Factor/Style Investing

Carry

November 7, 2013

Journal of Financial Economics

We define an asset's "carry" as its expected return assuming that market conditions, including its price, stays the same. A security's expected return can be decomposed into its "carry" and its expected price appreciation, where carry can be measured in advance without an asset pricing model.

We find that carry predicts returns both in the cross section and time series for a variety of different asset classes that include global equities, global bonds, currencies, commodities, U.S. Treasuries, credit and equity index options. This predictability underlies the strong returns to "carry trades" that go long high-carry and short low-carry securities, a strategy applied almost exclusively to currencies but shown here to be a robust feature of many assets.

We decompose carry returns into static and dynamic components and analyze the economic exposures. Despite unconditionally low correlations across asset classes, we find times when carry strategies across all asset classes do poorly, and show that these episodes coincide with global recessions.

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