

I DOUN KUO

Tunghai University, Taiwan

IRRATIONALITY AND TERM STRUCTURE ANOMALY

Abstract:

Campbell and Shiller (1991) find the presence of term structure anomaly, in which the slope of the term structure predicts inconsistently to the change in yield of longer-term bonds over the life of shorter-term bonds during 1952-1987. Focusing on the post Campbell and Shiller period, our findings suggest that the anomaly is not only attributed to term premia, but also relates to expectation errors. We found that macroeconomic surprises and irrationality from investors' behavior are important determinants of expectation errors. These factors are capable of explaining the rejection of the expectation hypothesis and the US term structure anomaly in long-term securities.

Keywords:

Irrationality; Term structure anomaly; Expectation hypothesis; Term structure of interest rates

JEL Classification: E43, G12, G14