Grantham Research Institute on Climate Change and the Environment

Centre for Climate Change Economics and Policy

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Policy brief
Lessons from COP26 for financing the just transition

Summary

- **At the COP26 climate summit, the just transition advanced as a critical factor for enabling a successful shift to a net-zero and resilient economy,** almost six years after it was included as a single line within the Paris Agreement.
- **Increased recognition extended from** the formal process to actions taken by governments, the trade union movement and business, as well as from civil society and the financial sector.
- **At least 10 new just transition initiatives** were launched at COP26 with a direct or indirect focus on making the just transition a reality. They have important implications for future efforts across the financial system. Among them are:
  - The Glasgow Climate Pact, agreed by over 190 states, in which fossil fuel phasedown is linked to the just transition.
  - A significant new partnership between South Africa, the EU, France, Germany, the UK and the USA on financing the just energy transition.
  - High-level principles from the multilateral development banks, which link the just transition with the Sustainable Development Goals.
  - Announcements on supporting a just transition away from coal, including by the Climate Investment Funds.
  - A first business-led framework and initial results from an assessment of corporate practice from the World Benchmarking Alliance.
- **Despite the unprecedented signals of support, actual delivery remains at an early stage** and action in 2022 needs to intensify as part of efforts to keep global warming to 1.5°C.
- **Five priorities on the just transition for the financial system in the lead-up to COP27 are:**
  1. Make the just transition integral to net-zero plans.
  2. Focus on emerging and developing economies.
  3. Deploy tailored financial instruments and mechanisms.
  4. Support just transition policy and regulation.
  5. Recognise the crucial role of dialogue and participation.

Policy briefs provide analysis on topical issues, presenting specific recommendations to inform ongoing policy debates. Drawing on the Grantham Research Institute's expertise, they summarise either our research findings or the state of knowledge about a particular issue.

This policy brief has been written by **Nick Robins and Sabrina Muller.**

As part of the Paris Agreement, governments committed to take into account: "the imperatives of a just transition of the workforce and the creation of decent work and quality jobs in accordance with nationally defined development priorities". With its partners, the Grantham Research Institute has developed a growing programme of research, policy dialogue and has convened stakeholders on how to bring the just transition to life, with a focus on the role of public and private finance.[1]

In this policy brief, we review the attention given to this crucial aspect of climate change action at the COP26 climate summit in Glasgow in November 2021, and the priorities that lie ahead for 2022.

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Growing momentum on the just transition ahead of COP26

In the run-up to the COP26 summit, the importance of a just transition to a net-zero economy emerged in a number of ways. On the policy front, the International Energy Agency launched the results of its Global Commission on People-Centred Clean Energy Transitions (IEA, 2021a). In the investment community, the Climate Action 100+ initiative included the just transition in its 2022 Net-Zero Company Benchmark (CA100+, 2021). Growing examples of finance sector action were also highlighted at the Just Zero conference in the week before COP, by leaders from the financial world, policymakers, trade unions and universities.[2]

New policy and public finance pledges at COP26

At COP26, the just transition was re-emphasised as a priority by governments and policy institutions – such as development banks. We describe the initiatives we consider most significant below.

1. Glasgow Climate Pact

Agreed by consensus by over 190 states, the Glasgow Climate Pact deepened the commitment of governments to the just transition. The Pact includes the first reference to fossil fuels in a UNFCCC agreement, with governments pledging to accelerate the "phasedown of unabated coal power and phase-out of inefficient fossil fuel subsidies". This was explicitly linked to "providing targeted support to the poorest and most vulnerable in line with national circumstances and recognizing the need for support towards a just transition" (para 36). A strong connection with financial alignment was also made, with the Pact stating "the need to ensure just transitions [...], including through making financial flows consistent with a pathway towards low greenhouse gas emission and climate-resilient development" (para 85).

2. Governments' Just Transition Declaration

Sixteen industrialised country governments along with the EU issued a declaration on Supporting the Conditions for a Just Transition Internationally. The Declaration follows on from the 2018 Silesia Declaration made at COP24 in Poland, and the commitment of close to 50 countries to develop just transition plans connecting climate action with social benefits made at the UN Climate Action Summit in 2019 (see ILO, 2019). The new Declaration sets out five principles, including supporting workers, social dialogue, economic strategies, decent work, supply chains and reporting. The reporting principle means that the signatories will include the just transition in the biennial disclosure on policies and measures to achieve their Nationally Determined Contributions (NDCs). The Declaration also has a strong development cooperation emphasis, and signatories represent over 70% of public climate finance provision (based on Bos and Thwaites, 2021).

1. See www.lse.ac.uk/granthaminstitute/research-areas/sustainable-finance/.

2. The Just Zero conference was organised by the Grantham Research Institute with the Initiative for Responsible Investment, Center for Public Leadership, at the Harvard Kennedy School, the Principles for Responsible Investment, and the International Trade Union Confederation. Other collaborators included CDC, the Institute for Human Rights and Business, the Powering Past Coal Coalition and the Place-based Climate Action Network. Recordings of the sessions can be accessed at www.lse.ac.uk/granthaminstitute/events/just-zero/.

3. International Just Energy Transition Partnership

One of the most substantive outcomes of Glasgow is the new Partnership between South Africa, the EU, France, Germany, the UK and the USA. The Partnership will provide $8.5 billion to support "a just transition to a low carbon, climate resilient society that promotes employment and livelihoods" through a mix of grants, concessional instruments and risk sharing mechanisms to crowd-in private investments (European Commission, 2021). The funds will be used to support workers and communities – particularly coal miners, women and young people – and to contribute to creating quality green jobs, especially in technological innovation. Operational details will be finalised in 2022.

South Africa was the first country to include the just transition in its NDC and it is at the centre of the country's efforts to achieve net-zero and build resilience. South Africa is the most coal-dependent country in the G20, with around 70% of the energy mix being coal-based (IEA, 2021b). Employment in coal mining stands at around 90,000 (Minerals Council South Africa, 2021), with many more dependent on the sector. At the same time, unemployment is over 30%, one of the highest rates in the world. The Partnership is designed to support South Africa's domestically determined strategy, which is being advised by the Presidential Climate Commission. With regards to the finance sector, the basis for developing a Just Transition Finance Roadmap in the country has been outlined in a recent TIPS report (Lowitt, 2021).

The relevance of the Partnership extends beyond South Africa and could provide inspiration for other countries to adopt economy-wide strategies to phase-down fossil fuels. Looking at **India**, for example, using coal generation and GDP per capita as proxies, extrapolating from the South Africa partnership suggests that over $80 billion in international climate finance would be equivalent.[3] Clearly, this is only part of the much wider uplift in climate finance that is required. In South Africa alone, estimates show a $33 billion annual investment gap in climate finance to reach the Paris goals (Cassim et al., 2021). A recent report finds that annual investments for clean energy in emerging and developing markets need to increase by a factor of seven, from $150 billion in 2020 to over $1 trillion by 2030 to achieve net-zero emissions in 2050 (IEA et al., 2021).

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4. Multilateral development banks' 'high-level principles'

International public finance institutions have often been leading the practical application of the just transition in the finance sector – these include the Asian Development Bank, CDC, the European Investment Bank, the European Bank for Reconstruction and Development, the World Bank and the Climate Investment Funds. At COP26, eight multilateral development banks (MDBs) released a joint statement of high-level principles. They focus on connecting climate action with the Sustainable Development Goals, delivering long-term economic transformation, mobilising public and private finance, mitigating negative socioeconomic impacts and increasing opportunities, and ensuring inclusive and transparent planning.

Turning these principles into practice will need to involve clear responsiveness to country-driven priorities as well as in-depth engagement with business, workers and communities. Action by the MDBs could also catalyse private finance efforts to support the just transition via credible blended finance initiatives.

5. A just transition past coal

As the host of COP26, consigning coal to history was one of the UK's policy priorities in Glasgow. Alongside the first-of-its-kind reference to phasing down coal in the formal Glasgow Climate Pact, over 40 national governments, plus regional authorities and other organisations, supported a 'coal to clean' transition statement,

3. Authors' calculation based on electricity generation from coal and GDP per capita in 2020.

prioritising the end of unabated coal in the 2030s in industrialised countries and in the 2040s in developing countries. A specific commitment was made to "provide a robust framework of financial, technical, and social support to affected workers, sectors and communities to make a just and inclusive transition away from unabated coal power in a way that benefits them, and expands access to clean energy for all".

The Climate Investment Funds (CIF) launched a $2.5 billion investment programme, too, designed to achieve a just transition from coal to clean energy in emerging economies. Pilots are set to kick off in India, Indonesia, the Philippines and South Africa. The role that private finance institutions can play in supporting a just transition from coal has also been profiled in an investor briefing from the Powering Past Coal Alliance and the LSE (Muller and Robins, 2021).

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Finance, industry and business: further steps on the just transition

A number of business, industry and finance sector initiatives were also announced at COP26, pointing to how voluntary action could make the just transition come to life in the real economy and the financial system.

6. Glasgow Financial Alliance for Net Zero

The Glasgow Financial Alliance for Net Zero (GFANZ), launched in April 2021, has boosted the number of financial institutions with net-zero targets to more than 450, representing around 40% of global assets at $130 trillion. Members of GFANZ have committed to net-zero financed emissions by 2050 at the latest, delivering their fair share of the 50% emissions cut by 2030 and drawing up detailed five-year reduction plans, reported on annually. In its progress report, GFANZ highlights the importance of including the just transition in both the real economy and the financial sector transition plans that now need to be designed and implemented (GFANZ, 2021). Banks, insurers, investors and other financial institutions will need to show how their climate action plans incorporate the interests of workers, communities and consumers.

7. Just Transition Maritime Task Force

The Just Transition Maritime Task Force launched at COP26 highlighted the potential for multi-stakeholder collaboration between industry, trade unions and others. The Task Force brings together the International Chamber of Shipping, representing shipowners, the International Transport Workers' Federation, representing seafarers and port workers, and the UN Global Compact, the world's largest corporate sustainability initiative. The International Labour Organization and the International Maritime Organization will also join the task force as formal partners.

The Task Force aims to support the decarbonisation of shipping while ensuring workers and communities are protected and have access to the opportunities created in the transition. Building the needed green skills and creating green and decent jobs will be key priorities. With changes to shipping having ramifications especially for labour in the Global South, emerging markets will be of particular relevance.

8. Just Energy Transition framework

For the first time a corporate sector actor has presented its own strategy for delivering a just transition. The Council for Inclusive Capitalism, with the Vatican and working with CEOs from ACEN, Anglo-American, BP, ENI, Reliance, Repsol and SSE, published a Just Energy Transition framework. It contains four pillars: universal net-zero energy access, evolving the energy workforce, community resilience, and collaboration and transparency. The framework defines 20 'building blocks' for driving forward a just transition, applying case studies to illustrate best practice.

9. Just transition corporate benchmark assessments

On the corporate accountability side, the World Benchmarking Alliance (WBA) has piloted this year the first Just Transition Assessments of corporate performance. The evaluation covers issues such as human rights, social dialogue, just transition planning, job creation, retaining and retraining, social protection, and policy advocacy. Looking at 100 oil and gas, 50 electric utility and 30 automotive manufacturing companies for its pilot, the WBA found that "the vast majority of high-emitting companies are failing to demonstrate efforts towards a just transition" (WBA, 2021). Only nine companies scored over 50% in the benchmark on their just transition performance. The WBA concludes that people most at risk are being left out of decisions that affect their future and argues that companies must commit to reskilling workers or risk a stranded workforce. The initial assessments also showed that businesses are still not using their influence to protect people, manage social impacts or advocate for a just transition and the WBA underlines that the just transition needs to be underpinned by companies' respect for human rights.

10. The UK's Financing a Just Transition Alliance

The UK's Financing a Just Transition Alliance, convened by LSE, is the first country-level initiative focusing on the role that banks, investors and other financial institutions can play in delivering net-zero with positive social impact. At COP26, the Alliance presented its first-year findings of its collaboration with over 40 members from across the country (Robins et al., 2021). Key priorities include making the just transition a core part of financial sector climate action, using shareholder engagement to improve corporate practices, focusing on place-based investment strategies and encouraging government to introduce just transition policies in the real economy and financial system. The next phase of the Alliance will focus on turning increasing financial sector recognition into specific commitments and transactions.

Disappointing progress on climate justice

These promising developments on the just transition at COP26 cannot hide the wider disappointments on the progress made on climate justice overall. Social equity was set to be a challenging topic for debate even before the summit began, with the globally uneven vaccine roll-out impacting emerging and developing countries.

COP26 ended with 90% of global greenhouse gas emissions being covered by long-term net-zero commitments. This kept the potential open for holding temperature rises to 1.5°C. But, in the words of COP26's President, Alok Sharma, "the pulse of 1.5 is weak", and Climate Action Tracker concluded that, "the vast majority of 2030 actions and targets are inconsistent with net zero goals" (Sharma 2021; Climate Action Tracker, 2021). The commitment by governments in the Glasgow Climate Pact to come to COP27 with upgraded NDCs for 2030 was a necessary recognition of the need to intensify action in the 2020s.

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The failure of the industrialised countries to meet their longstanding commitment to provide $100 billion in climate finance per year to developing countries was seen as a breach of faith at Glasgow. In the restrained diplomatic language of climate negotiations, the Glasgow Climate Pact noted this "with deep regret". Industrialised countries have now drawn up a Delivery Plan to fulfil the pledge. Demonstrating in 2022 that this is being done will be important both to resourcing real-world investments in developing countries and to restoring trust in the climate negotiations at COP27 in Egypt (Bhattacharya and Stern, 2021). In the words of

Nick Stern, "Over the next 12 months there is critical and urgent work to be done to unleash key sources of finance: bilateral, multilateral, multilateral development banks, private sector, and innovative sources, including philanthropy, Special Drawing Rights from the International Monetary Fund, and voluntary carbon markets" (Stern, 2021).

Mixed progress on adaptation and loss and damage

Advances were made on adaptation finance goals. In 2019, only a quarter of the $80 billion in climate finance was allocated to adaptation (OECD, 2021). The target was set at COP26 for developed countries to double this funding to developing countries by 2025 (UNEP, 2021).

The outcomes on loss and damage, however, left much to be desired. With vulnerable countries already facing harm caused by climate change to society, the environment and the economy, finance for existing loss and damage is becoming an ever more relevant issue. As Mia Amor Mottley, the Prime Minister of Barbados, stated at the World Leaders Summit at COP26: "Failure to provide the needed climate finance to the countries most affected by the impacts of climate change is measured in lives and livelihoods being lost in our communities. It is immoral and unjust."

Scotland became the first industrialised country to commit support for loss and damage, with a symbolic £2 million. On the penultimate day of the summit, Scotland's First Minister Nicola Sturgeon argued that the industrialised world owed "a debt to developing and vulnerable countries", with a responsibility to provide finance "not as an act of charity but as an act of reparation". Developing countries had called for a dedicated finance facility for loss and damage. Instead, the dedicated Glasgow Dialogue on loss and damage will be established, to run from 2022–24.

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Priorities for financing the just transition in 2022

Two competing realities emerged at COP26 for a just transition to an inclusive, resilient and net-zero economy: while there were unprecedented signals of support, these were set against highly limited real-world action and continuing inabilities to deliver climate justice at a strategic level. The impacts of the 10 initiatives highlighted in this brief will be judged both by their translation into measurable action and by the demonstration effect they have on other countries, institutions and sectors.

There are five priorities for the financial system in the run-up to COP27, scheduled to be held in November 2022 in Sharm El-Sheikh:

1. Make the just transition integral to net-zero plans. GFANZ has highlighted that the just transition is best practice in the formulation of net-zero transition plans, for both real economy businesses and the finance sector. In 2022, financial institutions will need to set out how they intend to make this a reality in terms of overall strategy and as commitments across business lines and asset classes, dialogue with key stakeholders and commitments to accountability. Banks and investors also have an important role in ensuring that the companies they finance adopt credible transition plans integrating the just transition.

2. Focus on emerging and developing economies. The greatest investment needs for net-zero and climate resilience lie in the Global South. Yet real constraints exist in terms of access to and the cost of capital, as well as limited institutional capacity to realise a just transition. For private sector financial institutions, tackling this will

mean understanding how the just transition can be realised in their portfolios across three dimensions: first, in the subsidiaries of developed world firms; second, in emerging market companies and assets; and third, in the supply chains connected to the Global South. Partnerships with development finance institutions will be particularly important to build strong policy foundations, develop innovative financial solutions and reduce financial risks. Before COP27, a concerted effort from the public and private sectors will be needed to mobilise the scale of investment required for a just transition in the developing world.

3. Deploy tailored financial instruments and mechanisms. Financial institutions will also need to translate the strategic imperative of the just transition into tailored instruments and mechanisms. For institutional investors, stepping up the pace with shareholder engagement is a key instrument, not least through the Climate Action 100+ collaboration. Given the early-stage nature of the corporate response, as highlighted by the World Benchmarking Alliance, now is the time to mainstream just transition engagement across all relevant sectors to drive real change in business practice.

Alongside, the just transition needs to be embedded into capital allocation decisions across all asset classes and banking transactions. Since COP26, further evidence has emerged on how this could be done in the banking sector (Clifford Chance et al., 2021) and as part of scaling up impact investment (Impact Task Force, 2021). In 2022, building an armada of credible and effective just transition mechanisms will be critical to demonstrate how finance can be reallocated at scale.

> "The just transition needs to be embedded into capital allocation decisions across all asset classes and banking transactions."

4. Support just transition policy and regulation. Governments have the primary responsibility to put in place the policy and financial frameworks to accelerate the just transition across macro-economic and fiscal strategy, industrial, sectoral and regional policies, employment and skills development, labour rights and social dialogue (ILO, 2015). In the years ahead, the just transition will need to be incorporated into both real economy policies across sectors and regions, and into financial policies and regulations. Financial sector institutions can support the development of these frameworks through their dialogue and advocacy with governments and other agencies.

Key action points for 2022 will be to include the just transition in new reporting frameworks for corporate net-zero plans (for example, as planned by the EU and the UK), and the roll-out of 'Green Plus' sovereign debt issuance, which explicitly targets social co-benefits as part of green spending (III and GRI, 2021).

5. Recognise the crucial role of dialogue and participation. An essential part of the just transition is for affected workers, communities and others to have a say in the decisions that impact them ('nothing about us, without us'). Social dialogue with workers and engagement with local communities have to be integral to government, corporate and financial decision-making. Of course, countries have very different traditions and models for participation in the workplace, in localities and at the national level. But developing replicable models for worker and community participation, and working to apply them, is a critical next step.

Financial institutions, such as banks and investors, can themselves reach out to trade unions and community organisations, to ensure their voice is reflected in just transition efforts. The quality of the social participation in company just transition plans can also become a key quality indicator in assessment exercises. Finally, financial institutions can also support and feed into broad-based initiatives, such as Just Transition Commissions, which can make sure that climate action is people-centred and inclusive.

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