G20 Sustainable Finance Working Group Input Paper

Finance for a Just Transition and the Role of Transition Finance

Input paper prepared for the G20 Sustainable Finance Working Group under the Indonesian Presidency

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Executive Summary

Achieving climate goals requires a far-reaching economic transformation that entails extensive employment and socio-economic implications. Ensuring a just transition is a crucial enabler of ambitious climate action and an engine of sustainable development. Delivering a just transition means maximising positive employment and socio-economic outcomes and avoiding and mitigating any negative impacts. Financial systems and their actors have a key role to play in a just transition. They complement conducive policy measures, and in turn these policy measures facilitate the efforts of financial systems and their actors towards a just transition.

While market participants increasingly commit to climate action, the level of integration of social and employment dimensions of the climate transition in financing activities is currently lagging behind. The recognition of the need to address socio-economic impacts as an integral part of the decarbonisation process is only nascent. Progress is hampered by a lack of consensus around definitions of social risks and impacts and limitations in their representation in financial markets infrastructure (including standardization of social metrics and availability of processes and mechanisms focusing on social considerations). Although currently tailored largely to environmental goals, the sustainable finance market infrastructure does offer several entry points to simultaneously target positive climate and social outcomes of the transition. A comprehensive approach that embeds social considerations within practices of the whole ecosystem of actors involved in climate financing can improve the interoperability of practices, bringing about operational synergies and increasing the overall availability of capital.

This paper presents several social and employment-related elements to be factored into financial decision making to align it with the objectives of a just transition; it highlights some building blocks of the financial market infrastructure that could be enhanced by including social aspects so as to deliver systematic positive contributions to sustainable development goals; and it connects these building blocks with elements of emerging transition finance frameworks, for further research and discussion by the G20 Sustainable Finance Working Group and other relevant platforms.
1. Introduction

The present paper is produced as a contribution to the development of a Transition Finance Framework by the G20 Sustainable Finance Working Group, as well as to support other workstreams in reflecting social and employment considerations towards a just transition.

Ambitious action is needed to achieve carbon neutrality and climate resilience. The climate transition presents opportunities to diversify economies, create productive employment, and promote the expansion of sustainable enterprises. But it also involves challenges: job losses in certain industries, extensive restructuring, economic uncertainty for regions heavily dependent on fossil fuel extraction and power generation. In addition, climate change and environmental degradation themselves are driving employment losses, declines in productivity and threats to economic growth and poverty eradication.

A just transition maximises positive economic, social and decent work gains and minimises and mitigates negative impacts. It ensures change processes and outcomes are inclusive and fair. It is a necessary condition for delivering sustainable development in its three dimensions. It is also a critical factor for achieving ambitious climate action because it fosters broad-based support and strengthens coherent approaches.

Aligning financing with a just transition approach optimises positive contributions and prevents and addresses negative consequences. It is thereby instrumental in supporting the Sustainable Development Goals in an integrated manner.

Commitments around a just transition have been increasing among governments, enterprises, and the financial sector itself. A growing number of countries are making pledges for a just transition and have included objectives on decent work, green jobs and just transition in their Nationally Determined Contributions. Among financial actors, Multilateral Development Banks and private sector players are showing an increasing interest in just transition considerations.

Nevertheless, there are still significant gaps in systematically aligning financial flows with just transition objectives. First, challenges persist in identifying and tackling the social and employment components of the just transition agenda from a finance perspective because of a lack of consensus around definitions, limited standardisation of social metrics, difficulties in obtaining decision-useful data, emerging but still limited market recognition of the need to address socio-economic impacts of the decarbonisation process, immaturity of available processes and mechanisms focused on social parameters and the fact that social spending is often seen as a cost rather than an investment. Second, supporting a just transition goes beyond addressing business and financial risks. It involves managing change and restructuring in emission-intensive industries in a manner that avoids leaving workers, communities and local economies behind. It also implies a proactive approach to leveraging the social and employment dividends of the transition. Finally, it requires solid social dialogue between governments’, workers’, and employers’ representatives as well as effective stakeholder engagement processes. These challenges apply to sectors undergoing decarbonisation, which fall under the primary scope of transition finance, as well as to net-zero aligned and enabling activities that benefit from green financial flows.

Given the complexity and breadth of a just transition, it is essential to have a common understanding of the concept. This will enable all relevant actors to address the social and employment impacts of the climate transition and it will support the credibility of the measures they take. The ILO Guidelines for a Just Transition towards Environmentally Sustainable Economies and Societies for All (henceforth ‘ILO’s Just Transition Guidelines’), agreed by governments, workers’ and employers’ representatives provide a clear definition of the concept, key principles and a menu of policy options that can guide financing for a just transition and inform the work of the G20 Sustainable Finance Working Group (thereafter ‘SFWG’).

The paper is structured as follows: section 2 outlines the social and employment impacts of the climate transition. Section 3 presents the concept of just transition and the ILO’s Just Transition Guidelines. Sections 4 and 5 address the Just Transition Financing ecosystem, identify building blocks for supporting alignment of financial flows and highlight selected potential entry points relevant for the design of transition finance frameworks. The elements put forward in sections 4 and 5 aim to provide initial considerations, based on a review of literature and existing practice.
and drawing upon ILO's expertise, which ought to be further explored and could inform future developments on just transition financing in the context of the G20 SFWG and other relevant platforms.
2. The Social and Employment Impacts of the Climate Transition

Climate change is causing widespread losses and damage across world regions and its adverse impacts on economies and societies are increasing, including on water security and food production, health and well-being (IPCC, 2022). Economic losses span across climate-exposed sectors, including agriculture, forestry, fishery, energy, and tourism. Globally 1.2 billion jobs depend on healthy ecosystems and a stable environment. If the current global warming trends continue, 2.2 per cent of total working hours will be lost due to heat stress by 2030 (ILO, 2019b). This represents a loss of productivity equivalent to 80 million full-time jobs.

As a matter of urgency, the underlying causes of climate change need to be addressed, while societies need to adapt to the current and foreseeable climate change impacts.

The climate transition¹ presents opportunities as well as challenges. It offers the potential for large-scale employment creation and upgrading, cost savings and the opening of new markets and investment avenues for enterprises, as well as access to clean energy. Green building, electric vehicles, improved management of water resources, renewable energy, and waste management in cities in emerging markets hold a $29.4 trillion climate investment opportunity (IFC, 2018). A net gain of 18 million jobs can be achieved globally by 2030 through energy-related measures alone (ILO, 2018).

At the same time, the climate transition comprises a number of risks. Deep restructuring could leave workers and communities behind in certain sectors or localities. SMEs could face challenges to shift rapidly to new technologies and business models. Low-income consumers may be hit by increases in energy and commodity prices unless remediation measures are in place.

In terms of impacts on labour markets, there will several dynamics at play in addition to job creation and job displacement. They include, among others, changes in labour market composition, skills needs, wages and labour incomes, gender, and occupational health and safety.²

Benefits and costs associated with the transition will not necessarily be equitably distributed and certain groups may stand at a disadvantage. Occupational gender gaps are likely to stay, and women will only gain a fraction of the jobs created, unless adequate measures are taken to enhance female participation in the labour market and in green occupations in particular (ILO, 2018; IRENA, 2021). Workers and communities heavily dependent on fossil-fuel industries and whose economies present limited diversification and gaps in terms of social protection risk to be strongly affected.

There are multiple possible pathways to reach net zero emissions and achieve the climate transition (IPCC, 2021), with national goals, policies and processes depending on the specific economic and social priorities, vulnerabilities, capacities, and composition of the economy. Policy choices and the allocation of financial resources will influence to the extent and nature of employment and socio-economic impacts. Therefore, it is crucially important to involve those who will be impacted – workers, employers, communities – in the decisions to be made.

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¹ Responding to climate change involves both mitigation and adaptation measures. Both will have large-scale social and employment impacts that have to be addressed to deliver a just transition. However, given the context of the paper, the general focus of transition finance on decarbonisation, and the specific impacts of adaptation, which would require a separate discussion, the report will focus on the mitigation dimension of the climate transition.

² In the restructuring of economies and labour markets, the following misalignments may occur: “Temporal misalignments, which occur when job losses precedes job gains on a large scale”; “Spatial misalignments, which occur when new jobs are emerging in other communities or regions and are a challenge for people who lost their jobs and might have the right qualifications but have ties to the region where they live”; “Education misalignments, which occur when the skills levels or the occupation required by the transition have not been developed or needed under the previous system”; “Sectoral misalignments, which occur because of changing value and supply chains under the transition” (IRENA, ILO, 2021, p.62).
Sectoral perspectives

Sectoral dynamics will have specific employment and social impacts. This section presents a non-exhaustive illustration of impacts in a few sectors. The impacts of the transition will be felt across economies, including in sectors such as heavy industry, agriculture, and tourism.

Impacts of the transition in the energy sector

The energy sector is critical to the transition. Together, electricity and heat production, transport, and buildings account for around 73 per cent of global GHG emissions. The energy transition presents considerable potential in terms of employment generation and other social and economic benefits, but also brings disruptive effects that need to be addressed.

Nearly 24 million jobs will be created through energy-related policies and investments, notably with net employment growth in the renewable energy sector, in manufacturing and construction. The latest study by IRENA conducted in collaboration with the ILO shows that similar trends are likely to continue until 2050: “the energy sector as a whole will grow to 122 million [jobs] in 2050 under the 1.5°C pathway, compared with 114 million under current policies and pledges. As is the case today, solar will make up the largest share of renewable energy jobs in 2050, with 19.9 million jobs, followed by bioenergy (13.7 million), wind (5.5 million) and hydropower (3.7 million)” (IRENA, ILO, 2021). However, 6 million jobs are expected to be lost globally through the energy transition by 2030, mainly in fossil-fuel-related sectors (e.g. mining and coal extraction, petroleum and natural gas, fossil-fuel based automotive industry).

Many of the jobs lost can be reallocated. We estimate that 5 million workers who will lose their jobs due to contraction in specific industries will be able to find jobs in the same occupation in another industry within the same country. Yet, irrespective of efforts towards the reallocation, between 1 and 2 million jobs will be lost without equivalent vacancies arising in other industries.

Notes:
1 World Greenhouse Gas Emissions in 2018 data provided by the World Research Institute
2 Notes: Percentage difference in employment outcomes between the IEA 2°C and 6°C scenarios by 2030 (ILO, 2018)
Furthermore, the transition from fossil fuel power generation to renewable energies will imply changes in value and supply chains. For example, phasing out fossil fuels and moving towards renewables such as solar energy will imply inter alia a shift of inputs from fuel extraction to semi-conductor materials. If both inputs are domestic, the shift will take place from one industry to another, and employment creation will depend on labour productivity. If a new solar panel value chain heavily depends on imports, employment creation will move to the country that supplies the intermediary inputs (IRENA, ILO, 2021).

Lastly, socio-economic impacts will be felt most strongly at the subnational level. With structural dependencies on the coal-producing industry and coal consuming sectors (power, cement, etc.), coal regions are facing specific challenges related to the changes of the local economy.

### Companies and the energy transition: emerging efforts in tackling employment and social impacts

While coherent public policy is a driving force for Just Transition, it also needs to be operationalised at company level. Initiatives that seek to address employment and social implications of decarbonisation measures are emerging.

**Ørsted**, a Danish energy company may serve as an illustration. Once one of the most coal-intensive energy companies in Europe, Ørsted has set the ambition to become CO2 neutral by 2025. In 2020, Ørsted signed an agreement with North America’s Building Trades Unions (NABTU) to move construction workers into the offshore energy industry. According to NABTU, labour unions have been wary of a rapid transition to renewable energy over concerns it will lead to a net loss of middle-class, career-sustaining jobs. However, NABTU and Ørsted have jointly agreed on a plan to transition the workers into the new jobs ensuring decent pay and social protection. NABTU represents more than three million tradespeople from 14 companies. Ørsted and NABTU collaborate to help train workers and expand career pathways in the offshore renewable energy.

Another example may be found in **Enel**, an Italian multinational in the electricity sector, employing 62,080 people, [which] has set a science-based CO2 emissions target and has committed to decarbonize its energy mix by no later than 2050. As part of its decarbonisation plan, Enel planned to close 13 GW of thermal power stations in Italy while expanding renewable energy, demand management and other measures. It worked with local government, business, and communities where the thermal plants are located to develop plans for new economic development post-closure. Enel also agreed a Global Framework Agreement with its sector global unions and a just transition agreement with its Italian unions which covers issues related to recruitment plans, training and skilling, early pension or professional mobility (Just Transition Center, the B Team, IP2018).

### Impacts of the transition in waste management and the circular economy

While the circular economy is an issue distinct from the climate transition, there are important ways in which the shift to circularity can support climate goals, especially through waste management, efficiency gains and waste-to-energy options. Waste accounts for 3.2 per cent of total global carbon dioxide (CO2) emissions with wastewater contributing 1.3 per cent and landfills 1.9 per cent5.

Through measures towards a circular economy, a net global gain of more than 7 million jobs will be generated by 2030. But while nearly 78 million jobs will be created, almost 71 million will be lost. A large proportion of those – nearly 49 million – can be reallocated, but nearly 22 million will be displaced without vacancies in the same occupation opening up in other industries (ILO, 2018). At the sectoral level, employment gains will be led by growth in services and waste management while losses are expected in mining and manufacturing. This can be largely explained by the replacement of the extraction of primary resources and the production of metals, plastics, glass, and pulp by the recycling and reprocessing of secondary metals, plastics, glass, and pulp.

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5 Ibid p.6
Impacts of the transition in land transport

Land transport is an important sector for the economy and the climate transition. It accounts for around 12% of global carbon dioxide (CO2) emissions while employing over 60 million workers globally. The transition in transport will have significant impacts on labour markets. As a way of illustration, an accelerated shift towards greener transport as part of the post-COVID-19 recovery could create in net terms up to 15 million jobs worldwide by 2030. At the global level, if half of all newly produced vehicles are electric, 10 million additional net jobs could be created, and almost 5 million new jobs could be generated through investment in public transport (UNECE; ILO, 2020).

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6 Percentage difference and percentage point difference in employment outcomes between the circular economy scenario and the IEA 6°C scenario by 2030 (ILO, 2018).
7 Ibid p.6
3. Ensuring a Just Transition to Achieve Climate and Sustainable Development Goals

The notion of a just transition is central to achieving climate targets along other sustainable development goals. If climate action is to be carried through and have the level of ambition required to avoid disastrous consequences to human societies and economies, it must take into account concerns over economic growth, inequalities, unemployment and other decent work deficits, and access to clean energy. Not doing so means failing legitimate aspirations to development. It is also likely to undermine bold commitments, acceptance of policy measures and the ability to mobilise a wide range of actors towards shared objectives. **It is therefore a key instrument to promote sustainable development** because at its very core it recognises the interdependencies between the three dimensions of sustainability.

In addition, the notion of just transition captures both the **outcome** of achieving carbon neutral climate resilient economies while delivering decent work and social justice, and the **process** to drive the shift to sustainability, acknowledging that the process fundamentally shapes the outcome.

As the outcome includes the pursuit of decent work and social justice, the process needs to include actors from the world of work and other stakeholders who are affected by the transition.

The ILO’s **Guidelines for a Just Transition towards Environmentally Sustainable Economies and Societies for All**, henceforth ‘the ILO’s Just Transition Guidelines’ provide the key international framework on just transition. The ILO’s Just Transition Guidelines outline principles and entry points across different policy fields. They were formulated by governments, workers’, and employers’ representatives from across world and enjoy broad-based support.

The ILO’s Just Transition Guidelines acknowledge that the transition presents economic and social opportunities while also bringing about challenges. Promoting a transition that is just is about acting on both fronts. This means identifying and maximising win-wins: optimising employment gains, leveraging opportunities for job upgrading and skills development, and ensuring benefits of the transition are widely and equitably shared. It also means addressing challenges in the form of potential negative impacts: minimising and mitigating employment losses, protecting vulnerable groups, offsetting the implications for consumers, especially those living in poverty.

While recognising that **no one size fits all**, the ILO Just Transition Guidelines set out elements that are central to a just transition:

**Strong social consensus**: social dialogue involving workers’ and employers’ representatives provides a basis for policy and decision-making, mobilises support, and helps to inform plans and policy instruments and projects relevant to needs. Given the far-reaching and diversified impacts of the transition, engagement with other stakeholders is an important aspect of just transition processes to voice concerns and generate inclusive solutions.

**Rights**: a just transition ensures that fundamental principles and rights at work are respected and promoted. This means upholding the elimination of child labour and forced labour, non-discrimination in employment and occupation, equal remuneration, freedom of association and the right to organise, and collective bargaining.

**Gender**: climate change affects women and men in different ways and so do climate change responses. Deliberate attention to differential impacts between women and men needs to cut across just transition instruments and may also require targeted support policies.

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Policy coherence: Climate action cannot rest solely on climate policies. If policies go in different directions, they limit impacts and cause inefficiencies. Delivering a just transition means aligning goals and instruments. This is also key to providing clear and stable policy signals to leverage private sector action and investment.

Just transition frameworks or plans provide a strong basis for policy coordination. They need to be based on anticipation. Quantifying and qualifying the impacts of the shift to sustainability in terms of employment and social outcomes is necessary to adequately plan for the transition, and address opportunities and challenges with sound policy measures. It is also important for monitoring and evaluation and for accountability.

Given the extent of the effort needed to achieve climate goals, action is needed across policy fields. The ILO’s Just Transition Guidelines highlight the relevance of alignment in macroeconomic policies, sectoral strategies, employment, enterprise development, skills and other labour market policies, social protection, occupational health and safety, rights, and social dialogue.

Macroeconomic and growth policies are vital to orient much needed investments towards sectors and economic activities that support mitigation or adaptation while maximising employment dividends and ensuring adequate support for the negatively impacted. Defining long-term financing needs and financing strategies for just transition plans is necessary for ensuring implementation and results at scale. Environmental tax reforms can contribute to funding compensation for those disproportionately impacted. Increasing public and private capital flows to green sectors that are employment-intensive or have strong backward linkages can stimulate job-rich growth and the shift to low-carbon economies.

Sectoral strategies can align with decarbonisation pathways, map the sectoral transformation in terms of impacts for enterprises and workers, skilling and reskilling needs, and gaps in terms of labour standards. Such strategies would be important both in the context of expanding green sectors (e.g. renewable energy) but also for emission-intensive ones.

Enterprise development measures tap into the role of the private sector in advancing a just transition and foster an enabling environment. They need to be fully responsive to the diversity of enterprises and the specific needs of SMEs, especially when it comes to access to finance and technology to support adoption of cleaner production methods, entrance into markets for green products and services, and climate resilience.

Skills development aligned with the skill needs emerging from the transition is key both to enabling climate action, sector growth and the uptake of clean technologies, but also to materialising job opportunities for new entrants to the labour markets and displaced workers.

Active labour market policies support workers, enterprises, and regions in navigating changes in labour markets resulting from the transition, help to match labour demand and supply and include employment services for negatively impacted workers.

Social protection systems fit to address climate risks and to protect those impacted from response measures play a vital part in shielding the vulnerable from negative impacts and in supporting the transition to alternative employment opportunities. With over 4.1 billion people lacking even a minimum level of protection to shield them from shocks, expanding coverage is a pressing challenge (ILO, 2021).

Occupational health and safety measures reduce risks and impacts of climate change at the workplace and prevent, minimise and address risks that emerge in expanding green sectors or through the development of new technologies and processes.

Commitment and action on just transition has been growing since the 2015 Paris Agreement and the 2015 ILO’s Just Transition Guidelines. At the 2019 UN Climate Action Summit, 46 countries signed just transition commitments and the Climate Action for Jobs initiative was launched. The Global Accelerator on Jobs and Social Protection for Just Transitions is providing further momentum in international cooperation in this field. Several countries have included references to decent work and just transition in their NDCs, embedded just transition planning and

\[ A \] clear illustration comes from skills development. If climate policies or investments do not take into account skill requirements, they will be hampered by skill shortages and opportunities for jobs in the local economy will not materialise. Policy coherence is still uneven across countries and policy area. In the first round of NDCs, less than 40 per cent of NDCs include training and skills development (Skills for a Greener Future: a global view, ILO, 2019). Similarly, out of 57 countries with adopted employment policies, only 11 took into account environmental sustainability considerations (ILO 2017).

\[ 10 \] see [https://www.climateaction4jobs.org/](https://www.climateaction4jobs.org/)


\[ 12 \] These include: Albania, Algeria, Andorra, Argentina, Armenia, Benin, Bolivia, Cabo Verde, Costa Rica, Côte d’Ivoir, Croatia, Dominican Republic, Finland, France, Germany, Ghana, Greece, Guatemala, Guinea, Honduras, Hungary, Ireland, Italy, Jamaica, Luxemburg, Mali, Mexico, Montenegro, Morocco, Netherlands, New Zealand, Nicaragua, Nigeria, North Macedonia, Panama, Peru, Poland, Republic of Korea, Romania, Samoa, Senegal, Serbia, Spain, Sweden, Ukraine, United Kingdom, United States, Uruguay
consultation in high level policy processes\textsuperscript{13}, or are taking measures at subnational level. Companies, especially in the energy sector, have also started to adopt a just transition approach when they embark in change processes linked to their decarbonisation paths. It is still early days in the uptake of just transition, but it is a critical time to give effect to commitments and scale up progress.

\textsuperscript{13} See e.g. South Africa
4. The Role of Finance in Supporting the Climate Transition

Sustainable Finance and its readiness for a just transition

Sustainable finance markets have evolved over the last decade. What started as responsible finance and paying attention to “do no harm” while continuing to earn competitive financial returns, soon expanded to financing businesses under consideration of Environmental, Social and Governance (ESG) risks and opportunities. Moving beyond “do no harm” and intentionally seizing positive social or environmental impacts is at the core of sustainable finance markets for businesses, investors and governments as illustrated in Figure 3.

*Sustainable debt annual issuance*

Illustrating the rising awareness of the need to decarbonize high-emitting industries, bonds explicitly labelled as Transition Bonds were first issued by companies in 2020 (CBI, 2021). This label attracted interest from highly polluting companies largely absent from the green bonds markets. However, it is argued that transition-labelled instruments have so far failed to take off due to the absence of a clear definition of transition and investor scepticism about potential greenwashing (BloombergNEF, 2022).

Very recently, Sustainability-Linked Bonds (SLB) have emerged (CBI, 2021). The International Capital Market Association defines SLBs as any type of bond instrument with predefined sustainability or ESG objectives. Entities that issue SLBs can set key performance indicators (KPIs) which are aligned with their sustainability strategies. High-emitting sectors, whose decarbonization is key to a successful economy-wide transition, are far more prominent within sustainability-linked bonds market compared to the green bonds segment (CBI, 2021).

Despite some level of recognition of social impacts, the sustainable finance market still focusses on environmental objectives and outcomes. Most asset managers who use ESG factors in their investment analysis continue to concentrate on the “E”, or climate change, as their leading criteria for their decisions (BNP Paribas, 2021). BNP Paribas Global ESG survey 2021 reports 51% of the respondents citing social as the most challenging component to assess and incorporate into their investment analysis.
These challenges relate to the breadth, interconnectivity, and complexity of social matters, including labour-related ones. It is further fuelled by the lack of agreement, and to some extent even awareness, among market participants on definitions and meaningful measurement methodologies as well as lack of standardization of social metrics and related challenges in obtaining relevant, quantifiable, and decision-useful data. In addition, as opposed to decarbonisation targets, the nature of social impacts goes beyond purely risk-driven considerations. It includes behaviours that can bring about positive effects both for society and for business performance.

However, the financial sector is ready and willing to support the sustainable development goals and just transition objectives (GFANZ, 2021). Governments can leverage this willingness with an appropriate enabling environment and regulatory frameworks that speak to jointly achieving positive social and environmental impact alongside positive financial returns.

**What do economic and social impacts of climate transition mean for capital providers?**

The transition to a low-carbon economy and the resulting socio-economic and employment impacts are also affecting the realities in which capital providers operate.

On the one hand, capital providers play an important enabling role in transitioning to sustainable low-carbon economies. In allocating capital away from businesses with emission intensive activities to businesses aligned or transitioning towards net zero, financial institutions can actively drive the low-carbon transition. At the same time, financial institutions' own business activities and future development perspectives depend on the overall progress of the transition process and its eventual outcomes. These new realities pose both risks and opportunities that capital providers need to consider.

On the risk side, the financial institutions face *climate change-related risks* such as acute or chronic physical risks related to climate events or longer-term physical consequences of climate change resulting in losses; transition risks related to the economic consequences of an unanticipated transition towards a low-carbon economy or regulatory changes, leading to a sharp depreciation of the exposed assets; liability risks related to damages caused by global warming.

In addition, both climate change and the low-carbon transition have economic and social implications (including employment-related ones). If the risk of potential negative impacts on workers, enterprises, consumers, or communities is not considered, it can result in operational and supply chains disruptions, changes in demand for goods and services, or deterioration of local economies which in turn influence the health of financial institutions themselves and their ability to continue offering financial services.

On the opportunity side, the climate transition opens up new business and investment options. These opportunities emerge across primary, secondary, and tertiary sectors, and across geographies. Examples include fast-growing areas of green infrastructure, innovative industries built around new technologies and regions home to positive transition trends. Financial institutions can benefit from transition dynamics by providing innovative products and solutions for zero and near zero emitting businesses but also supporting emission-intensive companies to substantially lower emissions and accompanying affected populations with responsive and climate transition-aligned financial instruments.

Adopting a just transition lens to assessing and addressing social and economic implications of the climate transition allows capital providers to effectively navigate the transition challenge, mitigate the inherent risks and benefit from emerging business opportunities.
5. Finance for a Just Transition

Transition dynamics and their employment and social dimensions

The climate transition will include two kinds of dynamics, both of which require financing: on the one hand, expanding zero and near-zero emitting activities; on the other hand, enabling the progressive reduction of emissions in high-emitting and hard-to-abate activities, which will require extensive changes in technology, processes, and business models, complemented by phasing out of activities incompatible with climate goals. In both dynamics, social and employment impacts come into play.

Zero and near-zero emitting activities may still present risks, if, for example, the human capacities or skills to enable the transition are absent, or if human and labour rights are not respected. They may also bring less than optimal co-benefits, for instance in terms of impacts on employment or productivity gains, and linkages with SMEs and the local economy.

Changes and restructuring in high-emitting and hard-to-abate activities also involve a range of implications: they may lead to displaced workers, stranded assets, and marginalised regions and entail missed opportunities in terms of employee retention and skill upgrading. Systematically factoring in such risks and opportunities is central to a just transition approach. An illustration of social and employment considerations relevant to the transition is provided in the tables below.

Table 1: Examples of social and employment impacts that need to be considered to support a just transition

<table>
<thead>
<tr>
<th>Jobs created and displaced (direct, indirect, induced)</th>
<th>Impact on those living in poverty (e.g. via employment impacts, increases in prices)</th>
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<tbody>
<tr>
<td>Risks/gaps related to respect of human rights</td>
<td>Geographical impacts (e.g. regions that stand to disproportionately lose from the transition)</td>
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<tr>
<td>Risks/gaps related to respect of labour rights</td>
<td>Impacts on indigenous peoples</td>
</tr>
<tr>
<td>Risks/gaps in terms of occupational health and safety</td>
<td>Impacts in terms of public services/ infrastructure (e.g. via losses in local government revenues)</td>
</tr>
<tr>
<td>Changes within occupations (content, skills)</td>
<td>Impacts on the local environment and community health</td>
</tr>
<tr>
<td>Wages, working conditions, social protection in newly created jobs</td>
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<tr>
<td>Gendered impacts (job created, job losses, wages and working conditions)</td>
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Table 2: Elements to be considered to track progress on just transition in terms of institutional arrangements and actions

<table>
<thead>
<tr>
<th>Mechanisms for social dialogue (which provide the basis for all other actions)</th>
<th>Coverage and level of social protection and contribution to social protection by enterprises</th>
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<tbody>
<tr>
<td>Arrangements for stakeholder engagement processes (to inform other actions)</td>
<td>Conversion of assets</td>
</tr>
<tr>
<td>Just Transition plans based on social dialogue and taking into account various impacts of the transition, including gendered ones</td>
<td>Job-rich economic diversification measures, including place-based investment plans for hard-hit regions</td>
</tr>
<tr>
<td>Measures to ensure full respect of labour and human rights</td>
<td>Measures in green investments that support local hiring, and link with local suppliers/service providers</td>
</tr>
<tr>
<td>Retraining schemes and their coverage</td>
<td>Use of revenues from environmental taxes or of fiscal space from fossil fuel subsidy reforms for social transfers to alleviate negative impacts and support human-centred investments (social protection, skills development, career guidance) and incentives for low carbon activities and decarbonisation strategies (for national/regional level transitions).</td>
</tr>
<tr>
<td>Retention and redeployment schemes and their coverage</td>
<td></td>
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<tr>
<td>Early retirement schemes and their coverage</td>
<td></td>
</tr>
<tr>
<td>Support to displaced workers in terms of skills upgrading or retraining, business development services, finance for business start-ups.</td>
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</tbody>
</table>
Levers available to financial ecosystem players to support a Just Transition

A range of financial ecosystem players are essential to ensure that capital flows are supportive of a transition that delivers social and employment gains. This ecosystem typically includes the government and regulatory authorities that set the rules of the game, develop policies, and allocate public funds. Industry support services help translate these rules into practice and build capacity of capital providers to adhere to the rules while capital providers arrange allocations through which they allow businesses to implement their business plans and serve clients.

Governments, through their policies, regulations, and international engagements, have a leading role in planning, designing policies, incentive mechanisms and public investment that are aligned with a just transition. Public authorities can integrate employment and social impacts of the climate transition in public finance strategies, through supportive macroeconomic, growth and fiscal policies, targeted allocation of public funds, and incentives for private sector co-investment. An emerging avenue that could play an important role in just transition financing concerns the use of revenues from carbon pricing and carbon markets to fund measures to address the social and employment impacts of decarbonisation.

Given the scale of the climate transition and a finite amount of public finance, an efficient combination of different public and private sources of funding is crucial, as is development finance for developing countries. Policy uncertainty represents a major risk factor for private sector actors and capital providers. To incentivise just transition, governments have an essential role to play in providing long-term policy visibility and stability, as well as a supportive regulatory environment. In their regulatory capacity, they can contribute to promoting transparency around the socio-economic impacts of low-carbon transition strategies via appropriate disclosure requirements and enforcing accountability of ecosystem players. Central banks as well as financial supervisors can increase their efforts to manage the risks posed by climate change to financial and monetary stability and thus can further explore their role towards enabling the financial system to support the just transition (LSE, 2021).

Removing knowledge barriers among the various stakeholders of the climate transition can increase collaboration, produce synergies, and improve the overall effectiveness of a common response to the numerous social challenges of the climate transition. Given the complexity of just transition issues, international organisations and relevant standard setters are well positioned to generate this common understanding as well as frameworks and can provide guidance and technical assistance.

Capital allocation decisions of financial service providers have a major role in supporting the climate transition. Net-zero alignment strategies, in which the financial sector has engaged alongside real economy actors, also provide opportunities for simultaneously maximizing the positive transition effects on people and communities. Emerging frameworks focusing on investor strategies (LSE, 2021) offer a rationale and an initial guidance on integrating the social dimension of the net-zero transition across investment activities. Research indicates that sustainability strategies of private sector banks can provide avenues for managing social impacts alongside with the climate targets (Clifford Chance et al, 2021).

Due to their development mandate, International Finance Institutions are well-positioned to champion the integration of social considerations in financing activities, including climate-related ones. Many Multilateral Development Banks' (MDBs) operational strategies touch upon at least some core aspects of a just transition and some have begun to explicitly target a just transition (Vivideconomics, 2021).

Mainstreaming the assessment and integration of social and employment impacts in Climate Funds, such as the Green Climate Fund and the Global Environment Facility, and developing targeted just transition financing windows in these funds would allow further expansion of the asset base and a better exploitation of the transformational potential of climate finance.

Enterprises are at the forefront of the climate transition. Their actions are also critical in ensuring a just transition and in creating sustainable value for investors and other stakeholders (Council for Inclusive Capitalism, 2021). Developing and implementing just transition plans as well as measuring and reporting progress are crucial elements to achieve the transparency and accountability that investors and other stakeholders increasingly look for (The B Team et al, 2018). Plans at company or national level need to be grounded in social dialogue with trade unions and in stakeholder engagement processes to ensure the voice of those directly impacted (JTC, 2017).
Table 3: Levers available to financial ecosystem players to support a Just Transition (based on literature review)

<table>
<thead>
<tr>
<th>Stakeholder</th>
<th>Levers available to support a Just Transition</th>
</tr>
</thead>
</table>
| Governments | ❖ Provide stable policy signals and regulatory frameworks to companies and capital providers to steer capital allocation towards a just transition.  
❖ Develop Just Transition plans basing on social dialogue and stakeholder engagement.  
❖ Develop integrated national financing frameworks (INFFs) explicitly addressing just transition considerations.  
❖ Mainstream just transition provisions in macroeconomic, regional development, social protection and educational policies and budgets.  
❖ Collaborate on policy development across local, regional and state government levels.  
❖ Establish policies and incentive mechanisms for private sector companies and financial institutions to avoid and mitigate negative social and employment impacts and maximise positive ones.  
❖ Promote dedicated just transition funds and de-risking mechanisms to attract additional private sector capital.  
❖ Align public finance strategies with the imperatives of a Just Transition (LSE, 2021). |
| Central Banks | ❖ Support government’s economic policy via just transition aware financial and prudential regulation, disclosure requirements and monetary policy and portfolio management.  
❖ Connect financial stability and employment objectives to the climate risk and net-zero agenda (LSE, 2021). |
| International Organisations / Standard Setters | ❖ Provide support to strengthen transition finance frameworks to support a just transition.  
❖ Promote metrics to measure social and employment effects of the climate transition.  
❖ Provide technical assistance to governments and other ecosystem players to reduce knowledge and capacity barriers. |
| Private Sector Financial Institutions (and Asset Owners) | ❖ Integrate just transition aligned approaches in their strategies and operations.  
❖ Support just transition aligned strategies in public finance by allocating some assets to public debt instruments dedicated to addressing local transition issues.  
❖ Participate in local, regional, and national dialogue about decarbonisation and just transition.  
❖ Collaborate with local, regional, and national governments, clients, and other partners, and develop financial products and non-financial services that support a just transition.  
❖ Increase capital allocated to support transition activities and collaborate with other stakeholders to mobilise additional resources for activities and communities in transition.  
❖ Engage and incentivise companies to effectively assess, plan and implement just transition aligned behaviour. |
| International Financial Institutions | ❖ Factor in social and employment impacts in financing decisions and results-frameworks.  
❖ Share development finance institutions’ experience and knowledge to promote adoption of just transition approaches by other types of financial institutions.  
❖ Leverage development finance to crowd in private capital for just transition aligned projects. |
| Climate Funds | ❖ Factor in social and employment impacts in financing decisions and results-frameworks.  
❖ Leverage the transformative potential of climate finance to intentionally support just-transition aligned projects.  
❖ Provide for dedicated windows to finance projects addressing a just transition. |
| Trade Unions | ❖ Provide a collective voice for workers impacted by climate change and transition measures.  
❖ Engage in social dialogue and play active role in policy design and implementation and evaluation of social and employment outcomes.  
❖ Engage in social dialogue to inform company-level just transition plans and implementation.  
❖ Explore just transition aligned approach for affiliated workers retirement saving plans. |
| Civil Society | ❖ Engage with government, businesses, and capital providers about transition related challenges to inform policies and national and company-level just transition plans. |
| Business | ❖ Engage with potentially affected workers, communities, and other stakeholders.  
❖ Develop and implement company-level just transition plans based on social dialogue and measure and report progress using for example impact assessments. |

The climate transition in each country will be a function of its unique domestic economic structure, priorities, stage of climate transition as well as capacities (OECD, 2021). These unique socio-economic circumstances will influence the path, the speed, and the ambition of the climate transition. Associated social considerations will equally differ among the countries. Therefore, a “one size fits all” approach will not work. However, interoperability of approaches among the different stakeholder types and across geographies is crucial for coordinated and impactful action.
The complementarity of expertise, roles, and constituencies of different actors should be built upon to establish partnerships, which are of vital importance for effective mobilisation and allocation of financial resources to attain results at scale, for sharing good practices and for strengthening capacities. For instance, cooperation programmes involving MDBs and specialised international organisations could be established to provide all-round financing and technical assistance packages to developing countries. Ways to leverage private sector financial commitments, such as just transition pledges by the members of the Glasgow Financial Alliance for Net Zero (GFANZ) should also be explored, including avenues to strengthen synergies with public sector resource mobilisation and a conducive policy environment at the national level. The ILO can contribute technical support and is ready to engage in partnerships leveraging its expertise on just transition and on employment, social and labour policies and investments and their nexus with climate goals.

Making Transition Finance Supportive of a Just Transition: Selected Building Blocks

In recent years, several countries as well as public and private sector financial institutions have issued Transition Finance frameworks. Government frameworks aim to define, regulate, and include transition economic activities in the scope of sustainable finance. Financial institutions and other market participants describe their philosophies and nascent approaches to financing companies engaged in decarbonization (Annex). The scope of some frameworks is specific to transition finance, others are broader and cover the transition concept as a part of green finance.

Most frameworks define transition finance as finance intended for high-emission and hard-to-abate economic activities important for future socio-economic development for which viable green alternatives are either not available or are not ready to be widely deployed. The objective of the transition is emissions reduction (OECD, 2021).

Our analysis and other reviews (LSE 2022; OECD 2021) find that at present social considerations, including employment impacts, are either not included or not sufficiently well articulated in transition finance frameworks, even though these can provide an important avenue for addressing such issues. This holds true for transition finance frameworks of both governments and financial sector players. Only some of them explicitly require the financier or the financed activities to adopt social safeguards and prevent negative social externalities (EU, Singapore, AXA IM, ICMA), but they do not provide guidance on how this should be achieved (OECD, 2021). Other frameworks do not explicitly mention any social aspect of the net-zero transition.

To support a climate transition that is just, clear guidance is required on the relevant social and employment factors and their interactions with climate goals. The Transition Financing Framework, being developed by the G20 Sustainable Finance Working Group members in 2022 presents a valuable opportunity to leverage the momentum of the emerging transition finance movement and its potential for mobilizing capital to deliver a shift to carbon-neutrality that generates positive social and employment outcomes.

The notion of a just transition connects the dots between governments’ climate and social policy objectives, the three pillars of advanced ESG finance thinking as well as impact investing. Many elements of existing financial sector and corporate sustainability practices provide room for embedding just transition-oriented building blocks and mainstreaming assessment and management of socio-economic impacts alongside with targeting low-carbon transition.

The basic but fundamental elements, such as scope, definitions, metrics, and materiality of socio-economic impacts of the low-carbon transition are universal and versatile. They can be adapted to various sectoral and regional transition pathways.

As of today, full-fledged guidance on addressing just transition challenges in transition finance, as outlined above, is not readily available (LSE, 2022). However, several social and labour considerations are addressed by a relatively scattered set of issue-specific frameworks. This accumulated body of practice and evidence can be built upon for designing integrated frameworks, accounting for a variety of just transition-related factors as well as their interactions. Table 4 provides initial considerations on potential building blocks, that emerge from the review of these frameworks, and presents some relevant resources and initiatives.
Table 4: Potential building blocks for accounting for socio-economic impacts in transition finance frameworks

<table>
<thead>
<tr>
<th>Building Blocks</th>
<th>Description</th>
<th>Actors Involved</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Scope, Definitions, Metrics, Principles</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Scope of just transition</td>
<td>Clarify common scope of just transition based on the ILO’s Just Transition Guidelines</td>
<td>International Organizations, Governments, Trade Unions, Communities</td>
</tr>
<tr>
<td>Definitions of socio-economic transition related risk factors and impacts as well as vulnerable populations</td>
<td>Create consistency via common definitions of socio-economic risks and impacts (both positive and negative) relevant for and aligned with just transition priorities (IRSG, KPMG, 2021) as well as clear definition of the affected populations.</td>
<td>International Organizations, Governments, Trade Unions, Communities</td>
</tr>
<tr>
<td>Mapping of socio-economic transition related risk factors and impacts as well as vulnerable populations</td>
<td>Establish sector and region-specific impact materiality matrices to identify most prominent impacts (positive and negative) and exposed population groups. Mapping enables prioritization.</td>
<td>Governments, International Organizations</td>
</tr>
<tr>
<td>Metrics and indicators to measure socio-economic transition impacts and contribution to just transition objectives</td>
<td>Compile a menu of measurable, collectable and decision-useful metrics and indicators. The menu can be used for different elements of corporate and financial decision-making including project design; disclosure requirements of companies, financial institutions, and public sector; financial instrument standards, labels, and certification schemes; credit and ESG ratings methodologies and benchmarks; due-diligence, risk and impact assessment, monitoring.</td>
<td>International Organizations, Standard Setters</td>
</tr>
<tr>
<td>Social and labour disclosure and reporting requirements</td>
<td>Enhance sustainability reporting and disclosure requirements by including social metrics (including on labour) in project, company-level and financial institutions’ disclosure requirements alongside environmental indicators.</td>
<td>Standard Setters, Governments/ regulators</td>
</tr>
</tbody>
</table>

The fundamental elements related to **scope, definitions, and metrics** outlined above can then be integrated into existing financial market infrastructure like disclosure requirements, taxonomies, sustainability rating methodologies, ESG labels, benchmarks, active ownership strategies. They can further be embedded in sustainable finance practices like institutional net-zero strategies and in conventional or dedicated just transition financial instruments. Table 5 highlights several potential elements which could serve as a basis for discussion around efficient integration of social considerations in financial sector infrastructure, based on a review of literature and existing practices.

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Potential Entry Points for Factoring in Social Impacts in Transition Finance Frameworks

The above sections show that the whole financial ecosystem is starting to embrace transition finance and there are indications that the system is ready to move one step further and integrate just transition approaches. The segments of the financial sector that are most advanced on the transition finance agenda offer a number of potential entry points.

Existing transition finance frameworks focus largely on debt financing (OECD, 2021). Debt-instruments, structured as use of proceeds bonds and loans, allow the financing of projects that target defined environmental and/or social benefits and therefore stand out as well-suited to provide capital for decarbonization purposes. Sustainability-linked debt instruments can provide the basis for going one step further and committing to explicit and measurable sustainability targets defined through KPIs. The achievement of the KPIs determine effective financial conditions and incentives. Such structures allow the financing of activities and assets that are not yet green taxonomy-aligned but that are undergoing the low-carbon transformation process.
**Table 6: Potential entry points to factor in socio-economic impacts in transition finance**

<table>
<thead>
<tr>
<th>Elements of Transition Finance Framework</th>
<th>Potential Entry Points</th>
</tr>
</thead>
<tbody>
<tr>
<td>General</td>
<td>Include social and labour safeguards in general purpose and transition finance instruments.</td>
</tr>
<tr>
<td>Corporate commitments to a low-carbon trajectory and governance</td>
<td>Include measures and targets contributing to a just transition (material for the company operations) in corporate strategies and/or long-term transition plans.</td>
</tr>
<tr>
<td>Taxonomies</td>
<td>Include contribution to social goals alongside climate objectives in green/transition taxonomies.</td>
</tr>
<tr>
<td>Transition pathways</td>
<td>Include material social aspects and targets in sector-specific decarbonization roadmaps, allowing for geographical variability of transition activities and different transition pathways.</td>
</tr>
<tr>
<td>Project Evaluation and Selection</td>
<td>Assess negative externalities and adverse effects on social and environmental objectives for transition finance projects.</td>
</tr>
<tr>
<td>Key Performance Indicators</td>
<td>Add KPIs for social and employment targets and outcomes alongside emission reduction targets for KPI-linked instruments.</td>
</tr>
<tr>
<td>Reporting and Disclosure Requirements Impact Measurement</td>
<td>Include specific just transition-relevant metrics to report on for eligible projects and entities that allow monitoring of environmental and social impacts of financed activities and the contribution to stated instrument targets and KPIs.</td>
</tr>
<tr>
<td>External Assessment and Certification</td>
<td>External pre- and post-issuance verification of adequacy of financial product structure versus the stated purpose, including examination of social/employment safeguards and targets, to increase transparency and issuer accountability by means of monitoring the use of funds and eventually triggering penalty mechanisms.</td>
</tr>
<tr>
<td>Financial Product and Instrument Labels</td>
<td>Explore creation of a dedicated Just Transition label for financial instruments destined to finance projects purposefully mitigating social risks of the low-carbon transition and/or targeting material social benefits alongside achieving climate transition objectives.</td>
</tr>
</tbody>
</table>

**Equity investors** also have mechanisms allowing them to influence the real economy, beyond the effects of capital allocation decisions. Active ownership approaches, which include using voting rights and/or engaging in dialogue with the investee companies, enable investors to drive the improvement of environmental and social practices and promote their alignment with just transition objectives. Corporate engagement, anchored in just transition objectives and based upon relevant evidence-based data, can be used for advancing social and labour-related practices by investee companies (LSE et al, 2018), as demonstrated by Royal London Asset Management and Friends Provident Foundation engagement with SSE\(^1\).

In summary, several of the structural elements of transition finance frameworks offer opportunities for including social and employment considerations. Certain entry points allow for the creation of dedicated financial instruments aiming to address specific just transition gaps and making them accessible to a large number of interested investors. Others provide opportunities for mainstreaming a social impact approach and applying it to a wide set of financial instruments and practices within the transition finance segment and beyond.

**Transition finance represents a crucial avenue to contribute to a just transition. Transition finance frameworks offer several potential entry points to maximise positive social and employment contributions and avoid negative impacts. The work of the G20 SFWG can play a pivotal role in advancing efforts in this field, contributing to achieving ambitious climate goals and sustainable development.**

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\(^{1}\) As a result of the dialogue with these committed investors, the energy utility company refined its approach (SSE, 2021) to addressing social implications of its decarbonization strategy.
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## Annex

### Table 7: A non-exhaustive list of existing transition finance frameworks and taxonomies

<table>
<thead>
<tr>
<th>Author</th>
<th>Transition finance framework</th>
<th>Actor Type</th>
</tr>
</thead>
<tbody>
<tr>
<td>Japan</td>
<td>Basic Guidelines of Climate Transition Finance</td>
<td>Government/Country</td>
</tr>
<tr>
<td>Singapore</td>
<td>Discussion Paper on Taxonomy</td>
<td>Government/Country</td>
</tr>
<tr>
<td>European Union</td>
<td>The Extended Environmental Taxonomy</td>
<td>Government/Country</td>
</tr>
<tr>
<td>Climate Bonds Initiative and Credit Suisse</td>
<td>Financing Credible Transitions - A framework for identifying credible transitions</td>
<td>Think Tanks/ Market Participant</td>
</tr>
<tr>
<td>Climate Bonds Initiative</td>
<td>Transition Finance for Transforming Companies</td>
<td>Think Tank</td>
</tr>
<tr>
<td>International Capital Market Association (ICMA)</td>
<td>Climate Transition Finance Handbook</td>
<td>Market Participant</td>
</tr>
<tr>
<td>AXA Investment Managers (AXA IM)</td>
<td>Guidelines for Transition Bonds</td>
<td>Market Participant</td>
</tr>
<tr>
<td>Standard Chartered</td>
<td>Transition Finance Framework 2021</td>
<td>Market Participant</td>
</tr>
<tr>
<td>DBS Bank</td>
<td>Sustainable &amp; Transition Finance Framework &amp; Taxonomy</td>
<td>Market Participant</td>
</tr>
<tr>
<td>European Bank for Reconstruction and Development (EBRD)</td>
<td>Green Transition Bond Framework</td>
<td>International Finance Institution</td>
</tr>
</tbody>
</table>