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Has Risk Parity Jumped the Shark?

Admission: I am not a great investor. Friends often ask me for my view on individual stocks and investments. I readily admit that I lost as much money as everyone else in 2008/2009, and that I have no more insight into the future performance of individual securities than anyone else. I like to think that, like our audience, I am a big-picture guy: I'm into asset allocation, not security selection.

It's through this big picture lens that I now view the risk parity industrial complex.

I use that term hesitantly. When President Eisenhower spoke of the military industrial complex, he wasn't railing against the need for a military—he was speaking to the motives behind the companies and individuals who benefited from that need.

Similarly, I'm not questioning the need for risk parity. A strategy that focuses on risks, not returns, and that is almost inherently humble—"Who am I to judge which asset class will outperform over the next X years?" is a common refrain among CIOs I speak to about risk parity—is something that intuitively fits with my worldview.

Yet recent events have my skeptic alarm going off. Are we in a risk parity bubble? Consider this:

· The granddaddy of risk parity funds—Bridgewater's All Weather—has been closed to new investors, with (I believe) late-comers being steered into an "All Weather Lite" fund.

· Defined contribution assets are now being steered into risk parity products, either through target-date funds or as a stand-alone option.

· Asset managers are headhunting risk-parity experts to bolster their "street cred" in this space.

· Our annual Risk Parity Consultant Views survey shows consultants increasingly recommending risk parity to clients.

· It seems that every asset manager has or is launching a risk parity product—sometimes by simply rebranding a GTAA product. (This is worrying on a few levels.)

I don't have the answer to the question posed in my title. As I said, I'm not actually that good at investment predictions, and predicting bubbles is a bit of a fool's game—a broken clock etc.

But there seems to be a bit of a feeding frenzy with risk parity right now. There is so much capital flowing in that funds are being closed to new investors. Everyone wants to start a new fund. Consultants are pushing it. Less-sophisticated investors are being offered entrée. It all has overtones of 2007/2008, doesn't it?

The next question is this: What would happen in a risk parity "crash"? But that's for another blog, and another day.