

---

# CLIENT NOTE

---

## HEALING BONDS: A RESPONSE TO FINANCIAL DISASTERS CAUSED BY COVID-19



### OVERVIEW

So far, COVID-19 has spread to 210 countries and has infected almost 2 million people. As a consequence, nearly 3 billion around the world are living in varying degrees of lockdowns which have been imposed by governments in order to slow the spread of the infection. It has caused a significant disruption in economic activity across the globe. Financial markets, in particular, have experienced surges in volatility that have not been seen since the 2007-09 financial crisis.

*Countries are coming up with innovative financial solutions. Efforts are being made within the capital markets to mitigate the negative health and socio-economic impacts of COVID-19 through the issuance of debt instruments, also known as “Pandemic Bonds.”*

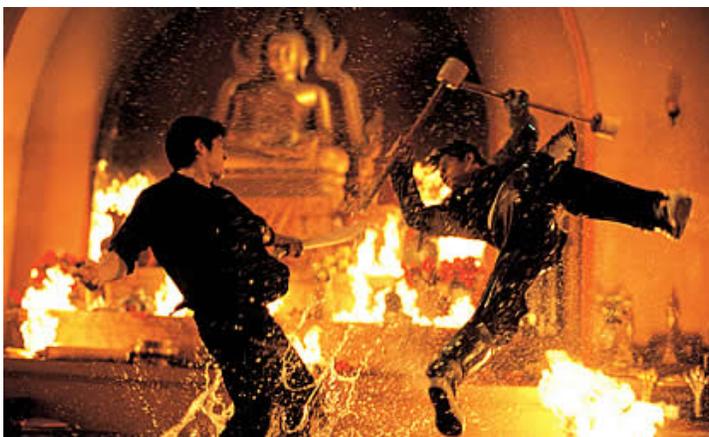
The consequences of COVID-19 are twofold:

- The healthcare infrastructure of the countries with the most cases and casualties are currently overwhelmed. Research by the World Health Organization (WHO) and others have indicated that only 43% of the countries are prepared to respond adequately to the outbreak.
- Social distancing and isolation have halted or slowed major segments of economies around the world. While essential services continue to function, many other activities have ceased to operate or have scaled back significantly, threatening businesses of all sizes, which may face immeasurable losses (financial and human capital) and raise the specter of a recession.<sup>1</sup>

Policymakers have responded by deploying a variety of measures to stabilize financial markets and prevent the real disruption from causing a full-blown financial crisis. **But is this enough to prevent major catastrophe?** The response to the current crisis requires the involvement of a broad range of actors, including governments, central banks and capital markets (companies, investors) to foster the financing of activities that can help to first, mitigate the effects of the pandemic, and secondly, to assist businesses, especially SMEs, that are facing adverse economic impacts. One of the main cures for today's financial system are bonds.

## HOW CAN BONDS HELP FIGHT COVID-19 CONSEQUENCES?

COVID-19 has been causing a significant economic and financial disturbance in emerging markets and developing countries. Therefore, huge financial and economic actors are trying to promote financing activities by involving additional funds, such as [social bonds](#) that will help mitigate the effects of the pandemic in both healthcare and economic sectors. These funds can be directed to, among others, to finance COVID-19 related-healthcare and medical research, medical equipment, as well as specific projects to alleviate unemployment generated by the crisis.



The social bond market is a road through which public and private sectors can access the essential capital required to meet healthcare needs, restore economic stability, and preserve jobs. Through this mechanism, Governments, Central Banks, Supra-governmental bodies and private entities are issuing securities certifying the right of its holder to receive from the issuer(s) (within the term specified therein) the nominal value of the bond and respective interest (if available). Furthermore, through the

---

<sup>1</sup> [https://www.sustainalytics.com/sustainable-finance/2020/04/07/covid-19\\_social\\_bonds/](https://www.sustainalytics.com/sustainable-finance/2020/04/07/covid-19_social_bonds/)

funds involved by the issuance of such bonds, the issuers have their contribution in maintaining the affected business sectors, social and educational sectors, health infrastructures, etc.

According to guidelines published by the [International Finance Corporation](#), social bonds finance projects that directly aim to address or mitigate a specific social issue and/or seek to achieve positive social outcomes and are capable of addressing the issues caused by COVID-19. At the same time, IFC suggests that such social bonds must comply **with the four main components of the [Social Bond Principles](#)**, which are:

1. *Use of Proceeds;*
2. *Process for Project Evaluation and Selection;*
3. *Management of Proceeds;*
4. *Reporting.*

According to IFC Social Bond Principles, the legal documentation (such as prospectus) for the bond shall involve information regarding the utilization of the proceeds of the so-called "**Pandemic Bond Project**." Additionally, the issuer shall provide a high level of transparency, as well as applicable information to the potential holder about the social objectives of the bond project and process by which the issuer determines how the projects fit within the eligible bonds' project objectives. The net proceeds of the bonds (or an amount equal to these net proceeds) should be credited to a sub-account, moved to a sub-portfolio, or otherwise tracked by the issuer in an appropriate manner. The issuer's lending and investment operations within the Pandemic Bond Project shall also be confirmed by the formal internal process of the issuer. Issuers should make and keep available up to date information on the use of proceeds to be renewed until the full allocation of the whole amount. The reporting shall also include information regarding the aim for which the Pandemic Bond Project proceeds have been allocated, as well as the allocated amount, a brief description of the aim, and the expected impact.

## EXPERIENCE IN DIFFERENT STATES AND ORGANIZATIONS

### *China*



China, the first country to be hit by the virus, has become the first country to bring the outbreak under control. China's economy has so far suffered the most significant slowdown as the outbreak drove strict quarantine orders, factory shutdowns, and travel bans. Now, China seems to be doing everything it can to stabilize their financial markets. The first step towards this was allowing private firms to issue bonds at a lower interest rate. Cheap bonds, though unconventional, have become an effective method to fund the efforts against the epidemic and kickstart the economy. However, most companies issuing these bonds are also using

them to pay back their existing debt. How? Regulators have encouraged the sales of virus-linked bonds by cutting the approval process from weeks to days while urging state-backed banks to buy them. To qualify for the program, companies must commit to spending at least **10 %** of the proceeds on measures to combat the epidemic. State-owned lenders have helped make the cost of borrowing cheaper for those issuing such bonds by buying up large stakes at low-interest rates. The activity allows China's government to issue liquidity to companies on the verge of default more directly.

Accordingly, companies across China are taking advantage of the coronavirus outbreak to shore up their balance sheets, as Beijing urges them to issue cheap bonds to support the world's second largest economy. More than **25** Chinese businesses, ranging from airlines to drug distributors, have already raised **\$3.4 billion** by selling "virus control" bonds since the start of February. Another 20 have announced plans to raise money in the upcoming weeks, as the outbreak shows few signs of tapering.

The analysis reveals that only the third of roughly **14 billion yuan (\$2.01 billion)** being raised under a new fast-track regulatory process for "virus prevention and control bonds" will be used for the cause.

Accordingly, the Chinese model of encouragement of bond issuance has become one of the most effective tools against financial catastrophe. The secret is that with a little maneuver, the Chinese Government succeeded in both credit easing of the issuing companies, and using money raised in the directions that their Financial market needs.

### **Indonesia**

The Indonesian government plans to raise nearly **\$27.21 billion** in "pandemic bonds."

Within the framework of this plan, on **April 6<sup>th</sup>, 2020**, Indonesia raised **\$4.3 billion** to help the government in the battle against coronavirus<sup>2</sup>. According to the details of the deal, Indonesia sold "pandemic bonds" in three tranches:

1. maturities of **10.5 years**, due on **October 15<sup>th</sup>, 2020**, total amount **\$1.65 billion** with an annual yield of **3.9 %**;
2. maturities of **30.5 years**, due on **October 15<sup>th</sup>, 2050**, total amount **\$1.65 billion** with an annual yield of **4.25 %**; and
3. maturities of **50 years**, due on **April 15<sup>th</sup>, 2070**, total worth **\$1 billion** with an annual yield of **4.5%**.



By this issuance, Indonesia has become the first Asian nation to issue 50-year dollar-denominated bonds and the funds raised by this issuance will be used by the Indonesian government to help finance a fiscal stimulus to counter the impact of the coronavirus pandemic on the Indonesian economy and financial system<sup>3</sup>.

<sup>2</sup> <https://www.thejakartapost.com/news/2020/04/07/indonesia-sells-asias-first-50-year-dollar-bond-to-fight-pandemic.html>

<sup>3</sup> <https://jakartaglobe.id/business/indonesia-raises-43b-from-pandemic-bonds>

## **Supra-Governmental Entities**

**Council of Europe Development Bank (CEB):** On April 2nd, 2020, CEB issued a €1 billion worth COVID-19 response called "Social Inclusion Bonds." According to the final details of the issuance, CEB issued bonds with 7-year maturity (April 9th, 2027) and a -0,000 % coupon rate. Over 60 accounts participated in the transaction with broad diversification among investor geographies and types, such as investors (Banks & Bank Treasuries, Asset Managers, CB/OIs & SSAs and Pension & Insurance Funds) based in France (24%), Asia (16%), the UK (14%), and Germany/Austria/Switzerland (11%)<sup>4</sup>.

The funding is planned to be used to support CEB member countries in mitigating the social and economic impact of the ongoing COVID-19 crisis<sup>5</sup>. In line with the "Social Inclusion Bond" framework, the proceeds raised will also finance new or existing social projects which support micro, small, and medium-sized enterprises (MSMEs) in order to create and preserve jobs.

**Nordic Investment Bank (NIB):** As a response to the worldwide spread of COVID-19, NIB, an international financial institution, issued a "Response Bond" for its member countries (Denmark, Finland, Iceland, Norway, Sweden, Estonia, Latvia, and Lithuania). According to the "Response Bonds" framework, the NIB will finance eligible projects that aim to alleviate the social and economic consequences of the pandemic in the Bank's member countries and eventually support the recovery process of the states. Loans financed by the NIB Response Bonds should support the provision of products and services contributing to health conditions and maintaining a living standard for groups challenged by COVID-19. In particular, the proceeds of the NIB Response Bonds will be used to finance eligible projects in **the public sector**, such as the financing of temporary and permanent measures to increase capacity in healthcare services, unemployment, sickness, child and elderly care benefits, and of government or government-related institutions' expenditures aimed at supporting member country companies in temporary need of subsidization due to supply or demand side disruptions in their operations in order to protect viable companies. As well as financing **the financial sector and real economy sector**: distribution of funding for small, medium-sized, mid-cap businesses negatively affected by the pandemic and providing recourses to medical equipment and healthcare sector large companies facing an increasing demand for equipment or services related to the pandemic<sup>6</sup>.

**International Financial Corporation (IFC), World Bank Group:** To involve additional funds and ensure a rapid source of finances and liquidity, the IFC issued two social bonds<sup>7</sup>. One of them is targeting companies in emerging markets involved in the production and delivery of medical equipment and pharmaceuticals, and the other is supporting the private companies and employees affected by the current economic downfall<sup>8</sup>.

**European Union (EU):** Along with others, the EU, in particular the **European Investment Bank (EIB)**, is considering the matter of issuing "pandemic bonds." Even though such plans are still at the level of discussion, some member states (Spain, Italy, France, Belgium, Luxembourg, Ireland, Portugal,

---

<sup>4</sup> [https://coebank.org/documents/936/Final\\_Press\\_Release\\_-\\_CEB\\_EUR\\_1bn\\_7yr\\_Social\\_Inclusion\\_Bond\\_bHXaqYz.pdf](https://coebank.org/documents/936/Final_Press_Release_-_CEB_EUR_1bn_7yr_Social_Inclusion_Bond_bHXaqYz.pdf)

<sup>5</sup> <https://coebank.org/en/news-and-publications/news/ceb-issues-social-inclusion-bond-response-covid-19-pandemic/>

<sup>6</sup> [https://www.nib.int/filebank/a/1585555664/59aa748f8c25ba29e2b145db6785d08e/10201NIB\\_Response\\_Bond\\_Framework\\_30\\_March.pdf](https://www.nib.int/filebank/a/1585555664/59aa748f8c25ba29e2b145db6785d08e/10201NIB_Response_Bond_Framework_30_March.pdf)

<sup>7</sup> <https://www.icmagroup.org/Regulatory-Policy-and-Market-Practice/covid-19-market-updates/covid-19-market-updates-sustainable-finance/>

<sup>8</sup> It was issued on March 11th, 2020, with a total worth of \$1 billion and a 3-year maturity date.

**Greece, and Slovenia)** find that the EIB shall implement joint debt instruments, such as bonds, to assist the member states of the EU in the fight against the economic consequences caused by COVID-19<sup>9</sup>.

## CONCLUSION

In conclusion, "pandemic bonds" can be solutions for governments and other institutions in the fight against the devastating consequences caused by COVID-19. They will help involve essential additional funds to aid affected sectors of economy and healthcare. It is a rare opportunity for States to use the involved funds today and repay debt in the future. Although, it is still a debt burden for a State. However, the current situation requires such sacrifices, to at least try to prevent an irreversible deterioration of the pre-epidemic situation. It is not the first time in history that bonds are used to heal the financial system. Throughout World Wars I and II, civilians supported the US economy in a multitude of ways. From 1941-45, Americans bought more than **\$185 billion** in "**war bonds**." These bonds were a way for citizens not on active duty to express their patriotism and have their contribution.

Will this work today? We can see some parallels with today's reality. Today's war is against a disease, which unfortunately, infects a world economy. Nowadays, **we, the World's Citizens, are willing to invest in the healing process not only because we are patriots, but also because we are all in the same boat.**

**NOTE: This material is for general information only and is not intended to provide legal advice.**

**Lilit Hakobyan,**  
Junior Associate

[lhakopyan@tk.partners](mailto:lhakopyan@tk.partners)



**Gohar Tovmasyan,**  
Junior Associate

[gtovmasyan@tk.partners](mailto:gtovmasyan@tk.partners)



---

<sup>9</sup> <https://www.euronews.com/2020/03/26/what-are-corona-bonds-and-how-can-they-help-revive-the-eu-s-economy>