

Title: Credit Default Swaps and GME Shorting

Author: TheLunarnautics

Created 2021-08-20 14:13:03 UTC

Permalink: /r/Autisticats/comments/p860y3/credit_default_swaps_and_gme_shorting/

Url: /r/Superstonk/comments/p7ehzk/theory_tying_credit_default_swaps_with_gme/

Linked Post Content:

So after re-reading the big short again, I think it finally clicked. Naked shorting may not be the big issue here. Naked shorting may just be a small tool used to support a much bigger derivative problem, synthetic credit default swaps.

How bad can it be that the NSCC itself called Vlad and cut a deal to turn off buys. Other short squeezes never had that type of manipulation before. Even if Shitadel and friends were overextended, I don't think it makes sense to risk the entire market over a few bad eggs to tlto blatantly openly manipulate to the point that even the most unlearned of congressman would be able to call out.

The report on credit derivatives just came out and many people will notice that by far the number one derivative traded between big banks are credit default swaps.

Before I get into the theory and my request to look into this more, let me introduce Credit default swaps in ape language.

From investopedia:

"A credit default swap (CDS) is a financial [derivative](<https://www.investopedia.com/terms/d/derivative.asp>) or contract that allows an investor to "swap" or offset his or her [credit risk](<https://www.investopedia.com/terms/c/creditrisk.asp>) with that of another investor. For example, if a lender is worried that a borrower is going to [default](<https://www.investopedia.com/terms/d/default2.asp>) on a loan, the lender could use a CDS to offset or swap that risk. To swap the risk of default, the lender buys a CDS from another investor who agrees to reimburse the lender in the case the borrower defaults. Most CDS contracts are maintained via an ongoing [premium](<https://www.investopedia.com/terms/p/premium.asp>) payment similar to the regular premiums due on an insurance policy. "

OKAY GREAT NOW WHAT DOES THAT FUCKING MEAN IN NORMAL VOCABULARY

A credit default swap is an insurance policy on the debt of others that you own. Normally it is used as a hedge against lending money to corporations AKA corporate bonds (as well as other types of bonds)

For example:

If Gamestop needs, oh I don't know, \$216 million in funding (total long term debt at the end of 2020), it can get its money from a big bank, Goldman Sachs for example. This then becomes a significant liability on the banks books. To offset this risk, the bank can then purchase a credit default swap from another bank lets say Credit Suisse, which will then ****act as insurance**** against Gamestop defaulting on its newly issued bonds

So GS buys \$213M in GME corporate bonds (effectively lending money to GME). GS then purchases a CDS from Credit Suisse to insure the \$213M in bonds and pays a premium on this policy (interest) for like \$5M a year for the life of the bond. If GME defaults during the life of the bonds, CS has to pay GS \$213M for the price of the now worthless bonds. If GME doesn't default, GS just paid \$5M a year to CS for 10 years.

****Now here's where it gets slimy and opens up to fraud.****

In the example above, the \$213M in actual debt was insured using the CDS. It was a real CDS.....but it doesnt have to be. A synthetic CDS is a bet on that corporate debt without ever being the lender. Bring in BofA for example.

While GS continues to pay CS year by year for \$5 for GME bond debt, BofA enters the game. BofA doesn't want to actually lend Gamestop money but thinks Gamestop will go bankrupt and default on its debt. It can then go to CS who sold the real CDS to Goldman Sachs and purchase a synthetic CDS using the same underlying (the GME corporate bonds that GS bought). **This effectively means that the CDS no longer is a hedge, but becomes a naked bet, PUTTING BofA SHORT GME. In this example, BofA are betting that GME will go bankrupt, not by shorting its stock, but by betting it will default on its debt.**

Thank you to The Big Short for showing how CDS's can be used as Much larger, repackaged, less regulated short positions on companies.

Now what the hell happens if that debt goes away?..... What if GME pays off its debt early? Who loses?

Anybody who was betting on Gamestop defaulting on the debt loses. The synthetic CDS's that were taken out by BofA on Gamestop's corporate debt would effectively evaporate, meaning that they paid \$5M per CDS contract, per year.

And if you are overleveraged in this larger, more thermonuclear, opaque area of the market by, I don't know 200:1? (looking at you, BofA) You just lost a hell of a lot of money, I'm talking many 10s if not hundreds of billions in unrealized losses and you continue to bleed that \$5million x #contracts per year. Multiply this by 20 or so big banks, all making 50 - 200:1 overleveraged synthetic CDS bets against Gamestop, The money at risk for GME alone could be Trillions of dollars.

Some of the questions I'm looking for.

1. Who would be on the other side of the CDS? Blackrock? Is that why Blackrock put RC into the chairman position, bought 9m shares and let it run? BR did say that they are sitting on more cash then they have in years and have been rapidly buying properties to hedge for inflation.
2. Does the timeline of defaults (Archegos, etc) match with GME financial statements on when they paid off their debt.
3. What the hell does a CDS look like on a balance sheet? Do the runups and debt payoffs correlate with all the big banks starting to lose a bunch of money.
4. Do CDS's just disappear when the underlying gets paid off early? Is it the same for synthetic CDS's
5. How do the quarterly derivative rollover dates affect this (u/Criand)

Unfortunately I'm too busy writing my Ph.D. Dissertation to really dig deep into a lot of this. Hoping some wrinklebrains with a bit more time can help to answer these.

****TLDR:**** Thanks to Burry and Friends, I'm starting to think that naked shorting is only a tool to help push companies to bankruptcy where the real payday is not in the equities market but in the Corporate bond debt credit default swaps. These markets are much less regulated, are worth almost a quadrillion dollars and CDS's can be used effectively as a MASSIVE put on a company while using your smaller fish (Shitadel and friends) to short GME in hopes of making that debt default come true.

I'm starting to believe the DTCC, Citadel, NSCC may not be the big players here and that the massively overleveraged Big banks have been taking out enormous synthetic CDS positions on Gamestop (and other companies in the past) in the hopes that they default on their debt. I need help looking into this. For example, who has owned Gamestop's debt at what time and when? Timeline of the runups with derivatives rollovers, and debt payoffs. (u/Criand) Anything else we can scrape from the ridiculously opaque derivatives market regarding over leveraging and using synthetic CDS's to bet on a company going bankrupt.

Edit: This may be what Burry was saying about corporate bonds. Once again a tool used to hedge risks is being used to make naked bets against companies. (Also edited for clarity and added a few questions at

end)

That is all. Buy and Hodl.■