Reward Governments, Not Projects

International incentives for national climate policy: section 4 in ten slides

Cash on the scale needed will not be voted. Pay instead in what the international system holds cheaply and governments value highly: balance-sheet strength, as guarantees on green borrowing, held by a trust and earned by policy.

Stephen J. Stretton · writing in a personal capacity

Cash rewards for national climate policy are too large to be voted

~$380bn

a year to pay $100 per tonne for a 10% cut in fossil CO_2 (37.8 Gt in 2024)

~$12.5m

the most Uruguay's flagship sustainability-linked loan can save its government

$1

of reward per donor dollar from a fund that pays out, and then it is gone

A guarantee saves the borrower the whole credit spread but costs the guarantor only its expected loss and the carry on its buffer.

Source: Global Carbon Budget 2025; World Bank (2023); papers 4.2 and 4.3.

Four routes to an incentive differ in what they cost the giver

Route	What the government gets	Cost to the giver	Paper
Policy crediting	Payment per tonne a policy cuts	Cash, per tonne	1.1, 6.1
Conditional de-risking	Guarantees for its clean power pipeline	Expected loss	3.1, 3.2
Sustainability-linked lending	A lower rate if targets are met	Forgone interest	4.3
Notional capitalized value + Trust	Guarantee capacity earned by policy	Expected loss and buffer carry	4.1, 4.2

Source: Section 4 overview, Table 1.

A climate balance that the carbon stock opens and emissions draw down

Opening balance: verified carbon stock times a low stock price.

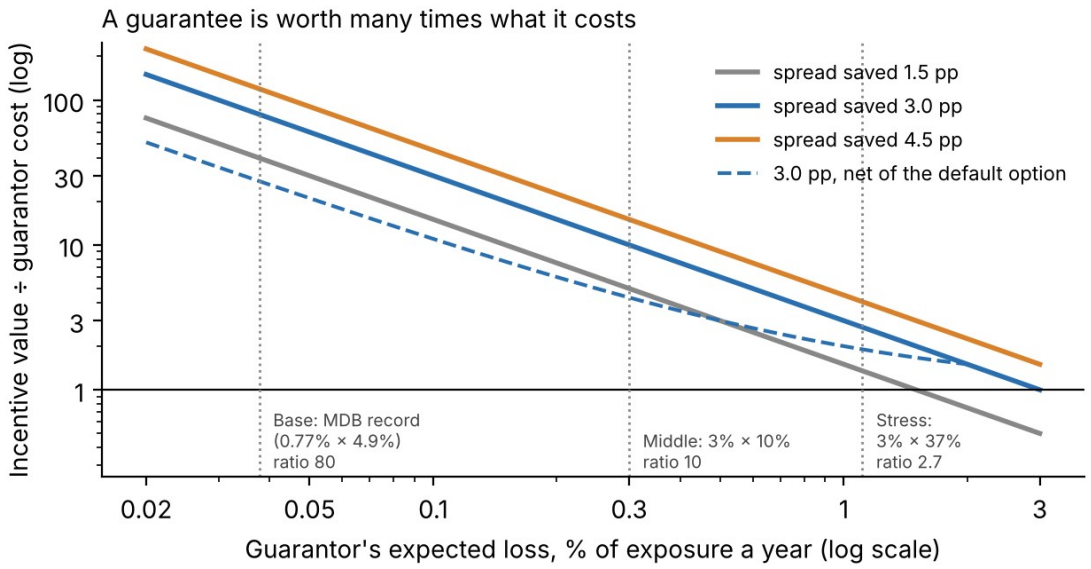
Each year: debited at a uniform price for every tonne above an allowance.

Never paid out: the balance caps the guarantees development banks provide on the country's green borrowing.

A forest country like Guyana: a $5bn balance saves $150m a year; about $30 per tonne at the margin if capacity binds.

Source: Paper 4.1.

A guarantee is worth many times what it costs the guarantor



Cost = expected loss (buffer earns the discount rate). Dashed: risk premium (a third of a 3 pp spread) plus expected loss.

Development banks' record: 0.77% default a year, 95% recovered: about $80 saved per $1 of expected loss.

Net of the default option: about $27 per $1.

Stress case, without preferred-creditor status: 2.7 (1.9 net).

Source: GEMs (2025); paper 4.1, Proposition 1.

A trust holds the capital behind the guarantees, and three conditions decide what it delivers

One pool, three jobs: second loss behind policy guarantees; co-investment in clean energy and first-loss funds; national accounts drawn after 2050.

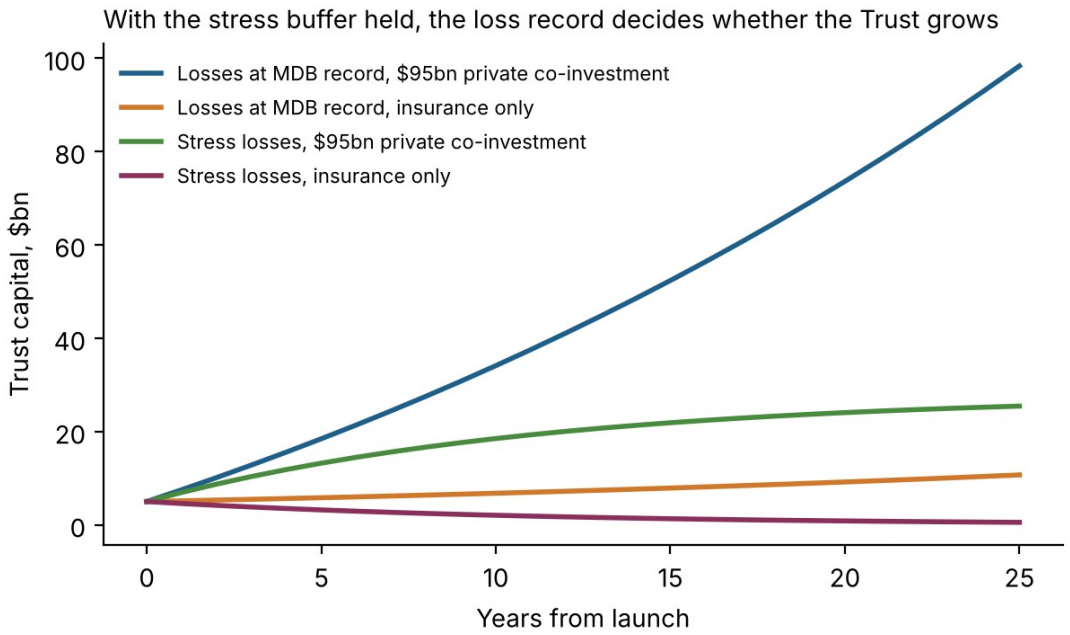
Preferred creditor: the base case needs the Trust's claims honored first; the practice is informal.

Carry: at 2%, pricing on the record while holding the stress buffer gives about 13 per dollar, not 80.

Liquidity: calls need cash; $5bn supports about $390bn, not $1tn, without a liquidity line.

Source: Paper 4.2, Proposition 1.

Holding the cautious buffer, the Trust grows on its own yield if losses follow the banks' record



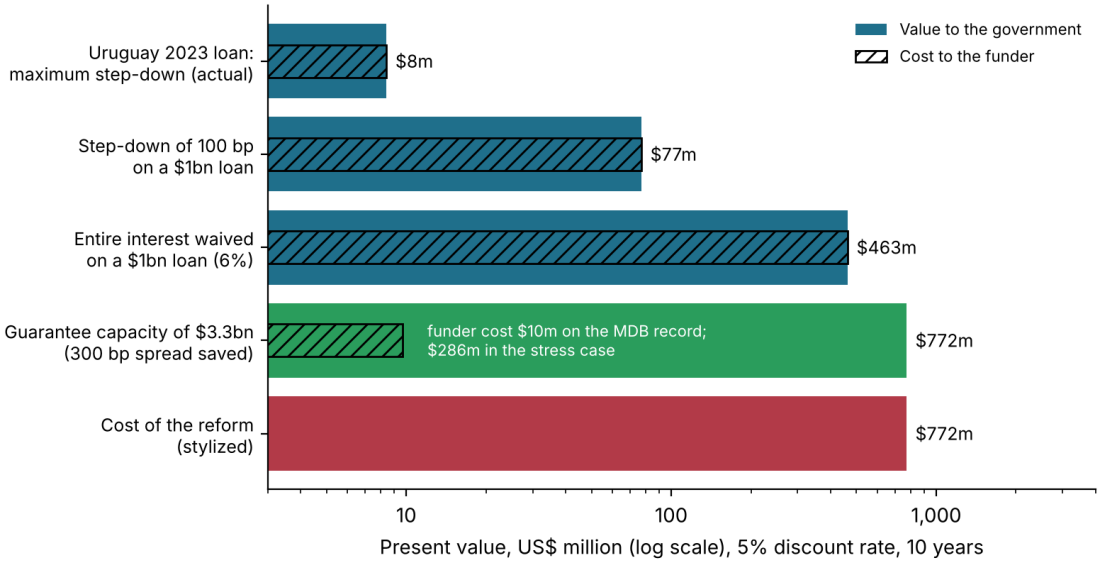
Record losses: grows about 3% a year with no fee.

Stress losses: shrinks about 8.5% a year without fees.

With $95bn co-investment (an upper case): about $34bn after 10 years.

Source: Paper 4.2, Figure 3.

Interest rebates are an order of magnitude too small; guarantee capacity is not



A 100 bp step on $1bn is worth $77m, against a $772m coal reform.

A market bond buys commitment, not money: the government pays for its own incentive.

Codify the loan, pay from outside, and make guarantee capacity the prize.

Source: Paper 4.3, Figure 1.

Pay a premium for acting now, and let the incentives build the capacity section 3 uses

The option to wait is valuable when clean technology is getting cheaper; an incentive must beat it.

Capacity that declines as technology costs fall halves the donor cost of inducing early action.

The sections compose: capacity earned under 4.1 can stand in 3.1's waterfall or behind 3.2's bonds; the Trust's regional funds hold 3.2's first loss.

Source: Dixit and Pindyck (1994); paper 4.1, Proposition 3; section 3.

What to do

What section 4 shows

Leverage: about $80 of interest saving per $1 of expected loss on the banks' record; 27 net; 2.7 in stress.

Conditions: preferred-creditor treatment, counted carry, a liquidity line.

Size: rebates are too small; guarantee capacity is the prize.

Actions

Development bank shareholders: rules-based guarantee capacity, allocated by notional capitalized value.

Donors and a development bank: launch the Trust as insurance first, holding the stress buffer, with a liquidity line.

Lenders: codify sustainability-linked loans and pay rewards from outside.