



RISK PARITY

Risk Parity Derangement Syndrome

February 7, 2018

You may have noticed the market turbulence lately. You may have also noticed the legion of commentators among the media, politicians, and famous investors, blaming this turbulence on “risk parity,” “trend-following strategies,” or my favorite, just “the machines.”

Poppycock. Yes, it's come to this; they've driven me to swear like Mrs. Doubtfire.

To be clear, it's not unreasonable to think that strategies that target volatility in a long-biased portfolio are likely to sell into the higher market volatility that often coincides with market losses. Nor is it unreasonable to think that strategies that explicitly follow trends are likely to sell into bear markets (that's kind of obvious). So I guess they get the direction right. But, size matters. To make a statement about this you have to have a vague idea about how many dollars are in such strategies and what they are likely to sell in a down draft. You may notice a conspicuous lack of relevant estimates from the many “machine” haters. This isn't surprising because the facts show “the machines” can't possibly be the culprit.

If those blaming “the machines” (sorry, I seem to be compelled to keep using the air quotes) have different numbers and want to debate these findings, let's do it. That's always fair game. But if they just want to make accusations with nothing to support them, then they're just irresponsible yentas throwing shade they can't back up.

Okay, you may have noticed that I too have not offered anything concrete. Mea culpa. But, I got something up my sleeve: peeps. Well one peep. My partner Michael Mendelson, who, thankfully, is far less belligerent and snarky than me, has been on top of this issue for the last several years and he explains [here](#) why risk parity and trend-following strategies are not to blame — and unless someone wants to argue with his views on the actual sizes, which again we'd welcome because legit debate is always great, they should [sit on it](#).

This document is not intended to, and does not relate specifically to any investment strategy or product that AQR offers. It is being provided merely to provide a framework to assist in the implementation of an investor's own analysis and an investor's own view on the topic discussed herein.

This document has been provided to you solely for information purposes and does not constitute an offer or solicitation of an offer or any advice or recommendation to purchase any securities or other financial instruments and may not be construed as such. The factual information set forth herein has been obtained or derived from sources believed by the author and AQR Capital Management, LLC (“AQR”) to be reliable but it is not necessarily all-inclusive and is not guaranteed as to its accuracy and is not to be regarded as a representation or warranty, express or implied, as to the information's accuracy or completeness, nor should the attached information serve as the basis of any investment decision. This document is not to be reproduced or redistributed to any other person. The information set forth herein has been provided to you as secondary information and should not be the primary source for any investment or allocation decision. Past performance is not a guarantee of future performance. Diversification does not eliminate the risk of experiencing investment losses.

This material is not research and should not be treated as research. This paper does not represent valuation judgments with respect to any financial instrument, issuer, security or sector that may be described or referenced herein and does not represent a formal or official view of AQR. The views expressed reflect the current views as of the date hereof and neither the author nor AQR undertakes to advise you of any changes in the views expressed herein.

The information contained herein is only as current as of the date indicated, and may be superseded by subsequent market events or for other reasons. Charts and graphs provided herein are for illustrative purposes only. The information in this presentation has been developed internally and/or obtained from sources believed to be reliable; however, neither

AQR nor the author guarantees the accuracy, adequacy or completeness of such information. Nothing contained herein constitutes investment, legal, tax or other advice nor is it to be relied on in making an investment or other decision. There can be no assurance that an investment strategy will be successful. Historic market trends are not reliable indicators of actual future market behavior or future performance of any particular investment which may differ materially, and should not be relied upon as such. Diversification does not eliminate the risk of experiencing investment losses.

The information in this paper may contain projections or other forward-looking statements regarding future events, targets, forecasts or expectations regarding the strategies described herein, and is only current as of the date indicated. There is no assurance that such events or targets will be achieved, and may be significantly different from that shown here. The information in this document, including statements concerning financial market trends, is based on current market conditions, which will fluctuate and may be superseded by subsequent market events or for other reasons.