ADIA Lab Scientist Receives Bernstein Fabozzi / Jacobs Levy Award

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ADIA Lab scientist and Advisory Board member, Professor Marcos Lopez de Prado, has been honored with the 25th Bernstein Fabozzi/Jacobs Levy "Outstanding Article" Award. His work, "Where are the Factors in Factor Investing?", was recognized for its critical examination of the econometric approaches used in factor investing studies.

Lopez de Prado's article, published in The Journal of Portfolio Management, identifies a significant logical inconsistency within the factor investing literature. He argues that while factor models are intended to have a causal interpretation, researchers virtually never justify their model specification choices in causal terms, hence the question "where are the factors in factor investing?" This oversight leads to misspecified models and the publication of false positives. Furthermore, through Monte Carlo experiments, he shows that misspecified factor models may be so biased as to estimate risk premia with the wrong sign, with the implication that factor strategies may be detrimental to investors in the long run. To rectify this, Lopez de Prado recommends that factor model specification choices are properly justified through causal graphs that are consistent with the empirical evidence.

Frank Fabozzi, editor of the Journal of Portfolio Management, praised Lopez de Prado's contribution: "Marcos's work brings to light the overlooked importance of causal reasoning in factor investing. His innovative analysis and recommendations could significantly strengthen the scientific basis of factor investing. Our readers believe that this is an exciting line of research, and the Journal looks forward to further discoveries in this direction."

Lopez de Prado commented on the significance of causal methods in economics and finance: "For over five decades, the heavy reliance on associational models has resulted in investment strategies that are not robust to parameter shifts. It is my hope that this prestigious award encourages other researchers to apply the tools of causal discovery and causal inference, so that financial economics may finally wake up from its associational slumber."

The annual Bernstein Fabozzi/Jacobs Levy Awards are determined by the readership of The Journal of Portfolio Management, and aim to recognize the year's most innovative and impactful research. Past recipients of the award include Nobel Prize laureates Robert Engle, Merton Miller, and Robert Shiller, along with prominent figures from both industry and academia, such as Cliff Asness, John C. Bogle, Campbell Harvey, Robert A. Jarrow, Martin L. Leibowitz, John M. Liew, Robert Litterman, Andrew Lo, Burton Malkiel, Lasse Pedersen, Jeremy Siegel, and Robert E. Whaley.

The article appeared in the April 2023 issue of The Journal of Portfolio Management, and it is available at https://www.pm-research.com/content/iijpormgmt/49/5/6

ADIA Lab supports the development of research across a range of computational and data science-related topics, with a special focus on societally important challenges.

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ADIA Lab is an independent institution engaged in basic and applied research in Data Science, Artificial Intelligence, Machine Learning, and High-Performance and Quantum Computing, across all major fields of study. This includes exploring applications in areas such as climate change and energy transition, blockchain technology, financial inclusion and investing, decision making, automation, cybersecurity, health sciences, education, telecommunications, and space.

Based in Abu Dhabi, ADIA Lab is an independent, standalone entity supported by the Abu Dhabi Investment Authority (ADIA), a globally-diversified investment institution that invests funds on behalf of the Government of Abu Dhabi.

ADIA Lab is governed by an Advisory Board of global thought leaders in data and computationally-intensive disciplines, including winners of the Nobel, Turing, Godel, Rousseeuw, Gordon Bell, and other prizes.

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