

Frequently Asked Questions regarding Bail-In Bonds

What are bail-in features in bonds?

In the event of a failure or likely failure of a bank, shareholders and bondholders may be bailed-in to absorb the losses, instead of a bail-out by taxpayers. As such, bondholders may lose the value of their holdings (in a write-down) or be converted into equity. This is to facilitate the recapitalization of the bank and prevent further consequences to the financial system.

Why have they come into effect?

This is mainly driven by the 2008 global financial crisis, when governments had to bail-out a number of Global Systemically Important Banks (G-SIBs). Bail-in features are seen as a way of mitigating the collapse of “too big to fail” institutions.

When will they come into effect?

G-SIBs have already commenced the issuance of bail-in bonds as well as, in some instances, retrospectively classified existing senior debt as bail-in bonds in order to meet the new capital requirements.

Which bonds are impacted?

Bail-in can be applied to a range of different liabilities, including but not limited to subordinated debt and unsecured senior liabilities.

Why does this matter to customers?

Prices, Yields and Credit Ratings of Bonds may not fully reflect bail-in features – Bail-in introduces additional risks (different from default risks) which are difficult to price. Furthermore, the mechanics of bail-in are complex and there are differences in regulations amongst various jurisdictions.

Bondholders may suffer heavy losses – There are significant risks for bondholders as bail-in affects liabilities up to unsecured senior debt. They may face heavy losses, should the value of their holdings be written down or converted into equity.

Lack of transparency on point of non-viability – The point of non-viability—the point where a bank has failed or is likely to fail and bail-in provisions may be implemented—may be interpreted differently by different local regulatory authorities. Additionally, there is still a lack of transparency over the point of non-viability, the triggers and the consequences.

Increased scrutiny of bank balance sheets – Bondholders may scrutinize bank balance sheets more closely as they have to bear the burden of failures now. They may want detailed information on the buffer of loss-absorbing debt as well as where their bonds rank in the hierarchy of creditors.

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