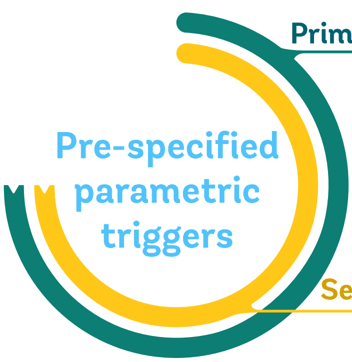
Climate Resilient Debt Clause (CRDC)

Definition

Multiple tools are increasingly necessary to address developing countries' urgent liquidity needs in the face of climate and other shocks. As the frequency and severity of climate-related shocks increase, countries require new tools for managing climate risks in debt portfolios.

Climate Resilient Debt Clauses (CRDC) embedded in loan or bond agreements enable a borrowing country to **pause debt service** in the event of a significant natural disaster. Implementing temporary ex-post debt service relief in the event of a shock is challenging - even under a well-recognized force majeure, as was the case with COVID.

CRDCs should be part of a risk-layered mix of financial products aiming to provide liquidity in times of catastrophes. This risk-layered mix should also include: budget reserves to finance small and recurrent disasters; contingent credit lines (such as World Bank CAT DDO), to finance less frequent but more severe disasters; (parametric) risk transfer instruments (such as catastrophe bonds or (re)insurance) to finance infrequent but very severe disasters.



Primary parametric triggers

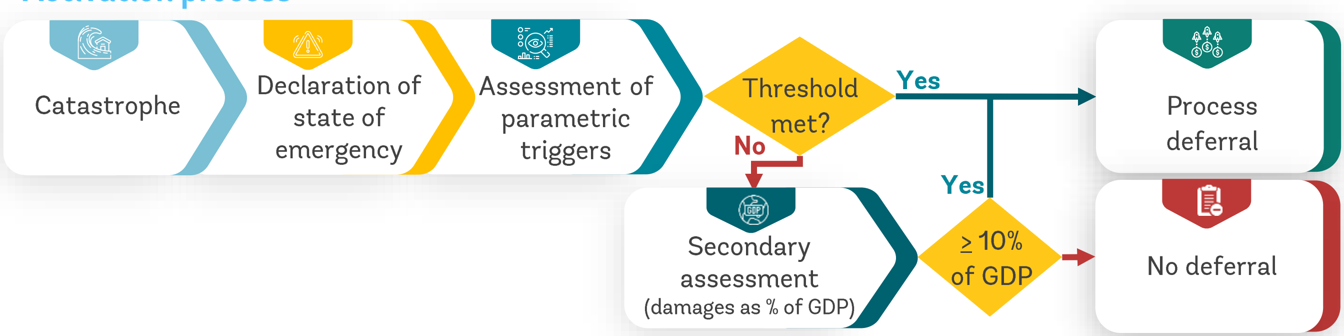
a. **Earthquakes**: Moment magnitude (Mw) 7.0 or above, with reported depth less than or equal to 175km with an epicenter within the covered area.

b. **Tropical cyclones/hurricanes**: Reported maximum sustained windspeed in the covered area at 178km/hr or above if reported as 1-min average windspeed; or 160km/hr or above if reported as 10-min average windspeed.

Secondary parametric triggers

Upon verification, the World Bank will determine whether estimated damages from the eligible event are greater than or equal to 10% of the country's GDP[1]

Activation process



Examples

CRDCs are relatively new instruments. Grenada (2015) and Barbados (2018) were the first two countries to include CRDC in bonds issued as part of their debt restructuring. The International Capital Market Association (ICMA) published a model for CRDC (2018) and a model term-sheet (2022) for sovereign issuers interested in inserting natural disaster provisions into their bond documentation. Several multilateral and bilateral creditors have introduced or are exploring the introduction of CRDCs in their loan contracts. The IMF's Catastrophe Containment and Relief Trust (CCRT) provides grants for relief on debt service to the IMF for the poorest and most vulnerable countries.

In September 2023, the WBG Executive Directors approved the introduction of CRDCs into IBRD and IDA loan agreements for the borrowers most vulnerable to natural disasters, namely small states[2].

Note:
1) Assessment based on the Global Rapid Post-Disaster Damage Estimation (GRADE) approach;
2) Small States Forum (SSF), Small Island Developing States (SIDS) , and WB-defined small states.

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