Editors’ Note

The value of voluntary COVID-19 securities disclosure—zero?

An age-old question in the world of securities disclosure is whether there is value in mandating that issuers disclose key pieces of information about themselves to the investing public or whether these issuers will voluntarily disclose the optimal amount of information as a function of reputational pressures. Many academic articles have been written about this topic, and different regulatory systems around the world take starkly different positions on the question. Yet, there is no clear answer to the core question of whether issuers will voluntarily disclose useful information that only they know to investors at key times (e.g., when investors are being asked to buy securities) or whether a mandatory system with penalties and monitoring is necessary to induce this disclosure.

The current COVID-19 pandemic may present an opportunity to examine this question in the sovereign issuer context. As a result of a strange confluence of factors, there seems to be little negative effect of this global pandemic on the international sovereign debt market. If anything, this market is booming more than ever with countries across the range ratings quality being able to borrow billions of dollars at rates comparable to pre-COVID times.¹ Important for purposes of the question we have raised, each and every one of these countries has been impacted by the pandemic differently. And, more important, each of these countries is taking different steps to tackle the crisis and has information as to what is going on at the local level that global investors likely know little about.

One might ask therefore: are we seeing these different issuers, who the market has been showering with billions of dollars in lending, disclose the kind of detailed information as to their responses to the pandemic and how they are going to get out from under it that investors would like to have? For sovereigns, there is no mandatory requirement that they disclose anything on the matter of pandemic responses, so what we are talking about is their voluntary disclosure.

Let us take the example of Brazil. It issued $3.5 billion in sovereign bonds in the international markets a few weeks ago. That Brazil was able to place such a large issuance in the context of the pandemic is particularly noteworthy since its government’s response to the pandemic is widely considered to be among the most disastrous in the world.² One might think though that perhaps, in order to persuade investors to give it these billions, Brazil’s leading public health expert will have prepared detailed explanations for how and why the

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¹ Emerging economies, according to the Financial Times, have borrowed more than $83 billion between the beginning of April and the second week of June. See Jonathan Wheatley, ‘Developing Economies Borrow More Despite Debt Relief Initiative’ Financial Times (London, 14 June 2020) <https://www.ft.com/content/54c545aa-01b5-4e95-8adc-e6805f5d82be1> accessed 15 June 2020.

² See, e.g., Tom Phillips, ‘Brazil Condemned to Historic Tragedy by Bolsonaro’s Virus Response—Top Doctor’ The Guardian (London, 5 June 2020) <https://www.theguardian.com/world/2020/jun/05/brazil-coronavirus-covid-19-virus-doctor> accessed 15 June 2020.
disastrous strategies pursued so far are a thing of the past and that the new strategies being pursued will lead the country out of its current condition.

Think again.

Brazil’s prospectus supplement dated 3 June 2020, at first cut, looks to contain pages and pages of information regarding how the country has been dealing with the COVID-19. Best we can tell, almost all of it has the quality of the following piece of disclosure, which is the first item of risk disclosure that appears in the risk factors section of the supplement. The language below, we think, makes our point better than we can. To our reading, it is hard to describe it as anything other than vacuous. There is not a single piece of useful information in this disclosure other than the fact that the government refuses to say anything useful. But read for yourself. From page S-8:

Risk Factors Relating to Brazil

*Developments relating to the outbreak of the coronavirus may have a material adverse impact on our economy.*

The global outbreak of COVID-19, and public health measures to mitigate it, are having a material impact on the economy in Brazil and around the world. The scope, magnitude and duration of the impact on Brazil cannot yet be determined. COVID-19 could increase the risks described elsewhere in this section.

The long-term effects of the COVID-19 and other public health crises on the global financial markets and economy are difficult to assess or predict. They may include risks to citizens’ health and safety, as well as reduced economic activity, which in turn could result in decreased revenue for the government and increased expenditures, among other relevant impacts. It is unclear whether these challenges and uncertainties will be contained or resolved, and what effects they will have on the global financial markets and economy in the long term. We cannot predict the evolution of the disease in Brazil or whether additional restrictions will be required. In addition to measures taken by Brazilian federal, state and local governments, Brazil may be affected by the impact of the disease elsewhere in the region and by measures taken by other countries or organizations, such as orders that suspend travel or that limit trade. The final impact of the COVID-19 pandemic is still uncertain, but it is expected to have a significant adverse effect on our economy.

COVID-19 is also present in Brazil, and the Brazilian government has taken extensive steps to mitigate the spread of the disease and its impact on public health. See “Recent Developments—COVID-19 Developments” in this prospectus supplement. The efficacy of these steps cannot yet be evaluated, and it is highly uncertain how long and in what form they will remain in effect. Since March 2020, the government has introduced several measures to address the COVID-19 pandemic. The measures implemented so far have resulted in a slowdown in economic activity that will adversely affect economic growth in 2020 and possibly 2021, to a degree that we cannot quantify as of the date of this prospectus supplement. Any prolonged restrictive measures put in place in order to control an outbreak of contagious disease or other adverse public health development in Brazil may have a longer lasting material and adverse effect on our economy. While the economic cost of the COVID-19 pandemic is difficult to predict, we expect that our fiscal deficit will increase. The long-term impact of the governmental measures on our economy, and the effectiveness of these measures, cannot be assured. If these measures are insufficient or are not successfully implemented, the effect on the Brazilian economy or on the Brazilian debt sector could be exacerbated.

Brazil’s economy is vulnerable to external shocks and to more general “contagion” effects, each of which could have a material adverse effect on Brazil’s economic growth and its ability to raise funding in the external debt markets in the future.
Emerging market investment generally poses a degree of risk because the economies in the developing world are susceptible to destabilization resulting from domestic and international developments.

Brazil’s economy is vulnerable to external shocks, including adverse economic and financial developments in other countries and market developments. A significant increase in interest rates in the international financial markets may adversely affect the liquidity of, and trading markets for, the global bonds. In addition, a significant drop in the price of commodities produced in Brazil, such as iron ore, oil, soybeans, sugar and corn, could adversely affect the Brazilian economy. A significant decline in the economic growth or demand for imports of any of Brazil’s major trading partners, such as China, the European Union, or the United States, could have a material adverse impact on Brazil’s exports and balance of trade and adversely affect Brazil’s economic growth.

Picking on the Brazilian disclosures though is unfair. One finds little that is different in any of the other disclosures to investors that have been made by sovereign issuers over the past few months. In fact, reading the COVID-19 disclosures for the different countries—each of them facing very distinct and different public health crises as a result of the pandemic—produces a strange sense of déjà vu since one gets the sense that the basic language of ‘we can’t predict anything, we don’t know anything, COVID-19 might be really bad for us and everybody else’ seems to have been copy-pasted from document to document by some junior lawyer rather than taken from a report to the Ministry of Finance prepared by the nation’s top public health experts.

The question has to be asked then. If this is the quality of securities disclosure, why bother? Having junior lawyers at some fancy New York law firm, copy and paste meaningless language is an expense that countries such as Brazil cannot afford in the midst of a pandemic. And the same is undoubtedly true for other recent issuers such as Egypt, Colombia, North Macedonia, Guatemala, Paraguay and so on and so forth.

The counterpoint from anyone who has spent time producing these documents might be: why would you expect anything different? Even in the best of times, it is not like the disclosures give the opinion of the country’s leading economic expert about why, say, the country’s economic policies are likely to spur growth. They just report basics about the economy (we get X% of FX from the export of A, B and C) and some generic risk factors (we are subject to FX risk, weather risk, etc.). And given the uncertainty about COVID impacts, it seems more not less reasonable to resort to generic risk disclosure language.

Maybe so. But doesn’t the foregoing just confirm that basic point that these disclosures are largely useless, where the only ones benefiting are the lawyers who bill hours for their copy-paste endeavours?

In the volume that follows, we have, as we always do, endeavoured to bring readers a set of articles that combine perspectives from both academia and practice. And in the next few issues (at least), we will try to continue to bring discussions of the impact of COVID-19 on capital markets law and regulation.

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