

London calls for carbon bonds

London's finance community said carbon bonds are needed to shore up investor confidence.

The City of London, which is one of Europe's main financial centres, wants to expand the range of climate-based financial instruments to curb the threat of regulatory risk.

Chief among these measures is an index-linked carbon bond, the City of London outlined in a report called 'Delivering Copenhagen'.

The government bond would have a fixed interest rate, although actual interest payments would vary depending on whether or not the issuer keeps an environmental promise.

"An investor in an index-linked carbon bond receives a better yield if the issuing country's targets are not met," the report states.

For instance, bond holders could receive "an extra percentage point of interest for each €1 that carbon dioxide prices fall below a floor price."

If governments deliver policies that meet their targets, they get cheap money by paying a lower interest on the bond.

But if governments fail to meet their green pledges, they pay a higher rate of interest on the bond.

"Any government (supra-national, national, state, province) could issue index-linked carbon bonds without the need for a global initiative," the report adds.

The International Monetary Fund estimates that government debt will grow by at least 36 per cent in three years in the aftermath of the global financial crisis.

Forestry products

The City has also called for a forest-backed bond that would help forest conservation.

By turning forests into financial instruments by securitising the physical assets, borrowers can then raise capital by issuing bonds.

The repayment of the bonds is underwritten by the performance of the package of forestry assets.

"This unlocks the necessary short-term cash flow, removing the need to cut down the forest and, as a collateral benefit, protecting its long term asset value, financial and otherwise," the report states.

Forest-backed bonds need to be issued through

a supranational entity, and incorporate powerful guarantees, the report adds, if they are to be attractive to institutional investors.

"Businesses must have confidence that the regulatory system will remain clearly defined and stable over the course of any investment," said Simon Mills, environmental co-ordinator at the City of London.