

# Informed and Strategic Order Flow in the Bond Markets

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## Abstract

We study the role played by private and public information in the process of price formation in the U.S. Treasury bond market. To guide our analysis, we develop a parsimonious model of speculative trading in the presence of two realistic market frictions—information heterogeneity and imperfect competition among informed traders—and a public signal. We test its equilibrium implications by analyzing the response of two-year, five-year, and ten-year U.S. bond yields to order flow and real-time U.S. macroeconomic news. We find strong evidence of informational effects in the U.S. Treasury bond market: unanticipated order flow has a significant and permanent impact on daily bond yield changes during both announcement and nonannouncement days. Our analysis further shows that, consistent with our stylized model, the contemporaneous correlation between order flow and yield changes is higher when the dispersion of beliefs among market participants is high and public announcements are noisy.

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