FINANCING POLICY BRIEF SERIES
INTER-AGENCY TASK FORCE ON
FINANCING FOR DEVELOPMENT

International Labour Organization

# ALIGNING FINANCIAL SYSTEMS WITH A JUST TRANSITION

RELEVANT ACTION AREAS

Domestic and International Private Business and Finance

Science, technology, innovation and capacity-building

International Development Cooperation

## Key messages

Addressing both social and environmental objectives is essential to mitigate risks and seize opportunities related to the low-carbon transition. A just transition requires supportive financial flows and enabling financial systems. Member States can support mobilization of financial resources for a just transition by leveraging public development banks, incentivizing the use of financing instruments that attract private capital, developing comprehensive sustainable finance frameworks that consider social and environmental objectives, and developing capacities within the financial system.

- Since the Addis Ababa Action Agenda was agreed in 2015, green and climate finance have significantly grown in volume and geographic coverage. However, the social dimension of sustainable finance has not developed at the same pace. This trend is despite the recognition of a just transition as a crucial enabler of ambitious climate action and an engine of sustainable development. The uneven pace risks that the transition to a low-carbon economy triggers new or exacerbates existing inequalities and misses opportunities for addressing these imbalances and for creating positive social impact.
- Achieving a just transition requires supportive financial flows. This necessitates the development of enabling financial systems, sustainable finance policies and practices, and the strategic alignment of the operations of financial institutions to effectively channel resources that address both social and environmental objectives.
- Member States can nurture financial systems that support a just transition by (i) leveraging the role of national and international public development banks as drivers of change in the financial sector, (ii) incentivizing financing instruments that stimulate and align private capital flows, (iii) developing sustainable finance policies and disclosure frameworks that explicitly address social aspects of a just transition, and (iv) supporting capacity building at different levels of the financial system.

ABOUT THIS SERIES

The Financing Policy Brief Series has been prepared by the Inter-agency Task Force on Financing for Development to inform the substantive preparations for the Fourth International Conference on Financing for Development (FfD4), to be held in Sevilla, Spain, from 30 June to 3 July 2025.

The Inter-agency Task Force on Financing for Development is comprised of more than 60 United Nations Agencies and international organizations. The policy briefs in this series were not subject to review by Task Force Members, and represent the views of the authoring organizations.

The full series is available at:
https://financing.desa.un.org/iatf/report/financing-policy-brief-series

## Problem statement

In 2015, the Addis Ababa Action Agenda put forth a global framework for financing sustainable development by aligning all financing flows and policies with economic, social and environmental priorities. Since then, climate finance flows have significantly grown. Average annual climate finance flows reached almost USD 1.3 trillion in 2021/2022, nearly doubling compared to 2019/2020 levels. Despite that progress, climate finance must increase by at least five-fold annually to avoid the worst impacts of climate change[1]. Similarly, significant regional and sectoral disparities in financing flows persist which must also be addressed urgently for achieving climate goals.

At the same time, the social dimension of financing the transition to a low-carbon economy has not developed at the same pace as environmental aspects. This is despite the recognition of the just transition as a crucial enabler of ambitious climate action and an engine of sustainable development. A just transition means greening the economy in a way that is fair and inclusive to everyone concerned, creating decent work opportunities, and leaving no one behind. The importance of a just transition, as defined by the ILO Guidelines for a Just Transition 2015, is also enshrined in the Paris Agreement and continues gaining momentum in the agendas of governments, employers, workers, and financial institutions worldwide.

The transition to a low-carbon economy presents opportunities to the financial sector to promote social justice and address poverty, diversify economies, create productive employment, and support the expansion of sustainable enterprises. But the transition also implies 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. These challenges directly impact financial institutions and their clients[2].

The transition to net zero will inevitably fail if undertaken without due regard to the social implications or if it is not done in an inclusive, consultative, and cooperative manner that promotes equitable distribution of transition benefits and burdens. The unintended negative externalities of the low-carbon transition could undermine social cohesion, weaken support, and slow climate action, leading to devastating environmental and economic consequences[3].

Financing is crucial to all pillars of the low-carbon transition: expanding green and low-carbon activities, transforming environmentally and socially unsustainable practices and activities, and developing society's resilience to adapt to the physical impacts of climate change and transition pathways.

When shaping their approaches to green and transition finance, actors in the financial sector are influenced by a complex ecosystem of policies, mandatory and voluntary frameworks. For example, several jurisdictions have developed taxonomies or guidelines to provide clarity within their markets on what assets or economic activities can be considered sustainable. These regulator-led taxonomies and guidelines can support transparency, reduce the risk of green and transition washing and deepen the market for sustainable assets. However, existing frameworks and initiatives in the green and transition finance ecosystem still place a relatively low, although increasing, importance on the social aspects of the low-carbon transition.

## Policy solutions

The "*ILO Guidelines for a just transition towards environmentally sustainable economies and societies for all*" provide principles and policy entry points to guide governments, employers, and workers' organizations in navigating this transformative journey[4]. They outline key elements of a just transition, emphasizing the necessity for coordinated action across various policy domains. This includes alignment in macroeconomic policies, sectoral

1. Climate Policy Initiative. Global Landscape of Climate Finance 2023.
2. ILO. 2022. G20 Sustainable Finance Working Group Input Paper: Finance for a Just Transition and the Role of Transition Finance.
3. ILO and UNEP FI. 2023. Just Transition Finance: Pathways for Banking and Insurance.
4. ILO, 2015. Guidelines for a just transition towards environmentally sustainable economies and societies for all.

strategies, employment, enterprise development, skills, labour market policies, social protection, occupational health and safety, rights, and social dialogue.

Well-designed policies form the basis for a just transition, but unless they are well coordinated, include all the relevant stakeholders and are financed, they will not be applied. To finance the implementation of such policies and objectives, public finance is not the sole source: there is significant scope for leveraging private sector finance, particularly for the financing of enterprises engaged in sustainable and low-carbon economic activities, embarking on decarbonization pathways or strengthening their resilience. The uptake of just transition considerations by the private sector can be strengthened by developing and enhancing sustainable finance frameworks that promote the objectives of a just transition, including through social requirements and incentives in addition to climate targets.

To boost the role of the private sector in financing a just transition, it is also important to build the capacity of financial sector practitioners, including through awareness-raising and practical guidance and tools, and to support financial innovation and experimentation, accompanied by thorough impact assessment of initiatives.[5]

Development finance can attract additional private sector capital through instruments like guarantees, equity and concessional loans. The action of development finance actors can reduce or transfer perceived investment risks and improve the risk–return profile for private investors, as well as lower the cost of funds for projects that are aligned with a just transition including in developing countries.

These entry points can enable the financial sector to play an even more important role to accelerate the shift to a low-carbon, resource-efficient, and resilient society. However, enabling conditions need to be in place to accelerate the flow of finance towards a just transition. These conditions include the creation of an enabling policy environment, providing for the development of skills needed for a just transition, ensuring social dialogue, access to adequate social protection and supporting the groups affected by the transition[6].

## Specific recommendations for FFD4

The outcome document of FFD4 could call upon Member States to nurture financial systems that support a just transition by

1. **Leveraging the role of national and international public development banks as drivers of change.** In line with their development mandate, public development banks can lead the efforts to finance a just transition. Member states can review the current policies guiding the operations of national and international development banks and increase the importance of social aspects in decision-making regarding green and climate finance.

2. **Incentivizing the use of financing instruments that stimulate and align private capital flows.** Member states can encourage and facilitate a wider use of instruments that channel both private money from the global financial markets and public resources towards just transition-aligned projects. Blended finance approaches can serve to reduce perceived risks for private sector investors and attract capital, while use-of-proceeds and sustainability-linked instruments can support financing towards projects and activities that align with just transition objectives.

3. **Developing sustainable finance policies and disclosure frameworks that explicitly address social aspects of a just transition.** Enabling financial sector policies, including those related to green and transition finance, as well as disclosure and reporting frameworks are crucial to guide financial systems. When developing such policies, Member States should consider proportionality of the full range

5. Examples of such tools include : Just Transition Finance Tool for banking and investing activities and Just Transition Finance - Pathways for banking and insurance.
6. ILO. 2024. Enhancing the social dimension in transition finance: towards a just transition.

of sustainability-related requirements, i.e. social, environmental, and economic, for different contexts as well as interoperability with other frameworks.

4. **Supporting capacity building at different levels of the financial system.** Member states can provide capacity building on just transition to key stakeholders in the financial system, including Ministries of Finance, Central Banks, other financial sector supervisors and regulators as well as financial institutions and their networks. Moreover, they can lean on international cooperation, International Organizations, industry platforms, academia and other stakeholders to accelerate the development and implementation of tools with that objective.