ASSET ALLOCATION

The Past and Future of Quantitative Asset Management

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The defining element in quant management is diversification. Good quants play a statistical game. They do something that works based on an average tendency.

The advantage of quant management is that the manager does not have to make a big bet on any one position. Its disadvantage is that quant managers tend to know far less about any given situation than qualitative managers do.

Value and momentum are not the only means of organizing a quant portfolio. But the basic premise of juxtaposing two such good but uncorrelated long/short portfolios is generally quite applicable. They work for a variety of investment decisions, and their behavior is observable by using simple measures.

Data included in this article suggests that implementing these strategies globally yields a far higher Sharpe ratio than on an individual country basis. While the effectiveness of the two strategies varies, systematic failures of the combination are not found.

It is important to remember that sound portfolio construction requires diversification not just by dollars but by volatility; implementing this approach generally requires leverage.

Based on the data in this paper, quantitative equity represents a strategy that has worked for more than 80 years and now looks even more attractive than usual. Its benefits have not been arbitraged away, although quant strategies are vulnerable whenever many managers are doing the same thing at the same time and financing shorter than their investing horizons.

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