

Strengthening the Role of Ministries of Finance in Driving Climate Action

Contents

1) Key Messages for Policy Makers	1
2) Background on the Coalition of Finance Ministers and the Guide	2
3) Main Messages	3
Why the role of Ministries of Finance matters for climate action and economic transformation	3
A Ministry of Finance framework for climate action	4
Priorities for action and implementation	5
Next steps for the Coalition	6
4) A call to action for Ministries and Ministers of Finance	6

1) Key Messages for Policy Makers

- **Ministries of Finance have significant levers** they can pull to accelerate the climate action needed to deliver on the goals of the Paris Agreement and drive sustainable, inclusive and resilient development and growth— but these levers are not yet being fully utilized.
- **Bold climate action can be instrumental in helping Ministries of Finance achieve their core priorities** of macroeconomic stability, growth and responsible management of public finances, with major benefits including:
 - tackling escalating risks that have macro- consequences, including economic and budgetary shocks, and rising cost of capital;
 - enhancing economic and financial resilience;
 - generating significant growth and development opportunities including jobs and investment; and
 - delivering clean, secure and affordable energy and food.
- **Ministries of Finance have a window of opportunity** to mainstream climate action within their core functions of economic strategy, fiscal and financial policy. This will involve broad-ranging changes to strengthen governance and leadership, coordination and human and analytical capabilities.
- **A big part of the role of Finance Ministers is contributing to and supporting climate action** by other government departments and other stakeholders. To help Finance Ministers fully utilize the tools at their disposal, their role in driving climate action could be further strengthened and recognized through their mandates and climate governance arrangements.
- **Ministries of Finance have the experience to be the strong leaders the moment demands**, with many demonstrating visionary leadership and progress. Urgent and comprehensive action is needed to take this work further, and this report sets out a framework to guide this process.
- **Taking forward the priority actions will be critical to implementing the Helsinki Principles.** The Coalition of Finance Ministers for Climate Action has been created to support its members to do this.

2) Background on the Coalition of Finance Ministers and the Guide

- The **Coalition of Finance Ministers for Climate Action** is a global initiative established in 2019.
 - Co-chairs from Netherlands and Indonesia; the World Bank Group/International Monetary Fund host the Secretariat.
 - 86 members; 26 Institutional Partners
 - 40% of global CO2 emissions, 65% of global GDP
- All members of the Coalition have signed up to the six **Helsinki Principles** that promote national climate action, especially through fiscal policy and the use of public finance.
 - Principle 1: Align our policies and practices with the Paris Agreement commitments.
 - Principle 2: Share our experience and expertise with each other in order to provide mutual encouragement and promote collective understanding of policies and practices for climate action.
 - Principle 3: Work toward measures that result in effective carbon pricing.
 - Principle 4: Take climate change into account in macroeconomic policy, fiscal planning, budgeting, public investment management, and procurement practices.
 - Principle 5: Mobilize private sources of climate finance by facilitating investments and the development of a financial sector which supports climate mitigation and adaptation.
 - Principle 6: Engage actively in the domestic preparation and implementation of Nationally Determined Contributions (NDCs) submitted under the Paris Agreement
- The guide is a **Helsinki Principle 2 product**, led by **Finland** and **Rwanda**. The guide was prepared in a collaborative effort by the Coalition of Finance Ministers for Climate Action, coordinated by a team at the Grantham Research Institute on Climate Change and Environment at the London School of Economics and Political Science.
- The **report and guide in numbers**
 - ~30 countries and ~30 partners involved
 - 30+ expert contributions
 - ~50 consultation submissions
 - 140+ country case studies and examples
 - 800+ comments received (review + consultation)
- **Aim of guide** is to support Ministries of Finance to accelerate climate action by helping them to identify solutions to the barriers they face. It is aimed at Ministries of Finance but designed to be useful to anyone seeking to better understand the role of these ministries in climate action.
- **The guide is not prescriptive:** provides a menu of options to help countries enhance their core functions and capabilities to act according to their national circumstances.
- **The guide is designed to:**
 - Connect the six Helsinki principles and offer guidance on how Ministries of Finance can implement them.
 - Showcase examples and case studies of positive climate action by Ministries of Finance
 - Shape the debate globally around the future role and mandates of Ministries of Finance.
- The guide is based on an extensive review of **existing literature, interviews conducted with officials in Ministries of Finance and consultations with key experts**, including a global public consultation on a draft of the guide launched at COP26.

3) Main Messages

Why the role of Ministries of Finance matters for climate action and economic transformation

- **Governments worldwide are facing an unprecedented series of crises:** an economic crisis with slow growth, rising debt and challenges in recovering from COVID-19; a cost-of-living and energy crisis; and a climate crisis. These crises are interlinked and need to be addressed concurrently.
- **Far-sighted leadership is now needed by the public and private sector to deal with these challenges and build a zero-carbon, climate-resilient economy.**
 - This means decarbonizing every economic sector by 2050; enhancing adaptive capacity; protecting natural capital; and a just transition.
 - This will help to create a future based on clean, secure and affordable energy, cities and communities in which people can move and breathe easily, resilient and productive agriculture, and dynamic green industries and jobs.
 - This future economy is firmly within the grasp of today's leaders.
- **Ministries of Finance need to be at the heart of driving this economic transformation: climate action will not be possible without them.**
 - They are at the center of government, coordinating economic strategy and fiscal policy, and regulating the financial system.
 - They collectively control well over US\$30 trillion in government expenditure, over one-third of global GDP.¹
 - They are shareholders in state-owned enterprises, development banks, and the multilateral system.
 - They will be key to unlocking the global investment to tackle climate change which needs to be increased and sustained above pre-COVID levels by at least 2% of GDP per year globally, and closer to 4–5% in emerging markets and developing countries other than China.²
- **Bold climate action can be instrumental in helping Ministries of Finance achieve their core priorities of macroeconomic stability, growth and responsible management of public finances, with four major benefits** including:
 1. tackling escalating risks that have macro-critical consequences, including economic and budgetary shocks, and rising cost of capital;
 2. enhancing economic and financial resilience;
 3. generating significant growth and development opportunities including jobs and investment; and
 4. delivering clean, secure and affordable energy and food.
- These benefits and opportunities plus the avoided costs and risks mean that climate action can help Ministers of Finance harness the **development and growth story of the 21st century**. And should be synonymous with sound economic policy.
- A big part of the role of Finance Ministers is in **supporting and accelerating action by other government departments and private actors** such as Ministries of Environment, Economy, Energy, Agriculture, Transport, Planning, Health and others to drive action and investment.
- **Ministries of Finance have the experience to be the national and global leaders that the moment demands.** The role in responding to COVID-19 pandemic, 2009 Global Financial Crisis, and in driving industrial transformation demonstrates that they can be the flexible, dynamic crisis managers and drivers of economic transformation the moment demands.
- **Ministries of Finance are showing growing engagement and leadership at the heart of the transition to a zero-carbon, climate-resilient economy.** 140 examples are highlighted throughout the report. Examples include:

Strengthening the Role of Ministries of Finance in Climate Action

Summary for Finance Ministers and Policymakers

- Jamaica's Ministry of Finance has developed a best-in-class disaster risk financing strategy.
- Uruguay's Ministry of Finance has supported the country's transition to almost 100% renewable electricity generation through fiscal incentives.
- Ireland's Department of Finance's carbon pricing scheme uses revenue to support a just transition.
- Denmark has updated the mission and vision of its Ministry of Finance to drive whole-economy climate action.

Many other inspiring examples can be found in the full report and summarized in the main report.

- **Ministries of Finance have significant levers** they can pull to accelerate the climate action but these levers are not yet being fully utilized.
 - Only 14 of 35 OECD countries are practising green budgeting.³
 - Few Ministries of Finance have dedicated climate strategies.
 - In 2020, only a quarter of the members of the Coalition of Finance Ministers were actively involved in all stages of the NDC development and implementation process.⁴
 - And only around US\$650 billion of the more than US\$4 trillion in annual investment needed for a pathway to net-zero by 2050 was deployed in 2019.⁵
 - Meanwhile, G20 governments continue to provide around US\$600 billion annually on average in explicit fossil fuel subsidies, and carbon pricing initiatives cover less than a quarter of global emissions.⁶
- **Ministries of Finance have a window of opportunity to mainstream climate action** within their core functions of economic strategy, fiscal and financial policy. This will involve **broad-ranging changes** to strengthen governance and leadership, coordination and human and analytical capabilities, including strengthening their **mandates** to drive climate action.

A Ministry of Finance framework for climate action

To step up, Ministries of Finance need to look for opportunities to **mainstream climate action within their core functions and to enhance their capabilities to act** to overcome these barriers to action.

The framework in the report is designed to guide and support Ministries of Finance to understand how they can enhance their core functions and capabilities, overcome the barriers to action they face, draw inspiration from real-world examples, and identify opportunities for action.

Ministries of Finance can mainstream climate into their **three typical core functions**:

1. **Economic strategy and vision:** using their responsibility for oversight or involvement in national development strategies, sector plans and capital investment planning to participate in the development of national climate strategies, greening national development and sector plans, shaping industrial and innovation strategies, and assessing investment needs for the transition – in partnership with relevant line ministries.
2. **Fiscal policies and budget management:** using their primary responsibility for fiscal policy, taxation and budget planning and execution to design carbon taxation and new forms of environmental taxation, reform fossil fuel subsidies, introduce new fiscal incentives for green sectors, reform multi-annual expenditure frameworks and annual budgets, and green public investment and procurement strategies. Introducing a zero-carbon tax system and managing contingent liabilities will be critical. The Ministry of Finance's central role in the budget formulation process is a particularly important entry point for driving climate action and investment.
3. **Financial policy and regulation and oversight of the financial system:** using their core responsibility for the regulation of state-owned banks and enterprises, sovereign wealth funds,

Strengthening the Role of Ministries of Finance in Climate Action

Summary for Finance Ministers and Policymakers

financial institutions and debt markets, interfaces with central banks, and shareholdings and relationships with the international finance institutions (IFIs) and multilateral development banks (MDBs) to green the entire financial system, improve financial resilience and stability, and mobilize finance into sustainable investments. This can be achieved through frameworks for green bonds, catalyzing private capital, adaptation and disaster risk finance and insurance, and international climate finance – in partnership with central banks and the private sector.

To enhance these core functions, it is equally important that Ministries of Finance build their capability to act. **Three capabilities are critical:**

1. **Leadership capability:** strengthening the range of champions for climate action at the political and officials level, strengthening the Ministry's vision, mission and mandate to drive climate action, and creating clear responsibilities and organizational structures for climate leadership.
2. **Coordination capability:** driving effective collaboration across government and with the private sector, civil society and international financial institutions, and multilateral platforms and processes supported by effective strategies for consultation and communication.
3. **Human and analytical capability:** ensuring dedicated staffing resources for climate action, upgrading expertise in climate policy, and revamping tools and analytical approaches for data collection and economic decision-making.

A particularly important cross-cutting issue is the critical need for Ministries of Finance to drive forward a just transition to sustain public support and inform effective policy design. A just transition ensures a fair and wide distribution of the benefits of the transition as well as mitigating its social costs by targeted support for those individuals, businesses, organizations and communities that may be adversely impacted.

Priorities for action and implementation

The guide identifies **15 transformative actions** that, if embraced by Ministries of Finance globally, could help to ensure implementation of the Helsinki Principles and send a strong signal that the world economy is poised to follow a low-carbon, climate-resilient path.

The 15 actions are grouped into 3 groups (full list below)

- 1) **Building capabilities to act** in the Ministry of Finance, including through strengthened mandates, dedicated capacity and expertise and suitable economic tools.
- 2) **Reforming core fiscal and financial policies**, including taxes and macroeconomic incentives, using the budget and public investment systems to drive the transformation and future-proofing tax systems and raising, steering and blending finance for investment.
- 3) **Working with others** to develop strong and aligned national climate, growth and development strategies and, building up on those, climate investment strategies, and develop just transition plans and policies.

All Ministries of Finance will have to prioritize and sequence the steps they take. Given key differences in terms of powers, capabilities, culture, flexibility and the structure of the economies, pathways and priorities for reform are ultimately country-specific. Accurately identifying these differences is fundamental to determining appropriate organizational reform strategies.

As part of determining priorities, Ministries of Finance will need to navigate a range of **trade-offs**. Officials can support Ministers and decision-makers in navigating the trade-offs they face by following a number of principles laid out in the report (see below). It is important to realise that not all climate actions can generate 'win-wins' but the solution space for generating win-wins is often far wider than is commonly accepted, and there are effective ways to navigate trade-offs.

Strengthening the Role of Ministries of Finance in Climate Action

Summary for Finance Ministers and Policymakers

Next steps for the Coalition

The Coalition of Finance Ministers is committed to supporting its members to implement the actions from the guide under the auspices of HP2. It will do so through:

- Enhancing awareness of the role of Ministries of Finance in climate action;
- Enhanced training and technical assistance programs on climate change offered to Ministries of Finance or being designed by the Coalition's Institutional Partners (e.g. World Bank, IMF, NDC Partnership, WRI, UN, RDBs);
- Developing knowledge and research partnerships in support of climate action by Ministries of Finance;
- Deepening awareness and dialogue on implementation of the guide using regional and country-level workshops;
- Enhancing engagement of Ministries of Finance in national and global climate processes.

4) A call to action for Ministries and Ministers of Finance

The 15 transformative actions identified across Ministry of Finance core functions and capabilities are as follows:

Building capabilities to act

1. Dedicated Ministry of Finance strategies and strengthened mandates for climate action.
2. Building dedicated capacity for climate action.
3. Active engagement in inter-agency and stakeholder coordination efforts.
4. Investing in skills and expertise.
5. Revamping economic tools, data and decision-making approaches.

Core policies

6. Introducing fiscal policies to transform macroeconomic incentives for climate action including through ambitious carbon pricing schemes, subsidy reforms, and other fiscal incentives.
7. Using the budget and public financial management to drive transformation in all sectors of the economy.
8. Redesigning the tax system for net zero and climate resilience.
9. Raising, steering and blending finance for investment at unprecedented speed and scale.
10. Leveraging international climate finance.

Working with others

11. Mainstreaming climate action into national growth and development strategies.
12. Active engagement in national climate strategies.
13. Developing sustainable, inclusive and resilient investment strategies.
14. Driving the green transformation of state-owned enterprises, national development banks, and sovereign wealth funds in cooperation with central banks.
15. Developing just transition plans and policies.

Notes and references

¹ Government expenditure typically under the purview of Finance Ministries is ~30% of global GDP on average, totalling over \$100 trillion (see Zouhar Y, Jellema J, Lustig N, et al. (2021) *Public Expenditure and Inclusive Growth - A Survey*. IMF Working Paper No. 2021/083.; and IMF World Economic Outlook database for further details).

² Songwe V, Stern N and Bhattacharya A (2022) *Finance for climate action: Scaling up investment for climate and development*. London School of Economics and Political Science.

³ OECD (2021) *Government at a Glance*.

Strengthening the Role of Ministries of Finance in Climate Action

Summary for Finance Ministers and Policymakers

⁴ Coalition of Finance Ministers for Climate Action (2020) *Ministries of Finance and Nationally Determined Contributions. Stepping Up for Climate Action.*

⁵ CPI (2022) *Global Landscape of Climate Finance: A Decade of Data.*

⁶ World Bank (2022) *State and Trends of Carbon Pricing 2022.*