Pricing carbon reduction

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Without decisive actions, the rapid transition to a low carbon world and limiting global warming to below 2 degrees will be impossible in the current global economic and financial circumstances. Most governments are struggling with large debts and persistent deficits, and public resources are scarce. We also lack mechanisms to induce a massive shift in private finance necessary from global financial markets for new low carbon investments. Though there is ample liquidity and excess savings in global finance, mobilizing it towards such a shift is difficult under the current financial system's culture and focus on short-term and speculative investments. Nevertheless, as researchers working across continents on galvanizing global climate change finance, we are convinced that a solution is possible: to reinvigorating jobs and growth in our global economy and simultaneously addressing climate change. We need tools to translate into action the decision taken by 196 nations in Article 2 of the recent Paris Climate Agreement: "to (make) finance flows consistent with a pathway towards low greenhouse gas emissions and climate-resilient development."

Across the world, everyone recognizes that massive and unsustainable current carbon emissions in our fossil-fuels dependent world should be accountable for their "dis-externalities" and have their true overall costs established. Implementing this 'polluter-pays' principle, by taxing producers for the global social cost of carbon emissions, is absolutely necessary. But any progress is likely to be gradual and difficult---given tough political resistance and an uphill battle to be fought and won, nation by nation---since taxation systems are national. There is, however, another possible solution: "positive pricing", that reverses the logic and recognizes up-front the social and economic value of carbon reduction. Fortunately, this is now enshrined in paragraph 108 of the Paris Decision, that carbon reduction or removal as "mitigation actions" should be positively priced. This will not replace taxing carbon. Both have their own specific roles in financing the transition to low carbon economy. The recognition of the "social, economic and environmental value" of carbon reduction and removal represents a "carrots than sticks" approach and countries can choose how far and how fast they wish to proceed.

The next step would be to translate this recognition of the positive social and economic value of carbon reduction/removal into workable financial tools. Government backed guarantees, recognizing and reflecting the 'positive pricing of carbon reduction', could mobilize accelerated resources from the private financial system for carbon reduction investments. This will allow nations, rich and poor, to choose their current levels and future pathways, and commit immediate public resources up-front to finance climate investments now and establish other innovative tools to reduce risks.

One possibility is to initiate action through an open architecture of countries committed to such actions through so-called 'climate clubs'. Some important countries might be more willing to sign-up earlier than others, and induce others to join quickly later in a cascading fashion. Yet another crucial aspect---that many central banks are starting to look at---is to realign their countries' monetary policy tools to encourage their financial systems to start investing in the shift to productive low-carbon assets (instead of 'junk bonds')---including "quantitative easing" operations of the kind being currently implemented by many central banks, including the European Central Bank. That would be a far better way to stimulate their economies and cope with deflation.

Let us imagine: a group of willing governments, central and development banks, along with multilateral institutions, forming a "Climate Club" providing guaranties for specific quantities of carbon reduction assets. Governments doing so can eventually use carbon taxation to cover their exposure. Bank loans for duly certified carbon reduction projects/policies could then be partially reimbursed in the form of "carbon reduction certificates". This new value, covering say 10% to 20% of those mitigation action investments, may become the tipping point for a major adjustment in the global financial system, in a sort of "low carbon Bretton Woods". Those carbon reduction assets, recognized as a unit of value, could eventually become a future convertible reserve currency.

It can also help communities adapt to climate change as well. Proceeds of such 'value' could be shared with adaptation projects, helping communities to prepare and devise their own solutions and innovations to cope with the ongoing effects of climate change. Hundreds and thousands of distributed, community-owned, scaled-up, 'bankable' projects would become possible: everything from protecting fragile coastlines and bio-diversity, to prevention climate disasters, droughts and managing water for small-holder crops and household needs, especially affecting women and the poor. With the help of numerous 'on-ground' civic society organizations. The recognition that carbon reduction/removal equals value sets new paths for future carbon neutral economies and for coping with both the long term consequences of climate change and the short term tensions of the current world economy.

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