On the Potential of Sovereign State-Contingent Debt in Contributing to Better Public Debt Management and Enhancing Sustainability Outcomes

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Summary

- Propose an innovative public finance solution, SCDI, to help combat climate change and achieve a sustainable growth.
- Provide a comprehensive review of the existing types of SCDIs including instruments linked to macroeconomic and price variables, those linked to the occurrence of specified events, and those linked to the sustainability outcomes.
- Discuss the challenges of using SCDI to promote climate and sustainability objectives
# Measurement Challenge

## Methodology

**Activation and weighting system**

- 172 ESG indicators
- If an indicator covers less than 50% of relevant countries, i.e. it is not representative enough, the indicator is removed from the database
- Each indicator is weighted on a scale from 1 to 3 depending on the materiality of the following elements:

<table>
<thead>
<tr>
<th>Nature</th>
<th>Relevance</th>
<th>Exposure</th>
</tr>
</thead>
<tbody>
<tr>
<td>3</td>
<td>2</td>
<td></td>
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<tr>
<td>SIGNIFICANCE WITH REGARD TO THE SUSTAINABLE DEVELOPMENT GOALS</td>
<td>ADEQUACY OF THE INDICATOR AGAINST THE PERFORMANCE IT IS SUPPOSED TO MEASURE</td>
<td>STATE'S RESPONSIBILITY REGARDING CHANGES TO THE INDICATOR</td>
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- $< 6$ INDICATOR DEACTIVATED
  - $= 8$ or $9$ INDICATOR WEIGHTED AT 1
  - $= 12$ INDICATOR WEIGHTED AT 2
  - $= 18$ or $27$ INDICATOR WEIGHTED
Measurement Challenge: Can we narrow down to some quantifiable metrics?

- Environmental aspect can be an important starting point:
  - A country’s carbon emissions
  - A country’s alignment with the Paris Agreement to meet the 2 Degrees Celsius carbon budget

- The EU Taxonomy (Come in force in January 2022)
  - The EU taxonomy is a classification system, establishing a list of environmentally sustainable economic activities. It could play an important role helping the EU scale up sustainable investment and implement the European green deal. The EU taxonomy would provide companies, investors and policymakers with appropriate definitions for which economic activities can be considered environmentally sustainable.
While using SCDI to promote sustainability is still early stage, some guidelines would be helpful

- **Consider to**
  - Summarize the existing measurement systems
  - Highlight the differences across the systems
  - Point out ways standard setters could reconcile the differences and reach a consistent and transparent scheme to measure **contingency**

- **For example**, the European Commission (EC) adopted a measure that labels some nuclear and gas energy activity as climate-friendly investments. However, it set out strict, potentially limiting technical screening criteria for those activities to qualify, prompting pushback from the nuclear and gas industries.
Economic consequences of SCDI

- **Explore the market implications of SCDI**
  - Liquidity improvement due to the green preferences of global institutional investors
  - Pricing discount

- **Examine the real effects of SCDI**
  - Link the SCDI to its sustainability outcomes
  - For example, disaster resilience, carbon emissions reduction, overall country-level sustainability performance.