



ALTERNATIVE INVESTING

Building a Better Equity Market Neutral Strategy

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AQR White Paper

Equity Market Neutral (EMN) is a well-established strategy designed to seek positive performance without exposing investors to the risk of the overall equity market. By definition, returns of EMN funds should be uncorrelated to traditional equity returns. EMN strategies are designed to make money when long positions outperform short positions, regardless of overall market direction. Thus, their returns are often considered pure alpha, and may be expected to improve a portfolio's expected returns, reduce its volatility, or both.

EMN works by taking long positions in stocks that are expected to outperform their peers and short positions in stocks expected to underperform. The positions are chosen so that the equity market exposure of the long side of the portfolio is offset by the exposure of the short side. This results in a strategy that is hedged to the aggregate stock market, thereby insulating investors from the major ups and downs in equities.

Institutional investors have long embraced alternative strategies such as EMN, whose long-term efficacy and diversification benefits have added significant value. With the emergence of liquid alternatives, a wider range of investors will be able to access these valuable tools so as to potentially improve the diversification and returns of their portfolios.

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