

PORTFOLIO



Julie Segal

## Investors Know They Own Too Much Tech. This Analysis Shows That It's Worse Than They Think.

An alternative way of looking at market-cap weighted index funds shows that investor exposure to the sector is higher than it was during the tech bubble.

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Michael Nagle/Bloomberg

Investors have long been worried about the handful of technology companies that make up a huge part of the S&P 500 and, as a result, their stock portfolios.

Turns out they may have reason to worry: A new analysis has found that investors actually have almost 15 percent more technology exposure than the amount shown by the most commonly used measures.

A yet-to-be-released paper from data science firm [Syntax Advisors](#) entitled, “Do You Know What You Own? How Much Technology is Really in the S&P 500?” shows that as of September 30, institutional and other investor portfolios that use market cap-weighted index funds tied to the S&P 500 had a tech exposure rate of 42 percent. In contrast, most traditional measures — which generally group companies according to broad sectors such as information technology, industrials, and financials — put tech exposure in the S&P 500 at 27.6 percent.

Because pension funds and other big institutions have adopted index funds for at least part of their stock portfolios, many of them now face new risks. One of the criticisms of funds that track indices such the S&P 500, which is weighted by the market capitalization of its stocks, is that the benchmark has gotten concentrated in the most expensive constituents — think Alphabet, Apple, and Microsoft, for example. Investors, as a result, are less diversified than they think and more exposed to a potential decline in these stocks.

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Syntax's systems were designed to address what it believes are weaknesses in a commonly used method called GICS, or global industry classification system, which lumps companies into the high-profile sectors long used by Wall Street analysts and bankers. Syntax's methodology, on the other hand, profiles companies by doing a deep dive into their product lines and other activities to show just how much the various security categorization systems can understate, or overstate, the biases in a portfolio. This is a tool that can be important at a time when investors are increasingly looking for more precise ways to understand and quantify the risks in their portfolios, especially if they use sector weights as a proxy when making larger investment policy and asset-allocation decisions.

While most CEOs would say their strategies are driven to some extent by technology, Syntax's research allows companies to drill down even further and understand more clearly the risks that a general tech downturn might have on their product lines, divisions, or even their research and development efforts.

"It's a concentrated trade, not a diversified trade," said Simon Whitten, product strategist at Syntax. Tech risk in the S&P 500 is "far higher now than it was in the tech bubble. Tech now is like financials [were] in '08." Whitten, who has worked in the industry for 17 years, including a stint as a managing director at State Street, where he set the research agenda, explained that financials permeated the broader market in the years preceding the global financial crisis in much the same way that tech has infiltrated most sectors today.

"If there is a change in sentiment away from tech, it will take 42 percent of the market with it," he said. And tech has already been testing investors. In early October, technology companies declined sharply, with Interactive Media & Services down 3.08 percent, semiconductors down 2.76 percent, and software off by 2.29 percent. At the same time, according to the report, the broad market dropped by only 1.30 percent, and the average stock declined only 0.63 percent.

Paul Kenney, the head of product development and client solutions at Syntax, spent almost 20 years at consultant NEPC and managed Ford Motor Company's pension plan before joining Syntax in May. As he put it, "Sectors were once acceptable, but the world has changed." Both Whitten and Kenney stressed that when sentiment for technology changes,

tech stocks will trade in tandem and go down more than the broader market. That's where Syntax comes in. "We aim to have a more precise way of measuring just how big [tech stocks] are," Whitten said, "and [then answering the question,] when is big too big?"

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