
Funding the Global Renewable Energy Transition with Interest Free New Money

A proposal from the World Future Council (WFC)

Questions and Answers

The World Future Council proposes that the IMF issue special SDRs worth \$ 100 billion annually over ten years to break the funding deadlock of the global renewable energy (RE) transition. The new money should be issued without interest in order not to create new debt; and it should be paid only against performance i.e. building new RE infrastructure especially in developing countries; therefore it will not be inflationary. By using SDRs the funding is based on a well established mechanism: in April 2009 the G20 Summit assigned the IMF to create additional SDRs worth \$ 250 billion. The goal was to provide IMF member states with more convertible reserve money to meet the additional needs of liquidity of the banking system during the international financial crisis. The core of the proposal from the WFC is to use the same tool to meet the liquidity needs of the renewable energy transition. In contrast to previous SDR allotments, this time it is used for the special purpose of climate protection and justice only; instead of meeting general liquidity needs. The following Q&A gives an overview of the proposal.

1. Which problem is addressed by the proposal?

The proposal addresses the funding problem of the global RE transition. Instead of redistributing funds out of governments' tight budgets the WFC proposes to "pre distribute" newly created money.

2. Who profits from a new allotment of SDRs to fund the RE transition?

All countries participating in the program will profit. The WFC proposes to invest the newly issued SDRs mostly in new infrastructure (solar and wind power, storage and networks) in developing countries. New jobs and economic activity are induced in developing as well as industrialized countries either through firms selling the respective equipment and building the infrastructure or through new economic development spurred by the new infrastructure.

3. Does the new money create a new debt burden?

No. The new SDRs should be created interest free and be non repayable.

4. How does it work?

The WFC proposes that IMF member states decide on the allotment of new SDRs worth about \$ 100 billion. The member states commit themselves to forwarding the new SDRs to the new Green Climate Fund (GCF) established at the Cancun COP 16. The new GCF will decide how to spend the new funding most fairly and effectively. The GCF will exchange SDRs for the respective national currencies needed to finance a concrete project in accordance with existing mechanisms. Part of the new funds (e.g. 10 to 20 percent) could be used directly by national governments of member states to be spent on climate protection projects.

5. How can it be assured that the new money creates new goods and values instead of merely increasing the global money stock?

Spending the new SDRs will be according to the principle of “money against performance only”. The Green Climate Fund should only provide newly created funds in payment for concrete projects.

6. Would the new money cause inflation?

The new money could cause inflation only if there are no excess production capacities in industrialized countries. Yet, empirical research (see e.g. Federal Reserve Statistical Release G.17, ECB Monthly Bulletins) shows that in the long term average only 80 percent of industrial capacities are used; and currently even less. In addition, the new demand created by \$ 100 billion needs to be compared with worldwide GDP of about \$ 60,000 billion. Assuming that, through multiplier effects, the global aggregate demand induced by the new SDR grows by \$ 300 billion, this corresponds to only 0.5 percent of worldwide GDP. Therefore it will be only a small part of normal growth of aggregate demand.

7. What happens if firms nonetheless react with higher prices to the new demand?

This is improbable. Most firms in industrialized countries need free capacities to deal with sudden changes of demand. So, they have space to first accommodate through higher production levels rather than higher prices. In addition, for firms subject to competition it is always risky to raise prices. In the midterm firms will need to regain their usual level of flexibility by increasing their production capacities. Raising prices are mostly a result of higher production costs or weak competition.

8. When the Green Climate Fund exchanges the new SDRs for national currency to finance concrete projects, the respective central banks need to issue new national currency. How can they mop up excess liquidity in case there is too much money in the market?

A central bank observing an excess liquidity can sell securities to soak up liquidity, or it can increase the reserve requirements for banks, i.e. the minimum amount of money banks have to deposit in their central bank accounts.

9. When the Green Climate Fund spends national currencies for concrete projects this money will be ultimately end up as deposits of banks. So, banks will receive new money without borrowing in the money market. What are the consequences?

Since banks receive new central bank money they will need less refinancing from their respective central bank. As a result the refinancing will be cheaper for the banking system, which corresponds to lower interest rates. Banks can provide cheaper loans to firms. If a central bank is afraid of overheating the economy it can mop up excess liquidity or increase the basic interest rate.

10. What happens if the banking system does not use the new central bank money to provide loans but, instead, to invest in financial capital markets and blow up asset bubbles?

The danger of new asset bubbles exists with or without new SDRs, especially since governments provided hundreds of billions of new liquidity to the banking system through quantitative easing. To curb excessive financial speculation is a matter of enhanced regulation.

11. What are the consequences for currency exchange rates?

Direct consequences are minor since SDRs are exchanged for different national currencies. In addition, compared to aggregate global trade in goods and currencies the amount of new money is small.

12. Why is it necessary to use SDRs at all, instead of national currencies?

SDRs are already accepted as a book keeping currency by 187 IMF member states. If one or a few national currencies would be singled out the danger of exchange rate volatility would raise.

13. The IMF (IMF; “Financing the Response to Climate Change”, March 25, 2010, SPN 10/06) and George Soros (George Soros; Special Drawing Rights proposal, Copenhagen, December 2009; Update 06.01.2010) have also made proposals to use SDRs as a funding tool. What is the difference to the WFC proposal?

The basic idea of the proposals of Soros and the IMF is to use part of the SDRs issued lately as a basis for a new Green Fund; and to attract private as well as institutional investors. The funding, therefore, is not debt free – in contrast to the WFC proposal. In the scheme proposed by Soros and the IMF the investments in climate protection need to deliver profits out of selling the saved carbon emission through a worldwide trade in carbon emissions. This would require substantially tightening the supply of carbon emission certificates which will be difficult to accomplish quickly on a global scale. The WFC proposal would kick-start the required investments immediately.

The World Future Council

The World Future Council brings the interests of future generations to the centre of policy making. Its up to 50 eminent members from around the globe have already successfully promoted change. The Council addresses challenges to our common future and provides decision makers with effective policy solutions. In-depth research underpins advocacy work for international agreements, regional policy frameworks and national lawmaking and thus produces practical and tangible results.

In close collaboration with civil society actors, parliamentarians, governments, business and international organizations we identify future just policies around the globe. The results of this research then feed into our advocacy work, supporting decision makers in implementing those policies.

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