Central Clearing: Effects on Corporate Credit Risk

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Abstract

In this paper we try to find the main drivers of corporate credit risk measured by the credit default swaps (CDS) spreads. The data sample between 2010 and 2015 enables to analyze the effects that trading CDS over central counterparty clearing houses (CCPs), which were recently implemented in March 3013, versus the over-the-counter (OTC) alternative have on the CDS spreads, i.e. credit risk. The analysis also compares both trading places' efficiency. The CDS data consist of US corporations listed in the S& P 500. Main drivers of the CDS spreads are shown to be more firm-specific factors than global macroeconomic drivers. Equity returns, implied equity volatility and its jump components, where the two latter are constructed from high-frequency data, are shown to have strong deterministic power. CCPs reduce counterparty risk, i.e. the risk that the seller of a CDS protection defaults and therefore improves the contracts quality by applying effective risk-management, but strongly diminishes the market's efficiency in contrast to trading OTC.

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