“Biggest tests may lie ahead” for market liquidity, says Minouche Shafik

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London Business School’s AQR Asset Management Institute hosts inaugural summit on the challenges of investing in a low return environment

Minouche Shafik, the Bank of England’s Deputy Governor for Markets and Banking, considered the implications of evolving market structures for academics, policymakers and practitioners at the inaugural summit for London Business School’s AQR Asset Management Institute, held on 26 and 27 October.

Attendees debated how asset owners should respond to expectations of low returns across asset classes, the options available to investors, and the implications for asset allocation. The discussion also examined the historical context for current asset prices, the role of market liquidity and the latest research available to help answer these questions.

In particular, the audience was warned that while analysis of historical data, when used in conjunction with economic intuition, can identify effective investment strategies, data mined can also be misleading and misused, so effective evaluation of sources and rationale is essential. Additionally, at current yields, bonds perform the role of ‘deflation hedge’ rather than acting as a source of significant real return.

Robert W. Jenkins, Chair of the AQR Asset Management Institute and Adjunct Professor of Finance, London Business School, commented: "The Institute brought together a unique combination of academics, practitioners and policymakers on a topic of importance to global investors. One of the main conclusions reached was that real returns are low by historical standards - and likely to remain low. This has implications not only for how one invests – but also for how one might organise a large investment organisation - both in terms of cost management and organisation by risk premia and asset classes”.

Delivering the keynote speech, Minouche Shafik spoke on the impact of changing market structures on liquidity, and the implications for policymakers, infrastructure providers and market participants.

“The recent bouts of volatility we have witnessed have not jeopardised the continued growth of the real economy…But the biggest tests may lie ahead”, explained Minouche Shafik, Deputy Governor, Markets and Banking, Bank of England.

Ms Shafik explained that over the coming years, three of the major factors that have dominated markets since the financial crisis – accommodative monetary policy, private capital inflows to emerging markets, and official sector outflows in the opposite direction – “seem set to change”, and those “tectonic shifts” may pose a challenge to the functioning of markets.

Alongside Ms Shafik, speakers included: Eduard van Gelderen, CEO of APG Asset Management; Cliff Asness, Managing Principal of AQR; Campbell R. Harvey, Professor of Finance, Duke University and Investment Strategy Advisor, Man Group; and Elroy Dimson, Emeritus Professor of Finance, London Business School.

David Kabiller, Founding Principal, AQR commented: “The Summit generated an extremely high calibre discussion on one of the most significant issues confronting the global investment community today –the current low expected return environment. A key purpose of the AQR Asset Management Institute is to drive discussion in a manner that will have a meaningful and lasting impact. We are dedicated to bringing academics, regulators, and industry practitioners together in this cause.”

Founded in January 2015, the AQR Institute promotes excellence in asset management through a combination of research, funding, and awards intended to further the sector’s ability to preserve and generate long-term wealth for individuals and societies.

The conference also saw the presentation of the inaugural AQR Fellowship Award on 26 October. Ryan Lewis, PhD candidate in Finance, London Business School, received the £10,000 prize in recognition of his research into the role of intermediaries in asset pricing.