ENVESTNET

Envestat Report

June 2017

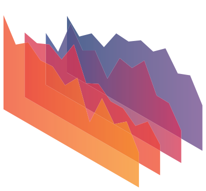
Are Investors Feeling Overconfident?

After many years of market gains, consumer confidence is high. The market environment appears to be making investors brave and willing to take on more risk. Is now the time to take on more risk and are consumers investing as if they're invincible? Have they forgotten how devastating large losses can be to a portfolio and how long and difficult it can be to recover?

Client risk profiles are often determined based on how they "feel" about risk. So clients are more comfortable now taking risk in equities versus 12 months ago when in fact they should be getting more risk averse since markets are at an all time high.

As equity markets keep advancing with surprisingly low volatility, the complacency seems to be driving investors toward risk taking. Against a backdrop of equity markets regularly hitting new highs and a flattened Treasury yield curve offering little return potential, many investors appear to be warming up to the idea of taking more risks in their portfolios. Not a good idea.

Investors should be paying attention to risks now more than ever. Older investors tend to be more risk-averse because they have less time to make up for large losses. More conservative investors typically don't want to stomach big drops and are likely to exit the market if they do. From an overall portfolio management perspective, if your time horizon and risk profile has not changed, the last thing you should do is to drive up portfolio risks when markets are at all time highs.

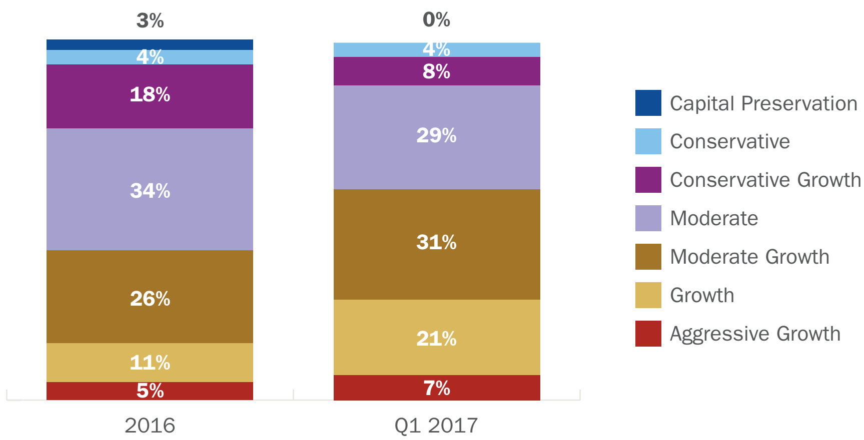


Clients are more comfortable now taking risk in equities versus 12 months ago.

All of these factors prompted us to take a look at the trend in where on the risk spectrum clients are allocating their assets at Envestnet. We set out to answer a couple of questions:

- Are advisors' clients selecting riskier asset allocations and taking on more risk in their portfolios this year than last?
- Where are we now?
- Are there signs of a risk-on or risk-off environment?

Allocation of Net Flows Into Fund Strategist Portfolios



Source: Envestnet, Inc.

Envestnet Observations

We see the emergence of a risk-on environment as exemplified by increased flows into the 3 (out of 7) most aggressive portfolio allocations. The percentage of investors selecting the most aggressive allocation (Aggressive Growth) increased from 5% to 7% since last year. The second most aggressive allocation (Growth) saw the percent of investors selecting that allocation nearly double from 11% in 2016 to 21% in 2017. The four most conservative allocations all experienced decreases in the percentage of investors selecting those models.

Envestnet believes that the risk-on trend we're seeing is potentially dangerous. Unless a client profile has changed, their risk profile should be maintained. Advisors need to talk to clients about the trade-offs of adding risk to a portfolio, drawdown potential, time to recover, what duration risk is, and more.

About Envestat

Envestat, Envestnet's industry analytics engine, delivers regular digests of business intelligence designed to provide context to the decisions that financial advisors and enterprise business owners face every day.

EN-STATREP-0617 / SR #1096512