# What is a Credit Default Swap?

*A credit default swap is an agreement between two parties that works like a side bet on a football game. Swap sellers promise swap buyers a big payment if a company's bonds or loans default. In return for the promise they get quarterly payments. Neither needs to hold the underlying debt when entering into a swap.*

Scott Pollack

**Widgets "R" Us Corp.**

**Borrows money from banks or issues bonds to finance operations.**

## Credit Default Swap Seller

**Promises to pay swap buyer a set amount if Widgets "R" Us defaults, often $10 million**

- Receives annual payments from swap buyer in return for "insurance"
- Can include banks, insurance companies, hedge funds or others

## Credit Default Swap Buyer

**Promises quarterly payments to swap seller**

- Receives promise of large payout if bond defaults
- Can include banks, insurance companies, hedge funds or others
- If Widget's financial fortunes turn sour, the swap becomes more valuable. A swap holder can resell it and get high payments in return