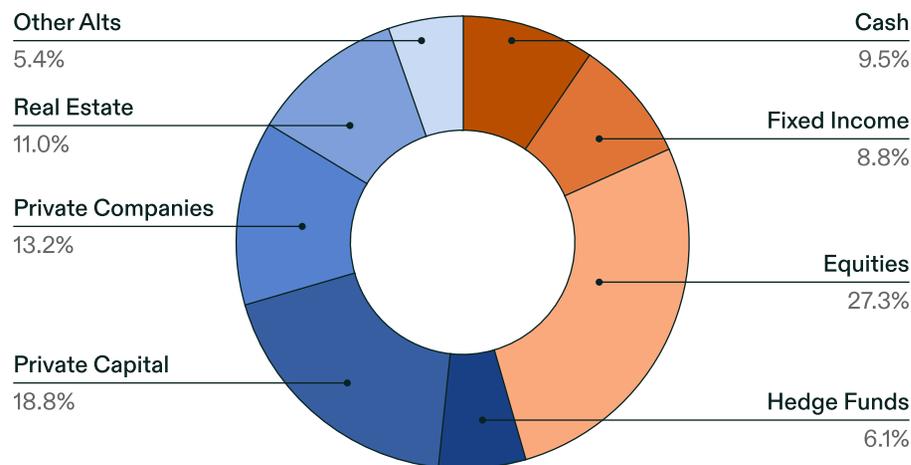
Year end is a time when most investment managers look ahead and make predictions. Yet, combining such forward outlooks with deeper analysis of what investors are doing with their portfolios *right now* can provide more holistic insights. Our findings are derived from the aggregated position and flow-level data from \$1.2 trillion on-platform assets compiled from 530 family offices. 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 asset allocation for a family office. Equities is the largest allocation at 27%. Alternative assets (e.g., hedge funds, private equity, venture, private credit, real estate) are an increasingly prominent feature of family office allocations, comprising 55% of a typical portfolio.

Asset Allocation

December 31, 2023

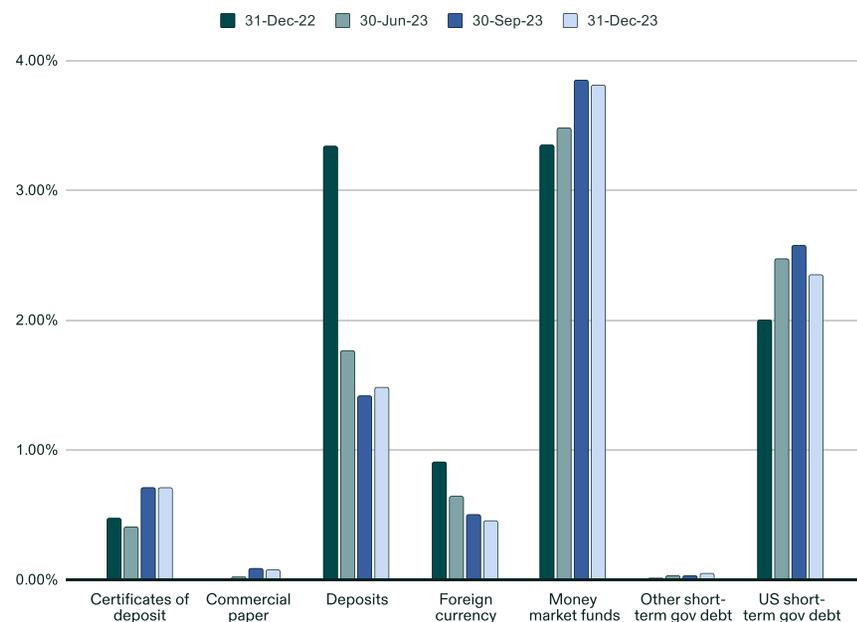


Private Capital includes Private Equity, Venture Capital, and Private Debt. Other Alternatives includes mixed allocation fund of funds, other collective vehicles, commodities and collectibles.

Asset class allocation trends

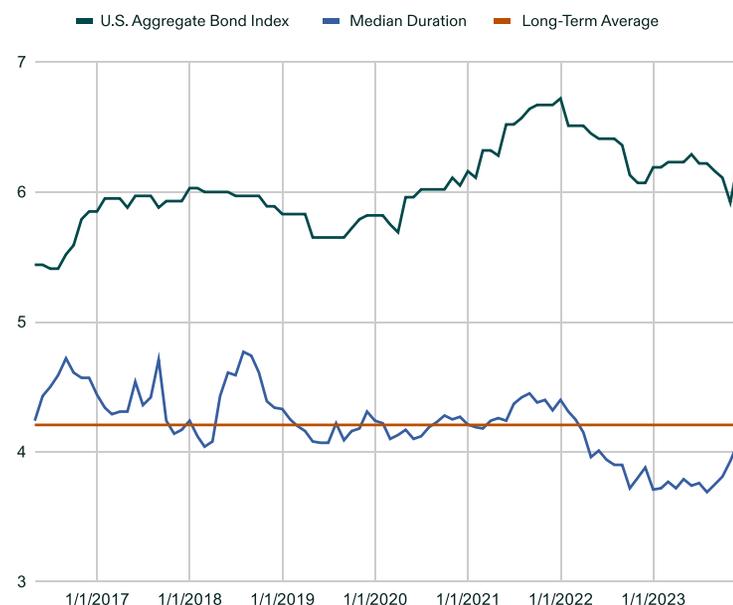
Cash: Rotation from deposits to low duration Treasury bills

After significant turbulence in the last few years, cash allocations have converged to approximately the long-term average.¹ Family offices reduced deposits and added to Treasury bills, money market funds and certificate of deposit exposures over the year. While generally low, the average maturity of Treasury bills drifted up from an average maturity of 3 months to 3.5 months during 2023.



Fixed income: Index duration increasing while duration held steady

U.S. Aggregate Bond Index duration (interest rate sensitivity) is at its highest level since 1976, while market interest rate volatility has increased back to historical norms from very low levels over the last decade. All else equal, portfolios tracking indices are experiencing increased exposure. On average, family office portfolios are holding 4.1 years of duration, slightly below the long-term average.

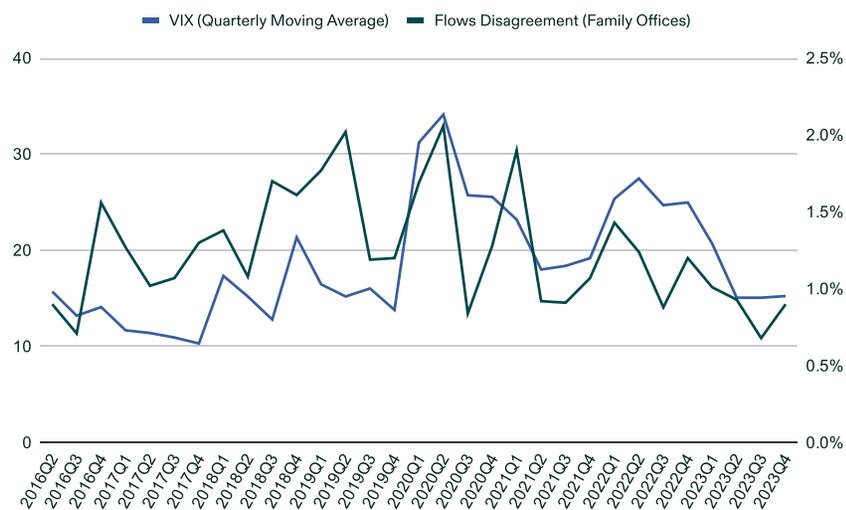


*Median duration excludes short rates

¹ Measured since January 2016

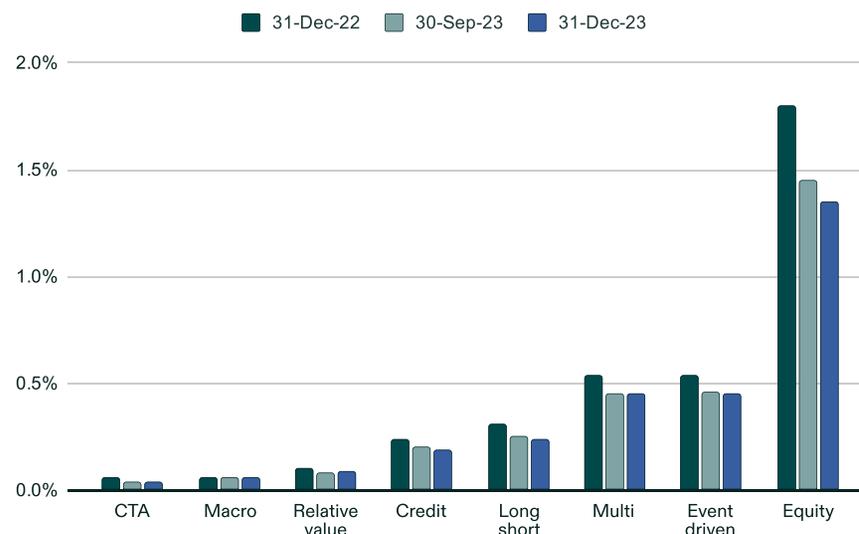
Equities: Flows disagreement at its lowest level since 2016

Flows disagreement² measures lack of consensus in direction of equity trading based on the magnitude of equity purchases relative to total portfolio sizes. 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. On a historical basis, flows disagreement and VIX are moderately correlated.



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

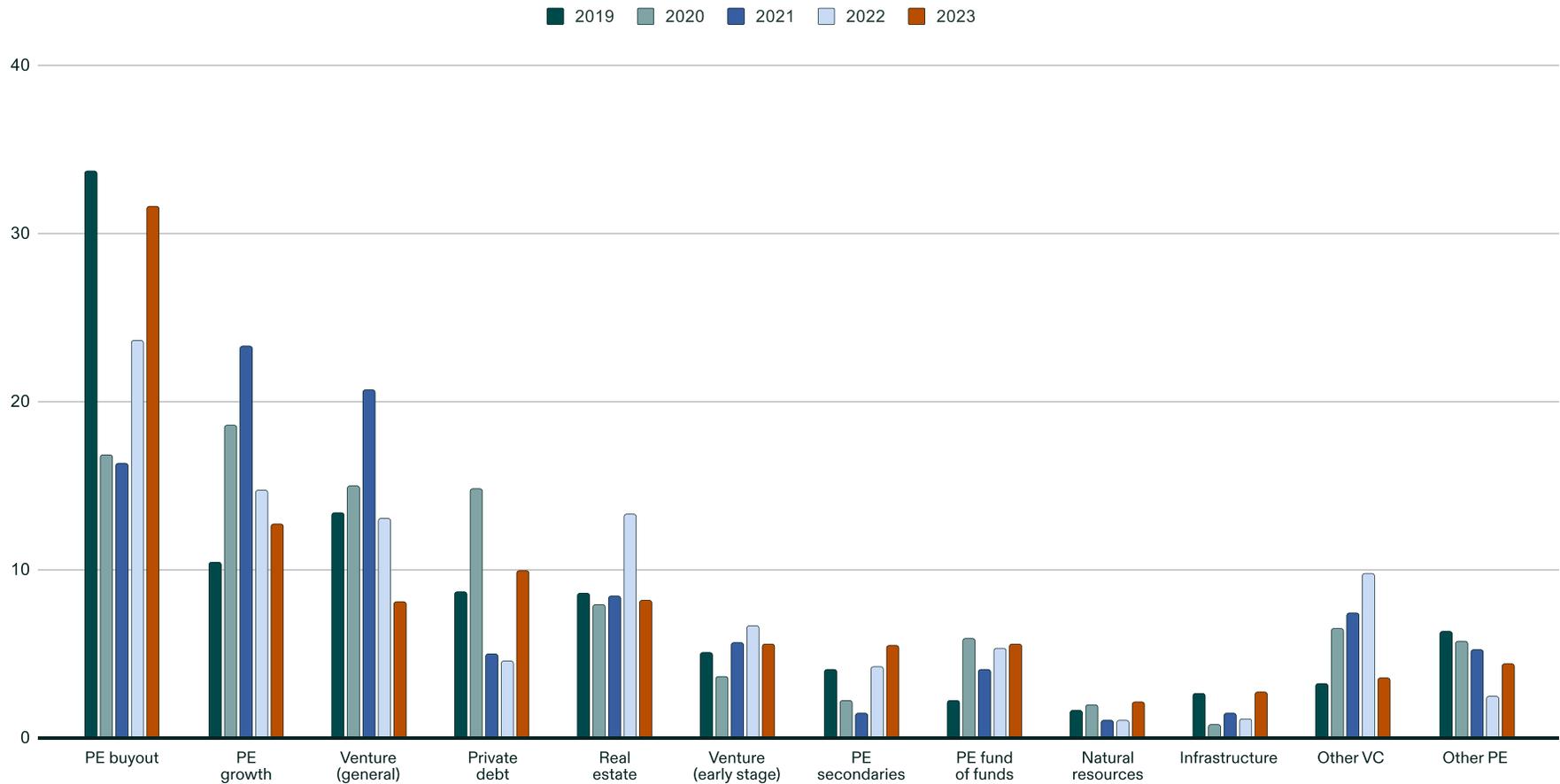
Coming into 2023, diversification through hedge funds (and other asset classes) was a significant area of discussion. Despite all the discussion, total allocations to hedge funds remain generally small and continue to secularly decline, particularly in equity strategies.



² 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. Buyout saw increases in 2022 and 2023. Private debt had a modest peak in 2023.



Spotlight

Warren Buffett, 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.”³

In this spotlight, we share evidence that supports this claim by applying a classic factor modeling⁴ 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.⁵ 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, many of whom are managed by family offices, are systematically generating positive alpha (returns from active management).⁶

The accompanying chart classifies portfolios along two dimensions: passive model fit⁷ and alpha. Each quadrant⁸ shows the percentage of portfolios (p) and average alpha (μ). 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.

³ 2016 Berkshire Hathaway investor letter

⁴ Three factor Fama-French. Analysis focuses on U.S. Equities, typically > 90% allocation for most equity portfolios

⁵ Model results are not sensitive to the degree the panel is balanced

⁶ Calculated at the equity portfolio level which is typically net of fees

⁷ Measured by r^2 of the regression

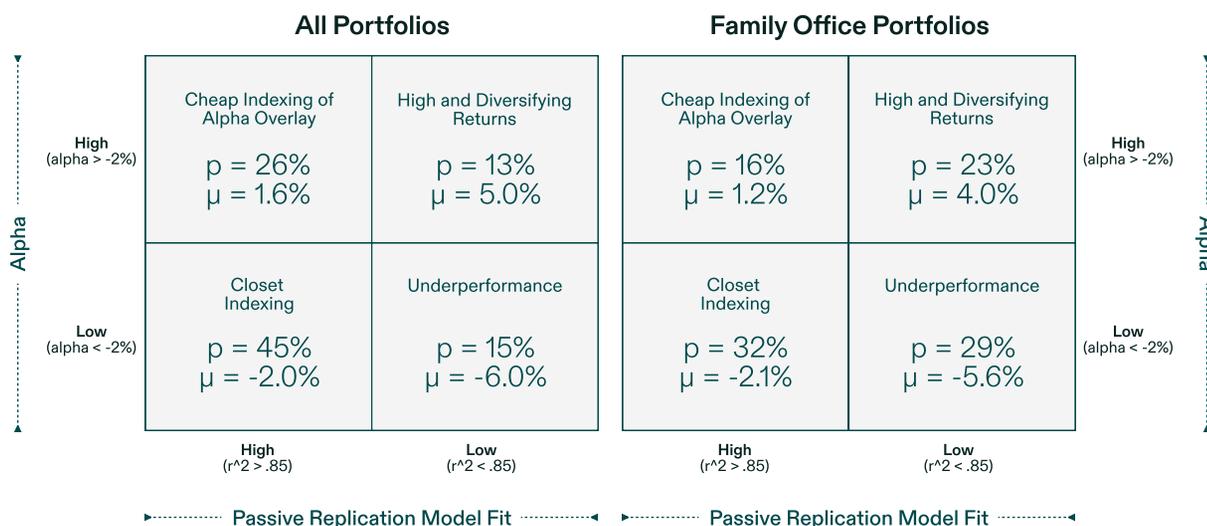
⁸ Qualitative conclusions of this analysis are not dependent on thresholds set for each 4-box quadrant

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—although interestingly, it is the smallest quadrant for family offices.

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, particularly within family offices, will be the topic of future spotlights.



Please reach out to us at research@addepar.com for deeper analysis and information on diagnosing your portfolios.

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