Research @ Citi Markets Edition: The Model Moment

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Transcript:

Opening Teaser: (00:00)

Research @ Citi, Markets Edition

Scott Chronert (00:03)

Hi, I'm Scott Chronert, Head of U.S. Equity Strategy at Citi Research. Welcome to Research @ Citi Markets Edition, covering various topics at work within the U.S. equity markets.

With me today is my good friend Tushar Yadava, who is Head of Markets, BlackRock Model Portfolios. And we're here to talk about “the Model Moment.” Tushar, thanks for joining today.

Tushar Yadava (00:23)

Scott, thanks for having me on.

Scott Chronert (00:26)

So we've got a title for the podcast, Model Moment, but this is far from identifying a new dynamic within equity markets. But I thought it was particularly relevant right now, given that for the past several episodes, the focus has been predominantly on U.S. equity topics.

But here we are, S&P up 17% year to date, 90% over the past three years. In our ETF work, we noted — this morning, in fact — another $130 billion into U.S.-listed ETFs, bringing the year-to-date total to about $1.2 trillion. So what we have is a flow situation, and I think because of the performance backdrop, an increasing asset-allocation decision ahead for many forms of U.S. equity investors.

We like to look at ETF flows as one indicator of investor sentiment, but as we'll discuss today, there's a lot more at work behind the scenes here. So to get the conversation going, talk to us a little bit about the growth in the model business, its importance for asset-allocation trends — and flows, for that matter — and perhaps put some context around the bigger picture here, Tush.

Tushar Yadava (01:36)

So you're probably listening to this and you're thinking, “What is the Model Moment?” I represent BlackRock's model-portfolio business. We are a model-portfolio provider to financial advisors. If you walk in off the street to a financial advisor and you fill out a questionnaire based on your risk tolerance and everything else, the chances are these days, more often than not, thanks to some combination of regulation, industry trends, and just the way that the financial advisor of today is evolving, you'll end up probably in a model portfolio if you give that financial advisor some money to manage.

And that's a good thing for a lot of reasons. But chief among them, I think it helps these broker-dealers manage and standardize risk. So these model portfolios, they then accrue money as the hypothetical consumer, or customer comes in, and keep contributing to that account or as these advisors keep moving money from brokerage assets, where they were paid by commissions, let's say, to fee-based advisory assets, which is a shift that's been under way for a decade plus.

As that continues to gather steam, the model-portfolio industry now is probably north of $3 trillion here in the U.S. It's a phenomenon unique to the U.S. in a lot of ways — it's not absent from other countries, it's just sort of hyper-charged here in the United States.

And those advisors and those models traditionally are a little bit more equity-heavy. They range in that sort of traditional 60-40 that you've thought of, toward all equity types of portfolios for clients. And those are centrally managed portfolios. So, they're managed by portfolio managers at houses like us here at BlackRock, or others across the Street that you can think of. And when they make asset-allocation decisions, they're managed centrally, and then cascaded to … we think we touch nearly 50,000 advisors in any given day.

And I think it's germane to a lot of the conversations that you've had, and I've listened back on the podcast. Because a lot of times you'll hear in institutional commentary, especially in trading desks, “retail was a big buyer today.”

And who does that look like? Well, more often than not, it's looking a lot like us. And what I think is interesting is that we're not as active as you'd maybe think. And it is a portfolio that in our instance, for example, manages itself to rebalance about four to six times a year with about 10% one-way turnover. So if you can think about those billions and trillions of dollars, they're not as active as you think, but they make big strategic asset-allocation decisions and all the things that you'd care about.

Stocks vs. bonds, U.S. vs. international, and then within the U.S. styles, factors, sectors, all different types of slices of the market that drive big allocation decisions. Big flows, obviously, as a result, but do take a very big view and lens on the market with a lot of money behind them.

Scott Chronert (04:06)

So roughly $3 trillion. I know there are different estimates that are put out there. And I know you and others, including ourselves, over the years have published on the expected growth on this. I think we can probably circle around on a view that there's at least a doubling out there between now and, say, 2030 — there are probably some estimates that are even higher. And that growth is going to come from, I think, just the ongoing prevalence of money being managed according to an asset-allocation framework, right?

OK, so you also mentioned this notion of going down a customization path and BlackRock having pioneered a lot of this. So speak a little bit about traditional 60-40, but then how you go down, again, the BlackRock angle in terms of how you think about customization on this.

Tushar Yadava (04:51)

Let’s play the little history game in our industry. It's not a very old industry by many standards, but for example, our portfolios here at BlackRock have been around for just over 10 years now. The time it took us to get to the first $100 billion in assets under management was long and winding. To your point about the doubling, it's been less than, I think, a third of the time to double our assets over that period of time.

So it's growing, it’s growing rapidly. I think our internal estimates that I've heard have been somewhere in the range of $11 trillion by the end of the decade — or by the next decade, rather — that we expect in terms of model portfolios. So the size is something to be reckoned with.

Certainly, when we talk about customization, a lot of the models 1.0 assets — the assets that first came in the door, like I said, you walk in off Main Street, you hit an advisor, and you talk to him about your asset allocation or your risk tolerance, and he puts you in an asset allocation portfolio, or he or she — that journey was very pre-prescribed, premeditated, very grooved, the channels are very well understood.

Well, the RIA space has been also growing at a massive clip over the last decade. RIAs tend to operate a little bit differently. They've traditionally come from wire houses or traditional brokerage, and they've hung up their shingle as an RIA on their own. But they like the scale, the simplicity, the repeatability of the model-portfolio business that they left behind at whatever broker-dealer they were. And so a lot of them have gravitated toward it.

And we realized that BlackRock, I think we probably championed this industry about five years ago when we talk about customization. We realized these RIAs would be willing to work with us in many different ways. It's just if there were a few different tweaks that they could make in the portfolios, a few changes, a few managers that they would like to see, a few differences in opinion in how they would view, say, growth value or some sort of moderate customization like that, they would be willing to work with us on nearly everything else that we do in a portfolio at a portfolio level decision.

And so what that led to was the rise of what we would call customization, right? It's sort of custom model portfolios. It's now about half of our business. So it launched about five years ago, gives you a good idea of about how quickly that's grown and how much that's helped power a lot of our growth in the model-portfolio business.

And as I sit in the industry now, whether it's my colleagues on the iShares side that are serving model-portfolio providers, or whether it's just me looking out at the competitive landscape, everyone has moved their lens to focus on custom model portfolios, because it's an area where you can really gain a lot of scale with a little bit of coding, a little bit of simplicity. But by and large, the changes are very, very simple or narrow, and they often just reflect iterations.

And going back to models 1.0, a lot of those iterations weren't allowable earlier on, because there were things like commission trading, right? Now everyone's moved to commission-free trading, the rise of the ETF structure, the incorporation of active ETFs. Just a lot of these changes that have come over the last five years have really helped and supercharged this custom model-portfolio business that we think will continue to be the fastest-flowing river.

So as we talk about that growth trajectory to $11 trillion, custom model portfolios are going to make up more than half of that. They're all open architecture and they're going to incorporate all different types of sort of structures and asset classes over the next five years, including public and private, including SMAs and including obviously the sort of base foundations, which are ETFs and active ETFs.

Scott Chronert (08:14)

So let's cut to the chase as we wrap up our allotted time for this, and let's step back and take a look at your views as we head into 2026 from an asset-allocation perspective. What are you guys thinking about this point? And where are you pointing the users of your models?

Tushar Yadava (08:30)

Yeah, great question. We've just rebalanced our portfolio, so this is good timing. We're hearing so much concern from our client base about equity market valuations. Are we in a bubble? I think anyone that reads your research, we're very much aligned in our views in terms of where valuations are. They're full, but not bubble-ish. And so, our last rebalance was to add to equity overweight.

So we're already in a 60-40 portfolio, for example, we were 2% overweight stocks relative to bonds, we're now up to 3% overweight stocks relative to bonds. That's a big driver of returns. It might not seem like much. And then we're max overweight U.S. in emerging markets, relative to developed markets. So, our developed-market weight is at its lowest that we've probably held in a long time.

Most of that's gone to the U.S. And then within the U.S., we were recently selling some quality to buy momentum, and then adding some value, but not because we're massively convicted on value. We're generally a little bit growth overweight at the moment, but we want to bring up our value underweight. And so we added to value as the fastest way to do that, but kept our big overweight at a sector level of technology within AI and defense spending as a theme within our big thematic bets we have in the portfolios.

Scott Chronert (09:38)

Perfect. So to sum all of this up, we think that the trend in terms of assets flowing into asset allocation models is just getting going. If we're at $3 trillion now, there's an opportunity for that number to increase materially. We have to be attentive to how this influences the way we think about things like ETF flows and other broader flows.

But in aggregate, I think we can step back and say, “Look, this is a trend that is well under way and still has a lot of room to go.” And to Tushar’s point, the setup as we head into 2026 is still a fairly constructive one in terms of how you're thinking about the equity allocation component of this.

Tushar, thank you so much for joining today. Just in terms of wrapping up, this podcast was recorded on Dec. 1, 2025. Thanks for joining.

Next week's Markets Edition podcast will feature Dirk Willer, Citi's head of global asset allocation. And be sure to watch for our Research @ Citi podcast, which you can view on this same channel. Thanks, and have a great day.

Disclaimer (10:33)