THE ITALIAN INDEPENDENT ENERGY AND CLIMATE CHANGE THINK TANK

POLICY PAPER

AN ITALIAN CLIMATE FINANCE STRATEGY. COMMITMENTS, RESOURCES AND CHANNELS

October 2021

This paper analyses and identifies new climate finance commitments in the run up to the G20 Summit and COP26 in Glasgow, as well as the strategic levers at our disposal and how to use them to achieve our goals. The paper follows on from the initial report published in June 2021 entitled "Finanza per il clima: Dove siamo, dove andiamo e quali nuovi impegni per l'Italia". [Climate Finance. Where we are now, where we are heading and new commitments for Italy]

Sections:

KEY POINTS – EXECUTIVE SUMMARY

Keeping the USD 100 billion pledge made in Copenhagen in 2009 and confirmed in Paris in 2015 is crucial for the success of COP26. Without this sign of support and trust between nations, it will be hard to build the foundations of an agreement at COP26. The deadline for mobilising the USD 100 billion a year was 2020. The latest OECD figures for 2019 show that there is still a gap of USD 20.4 billion. The announcement by the United States of USD 11.4 billion in bilateral public finance at the United Nations General Assembly (UNGA) on 21 September goes some way towards closing the gap. As well as bilateral finance there will also be multilateral and private finance for an estimated potential total value of USD 25-30 billion. However, the public finance is dependent on a vote by Congress and this uncertainty effectively leaves open the question of when the gap will be closed. Other donor countries will therefore play a decisive role not only in reaching but in exceeding the USD 100 billion, which is still just a fraction of the estimated global climate requirements. All the G7 countries - with the exception of Italy - made new commitments at the G7 Summit in June.

The G7 leaders have committed to increasing international climate finance resources to 2025. Italy is the only G7 country that has not yet presented new commitments, and is also behind in complying with the commitment it made in Paris to mobilise a cumulative USD 4 billion between 2015 and 2020. The estimated commitment gap at the end of 2020 is USD 800 million, following reported average annual expenditure (2015-2019) of USD 500 million, which equates to 0.5% of the USD 100 billion.

At the UNGA, Prime Minister Draghi committed to presenting a new climate finance commitment before COP26. The available estimates for Italy's fair share of the USD 100 billion are between 3.4 and 4.7%. **If we take as an example a fair share for Italy of 4%, or USD 4 billion per year (equivalent to approximately EUR 3.4 billion)**, **then Italy would only reach 12.5% of its fair share according to current reporting.**

By using all five of the strategic levers identified and detailed in this report, Italy has all the requisites to reach and to exceed its fair share of USD 4 billion per year well before the end of 2025. However, a strong push and political commitment is needed, starting with Prime Minister Draghi, in order to make new commitments and to embark on a far-reaching process of reforming, tracing and allocating public finance and mobilising private climate finance.

The G20 Summit in Rome and COP26 in Glasgow are key opportunities for Italy to make new commitments, i.e.:

1. **to close the deficit, estimated to be USD 800 million, no later than 2022 in line with its commitment made at the COP21 in Paris in 2015;**

2. **in addition to closing the deficit, to double effective public finance spending in 2022 to EUR 1 billion** (approximately double effective average annual spending as already supported by Minister Cingolani);
3. **to commit to presenting a "Climate Finance Roadmap" in 2022 outlining how to reach the fair share of USD 4 billion (EUR 3.4 billion) per year well before the end of 2025.** This would leave the administrations sufficient time to adapt and to plan for the necessary resources.
4. **to commit to allocate and manage climate resources in such a way that at least 50% are set aside for investments in adaptation, loss and damage** as set out by the United Nations Secretary-General Antonio Guterres and the COP26 manifesto for vulnerable nations;
5. **to accompany the 2022 doubling with an additional EUR 250 million in public finance per year from 2022 to 2025 to create a "Climate Fund" at the Cassa Depositi e Prestiti (CDP).** The aim is to significantly increase private finance mobilised by means of public interventions and a 1:3 leverage effect. Achieving this goal each year from 2022 would mean mobilising an additional EUR 2 billion in climate finance by the end of 2025.
6. **to commit to completing payment of the first contribution to the Green Climate Fund by the end of 2023 and to doubling the second contribution, to reach a total of EUR 600 million;**
7. **to double its contribution to the Adaptation Fund bringing it to EUR 60 million a year and renewing it each year from 2021 to 2025** (compared with the EUR 30 million paid to December 2020 by Conte's government);
8. **to take part in climate-risk insurance and forecast-based finance programmes** to support countries affected by extreme weather and already exposed to significant loss and damage;
9. to reallocate part of the USD 20.6 billion of the Special Drawing Rights allocated to Italy by the International Monetary Fund (IMF), for example **USD 2 billion, to the new IMF Resilience and Sustainability Trust.**

The five strategic levers available to Italy are:

1) **Bilateral**: The resources available to the Ministry of Foreign Affairs and International Cooperation (MAECI) and the Italian Agency for Development Cooperation (AICS) are not specifically dedicated to the climate at the moment. The share of Official Development Assistance (ODA) for climate needs to be increased. Italy should aim to reach a climate finance-to-ODA ratio of 30% by the end of 2022, 40% by the end of 2023 and 50% by the end of 2024. Germany and France have already reached similar levels. This would translate into a contribution of EUR 458 million with the current ODA, which has remained at 0.22% of gross national income. If instead, as is to be hoped, ODA were to be brought to at least 0.5% in 2025 and 0.7% by 2030 in line with the European goal - and at the same time the climate share of ODA were increased to 50% - this would mobilise up to EUR 4.5 billion (at 2020 gross national income levels) and cover the fair share entirely. At the same time three key operations are necessary. The first is mainstreaming. In other words to apply climate goals to all

Italian cooperation. The second is to revise cooperation governance. Finally, the third is to update the AICS sector climate and environment guidelines. Another priority is also to dedicate 100% of the revenues from emission trading system (ETS) auctions to national and international climate finance rather than dividing them between the Ministry for Ecological Transition (MITE) and the Ministry of Economics and Finance (MEF) as is currently the case. This would require an amendment to the Decree governing the sharing of ETS auction revenues. The revenues for international climate finance would amount to EUR 1.1 billion a year (at 2021 CO2 prices).

2) **Multilateral**: Italy is not just a contributor to the replenishment of the main multilateral climate funds, it also participates in the replenishment of Multilateral Development Banks (MDBs) and International Financial Institutions (IFIs) by means of its MEF. Payments are negotiated and agreed by means of the relevant governance mechanisms. If Italy were to play a more ambitious role in these processes with higher levels of replenishment by means of its MEF, this would considerably increase multilateral public climate finance, which was unchanged at USD 276.5 million in 2019. Alignment with and achievement of the Paris Agreement goals also needs to become another strategic priority of MDBs and IFIs. Finally, should the International Monetary Fund's new Resilience and Sustainability Trust (RST) dedicated to the reallocation of Special Drawing Rights (SDRs) be considered climate finance, reallocation of part of the USD 20.6 billion allocated to Italy - say USD 2 billion - would significantly increase Italy's climate finance share.

3) **Private Finance and the CDP**: Mobilising private finance using the public lever is a great opportunity but remains challenging for Italy, which only managed to report EUR 61 million in private finance between 2015 and 2018. In comparison, Germany managed to report almost EUR 1 billion in just two years in 2017-2018, while France had already recorded EUR 1.2 billion in 2014-2015. The role of the CDP as a climate development bank needs to be reinforced. One way could be through a public endowment of EUR 250 million per year to the new "Climate Fund" in the Budget Law and/or auctions, in order to increase private finance mobilised through a 1:3 lever effect. This would equate to mobilising an additional EUR 1 billion a year, three-quarters of which would be from private finance. Furthermore, unless the system of reporting and tracing public finance is improved, it will not be possible to report it and to have information about volumes, projects, geography and impacts.

4) **Private Finance and SACE and Simest**: The Italian Export Credit Agency SACE can play a key role in supporting and mobilising private investments. This will require a shift away from the current support for fossil fuels to "green credits and guarantees". Between 2016 and 2020, SACE supported the Oil & Gas sector alone through EUR 10.8 billion in new volumes. SACE should therefore be aiming to mobilise at least EUR 2 billion a year in green credits and guarantees, at the same time ending its support for fossil energy investments by the end of 2022. The role of the Italian Company for Mixed Enterprises Abroad (Simest, majority-owned by SACE) must also play a stronger role in supporting "green"

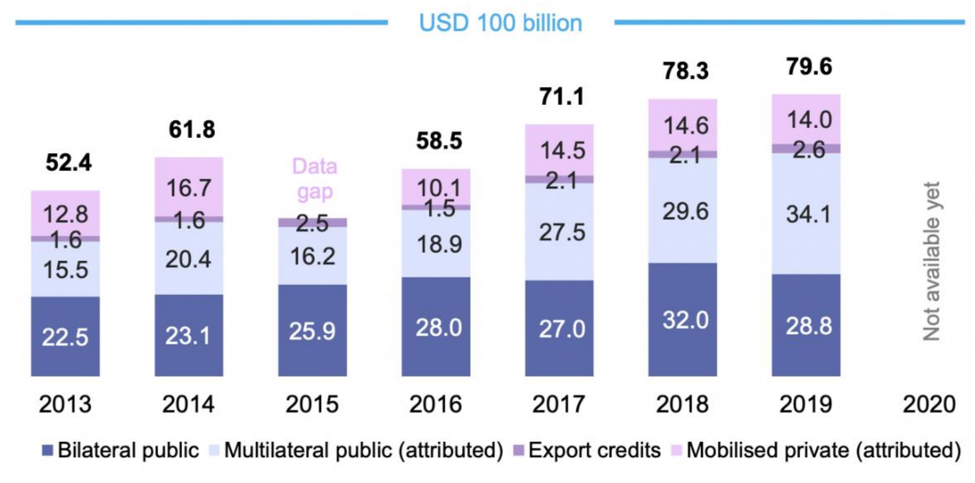
investments and enterprises and end its support for activities directly or indirectly linked to fossil fuels.

5) **The Budget Law and Fossil Fuel Subsidies**: The law should increase the public resources dedicated to international climate finance (like the new CDP “Climate Fund”). Resources should be generated by reallocating public resources, such as environmentally harmful subsidies (SAD), which include EUR 17.7 billion of fossil fuel subsidies, and which should be eliminated by the end of 2025 in line with the G7 international commitment. Reallocating at least EUR 1 billion a year of fossil fuel subsidies to international climate finance – from 2023, leveraging the Budget Law and tax reform and giving a mandate to the institutions and specialist bodies to identify specific recommendations – would be another decisive step towards reaching Italy’s fair share.

WHERE ARE WE NOW?

Keeping the USD 100 billion pledge made in Copenhagen in 2009 and confirmed in Paris in 2015 is crucial for the success of COP26. Without this sign of support and trust between nations, it will be hard to build the foundations of an agreement at COP26. The deadline for mobilising the USD 100 billion a year was 2020. Official OECD figures show that there was still a gap of USD 20.4 billion in 2019.

Climate Finance Provided and Mobilised (USD billion)



Source: OECD (2021)

At the G7 Summit in June, heads of state and government leaders committed to increasing international climate finance resources to 2025. At the same time, Germany announced that it would increase its federal funding for international climate finance from EUR 4 billion to EUR 6 billion a year by the end of 2025; Canada announced that it was doubling its share to CAD 4.4 billion by the end of 2025; France confirmed its commitment of approximately EUR 6 billion a year; and Japan confirmed a share of USD 11.8 billion a year until 2025. In its State of the Union address on 15 September, the European Commission also announced that it would be increasing its climate finance by USD 4 billion a year until 2027. Meanwhile in 2019 the UK had already committed to mobilising GBP 11.8 billion between 2022 and 2026. At the United Nations General Assembly (UNGA), Denmark announced that it will contribute 1% of the USD 100 billion, so approximately USD 1 billion a year, while Sweden announced its recent intention to double its Official Development Assistance (ODA) for climate finance in order to reach USD 1.7 billion by the end of 2025.

The most important signal came from the United States on 21 September at the UNGA. Joe Biden committed to doubling the commitment made at his climate summit in April. This means mobilising USD 11.4 billion a year by the end of 2024 in bilateral public climate finance alone. The total American climate finance share could therefore reach USD 25-30 billion a year with the addition of multilateral contributions (through multilateral development banks) and the mobilisation of public finance. Joe Biden's announcement was therefore an important step towards closing the gap by the end of the year.

However, the US Congress has to vote on the matter, and the estimates and actual costs are uncertain. Therefore other developed countries need to meet their existing commitments and announce new ones. This would ensure not only that the gap is effectively closed before COP26 in line with their fair shares, but also that the USD 100 billion is exceeded, given that this is just a fraction of global climate requirements. More than 150 organisations have written to the donor countries asking for a total of USD 600 billion to be mobilised between 2020 and 2025. In fact, the UN estimates that USD 300 billion a year is required for investments in adaptation to the impact of extreme climate events (ten times the amount mobilised in the two years 2017-2018) and the International Energy Agency estimates that USD 4 thousand billion, or USD 400 billion a year - three times the amount mobilised to date - is required for clean energy between now and 2030 in order to meet the targets of 1.5 degrees and net zero emissions by 2050.

At the Ministerial held on 25 and 26 July, Germany and Canada were asked to draft a "Schedule of Commitments" of the donor countries showing how the USD 100 billion will be reached. At the Pre-COP in Milano, talks began on the principles and methods for setting out the new post-2025 target, and a decision is expected at the COP26.

It is therefore encouraging to note the commitment made by Prime Minister Draghi to present a new climate finance commitment before COP26. Italy is in fact the only G7 country that has not yet presented new commitments, and is also behind in complying with the commitment it made in Paris to mobilise a cumulative USD 4 billion between 2015 and 2020. According to current reporting, there is an estimated gap of at least USD 800 million and average annual expenditure (2015-2019) of USD 500 million, equating to 0.5% of the USD 100 billion.[1] Italy is therefore a long way from the multi-billion-dollar annual contributions of its international partners and from the estimates of its fair share.

[1] At COP21 Italy committed to mobilise USD 4 billion in the six year from 2015 to 2020. From 2015 and 2019 it mobilised USD 2.5 billion, a long way off its target. The figures for 2020 are not yet available, but it is estimated that, given the unfavourable global conditions, public resources have not increased significantly from the 2015-2019 annual average of USD 500 million.

According to the latest update of the climate finance figures reported by the European Commission, Italy has in fact mobilised USD 3.17 billion.[2] These figures are still not final, as they do not yet include the finance mobilised in 2019 and 2020. On average Italy mobilised USD 15 million a year between 2015 and 2018, with significant variations from year to year. However, there is still a major gap to be bridged in order to reach the target of USD 4 billion by the end of 2020.

The figures from the new World Resources Institute report confirm Italy's weaknesses. Direct support from public finance through bilateral cooperation and multilateral climate funds - without counting the EU's contribution, which takes place via independent channels - represents just a third of Italy's indirect contribution through the multilateral development banks. Furthermore, Italy is one of the donor countries with the lowest climate finance per capita ratio. The Germans and the French respectively contribute 3.6 and 3 times more than the Italians to international climate finance.

WHAT IS A FAIR SHARE FOR ITALY, AND WHAT ARE OUR COMMITMENTS IN THE RUN UP TO THE G20 SUMMIT AND COP26?

The estimates available for Italy show a fair share of the USD 100 billion ranging from 3.4 to 4,8%.[3] The difference depends on the strictness of the weight given to the reference parameters, i.e. gross national income, the cumulative share of emissions and the population. **A fair share for Italy of 4% or USD 4 billion a year (equivalent to approximately EUR 3.4 billion)** can be taken as an average benchmark. According to current reporting, Italy has only reached 12.5% of its fair share

The G20 Summit in Rome and COP26 in Glasgow are opportunities for Italy to commit:

1. **to close the deficit, estimated to be USD 800 million, no later than 2022 in line with its commitment made at the COP21 in Paris in 2015;**
2. **in addition to closing the deficit, to double effective public finance spending in 2022 to EUR 1 billion** (approximately double effective average annual spending as already supported by Minister Cingolani);
3. **to commit to presenting a "Climate Finance Roadmap" in 2022 outlining how to reach the fair share of USD 4 billion (EUR 3.4 billion) per year well before the end of 2025.** This would leave the administrations sufficient time to adapt and to plan the necessary resources;
4. **to commit to allocate and manage climate resources in such a way that at least 50% are set aside for investments in adaptation, loss and damage** as set

[2] Italy's climate finance includes the resources from bilateral channels committed each year to benefit developing countries and not included in Annex I of the UNFCCC convention, resources provided directly to development finance institutions (inflows), such as those for multilateral climate funds and private finance mobilised through public interventions. Italy does not report based on the outflow of multilateral institutions, not does it report the climate finance share provided by the European institutions (which come from the Member State contributions)

[3] WRI, ODI, Oxfam, ETH Zuerich (for Italy's figures see WRI)

out by the United Nations Secretary-General Antonio Guterres and the COP26 manifesto for vulnerable nations;[4]

5. **to accompany the 2022 doubling with an additional EUR 250 million in public finance per year from 2022 to 2025 to create a "Climate Fund" at the Cassa Depositi e Prestiti (CDP).** The aim is to significantly increase private finance mobilised by means of public interventions and a 1:3 leverage effect. Achieving this goal each year from 2022 would mean mobilising an additional EUR 2 billion in climate finance by 2025;
6. **to commit to completing payment of the first contribution to the Green Climate Fund by the end of 2023 and to doubling the second contribution, to reach a total of EUR 600 million;**
7. **to double its contribution to the adaptation fund bringing it to EUR 60 million a year and renewing it each year from 2021 to 2025** (compared with the EUR 30 million paid in December 2020 by Conte's Government);
8. **to take part in climate-risk[5] insurance and forecast-based finance programmes** to support countries affected by extreme weather and already exposed to significant loss and damage;
9. to reallocate part of the USD 20.6 billion of the Special Drawing Rights allocated to Italy by the International Monetary Fund (IMF), for example **USD 2 billion, to the new IMF Resilience and Sustainability Trust.**

FIVE STRATEGIC LEVERS. WHERE DO THE RESOURCES COME FROM, HOW TO INCREASE THEM AND HOW TO MOBILISE THEM?

If it uses the five strategic levers at its disposal (bilateral, multilateral, private finance via the CDP, export credits through SACE, Simest and Budget Law leverage together with fiscal leverage to reform environmentally harmful subsidies), Italy has all the tools its needs to reach its fair share of USD 4 billion well before the end of 2025. **However, a strong boost and policy commitment is needed, particularly from Prime Minister Draghi and the Presidency of the Council of Ministers, in order to embark on a far-reaching process of reforming, tracing and allocating public and private climate finance.**

1. THE BILATERAL PUBLIC LEVER THROUGH INTERNATIONAL COOPERATION

The bilateral public lever is the most important lever available to Italy for decision-making control, strategic direction and the projection and external influence it offers. However, it is also the lever that has most suffered from a lack of political and institutional focus since 2015 and therefore needs to be re-established as a priority.

[4] Italy is moving in the right direction, having, in 2020, committed 28% of bilateral climate finance to adaptation, 15% for mitigation and the remaining 57% for activities targeting both goals.

[5] For example, through InsuResilience, African Risk Capacity (ARC) and ARC Replica, the Global Risk Financing Facility, or the ADB Africa Disaster Risks Financing programme. Italy could also become active in the Risk-Informed Early Action Partnership (REAP) and InsuResilience Global Partnership (IGP).

➢ The role of the Ministry of Foreign Affairs and International Cooperation (MAECI) and the Italian Agency for Development Cooperation (AICS)

The available resources of the MAECI and AICS for cooperation and development for 2021 and 2022 amount to approximately EUR 1.3 billion a year. There are currently no resources specifically dedicated to climate action. The total volume of Official Development Assistance (ODA) from in Italy was around EUR 3.9 billion as at 2019, equivalent to 0.22% of gross national income.

The method used to calculate Italian climate finance, like that of other donors, is based on the Rio Markers, which have been integrated into the ODA data collection methodology. These markers enable the identification of mitigation actions, resilience, improvements in early warning systems and actions to increase renewable energy.

The percentage of ODA for the climate in Italy in 2019 was 22%, half that of Germany and France and the equivalent of USD 236 million. This made it 35 times lower than that of Germany in absolute terms.

G7 country	% ODA for the climate (2019)	Volumes (2019, USD)
Italy	22%	236 million
Germany	43%	8.2 billion
France	44%	4.7 billion
Japan	46%	6.3 billion
United Kingdom	23%	2 billion
US (pre-Biden)	3%	931 million
Canada	15%	532 million

Using the 2019 Italian ODA (EUR 3.9 billion) as a conservative baseline and the relative share that can be allocated bilaterally, if the share of bilateral ODA increases, so do the volumes. For example:

- A 30% increase corresponds to an increase of up to USD 325 million (EUR 275 million) in the bilateral share.
- A 40% increase corresponds to an increase of up to USD 434 million (EUR 367 million) in the bilateral share.
- A 50% increase corresponds to an increase of up to USD 542 million (EUR 458 million) in the bilateral share.

The logical conclusion is that in the event of an increase in total ODA - for example from the latest available figure of 0.22% of gross national income in 2019 to 0.5% - the figures would increase significantly as a result. Europe aims to reach 0.7% of gross national income by the end of 2030, in line with the demands of international and Italian civil society.

How to increase climate finance through the MAECI and AICS:

→ **The share of ODA dedicated to fighting climate change needs to be increased to 50% by the end of 2024**. Italy could aim to reach a climate finance-to-ODA ratio of 30% by the end of 2022, 40% by the end of 2023 and 50% by the end of 2024. This would translate into a contribution of **EUR 458 million a year.**

→ **Total resources available for ODS need to be increased to at least 0.5% by the end of 2025 and 0.7% by the end of 2030 in line with the European target**. This ODA expansion programme, along with 50% of ODA being dedicated to climate, would deliver up to **EUR 4.5 billion a year** (based on 2019 gross national income), which alone would cover Italy's fair share of climate finance.

→ **A mainstreaming operation is needed in order to apply climate goals to all Italian cooperation, and not just to provide dedicated support**. If all development cooperation projects also pursued environmental and climate-related goals, and had a mitigation or adaptation component, this would automatically and significantly increase climate finance for the countries that need it most.

→ **There needs to be action on cooperation governance**: The three-year document on programming and strategy must specifically allocate a percentage of ODA to climate action;

→ **AICS needs to update the sector climate and environment guidelines**, strengthening the technical tools for evaluating mainstreaming. Furthermore, the OECD has found [6] that Italy has not updated its Ministry of the Environment environmental guidelines since 2011[7].

- The role of the Ministry for Ecological Transition (MITE) and the Ministry of Economics and Finance (MEF)

Revenues from emission trading system (ETS) auctions of greenhouse gas emission shares play and must continue to play a key role.[8] The latest Decree requires 50% of the auction revenues to be reassigned to the MEF Sinking Fund. The remaining 50% is assigned 70% and 30% respectively to the MITE and to the Ministry for Economic

[6] See page 44 of the OECD's Peer Review of Italy's development cooperation https://www.oecd.org/italy/oecd-development-co-operation-peer-reviews-italy-2019-b1874a7a-en.htm
[7] Seehttps://www.aics.gov.it/wp-content/uploads/2016/04/Linee-Guida-Ambiente-CORRETTO.pdf For other programming documents, see https://www.aics.gov.it/home-ita/settori/linee-guida/
[8] Legislative Decree 30/2013, as amended by Legislative Decree 111 of 2 July 2015, regulates the method of sharing the auction revenues on the basis of the harmonised regulations established by Directive 2003/87/EC as amended by Directive 2009/29/EC (known as the Emissions Trading Directive). Legislative Decree 47 of 9 June 2020 transposed Directive (EU) 2018/410 for the 2021-2030 period, replacing the previous Decree.

Development (MISE) . These revenues are allocated to specific categories for investment expenditure in the relevant budget forecasts, with usage constraints under European obligations.

The European obligations[9] specifically refer to certain international climate finance activities:

- To contribute to the Global Energy Efficiency and Renewable Energy Fund and to the Adaptation Fund.
- To encourage measures to avoid deforestation and increase forestation and reforestation in developing countries.
- To transfer technologies and encourage adaptation to the adverse effects of climate change in such countries.
- To finance climate-friendly activities in vulnerable third countries, including adaptation to climate change.

Following the reorganisation of duties between the Ministries, a greater share of revenues from the ETS auctions may be reallocated. However, 50% of the share of auction revenues is currently still allocated to the government securities sinking fund. Instead, **the MEF should also allocate this share to activities to combat climate change, both internationally and at home.**

For the 2020-2022 period, the MITE budget for development cooperation specifically targeting the environment and the climate is approximately EUR 210 million. For the same period the amount available from ETS auction revenues for development cooperation managed by the MITE is EUR 205 million.

In 2020 Italy collected EUR 1.27 billion in revenues from the auctions for 2019, of which EUR 635 million was allocated to the MITE and the MISE: EUR 444.5 million to the MITE and EUR 190.5 million to the MISE. According to the Update to the Economics and Finance Document (NADEF, October 2021), Italy collected EUR 1.6 billion in the first eight months of 2021. This means **we could see an estimated doubling of 2021 auction revenues to EUR 2.2 billion** (based on the monthly average of the first eight months of the year). In fact, the weighted average price of shares on the primary market increased from EUR 20.9 in 2Q 2020 to EUR 49.8 in 2Q 2021.

If the MITE and the MEF were to dedicate at least 50% of the revenues they receive to international climate finance, this would translate into an additional contribution to ODA from each of - at a conservative estimate - between EUR 222 million (based on the 2020 price and current distribution) and EUR 575 million (based on the 2021 price and distribution of 50% entirely to the MITE).

If Italy were to dedicate at least 50% of all the revenues from auctions to international climate finance, this would translate into an additional contribution to ODA of - at a conservative estimate - between EUR 635 million (based on the 2020 price) and EUR 1.5 billion (based on the 2021 price).

[9] Article 23(7) of Decree 47/2020

How to increase climate finance through the MITE and MEF:

- → **100% of the revenues from the emission trading system (ETS) auctions of greenhouse gas emission shares must be dedicated to national and international climate finance,** where they would have the greatest economic, social and environmental impact:
  - Allocate 100% of auction revenues to domestic and international climate finance in the medium term, **amending the Decree for the allocation of ETS auction revenues.**
  - Then allocate 50% of revenues to the MITE and 50% to the MEF for their management.

2. THE MULTILATERAL PUBLIC LEVER OF MULTILATERAL FUNDS AND DEVELOPMENT BANKS

The multilateral funds, particularly those that act as a financial mechanism of the Rio Conventions and created under the UN Framework Convention on Climate (UNFCCC), play a key role in supporting action on climate in developing countries. These include the Global Environment Facility, Green Climate Fund, Adaptation Fund, Multilateral Ozone Fund, Land Degradation Neutrality Fund and other Trust Funds. **Italy must accelerate its planned payments into these multilateral funds in order to guarantee capital flows well before 2025, increase its contributions and take part in new initiatives, in particular in adaptation and loss and damage.**

Italy is not just a contributor to the replenishment of the main multilateral climate funds, it also participates in the replenishment of Multilateral Development Banks (MDBs) and International Financial Institutions (IFIs) by means of its MEF. Payments are negotiated and agreed by means of the relevant governance mechanisms for each development fund, bank or financial institution.

It is to be hoped that Italy will play an ambitious role in these replenishment mechanisms on both fronts, making new additional resources available. In addition, there should be complementary work on the governance mechanisms and strategic priorities of the MDBs and IFIs, to increasingly integrate climate action targets in all the projects financed and to reorientate the entire investment portfolio to bring it in line with the targets of the Paris Agreement. This would increase bank outflows to support climate action, more than proportionally helping to reach the collective financial goals.

In 2019 Italy's climate finance component from the multilateral climate funds, MDBs and IFIs was USD 276.5 million (EUR 233.5 million). More ambitious participation from Italy in the replenishment processes of the various funds would lead to a considerable increase in Italian international climate finance.

How to increase climate finance through multilateral channels:

- → **Complete payment of the first contribution to the Green Climate Fund by the end of 2023 and double the second contribution, for a total of EUR 600 million**
- → **Double the contribution to the Adaptation Fund bringing it to EUR 60 million a year and renewing it each year from 2021 to 2025** (compared with the EUR 30 million paid to December 2020 by Conte's government).
- → **Take part in climate-risk[10] insurance and forecast-based finance programmes** to support countries affected by extreme weather and already exposed to significant loss and damage.
- → **The MEF will take part in the various replenishment operations of the MDBs and IFIs with contributions to be decided.[11]** An ambitious participation in these replenishment processes would considerably increase Italian international climate finance, given the growing climate portfolio of these institutions.
- → **It is important to insist that achieving the Paris Agreement targets becomes a strategic priority of the MDBs and IFIs,** insisting on a clear strategy for financing activities that pursue climate-related aims, a plan for realigning investment portfolios with the Paris Agreement targets, and a definite date for ending support for all fossil energy sources. Increasing the climate share of multilateral institution portfolios means more than proportionally increasing with Italy's share of multilateral climate finance allocated by institutions (outflows) with respect to its national contribution (inflow), which would combine to help move towards achieving the collective international finance goals.
  - In this context Italy's representatives on the Boards of MDBs and IFIs need to systematically push forward these three objectives as conditional policy priorities of their contribution, together with other key donors.
- → Should the **International Monetary Fund's** new **Resilience and Sustainability Trust (RST)** dedicated to the reallocation of Special Drawing Rights (SDRs) be considered climate finance, reallocation of part of the USD 20.6 billion allocated to Italy - say USD 2 billion - would significantly increase Italy's climate finance share.

3. THE PRIVATE CLIMATE FINANCE LEVER OF THE CDP

Mobilising private finance using the public lever is a great opportunity but remains challenging for Italy. From 2015 to 2018 a total of just EUR 60.8 million was reported as mobilised finance, and so far there has been neither an increase in volumes nor

[10] For example, through InsuResilience, African Risk Capacity (ARC) and ARC Replica, the Global Risk Financing Facility, or the ADB Africa Disaster Risks Financing programme. Italy could also become active in the Risk-Informed Early Action Partnership (REAP) and InsuResilience Global Partnership (IGP).
[11] Including IFAD-12, ADF-13, IDA-20, AfDF-16, GEF-8 and GCF-2

programmatic developments to exploit its potential and to put in place the governance for its management. In comparison, Germany managed to report almost EUR 1 billion in just two years in 2017-2018[12]. France had already recorded EUR 1.2 billion in 2014-2015.[13] In total, in the two years 2017-2018, donor countries mobilised approximately USD 28.3 billion (OECD, 2021).[14]

Public resources need to be allocated to where the impact in terms of mitigation and adaptation may be transformational, aligned to the goal of this "mission" and capable of overcoming "market failures", acting as a catalyst for action in the private sector. Even a marginal absolute increase could, at this stage, easily mean doubling or more than doubling the mobilisation of private Italian finance through public climate initiatives.

How to increase climate finance through private finance:

- → **The CDP needs to play a stronger role as a Development Bank**, capable of using public resources, contributing its own resources and leveraging private finance sources.
    - Set up a "Climate Fund" within the CDP **with EUR 250 million of public money allocated per year between 2022 and 2025 by means of the Budget Law and/or auctions.** The aim is to mobilise increase private finance by means of a 1:3 leverage effect. Achieving this goal each year from 2022 would mean mobilising an additional EUR 2 billion in climate finance by the end of 2025. This fund needs to be established in order to provide support to developing countries and to achieve Italy's medium-term climate plans (nationally determined contributions, or NDCs) and long-term strategies (LTS) and adaptation and loss and damage actions.
    - Agree on a clear taxonomy and monitoring CDP's climate-dedicated investments and international support based on existing methodologies and in line with the UNFCCC reporting rules.

- → **The system of reporting and tracing private finance mobilised by the cooperation actors needs to be improved.** The current system is patchy, and date collection is not systematic, even if it is part of the OECD DAC reporting system.
    - A stronger mandate from the Presidency of the Council of Ministers is needed for MITE, MAECI, AICS and MEF to make the collection of

[12] In the 2017-18 two-year period, Germany mobilised EUR 468 million in 2018 and EUR 486 million in 2017 via KfW and DEG (calculation made using methodologies comparable with those of Italy's estimates).
[13] 2015 Estimates, seehttps://www.oecd.org/env/researchcollaborative/Final%20report-V5%20Artelia%20Trinomics.pdf
[14] The donor countries include: the EU Member States and the European Commission, Australia, Canada, Iceland, Japan, Luxembourg, Malta, Monaco, New Zealand, Norway, Switzerland, the United Kingdom and the United States. See https://www.oecd-ilibrary.org/docserver/03590fb7-en.pdf?expires=1634394035&id=id&accname=guest&checksum=21097589DDB7ED79761827EB31B0ED08pter

information about private co-finance and contributions from private actors by means of financial instruments more far-reaching.

4. THE EXPORT CREDIT LEVER OF SACE AND SIMEST

As an Export Credit Agency (ECA), SACE has the - largely unexplored - potential to play a key role in financing green enterprises and investments abroad, as well as in Italy, which would help to meet its climate commitments. It could aim to become the Italian climate ECA.

However, this would require a significant change to its policy and portfolio. Indeed, the SACE Group is still very active in the oil and gas sector - having provided EUR 10.8 billion in new volumes to Oil & Gas between 2016 and 2020 - and a specific commitment to end public support for all fossil fuels has not yet been made, despite the prohibition on supporting carbon-based projects and operations.

Together with CDP, SACE is a crucial vehicle for supporting and mobilising private investments. This requires shifting the current portfolio away from fossil fuels to "green credits and guarantees". SACE could therefore aim to mobilise at least EUR 2 billion a year in green credits and guarantees, at the same time ending its support for fossil energy investments by the end of 2022.

As part of the recent role taken on by SACE domestically ("August" Decree, Decree-Law 104/2020), it has undertaken to provide "Green" guarantees to Italian enterprises aiming to finance their green investment projects by obtaining facilitated access to medium-to-long-term finance, with a fund available for 2021 to cover the "Green New Deal" Guarantees of EUR 2.5 billion, and the SACE "Green Guarantees" of EUR 700 million. Under this programme, for projects to be eligible for coverage by SACE, they need to meet European Green Deal objectives and the parameters of the European regulation on taxonomy. This framework could already act as a benchmark for evaluating activities supported by export credit at international level.

In 2020 Simest - which has EUR 87 million in share-based investments, more than EUR 1 billion in subsidised loans for international expansion for businesses and EUR 3.2 billion in support for exports - also mainly provided finance to the chemical/petrochemical industries (EUR 28 million out of EUR 64 million in equities purchased and capital credit) and the cruise industry (40% of export support volumes destined exclusively to the overseas territory of Bermuda), only allocating EUR 3 million to renewables.[15]

How to increase climate finance through private finance:

→ **SACE needs to set a goal to support and mobilise private investments through "green credits and guarantees", aiming to mobilise at least EUR 2 billion a year in green credits and guarantees by the end of 2025, and end its support for fossil energy by the end of 2022.**

[15] See the Simest 2020 financial statements (pages 22-33)

- It is of key importance that SACE joins the Export Finance for the Future coalition and - in line with its subscribers' policies - makes tangible commitments to make export finance one of the main vehicles in the fight against climate change.
- In line with the leading European ECAs, SACE should make a clear commitment to no longer support carbon-based projects by the end of 2021.
- SACE should answer the call led by the United Kingdom and the European Investment Bank, and use COP26 as an opportunity to commit to ending all its investments in fossil fuels by the end of 2022, in line with the Paris agreements and the 1.5°C target.
- SACE should restructure its export support portfolio based on the EU taxonomy for sustainable activities, set up an appropriate monitoring system and commit to fully transparent data and policies, including by aligning its financial instruments with the 1.5°C temperature target.

→ **The role of Simest needs to be strengthened in order to support "green" investments and enterprises** in third developing countries, reallocating its portfolio based on the EU taxonomy for sustainable activities and ruling out support for activities directly or indirectly linked to fossil fuels. It is also necessary for Simest to adopt a system for monitoring support for sustainable activities.

5. THE BUDGET LAW AND FISCAL LEVER OF REORGANISING ENVIRONMENTALLY DAMAGING SUBSIDIES

In addition to the areas of action to increase Italian climate finance set out above, the main vehicle for increasing Italian climate finance is to increase the public resources available for this purpose "upstream", in other words **to include an increase in international climate resources in the Budget Law.**

These resources will need to come from a reallocation of resources currently allocated for other purposes. One of the possible new sources are the environmentally harmful subsidies (SAD), which each year are recorded by the MITE in its "Catalogo dei sussidi ambientalmente dannosi ed ambientalmente favorevoli" [Catalogue of environmentally harmful and environmentally friendly subsidies], which has to be presented by the Minister to the Chambers and the Interministerial Committee for Ecological Transition (CITE) by 15 July. The Catalogue analyses the environmentally harmful subsidies which, if appropriately reallocated, would free up resources that would not only no longer finance activities that are harmful to the environment, but could in fact help developing countries reach their NDCs. Italy also conducted a *peer review* with Indonesia and published an independent report on fossil fuel subsidies within the context of the G20.

Despite repeated the efforts of successive governments to assume policy leadership of the process, most recently with the failed attempt to appoint the

CITE to restructure the environmentally harmful subsidies, an effective mechanism for reallocating at least part of the EUR 19.7 billion, of which EUR 17.7 billion are fossil fuel subsidies, has not yet been found.

Although the purpose of the national catalogue is primarily informative, with the primary aim of informing Parliament and the Government about forms of subsidy that are inconsistent with the country's environmental policy commitments rather than proposing specific reforms, the analysis provides information about areas where the subsidy could be reformed (e.g. at international, EU and national level)[16].

The most costly subsidy is the difference in excise duty on petrol and diesel fuel, which is much lower on diesel. The lost revenue from car passenger transport is approximately EUR 5 billion (approximately EUR 6 billion including VAT). Environmentally harmful subsidies account for 71% of fiscal expenditure (subsidies). Analysis by industry shows excise duty measures on energy products at the top (72% or EUR 11.6 billion), followed by VAT subsidies on products (22% or EUR 3.6 billion), transport (EUR 202 million) and agriculture (1% or EUR 154 million).

In some cases, the analysis can provide initial indications on how to improve the subsidy's environmental compatibility. There are also many subsidies classified as "uncertain" (with wide-ranging environmental effects), which could become environmentally friendly subsidies (SAF) by introducing environmental conditions that would be more or less simple to implement (EUR 5.8 billion).

The Government may consider various actions, ranging from the option of progressively removing the harmful subsidy, in order to recover the revenue for other uses, to reforming the subsidy, retaining the financial payment but introducing environmental conditions for its disbursement.

Some indications, set out in a dossier by the Senate, could constitute low-risk actions (known as low-hanging fruit), freeing up resources to reallocate to international climate finance:

- realignment of the excise duty on diesel fuel for cars with that on petrol, where the energy content is the same;
- alignment of subsidised tax brackets for goods where the subsidy determines a significant environmental impact with respect to the "normal" bracket, reducing the price stimulus on more efficient forms of consumption. This category includes VAT subsidies on fertilisers containing nitrogen, or on mineral oils and fuels, for example;
- excise duty on natural gas also includes subsidies that create distortions from an environmental point of view. Their gradual removal needs to be explored as a matter of urgency, as does that which favours major gas consumers for industrial purposes;

[16] Restructuring the environmentally harmful subsidies may have regressive and socially or economically undesirable effects. This is why careful planning and estimates of the environmental, economic and social effects of the subsidies are necessary, along with the introduction of compensatory measures where necessary.

- there is a possibility of eliminating the total exemption on maritime fuel, reducing it to a partial subsidy;
- in agriculture, eliminating the direct subsidies paid for intensive livestock farming regardless of whether good environmental practices are in place;
- avoiding providing support for industries that use their auction revenues (an environmental taxation instrument) to relocate their industries abroad.

How to increase climate finance by restructuring environmentally harmful subsidies:

- **The Government and Parliament need to reallocate at least EUR 1 billion a year of environmentally harmful subsidies to international climate finance from 2023 using the Budget Law and tax reform as levers.**
- **The mandate for identifying recommendations on measures for reducing environmentally harmful subsidies and implementing a phase-out of subsidies for fossil energy by the end of 2025 needs to be stepped up, as required by the international commitments Italy has signed up to at G7 and G20 meetings.**
  - Technical bodies need to be appointed to make specific recommendations for reforming environmentally harmful subsidies.
  - Governance must be put in place that enables technical bodies and policymakers to examine various possibilities for reforming environmentally harmful subsidies.
  - A mechanism must be put in place to reallocate subsidy-related resources fairly and in line with Italy's industrial and social innovation priorities and international climate finance.
  - In this sense, also encouraging subnational governments[17] to record environmentally harmful subsidies based on the cataloguing regularly carried out by the MITE would deliver greater widespread policy awareness and free up resources for many cooperation actors in Italy.

CONCLUSION - A CLIMATE FINANCE ROADMAP

To follow up on the goals outlined above and confirm the leadership role on climate that Italy has often expressed great interest in as a G7 member country and current holder of the Presidency of the G20, Mario Draghi and his Government should, in a break with the past, draw up a long-term programme involving all of the administrations and relevant institutional actors in order to guarantee a serious, agreed and practicable commitment to Italian climate finance. In this regard, it appears crucial that **at the next G20 Summit in Rome, Italy commits to presenting an "Italian Climate Finance Roadmap" with the specific aim of reaching a fair share of USD 4**

[17] See the examples of Trentino Alto Adige https://agenda2030.provincia.tn.it/Documenti/Catalogo-Provinciale-dei-Sussidi and Lombardy https://svilupposostenibile.regione.lombardia.it/it/b/201/svilupposostenibileinlombardiailprimocatalogoregionaledeisuss

billion a year well before the end of 2025, in line with the proposed lines of intervention. A strong policy boost from the executive in this sense would facilitate the coordination of public administrations and the most relevant institutional actors, which would therefore be operating within a clear and efficient institutional and programmatic framework, building the foundations to meet the objectives set. Specifically, a shared long-term vision would leave sufficient time to free up resources, implement internal reform of international climate finance governance, tracing and reporting, and mobilise private finance, ensuring the full implementation and functionality of the levers identified.