

New-Keynesian Macroeconomics and the Term Structure

(with Seonghoon Cho and Antonio Moreno)

Abstract

This article complements the structural New-Keynesian macro framework with a no-arbitrage affine term structure model. Whereas our methodology is general, we focus on an extended macro-model with an unobservable time-varying inflation target and the natural rate of output which are filtered from macro and term structure data. We obtain large and significant estimates of the Phillips curve and real interest rate response parameters. Our model also delivers strong contemporaneous responses of the entire term structure to various macroeconomic shocks. The inflation target dominates the variation in the "level factor" whereas the monetary policy shocks dominate the variation in the "slope and curvature factors".