Applied Economics, , .

The impact of (un)conventional monetary policy on the sovereign-bank nexus in the euro area

P. Claeys; M. Gómez I Puig; S. Sosvilla Rivero

Abstract-

Sovereign debt holdings by banks and large-scale asset purchase programmes influence the transmission of risk between the banking sector and the government. This study examines their impact in the euro area from February 2005 to December 2023. Using a standard measure of dynamic net directional connectedness between sovereign and bank risk, we assess how sovereign debt holdings by banks and large-scale asset purchase programmes by the ECB affect the transmission of risk, while controlling for the conventional monetary policy stance and other standard macro-financial variables. Our results show that risk transmission varies over time but generally flows from banks to sovereigns, except during periods of economic distress. Bank holdings of sovereign debt emerge as the primary channel for transmitting risk to the sovereign sector, with conventional monetary policy also playing a significant role. By contrast, the ECB’s large-scale asset purchase programmes have had a neutral effect on this transmission.

Index Terms- Bank risk; sovereign risk; Sovereign-bank nexus; euro area