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Covering the World: Global Evidence on Covered Calls

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Typical covered call strategies may be decomposed, using a risk and performance attribution methodology, into three components: equity exposure, short volatility exposure, and equity timing. This paper applies that attribution methodology to covered calls on eleven global indexes. We find that, in our cross-section of indexes, the risk and return contributions of the three components are remarkably consistent. Across the board, the covered call's equity exposure is responsible for most of the strategy's risk and return, while the short volatility exposure has the highest Sharpe ratio of the strategy's components. The returns from the equity timing exposure are statistically insignificant in all eleven indexes, yet this exposure contributes a relatively large amount of the strategy's risk.

These results provide further evidence that managing equity exposure in covered calls provides superior risk-adjusted returns. Further, a globally-diversified portfolio of risk-managed covered calls may be viewed as a defensive alternative to global equity, providing similar returns with lower volatility and lower drawdowns.

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