Introduction

Revisiting pairs trading 20 years after Gatev2006

Pairs trading first took shape in the mid-1980s when Nunzio Tartaglia's quantitative desk began systematically scanning U.S. equities for temporary deviations in the relative prices of stocks that had historically moved in tandem. The recipe is intuitive: locate two securities whose past price paths exhibit a tight long-run relationship, short the one that has recently run ahead, go long the laggard, and close the position as soon as the spread mean-reverts. Gatev2006 famously showed that this seemingly nave contrarian rule delivered annualised abnormal returns of roughly 11 percent between 1962 and 2002–even after conservative trading-cost assumptions–prompting an explosion of interest among hedge funds and proprietary "market-neutral" desks. Yet the very popularity that followed appears to have eroded the opportunity: these same authors already noted shrinking profits in the late 1990s, and the follow-up study by Do2010 documented a further decline. Extending the evidence through 2024, fig:pairs$_{d}ecayshowsthatthecanonicalimplementationofthestrategyhasfailedtogen$
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