

Term Premium Spillover from the US to Indian Markets

The Reserve Bank of India today placed on its website a Working Paper titled "Term Premium Spillover from the US to Indian Markets" under the Reserve Bank of India Working Paper Series. The Paper is authored by Archana Dilip.

The paper estimates and analyses term premium in India and makes an assessment of interconnectedness and transmission of shocks from the US term structure of sovereign bond yields to that of India. The term premium is estimated by decomposing the yield into two components - risk-neutral rate which reflects

expectations of future short-term rates; and term premium which captures the investors' expectations of future central bank policy, inflation and growth shocks. The paper identifies inflation volatility and monetary policy uncertainty as the two important factors influencing term premium in India. Further, empirical findings indicate that the spillovers between the US treasury yields and government security yields in India have increased during the sample period from April, 2009 to April, 2019. The paper finds stronger spillover with increased financial integration and volatile bond markets. The paper concludes that for the long-term yields, the term premium channel is a stronger transmission channel as compared with the risk-neutral rates channel.