
Portfolios are derisking

Asset Allocation Research Note | July 2023

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Introduction

At Addepar, we've been working on developing improved asset classification to provide you with higher resolution analytics. In this note, we'll share our standard asset allocation analytics with additional granularity to the sub-asset class level. In the first section we share trends in broad asset allocation and flows. We then dive into allocation and flows for each asset class. As always, we welcome your thoughts and feedback on how we can continue to improve and make our benchmarking more relevant to you.

Key takeaways

Investors have been modestly de-risking their portfolios over the previous quarter:

- Cash allocations are near historic highs of almost 11%
- Investors are rotating out of equities and into fixed income
- Interest rate exposure has declined due to a reduction in portfolio duration over 2022
- Private capital net commitments are small and declining, indicating a stabilization of allocations
- Hedge fund flows are flat, potentially indicating a 'wait and see' stance

Broad asset allocation trends

We start with the examination of the average asset allocation across the Addepar platform (see Exhibit 1). The percentages shown are portfolio-weighted across 275,000 portfolios. Equities

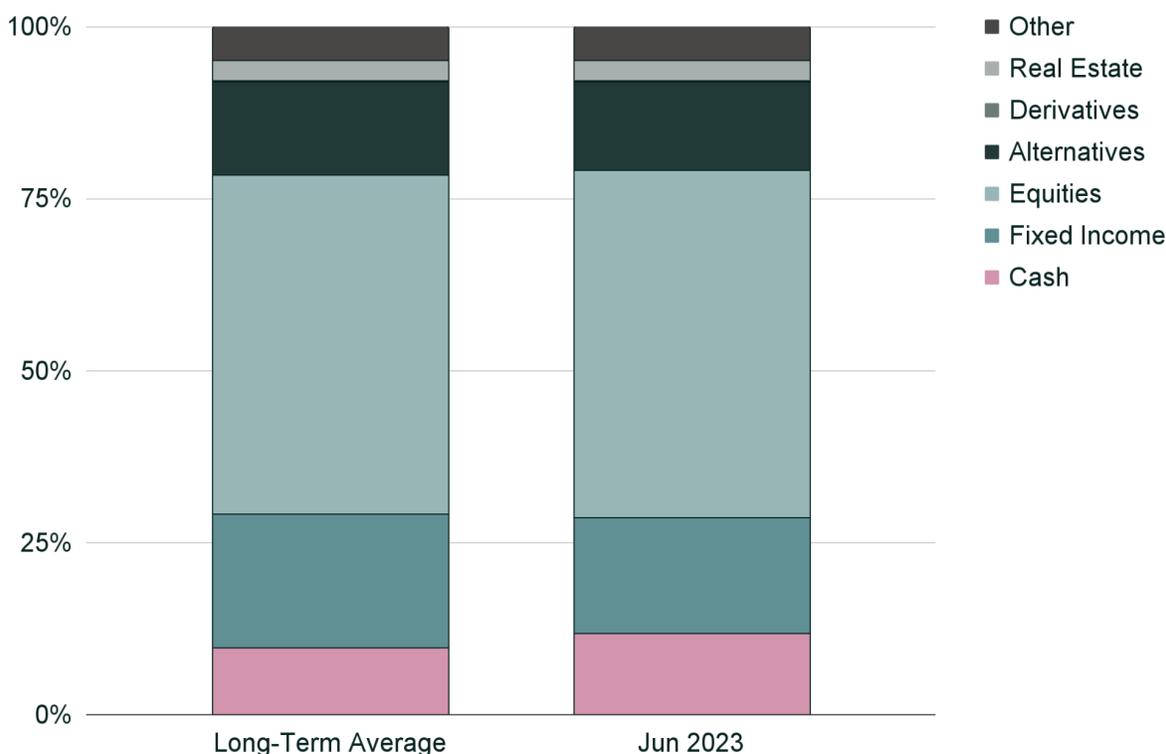


(51%), fixed income (17%) and alternatives (13%) make up the vast majority of capital allocations.

Allocation averages remain remarkably stable over the long term. On average, capital allocations typically do not shift by more than 1–2% above or below long-term averages. **Investors are currently holding 2% more cash, 1% more equities and 3% less fixed income positions relative to the long-term average.** While averages remain stable, comparisons of individual allocations against the average can be a useful data point in a broader benchmarking analysis.

Exhibit 1

Allocations are near long-term averages, with slightly higher cash and lower fixed income exposure
 Average portfolio allocations, Jan. 2016–June 2023 vs. June 2023



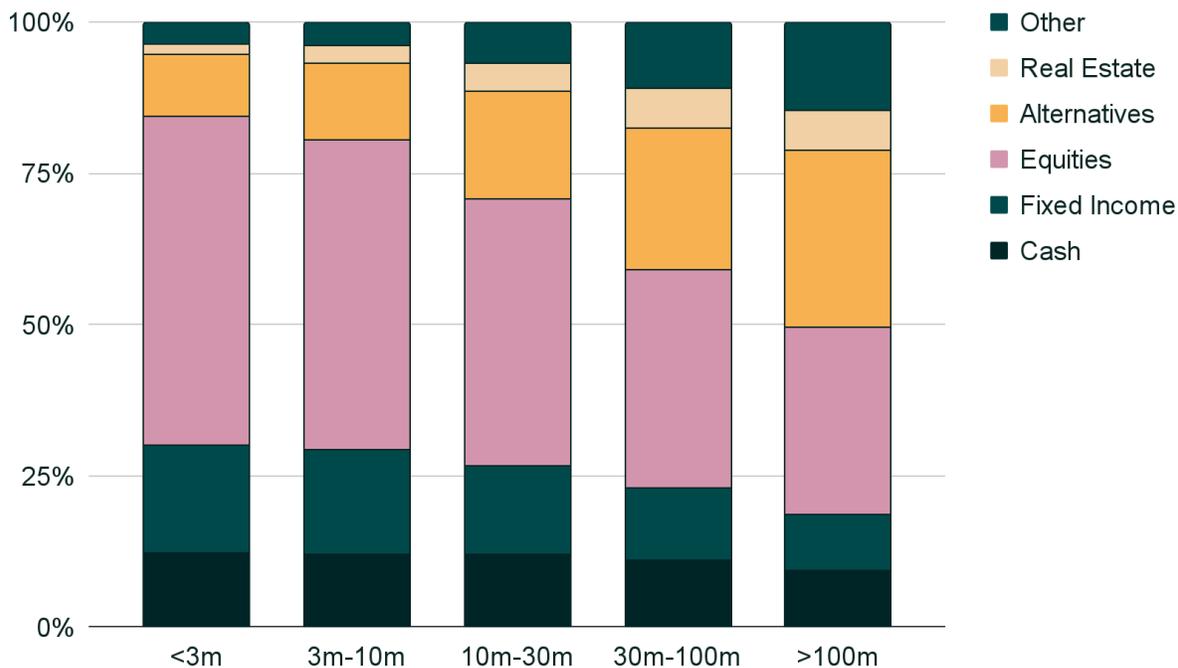
Source: Addepar

Addepar is used by a highly diverse group of investors. One dimension we examine is how asset allocations differ by the size of their portfolio (see Exhibit 2). Leveraging their competitive advantage of scale and access, we see that larger investors make proportionally smaller allocations to public equities and larger allocations to alternatives.



Exhibit 2

Allocations toward alternatives increase while equity holdings decline with investor wealth
 Average portfolio's holdings by asset class, June 2023



Source: Addepar

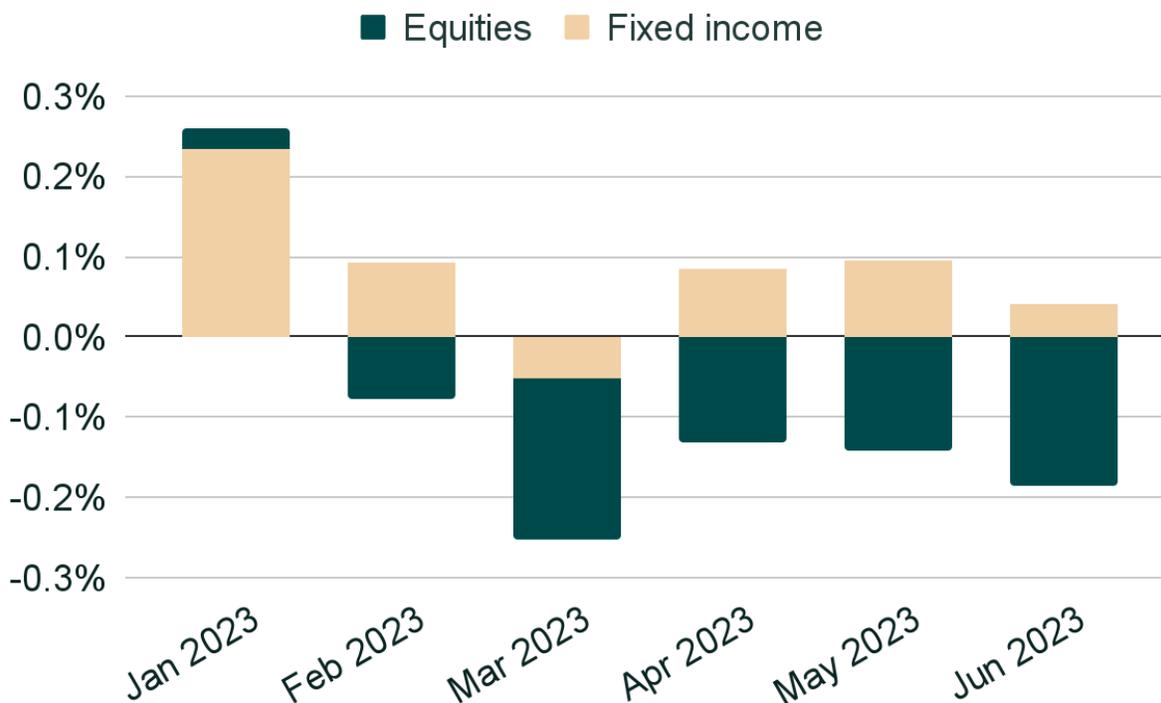
Asset allocations change over time, based on a combination of (1) Investment flows into and out of individual assets (e.g., buying, selling), and (2) The investment performance of individual assets. Below, we examine investment flows in isolation. Investment flows are highly informative due to the fact that they're an outcome of the investor decision-making process.

In Exhibit 3, we zoom into flows since the beginning of the year. Of particular note, we see flows out of risky assets in March (equities and fixed income) occurring during the regional banking crisis and debt ceiling negotiations. **Throughout Q2, investors rotated modestly into fixed income and out of equities.**



Exhibit 3

Investors continue to reduce their exposure to equities by adding to their fixed income positions
 Average equity and fixed income flows as a percentage of portfolio size, Jan. 2023–June 2023



Source: Addepar

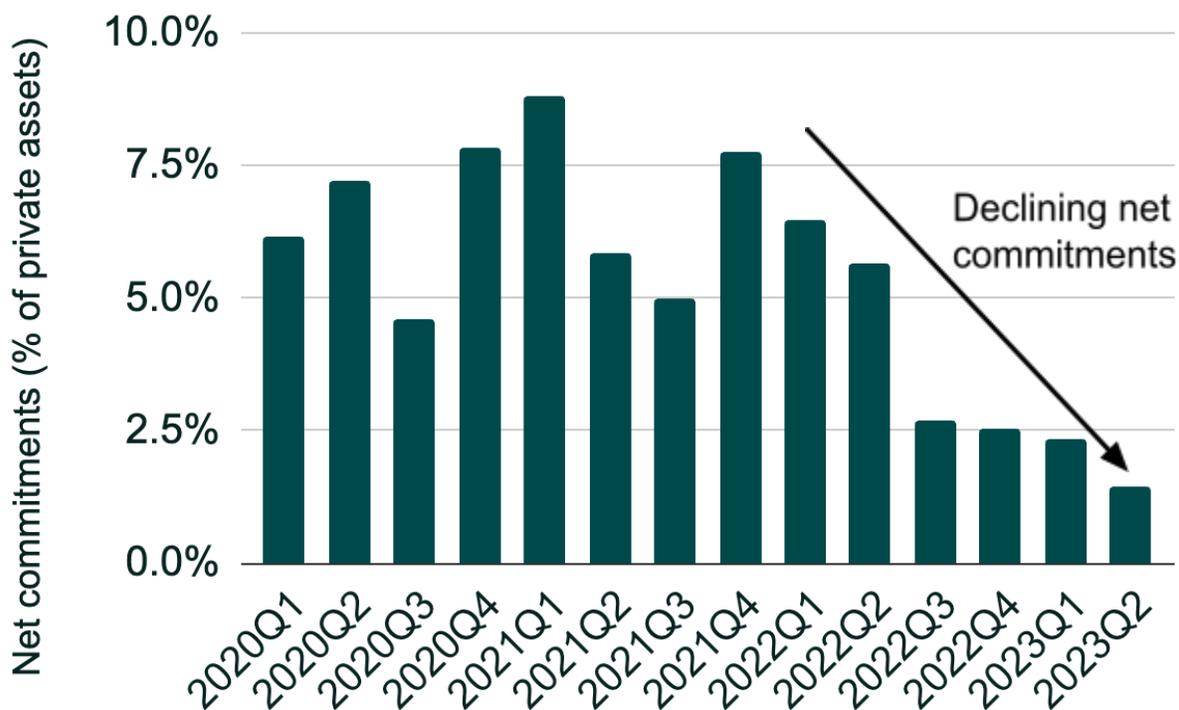
Private capital net commitments often relate to flows for public assets. They measure the total dollars entering minus the total dollars leaving a private capital fund over time. A positive net commitment signifies that portfolios are adding to their allocations toward a fund. Exhibit 4 shows the net commitments into private equity, private debt and venture capital from 2020 through 2022. As can be seen, **net new commitments have trickled down significantly since the second quarter of 2022.**



Exhibit 4

Private capital net commitments are low and continue their multi-year decline

Net commitments, % of private capital assets, quarterly, Q1 2020–Q2 2023



Source: Addepar

Net commitments are defined as new commitments minus distributions and redemptions as a percentage of total private capital assets.

In the following section, we dive deeper into asset allocation analytics within each asset class.

Cash

Private wealth investors are allocating heavily to cash, holding almost 11% of their portfolios relative to a 9.7% historical average. Much of the growth is fueled by **direct holdings of short-duration Treasuries,¹ which now account for one-third of cash positions.** This trend began with rising interest rates in the beginning of 2022 and has quickened this year. Meanwhile, allocations to banking products are declining.

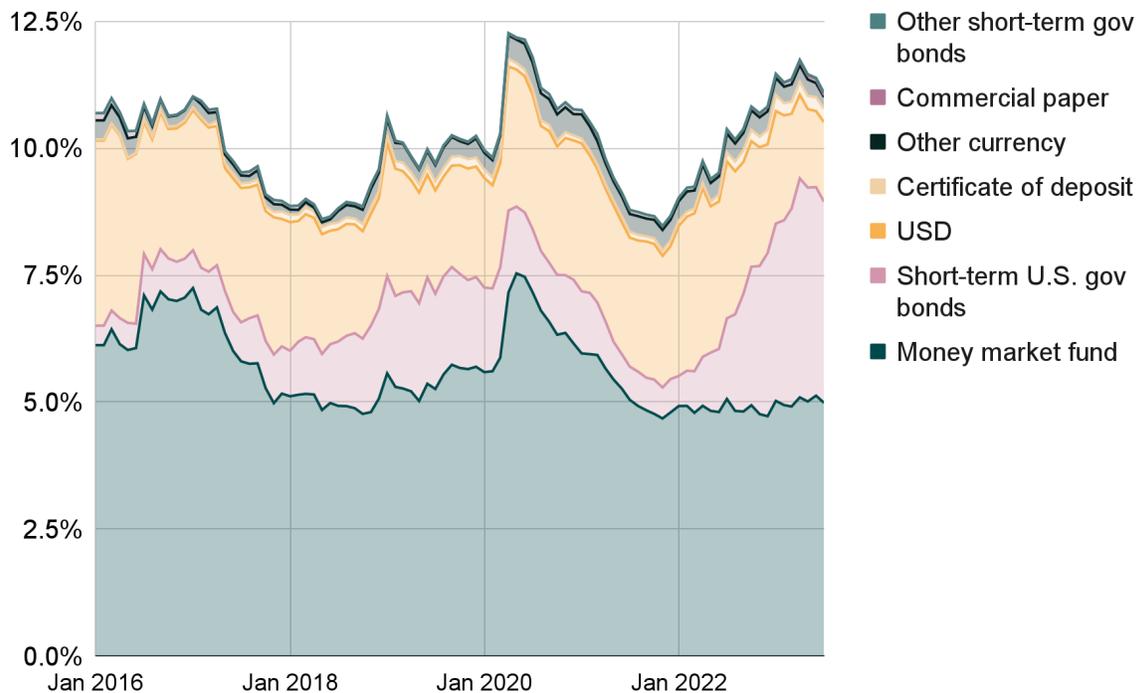
¹ Up to 1-year maturity.



Exhibit 5

Allocations to cash remain high, but fell slightly from a peak in March 2023

Cash holdings by investment type, % of total assets, Jan. 2016–June 2023



Source: Addepar

USD and ‘other currency’ are defined as paper money and cash held at banks. Money market funds are ETFs and mutual funds that invest in relatively safe fixed-income instruments with maturities of one year or less. Short-term U.S. government bonds are Treasury bills and off-the-run Treasury securities set to mature in one year or less.

Fixed income

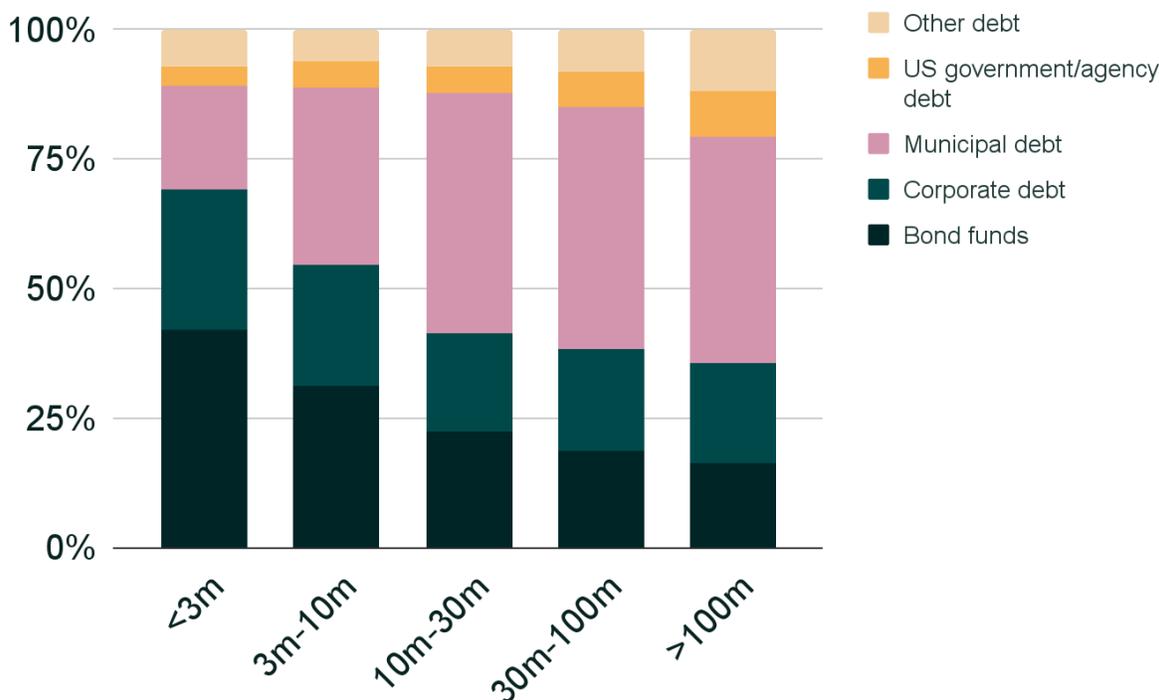
Portfolio size plays a determining factor in the way investors choose their fixed income holdings. As shown in the exhibit below, investors with smaller budgets tend to more heavily rely on bond funds in their fixed income portfolios, while **investors with over \$10mm in holdings allocate more of their portfolios to tax-advantaged municipal bonds.**



Exhibit 6

Smaller portfolios hold more bond funds, while larger portfolios hold more municipals

Average portfolio's fixed income holdings by instrument type, June 2023



Source: Addepar

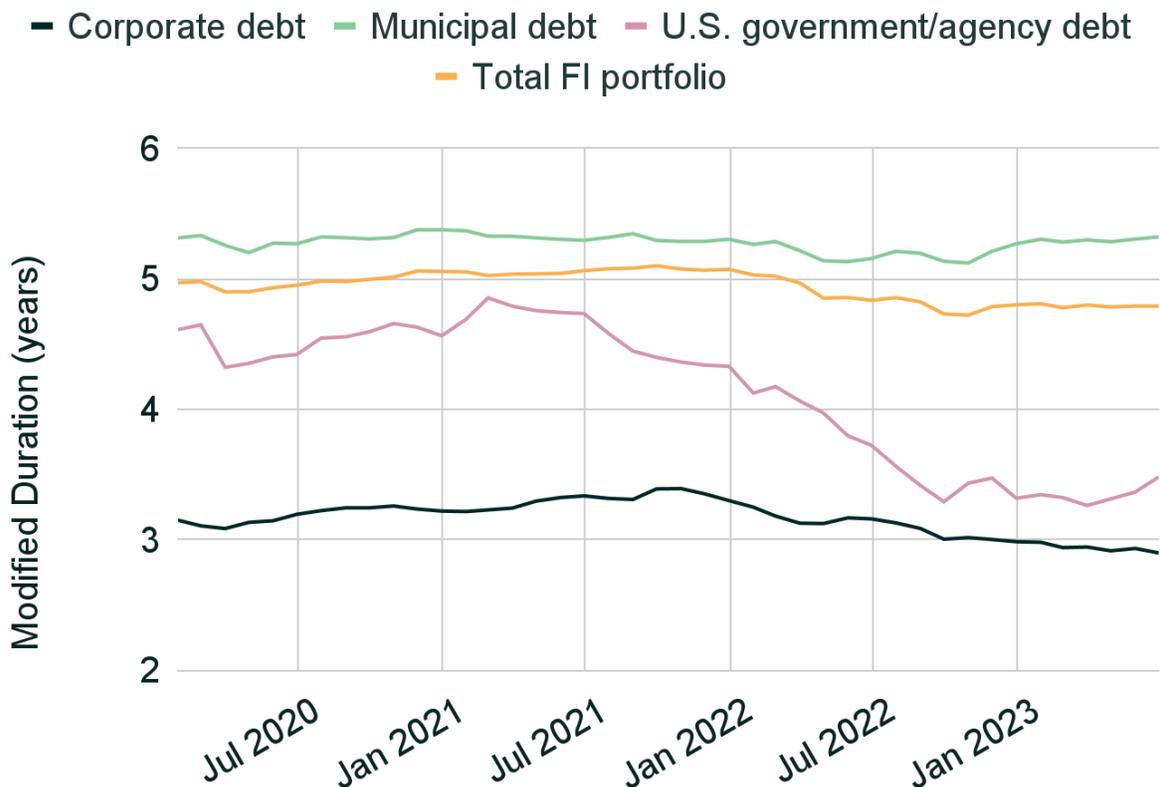
Other debt includes international government debt, ABS/MBS and structured debt.

Investors can reduce their interest rate risk by decreasing durations and by selling out of fixed income instruments. They did both of these in the lead-up to the Federal Reserve's recent tightening cycle. As shown in Exhibit 7, **from July 2021 to September 2022, investors reduced their Treasury durations by over a year.**



Exhibit 7

Investors decreased Treasury durations by a year while keeping other durations mostly unchanged
 Median portfolio's fixed income durations by instrument type, Jan. 2020–June 2023



Source: Addepar

This analysis excludes cash instruments, such as commercial paper and U.S. Treasuries with less than one year to maturity.

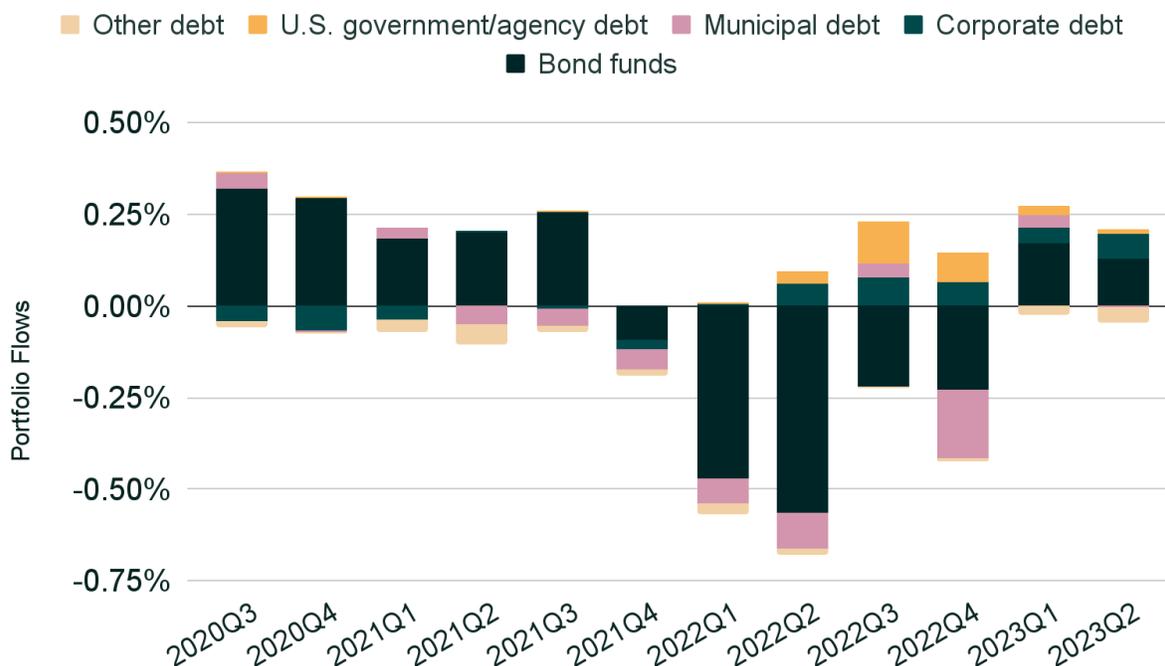
Investors also sold out of their fixed income holdings, as **large outflows began in Q4 2021 and continued through the end of 2022. The trend has reversed in 2023, when investors rotated out of equities and into fixed income.**



Exhibit 8

Investors reduced their fixed income exposures throughout much of 2022

Fixed income flows by instrument type as % of total fixed income holdings, Q3 2020–Q2 2023



Source: Addepar

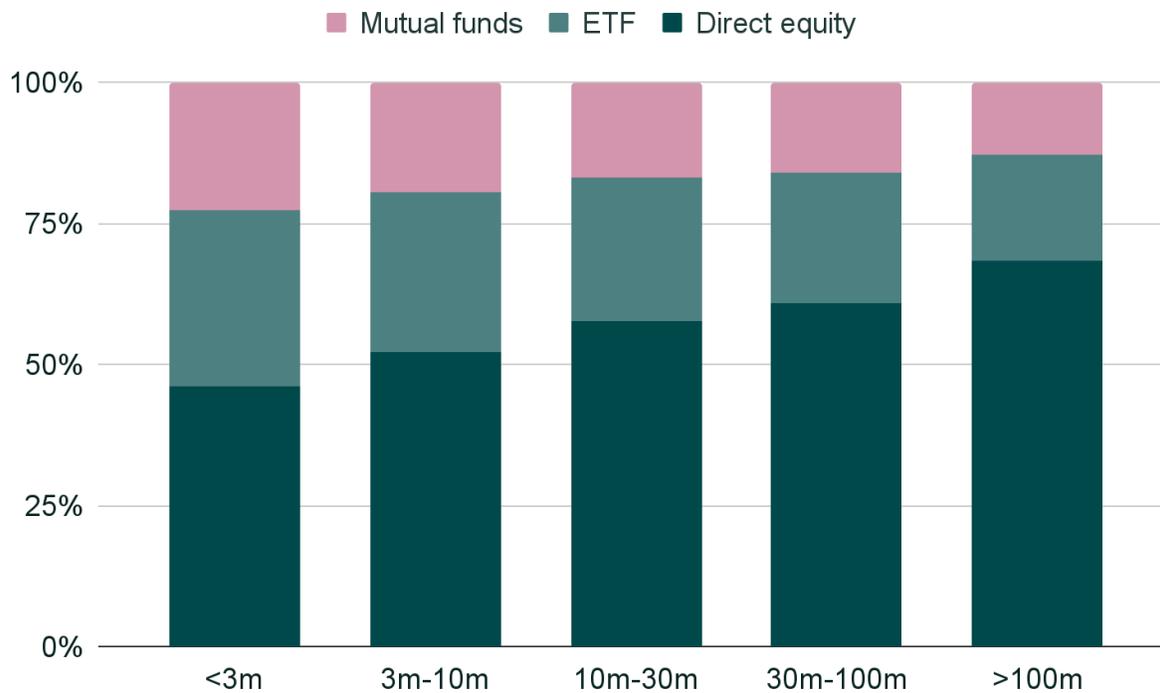
Equities

Larger portfolios have more flexibility in the way they invest in equity markets, with the ability to use techniques such as direct indexing to customize their desired exposures. We see that **investors with larger portfolios tend to hold more direct equities than do smaller portfolios**, with the smallest portfolios achieving more than half of their equity exposures through funds.



Exhibit 9

Larger investors tend to invest more heavily in single-name equities than they do in equity funds
 Average portfolio's equity holdings by instrument type, June 2023



Source: Addepar

Within single-name equity holdings, investors are generally holding market weights, although they modestly hold a higher allocation toward financial service companies and a lower allocation in technology stocks relative to the market².

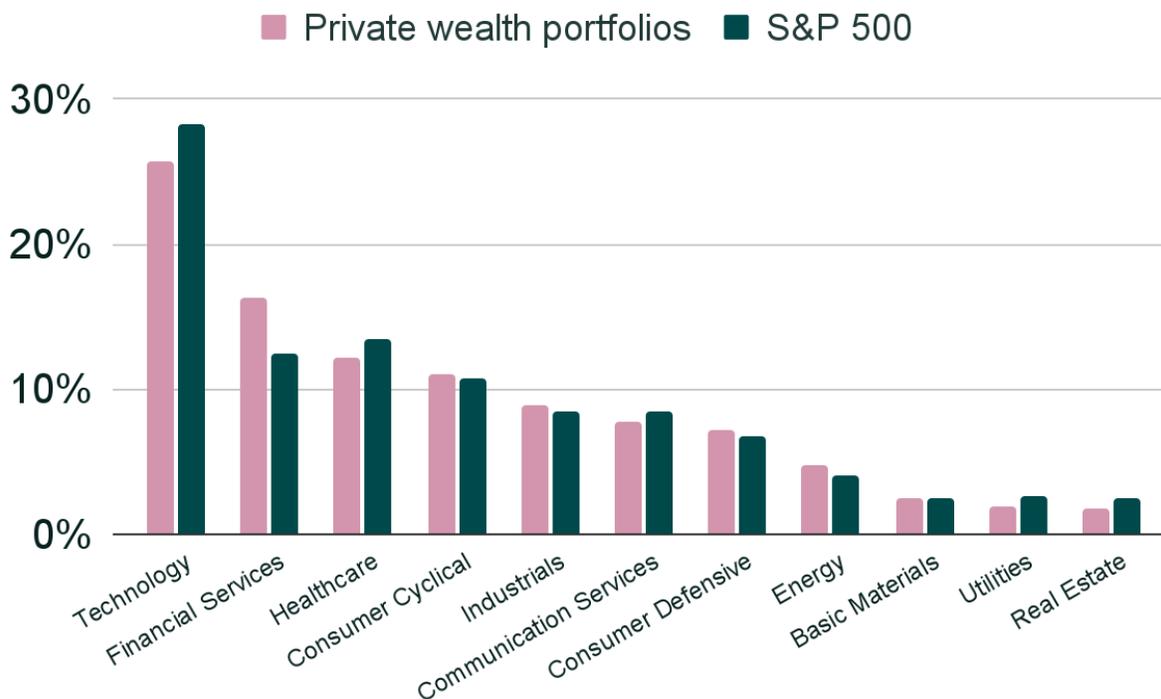
² The market is proxied with S&P 500 weights.



Exhibit 10

Investors hold slightly more financials and less technology than is held in the S&P 500

Average portfolio's equity holdings by sector vs. the S&P 500, June 2023



Source: Addepar, S&P

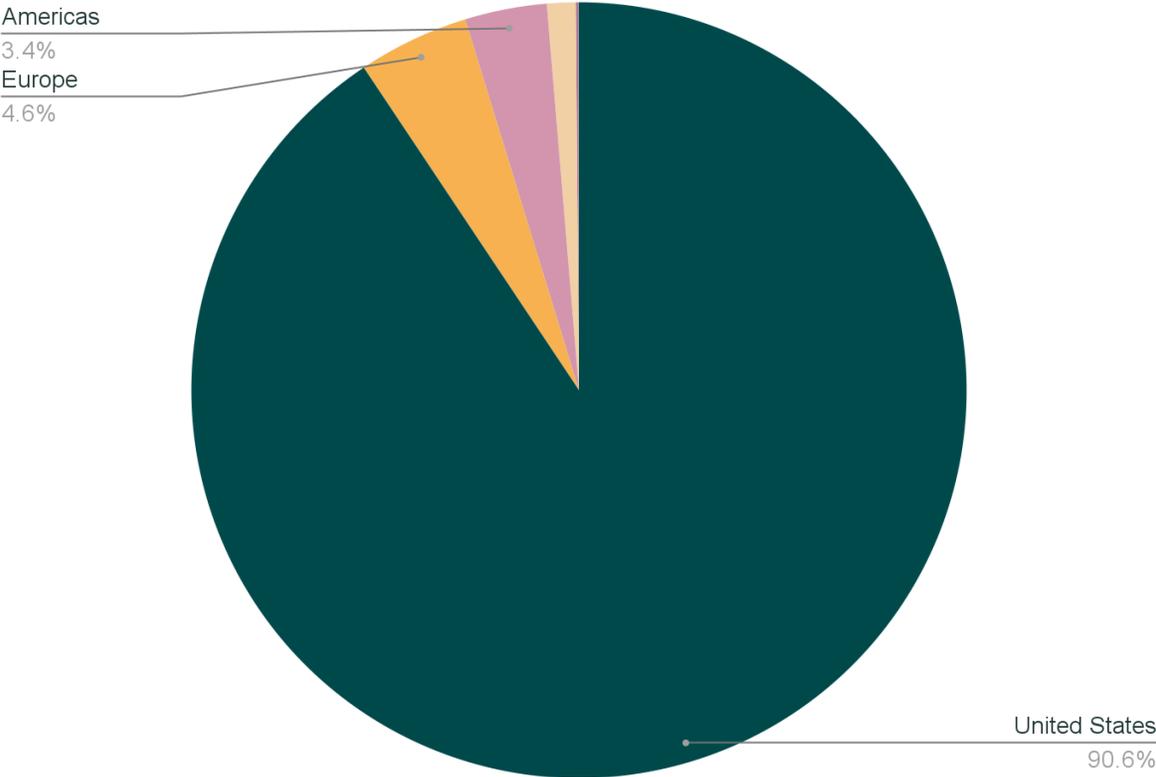
From a geographical perspective, investors have a strong home bias, holding the vast majority of direct equity exposure in U.S equities. U.S. equities are the single largest exposure in most portfolios and tend to drive performance within equities and other related asset classes.



Exhibit 11

Investors hold most of their direct equity exposure in U.S. stocks

Average portfolio's direct equity exposure by primary country of business, June 2023



Source: Addepar

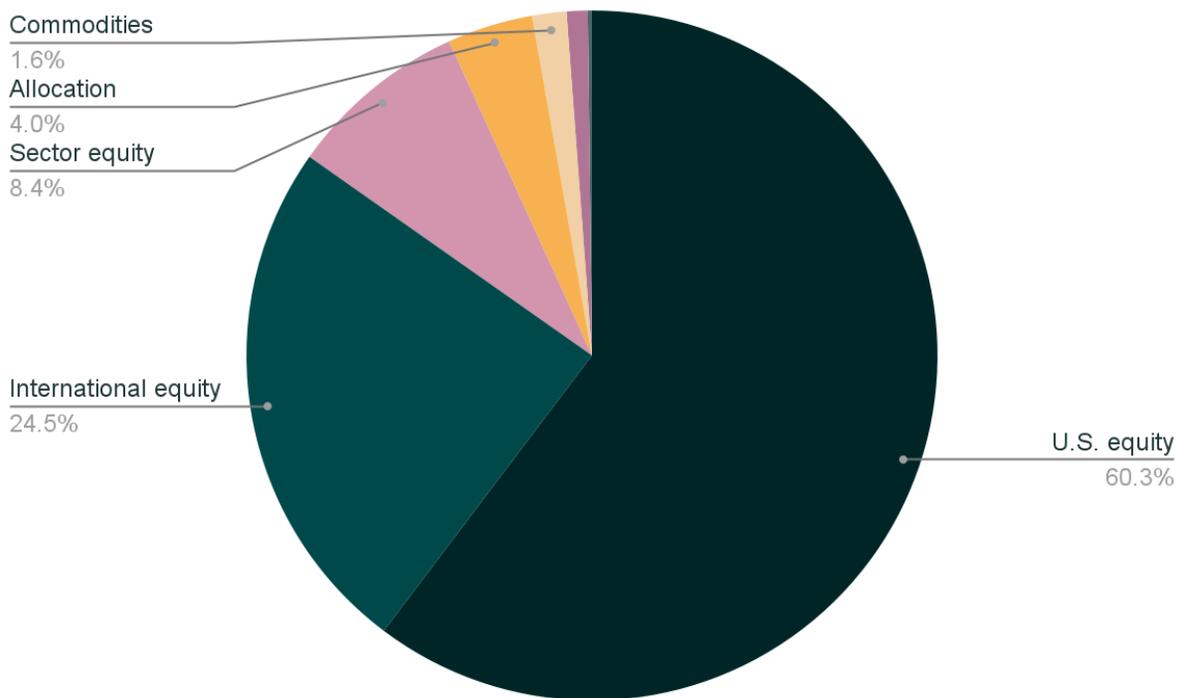
Investors who choose to increase their geographical diversification tend to do so via equity funds, with approximately 25% of fund holdings being international in nature. U.S. equity funds make up the majority of fund investments at 60%, with more specific holdings in sector, allocation and commodity funds filling out the remaining allocations.



Exhibit 12

Allocation to international equity via funds tends to be much higher than via direct equities

Average portfolio's equity fund allocations (mutual fund + ETF), June 2023



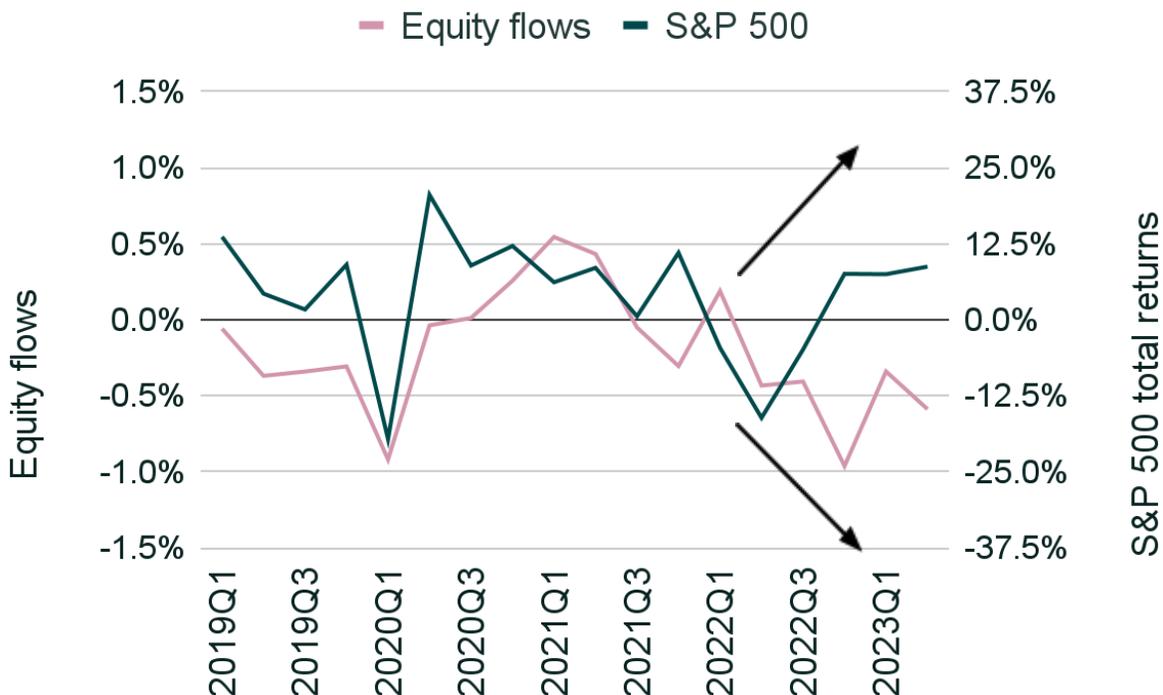
Source: Addepar

From a flows perspective, we continue to see signs of de-risking. On a historical basis, equity flows tend to track market performance. **Despite solid market performance, the past three quarters have had significant equity outflows.** In Q4 2022, investors sold securities for tax reasons. In Q1, concerns around the financial sector and debt ceiling had investors reducing risk despite the aggregate market's rise. That behavior has persisted into Q2.



Exhibit 13

The usual correlation between equity flows and the S&P 500 has broken down since Q4 2022
 Quarterly equity flows as percentage of equity holdings vs. the S&P 500, Q1 2019–Q2 2023



Source: Addepar

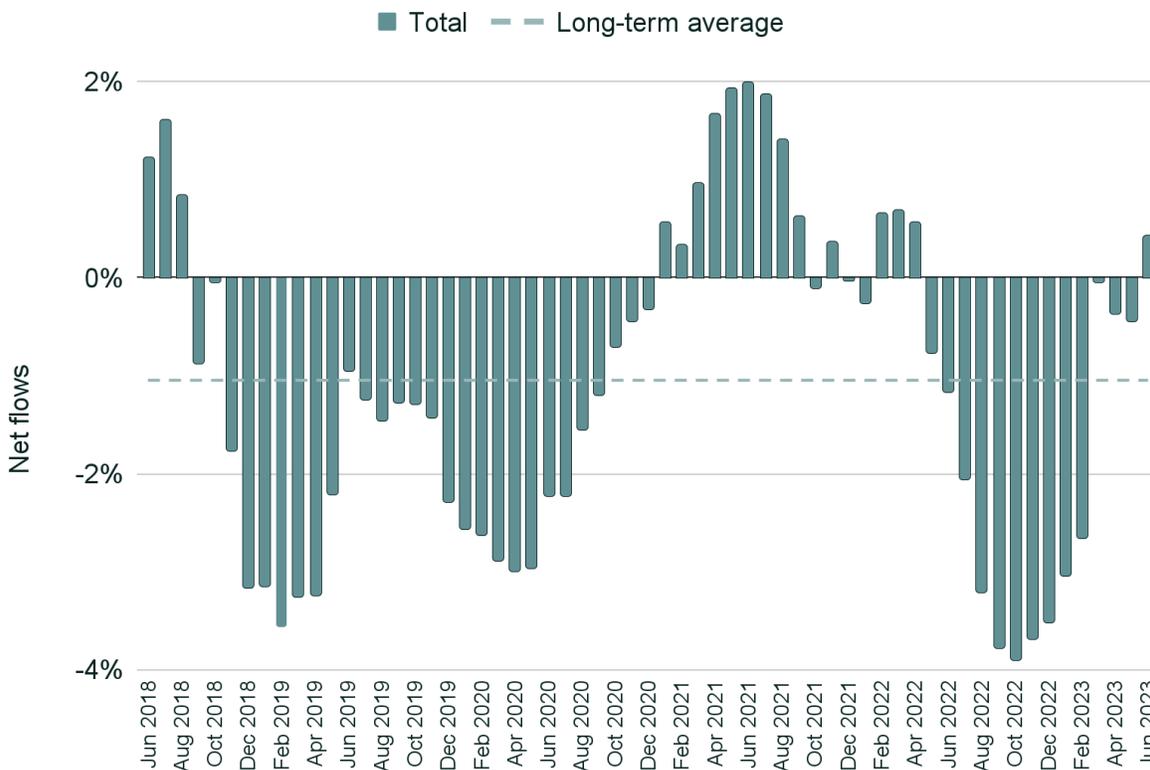
Hedge funds

Hedge funds are often added to portfolios to diversify returns. In the past several years, investors reduced their exposures to hedge funds as public equity markets provided above average returns. This trend moderated in the second quarter however, as investors mostly held their positions flat.



Exhibit 14

Secular flows out of hedge funds moderated in Q2 as net flows finished the quarter flat
 Aggregate flows to hedge funds, six-month rolling average, June 2018–June 2023



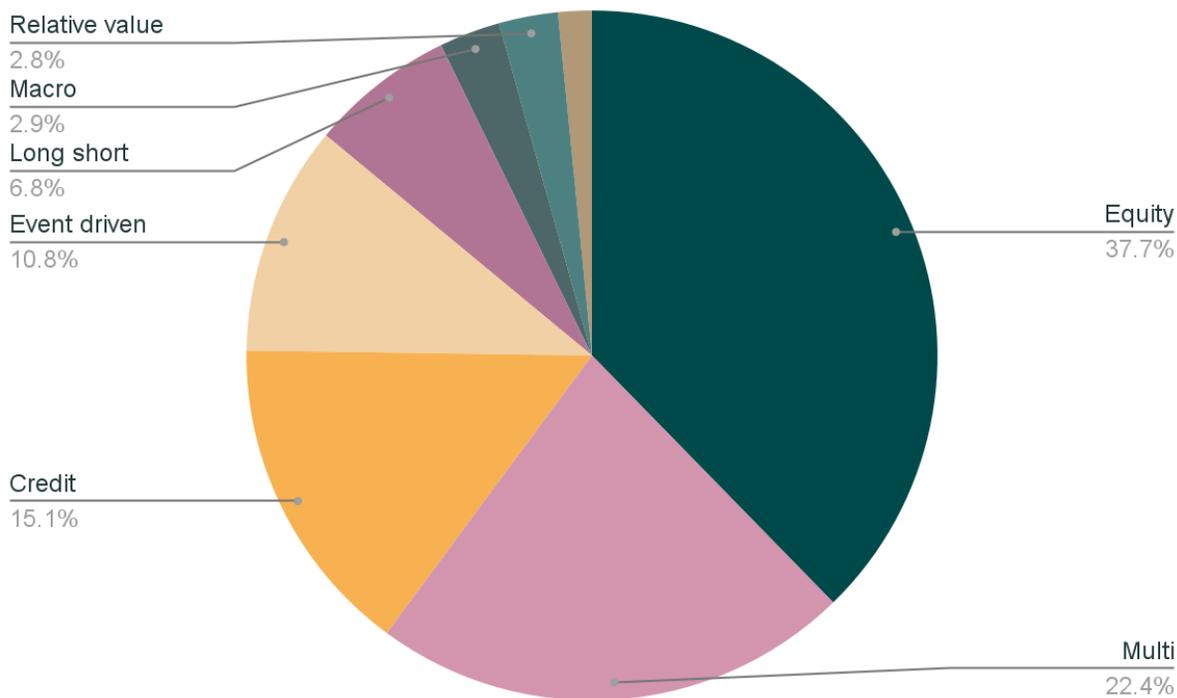
Source: Addepar

Hedge fund investors are primarily positioned in equity, multi-strategy and credit funds, with only small portions of their portfolios allocated toward macro and relative value funds.



Exhibit 15

The majority of investor hedge fund holdings are allocated to equity, multi-strat and credit funds
 Hedge fund allocation by strategy, % of total hedge fund assets, June 2023



Source: Addepar

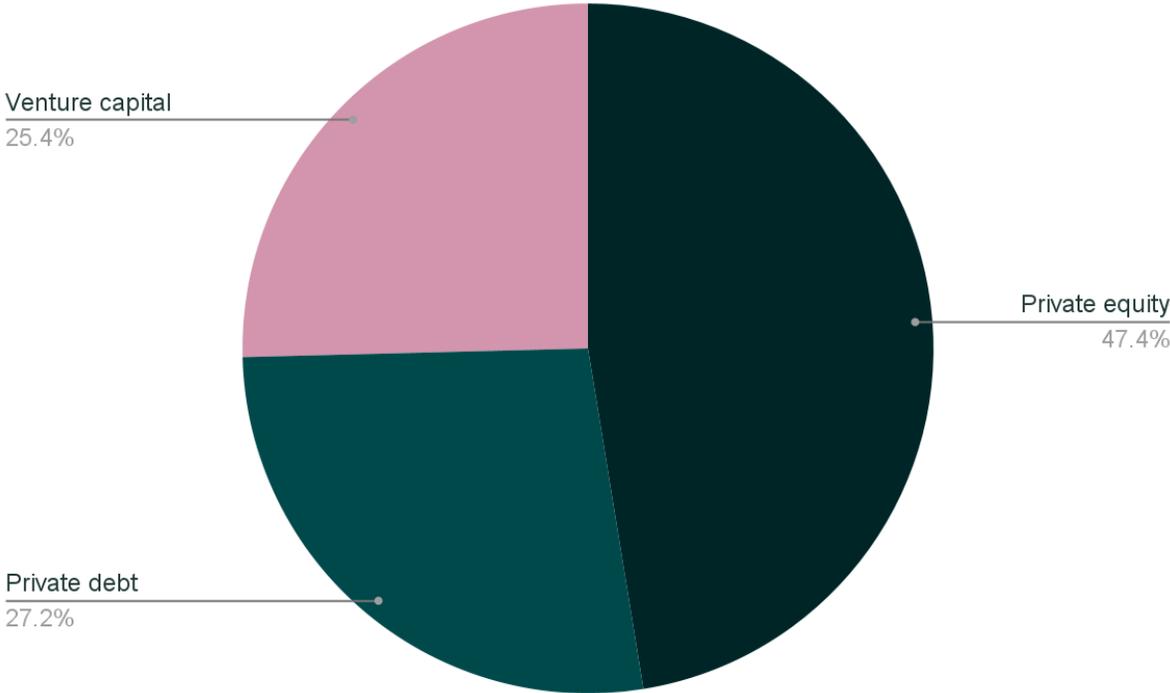
Private capital

Rising rates and less deal-making has led to a challenging period for private capital, yet it remains an important component of investor portfolios thanks to its low-risk, high-return profile. As of the end of June, investors are positioned with approximately half of their private capital portfolio in private equity, with the remaining portfolio split between venture capital and private debt.



Exhibit 16

A typical private capital portfolio is 50% private equity, 25% venture capital and 25% private debt
Private capital allocation by strategy, % of total assets, June 2023



Source: Addepar

Real estate

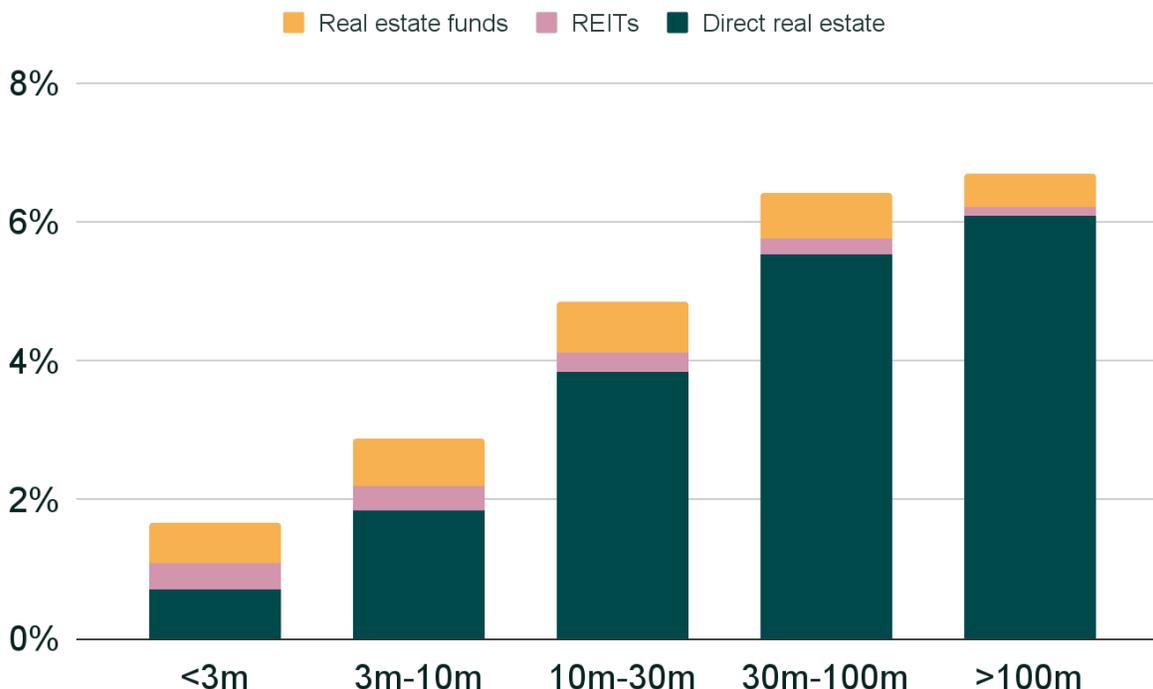
Investor real estate holdings tend to increase with portfolio size. As shown in the exhibit below, differences by portfolio size are almost entirely due to wealthier investors holding more direct real estate. Interestingly, excluding direct real estate, all portfolios hold similar allocations to public and private funds.



Exhibit 17

Larger portfolios have much greater exposure to direct real estate

Average portfolio allocations to real estate, % of total portfolio, June 2023



Source: Addepar

Conclusion

We’ve provided a range of views and transparency into the asset allocation of portfolios on the Addepar platform. As we mentioned, we’ll be publishing updates to these views on a quarterly basis. In addition, you’re invited to read our companion note on Q2 2023 portfolio performance. Please email research@addepar.com if you have any thoughts or suggestions on how this publication can be improved.



Asset classifications

Asset class	Sub-asset class
Cash	Certificate of deposit Commercial paper Foreign currency Money market funds Other short-term government debt U.S. short-term government debt U.S. dollar (USD)
Fixed income	ABS/MBS Bond funds Corporate debt International government debt Municipal bond funds Municipal debt Other debt Other government debt Structured debt U.S. government/agency debt
Equities	Developed market equities Emerging market equities Global equity Other equities Other funds U.S. equities
Alternatives	Direct private companies Fund of funds Hedge funds Other alternatives Private equity and venture
Real estate	Direct real estate Real estate funds REITs
Other	Crypto Call options Forwards and futures Put options Other



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