Derivatives based on a CMS spread are therefore traded by parties who wish to take a view on future relative changes in different parts of the yield curve.

Who Uses a Constant Maturity Swap (CMS) and why?

The Constant Maturity Swap is employed by two types of users: 1. Investors or institutions attempting to hedge or exploit the yield curve while seeking the flexibility that the swap will provide and 2. Investors or institutions seeking to maintain a constant liability duration or constant asset.

The advantages of a constant maturity swap are:

1. It maintains a constant duration
2. The user can determine “constant maturity” as any point on the yield curve
3. It can be booked the same way as an interest rate swap

The disadvantages of a constant maturity swap are:

1. It requires documentation from the International Swaps and Derivatives Association (ISDA)
2. It has the potential for unlimited losses