Discussion of

# Blades of Carry: The Big Short

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# Summary

Exciting paper!

- An innovative predictor, termed middle correlation risk (MCOR), forecasts carry trade returns.
- A strategy combines momentum and MCOR, termed Momentum-at-Carry (MaC), outperforms the traditional carry trade strategy.

# Contribution

- Time-series predictability of carry trade returns using currency correlations.
- Global currency hedging using middle portfolio currencies.

# Major comment (1): Mechanism

Why does MCOR work as a predictor?

- Middle portfolio currencies are exposed to economic states (to test).
- In economic downturns, currencies tend to become more positively correlated with each other, leading to a high MCOR (to test).
- Carry trade returns (high-minus-low) are less exposed to economic states when MCOR is high, leading to lower future excess returns.

## Major comment (2): Robustness of MCOR

A comparison with existing predictors in literature:

- FX market variance (Cenedese et al., 2014)
- Changes in a commodity index (Bashi and Panayotov, 2013)
- ...

# Minor comments

- Step-by-step constructions and more interpretations for MCOR and MaC.
- Robustness test using alternative base currencies

  E.g. 48 currencies from Menkhorff et al. (2012).
- Predictability: report Hordrick (1992) t-test statistic.
- Clearer definitions for some terms

  E.g. ”currency dispersion” and ”middle portfolio currencies”.