

Term Premia and Credit Risk in Emerging Markets: The Role of U.S. Monetary Policy

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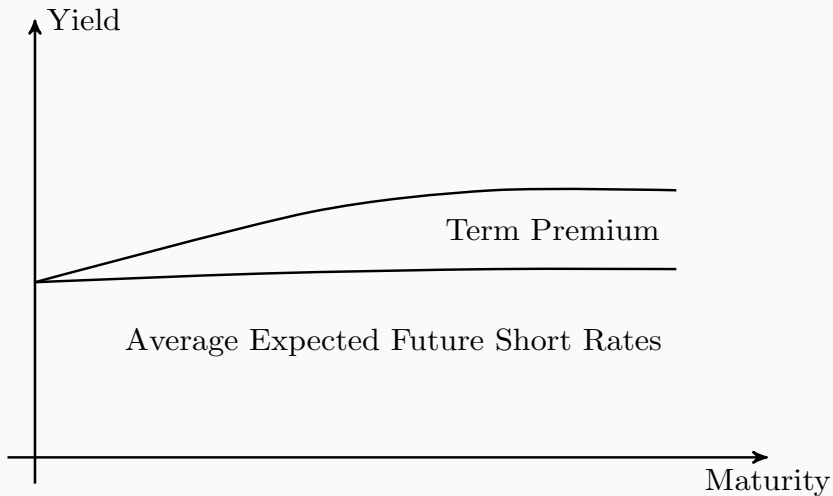
U.S. Monetary Policy Spillovers

Asset price effects of U.S. monetary policy abroad

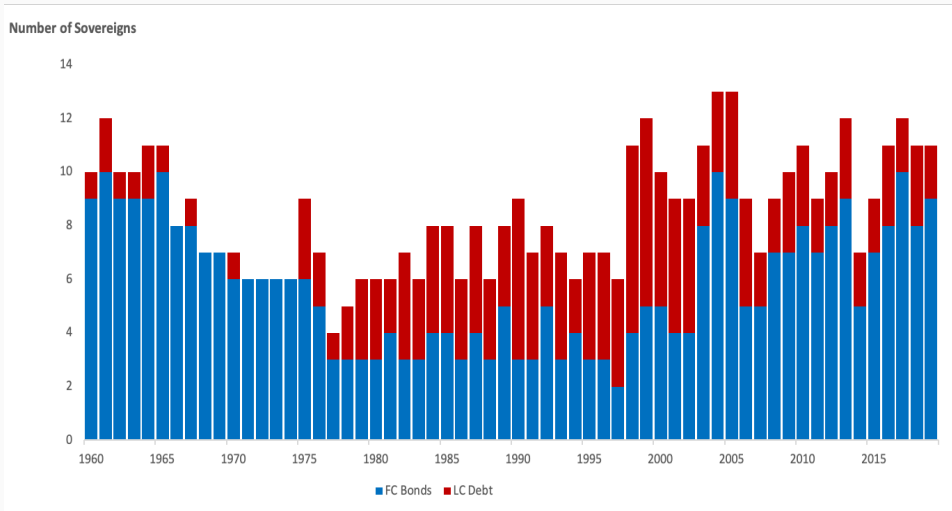
- Stocks
- Exchange rates
- Bonds
 - Foreign currency
 - Local currency: 90% of emerging market (EM) sovereign debt in 2018

Research Question: How does U.S. monetary policy transmit to EM yields?

Traditional Yield Curve Decomposition

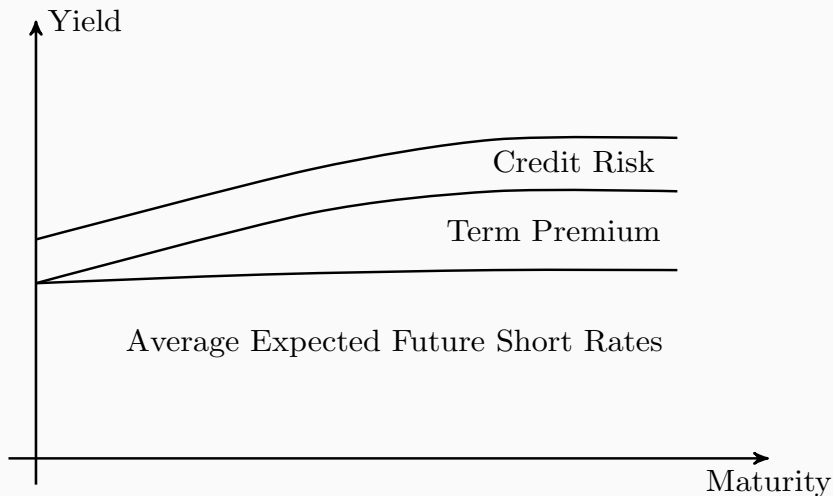


Do Sovereigns Default on Local Currency Debt?

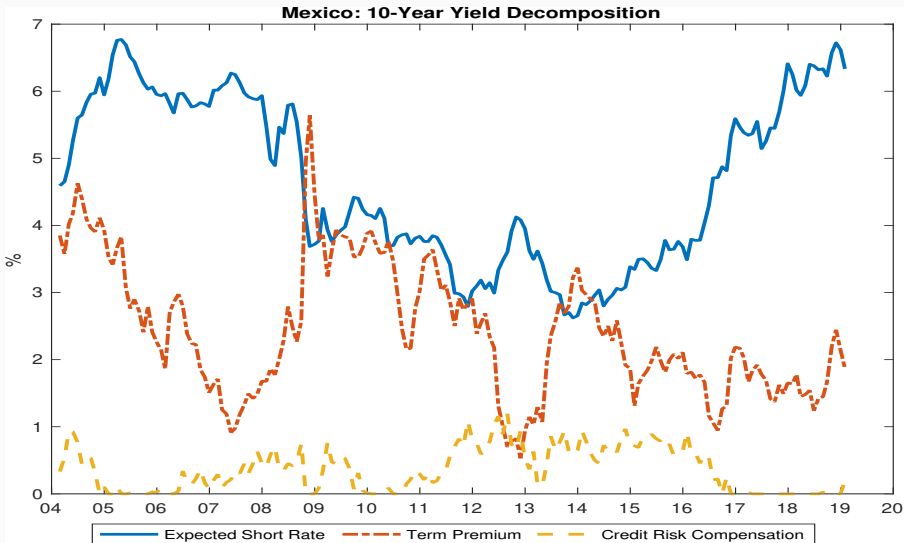


Source: BoC-BoE Sovereign Default Database.

Proposed EM Yield Curve Decomposition

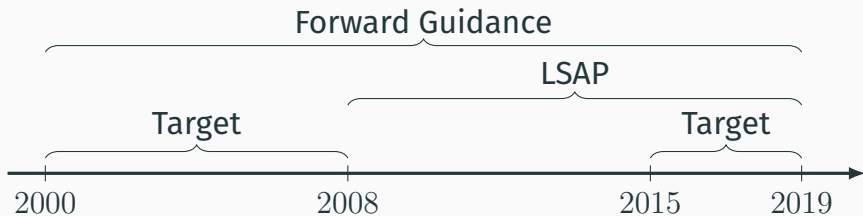


EM Yield Curve Decomposition



U.S. Monetary Policy Surprises

Asset price changes in 2-hour windows around FOMC meetings



U.S. Monetary Policy Spillovers

1. EM yields' response is **economically significant**, yet **delayed**
 - Response in EM lasts longer than in U.S.
2. **All three** components react to U.S. monetary policy
 - EM central banks expected to follow Fed's monetary stance
 - Similar effects on EM term premia than on U.S. term premium
 - Fiscal implications in EM of U.S. monetary policy
3. Unconventional policies **limit** EM monetary autonomy along yield curve
 - Global financial cycle more relevant at the long end