

Toward a Just Transition Finance Roadmap for South Africa: Action Agenda 2022-2025

OVERVIEW

Research undertaken in 2021 generated an evidence base of just transition project characteristics and financing needs in South Africa. The Mpumalanga sample of 26 projects covered a range of economic diversification interventions. Projects with novel technology opportunities related to land, water rehabilitation and agricultural dominated the sample. All the projects were designed specifically to provide alternative employment and livelihood opportunities for workers and communities negatively affected by climate change and decarbonisation activities. The research showed that decarbonisation projects and associated investments were predominantly technology driven and sought as their core outcome reduced carbon emissions. Just transition projects and associated investments were people driven and sought as their core outcome improved socio-economic circumstances such as increased employment, new livelihood opportunities, skills development, improved access to services, and increased community asset ownership. Adaptation investments were more closely aligned to just transition outcomes than decarbonisation outcomes. Based on this research, it is argued that while the funding for decarbonisation and just transition investments are fundamentally interrelated, intertwined (and usually negotiated as a single package of funding), decarbonisation transactions and just transition transactions will chase different outcome measures resulting in different risk return profiles and different instruments and deployment channels. It is therefore necessary to understand just transition finance supply and demand as a separate use of funds.

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INTRODUCTION

The 2021 research observed a broad duality in the funding demands of just transition projects. High-ticket price investments that were relatively modest in their socio-economic impacts but stronger on risk-related returns were identified as likely to be funded by the current finance ecosystem. One finding was that the number of such projects delivered would increase if the existing finance ecosystem improved its ability to price technology risk and if more risk sharing and blended finance instruments were available. Conversely, the research showed that projects with higher just transition ambitions – irrespective of ticket price – exhibited finance demand characteristics which would not easily be funded by the existing finance ecosystem.

The key characteristics of higher just transition ambition projects that make funding them challenging through the existing financial ecosystem include:

- Most of these projects consist of a suite of sub-projects that are interrelated and

build on each other's outcomes. These suites require a single funding solution which avoids cherry picking components with the highest level of return.

- Most suites of projects require funding from different financial institutions to be negotiated and co-ordinated up-front as a single financing solution. Concessionary, grant, impact and commercial return-related streams of funding need to be sourced, negotiated and co-ordinated, with residual risk pooled and de-risking measures applied.
- Just transition financing demands will require increased use of blended finance to unlock private sector flows. Given limited domestic fiscal space and Paris Agreement commitments, the just transition finance space will raise the challenge of increased systemic participation of offshore funding in local just transition project delivery.
- The drivers of, and participants in, just transition projects differ from traditional transaction parties and often lack the technical and commercial track records

This first iteration of a Just Transition Finance Roadmap for South Africa is supported by a first action plan covering 2022 to 2025. It sets out a series of steps that will support and enable concrete and iterative progress to be made towards an end goal finance ecosystem.

emphasised in financial intermediary due diligence processes. This will challenge the finance ecosystem's risk assessment and decision-making frameworks (especially credit committees).

- Higher ambition just transition projects characteristically require financial institutions to come on board earlier in the project development cycle than is the historic norm. The idea of the finance ecosystem "making deals" as opposed to "buying deals" will require new skill sets and capabilities.
- Many higher ambition projects have very low ticket prices and are small scale. Channelling funds to such projects has typically been a challenge in South Africa, and renewed innovative attention is required to ensure such funding can be mainstreamed at the required levels.

The finance ecosystem needs to sustainably mainstream just transition funding of an appropriate quantity and quality as part of the normal course of business. To achieve this, the ecosystem will need to change at a system level. This system level change or end state is the desired destination of a just transition finance roadmap. To achieve this long-term system level change, progressive and iterative short-term action plans are required.

In this first iteration of a Just Transition Finance Roadmap for South Africa, a vision of an end state finance ecosystem are described using desired key characteristics and competencies. This is supported by a first action plan covering the period 2022 to 2025. The action plan sets out a series of steps that will support and enable concrete and iterative progress to be made towards an end goal finance ecosystem.

The roadmap and action plans are based on a theory of change which sees the financial ecosystem experimenting and learning by doing. Iterative learning, accompanied by regulatory change will, in time, deliver system level change.

2050 VISION FOR THE FINANCIAL ECOSYSTEM

Globally, and in South Africa, the specific parameters, nature and beneficiaries of a just transition remain complex, contested and nascent. Despite this, there is a universally shared belief that a transition to net zero must be undertaken in a way that leaves no one behind. This is an economic, social and environmental necessity. The question of a just transition is not a question of "if" but a question of "how".

At a conceptual level, a just transition vision for the finance ecosystem is premised on a system which is

perfectly aligned to some "idealised" form of both a government's environmental policy and its social and economic development agenda.¹ At a more concrete level, the vision is premised on the finance ecosystem accepting the investment logic that a just transition portfolio in the South African context *is a necessary and desirable portfolio* for reducing climate, environmental, economic, governance, social, developmental and political risks. A just transition portfolio should be viewed by the ecosystem as a mitigation strategy against the risk of stranded assets, higher social protection costs, erosion of markets, environmental degradation, increased social strife and political instability.

To design and fund such a portfolio of investments will require the financial ecosystem to address, inter alia, four key challenges.

First: The current ecosystem stakeholders will need to accept that just transition risks will materialise in the short run and that just transition investment financing will be time sensitive. The system will need to be able to fast-track improvements in technology risk pricing; experimentation in due diligence processes suited to transitional contexts; and appropriate instrument development and structuring solutions for long-term investments requiring multiple tranches of patient capital rather than short-term returns. To meet just transition project demands in the short run, the ecosystem needs to engage with current project portfolios even in the absence of an enabling environment.

Second: As most higher ambition just transition projects comprise an interdependent portfolio of projects that cannot be deconstructed and need to be implemented in a preferred sequence, the required response of the financial ecosystem will be to develop and pilot financial innovations that pool investments and spread risk across several investors. Innovations need to facilitate a cascading effect (Naidoo, 2021) where essential and foundational projects are funded first; followed by subsequent projects building on these foundations. In addition, the interdependent nature of many just transition portfolios require the finance ecosystem to move away from due diligence and risk assessment at a project level and to expand assessments that deal with complex multi-project suites. Decision-making frameworks will similarly need to change, especially in the functioning of traditional credit committees.

¹In the current South African context this would be the government's National Determined Contribution (NDC) and the National Development Plan (NDP).

Figure 1: 2050 Vision of the characteristics of a future ecosystem perfectly aligned to government’s Climate Change Response Policy and Socio-Economic Development Goals

CHARACTERISTIC	NEW ECOSYSTEM
Financial Stability	Short-term and long-term environmental, social, governance and developmental risks are measured, priced and managed at a system level and at the level of individual projects.
Public Finance Effectiveness	Government designs and implements an integrated set of consistent interventions that focus on creating and supporting an enabling environment for sustainable, and especially just transition, finance, and that all legislative and regulatory barriers to such finance have been removed.
Culture and Beliefs	All stakeholders across the ecosystem have incorporated just transition and sustainable finance practices into their core operations and business as usual decision-making. Incentive structures are expanded beyond simple profitmaking, and are also aligned with climate and developmental outcomes and impacts
Market Integrity	ESG disclosure measurement is standardised and effectively measures environmental, social, governance and developmental impacts and outcomes. ESG standards are adopted by all and applied with integrity and consistency. ESG standards are implemented and incorporated as standard financial market integrity practices.
Financial Access	Access to finance is universal, and appropriate new sustainable and developmental instruments, mechanisms, support systems and institutional arrangements have been put in place to systemically support real economy financing needs at a sector, industry, project and transaction level.
Financial Institutional Mix	The ecosystem reflects a rich and diverse collection of financial institutions and financial support services which collectively provide the necessary scope and depth of sustainable finance mobilisation and deployment to meet the diverse nature of real economy financing needs – most especially those related to small enterprise funding, place-based investment, early stage technology funding and impact investing

Source: Author, inspired by UNEP-WB, 2017

Third: Just transition projects will require a behavioural change in the financial ecosystem which fosters collaborative and sincere engagements with partners in, and parties to, just transition transactions. The finance ecosystem response will need to include becoming more involved with project counterparts and engaging with project design and development earlier than is undertaken at present. Just transition projects will require the finance ecosystem to respond to the demand for finance access by traditionally marginalised groups especially the youth, women, small and medium enterprises (SMEs), start-up entrepreneurs and communities with no commercial track record. To enable and support these more collaborative engagements, the system, as a whole, will need to offer a greater range of support services, capacity building and technical assistance as part of its business as usual offering.

Fourth: The nature of just transition projects and their financing requirements suggest that a fourth requirement of a just transition aligned finance ecosystem will necessitate institutions and enterprises within the financial ecosystem learning to work together in new and innovative collaborative ways. Due to the portfolio nature of most just transition projects, inter-financial institutional relations along the investment value chain will need to become

increasingly integrated, mutually re-enforcing and seamless (Naidoo 2021). Increased explicit institutional co-ordination will be needed – a role which does not exist in the current system. The ecosystem will also need to respond to increased partnerships and co-funding between the public sector and the private sector; and between the domestic finance sector and the offshore investors and financiers – especially Development Finance Institutions (DFIs) and Multilateral Development Banks (MDBs). Partnering and pooling of investors will likely be a defining characteristic of a future just transition financing ecosystem.

South Africa’s finance ecosystem has experimented with solutions for some of these in a piecemeal fashion, as seen for example in community investment trusts as part of the Renewable Energy Independent Power Producer Programme (REIPPP). Support for system level change (as opposed to ad hoc and piecemeal change in a business as usual scenario) will require a rich and dynamic mix of iterative thinking about an evolving enabling environment, new behaviours and cultures about climate and social risk and opportunities; and a plethora of innovations in incentive structures, instruments, institutions, frameworks and technology application.

ROADMAP ACTION PLAN 2022-2025

The organising idea informing the action plan is that, in these early days of just transition financing, the imperative is not to foresee the future but to enable it. As financing a just transition will be a collective effort, the identified enabling activities include all major stakeholders in the finance ecosystem. Enabling activities are viewed more broadly than merely state regulatory and policy measures and include proof of concept, and institutional and instrument experimentation at scale to create a body of evidence to guide future thinking and iterations of subsequent action plans. In this iteration, roadmap stakeholders are divided into state, private and international players. More granular action plans which distinguish between different types of private sector investors for example will be required in the future.

This first iteration of an action plan is organised around: 1) public finance measures, policy and regulation; 2) financial instrument innovation; 3) financial institution culture and behaviour; 4) disclosure, monitoring and evaluation; and 5) international financial flows.

Public finance measures, policy and regulation

The state plays a pivotal role in supporting the creation of an enabling environment for sustainable finance through its core institutions: National Treasury, the South African Reserve Bank, the Prudential Authority and the Financial Sector Conduct Authority. The current state focus is to ensure the stability of the financial system in the face of environmental and social risks. To achieve this it aims to “ensure all financial institutions embed and improve their capacity for identifying, managing and disclosing the environmental and social risks in their portfolios” (National Treasury, 2020). Although social risks are included as a challenge, current state policy and regulatory thinking has prioritised environmental risk. Work and thinking on social risk lags behind. The civil unrest of July 2021 indicates that **social stability needs to be accepted as a real and imminent risk** and that such risk increases exponentially as accelerated decarbonising investments and climate change threaten jobs and community livelihoods.

A first action item therefore is for state finance institutions, bodies and authorities (henceforth referred to as state finance entities) to recognise that social risk identification, management and disclosure need to be prioritised alongside environmental risk and not as a lesser risk to be dealt with at a later date. Such prioritisation will accelerate state finance entities to develop official and transparent views on what they consider a just transition. The work of the Presidential Climate Commission and Inter-Ministerial Committee on the Just Transition should provide valuable direction and signals. However, each state finance entity will require an internal process to frame, develop and articulate an official just transition view.

An official position in each state entity will inform the entity’s mandate. This mandate will explain the role of levers and methods available to the entity to support

the behavioural shifts required to unlock adequate just transition financing in a sustainable manner. Such positions and mandates will not be easily arrived at given the overlap between a just transition agenda and a more generalised national socio-economic development agenda and climate agenda. The action plan calls on state finance entities to hasten internal activities to support position and mandate clarity, given that both provide crucial signals to the private and offshore financing community.

TIPS’s 2021 research reflects the frustration of local private finance sector institutions, institutional investors and the vanguard of offshore just transition financiers at the lack of clear state signals and expectations about just transition risk, management, disclosure and financing. Increased certainty and better communication of consistent signals would unlock increased just transition financial flows. Clarity on state finance entity views and mandates on the just transition are a prerequisite for any change in policy or regulatory requirements.

A second action identified for the state finance sector in the four years to 2025 is to scope and fund a series of short, focused research projects on possible levers in the state’s arsenal to support place-based just transition finance flows. There is broad agreement that a body of evidence is required to inform policy and regulatory reform necessary to unlock and allocate capital for just transition investments. This body of evidence can only be generated if experimentation at scale, proof of concept investments, and demonstration-effect programming on the ground is undertaken monitored and evaluated.

Multiple state levers exist that can be used to support such evidence-generating activities, and research plays an important role in identifying the costs, benefits, effectiveness and suitability of such levers to deliver widescale appropriate experimentation and learning.

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Several levers are available to state finance entities that can support the creation of an enabling environment for just transition financing flows, experimentation and learning. The use of these levers must be seen in the context of a broader state position on who will pay for, and who will benefit from, just transition activities.

The research approach should include lessons already learned in South Africa through interventions such as: REIPPP; the early proof of concept for Climate Investment Funds (CIF) renewable energy funding and impact case studies; and existing tax exemptions for revenue from trading certified emissions. Important insights on levers could also be sourced from the experiences of international coal transitioning regions.

Based on TIPS's 2021 research, several (non-regulatory) levers are available to state finance entities that can support the creation of an enabling environment for just transition financing flows, experimentation and learning. The use of these levers must be seen in the context of a broader state position on who will pay for, and who will benefit from, just transition activities. At the heart of the debate is the role of the state and its position on providing social security measures for workers and communities negatively affected by climate action.

This debate is not limited to the just transition context and takes place amid a broader national discussion on the Basic Income Grant and the COVID-19 Social Relief of Distress Grant. This first iteration of a Just Transition Finance Roadmap, notes the fundamental contextual importance and impact of the social security measure debate on just transition financing but does not explicitly suggest actions on the topic in the four years to 2025 due to the lack of clarity of the position of state entities on the subject. It is anticipated that such measures will be central in a second iteration of a roadmap action plan.

A first lever state finance entities should research and consider is improving the capital position of the country's development finance institutions (DFIs). Due to limited fiscal space, the state is currently unable to underwrite the losses of the country's DFIs or support DFIs to offer substantial quantities of grant and highly concessional funding. As a result the country's DFIs operate on a largely for-profit basis with limited space to act on their developmental mandate.

As a precursor to a formalised conversation about a South African Just Transition Fund (see Institutions section on page 8), and how such a fund should be structured and operate, an injection of capital ring-fenced for Just Transition project finance for local DFIs would provide valuable evidence and insight into just transition finance deployment, transaction structuring, risk return profiles, and the integration of just transition economic diversification investments into broader value chains.

Improving the capital position of South Africa's DFIs would also lay a basis for increased experimentation and learning about blended finance and crowding in private sector funding.

Given the current limited fiscal space of the South African government, the role of international DFIs and Global North governments that made financial pledges under the Paris Agreement and COP26 could become an important source of cheap (or free) capital. Research into the true cost of overseas concessionary finance made available to South African DFIs needs to be considered as a matter of urgency. Benefits can be appraised based on outcomes achieved using such funds.

In addition to increased direct financial support to DFIs, financial state entities need to consider the range of credit enhancement tools at their disposal, and identify if the deployment of such tools would be advantageous in the current context of just transition activity. Key credit enhancement tools to consider and evaluate are: risk buy-down schemes, state-backed guarantees, political risk insurance, and risk pooling facilities. Any assessment of the merit of the state providing such enhancements must be balanced with the state's fiscal space and competing needs. In the International Finance Institutions (IFIs) analysis that follows it is suggested that the state enter discussions with IFIs about the role they can play in such credit enhancement schemes.

A second lever for public finance entities to consider is the use of incentives to drive desired behavioural change. Incentives such as tax free status for interest and other income received from just transition instruments would support increased portfolio allocation into such instruments. Alternatively, just transition projects could be directly incentivised using research and development (R&D) and accelerated depreciation tax incentives. Incentives in the green and sustainable finance space provide local precedent and a body of evidence to assess the costs and benefits of such schemes. Of particular interest would be: an analysis of the effectiveness of the tax exemption for revenue earned from trading certified emissions; the impact of the accelerated depreciation for machinery used for renewable electricity generation and biomass; and the effectiveness of the R&D incentive for green technology.

In addition to traditional incentives, public finance entities must consider more novel incentivisation programmes. National Treasury identifies the key challenge facing financial institutions as the need to expose staff to new areas of knowledge in ways that

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support new behaviours and decision-making. New skill development, behaviour and decision-making will be driven by experimentation and learning by doing. Treasury argues that the development of such knowledge and skills must take place at a transaction level first, then at a portfolio level, and ultimately at a system level. In the short run there is therefore an argument that public finance entities must consider and research how best to incentivise private financial sector experimentation at the transactional level. The outcome of the incentive is increased experimentation and learning that supports new skills development and capabilities.

A third lever at the disposal of state financial entities is the adoption of policies to support line departments and local municipalities funding just transition demonstration and proof of concept novel funding solutions, mechanisms and instruments, not novel technology. Support could be provided directly through the budget, through DFIs, or as a blended finance option with the participation of the private sector. Such “flagship projects” could provide a demonstration effect of what is possible in innovative funding of just transition projects. It is not clear whether this is an appropriate course of action. Previous flagship projects in the climate finance space have been unsuccessful.

A fourth potential lever state finance entities must begin to research and engage on in the next four years is establishing a Just Transition Fund. Debate on the mandate, structure, operations and positioning of such a fund is heated. This lever is considered in the Institutions section on page 8.

Instruments

The South African financial ecosystem is sufficiently dynamic and sophisticated that innovative instrument development is not a system level bottleneck. In response to a mandatory policy requirement or an attractive risk-related return, the current financial ecosystem can efficiently and effectively create the necessary instruments for a just transition *if it wants to*. To make financial institutions want to develop such instruments will require: clear and consistent public sector signalling, ramped-up regulatory pressure (such as that seen in ESG regulations for environmental risks) and support in the form of credit enhancements, de-risking and possibly sweeteners to support creative innovation. Sweeteners could include: cost sharing on due diligence and transaction costs²; incentives to experiment; and tax breaks on new instrument returns. Such incentives will be complex and time-consuming to deliver.

In the next four years the action plan suggests that four areas of instrument innovation be focused on. This prioritisation is based on interviews with stakeholders, current areas of activity and research in the domestic and international market, and just transition project characteristics identified in the 2021 TIPS research. Progress in these four areas will support increased learning by doing and inform longer-term instrument innovations in subsequent iterations of the roadmap.

The first area of instrument innovation prioritised to 2025 relates to bonds³ and standard issuances of Domestic Term Note Programmes⁴ and Commercial Paper⁵ widely used by large corporates and in the listed securities market. These instruments can be adapted for purpose driven capital raisings to support the mobilisation of funds for the just transition in both the short and long run. The required innovation is to define an initial just transition use of proceeds. A first iteration will provide guidance to investors and support experimentation and the creation of an evidence based and lessons which can inform future developments.

The action plan suggests that an initial framework for a just transition use of proceeds be researched, developed and piloted in South Africa. The framework will provide guidance to financial system ecosystem players and large non-financial corporates looking to dip their toe into just transition investing.

Research and drafting should build on the deep thinking completed by the Development Bank of Southern Africa (DBSA) for its Green Bonds and Just Transition Bonds, the new ESG guidance published by the JSE (which includes specific recommendations for just transition indicators) and the broad array of international frameworks developed in the Global North. The research should culminate in a first iteration use of proceeds description with related indicators and metrics (see Disclosure, monitoring and evaluation section on page 10). This guidance is an important step in creating an enabling environment for instrument experimentation and learning by doing.

² *Could be achieved by expanding the use of corporate responsibility investments to cover such costs.*

³ *Securities with a maturity profile over 5 years. The bonds considered are designed to offer a financial return and do not include Social Impact Bonds.*

⁴ *Securities with a maturity profile between one and five years*

⁵ *Securities with maturity profiles of less than one year.*

TIPS research in 2021 identified the need to provide just transition project developers with technical support and access to financiers earlier in the project development cycle than in traditional investments

A second instrument which should be prioritised for innovation and experimentation in the local context is the social impact bond (SIB). This bond market is nascent but scaling up such a market creates the opportunity for new investment partners in the just transition. SIBs are technically not a bond as such as repayment and return on investment are contingent on the achievement of desired social outcomes. If social outcomes are not met, the investor gets no repayment of the principle and no return. If social outcomes are achieved the investor receives a return, but case studies show that the rate of return is well below the market rate. SIBs currently exist because there are investors who place value on social impacts and not only financial returns. SIBs are notoriously difficult to structure because it is hard to determine the success of a SIB, given that social impact is hard to measure.

To date, globally, the SIBs market is dominated by issuance from the public sector. In a 2050 vision of a financial ecosystem better aligned to government social development and climate policy, expanded private sector issuance of SIBs would be anticipated as part of a business as usual scenario.

The action plan suggests that in the next four years public sector DFIs (especially DBSA) make meaningful progress on testing the market and providing experimental evidence of the challenges and potential of SIBs as an instrument to fund a just transition. Such experimentation would provide proof of concept and an important signals to the broad financial ecosystem of the challenges and merits of SIBs. Such evidence and signalling would create space for the JSE and even banks and pension funds to consider listing social impact bonds, or privately placing such bonds to attract investment from philanthropic investors or high-net worth individuals. This would widen and diversify the source of funds being tapped to invest in the just transition.

A risk pooling mechanism is the third instrument identified for investigation and experimentation in the four years to 2025. Risk pooling is the collection and management of financial resources so that large, unpredictable individual financial risks become more predictable, and are distributed among all members of the pool. The findings of the place-based research sample of just transition projects in Mpumalanga clearly shows that a defining characteristic of just transition projects is that they are not a single standalone investment but a portfolio of interrelated and interdependent projects, which have a diverse range of capital requirements and return profiles.

The just transition challenge for the financial ecosystem is to fund such portfolios as a unit without cherry picking high-return individual projects. To achieve the required funding solution, a myriad of different types of investors need to come to the table simultaneously. These different financial actors will need to collaborate and structure their investments such that residual risks are shared across participants. In principle, the state or offshore DFIs could support such risk pooling as part of their credit enhancement approach.

The action plan proposes that research and discussion on such a mechanism be prioritised and fast-tracked as it is a necessary enabler to support instrument innovation and experimentation to support the financing of suites of just transition projects. This could initially take place through the existing National Treasury Sustainable Finance work stream on instruments (if the scope of the work stream is/or could be expanded to include the just transition).

A fourth instrument issue for action to 2025 is for the public and private sector to undertake an inventory of unutilised sources of finance that can potentially be leveraged to increase financial flows towards a just transition. For example, regulations published under the National Environmental Management Act No. 107 of 1998 require all mining operations to make a financial provision for mine closure. This provision guarantees that sufficient funds are available to undertake the rehabilitation of environmental damage caused by mining activities. Such monies are distributed across different institutions. Similarly REIPPPP requirements have resulted in considerable enterprise development and Socio-Economic Development (SED) contributions which have not been deployed. Once an audit of such funds has been made, a collaborative effort between the public and private sector can be considered to think through options of how such funds can best be leveraged to increase financial flows to just transition investments.

A final instrument to be considered in the next four years is a possible expansion to the accepted uses of Corporate Social Investment (CSI) monies in South Africa. The 2021 TIPS research identified the need to provide just transition project developers with technical support and access to financiers earlier in the project development cycle than in traditional investments. The research also highlighted the challenge of funding low-ticket price projects due to high transaction costs. These high transaction costs are largely driven by high due diligence costs. Using CSI funds to decrease due diligence and transaction costs, and to fund technical support and closer relations with financiers, early in the

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project design process will fundamentally improve the quantity and quality of the just transition project pipeline. Amending the accepted uses of CSI to incorporate this may be an important contribution to addressing the project pipeline challenge which has long been a system level challenge in South Africa.

A discussion of instrument innovation for a just transition would not be complete without addressing the issue of scale and the preference of financiers to fund large programmes of work instead of individual projects. Attaining scale is a necessity to achieve South Africa's NDC commitments as well as to mobilise offshore funding (especially Paris Agreement pledges). The adopted theory of change underpinning the roadmap foresees that lessons learned at a project level will support the development of larger just transition finance mechanisms over time. This approach is aligned to National Treasury thinking (National Treasury, 2020). Options for larger funding opportunities are already emerging from the Mpumalanga sample of projects where a thematic financing instrument for a range of water rehabilitation projects is being considered.

Institutions

Any envisaged long-term system level change will be accompanied by significant institutional change. Long-term changes to support the financing of a just transition in South Africa would likely include a change in the composition of ecosystem players, such as an increase in the number and size of impact and angel investors, venture capitalists and fund of funds. This compositional change will also likely include new institutions such as entities to co-ordinate and convene groupings of different types of investors to finance a differentiated suite of projects under a single project banner. Financial institutions would also need internal changes to key performance indicators and incentive structures to increase the allocation of capital to just transition investments.

For example, if bonus calculations include an assessment of funds allocated to just transition projects, individual financier's activities will become more aligned with corporate just transition goals. New and extended skills and capabilities will also be required. New skills will include the ability to: engage with ESG and just transition metrics and indicators; co-create projects and provide technical assistance in the normal course of business; collaborate and co-ordinate with other ecosystem players; design new risk and project evaluation frameworks; and an increased ability to collaborate with the public sector and offshore sector.

The short-term action plan for institutions is modest, given the lack of public sector signalling and an enabling environment. The three areas identified for focus to 2025 are: increasing awareness and inclusion of just transition goals in corporate investment strategies; supporting institutions willing to begin experimenting with just transition investments; and consideration of the institutional options for establishing a Just Transition Fund for South Africa.

Outreach, awareness and communication are core elements of most current global just transition roadmaps. In specialist research commissioned for the roadmap Nicole Martens (2021) found that local financial institutions with formal ties or exposure to Global North markets have a deeper and more confident view on just transition risks and opportunities. Local institutions without such exposure did not exhibit the same degree of understanding. A need therefore exists to support, educate and sensitise financial institutions about just transition investing. The action plan calls for increased outreach, awareness and communication with the entirety of the financial ecosystem. The Presidential Climate Commission, the Inter-Ministerial Committee on the Just Transition, Industry Associations, lobbying groups, researchers and academics all have a role to play. Key activities to consider include: working towards shared language; improved articulation of the narrative and discourse; straw man examples to move the needle on complex issues; access and dissemination of global shared views; best practice; case studies and standards; public private roundtables; and expanded engagement opportunities.

In line with the roadmap's underlying theory of change, the short-term action plan emphasises the need to learn by doing and hence to support those institutions best positioned to experiment with financing just transition projects in the near term, to provide proof of concept and case study evidence to crowd in increased experimentation.

Supporting research (Marten, 2021) on local willingness to experiment raises an interesting local dynamic. In developing countries, financial institutions are actively seeking first mover advantage in the just transition finance space (Robins et al, 2019).

In South Africa, financial institutions (which express a keenness to invest in just transition projects) are not closing such deals for fear that civil society organisations and labour will publically challenge their definitions, ambitions or positioning as just transition financiers. Reputational risk of just transition washing,

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or in being linked to self-identified just transition investments, is viewed as prohibitively high in the domestic market.

With definitional uncertainty, a lack of clarity on government expectations, the nascent nature of the just transition finance space, and a South African concern about reputational risk, it is very difficult to imagine that the local private sector will unilaterally take the first step in investing in a proof of concept experiment at scale. Similarly, given the process of establishing a just transition view and mandate across public finance entities, it is unlikely that direct public finance measures, line item departmental budgets, or even DFI investments, will be forthcoming without substantial risk sharing from global investors, IFIs or MDBs.

The role of foreign DFIs and MDBs in supporting experimentation, proof of concept and market was well documented in the renewable energy space in South Africa in the early 2000s. This approach will need to be replicated for just transition project finance, proof of concept of innovative financial structuring, instrument design, project assessment, risk pooling, and implementation. Such a proof of concept could form part of the COP26 Political Declaration task team's deliberations. A preferred option would be the use of existing global climate financing platforms and mechanisms mandated to support developing countries to implement their climate obligations. Various on-the-ground programmes already operating in the climate finance space in South Africa could be approached and progress made in 18 to 24 months to finance at least two proof of concept projects.

The third and most topical institutional consideration in the just transition finance space is the idea of a single, purpose built, Just Transition Fund. The European Union (EU) Just Transition Mechanism (JTM) provides the most resolved thinking of a Just Transition Fund (JTF) in the current literature. The example demonstrates the complexity of public sector led just transitioning financing. Although the EU model is not a replicable model in the South African context (both because of capacity constraints and a lack of fiscal space) it is a useful case study in that it highlights the broad array of financing necessary to support a just transition. In the EU model a JTF is just one part of a broader and more complex Just Transition Mechanism.

The JTM is complex and multitiered. At its centre is the provision of key tools to support locations negatively impacted by the undertaking of climate

neutral activities. Three tools are available for a qualifying location.

The first tool is a JTF. This fund is designed specifically to alleviate the socio-economic costs triggered by climate transition. The fund supports the economic diversification and reconversion of negatively impacted locations. Funding is used to back productive investments in SMEs; the creation of new firms; research and innovation; environmental rehabilitation; clean energy, upskilling and reskilling workers; job search assistance; and active inclusion of job seeker programmes. The JTF does not have to fund strategic investments in infrastructure, this is provided by the second part of the JTM – the just transition scheme under InvestEU.

InvestEU is a strategic investment plan to broadly support a green and competitive European economy. It includes a dedicated facility to support a broader range of strategic investments in locations negatively impacted by transitioning activities. The locations for the JTF and the just transition scheme of InvestEU are the same locations, but the scope of projects financed differs.

The just transition scheme of InvestEU funds can be applied to energy, transport and social infrastructure as well as decarbonisation projects and large-scale strategic investments in economic diversification investments. In this way funding from the just transition scheme of InvestEU provides funding for improving the strategic and enabling infrastructure in a qualifying location. This will assist the diversification and reconversion activities undertaken and funded by the JTF, which operates at a more micro level.

The terms of the just transition scheme of InvestEU are superior to the terms of the general InvestEU facility in that the EU provides budgetary guarantees to implementing partners of just transition projects. In addition, the just transition scheme includes the InvestEU Advisory Hub to assist in developing and implementing projects in such locations. The hub provides tailor-made technical assistance and capacity building for project promoters. In addition to supporting the development of project promoters, the hub also offers advisory support for the identification, preparation, development, structuring, procuring and implementation of projects in impacted locations.

The third and final pillar of the EU JTM is the Public Sector Loan Facility. The instrument is exclusively targeted to public entities to provide support to projects that do not generate a sufficient stream of own resources to be financed commercially.

While a Just Transition Fund may be part of the solution to mobilising and deploying funds in areas negatively affected by decarbonising actions, it will not be a complete answer and should not be viewed as a silver bullet. South Africa has an extensive track record of purpose-driven funds, such as the Jobs Fund, Infrastructure Fund, Green Fund and Youth Fund. An analysis of the effectiveness of such single, centralised, national approaches needs to be considered in the context of a just transition especially given the place-based nature of funding requirements.

Projects are expected to include: public infrastructure investments in areas such as energy and transport; energy efficient building renovation; and social infrastructure.

The EU approach suggests some signals that are relevant to thinking about just transition funding in South Africa. First, the EU approach supports the idea of a place-based or location-specific approach. Second, the separation of just transition funding for socio-economic outcomes (JTF) and funding for decarbonising and economic diversification infrastructure (just transition scheme of InvestEU) underscores the idea of thinking about separate pots of money for different desired outcomes. Third, the EU model acknowledges the crucial need to capacitate project promoters and to provide project development technical assistance as an integrated part of financing a just transition. Finally, the EU model shines a spotlight on the multiple layers of financing that will be required simultaneously to allow impacted locations to re-establish strong place-based economies and opportunities.

This suggests that while a JTF may be part of the solution to mobilising and deploying funds in areas of South Africa negatively affected by decarbonising actions, it will not be a complete answer and should not be viewed as a silver bullet.

South Africa has an extensive track record of purpose-driven funds, such as the Jobs Fund, Infrastructure Fund, Green Fund and Youth Fund. An analysis of the effectiveness and efficiency of such single, centralised, national approaches needs to be considered in the context of a just transition, especially given the place-based nature of such funding requirements.

Some suggest that a single, primary, just transition fund in South Africa will entrench the fragmentation of the present engagement of the just transition. These proponents suggest placing access to funds closer to the beneficiaries of such funds, and with limited use of intermediaries (Naidoo, 2021). Examples of such approaches can be found in Kenya's provincial climate change funds, India's mining restoration fund, and some regionally based United States funds. Similarly, it would be useful to consider the structure and operationalisation of climate investment funds developed by multilateral development banks to accelerate climate action.

These examples can provide rich learnings about how finance facilities located at different institutions can collectively deploy finance for shared outcomes. Ideas in the South African just transition finance discourse have raised the idea of locating just transition financing facilities within every financial institution such that each bank, pension fund and DFI would have access to a special pool of funding to support any residual risks of financing a just transition that such a particular institution is unable to absorb.

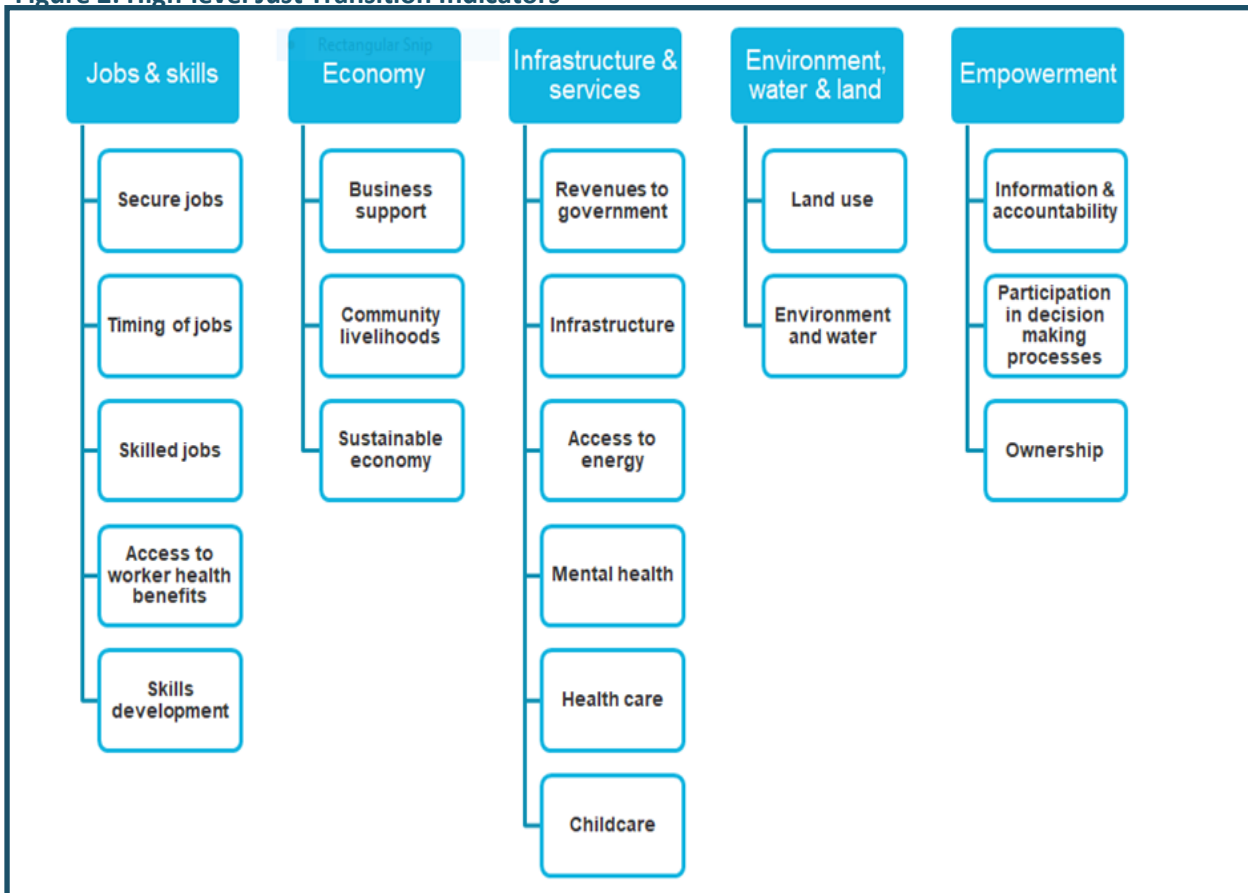
As an immediate action requirement, research must be commissioned to consider different possible institutional and operational structures for a South African just transition fund, or funds, or facility. An understanding of the different structure's pro and cons needs to be articulated, so as to fast-track and catalyse collaborative discussions between the private, public and offshore funding sectors on piloting or designing such a key institution/institutions/facility using existing institutions.

Disclosure, monitoring and evaluation

System-level mainstreaming of just transition finance will not become a reality until the tough nut of disclosure has been cracked. The green finance environmental disclosure discourse reveals three core dimensions of concern that will apply equally to the consideration of just transition disclosure.

First is the need for appropriate disclosure across all layers of the real and financial economy (including the public sector). This means that financial institutions as well as non-financial corporates will need to measure just transition outcomes. This makes the project an economy-wide project and not simply a financial sector challenge. Second is a lack of a common approach to what should be measured and how it should be measured. Approaches cover a spectrum of ambitions from measuring intention to impact to outcomes. Actual metrics of what is measured are also crucial to ensuring consistency and meaningful transparency. The final dimension of the disclosure discourse deals with disclosure requirements being voluntary or mandatory. Most current literature suggests that voluntary reporting is a first step to longer-term mandatory reporting, which will be a requirement for system level change.

Figure 2: High-level Just Transition Indicators



Source: Synergy Global, 2020

Over time all of these issues will need to be dealt with by iterations of just transition finance roadmaps. For the four years to 2025, the roadmap suggests that action focus on research, discussion and collaboration aimed at creating a **first cut, experimental list of “what needs to be measured” to identify and differentiate just transition investments from other types of investments.** Such a working list will support transaction and project level experimentation and learning by doing.

In research to support the roadmap, some interesting work on just transition indicators has been completed.⁶ Research by Synergy Global (2021) describes and measures a scenario of an unjust transition in which no action is taken to ameliorate the impacts of decarbonising activities on workers and the community.⁷ This is contrasted with an ideal scenario in which all active steps are taken to ensure that a transition is just and improves the socio-economic standing of workers and the community. The research then lists the activities that need to be undertaken to move from an unjust scenario to a just scenario. These actions become the list of what needs to be measured as just transition indicators.

The research considers broad buckets of indicators at a thematic level (Figure 2) as well as a disaggregation of each bucket into more specific indicators. It further suggests that the importance of some indicators will change over time and that the disclosure, monitoring and evaluation discourse needs to consider temporal dimensions of required just transition actions (investments) and hence indicators.

Language for disaggregated indicator descriptors, available data for metrics and temporal considerations all point to the complexity of moving the needle on what will and what will not qualify as a just transition investment in the South African context. Core to the disclosure discourse will also be decisions about how South African indicators and metrics align and converge with global standards and benchmarks. Such convergence is important in attracting offshore funds to local just transition investment opportunities.

⁶ Work is also being completed by Carbon Trust to add social indicators to the green taxonomy.

⁷ For example a coal mine closure in a mono economy town. Scenarios were mapped using historical data and research of gold mine closures in South Africa.

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The role of international DFIs, MDBs and Global North Paris Agreement pledges

There are diverse views on the role of IFIs in the funding of South Africa's just transition. Some believe international funding should be seen as an enhancement to local financing but not a substitute for it. Others believe that the Global North should pick up the entire bill for all South Africa's decarbonisation, climate change impact and transition costs. The government will play the determining role in negotiating the terms, conditions and extent of financial and non-financial support received from IFIs. This will be an ongoing task that will evolve over time with the COP26 proposal seen as an important initial marker of local agenda parameters and views.

The research underpinning the roadmap suggests several key issues related to offshore funding for the South African just transition. These are issues that government could consider researching and discussing in its current and future interactions with global players.

The first highlighted issue is that just transition finance in South Africa needs to be considered as a separate pot of money from climate finance money due to the difference in investment drivers, outcomes, returns and deployment instruments. This distinction is acknowledged by the EU where money set aside for decarbonising and greening the EU economy was later augmented by fresh, additional budgetary allocations ringfenced specifically for just transition projects. This distinction impacts how a funding package (such as the US\$8.5 billion that was announced at COP) is allocated between decarbonising actions and just transition actions.

The second issue on the role of IFIs in South Africa's just transition relates to the terms and conditions of funding and their impact on fiscal space. Offshore inflows in the form of loans (even if at 0% interest), or deals which require government guarantees, will decrease domestic fiscal space. However, substantial grants received from IFIs can expand the fiscal space.

Increased fiscal space could be created if IFI grant funding catalyses higher GDP growth, resulting in increased taxation revenue. Increased fiscal space could also be created if, for example, social

infrastructure projects or economic diversification projects currently financed by the government in locations that qualify for just transition funding, could be funded from a new and separate pot of IFI grant monies. The idea of substituting IFI just transition grant money for budgeted social development funding could offer expanding fiscal space for government as decarbonisation activities are accelerated across sections and locations. Such increases in fiscal space could allow the government to adopt expanded social protection measures, especially income support measures such as a basic income grant or worker income support programmes for workers who lose their jobs through decarbonisation activities.

A third issue related to IFI funding focuses on what type of just transition funding is required in the short term while the country is experimenting and learning about just transition finance. The roadmap urges that the discourse with IFIs on the quantum of just transition finance required in South Africa urgently be expanded to consider the quality of such funding. Specifically, a conversation needs to begin about whether the financial flows being offered by the Global North, match the demand for funds as characterised by current place based just transition project evidence.

The roadmap also suggests that the government prioritise work on accessing offshore funding to inject capital into the country's DFIs to support a specific just transition mandate and use of funds. Negotiations with IFIs should also look at how such institutions can assist the South African finance ecosystem to experiment with new and novel financial approaches, instruments and mechanisms. IFIs could provide support to funding proof of concept projects and assist in making a market for just transition finance.

Detailed conversations are also required with IFIs on the specific types of de-risking, credit enhancement and blended finance support required in these early days of moving towards a system level change for the ecosystem as a whole.

Finally, but no less important, the role IFIs and partner governments can play in supporting research, knowledge transfer and capacity building needs to be considered and actioned.

Negotiations with International Finance Institutions (IFIs) should also look at how such institutions can assist the South African finance ecosystem to experiment with new and novel financial approaches, instruments and mechanisms. IFIs could provide support to funding proof of concept projects and assist in making a market for just transition finance. Detailed conversations are also required with IFIs on the specific types of de-risking, credit enhancement and blended finance support required in these early days of moving towards a system level change for the ecosystem as a whole.

CONCLUSION

The roadmap takes as a point of departure the contested view that just transition funding needs to be understood as a separate pot of money from broader climate finance. The roadmap acknowledges that climate finance and just transition finance are fundamentally interrelated and intertwined and most often negotiated as a single tranche of funding. Research, however, shows that decarbonisation transactions and just transition transactions will chase different outcome measures resulting in different risk return profiles and use different instruments and deployment channels. It is therefore necessary to understand just transition finance supply and demand as a separate use of funds.

The roadmap is also a major departure from international equivalents which focus heavily on conceptual and theoretical analysis. This global trend has led the current just transition finance discourse to be labelled as “stratospheric” (Robins et al, 2019). In designing the research to underpin this first iteration of a just transition finance roadmap in South Africa, stakeholder groups were interviewed. Collectively stakeholders argued against a stratospheric approach and called instead for a focus on creating traction, moving the needle, and actually implementing just transition activities on the ground. On this basis a bottom-up, place-based research approach was adopted aimed at creating a body of evidence to inform an agenda of change.

The financial ecosystem agenda of change presented delivers both a long-term vision of a financial system which mainstreams just transition finance in a business as usual scenario; and an initial set of actions to begin moving the country and involved stakeholders in the direction of such a long-term vision.

The theory of change linking the proposed short-term action agenda to 2025 and the long-term 2050 vision is based on experimentation and learning by doing. All short-term action items for the next four years either directly support experimentation and learning by doing; or support the creation of an environment which will enable increased experimentation and learning by doing.

Many of the activities to enable learning by doing necessitate the creation of reductionist, simplified answers to highly complex questions. For example, the roadmap suggests that a working version of just transition indicators be adopted to support proof of concept just transition investment decisions.

Such a working version will be imperfect but will become a basis for increasingly sophisticated articulation through future iterations of the roadmap. Importantly, such working versions will always be subject to increased learning and understanding arising from more conceptual and theoretical work on the issue. As such, it is crucial that the short-term actions of the roadmap consistently be appraised and considered within the broader discourse of not only just transition thinking but also relevant thinking from the broader climate finance field.

In this initial iteration, financial ecosystem stakeholders are dealt with at the broadest level of public, private and IFIs players. As just transition thinking evolves, more granular actions will be required across different classes of investors and other operators in the investment value chain. This level of disaggregated action identification needs to be fast tracked and should play a prominent role in the second iteration of the roadmap.

Finally the roadmap has been drafted in a busy space with many parties auctioning work related to just transition funding and projects. Care has been taken to try to complement existing processes and activities and to build in mechanisms to learn from related workstreams. The roadmap is a living document and will benefit from constant revision, updating and engagement

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