Factor/Style Investing

How Can a Strategy Still Work If Everyone Knows About It?

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Some people assert that once a strategy is "discovered" it can't work anymore. Others, often implicitly, assume the future will look as wonderful as the past. In this article, AQR Managing and Founding Principal Cliff Asness stakes out a middle ground. He argues that certain well-known classic strategies that have worked over the long term should continue to work going forward, though perhaps not at the same level and with different risks than in the past.

Classic investment strategies are things like value, momentum, carry and quality/defensive. When they are available at a fair fee, he believes such strategies are "very special" in the investment world because they can be a source of return with very low correlation with the rest of most investors' portfolios.

It is hard to argue that widespread knowledge of any successful investing strategy is a good thing for those few who knew about them first, but Asness contends that it does not necessarily mean that such strategies will stop working; some of the return is a rational risk premium and some is due to other investors' errors. While investors should watch out for potential problems that might come with extreme crowding into these strategies, he concludes that investors should not assume that once something is known it's gone forever.

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