

## PROPOSAL

# Lowering the cost of ecological transition with a green interest rate from the ECB

FINANCE &amp; MONEY, INVESTMENT

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**Main objective**

Lower the financing rate for transition investments.

**Scope**

European Union

**Type of measure**

Monetary policy

### Content of the proposal

The European Central Bank (ECB) is setting up a reduced-rate refinancing program for banks, targeting “green” investments as defined by the European taxonomy.<sup>1</sup>

## Argumentation and justification

01

### Tackling fossilflation at its roots

Achieving our climate objectives requires public and private investment in the order of 2% to 4% of GDP in Europe. However, the rise in interest rates orchestrated by the ECB in 2022 – and by other central banks around the world – is putting the brakes on these crucial investments. The reason is simple: “green” investments (renewable energies, energy renovation, etc.) are generally more capital-intensive.<sup>2</sup> than “brown” investments (fossil fuels or industries with high greenhouse gas emissions). For example, a wind turbine requires a substantial initial investment, but its operating costs are very low afterwards (wind and sun are free). Conversely, the cost of a gas-fired power plant depends essentially on the cost of fuel supply, which in the long run is much higher than the initial cost of building the plant.

For this reason, many offshore wind projects were cancelled in 2022-2023, as rising interest rates made them unprofitable.<sup>3</sup> Indeed, it is estimated that a 3% rise in interest rates increases the cost of offshore wind power by almost 25%.

The European Union's heavy dependence on imported fossil fuels represents a major vulnerability, and a risk of "imported" inflation: the notorious "fossiflation". The inflationary episode of 2022-2024 showed how difficult it is for the ECB to control this phenomenon.

To avoid further energy shocks of this kind, it is widely recognized as desirable to accelerate the deployment of renewable electricity production, increase the interconnectivity of the European electricity grid and storage, and generalize energy sobriety in industry and through building renovation. This is the aim of the French National Low-Carbon Strategy (SNBC).<sup>4</sup> in France.

By supporting the energy transition, the ECB could help to protect Europe against such inflationary shocks – which would at the same time make it easier for the ECB to pursue its price stability objective. Several studies show that, in the long term, a greater share of renewable energy generation could reduce energy prices, and hence inflation.<sup>5</sup> The International Energy Agency, for example, shows that growth in photovoltaic and wind power capacity in the EU between 2021 and 2023 could reduce the average wholesale price of electricity by around 15% in 2023.<sup>6</sup>

To ensure that renewable investments do not suffer disproportionately from interest rate fluctuations, the ECB should apply a differentiated "green interest rate" for projects that promote energy transition.

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## The green interest rate mechanism

A green interest rate could be introduced by the ECB via a bank refinancing program, conditional on a certain green performance. Commercial banks would then obtain

loans at a “green rate”, i.e. lower than the normal ECB rate.

The mechanism would thus be similar to the “TLTROs” programs,<sup>7</sup> which the ECB set up between 2014 and 2024 and which provided liquidity on very favorable terms for banks. For example, banks could borrow for 4 years, at a rate of up to -1% if they demonstrated that they were sufficiently financing the real economy.<sup>8</sup>

In practical terms, each bank could borrow the total amount of “green loans” (i.e. loans aligned with the criteria of the European taxonomy).<sup>9</sup> If it had “produced” in the previous year. If banks reach a certain target for increasing their green asset ratio<sup>10</sup> they can obtain an additional bonus in terms of interest rate reduction. This mechanism would reduce the cost of capital for green loans, while encouraging banks to develop ambitious strategies to increase their financing for the ecological transition.

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## Potential impact of a green interest rate

For a green interest rate policy to have a real effect, the green interest rate must be set sufficiently lower than the ECB’s normal rate, and for a sufficiently long period.

In his report for the European Commission published in September 2024, former ECB President and Italian Prime Minister Mario Draghi estimates that a 250 basis point reduction in the cost of capital would be needed to achieve a level of private investment of around 4% of GDP for the transition.<sup>11</sup>

In the same order of magnitude, a study by Dutch bank ABN Amro estimates that a green rate set 200 basis points below the ECB rate would improve the profitability of most renewable technologies for solar and wind power in Germany, France, Italy, the

Netherlands and Spain by 24% to 53%.<sup>12</sup> Another study by two of the same researchers for Sustainable Finance Lab estimates that a lower rate differentiation, of the order of 100 basis points, would deliver 5% to 12% of the emissions reductions needed to meet EU targets.<sup>13</sup>

In September 2024, the ECB's key interest rate was 3.5%. A green rate of between minus 100 and minus 250 basis points would be in the 1% to 2.5% range.

## Legal and political feasibility

### There are many precedents


The Banque de France and the Bundesbank, for example, have successfully applied differentiated interest rates during periods of inflation, to support certain sectors that helped reduce inflation.<sup>14</sup>

In 2021, the People's Bank of China (PBoC) has introduced a "Carbon Emission Reduction Facility" (CERF) allowing banks to borrow at a preferential rate of 1.75% for an amount corresponding to 60% of their loan volume issued to support the transition to a low greenhouse gas emission economy.<sup>15</sup> The Bank of Japan followed suit in January 2022, launching a new program called "Transactions for Climate Response Financing Operations", under which banks can borrow at 0% from the Bank of Japan. By July 2024, Japanese banks were able to borrow 11,963 billion yen (76 billion euros).<sup>16</sup>

The TLTRO III programs set up by the ECB between 2014 and 2024 have very similar characteristics, although they are not specifically targeted at green investments.

In 2020, the ECB had already considered such a measure (the "green TLTRO"), as part of a review of its strategy. But it concluded that data gaps and insufficiently developed methodologies made it impossible to determine what was "green".<sup>17</sup>

According to a recent report by the Dutch think tank Sustainable Finance Lab, these problems seem to have been resolved.<sup>18</sup> Indeed, the implementation of the European taxonomy on sustainable activities provides a solid definition of sustainability criteria. On the basis of this taxonomy, since 2024, banks have been obliged to publish their “green asset ratio” each year, which implies the systematic collection and processing of data relating to the environmental impact of companies, via the CSRD directive. These advances greatly facilitate the implementation of a green rate program by the ECB.

In 2021, the ECB has introduced a green factor in its corporate debt repurchase programs, which is a first step towards at least partially abandoning its neutrality principle (see our [module on money](#) ). In January 2024, the ECB pledged to continue examining the possibility of greening its monetary policy operations.<sup>19</sup> Following on from this, the ECB announced its intention to introduce “structural refinancing operations” by 2027, the terms of which should take account of climate-related objectives.<sup>20</sup> A green interest rate policy would fit perfectly into this perspective.

### **Politically, the context seems to be favourable:**

The European Union has launched its 2019 Green Climate Pact and the “Adjustment to Target 55” legislative package has been adopted. The new targets for the EU cannot be achieved without additional investment.

## **Origin, related works and supports for the measure**

### **A proposal that enjoys a wide range of support**

This proposal was dreamed up in 2019 by Irish economist Eric Lonergan<sup>21</sup> and relayed in France by Hubert Kempf.<sup>22</sup> Then, it was taken up and pushed by think tanks Positive Money and Sustainable Finance Lab in 2020<sup>23</sup> and the French NGO

Reclaim Finance.<sup>24</sup> ECB President Christine Lagarde welcomed the proposal.<sup>25</sup>

Since then, a number of economists from universities and the banking sector have supported the project, including Éric Monnet (EHESS and Paris School of Economics), Jens van't Klooster (University of Amsterdam) and others.<sup>26</sup> Frédéric Ducrozet (Pictet), Louis Harreau (Crédit Agricole), Carsten Berzski (ING), Nick Kounis (ABN Amro), Sandra Phlippen (ABN Amro), Barbara Baarsma (Rabobank).<sup>27</sup>

Speaking at COP28, Emmanuel Macron said that “we need a green interest rate and a brown interest rate”.<sup>28</sup> A group of nearly 30 economists, investors, business leaders and associations also recently called for this in an article in *Le Monde*.<sup>29</sup>

## FIND OUT MORE

-  [In everyone's interest: How the ECB can support the energy transition with green interest rates, WWF, 2025](#)
-  [Stanislas Jourdan, Rens van Tilburg, Aleksandar Simić, Brenda Kramer and Gaston Bronstering, A green interest rate for the Eurozone: evaluating the design choices. Sustainable Finance Lab, 2024.](#)
-  [Is a lower interest rate needed to boost the green transition? Alternatives Economiques \(04/23/2024\)](#)
-  [Éric Monnet and Jens van't Klooster, Using green credit policy to bring down inflation-what central bankers can learn from history, LSE and Grantham Research Institute, 2023.](#)
-  [Les leviers d'action de la BCE pour le climat, post by Alain Grandjean on his blog Les Chroniques de l'Anthropocène \(04/01/2024\)](#)

## Other resources on The Other Economy

[Money](#)  module

[Public debt and deficit](#)  module

Proposal [Launch an ecological reconstruction plan](#) 




Proposal [to reform the European Stability and Growth Pact](#) 

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- 1 The European taxonomy is a classification of economic activities designed to identify sustainable (“green”) activities, and *ultimately* to direct investment towards these environmentally-friendly activities. 
- 2 See Rupert Way, Matthew C. Ives, Penny Mealy, J. Doyne Farmer, [Empirically grounded technology forecasts and the energy transition](#), *Joule*, 2022. 
- 3 [The struggles of the offshore wind industry](#), *Financial Times* (31/10/2023). 

- 4 The National Low-Carbon Strategy is France’s roadmap for combating climate change. Applied to all sectors of activity, it defines a trajectory for reducing greenhouse gas emissions up to 2050, and sets short- and medium-term targets: annual “carbon budgets”. 
- 5 Javier Quintana, [The impact of renewable energies on wholesale electricity prices](#), Bank of Spain Economic Bulletin, 2024; Paul Schreiber, Henri Her, [Inflation management calls for a sustainable energy transition in Europe](#) Reclaim Finance, 2023. 
- 6 International Energy Agency, [Renewable Energy Market Update – June 2023](#). 
- 7 Targeted longer-term refinancing operations. Targeted longer-term refinancing operations. 
- 8 See for example [La BCE veut s’attaquer aux profits des banques sur leurs dépôts](#), Les Echos (14/10/2022). 
- 9 The ECB could also decide to restrict the scope of this policy to specific segments of the EU taxonomy. 
- 10 An alternative to the greenasset ratio would be the “BTAR” *Banking Book taxonomy Alignment Ratio*, which also takes into account companies not subject to the CSRD directive. 
- 11 Mario Draghi, [The future of European competitiveness](#), European Commission, 2024. 
- 12 Moutaz Altaghlibi, Rens van Tilburg, Gaston Bronstering, [The impact of a Green LTRO on the energy transition](#) ABN Amro, 2024. 
- 13 Moutaz Altaghlibi, Rens van Tilburg, Mark Sanders, [How much of a help is a green central banker?](#) (Working Paper) Sustainable Finance Lab, 2022. 
- 14 Éric Monnet and Jens van’t Klooster, [Using green credit policy to bring down inflation-what central bankers can learn from history](#) INSPIRE, 2023. 

- 15 [PBoC launches targeted green lending](#), *Green Central Banking* (10/11/2021). 
- 16 [Outline of Transactions for Climate Response Financing Operations](#), Bank of Japan website (accessed September 19, 2024). 
- 17 “The feasibility of such operations hinges on the availability of a proper definition of ‘green lending’”, [Climate change and monetary policy in the euro area](#) (page 153), ECB, 2021. 
- 18 Stanislas Jourdan, Rens van Tilburg, Aleksandar Simić, Brenda Kramer and Gaston Bronstering, [A green interest rate for the Eurozone: evaluating the design choices](#). Sustainable Finance Lab, 2024. 
- 19 See the European Central Bank’s [Climate and nature plan 2024-2025](#), published in January 2024). 
- 20 [Changes to the operational framework for implementing monetary policy](#), ECB press release (13/03/2024). 
- 21 Eric Lonergan, [It’s time for the ECB to use its monetary power](#) (28/03/2019). 
- 22 Hubert Kempf, [Verdir la politique monétaire](#), *Revue d’économie politique*, 2020. 
- 23 Jens van ‘t Klooster, Rens van Tilburg, [Targeting a sustainable recovery with Green TLTROs](#), Positive Money Europe and Sustainable Finance Lab, 2020. 
- 24 Paul Schreiber, [Managing inflation by supercharging a clean energy transition](#). Reclaim Finance, 2022. 
- 25 [Christine Lagarde re-affirms willingness to consider lower rates for climate investments](#), Positive Money (13/06/2022). 
- 26 Éric Monnet and Jens van’t Klooster, [Using green credit policy to bring down inflation-what central bankers can learn from history](#), INSPIRE, 2023. 
- 27 [R.I.P. TLTROs, long live green dual rates](#), open letter to the ECB Governing Council published by Sustainable Finance Lab in June 2022. 

- 28 [Speech by the President of the French Republic at the plenary session of COP 28 in Dubai, December 1, 2023.](#) 
- 29 [The ECB could apply lower interest rates to the refinancing of bank loans allocated to the ecological transition, Le Monde \(2/03/2024\).](#) 