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The Skewness of Commodity Futures Returns

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Abstract

This article studies the relation between the skewness of commodity futures returns and expected returns. A trading strategy that takes long positions in commodity futures with the most negative skew and shorts those with the most positive skew generates significant excess returns that remain after controlling for exposure to well-known risk factors. A tradeable skewness factor explains the cross-section of commodity futures returns beyond exposures to standard risk premia. The impact that skewness has on future returns is explained by investors' preferences for skewness under cumulative prospect theory and selective hedging practices.

Keywords: Skewness; Commodities; Futures pricing; Selective hedging

JEL classifications: G13, G14

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