



IS IT TIME FOR SOME ARTIFICIAL INTELLIGENCE? - DIARY OF A FUND MANAGER SUPPLEMENT



In March, I attended the first NextGen Alpha Artificial Intelligence Investor conference and since then have been reflecting on what I heard and reading all that has come across my desk. What impact will artificial intelligence (AI) have on financial markets and how can I, as a conventional investment manager, take advantage of the accelerating rate of change we are surrounded by?

To start with I should admit to biases, or perhaps more correctly, where I have come from and where I am today. Back when gene sequencing was in its infancy and when we programmed computers using low level languages to leave enough memory space to do calculations, I studied the natural sciences. Sad to say not much is left of what I learned other than basic numeracy and a working knowledge of scientific method. However, scratch the surface and you will find a rational empiricist, less interested in clever theories than real results and that those who want to believe in something should go to church.

For over 30 years, I have been immersed in financial markets, gathering information, making decisions and reporting results to those whose savings I have responsibility for. The fund manager I was in the 1980s is very different to today's version, and I fully expect to be different again tomorrow. As Heraclitus said: "No man ever steps in the same river twice, for it is not the same river and he is not the same man".

So what right have I to write about the impact of AI on investment other than acknowledging the importance of embracing change? Progress has always been driven by those who ask questions and then either search for answers themselves or provoke others into action. When he was still at school, Einstein asked himself what the world would look like if he rode on a beam of light. The answer is full of paradox and that made it hard to answer, but a few years later he got there with his famous 1905 paper.

Running ahead of progress is imagination and, as ever, literature and films are way ahead of reality as anyone who has read Asimov's, I Robot, Orson Scott Card's, Ender's Game or Do Androids Dream of Electric Sheep? by Philip K. Dick will know. The film version of the Androids, Blade Runner, was all about questions, whether the Voight-Kampff Test or, most memorably, the Roy Batty character in search of a longer life asking, "questions, yes questions", before doing something gruesome to his creator.

So this first, but not last venture into AI is a collection of questions. Some will expose my ignorance, whilst others will provoke immediate answers, but if I'm lucky a few will fall into the hard to answer category. When Edmond Halley asked Newton if he could describe the motion of the planets around the sun, his immediate response was that they followed an elliptical path and that he would send the proof as soon as he could find it amongst his papers. It took three years to deliver on this promise, but his Principia Mathematica was worth waiting for.

There is no doubt that AI is changing the world. The Google AI search engine is our favourite gateway to the internet, machines can now beat humans at chess, Go, Poker and America's favourite quiz show, Jeopardy! The question is whether AI is better than humans in the game of investment which has seven billion moving pieces (all of us) and also has to cope with the weather. Although it is obvious that man plus machine, will win against man without machine the fund management industry has questions to answer. Most importantly, are machines alone already good enough to win without human intervention? If not now, then when or could it be never?



A variant of this question is, does the fund management industry need AI? Various answers occur. Is AI better than other technologies designed to replace human intervention in the decision making process? Time and the acid test of performance will tell. At present, the way in which AI investment strategies are described tends to be rather two dimensional, and so it strikes me of limited use in a three dimensional world. Beating indices is one thing, but making money is quite another. Gathering and analysing the huge amounts of information that we now have access to followed by efficient execution should be a winning combination, but arbitrary rule changes initiated by governments or the occasional collective emotional crises that remove liquidity from markets are hard to predict or plan for partly because there tends to be no time to react or learn. What happens if listed markets fail to capture growth opportunities because winning companies stay private? What if inflation makes a comeback widening the gap between nominal and real value to extremes not seen in the major economies for a generation? Will AI investment strategies be able to cope? In extreme circumstances, and how do we define extreme, who will be empowered to switch the machine off? Yet another science fiction allusion by the way, this time Obi Wan Kenobi talking to Luke Skywalker as he was attacking the Death Star in the first (and best) Star Wars film.

The move from single capacity stock markets to dark pools and high speed trading may have narrowed the bid offer spread, but hasn't changed returns. As AI gains ground in the investment world, will it alter markets, creating more or less volatility? More profoundly, will AI change the cost of capital for the companies that we invest in and which drive the global economy? Questions, questions.

What is clear is that the rate of change is accelerating and so those of us who consume investment products or create them need to be better informed than we are at the moment. Judgements will have to be made about change, whilst acknowledging that some of the constants of investment never will. Just like the natural world, financial markets can be red in tooth and claw, nasty, brutish, short and chaotic. Attempts to model certainty are doomed to failure. Faites vos jeux.

I will be chairing a panel discussion at the second NextGen Alpha Artificial Investor Conference in Frankfurt on 26th October, which will be an ideal opportunity to quiz the experts about these questions and many more.

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