

The determinants of credit default swap rates: an explanatory study

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Abstract

The aim of this paper is to explain empirically the determinants of credit default swap rates using a linear regression. We document that the majority of variables, detected from credit risk pricing theories, explain more than 60% of the total level of credit default swap rates. These theoretical variables are credit rating, maturity, risk-free interest rate, slope of the yield curve and volatility level of equities. The estimated coefficients for the majority of these variables are consistent with theory and they are significant both statistically and economically. We conclude that credit rating is the most influential determinant of credit default swap rates.

Key words: credit derivatives; credit risk; credit default swap; credit rating; market variables.

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