

EDHEC-Risk Institute papers present a complete analysis of the two most popular fixed income factors: value and momentum

Following up on more than a decade-long research effort in the area of factor investing in equity markets, we have felt a timely need among asset owners and asset managers to gain a better understanding of the theoretical and practical challenges involved in harvesting risk premia in fixed-income markets.

Two new studies produced as part of the Amundi research chair on “ETF, Indexing and Smart Beta Investment Strategies” **focus on the two factors that explain a large fraction of differences in the cross-section of bond returns, namely “value” and “momentum”, using economically justified proxies for these attributes.**

In the publication entitled “[*Factor Investing in Fixed-Income – Defining and Exploiting Value in Sovereign Bond Markets*](#)”, the authors propose a definition of value in Treasury bonds that is more satisfactory than those found in the recent literature, and that allows for statistically significant and economically relevant predictions of cross-sectional excess returns.

- They give an explanation of the profitability of the strategy built using their value signal by linking it to market liquidity and Treasury market volatility.
- Their value pricing factor exploits the differences between the market and the theoretical values of Treasury bonds, where value is ascertained using an economically-motivated term-structure model.
- They provide an explanation for this strong link using arguments similar to what can be found in the recent literature on liquidity in Treasuries.

In a companion paper entitled “[*Factor Investing in Fixed-Income – Cross-Sectional and Time-Series Momentum in Sovereign Bond Markets*](#)”, they undertake a systematic, *security-level* analysis of momentum and reversal strategies in US Treasuries, covering more than 40 years of data.

- They find that look-back and investment periods exist for which momentum times series strategies give rise to statistically and economically significant Sharpe ratios.
- They find that, after adjusting for duration, the reversal cross-sectional strategy has even larger Sharpe ratios, and is profitable over a wider range of look-back and investment periods.
- They find an explanation for this finding in the mean reverting properties of the yield-curve slope.
- They show that the duration-adjusted reversal cross-sectional strategy can be successfully implemented in a long-only fashion.

Commenting on this research, Riccardo Rebonato – Professor of Finance at EDHEC-Risk Institute, EDHEC Business School, said “Return predictability in Treasury Bond market is currently one of the most exciting areas for smart-beta investment. The papers mentioned above are two contributions in a much wider research programme at EDHEC, focused on the cross-sectional and time series predictability in the fixed-income space”.

Bruno Taillardat, Head of Smart Beta & Factor Investing at Amundi, added his thoughts: "The increasing adoption of Smart Beta and factor-based solutions, particularly in the area of fixed income investment, represents an exciting challenge for asset managers seeking to design the right solutions to address clients' needs. To further enhance Amundi's strong engagement to helping investors meet their asset allocation goals, our partnership with the EDHEC-Risk Institute is a key element to strengthen our leadership in providing education and research tools."

You can access here the publications “[Factor Investing in Fixed-Income – Defining and Exploiting Value in Sovereign Bond Markets](#)” and “[Factor Investing in Fixed-Income – Cross-Sectional and Time-Series Momentum in Sovereign Bond Markets](#).”

In a companion paper released in May entitled [Factor Investing in Sovereign Bond Markets - A Time-Series Perspective](#), the same authors focused on the two factors that explain a large fraction of differences over time in bond returns, namely the “level” or “slope” of the yield curve.



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About EDHEC-Risk Institute

Academic Roots & Practitioner Reach

For more than 15 years, EDHEC Business School has been pursuing an ambitious policy in terms of practically relevant academic research. This policy, known as “Make an Impact”, aims to make EDHEC an academic institution of reference for the industry in a small number of areas in which the school has reached critical mass in terms of expertise and research results. Among these areas, investment management has occupied a privileged position, leading to the creation in 2001 of EDHEC-Risk Institute, which has developed an ambitious portfolio of research and educational initiatives in the domain of investment solutions for institutional and individual investors.

This Institute boasts a team of permanent professors, engineers and support staff, and counts a large number of affiliate professors and research associates from the financial industry among its ranks. EDHEC-Risk Institute is located at campuses in the City of London (United Kingdom) and Nice, (France). The philosophy of the Institute is to validate its work by publication in international academic journals, as well as to make it available to the sector through its position papers, published studies and global conferences.

To ensure the distribution of its research to the industry, EDHEC-Risk also provides professionals with access to its website, <https://risk.edhec.edu>, devoted to asset and risk management research for the industry, with a focus on investment solutions. Additionally, its quarterly newsletter is distributed to over 150,000 readers.

In addition to the EDHEC Alternative Indexes, which are used as performance benchmarks for risk analysis by investors in hedge funds, and the EDHEC-IEIF Monthly Commercial Property index, which tracks the performance of the French commercial property market through SCPIs, EDHEC-Risk has recently launched a series of new initiatives.

- The [EDHEC-Princeton Retirement Goal-Based Investing Index Series](#), launched in May 2018, which represent asset allocation benchmarks for innovative mass-customised target date solutions for individuals preparing for retirement;
- The [EDHEC Bond Risk Premium Monitor](#), the purpose of which is to offer to investment and academic communities a tool to quantify and analyse the risk premium associated with Government bonds;
- The [EDHEC-Risk Investment Solutions \(Serious\) Game](#), which is meant to facilitate engagement with graduate students or investment professionals enrolled on one of EDHEC-Risk's various campus-based, blended or fully-digital educational programmes.

EDHEC-Risk Institute also has highly significant executive education activities for professionals, in partnership with prestigious academic partners.

In 2012, EDHEC-Risk Institute signed two strategic partnership agreements. The first was with the Operations Research and Financial Engineering department of Princeton University to set up a joint research programme in the area of investment solutions for institutions and individuals. The second was with Yale School of Management to set up joint certified executive training courses in North America and Europe in the area of risk and investment management.

As part of its policy of transferring know-how to the industry, in 2013 EDHEC-Risk Institute also set up ERI Scientific Beta, which is an original initiative that aims to favour the adoption of the latest advances in smart beta design and implementation by the whole investment industry. Its academic origin provides the foundation for its strategy: offer, in the best economic conditions possible, the smart beta solutions that are most proven scientifically with full transparency in both the methods and the associated risks.

EDHEC-Risk Institute also contributed to the 2016 launch of EDHEC Infrastructure Institute (EDHEC*infra*), a spin-off dedicated to benchmarking private infrastructure investments. EDHEC*infra* was created to address the profound knowledge gap faced by infrastructure investors by collecting and standardising private investment and cash flow data and running state-of-the-art asset pricing and risk models to create the performance benchmarks that are needed for asset allocation, prudential regulation and the design of infrastructure investment solutions.

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About Amundi ETF, Indexing and Smart Beta

With more than €112 billion¹ in assets under management, Amundi ETF, Indexing and Smart Beta is one of Amundi's strategic business areas and is a key growth driver for the Group.

Amundi ETF, Indexing and Smart Beta business line provides investors – whether institutions or distributors – with robust, innovative, and cost-efficient solutions, leveraging Amundi Group's scale and large resources. The platform also offers investors fully customized solutions (ESG, Low Carbon, specific exclusions, risk constraints, etc.).

With over 30 years of benchmark construction and replication expertise, Amundi is a trusted name in ETF & Index management among the world's largest institutions. The team is also recognized for its ability to develop Smart Beta & Factor Investing solutions, with more than 10-year track-record.

1- All figures and data are provided by Amundi ETF, Indexing & Smart Beta at end March 2019