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Central Bank Communication and the Yield Curve

(co-authored with Matteo Leombroni, Gyuri Venter and Paul Whelan)

Abstract

Using the institutional features of ECB monetary policy announcements, we provide evidence for the risk premium channel of central bank communication. While central bank communication had a homogeneous effect across Euro-area sovereign bond yields before the European debt crisis, it drove a wedge between peripheral and core yields afterwards. Guided by the predictions of a theoretical model in which central bank communication reveals information about the state of the economy, we empirically link the periphery-core wedge to break-up and credit risk premia, and show that equity response to shocks can identify the strength of this risk premium channel.