

THERE FOR THE ADVISORS  THERE FOR THE JOURNEY

Rearranging Deck Chairs

The Industry's Obsession with 60/40

Executive Summary

For decades, the 60/40 portfolio has served as the industry's default approach to long-term investing. Its endurance reflects simplicity and familiarity—not rigorous academic validation. Despite significant advances in financial research and portfolio construction, many advisors continue to rely on a static framework that was never designed for today's dynamic markets.

Research has long shown that **asset allocation is the most important driver of portfolio outcomes**, yet it remains one of the least examined decisions in practice. More sophisticated investors have responded by moving beyond narrow stock-and-bond allocations toward broader, risk-aware, and adaptive frameworks grounded in decades of academic insight.

This paper examines why the 60/40 portfolio persists, what modern research suggests instead, and how a more resilient approach to asset allocation can be constructed without relying on speculative forecasts or unnecessary complexity.

Key Takeaways

- 1 The 60/40 portfolio is a product of convention, not scientific optimization
- 2 Asset allocation decisions matter more than security selection or manager choice
- 3 Modern multi-asset, risk-based, and dynamic frameworks offer a more robust foundation



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In 2016, Jason founded Rayliant, an asset manager delivering innovative strategies in dynamic asset allocation, systematic ETFs, and alternative investments. Previously, Jason co-founded Research Affiliates and co-authored the groundbreaking Fundamental Indexation research (2005) which launched the smart beta revolution. A finance professor at UCLA Anderson School of Management, he is recognized worldwide for his award-winning contributions to portfolio design and quantitative investing. His passion lies in bridging cutting-edge research with practice, making complex investment ideas clear and actionable. He holds degrees from Caltech, Stanford, and UCLA.

The Current State of Asset Allocation

The 60/40 allocation remains the industry default—but why?

Today, for the most part, home country bias means this 60/40 is 60% U.S. equities and 40% U.S. bonds. Although this allocation's name has a nice 'quantitative' ring to it, my view is that advisors' preference for the 60/40 portfolio is not rooted in rigorous academic research. It does not evolve from decades of industry innovation or fierce product competition. Instead, I believe the 60/40 allocation survives for the same reason so many other sub-optimal 'rules of thumb' persist: because of inertia and herd behavior.

Any claim that 60/40 is "optimal" borrows from a false analogy to the S&P 500 as optimal. For context, equity management—if one traces how investors picked stocks back through the decades—actually began as highly concentrated stock picks. Investors' approach to choosing an equity exposure only migrated—kicking and screaming—toward indexing after decades of resistance. Nobel laureates and industry pioneers, armed with theory and empirical evidence, forced this transition. Unfortunately, the 60/40 portfolio simply never benefited from a comparable intellectual journey. Instead, the 60/40 emerged from a simple historical convenience: In the early 1960s, equities were expected to return 10% and bonds 5%. Weighted together, $60\% \times 10\% + 40\% \times 5\%$ produced 8%—a tidy number that matched pension fund return targets. No elegant theory. No deep science. Just simple arithmetic that produced a round number everyone liked.

Asset Allocation: 60/40 is Sub-Optimal

Unlike the S&P 500, which has been validated by academics and practitioners, both theoretically and empirically, the 60/40 construct has no robust foundation. Research overwhelmingly shows it to be under-diversified, especially in its US-centric form. But no one seems to do much about this. Perhaps this is a problem that has low impact—and thus isn't worth fixing?

In fact, as the iconic 1986 CFA study by Brinson, Hood, and Beebower demonstrates rigorously and convincingly, allocation has the biggest impact on an

investor's portfolio outcome. Allocation does matter. It matters a lot!

Yet, paradoxically, advisors and CIOs lavish effort on manager selection—or even individual stock picks. Rationally, asset allocation should command top priority. Instead, it garners scant advisor efforts in management of a client's portfolio.

Asset Allocation: Why Advisors and CIOs deprioritize Asset Allocation

Interviews with advisors reveal the industry's logic. They know asset allocation matters for client outcome, but they also know 'safety in numbers' matters for job security. 60/40 may be on shaky ground, but it remains widely used in practice, because "everyone is doing it". In an industry where success depends so much on luck, keeping business is not about outperforming, so much as it is not straying too far from the pack. On the great African savanna, a zebra survives not by running faster, but by blending in with the other zebras. Privately, many advisors confess that they prefer tinkering with stocks and funds because those moves look busy but carry little impact. You can flub those individual stock picks and fund manager selections and still not underperform the peer group by much more than a percent; an advisor won't get fired for that. There is an unspoken cynicism in the wealth industry: It is far easier to rearrange the deck chairs than to man the ship. From 'Management 101': when skill is high, effort should apply toward decisions with the greatest impact, and when skill is uncertain, that effort is best reserved for decisions that matter least.

The fact that we choose to rearrange deck chairs is telling.

Of course, there is the common refrain that no one has offered a "better" answer. On the basis of this claim, advisors retreat to 60/40 in defense, waiting for improved solutions; clients must not interpret this as abdication of duty out of ignorance! That "no better way exists versus 60/40" is one of the great myths in investment management.

The perfect allocation may be debated endlessly, but the “optimality” of a 60/40 allocation is taken as a given. In fact, a vast body of research does exist offering superior approaches. It’s just that convention, once entrenched, becomes its own defense.

Asset Allocation: Rise of the Endowment Model

It took 30 years from academic theory to an underground industry movement

While most advisors remain loyal to the 60/40 portfolio, more sophisticated investors have embraced the Endowment Model, introduced in 1985 by David Swensen. When he was running the Yale Endowment, Swensen saw from his own experience that a 60/40 split was dangerously undiversified. His solution was to add “alternatives”—real estate, commodities, foreign securities, and high-yield credit—to improve diversification and reduce the severity of drawdowns. For two decades with Swensen at the helm, Yale’s endowment was one of the most successful institutional portfolios in the world, due in large part to its multi-asset investing.

Of course, this was hardly a new idea. My co-author and Nobel Prize winner, Harry Markowitz had already established the benefits of multi-asset diversification in his seminal 1952 paper on portfolio optimization. It just took three decades for Swensen and the endowment world to carry the concept into practice. Today, multi-asset portfolios are still only embraced by unusually discerning CIOs. In terms of popularity and consumer sophistication, 60/40 is the ubiquitous domestic light beer of investing, and multi-asset diversification is still a cult IPA.

Meanwhile, equity management has evolved at lightning speed. In the 1960s, Nobel Laureate William Sharpe introduced the CAPM. Fellow Nobel Winners, Eugene Fama and Paul Samuelson then advanced the case for indexing with empirical studies in the early 1970s. By 1975, Jack Bogle launched the first S&P 500 index fund at Vanguard. Today, more than half of mutual fund and ETF assets are indexed. When the industry functions properly, the best solution—before too long—becomes the popular solution. Sadly, multi-asset diversification hasn’t enjoyed the same trajectory.

Most endowment portfolios are closet 60/40?! Endowment-style diversification has gained some traction, but often more as fashion than as true investment philosophy. Many of the “multi-asset” portfolios offered by the largest “model strategists” to financial advisors are nothing more than closet 60/40s. They are lightly disguised with a sprinkling of emerging markets, high-yield bonds, or commodities. But despite this exotic window dressing, they still correlate more than 90% with the classic 60/40 mix. It is multi-asset in appearance, not in substance. The mantra is “avoid business risk”: do appear differentiated, but don’t actually do anything differently. It harkens to Hollywood studios’ strategy to appear “indie” while continuing to write scripts optimized for mass-market box office consumption.

Asset Allocation: The Fee Problem

Another obstacle is cost. A simple 60/40 built from the S&P 500 and U.S. Treasuries carries a dirt-cheap total expense ratio, often under 20 basis points. Adding meaningful exposure to emerging markets, commodities, or high-yield credit raises fees by 10–15 bps. Clients see the fee increase immediately. The improved risk-return benefits only compound slowly over full market cycles. No wonder enthusiasm is muted for both the client and advisor. It is simply not human nature for consumers to value or pay much for future gains. We wouldn’t otherwise have to preach so much about an ounce of prevention outweighing a pound of cure.

The misalignment of incentives is thus obvious: More expensive funds added to improve portfolio diversification lead to higher fees. But clients benefit from true multi-asset investing only in the long-run but; at the outset, they are angry and suspicious about a higher overall portfolio expense ratio. Advisors, meanwhile, bear the burden of defending higher total portfolio costs without compensation. Sure, advisors are fiduciaries, but they’re also rational economic agents. Unsurprisingly, many can conclude that it is easier to hide in comfort behind the safety of 60/40.

¹ Brinson, Hood, and Beebower (1986).

Multi-Asset Portfolio Management: Ray Dalio's Risk Parity

Telling advisors to “diversify into low correlation asset classes” is vague. How much should go into alternatives—10%, 30%, 50%? What framework should guide the decision? Markowitz's optimization remains elegant in theory, but unworkable in practice. No one can reliably forecast asset-class returns, which are the most crucial inputs to the Markowitz machinery.

Ray Dalio's great contribution was to strip out the impossible part and focus on what can be more reliably estimated: volatility and correlations. His risk parity framework balances asset risks in the portfolio, which then creates portfolios that are more resilient to shocks. It was, in effect, Markowitz portfolio optimization without the dependence on fortune-telling when it comes to asset class returns.

Multi-Asset Portfolio Management: The Intuition behind Risk-Based Allocation

Other risk-based asset allocation approaches, such as equal risk contribution (ERC), which I have published on frequently, have become more widely used today. The idea is simple: First, identify assets with credible and substantive long-term risk premiums, without pretending to know exactly what those premiums will be or when they will show up. Second, build a portfolio focusing only on the drawdown risk. The goal isn't to hit a homerun for a short-term focused speculative investor. The goal is to reduce hard-to-stomach portfolio shocks so clients can stay invested through full cycles to compound their wealth into a bountiful retirement.

By focusing on risk rather than return forecasts, risk-based methods naturally suppress the usual investment hubris. Overconfidence and recency bias are known to creep into allocation decisions when ‘investment jocks’ sit around a conference table arguing their macro predictions. The alpha energy behind knowing the future and laying down bets to validate one's ego are generally best reserved for prop trading, rather than financial planning on behalf of clients planning for retirement.

Risk estimation—asking “What could go wrong?”—by its very nature, creates a healthy fear of markets and the ‘unknown unknowns’. This is the appropriate mode for managing retirement portfolios, and for ensuring client's sleep quality. In other words, risk-based allocation exercises force advisors to think less like sports bettors and more like sports bookies: You don't have a strong view on which teams will win, you just balance the book so you can't lose, then sit back and comfortably rake in the spread.

As nice as that sounds, adoption has been slow. Inertia is truly the strongest force in the universe. Advisors still ask, “What evidence do I need to move away from 60/40?” when the real question should be, “What evidence justifies abandoning global diversification for a concentrated bet on U.S. equities?” To give up that much diversification, one would need extraordinary conviction that U.S. stocks will dominate all other assets, that U.S. cash will dominate gold for the next decade. Few advisors have that kind of clairvoyance, even if the business often requires that they act as if they do.

Market Timing: Taboo or Wisdom?

Conventional wisdom says: never time the market. Ironically, academic research is filled with evidence that returns and risks are time-varying and timeable! Nobel Prize winner Robert Merton's iCAPM launched the literature on mean-reverting equity premium. Nobel Prize winner Robert Shiller anchors the long empirical literature documenting mean-reverting equity returns, which lead to predictability and timing profits. Nobel Prize winners Robert Engle and Lars Hansen have built models for characterizing the mean-revert nature of volatility and correlation risk. Both empirical data and theoretical models suggest that mean-reverting expected returns and risks are integral features of our financial markets.

And then there is Warren Buffett. He times the market with unapologetic clarity. Today, he sits on \$350 billion in cash—roughly 25% of his portfolio—after being fully invested five years ago. His advice is blunt: “Be fearful when others are greedy, and greedy when others are fearful.” In other words: market timing could make

sense, if it's about taking the other side of behaviorally biased investors' mistakes.

Buffett reduces equity exposure when investors are euphoric and ignoring risks. Each cycle, he is mocked for being "too early," and each cycle, he laughs all the way to the bank. Perfect timing is impossible, but that is not the point. Market timing in its proper form is about avoiding bad bets and leaning into good ones as markets seesaw between fear and greed.

Market Timing: Scientific vs. Voodoo Timing

Like Buffett's approach, the timing researched in the academic literature is not some mystical top-and-bottom calling. It can't predict the future and make investing a risk-free exercise. An astrologer would be better suited for that sort of 'voodoo timing' than a macro economist. Academic and Buffett-style market timing is about assessing whether markets are offering fair compensation for risk at this moment in time.

When investors are greedy, expectations are often too high, and the odds of continued strong performance are poor. When investors are fearful, expectations are often too low, and the odds of a rebound are favorable. There are no 'sure things' here; think of it as the difference between placing a wager as the player or the house. The player may get lucky in the short run, winning a few hands here and there, but the house, with odds behind it, almost always wins over time. Sensible timing, under this view, is about seeking to more often play as the house.

Putting it all Together: A Smarter Alternative to Classic 60/40 Investing

I hope it will be clear from the discussion above that claims of the superior performance of the 60/40 portfolio are often overstated and rest on some weak assumptions that likely won't hold in practice. It's an approach born of convenience—simple, easy to remember, with a name that suggests some kind of vague quantitative rigor. Over time and with widespread adoption, it's become a way for advisors to avoid taking responsibility for what economists have shown is the most impactful investment decision a client will make:

their portfolio's asset allocation. But the good news for clients and their advisors is that there are alternatives to the 60/40 portfolio. The best institutional CIOs are already using them.

Just as Jack Bogle's index fund and the multi-factor "smart beta" strategies I helped to launch over two decades ago put superior, scientifically grounded equity portfolio management tools into the hands of stock investors, in the time since the 60/40 portfolio first gained mass appeal, academics and clever

It's time for us to retire the 60/40 'default option'

practitioners have made huge advances in research around smarter approaches to the all-important asset allocation decision. I've described some of the key building blocks here. In keeping with most good bits of investing wisdom, the tools for constructing a better asset allocation turn out to derive their power not from complexity, but from the systematic application of common sense.

The problems with a 60/40 allocation are obvious: It focuses solely on stocks and bonds, despite investors having access to many more sources of less correlated returns. Even within traditional asset classes, it's woefully under-diversified. And it's a static portfolio in a world we know to be inherently dynamic. Making smarter asset allocation decisions involves addressing each of these weaknesses with weapons from an arsenal we've developed over the last few decades.

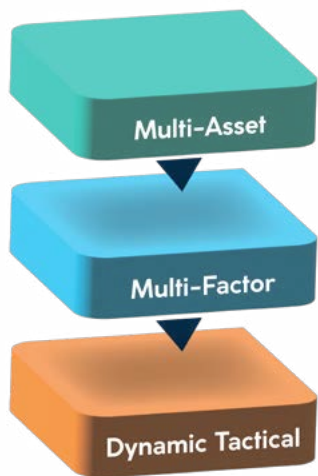
The Challenge: Being Better Means Looking Different

The industry's reliance on a 60/40 portfolio has never been about creating an optimal allocation for the client. It was always about convention, safety, and the comfort of doing what everyone else does. Investment titans and decades of good academic research argue that more diversified, risk-aware approaches—endowment-style multi-asset investing, weighted by risk and managed

countercyclically against the fear-and-greed cycle—could produce robust portfolios with likely better odds of long-term success.

The biggest challenge in adopting a better framework isn't about some inherent difficulty in the methodology. As we've seen, the foundation of a modern approach to asset allocation is simple and intuitive, and it's easy enough for a competent practitioner to implement such a strategy. Indeed, I've applied these principles across a range of institutional and advisory portfolios.

In reality, the principal hurdle for an advisor to overcome in moving away from the 60/40 is having the courage to do something different. It means dropping the long-held default option to which most advisors cling on blind faith.



It means abandoning the 'safety-in-numbers' that comes from following the herd.

And in the short run, a smarter framework for asset allocation also means accepting slightly higher costs: the price of accessing a wider range of assets. While most advisors will understand the modest added expense as a small price to pay for a smoother journey, it's something they'll need to explain to clients, and that requires skill.

But for advisors who seek something better than a low-

effort generic default—for advisors who want to give their clients access to a powerful modern approach based on strong academic foundations—a good alternative is available and ready to go. I believe strongly that advisors with the motivation and mastery to message these advances to their clients may not only enjoy better investing outcomes, but also the triumph of avoiding what's easy to do and instead taking the path they believe is right.

Multi-Asset

Just as David Swensen discovered when he took over Yale University's endowment in the late '80s, one approach to reducing a portfolio's risk is simply recognizing that equities and fixed income aren't the only game in town. The Endowment Model brings a range of alternative asset classes to bear in a portfolio, helping investors to truly exploit the "free lunch" of diversification through ownership of things like liquid real estate investments, commodities exposure, foreign stocks, and allocations to high-yield credit.

Risk-Based

Expanding the universe of investment types is likely the easiest step to a smarter allocation, but we can't stop there. The next important question an investor needs to answer is how to divvy a portfolio up across those asset classes. Ray Dalio understood that the key to doing this well is a simple change in perspective: Rather than focus on return—the number most investors' target, but one that is undoubtedly the hardest to forecast—an allocator should seek to balance the risk arising from each sleeve of a portfolio. In managing risk, we spend our time worrying about what we can actually control, and the returns naturally roll in without our help.

Dynamic

Investors wary of attempts to time the market aren't wrong: When most of us hear "market timing", we imagine a technical analyst trying to perfectly catch the index at its top or bottom. That sort of "voodoo timing" should be avoided. On the other hand, we know from decades of research—giving rise to numerous Nobel prizes—that markets are time-varying and that the ebbs and flows can be predictable. The technology to harness that predictability rests on a common-sense intuition that Warren Buffett put better than anyone when he advocated leaning in during times of fear and pulling back during times of greed.

Putting it All Together: Stacking the Benefits

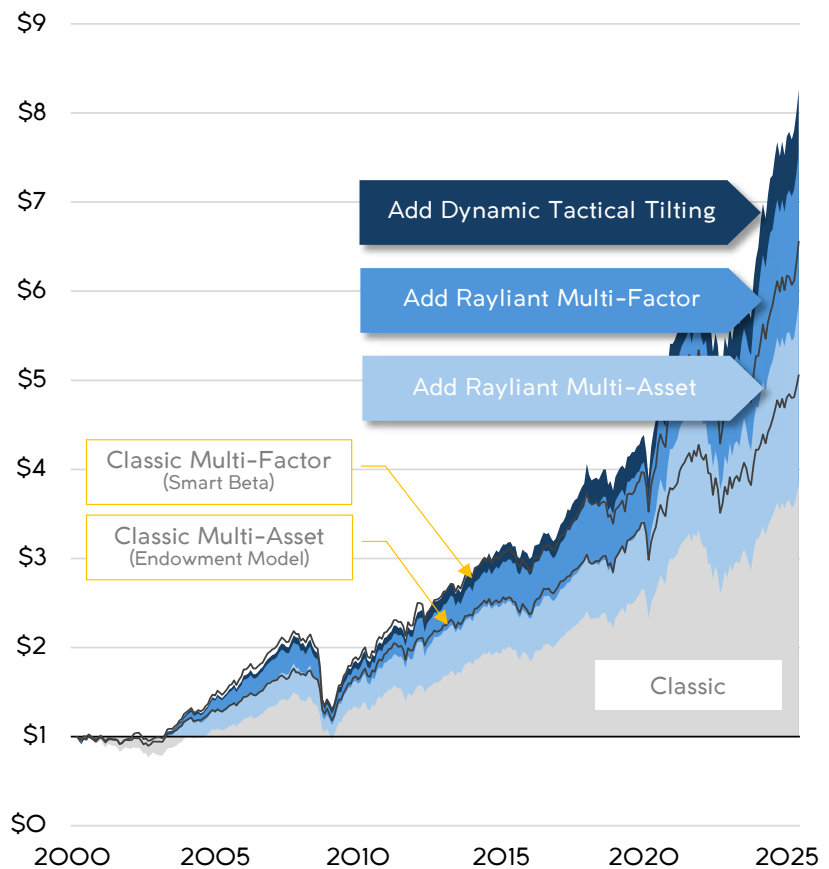
From what I've written here, it's easy enough to understand the appeal of modern asset allocation theory, but the proof is in the pudding: How have these approaches actually performed in practice? In the chart below, I've simulated a simple 60/40 strategy, many advisors' default strategy, and compare that side-by-side with a modern alternative approach like the one I've just outlined for readers. To illustrate the benefits of each component—and the way in which those benefits “stack” as we build out the approach with insights from decades of research—I've built up the methodology I implement for clients step-by-step. Alongside each step, I offer some thoughts on what we're doing and why it works.

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The Long-Term Benefits of “Alpha Stacking”



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Each improvement builds on the last—layering decades of research into a stronger, more resilient portfolio.

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Putting it all Together: Moving to a Multi-Asset, Risk-Based, Dynamic Asset allocation framework

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Important Considerations Regarding Market Timing

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