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Macroeconomic uncertainty and credit default swap spreads

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Abstract

This article empirically investigates the impact of macroeconomic uncertainty on the spreads of individual firms' Credit Default Swaps (CDSs). While the existing literature acknowledges the importance of the levels of macroeconomic factors in determining CDS spreads, we find that the second moments of these factors–macroeconomic uncertainty–have significant explanatory power over and above that of traditional macroeconomic factors such as the risk-free rate and the Treasury term spread.

Notes

[1] Tang and Yan (2006, 2008b) model firms' default risk as depending on (among other factors) the volatility of aggregate economic growth. However, their model contains a fixed level of volatility, while we focus upon the variations in macroeconomic volatility as a factor influencing CDS spreads.
