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An exploratory inquiry into the impact of budget deficits on the nominal interest rate yield on Moody's Aaa-rated corporate bonds, 1973–2012

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Abstract

This exploratory empirical article provides recent evidence on the impact of the US federal budget deficit on the nominal interest rate yield on Moody's Aaa-rated long-term corporate bonds. The study is couched within a loanable funds model that includes an ex ante real short-term real interest rate yield, the monetary base, expected inflation and the change in per capita real GDP. Using data for the period 1973–2012, which time frame includes 'quantitative easing' monetary policies in the US, autoregressive two-stage least squares estimation reveals the preliminary finding that the federal budget deficit, expressed as a per cent of GDP, has exercised a positive and statistically significant impact on the nominal interest rate yield on Moody's Aaa-

rated long-term corporate bonds, even after allowing for ‘quantifying easing’ and other factors.

Keywords:

nominal interest rate yield | Moody's Aaa-rated corporate bonds | federal budget deficits | quantitative easing

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