UN environment programme

GREEN economy

Policy Brief

Building Back Better: the Role of Green Fiscal Policies

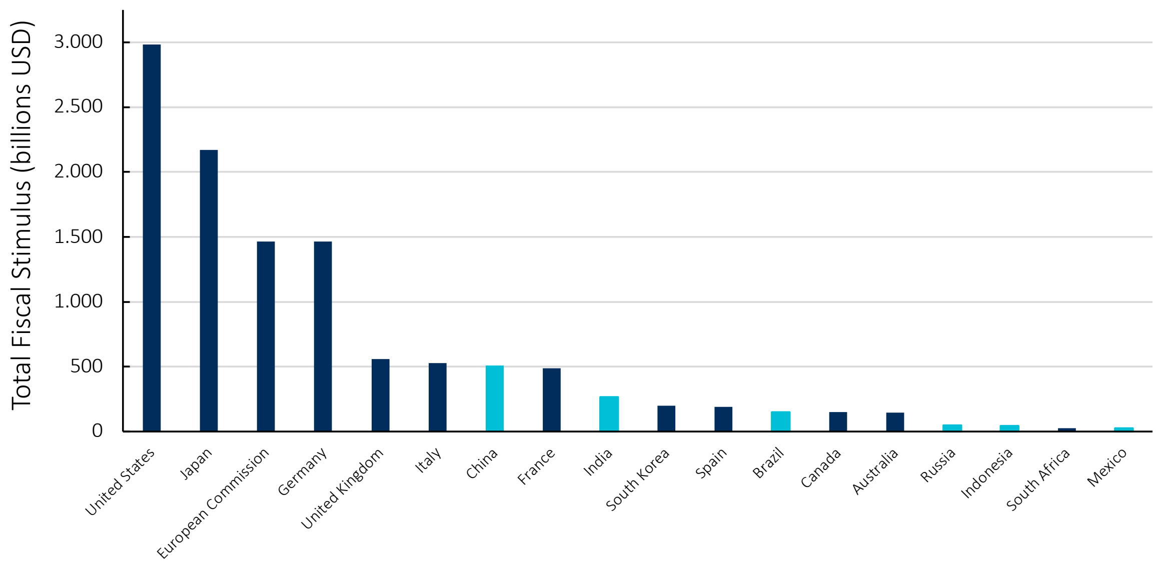
KEY MESSAGES

The COVID-19 pandemic has exposed the many fragilities of our economies, and deepened existing inequalities, while highlighting the need for resilience, innovation, and cooperation in our societies. The immediate priority is on emergency measures to address the health crisis and its economic fall-out; but greening recovery efforts can help nations build back better after the pandemic to increase resilience to future crises by ensuring a healthy environment that backs healthy people. Green fiscal policies can play a key role in countries' recovery efforts by removing inefficiencies in public expenditures and raising additional fiscal revenues which can be directed towards immediate COVID-19 relief measures while supporting medium- to long-term investments and planning for a more sustainable, resilient and inclusive future.

GOVERNMENTS RESPONSES HAVE BEEN LARGE, BUT NOT SUFFICIENTLY "GREEN"

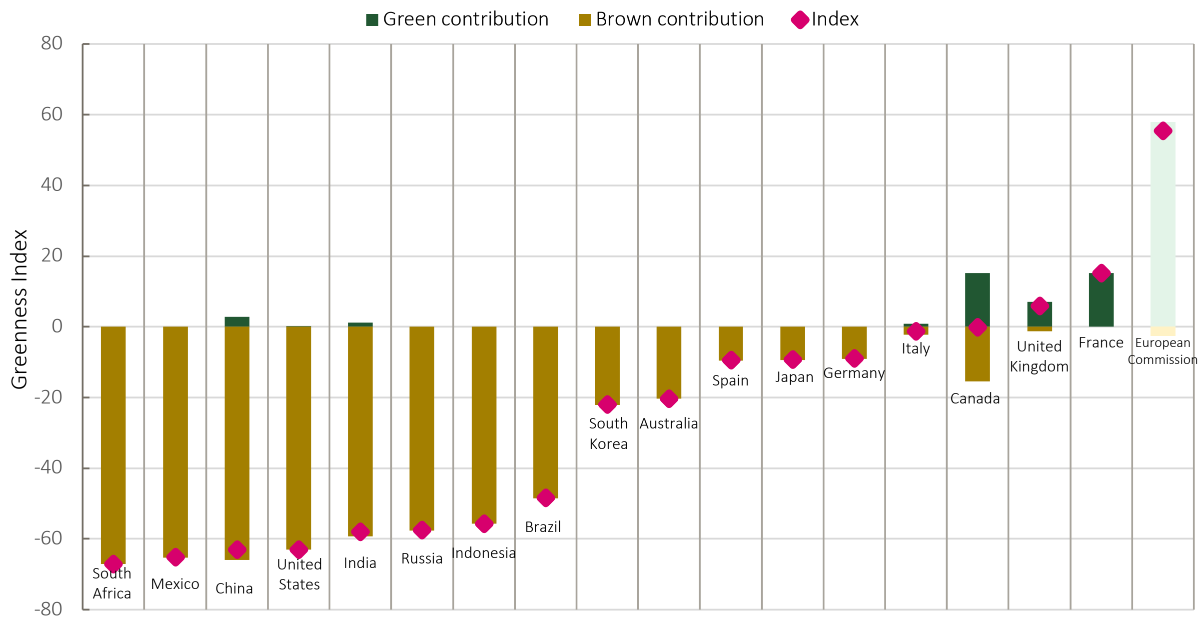
COVID-19 has necessitated the mobilization of large-scale government stimulus measures to avoid the public health crisis becoming a socio-economic catastrophe. The past few months have seen governments around the world roll out various measures to provide immediate and short-term relief to their economies (IMF, 2020). **While the sheer scale and speed of these responses has been significant** (see Figure 1), analysis of recent stimulus measures by selected major economies shows **the majority of public resources are going towards business-as-usual activities and sectors,** with a notable lack of consideration for environmental sustainability (see Figure 2).

Figure 1: Fiscal stimulus packages in selected countries



Source: Vivid Economics using IMF COVID response tracker and Oxford Coronavirus Government response tracker.
Note: Dark blue represents developed and light blue represents developing countries. Assumes the proposed 'Next Generation EU' recovery package is implemented in full. Does not include Germany's latest EUR130 billion announcement. Updated on June 3, 2020.

Figure 2: How green is the stimulus? (Green Stimulus Index by Vivid Economics, June 2020)



	ZAF	MEX	CHN	USA	IND	RUS	IRD	BRA	KOR	AUS	SPA	JPN	GER	ITA	CAN	GBR	FRA	EC
Agriculture			✓		✓										✓			✓
Energy				✓										✓	✓		✓	✓
Industry															✓			✓
Transport			✓												✓	✓	✓	✓
Waste															✓			✓
Agriculture				✓				✓		✓					✓	✓		
Energy		✓	✓	✓		✓		✓		✓					✓			
Industry			✓	✓	✓	✓	✓		✓	✓					✓			
Transport			✓	✓		✓		✓	✓	✓	✓		✓	✓		✓		
Waste				✓														

Source: Vivid Economics using a variety of sources.

Note: The European Commission score is calculated assuming that the proposed 'Next Generation EU' recovery package and related environmental measures are implemented in full. Its score is provisional. Updated on June 3, 2020.

WHY WE NEED A GREEN FRAMING FOR COVID-19 RELIEF AND RECOVERY

The scale of current relief and recovery packages is unprecedented and will leave a long-lasting impact on the direction of our economies. Hence, consideration of resilience and sustainability is critical to ensure a recovery that does not derail from the sustainability track world leaders have committed to under the Sustainable Development Goals (SDGs). **Focusing on environmental sustainability can deliver multiple benefits** in terms of job creation, stimulating demand and economic activity. For example, according to World Bank estimates, USD1million invested in the oil and gas sector in the United States would create just five jobs, compared to 17 jobs per USD1million invested in energy-saving building retrofits, 22 jobs for mass transit, 13 for wind, and 14 for solar (World Bank, 2011). Greening recovery efforts can also help reduce the probability of future pandemics, support public health efforts, reduce environmental and climate change risks, and strengthen resilience to future crises. There are **growing calls for a green recovery and for using the crisis as an opportunity to build more sustainable, inclusive and resilient economies and societies** – see Box 1.

Box 1: Shaping a better recovery together

UN Secretary General António Guterres has set out six climate-related actions to shape a better recovery[1]:

1. Deliver new jobs and businesses through a clean, green transition.
2. Tie public bailouts of businesses to achieving green jobs and sustainable growth.
3. Use fiscal firepower to drive a shift from the grey to green economy
4. Use public funds to invest in the future, not the past. ***End fossil fuel subsidies and make polluters pay for their pollution***.
5. Incorporate climate risks and opportunities in the financial system, public policy making and infrastructure.
6. Work together as an international community.

[1] See speech and key messages by UN Secretary-General António Guterres at the 11th Petersberg Climate Dialogue on 28 April 2020 available here: **https://www.bmu.de/en/petersberg-climate-dialogue-xi/#c45111**

GREEN FISCAL POLICY IS KEY TO RESOURCING A SUSTAINABLE AND RESILIENT RECOVERY FROM COVID-19

With historically low interest rates in most developed countries and a combination of high debt-to-GDP ratios, capital flight and widening spreads in developing and low-income countries, monetary policy alone cannot deliver the enormous scale of relief and recovery resources needed. While developed economies can still finance government spending at extremely low rates and without fear of inflationary pressures in the short-to medium-term, **many developing and low-income countries, are likely to face constrained fiscal space due to high existing debt-to-GDP ratios and the risk of inflationary pressures** (IIF 2020). Many developing countries dependent on resource rents have also seen budget positions weakened due to the fall in demand for commodities, while countries dependent on oil and gas revenues have been doubly affected by the decline in oil prices. Thus, **improving the efficiency of public expenditures, reallocating scarce public resources and reforming fiscal policies to raise additional revenues will be priority actions in most countries**.

Green fiscal policies can be an important element in a government's COVID-19 response toolkit. **Green budgeting for instance can increase the efficiency and effectiveness of budgetary processes and align them with climate and broader environmental objectives**. It allows a precise management of green recovery-compatible expenditures and taxes, and the identification of potentially harmful expenditures (especially tax expenditures) and perverse incentives. This would allow governments to identify misalignments of spending and objectives, help identify possible resources which could be re-directed to COVID-19 relief measures and allow long-term integration of environmental and climate sustainability in budgetary processes.

Rationalising inefficient public expenditures including environmentally harmful subsidies in key sectors such as energy and agriculture can free up significant public resources which can be re-allocated towards COVID-19 relief and recovery measures. Removing fossil fuel subsidies and introducing taxes on fossil fuels that take externalities into account could provide average revenue streams to governments of about 2.6 per cent of global GDP (Parry et al., 2014). The current low oil price provides a particular opportunity to **reform inefficient fossil fuel subsidies and support a shift towards a more resilient, sustainable energy system over the long-term.** Similarly, agriculture subsidies account for a large share of public spending in many countries and certain subsidies can create perverse incentives and lead to negative environmental and health impacts (UNEP 2020a). As part of countries COVID-19 recovery efforts, such **inefficient/ineffective agriculture subsidies could be repurposed and directed towards strengthening smallholder farmers and scaling up nature-based farming practices** as part of efforts to ensure food security and build resilience of rural communities to future pandemics.

Environmental taxations can also **raise additional public revenues which can be used to finance recovery efforts and support needed investments in priority sectors** such as health, education, agriculture, and the rural economy. Carbon taxation can be especially effective in the current low oil price environment. For example, the IMF estimates that a **carbon tax of $75 per ton would increase pump prices by less than the overall decline due to the oil price collapse** (IMF 2020a)**.** Such policies should be combined with other measures like feebates to incentivise greener transport solutions and energy efficiency improvements; and accompanied by smart communication and assistance for low-income and vulnerable households and communities. As countries begin to re-imagine/reassess their relationship with nature to help reduce the risks of future pandemic outbreaks, **fiscal policies and other market-based mechanisms can play a role in transforming agriculture and food systems** through incentives that shift production and consumption behaviours towards more sustainable practices; reduce large-scale deforestation, habitat destruction and fragmentation, strengthen ecosystem functioning and reduce the risks of future infectious zoonotic disease outbreaks.

UNEP WORK ON GREEN FISCAL POLICIES IN THE CONTEXT OF COVID-19

UNEP is committed to supporting countries efforts on investing to build back better (UNEP 2020) by providing policy advice to countries, facilitating knowledge sharing and promoting dialogue on how green fiscal policies can mobilise resources towards COVID-19 relief and recovery measures in the short-term and create incentives for long-term resilience, increase efficiency and effectiveness of public spending and align budgetary processes with sustainability. This work cuts **across different sectors and thematic areas**, including energy and climate change, agriculture and food systems, biodiversity, pollution and health, and extractives.

At the global level, UNEP supports efforts to **reform fossil fuel subsidies** under **the SDG process** by providing training on measuring fossil fuel subsidies and helping countries to monitor and report on subsidies under the SDG process.

UNEP is also leading a global initiative on fiscal reform for sustainable agriculture and food systems to support commitments under the SDGs and post-2020 biodiversity framework which engages several partners including UNDP, FAO, IMF, OECD, WHO, International Food Policy Research Institute (IFPRI), CBD, among others.

This support is provided in collaboration with partners including through the **Partnership for Action on the Green Economy (https://www.un-page.org/)** - where UNEP is working with UN partner agencies to deliver country support for a green recovery from COVID-19; and through the **Green Fiscal Policy Network** - a collaboration between UNEP, IMF and German Development Cooperation Agency (GIZ) for knowledge exchange and country dialogue on green fiscal policy experiences and best practices. The Network works with several associated partners and is supported by the International Climate Initiative (IKI) of the German Federal Ministry for the Environment, Nature Conservation and Nuclear Safety (BMU).

Further reading

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Parry et al. (2014). ***Getting energy prices right: From principle to practice.* International Monetary Fund.**

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