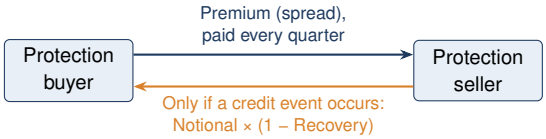
A gentle introduction to CDS indices

Understanding iTraxx Europe Main 5Y

SELWOOD ASSET MANAGEMENT

1. What is a CDS? An insurance policy on a company

A **credit default swap (CDS)** works like an insurance contract on the debt of a company (the *reference entity*). The **protection buyer** pays a regular premium, the *spread*, quoted in basis points per year of the insured amount (the *notional*). The **protection seller** collects this premium and, in exchange, compensates the buyer if the company suffers a *credit event* (bankruptcy, failure to pay, or, in some cases, a restructuring of its debt).



The analogy has one limit: the buyer does not need to own the company's bonds. Selling protection is therefore economically close to **owning a corporate bond without having to fund it**: the seller earns a spread and bears the credit risk. The compensation is set by an industry-wide *auction* that fixes the recovery value of the defaulted debt, so all contracts settle at the same price.

2. From one company to 125: the CDS index

A **CDS index** bundles many single-name CDS into one standard contract. **iTraxx Europe Main** ("iTraxx Main") references **125 European investment-grade companies**, each with the **same weight of 0.8%**. In a single trade, an investor gets a diversified exposure to European corporate credit. If one company defaults, it is settled and removed; the index carries on with 124 names and a notional reduced by 0.8%.

iTraxx Main at a glance

Constituents	125 European IG companies
Weighting	Equal, 0.8% per name
Benchmark tenor	5 years
Fixed coupon	100bp per year, paid quarterly
New series	Every 20 March and 20 September
Payment upon default	$0.8\% \times N \times (1 - RR)$ per name

N: notional of the trade; *RR*: recovery rate set by the auction.

The roll. Every six months a new index *series* is launched with a refreshed list of names and a maturity extended by six months. The newest series (*on-the-run*) is where liquidity concentrates, so investors typically *roll* their position into it.

Because credit curves usually slope upwards, moving to a six-month-longer maturity tends to earn extra spread: since 2004, 38 of the 44 rolls (86%) delivered a positive pick-up (about +4 to +5bp on average), and only one (March 2009) was clearly negative.

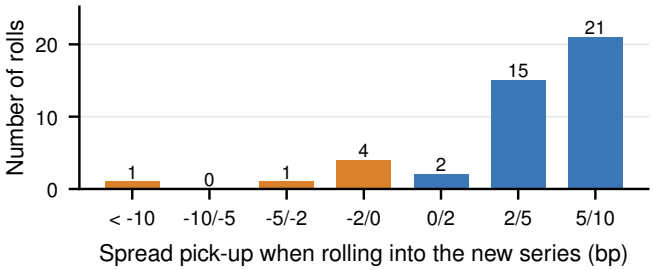


Figure 1: Spread pick-up at each iTraxx Main roll since 2004.

Source: Bloomberg, calculations. Data as of March 2026.

Composition rules. At each roll, the index administrator (S&P Dow Jones Indices) rebuilds the list with transparent, published rules:

- companies incorporated in the EU, EFTA or UK, with at least €100m of publicly traded debt;
- **investment grade** on the *lowest* of their Moody's, S&P and Fitch ratings, and not on negative outlook at BBB–;
- ranked by **CDS trading volumes** (DTCC data): the most traded names are selected;
- within **fixed sector ranges**, with exactly 30 financials.

Names that were downgraded, merged or became less traded are replaced. Changes are limited: at the September 2026 roll, only **4 of the 125 names** changed.

A stable profile over time. Because every name must be investment grade at each roll and sector weights are kept within set ranges, the index offers a **consistent exposure**: an investor rolling the index holds broadly the same type of risk from one series to the next.

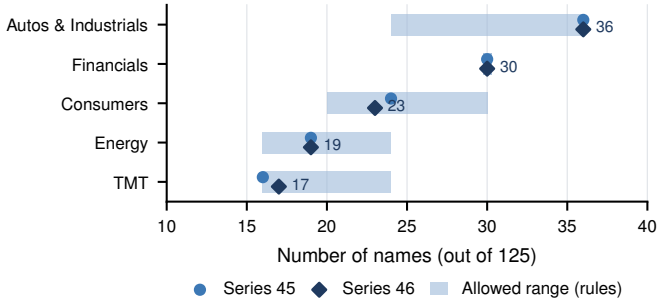


Figure 2: iTraxx Main sector composition vs. the ranges allowed by the rules.

Source: S&P Dow Jones Indices: iTraxx Europe rulebook, Series 45 and 46 lists.

Figure 3: iTraxx Main 5Y spread (on-the-run, mid), October 2005 – October 2026.

Source: J.P. Morgan, Selwood AM France. Mean 77bp, median 69bp; all-time high of 215bp on 5 December 2008.

3. Liquidity: the most traded credit instrument in Europe

iTraxx Main is the reference tool for professionals to buy or hedge European credit risk. Average daily volumes rose from about **€13bn in 2025 to €22bn in Q1 2026**, far more than any single corporate bond. Its US counterpart, CDX IG, is equally liquid: together they are the most traded credit instruments in the world.

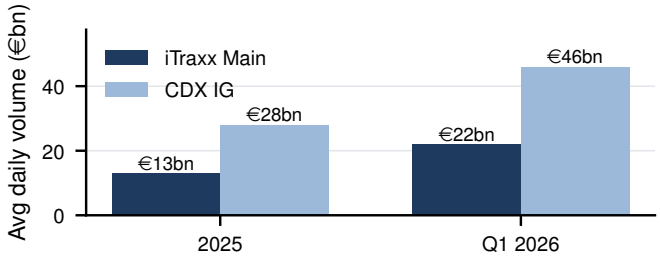


Figure 4: Average daily traded volumes.

Source: Bloomberg. Data as of 31 March 2026.

Bid-ask spreads are tiny. In normal markets, the difference between the buying and selling price is around **0.2bp** of spread, i.e. less than €1,000 on a €10m trade. Liquidity also held up in stress: in March 2020 (Covid), iTraxx Main bid-ask widened to about 3bp (roughly 0.15% of notional), while the largest US investment-grade corporate bond ETF (LQD) closed at a **5% discount** to the value of its bonds (12 March 2020).

4. How it is traded: a fully standardised contract

- **Standard terms.** Every contract shares the same series, maturity dates, fixed coupon (100bp) and payment dates (20 March, June, September, December). Only the notional, the direction and the price are negotiated.
- **Upfront payment.** Because the coupon is fixed, the difference with the market spread is settled at inception. Example: with the index at 60bp, the protection seller pays about $(100-60)\,\text{bp} \times 4.5 \approx 1.8\%$ upfront, then receives 100bp a year: economically the same as receiving 60bp a year (like buying a bond above par).
- **Documentation and defaults.** Contracts follow ISDA standard documentation. A *Determinations Committee* rules on whether a credit event occurred, and an auction sets the payout for everyone.
- **Central clearing.** Trades are cleared through a clearing house (ICE Clear Credit, LCH CDSClear), which stands between buyer and seller. In the EU, clearing of iTraxx Main 5Y is mandatory for most financial counterparties (EMIR). Gains and losses are exchanged daily (variation margin), plus an initial margin.
- **Unfunded.** No cash is needed beyond margins: the investor's cash can stay invested in short-term, high-quality bonds.
- **Easy exit.** A position is closed by an opposite trade with any dealer; the clearing house nets the two.

5. Defaults: rare, and filtered out by the roll

Since the launch of iTraxx Main in 2004, only **3 credit events** have occurred among its constituents, and **none in the on-the-run series**. Over more than twenty years, including the 2008 crisis and the euro crisis, an investor rolling into each new series has never had to pay out on a default. The roll acts as a regular quality filter: every six months, only companies that are still investment grade are kept.

6. Basket quality, and how it differs from the US index

iTraxx Main is **100% investment grade at each roll**, equally weighted and diversified across sectors, with no name above 0.8%. Its US counterpart, **CDX North America IG**, looks similar (125 IG names, 100bp coupon, same roll calendar) but holds a different economy:

- **Financials.** iTraxx Main always holds 30 financials, including Europe's largest banks. CDX IG excludes swap dealers by rule, so it holds none of the large US banks; its 14 financials are mostly insurers and card issuers.
- **Hyperscalers.** CDX IG has become a growing proxy for US big tech: Alphabet, Meta and Microsoft joined in March 2026, and Nvidia in September 2026, alongside names such as Amazon and Oracle. In iTraxx Main, the TMT sector is mostly **telecoms and media** (Deutsche Telekom, Orange, Vodafone, Publicis…); STMicroelectronics and Ericsson are its only technology hardware names. The credit risk linked to AI-related investment and its financing is therefore mainly a CDX IG story.
- **Contract terms.** iTraxx Main counts debt restructuring as a credit event; CDX IG does not.

	Large technology names
iTraxx Main (S46)	STMicroelectronics, Ericsson
CDX IG (S47)	Alphabet, Amazon, Meta, Microsoft, Nvidia, Oracle, IBM, Intel, AMD, Broadcom, Dell, HP…

Source: S&P Dow Jones Indices (index lists and roll announcements, 2026).

Key takeaways

- One trade gives an equally weighted exposure to 125 European investment-grade companies.
- Selling protection is economically close to owning corporate bonds, without funding them.
- The semi-annual roll keeps the basket investment grade and its profile stable over time.
- It is the most liquid credit instrument in Europe, including in stressed markets.
- Standard terms, central clearing and daily margining keep counterparty risk low.
- Unlike CDX IG, iTraxx Main has almost no exposure to US-style big tech and hyperscalers.