

Accepted Manuscript

Price discovery in euro area sovereign credit markets and the ban on naked CDS

Jacob Gyntelberg, Peter Hördahl, Kristyna Ters, Jörg Urban

PII: S0378-4266(18)30175-4
DOI: <https://doi.org/10.1016/j.jbankfin.2018.08.008>
Reference: JBF 5402



To appear in: *Journal of Banking and Finance*

Received date: 25 May 2016
Revised date: 22 June 2018
Accepted date: 14 August 2018

Please cite this article as: Jacob Gyntelberg, Peter Hördahl, Kristyna Ters, Jörg Urban, Price discovery in euro area sovereign credit markets and the ban on naked CDS, *Journal of Banking and Finance* (2018), doi: <https://doi.org/10.1016/j.jbankfin.2018.08.008>

This is a PDF file of an unedited manuscript that has been accepted for publication. As a service to our customers we are providing this early version of the manuscript. The manuscript will undergo copyediting, typesetting, and review of the resulting proof before it is published in its final form. Please note that during the production process errors may be discovered which could affect the content, and all legal disclaimers that apply to the journal pertain.

Price discovery in euro area sovereign credit markets and the ban on naked CDS [☆]

Jacob Gyntelberg

Nordea Bank, Copenhagen, Denmark.

Peter Hördahl¹

Bank for International Settlements, Hong Kong.

Kristyna Ters

University of Basel, Basel, Switzerland.

Jörg Urban

University of Basel, Basel, Switzerland.

Abstract

The sovereign debt crisis in the euro area saw credit spreads on sovereign bonds and credit default swaps (CDS) surge for a number of member states. The rise in sovereign yields was accompanied by a significant increase in sovereign CDS market activity. This pattern raised concerns that destabilising speculation via outright short-selling of CDS (so-called ‘naked CDS’) was behind the increase in bond yields. In response policy-makers introduced a ban on naked CDS trading. We investigate the effect of the ban on the price discovery process of sovereign credit risk, contrasting results for the post-ban period with those obtained prior to the ban. We use intraday data on sovereign CDS and bonds across a number of euro area countries. Our first main finding is that the CDS market dominates the bond market in terms of price discovery. That is, CDS premia in most cases adjust quicker to reflect new information than bond spreads. This result holds also when taking into account transaction costs. Our second main finding is that the ban on short-selling did not alter price discovery dynamics or reduce the efficiency of the market. Finally, we find that prior to the ban, CDS spreads were persistently higher than bond credit spreads, even after controlling for transaction costs. This points to the presence of market frictions that limit the ability of arbitrage forces to fully close pricing gaps between the two markets. However, these pricing discrepancies were in many cases largely eliminated following the introduction of the ban.

Keywords: Sovereign credit risk, credit default swaps, price discovery, intraday data.

JEL: G12, G14, and G15.

Download English Version:

<https://daneshyari.com/en/article/10147137>

Download Persian Version:

<https://daneshyari.com/article/10147137>

[Daneshyari.com](https://daneshyari.com)