Trust the machines? Funds run by artificial intelligence

July 5 2018, by Alex Veiga

This undated photo provided by ETF Managers Group shows Sam Masucci, founder and CEO of ETF Managers Group. Masucci recently talked to the Associated Press about his firm's investment funds and why an AI fund manager might prove to be better at generating investment returns than the human variety. (ETF Managers Group via AP)

A computer can trounce a human chess master and solve complex mathematical calculations in seconds. Can it do a better job investing your money than a flesh-and-blood portfolio manager?

Investors willing to test that question can do so with a couple of exchange-traded funds, or ETFs, that leave the investment decisions to a computer's so-called artificial intelligence, or AI.

ETF Managers Group and Ocean Capital Advisors launched an AI-powered fund last month dubbed the Rogers AI Global Macro ETF (BIKR) that invests primarily in single-country ETFs. The fund's AI sifts through millions of data points from countries around the globe and uses what it learns to determine how best to allocate the fund's holdings. (Humans carry out the trades, however.)

Does this approach work? Another AI fund launched last November by ETF Managers Group and Equbot shows some promise.

The fund, which is called the AI Powered Equity ETF (AEIQ), invests in a variety of U.S.-based companies and seeks to beat the returns of the S&P 500. So far, it's getting it done. The ETF is up 8.1 percent this year, while the S&P 500 has gained about 1.5 percent.

Still, a track record of less than a year on a single fund isn't nearly enough to gauge the merits of the AI approach. Also, like any fund, one should weigh potential gains against the fund's fees. At 75 basis points, AEIQ's expense ratio is on the higher end of ETF fees, even if the AI is doing all the thinking. By comparison, Schwab's US Broad Market ETF, which also invests in a broad swath of U.S. stocks, has an expense ratio of 3 basis points.

Sam Masucci, founder and CEO of ETF Managers Group, recently talked about his firm's investment funds and why an AI fund manager might prove to be better at generating investment returns than the human variety. Answers have been edited for clarity and length.

Q: How is AI different or better than the computer algorithms used for high-speed trading or robo-advisers that can rebalance an investor's retirement portfolio?

A: It's different. If you think about algorithmic trading or robo-advisers these are tools that are used by human portfolio managers to make decisions on what to invest in. Artificial intelligence is very, very different. While there are humans that obviously are continuing to feed data into it, it's the computer, the AI environment, that is distilling that information and making the ultimate portfolio selection.

In the case of AI, the portfolio manager is not looking at a trade signal and making a decision. The AI model is prescribing the action that needs to be taken, whether it's a purchase or a sell.

Q: Is AI better at picking stocks and curating funds than more conventional approaches?

A: We will find out. Theoretically, it should be better, because it has the ability to crunch a much larger universe of daily information and risk-weigh and apply it to a portfolio much faster and efficiently than humans can. In addition, the computer learns from its past actions and the result of those actions and gets smarter over time. And it removes any human bias, because it's a machine. But it's still new.

We launched the first AI fund, AIEQ, in November. That fund is designed to offer S&P 500-like exposure with a better return and less volatility, and it has been doing that. And it's getting better at doing that.

Q: Can these AI funds anticipate market corrections?

A: The more predictive information you can have and analyze, the better. And I am confident machines are better at that. They have the bandwidth.

Q: Is AI going to eventually replace the active, human fund manager?

A: No. I don't think the computer is going to put us out of a job anytime soon. But it will allow us to enter into markets and offer people another portfolio solution that takes advantage of the newest technologies.