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CORPORATE BOND ISSUANCE DURING THE COVID-19 PANDEMIC: A COMPARISON WITH THE GLOBAL FINANCIAL CRISIS

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ABSTRACT

In the early stages of the global financial crisis and the COVID-19 crisis, bond issuance by non-financial and non-bank financial corporations in the developed economies hit record levels. However, the underlying reasons for this are different: during the global financial crisis, bond issuances were made to replace bank loans, whereas during the COVID-19 pandemic they have been made to address a liquidity problem caused by the restrictive measures adopted to combat the virus. There are also significant differences between the issuances made during the two crises; notably the considerable decline in financing costs on account of lower market interest rates, which may partly explain the longer average duration of bonds, and the greater use of funds to refinance existing liabilities. The issuance of high-yield bonds has also risen and the sectoral breakdown of the issuers has changed.

Keywords: debt issuance, corporate bonds, global financial crisis, COVID-19, pandemic.

JEL classification: G01, G23, G32.

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Introduction

In the months following the onset of the last two global economic and financial crises – the global financial crisis (GFC) of 2008 and the COVID-19 crisis of 2020 – corporate bond issuance[1] in the developed economies[2] surged, with gross issuance volumes substantially higher than in the pre-crisis periods. Thus, corporate bond issuance totalled $1,112 billion in 2009 Q1 and $1,518 billion in 2020 Q2, much higher than the average issuance ($646 billion and $850 billion) in previous years (see Chart 1). Issuance levels in 2007–2008 were very low compared with previous quarters, but this was not the case in the pre-pandemic period. The reason for this is the different nature of the two crises: while the GFC was gradually brewing in previous years owing to the build-up of financial stress, which was reflected in debt issuance, COVID-19 is a health crisis that had a much more sudden impact on the economy.

Accordingly, the reasons for these sharp increases in corporate bond issuance are different in the two episodes. In the GFC, the increase was driven by the need to replace financing that was hitherto obtained from banks. The serious difficulties facing financial institutions led to a tightening of their credit standards and a decline in the volume of their lending to customers.[3] By contrast, during the pandemic, companies have faced liquidity problems stemming from their lower income due to lockdown measures and restrictions, in a setting in which market funding was more accessible. This meant that they were able to use all available channels, including bank loans, public support measures and debt issuance, in the case of this latter option with the help of central banks' asset purchase programmes.[4]

This article aims to describe and compare both episodes of significant increases in corporate bond issuance in the developed economies, specifically in the United

1 By non-financial corporations and non-bank financial corporations (pension funds, insurers, public agencies, etc.). Bonds issued by governments, supranational entities and banks are therefore excluded.

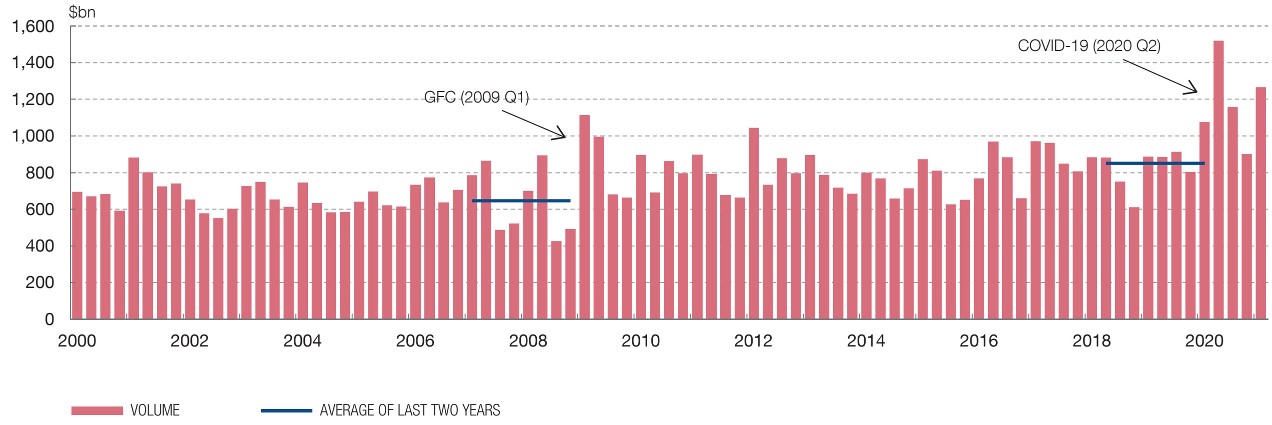
2 The United States, euro area, United Kingdom, Japan, Australia, Canada, Denmark, Iceland, New Zealand, Norway, Sweden and Switzerland.

3 See Kwan (2010), De Fiore and Uhlig (2015) and Hogan (2019).

4 See Álvarez et al. (2021). The main examples are the measures taken in March 2020 by the US Federal Reserve (with several asset purchase programmes and facilities to sustain the flow of credit), the European Central Bank (ECB) (which announced the pandemic emergency purchase programme (PEPP) to purchase public and private assets during the pandemic), and the Bank of England (which expanded its asset purchase programme).

Chart 1
CORPORATE BOND ISSUANCE IN ADVANCED ECONOMIES

QUARTERLY GROSS ISSUANCE



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SOURCE: Dealogic.

States and the euro area. In particular, it analyses the differences and similarities in terms of the cost and duration of debt and its credit quality, the sectoral breakdown of the issuers and the use made of the funds received.[5]

Comparison between the COVID-19 crisis and the global financial crisis

Issuance volume: general overview

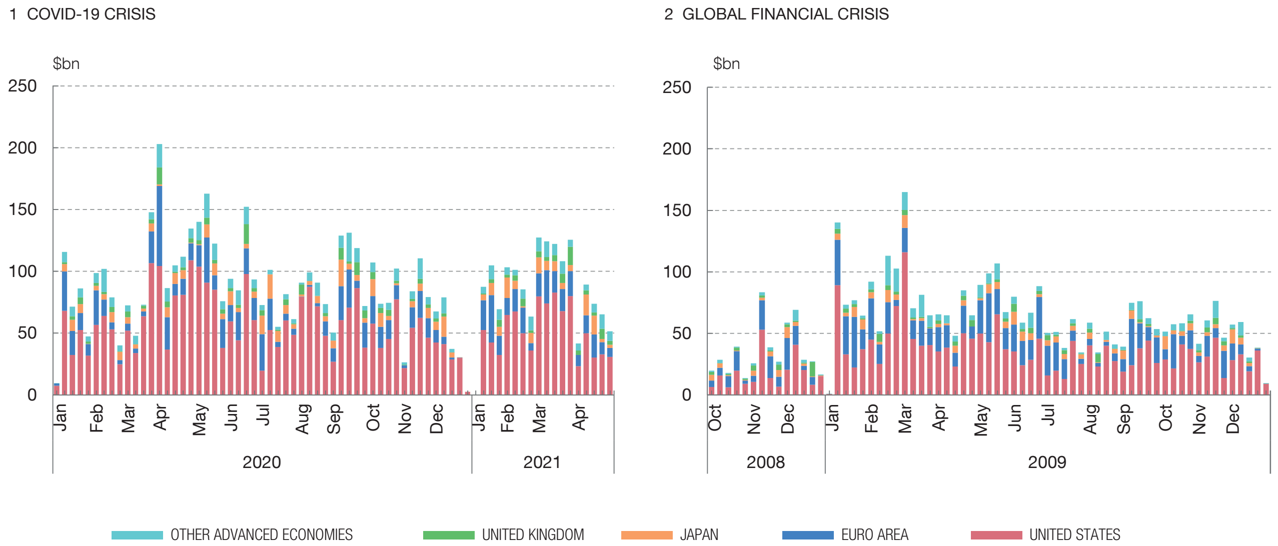
Corporate bond issuance volume reached record highs in March/April 2020 as the spread of coronavirus took hold and restrictions were introduced. The gross issuance volume reached $147 billion in the last week of March and $202 billion in the first week of April (see Chart 2). In the case of the GFC, the highest volumes were recorded in January and March 2009, when bond issuance totalled $140 billion and $165 billion, respectively. In this case, issuance peaked some time after the crisis emerged.[6]

Over the following months, the volume of new bond issuance declined, although it remained high on average. Thus, following the peak recorded in April 2020, the weekly average was $89 billion for the year overall and $91 billion for the period January-April 2021. In the case of the GFC, following the peak recorded in March 2009, the weekly average for the rest of the year was $60 billion.

5 Analysed on the basis of gross issuance volume (data provided by Dealogic).

6 As indicated above, the GFC built up gradually, although the financial stress is generally considered to have peaked with the collapse of Lehman Brothers in September 2008.

Chart 2
CORPORATE BOND ISSUANCE IN THE GFC AND THE COVID-19 CRISIS: ADVANCED ECONOMIES



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SOURCE: Dealogic.

There are various factors that may explain the increase observed between the two crises, notably including: a) tighter prudential regulations for financial institutions following the 2008 crisis, including new limits on leverage and minimum liquidity requirements, which limited funding provided by banks; b) central banks' accommodative non-standard monetary policies, which helped to maintain favourable financing conditions and reduce the cost of debt obtained through other channels, such as private asset purchase programmes; and c) enhanced and easier access to funding markets for non-financial institutions (more common in the United States than in Europe).

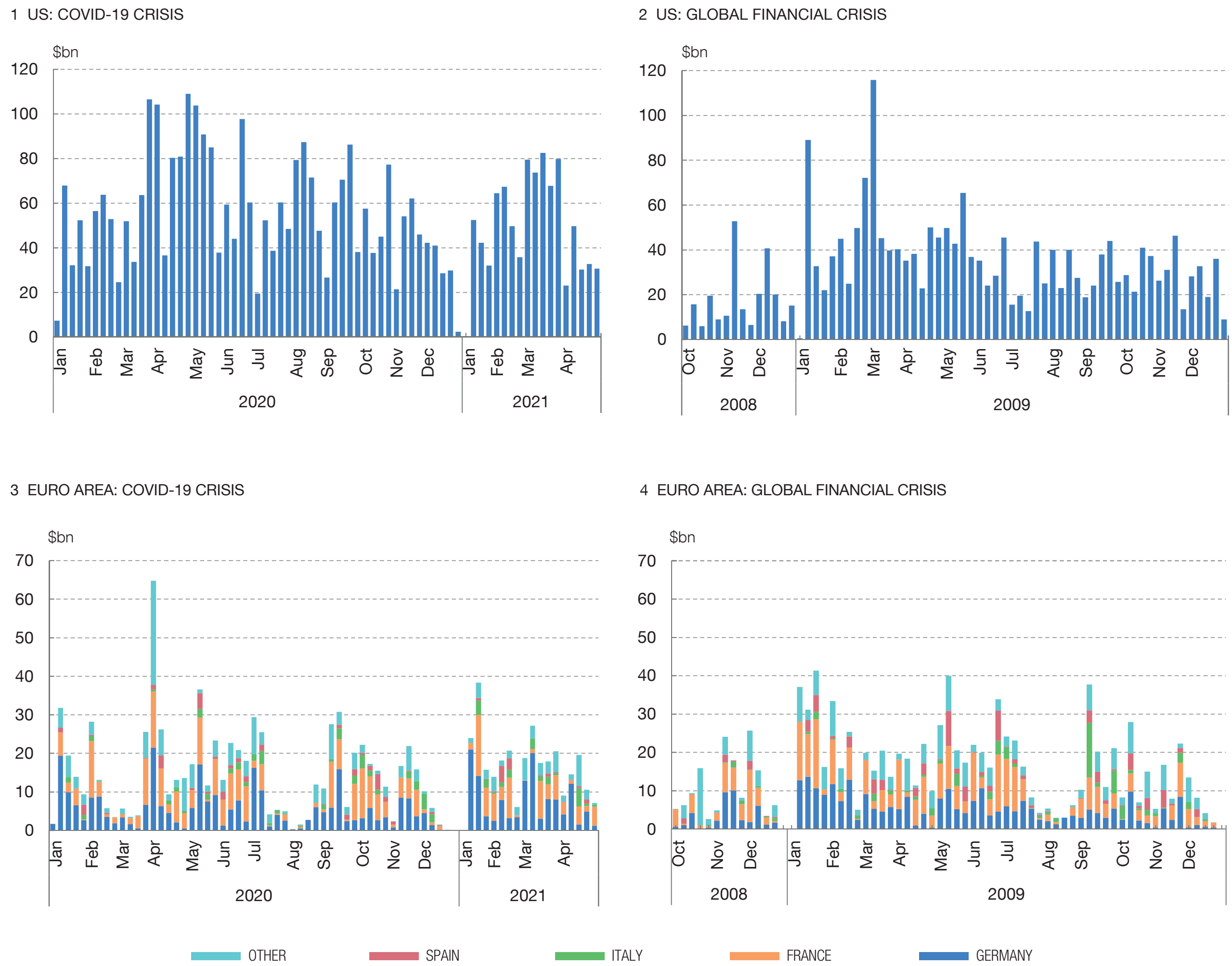
The United States accounts for most corporate bond issuance, with a share that has risen from 54% (GFC) to 62% (COVID-19 crisis) of the total in the periods shown in Chart 2. The euro area accounts for 26% and 17%, respectively, of the total.[7] This difference between the two areas appears to stem from the fact that US corporations have traditionally attached greater importance, and have had easier access, to market funding than their euro area counterparts,[8] evidencing the continuing need to further the capital markets union (CMU).

At the start of the COVID-19 crisis, corporate bond issuance rose significantly and almost simultaneously in both areas: in the United States, issuance totalled

7 To put these figures in perspective, US GDP accounts for around 45% of the total GDP of the advanced economies and euro area GDP for around 27% (data as at 2021 Q2).

8 In the United States, 16% of funding is obtained through bank loans, compared with 28% in the euro area (Federal Reserve and ECB data as at end-2020).

Chart 3
CORPORATE BOND ISSUANCE IN THE GFC AND THE COVID-19 CRISIS: UNITED STATES AND EURO AREA

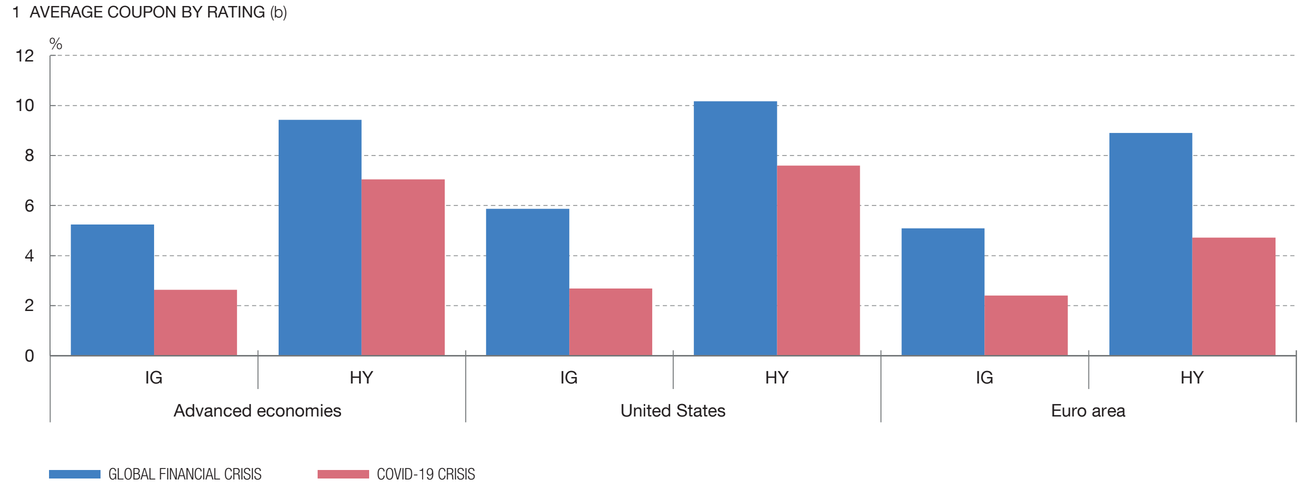


SOURCE: Dealogic.

$106 billion in the last week of March, while in the euro area the peak was reached in the first week of April, when it amounted to $64 billion (see Chart 3). However, while in the United States this issuance volume remained steady in subsequent weeks, in the euro area it fell considerably, as it decreased in Germany and was much higher in April in certain small countries (such as the Netherlands, Austria and Belgium) than in the rest of the year.

During the GFC, the increases in issuance volume in the United States in January and March 2009 were followed by a decline in the average volume in the rest of the year. In Europe, the pattern was similar to that observed during the pandemic since, with the exception of the peak recorded in April 2020, issuance volumes in both episodes were quite similar at the start of the crisis and over the following months.

Chart 4
COST OF CORPORATE BOND ISSUANCE (a)



SOURCE: Dealogic.

a Calculation periods: January 2020 to April 2021 (COVID-19 crisis) and October 2008 to December 2009 (GFC).
b Calculated drawing on fixed-coupon issues.

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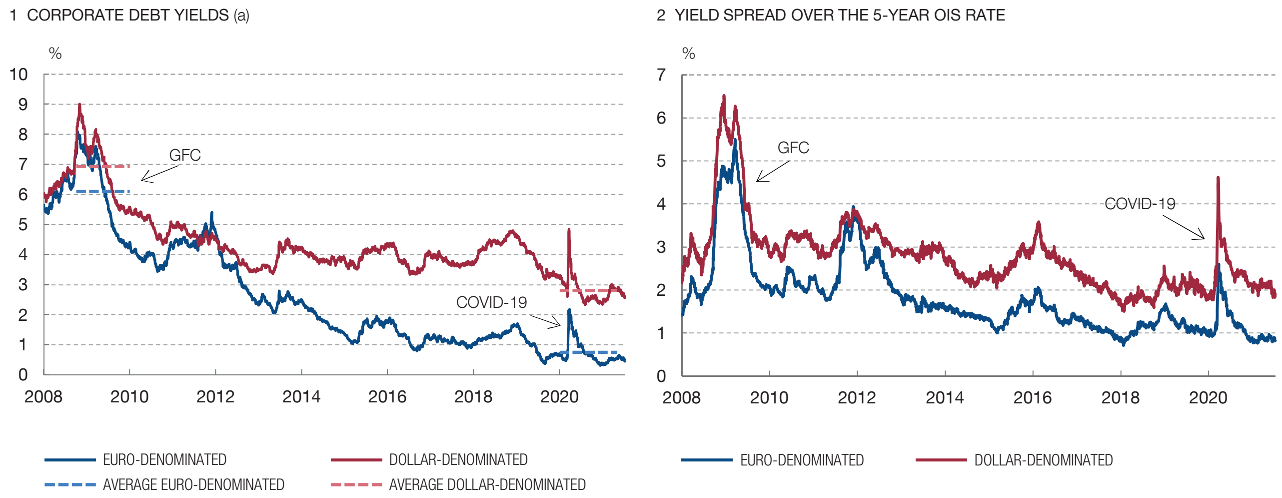
Cost of issuance

The cost for issuers of the different types of debt, according to their credit rating, was substantially lower during the COVID-19 crisis than during the GFC (see Chart 4). This is not surprising, considering the general decline in interest rates in recent years. On average, in both crisis episodes, bonds issued in the United States have higher coupons than those issued in the euro area, be they investment-grade (IG) or high-yield (HY) bonds. This is consistent with the different approaches adopted by the respective central banks (the Federal Reserve has a higher policy rate than the ECB), and with the different credit risk perception in the two regions.[9]

The downward costs are also reflected in the iBoxx corporate bond indices (see Chart 5). While at the start of the GFC, the average yield to maturity was 6.9% for dollar-denominated debt and 6.1% for euro-denominated debt, during the COVID-19 crisis the average has been 2.8% and 0.7%, respectively. The sharp increase observed in the first weeks of each crisis is noteworthy, although in the case of the pandemic crisis, yields returned relatively swiftly to their previous levels.

9 In the period between the crises, the German 10-year government bond yield (the European benchmark) was lower than the US 10-year government bond yield, especially after 2012, and in 2019 it was even negative for a continued period.

Chart 5
CORPORATE DEBT YIELDS



SOURCES: iBoxx and Bloomberg.

a GFC: from 2008 Q4 to 2009 Q4; COVID-19: from 2020 Q1 to 2021 Q1.

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Issuance volume by debt duration

The average duration of corporate debt increased between the two crisis episodes[10] (see Chart 6). The proportion of short-term issues (with a duration of 1-5 years) fell from 44% to 32%, while the share of medium and long-term debt rose (debt with maturities of 7-10 years, from 12% to 19%, and debt with maturities of over 10 years, from 29% to 33%). This pattern is more pronounced in the euro area, where short-term debt is no longer predominant, having halved between the two episodes. Meanwhile, debt with a duration of 7-10 years more than doubled and debt with longer maturities grew by 10 percentage points (pp). By contrast, in the United States short-term debt is still prevalent, although it has declined and longer-term debt has increased.

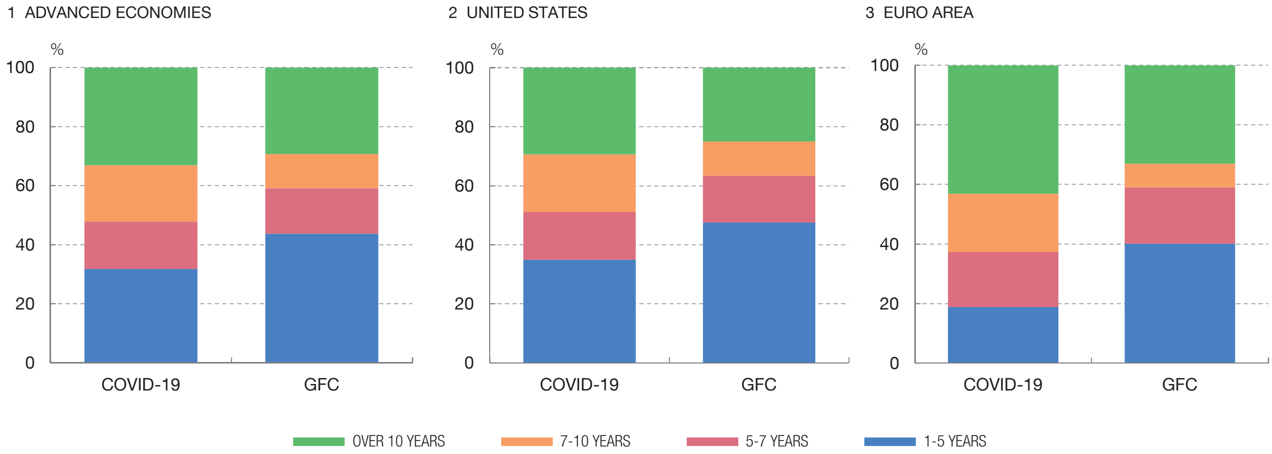
The increase in duration may have been favoured by the widespread reduction in the cost of debt, which has allowed debt with longer maturities to be issued at a lower cost. Many firms have taken this opportunity to issue longer-term debt to repay existing short-term debt.[11] There is also empirical evidence linking monetary policy interest rates with debt duration, showing that when rate cuts occur, debt duration tends to increase.[12]

10 Based on the relative share of each years-to-maturity tranche.

11 Especially in the United States, as shown in the section on the use of funds.

12 See Fabiani, Falasconi and Heineken (2020).

Chart 6
ISSUANCE BY DEBT DURATION (%) (a)



SOURCE: Dealogic.

a Calculation periods: January 2020 to April 2021 (COVID-19 crisis) and October 2008 to December 2009 (GFC).

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Issuance volume by credit rating

Investment-grade bonds accounted for the vast majority of new issuance in both crises, although the percentage of high-yield bonds significantly increased during the COVID-19 crisis (see Chart 7). Indeed, their share rose from 6% to 14% thanks to developments in the United States, where their share reached 17% of the total, but also in the euro area, where it tripled (from 3% to 10%). While in the United States the volume of HY debt was already considerable as early as April 2020, in Europe it did not account for a significant share until the summer.

The actions of central banks have been key in explaining these developments.[13] Specifically, the US Federal Reserve included HY bonds in two of its purchase facilities,[14] allowing debt to be purchased from so-called "fallen angels".[15] More significantly, it also expanded the purchase of exchange-traded fund bonds to allow a greater exposure to HY debt (in fact, these accounted for the vast majority of its HY bond holdings). For its part, the ECB lowered the eligibility requirements for debt in its PEPP, although it maintained the requirement that it be IG debt.

13 See Khametshin (2021). Specifically, monetary policy measures can influence debt markets and the HY segment by increasing market prices through their purchase programmes (thereby reducing the cost of financing), restoring liquidity in secondary markets (which increases liquidity in the primary market) and supporting demand for bonds by stimulating bank lending.

14 The Primary Market Corporate Credit Facility and the Secondary Market Corporate Credit Facility, with a combined envelope of up to $750 billion.

15 Bonds that were downgraded from IG to HY in the initial stages of the crisis (provided that issuers had maintained IG status up to 22 March 2020).

Chart 7
ISSUANCE BY RATING (%) (a) (b)

SOURCE: Dealogic.

a Calculation periods: January 2020 to April 2021 (COVID-19 crisis) and October 2008 to December 2009 (GFC).
b Ratings calculated by Dealogic drawing on S&P, Moody's and Fitch.

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Issuance volume by sector

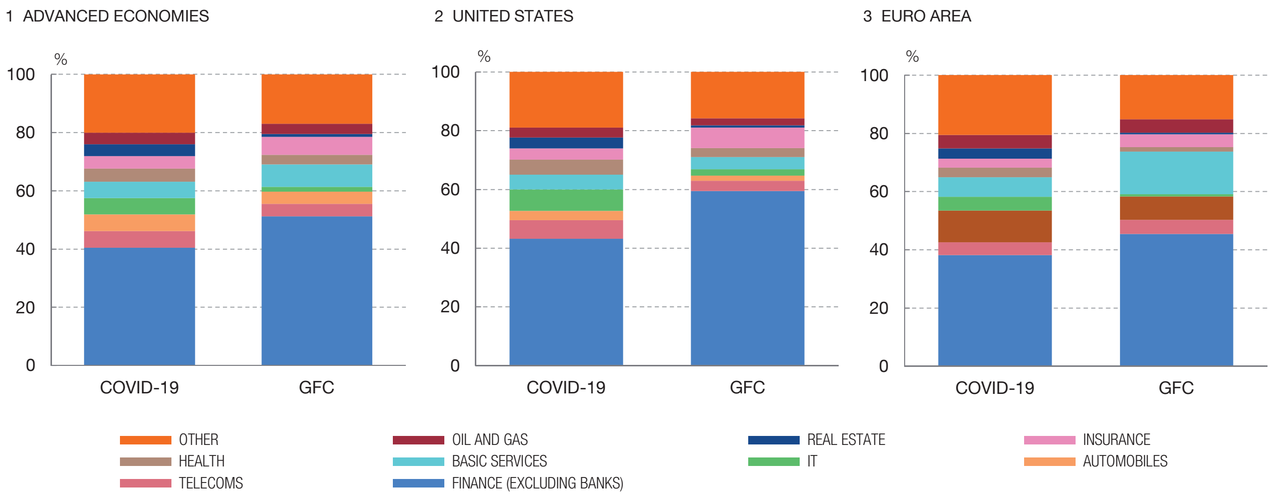
Non-bank financial corporations was the sector that issued the largest volume of bonds, although its share of the total declined between the two crises. While in the first year of the GFC it accounted for half of the total, its share fell to 40% in the COVID-19 crisis (see Chart 8). This drop in relative importance is very marked in the case of the United States, where the sector issued up to 60% of the total during the GFC, but can also be observed in the euro area.

The decline occurred despite the fact that these corporations increased their issuance during the COVID-19 crisis. The reason behind this was the sharp growth in issuance by non-financial corporations as a whole. Among these, the sectors with the greatest increases in volume between the two crisis episodes were IT, health, real estate and automobiles. By contrast, declines were observed in the share of basic services, insurance, and oil and gas. This pattern is observed both in the United States and the euro area, albeit with some differences given the greater importance of the automotive sector in Europe and the telecommunications sector in the United States.

Issuance volume by use of funds

The funds obtained were used differently in each crisis, and in the United States and the euro area (see Chart 9). Thus, in the United States, “general uses” (linked to firms' basic activity), which accounted for 72% of the total at the onset of the GFC, fell to 43%

Chart 8
ISSUANCE BY SECTOR OF ISSUING FIRM (%) (a)



SOURCE: Dealogic.

a Calculation periods: January 2020 to April 2021 (COVID-19 crisis) and October 2008 to December 2009 (GFC).

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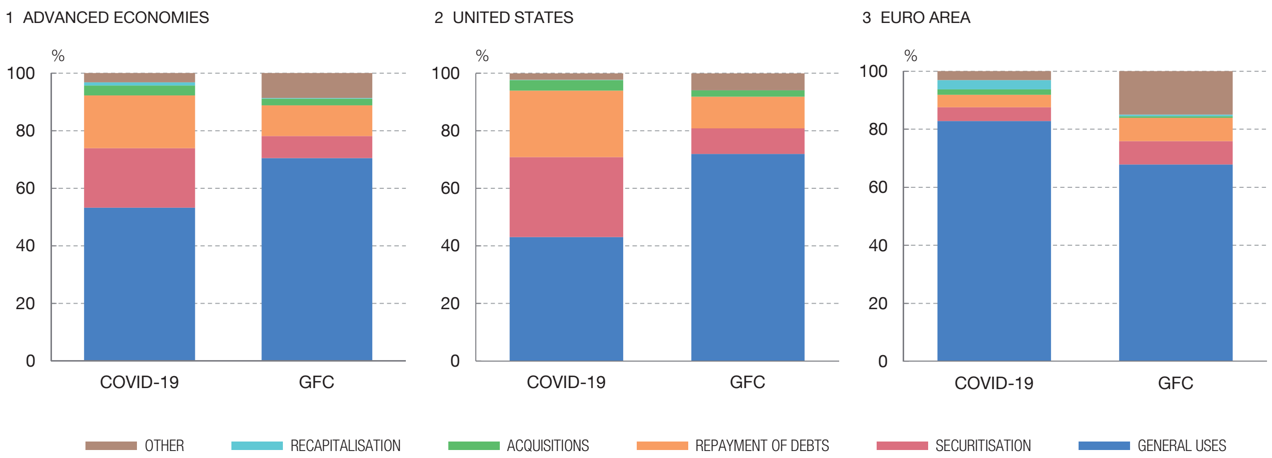
Chart 9
ISSUANCE BY USE OF FUNDS ACQUIRED (%) (a)



SOURCE: Dealogic.

a Calculation periods: January 2020 to April 2021 (COVID-19 crisis) and October 2008 to December 2009 (GFC).

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in the more recent crisis. Meanwhile, debt securitisation[16] and repayment of existing debts increased sharply, accounting for 28% and 23% of the total, respectively.

16 The vast majority of firms that resorted to securitisation were non-bank financial corporations.

By contrast, in the euro area, the relative share of "general uses" increased, from 68% of the total in the GFC to 82%. But the share of securitisation and repayment of outstanding debt declined. In both areas, the share of debt issued to finance acquisitions increased.

The data suggest that, while European firms mostly opted to raise liquidity in order to continue their activity during the COVID-19 crisis, US firms took advantage of the reduced cost of debt (compared with previous years) to lower the cost of their liabilities, exchanging older, more expensive ones for cheaper debt. High yield-rated firms benefited the most, while investment-grade firms tended to use the funds for their own activity.[17]

Conclusions

In the early months of the GFC and the COVID-19 crisis, bond issuance by non-financial and non-bank financial corporations in the developed economies hit record levels. Thus, in 2009 Q1 and 2020 Q2, sharp increases were observed compared to previous periods. However, the underlying reasons for this are different: in the GFC firms sought to replace bank loans (due to tighter credit standards and a decline in lending), whereas during the COVID-19 pandemic they were looking to address a liquidity problem caused by the lockdowns and restrictive measures adopted to combat the virus.

During the COVID-19 crisis, central banks have played a key role in sustaining and supporting this issuance. Asset purchase programmes (such as the PEPP in the euro area or the facilities implemented by the US Federal Reserve) announced at the outset have injected liquidity into the system, contributed to reducing issuance costs and allowed firms to weather the difficulties arising from lockdowns.

There are significant differences between the issuances made during the two crises; notably the considerable decline in financing costs on account of lower market interest rates. This may have favoured a longer average duration of bonds (most clearly observed in the euro area) and the greater use of funds to refinance existing liabilities with comparatively cheaper debt (seen only in the United States).

Furthermore, although HY bond issues have increased in Europe, they have done so more markedly in the United States, thanks to the inclusion of HY debt in the Federal Reserve's purchase programmes. Firms with this credit rating have also been able to benefit from lower issuance costs and thus repay outstanding debt.

Another noteworthy difference is the change in the sectoral breakdown of issuing firms, with the share of non-bank financial corporations decreasing while that of IT,

17 Dealogic (2021).

health and real estate firms has increased owing to the sharp rise in their issuance between the two episodes.

Despite its positive effect in guaranteeing liquidity and the survival of firms, this growth in issuance also entails a series of risks. Increased debt levels could affect the post-pandemic recovery process if these firms are unable to service their debt or do not survive the crisis.[18] Further, central banks' efforts to inject liquidity through non-standard measures such as purchase programmes will be gradually phased out at some point, requiring vigilance with regard to their effects on the private debt market.

28.9.2021.

18 Abraham, Cortina and Schmukler (2020).

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