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# A framework for central banks navigating political uncertainty in the transition

Monica DiLeo

Policy insight  
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# Summary

As central bankers have increasingly considered the impacts of climate change and a net zero transition on their mandates, analysis has focused on the challenges of the technical uncertainty presented by financial and climatic systems. This report builds on previous work by focusing on how uncertainty created by political systems affects central banks. Political uncertainty is not inherently negative. It is often a byproduct of the dynamism inherent in democratic political systems. However, it can generate practical challenges for central banks and create a risk that they will avoid action on certain topics relevant to their mandates. This report offers central bankers a framework for defining different types of political uncertainty and principles to enable them to cope and move forward.

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Central bankers face three different types of political uncertainty in their work: **domestic, transnational and dynamic**. The first two are caused by factors largely external to the central bank. **Domestic political uncertainty** is caused by an inherent feature of democratic systems: the government and its preferences may shift with the next election, or even sooner. Beyond domestic borders, central bankers face **transnational political uncertainty** because they are embedded in global financial and economic systems that are impacted by the actions of governments around the world. **Dynamic political uncertainty** is caused by central bankers' interactions with their political systems; for example, they might receive political support or face a backlash when analysing or acting on politically sensitive topics.

Central bankers encounter each type of political uncertainty in the context of climate change and a green transition. For instance, there may be uncertainty over how the climate priorities of present or future governments may shift through democratic change (domestic). Similarly, the possibility of political shifts on climate policy in other countries can also impact any given central bank (transnational). Central banks may further be concerned about the potential political effects of any financial risk mitigation policies they undertake on climate change, and how these might be viewed by their government or other political actors (dynamic).

These forms of uncertainty also manifest in non-climate realms: for example, through sudden democratic change in funding priorities driving fiscal expansion or constraint (domestic); the nature and longevity of other countries' support in the event of a global financial or economic event, for instance via swap lines or fiscal support (transnational); or the domestic political effects of unconventional monetary policies (dynamic).

**How can central bankers think about these types of political uncertainty in relation to their work on climate change?** First and foremost, we caution against the risk of inaction in the face of uncertainty. It may be tempting to equate inaction with neutrality. However, inaction itself is a choice, not a default setting, and one that comes with serious risks of mandate failure. This report draws on political science, legal and other relevant scholarship, and offers three principles for coping with political uncertainty:

1. First, central banks should not seek ostensibly settled preferences as a prerequisite for action, given that social and political preferences on any topic rarely reach consensus and are also subject to ongoing change and dynamism. They must instead remain guided by their objectives, which are themselves the product of democratic processes.
2. Second, coordination, both domestically and internationally, can help reduce some types of political uncertainty and deliver well-managed transitions.
3. Finally, existing insights on how to cope with uncertainty in analytical work can be applied and extended to political forms of uncertainty, particularly in encouraging flexibility towards the future.

# 1. Introduction

Central bankers not only face technical uncertainty in understanding how climate change and a low carbon transition will affect their objectives, but also political uncertainty. This should not be viewed negatively, as it is a core part of the functioning of a robust democracy, reflecting the expression of a plurality of viewpoints as well as a range of possible futures and opportunities. However, as independent institutions, central bankers may find navigating these complexities challenging where they intersect with their work, given their remoteness from political processes.

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Over the past decade, central banks have increasingly begun to consider climate change in relation to their mandates for price and financial stability, advancing various forms of action in response. Central banks have typically come to understand the risks posed by climate change to their mandated objectives through the lens of physical and transition risks. Physical risks encompass the hazards posed to the financial system by the impacts of climate change, while transition risks are those posed by the shifts in productive structures and investments associated with a net zero transition. Central bankers have worked both in-house and through groups like the Network for Greening the Financial System (NGFS) to build the resources, capacity and tools to begin monitoring and responding to these risks as they relate to managing price stability in the face of various climate-related drivers of inflation, supervising banks' exposure to risk through their balance sheets and proactively addressing systemic sources of risk to the entire financial system.

**While the resources available for central bankers to measure and manage the impacts of climate change and a net zero transition have increased substantially, a recurring theme in these materials remains the challenges posed by uncertainty at various levels.** Which models and which parameters are best suited to model the highly complex dynamics of interdependent planetary, economic and financial systems? Existing work on uncertainty by central bankers has primarily – and importantly – focused on what this report calls technical uncertainty: how central bankers can measure and anticipate the financial impacts posed by climate change and a low carbon transition.

**However, this work has often abstracted from political uncertainty.** Central banks operate both within their domestic political systems, and global financial and climatic systems impacted by the political choices of other countries. These political types of uncertainty, in the context of a green transition, are the focus of this report. The report analyses central banks' embeddedness in political systems and the ways the uncertainty created by these systems impacts how they approach their tasks. This builds on earlier work on how different transition pathways will impact the mix of physical and transition risks.

**This report specifies the nature of political uncertainty for central bankers, the forms it can take and the opportunities and challenges that it presents. It categorises three types of political uncertainty that are relevant to central banks: domestic, transnational and dynamic.** The first two, domestic and transnational, are caused by factors largely external to central banks. Domestic political uncertainty is caused by the inherent variability associated with democratic systems. There is always the possibility that the policy stance of the government will shift with the next election – or even sooner – given the plurality of views likely to exist on any given topic. Transnational political uncertainty applies similarly at the international level and is instead caused by the variability of other governments' policy choices and the unknown futures of international collaborations. The third type, dynamic political uncertainty, is instead caused by central bankers' interactions with their broader political contexts. For example, central bankers often face the possibility of receiving political support or experiencing a backlash when their work intersects with politically sensitive topics.

**Specifying the varieties of political uncertainty that may hold central bankers back is important because of how much /s certain when it comes to climate change.** We know, for example, that the

climate is already changing, that global carbon emissions are continuing to rise and that the impacts of extreme weather events on economic and financial systems can be deeply consequential. As has been well covered in the economics literature, the primary risk of uncertainty is that it leads to inaction. Usually, this inaction comes in the form of economic actors delaying decisions, often as they relate to investment or consumption, but for central bankers uncertainty may instead lead to delaying policy or analysis. If it is difficult, or even impossible, to predict how some future government might redirect transition pathways, and whether they might look unfavourably on past climate work, would it not be easier for the central bank to do nothing at all?

There are two reasons why this strategy does not mitigate political uncertainty. First, **inaction creates its own risk for central banks that they will not be able to deliver on their primary mandates** for price and financial stability — precisely because of how much certainty exists regarding climate change (see Bolton et al., 2020). Second, **avoidance is not a substitute for neutrality**. At the most extreme end of the spectrum, ignoring climate change entirely would not be a politically neutral choice, but rather one that aligns solely with the preferences of those who support inaction. This leaves central banks no better off in the face of political uncertainty and at risk of failing to deliver on their mandates.

**This report offers three high-level principles for how central banks can cope with political uncertainty.**<sup>1</sup> First, central bankers do not need a settled political consensus to act on issues relevant to their primary mandates. A broad consensus may never exist on any given issue — for example, the particular pathway that a country should take to a net zero objective — and even where it does exist it is likely to grow and evolve. That a variety of views can co-exist is the dynamism of democracy. However, within these systems, central banks have been delegated a specific task and their achievement of that mandate is dependent on responsiveness to new developments. Second, coordination can help to reduce some forms of political uncertainty, though never fully. Finally, given that this dynamism should be expected, rather than resisted, central bankers should explicitly incorporate it into their analytical work where relevant.

**This report is intended to guide central bankers in thinking about political uncertainty when they face challenging circumstances and find themselves questioning how they can approach politically sensitive topics that are nonetheless relevant to their mandates.** While this report is focused on climate change and the net zero transition, it is also relevant for other testing — and often interlocking — areas of political uncertainty.

The remainder of this report is structured as follows:

- **Section 2** defines and introduces the differences and overlap between technical and political uncertainty.
- **Section 3** introduces a framework for categorising the three types of political uncertainty covered in this report.
- **Section 4** provides three high-level principles for coping with political uncertainty.
- **Section 5** concludes and summarises the policy recommendations covered by this report.

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<sup>1</sup> Thanks to Sylvain Maechler for suggesting the term ‘cope’.

## 2. Technical versus political uncertainty

This section defines and specifies how the technical and political forms of uncertainty faced by central banks differ. This helps to highlight the differences between uncertainty created by (1) the calculation of relative levels of physical and transition risk and (2) the way political systems impact the scope for central bank action. Technical and political forms of uncertainty share some overlap and can also interact to further empower or limit the scope for policy and political action.

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Uncertainty is an inherent feature of the central banking landscape across monetary policy, financial stability and bank supervision functions (see Box 2.1 for a conceptual overview). As former Fed Vice Chair Alan Blinder once remarked, “I don’t know of any interesting question in economic or social policy to which there is only one clear answer” (quoted in Conti-Brown, 2017).

The challenges of addressing uncertainty are compounded in the case of climate change and nature loss, where central bankers must also understand how unprecedented shifts in complex climate systems will interact with economic and financial systems and impact their objectives. For example, these challenges include predicting catastrophic climate impacts that may stem from tipping points such as extreme sea level rise from ice sheet melt. Another layer of uncertainty is contained in modelling the macroeconomic and macrofinancial impacts of climate change. While the integrated assessment models (IAMs) central banks use for this purpose continue to advance and provide a crucial form of foresight, a gap exists between any model and its underlying reality. For example, damage functions, which determine how the physical impacts of climate change will affect economic variables, often only consider temperature change because of modelling limitations, leading to uncertainty in how different climate impacts, such as sea level rise or drought, may interact to impact the economy (NGFS, 2024a). A similar dynamic exists for transition risks, where transition policies are often modelled as carbon prices, whereas different types of government climate policies such as incentives for investment or regulation may have distinctive macroeconomic and macrofinancial implications (NGFS 2024b).

Much of the literature on how central banks should manage uncertainty when it comes to climate change and nature loss has focused most acutely on what this report calls **technical uncertainty** (e.g. Chenet et al., 2021; Maechler and Graz, 2022, 2024). This, for example, encompasses the challenges described in the last paragraph. This form of uncertainty is defined as follows:

**Technical uncertainty** refers to the uncertainty that results from the task of measuring or anticipating climate-related impacts to the financial system.

Work on technical uncertainty usually focuses on physical and transition sources of climate-related financial risks. As is often recognised in existing works, the level and nature of both physical and transition risks are determined by both planetary and political systems (Bolton et al., 2020; Chenet et al., 2021; NGFS, 2024b). Different scenarios of physical and transition risk inherently encompass different policy mixes that imply different choices by governments to transition to a lower carbon economy sooner, later, or not at all.

However, the *politics* of such transition pathways are often abstracted in favour of a narrower focus on defining and measuring climate-related financial risks that flow from these policy mixes. The starting point for this report is an insight from the existing work — that central banks’ political environments are relevant for the ways that they achieve their mandated objectives — but rather than focusing atomistically on central banks as isolated in independence, it takes a fuller view of their embeddedness in their political landscapes, and the dynamics to which this gives rise.



There are three broad ways that central bankers are embedded in their political contexts:

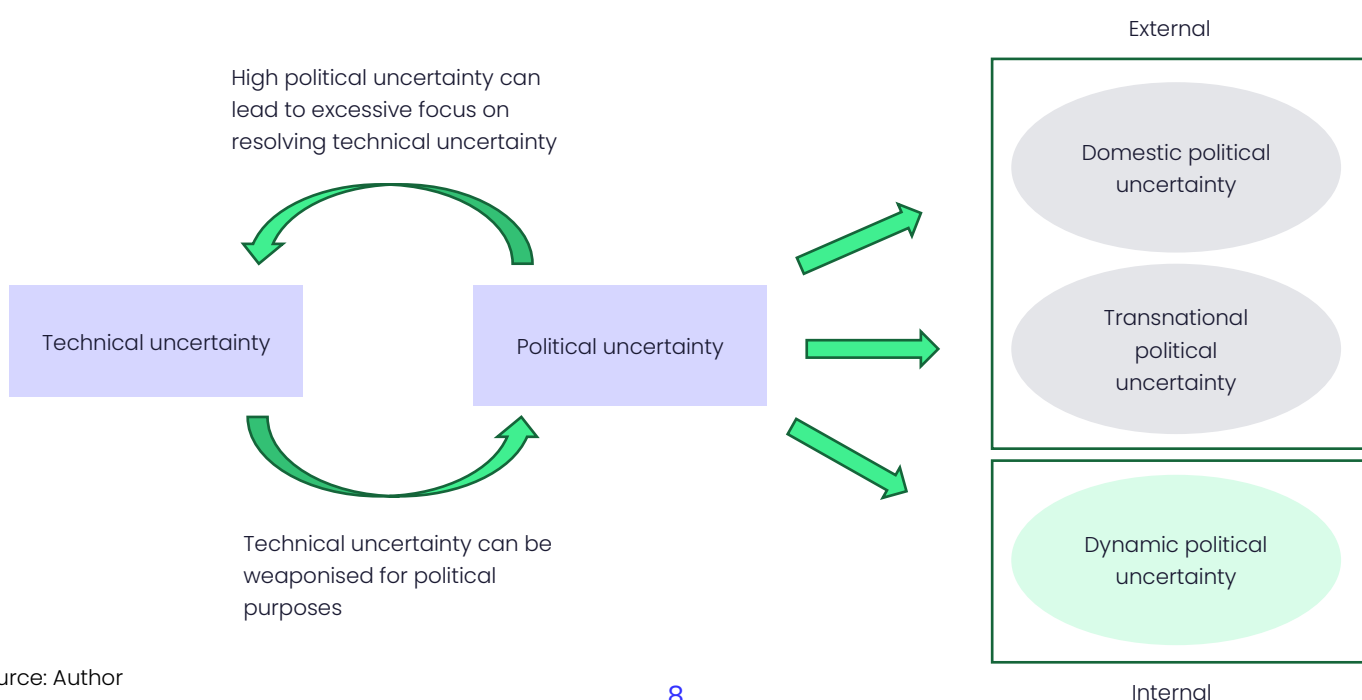
1. First, these political contexts are **impactful for central banks' ability to achieve their mandated objectives**. As recognised in other works, the nature and pace of a net zero transition will primarily be set by governments, both domestically and abroad (Reitmeier et al., 2025; Bolton et al., 2020).
2. Second, **central bank policies and research outputs are also relevant to government agendas and different political actors' abilities to achieve certain objectives** (Bateman and van 't Klooster, 2024; van 't Klooster and Weber, 2024). This means that these political actors are likely to have views, sometimes strong, on central bank policy decisions.
3. Finally, **central banks are institutions whose governing legislation is in the hands of elected officials to whom central banks are accountable, including under conditions of independence** (Downey, 2024a). Even central bank mandates are the outcomes of political discussions and processes, rather than inalienable institutional features. This means that shifts in political preferences may also impact the scope or parameters of central banks' work.

Taken together, these features illustrate former ECB President Mario Draghi's observation that central bank independence is better defined as "independence in interdependence" (Draghi, 2016). Given the variability present in political systems, this interdependence introduces a persistent source of uncertainty for central bankers. At a high level, political uncertainty can be defined as follows:

**Political uncertainty** refers to forms of uncertainty faced by central bankers that result from the political and social contexts within which they are embedded.

**Technical and political sources of uncertainty are related to one another.** Figure 2.1 summarises these relationships. On the one hand, as above, they will overlap: different scenarios of physical and transition risk stem in part from uncertainty in the decisions of political actors. They can also interact (Jensen and Wu, 2016; Wu et al., 2016). Technical uncertainty may change the political calculus for central banks, because it can be weaponised for political purposes. Political actors who would prefer not to have climate policies may point to uncertainty as a reason for inaction (Elliott, 2023) or criticise central banks for precautionary action. At the same time, excessive focus on resolving technical uncertainty through metric-building, rather than implementing policy in the face of unresolvable technical uncertainty, can be a strategy for central banks embedded in contexts of high political uncertainty where climate-related policies may have uncertain political consequences, even when directly tied to their primary objectives (Maechler and Best, 2025).

**Figure 2.1. Overview of report typology**





## Box 2.1 Risk and uncertainty

Scholars writing about central banking and climate change have often distinguished between events that have a calculable probability (**risk**) and those that do not (e.g. **radical** or **Knightian uncertainty**) (Bolton et al., 2020; Chenet et al., 2021; Elliott, 2023; Kedward et al., 2023; Maechler and Graz, 2022). In other words, there can be both ‘known unknowns’ (calculable) and ‘unknown unknowns’ (incalculable) (Maechler and Graz, 2022). These scholars have often used this distinction to indicate the radical forms of uncertainty involved in anticipating the impacts of climate change on the financial system and argue in favour of precautionary action when risks are incalculable.

In the context of democratic political systems, Przeworski (1991) posits that political uncertainty often follows the first description of ‘known unknowns’: in principle, actors know what is possible and even likely to occur because of the institutional frameworks governing the rules of politics, and because they are aware of the positions of different political groups. However, more radical departures in existing terms of political engagement that cannot be anticipated are also possible, for example a rupture in existing levels of global cooperation or democratic norms (Matejova and Shesterinina, 2023). In the central banking context, such radical departures could instead take the form of major shifts in institutional frameworks that govern independence.

In addition to risk versus uncertainty, scholars have also distinguished foundationally between different forms of uncertainty. Several of these forms, with examples from the political realm, are given in Table 2.1. Each of the types of political uncertainty covered in this report in the context of central banking can have elements of each of these foundational categories.

**Table 2.1. Foundational forms of uncertainty**

Form	Definition	Political examples
Epistemic	A lack of information or knowledge	Lack of information sharing among relevant actors (e.g. central bank, other regulators, finance ministry, elected officials)
Ontological	Inherent and irreducible variability in the world	Changing political preferences and priorities institutionalised in democratic systems
Complexity	Too much information	High number of relevant policy actors and institutions both domestically and internationally
Ambiguity	A lack of shared meaning	Different “frames of reference” (Dewulf and Biesbroek, 2018) or “worldviews” (Katzenstein, 2022) which cause different political actors to interpret events in different ways

Source: Author’s table, drawing from Dewulf and Biesbroek (2018), Maechler and Graz (2022) and Matejova and Shesterinina (2023); see also Hiebert and Monnin (2025). Note that these sources are not presented as being mutually exclusive but can overlap and intersect.

### 3. A framework for understanding political uncertainty

This section focuses on political uncertainty in the context of central banking, identifying three types of political uncertainty for central bankers – domestic, transnational and dynamic – and reviewing each in detail. The first step in coping with political uncertainty is understanding it. This framework provides a basis for central bankers to make sense of their experience in interacting with the variability of the political systems in which they are embedded.

Very few guidelines exist for central bankers that outline what political uncertainty means for their institutions. One reason for this is the taboo associated with political topics for independent central banks. Central bankers may feel uncomfortable acknowledging the ways that their political contexts impact their institutions for fear that this may be perceived as crossing a boundary of independence (Best, 2022). However, central bankers cannot avoid politically charged topics relevant to their work. To discuss political uncertainty is not to undermine central bank independence, but to systematise an inherent feature of any public institution embedded in a political landscape – including in the context of central banks’ primary mandates.

#### The framework

**Table 3.1. Types of political uncertainty for central banks**

Type	Mechanism	Monetary policy	Macro- and microprudential supervision
Domestic political uncertainty	Varied preferences among politicians and the public in democratic systems; continuous possibility of policy changing course in the domestic setting	How might unstable transition pathways impact primary objectives? How to manage changing priorities in secondary mandates?	How to assess alignment with transition pathways and the level of associated risk? Are pathways stable?
Transnational political uncertainty	Uncertainty in the nature and longevity of other countries’ climate approaches and developments in transnational collaborations	How do policies in other countries impact the mix of physical and transition risks? How stable are these policies?	Will there be international harmonisation in the supervision of climate risks? What spillover effects might there be?
Dynamic political uncertainty	Political effects of central bank activities	How to conduct analysis, develop policy and manage communication for politically controversial topics that are relevant to central banks’ mandates? Will there be a backlash?	

Source: Author

**Table 3.1 distinguishes three types of political uncertainty for central bankers: domestic, transnational and dynamic.** The first column introduces the type, the second provides a definition and the third and fourth columns give examples of how each type of uncertainty can manifest in different areas of central banks' work. The first two types, domestic and transnational, largely arise exogenously to the central bank. The third type, dynamic, is rather caused by the uncertainty faced when central banks act, or contemplate action, and the ways that these actions interact with broader political contexts.

**Importantly, these types of political uncertainty are not inherently undesirable, and in fact are often explicitly part of the design of our political systems and institutions. They can promote flexibility and allow for a plurality of views to inform economic policy formulation.** This also means that while some forms of uncertainty can be reduced, this is not always possible or even desirable, as is explored in detail in Section 4. The purpose of this framework is rather to promote an explicit recognition of these uncertainties, so that the opportunities they pose can be harnessed and central bankers can cope with the challenges posed by being institutionally situated in uncertain political environments.

## Domestic political uncertainty

First, **domestic political uncertainty.** Domestic forms of political uncertainty are caused by the design of the social and political systems within which central banks are embedded (see Matejova and Shesterinina, 2023). For central banks in democratic political systems, like those focused on in this report, the dominant form of political uncertainty faced at the system level comes from the uncertainty that is one of the central mechanisms of democracy itself. There is always the possibility that the government may change in small or large ways with the next election, and with the change in government may come a change in priorities and policy (Shapiro, 2003; Downey, 2024a).

Furthermore, central bankers may prefer in theory to act solely on issues where there is a stable social consensus with 'settled' preferences, as suggested by former Bank of England (BoE) Deputy Governor Paul Tucker (Tucker, 2018). However, in practice it is rare for this to be the case for any of the policy areas covered by central banks, from interest rates to bank capital to managing climate risks.

That such varied views can be held and expressed by different elected officials and the public is one of the strengths of democratic systems. Domestic political uncertainty is itself one of the core features of a healthy democracy (Przeworski, 1991). At the same time, these inherent features also present practical challenges for central bankers.

**For climate change and a green transition, domestic political uncertainty can come in many forms.** In the case of the United States, the changes in presidential administrations with the 2016, 2020 and 2024 elections had major consequences for a green transition, as different administrations oscillated between climate denialism and ambitious green legislation. One impact for the central bank is the difficulty of anticipating longer term policy considerations.

Parallel dynamics unfold in other countries, though often at less drastic scales. In the United Kingdom, the major parties have shown an appetite for some level of climate action, yet the relative emphasis on both the priority and the pace of a green transition has fluctuated in recent years. While Rishi Sunak as Chancellor of the Exchequer supported the initial addition of climate change to the BoE's annual remit letters, as Prime Minister he led a rollback of several key emission-cutting programmes (Pearce, 2023; Brenton, 2024). In 2023, climate change was also downgraded in the annual remit letter and BoE Governor Andrew Bailey stated that the bank would spend fewer resources on its climate work as a result (Economics Affairs Committee, 2024).

In the European Union, these dynamics are playing out at both the national and EU-wide levels, as recent years have witnessed both climate leadership through the Green Deal and the electoral ascent of political parties that reject climate policy (Youngs, 2024; Eichhorn and Grabbe, 2025; Gros, 2025).

**For central bankers, this can present analytical challenges in anticipating transition pathways — or lack thereof — and thus relative levels and sources of physical and transition risk.** There is still a substantial gap between existing government policies and those that would be required to meet the nationally determined contributions (NDCs) under the Paris Agreement, which implies uncertainty in terms of

both (1) which future types of policies may be pursued to achieve these commitments and (2) the pace at which those policies will be enacted (e.g. an orderly or disorderly transition) (IPCC, 2023).

Different types of climate policies – subsidies and investment, regulations and standards, and carbon prices – each have their own distinctive macroeconomic and macrofinancial implications that are relevant to central banks (Gabor and Braun, 2025). On the monetary policy side, the nature and longevity of climate policies have important implications for investment, consumer and investor preferences, supply chains and, ultimately, inflation, both in the medium and longer term (NGFS, 2024b; van 't Klooster, 2025). In prudential supervision, this form of uncertainty becomes relevant when anticipating the relative levels of physical and transition risks to which banks and insurers will be subject, and thus how to calibrate supervisory action.

**Importantly, taking the perspective of political uncertainty highlights the reality that, while certain elements of transition pathways will become clearer over time, they will never be fully known: they will always be the product of ever-shifting political preferences, priorities and processes.** There are always likely to be different factions supporting or opposing different types and levels of policy action for climate change and the shape that a net zero transition should continue to take. It is not the central bank's job to choose among these factions, deny that they exist, or replace the political processes that already exist to mediate among them. Central bank approaches should embrace and be robust to this uncertainty, rather than anticipating its eventual resolution.

## Transnational political uncertainty

Second, **transnational political uncertainty. While central banks may govern as domestic institutions, or supranational representatives of democratic nation states, as in the case of the European Central Bank (ECB), they are embedded in global political, climate, financial and economic systems that impact their tasks** (Best et al., 2025; Borio et al., 2008). The levels of climate impact and the pace and nature of a green transition are not only determined domestically, but also internationally. While initiatives such as the Paris Agreement seek to reduce some of this uncertainty, in practice the pace, coverage and nature of the policies that other national governments may implement are largely uncertain.

Policies such as green subsidies versus emissions trading systems (ETs) have different global macroeconomic impacts and spillover effects (Mann, 2023). At the same time, Larch and Wanner (2024) estimate that US non-participation in the Paris Agreement would eliminate more than one-third of global emissions reductions. Each of these considerations impacts the potential climate- and transition-related effects on inflation and output that any given country will face, depending on the balance of physical and transition risks that materialise. These latter risks would also be heightened by the possibility of a globally uncoordinated (or worse, uncooperative) transition, transmitting via trade and investment channels to impact prices and output (Espange et al., 2023; Gardes-Landolfini et al., 2023; Barmes et al., 2024; Weber et al., 2025).

**This combination of high uncertainty and high impact creates a challenge for central bankers.**

Currently, central banks in any given country are institutionally remote from the development of other countries' climate and trade policies, but at the same time whether they achieve their mandated objectives is deeply dependent on those policies. While central bankers may be able to reduce some dimensions of this uncertainty, for example by coordinating with other central banks on best practices for climate-related banking supervision through transnational forums (see Section 4), another element of this uncertainty is irreducible given the inherent and enduring unpredictability of political actors in other jurisdictions (Dewulf and Biesbroek, 2018). Furthermore, broader shifts in geopolitics and a trend towards geoeconomic fragmentation, most recently exemplified by the tumult around the moves towards unprecedented levels of tariffs by the US, will further exacerbate these climate-related uncertainties.

These dynamics also play out in a unique way for the ECB. While it acts similarly to other domestic central banks in transnational forums, unlike them it has to contend with intra-EU dynamics within its jurisdiction and no EU-level political institution is equivalent to those associated with the other central banks (Quaglia et al., 2025). National cleavages in support for both the nature and scope of measures

taken by the ECB and other EU institutions — for example, the issuance of common EU debt — create a special political complexity for the ECB (Jones, 2021). This is a particular issue at times of crisis.

**These challenges manifest clearly in the realm of cross-border banking supervision.** For example, at the ECB the new Capital Requirements Directive (CRD) VI requires credit institutions to develop transition plans for the purpose of managing climate risks (Smolenska, 2025). These plans must not only take into account transition risks from the EU's 2050 objective for climate neutrality, but also relevant third country regulations and objectives for 'internationally active' institutions (EBA, 2024, 2025). Where these third country regulations and objectives have either not yet been specified or are subject to volatility, this creates challenges for banking supervisors, who must nevertheless ensure that firms are prepared to manage the risks and opportunities of a net zero transition in their home country. This uncertainty creates an imperative for higher standards for regulators to ensure that banks exposed to third countries are prepared for the balance sheet impacts associated with a range of possible transition pathways, for example through the scenarios selected as input to transition plans (Dikau et al., 2025).

## Dynamic political uncertainty

Third, **dynamic political uncertainty**. Central bankers face dynamic forms of political uncertainty **because the actions they take in executing their objectives can have political consequences**. Compared to the other two types of political uncertainty, this form is distinctive in that it is caused by the actions of the central bank.

**One version of dynamic political uncertainty is captured in the literature on the reputational politics of central banking.** Central bankers may be uncertain over how their work will be perceived by elected officials, the broader public, or other audiences (Blondeel et al., 2024; Moschella, 2024; Moschella and Pinto, 2019). They may face the risk of a political backlash when they apply their technical expertise to problems that are politically contentious. This can be the case for anything from analytical work to more substantive policy intervention. There may be uncertainty over the degree and nature of that backlash, which can incentivise a certain level of delay or inaction. This often has to do with the strength of the vested interests that stand to be impacted given certain courses of policy. At the same time, there can also be positive political effects from other groups, and more broadly when central banks are viewed as achieving their mandated objectives.

It is the responsibility of elected governments to facilitate policy processes that adjudicate between the preferences of different groups. **However, it is practically impossible for central banks to entirely avoid these topics in their work where they impact their primary objectives.** At the mild end of the spectrum, a backlash may take the form of public criticism of the central bank, bringing unwanted attention and a perception that it is being overly political. While this should not be an impediment to independent central banks acting within their mandates, there are incentives to self-censor in order to mitigate political risks and threats to their independence (Blondeel et al., 2024; DiLeo et al., 2023; Jabko and Kupzok, 2024; Moschella, 2024). At the extreme end of the spectrum, central banks may worry that a backlash could lead to weightier charges of overstepping their mandates, potentially leading to more serious consequences involving the political bodies responsible for overseeing them.

There are several examples of dynamic political uncertainty in both the climate and non-climate realms. For example, in the absence of clear government action, the central bank might assess climate risks assuming a business-as-usual scenario and act accordingly, which could encompass risk management across its financial stability, bank regulation and even monetary policy functions, ranging from conducting research and analysis to issuing new regulatory requirements for banks. However, this runs the risk of attracting criticism from elected officials or the general public if action taken to mitigate such climate-related risks is interpreted as a rebuke to the government's position. This kind of risk is reminiscent of 2016, when then-BoE Governor Mark Carney drew sharp criticism for suggesting that Brexit might lead to a recession in the UK. Carney defended himself by saying that the BoE's role was to "identify risks, not to cross your fingers and hope risks would go away" (BBC, 2016).

**Dynamic political uncertainty also intersects with the other forms:** for example, the central bank may anticipate a *future* backlash from current work as political tides and government administrations shift

domestically. The political risk described here often comes from tasks relevant to the central bank's primary mandate and essentially presents a trade-off between pursuing analytical work and relevant policies and seeking an image of strict political non-intervention. These aspects of dynamic political uncertainty point to the most profound risk of all: that the seemingly risk-averse choice of policy inaction in the present will lead to a much higher level of mandate failure in the future. This is covered in the next section.



## 4. Coping with political uncertainty

Political uncertainty is a feature, not a bug, of central banking. While some political uncertainty can be reduced – for example, through coordination – in many circumstances it is neither possible nor desirable to do so. Central bankers must learn to cope with political uncertainty, rather than shy away from it. This section offers three principles to inform action in the face of political uncertainty. It encourages central bankers to guard against the greatest danger associated with political uncertainty: leaving vital parts of their mandates unfulfilled and abdicating their obligations as public servants.

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### The risks and opportunities of political uncertainty

**Political uncertainty presents both risks and opportunities for central bankers.** The biggest risk is that uncertainty leads to inaction in an attempt to stay out of the political fray, even where it involves work that is directly relevant for central banks' abilities to achieve their mandates. Hiebert and Monnin (2025) similarly refer to this risk as an 'inaction bias'. Prospect theory offers a useful analogy for the trade-offs that might be perceived by central bankers: they may be motivated to delay action to minimise present political risk and maintain the status quo, even when the longer-term gains of proactive climate risk management and transition alignment are substantial (Levy, 1992; Wu et al., 2016).<sup>2</sup>

**However, political avoidance is a false substitute for political neutrality, even where there are different social or political groups with divergent preferences.** In the simplest case of climate policy versus no climate policy, inaction simply aligns the central bank with the preferences of those who advocate for inaction, rather than aligning the central bank with its own institutional objectives.<sup>3</sup> Often, the flip side of inaction in the face of political uncertainty is an even larger risk of mandate failure. Looking at the problem from this angle, central banks face a certainty of mandate failure if they ignore climate change. As put by former ECB President Mario Draghi (2019) in the context of the ECB's controversial Outright Monetary Transactions (OMT) programme:

*So, what gave us the courage to act was the conviction that there was a far greater risk if we did nothing. Inaction would have meant nothing less than the failure of our mandate and, potentially, of the currency we had been tasked with preserving. This reality made the course taken inescapable – meaning it was the only viable option for any responsible policymaker.*

### Principles for coping with political uncertainty

#### Principle 1: Consensus is not a prerequisite for action

**The inescapable presence of uncertainty in democratic political systems means that a broad consensus or settled preferences on any issue area should not be taken as a prerequisite for central bank action.**<sup>4</sup> First, because consensus itself is poorly specified. What threshold constitutes a consensus that is strong enough for central bank action on any given issue? What level of specificity

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<sup>2</sup> Weighing the outcomes of action versus inaction is also compounded by the reality that it may be impossible to calculate a risk distribution for different courses of action, for reasons outlined in Sections 2 and 3 of this report.

<sup>3</sup> The political conflicts over bank capital provide an insightful analogy on this point, see Michaels (2023) and Conti-Brown (2024).

<sup>4</sup> On this, also see Downey (2024b).



should this consensus demonstrate? And why should we expect that any consensus would be permanently settled?

Second, because consensus is not the primary mechanism of democratic governance. As independent agencies, central banks are bound to democratic governance by their legislation (and ongoing accountability arrangements), which itself is typically the product of a majority of representatives. While infrequent, their legislation can also be changed by the same majority threshold (with the treaty-governed ECB a particular case<sup>5</sup>). Given this, central banks must be guided by their mandated objectives, rather than their approximation of a social consensus on a given issue.

**What does governing in the midst of this dynamism look like in practice?** As central banks have begun to broadly recognise, their primary mandates already require that they pay attention to climate change and a well-managed green transition, given the profound impacts of both on price stability. However, given that there is never likely to be a broad consensus on what exactly central banks should do, central banks will also face dynamic political uncertainty and its attendant political risks when they do choose a course of action.

How can they think about this? Central bankers' institutional frameworks limit their institutional remit and also compel them to act to achieve their objectives in the public interest. Having institutional integrity means remaining committed to these principles even where they come with attendant political risks – having 'courage', as conceived by Draghi.<sup>6</sup> The ongoing integrity of a central bank depends on its ability to respond effectively to novel issues as they arrive.

**At the same time, integrity is also the foundation for both boundaries and accountability, which are crucial pillars for any independent agency.** While central bankers should not hesitate to make technical judgements about political topics relevant to their mandates, they should avoid the opposite scenario where they adjudicate between the values that underpin the preferences of different social groups (Conti-Brown and Wishnick, 2021). As above, the alternative is that central banks instead risk mandate failure.

## **Principle 2: Coordination can help to resolve some, but not all, political uncertainty**

**While many of the examples of political uncertainty covered in this report are irreducible, some forms can be mitigated through better coordination at both the domestic and international levels.** Domestic coordination can to some extent reduce the unknowns surrounding dynamic political uncertainty – the political consequences of central bank action – by (1) making it more likely that the central bank's approach will align with that of other domestic political actors in legislatures and other government ministries and/or (2) building support for the central bank's approach through proactive communication about how this helps fulfil its objectives. Domestic coordination can also deliver a more effective response to the challenges posed by climate change.

**On the one hand, central banks are policy takers. As has been widely emphasised, it is up to elected officials to set the pace and nature of a net zero transition, not central banks.** Several authors have provided specific suggestions for the forms that better domestic coordination can take, especially where central banks have secondary mandates to support government objectives. For example, in the case of the ECB, van 't Klooster and de Boer (2023) recommend several avenues for the European Parliament to articulate explicitly how the bank should interpret its secondary mandate (see also Grünewald and van 't Klooster, 2023; Smolenska et al., 2024).

**At the same time, central bankers also have an active role to play in monitoring a broad range of issues relevant to their tasks and coordinating with fiscal authorities and other actors where warranted, even when acting themselves is outside of their scope** (van 't Klooster, 2025). While central banks are politically independent, they are not fully exogenous from their broader policy ecosystems. They can apply their expertise on topics such as the macrofinancial implications of climate change and a green transition to co-construct shared meaning on the role that central banks can play and

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<sup>5</sup> Interestingly in this context, there have been recent pushes for an expansion of qualified majority voting within the EU; see, for example, Draghi (2025) and Lagarde (2025).

<sup>6</sup> Also see Perez (2014) on regulatory courage.

also the financial and economic implications of other actors' policies. Practically speaking, this could take the form of inter-agency committees in which different institutions coordinate on a green transition, while remaining squarely within their respective legal mandates (Tamez et al., 2024).

**Going further, monetary–fiscal coordination can be effective in delivering a well-managed net zero transition, where central banks have the mandate.** Central bank interest rates have a direct bearing on the investments needed to finance a green transition, through both public and private channels (Svartzman et al., 2021), and monetary and fiscal authorities can work together on the design and implementation of green finance policies that are adaptive to different interest rate environments. Reitmeier et al. (2025) furthermore provide a functional and comprehensive framework for policy coordination in the context of the net zero transition.

**Similar principles can apply at the international level. While some forms of transnational uncertainty are inherently irreducible because the future actions of relevant actors in other countries will always to some extent be unknown, coordination through international networks is an important tool for complexity reduction.** These networks can serve several purposes, including the *harmonisation* of policies through standard-setting networks such as the Basel Committee on Banking Supervision or the Financial Stability Board (Slaughter, 2004). The NGFS brands itself as a “coalition of the willing”. It has both *informational* and *normative* roles, serving as a forum to share information and work through challenges, and also to define new shared best practices, reducing some level of uncertainty (Helleiner et al., 2024).

Recent years have seen an increase in geoeconomic competition and in some instances fragmentation of global cooperation, for example with the withdrawal of the Fed and other US institutions from the NGFS. However, **these networks have already proved highly resilient** to US intransigence: the NGFS in fact emerged and grew rapidly in a period of US non-cooperation on global climate initiatives during the first Trump administration (Helleiner et al., 2024). One possible outcome is a new era of ‘like-minded internationalism’ for both central banks and other key policy institutions, defined by issue-driven coalitions rather than universal consensus (Ishmael et al., 2025).

### **Principle 3: Consider the possibilities of political uncertainty in analysis**

The analytical implications of political uncertainty are largely the domain of the existing works mentioned in Section 2, which focused on technical forms of uncertainty. For example, to anticipate how different government transition pathways — or lack thereof — are likely to impact the relative mix of physical and transition climate-related financial risks, central banks have pioneered the application of scenario analysis to climate change (NGFS, 2025). This report will not repeat these approaches here. However, situating existing approaches in a broader frame of political uncertainty does warrant a few additional observations.

**First, given both domestic and transnational forms of political uncertainty, regularly updated scenario analysis will almost certainly always have a place in central banks' toolkits on climate change.** Even as certain aspects of transition pathways become clearer — for example, whether net zero is likely to be achieved in a certain timeframe, and the policy mix used to achieve that particular objective — there will always be various groups advocating for different pathways, and the possibility of policies changing course. Given this, central banks need to stay flexible in their approaches and remain attuned to how possible futures will impact their mandated objectives.

**Second, part of this flexibility comes from non-traditional sources of knowledge and expertise.** For example, Conti-Brown and Wishnick (2021) identify four different sources of relevant expertise for central banks: input from the public, internal knowledge production, dialogue within the administrative state and experiments in the field. Each one of these forms of expertise produces a new stream of knowledge for central banks. Others have also advocated for central bankers to look to experts in other fields, for example climate scientists, a practice some central banks have begun to embrace (Maechler and Graz, 2022; Helleiner et al., 2024). The forms of political uncertainty highlighted in this report indicate the benefits of looking more broadly at collaborations with a broad range of social and natural scientists. These collaborations could, for example, continue to build on work like that by Gardes-Landolfini et al. (2023) to incorporate geoeconomic considerations into scenario design.

**Finally, the strength of scenarios is not necessarily predictive, but rather analytical.** They encourage central bankers to ask different types of questions; to understand how other types of social, political and natural systems function and interact with financial and economic systems; to think in different time horizons; and through all of these tasks to become more flexible in the face of persistent uncertainty. In this way, uncertainty can be 'organised', even if it is not reduced (Power, 2008; Smolenska and van 't Klooster, 2022). While many forms of political uncertainty are not reducible, these forms of organisation, including the framework introduced in this report, can help central bankers cope with these realities.

## 5. Conclusion and policy recommendations

This report has introduced a framework for understanding the different types of political uncertainty that central bankers face and underscored the importance of moving forward on issues relevant to central bank mandates, even in the face of substantial political uncertainty. While central bankers must take care to adhere to their mandated objectives, they must not shy away from addressing issues relevant to those mandates, including climate change and a green transition, when they have high levels of political uncertainty. Ignorance does not make central banks' political entanglements disappear nor does it render them neutral; it only makes them less prepared for issues that are of direct relevance to their mandates.

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We argue first and foremost that central bankers should not let political uncertainty get in the way of their work, taking caution to avoid the 'inaction bias' that uncertainty can cause (Hiebert and Monnin, 2025). Otherwise central bankers face an even greater risk of mandate failure. As Mario Draghi said, "There are situations in which even the best analysis does not provide enough certainty to render making a decision easy; it is often tempting not to make a decision at all. But this is precisely the point at which policymakers must draw on [a] second quality: courage. For inaction is also a decision" (Draghi 2019).

**Central bankers face three types of political uncertainty in their work: domestic, transnational and dynamic.** The first two are largely external to the actions of central banks, whereas the third results from the impacts of central bank actions. Domestic political uncertainty is caused by the inherent uncertainty specific to the design of democratic political systems, given that a plurality of viewpoints is encouraged and there is always the possibility of governments shifting course, through elections and other mechanisms. Transnational political uncertainty is caused by uncertainty in the actions of other countries and the ways in which those impact central bank objectives, as well as the possibilities for global cooperation. Dynamic political uncertainty is caused by the potential for political effects from central banks' actions in pursuing their mandated objectives, for example a political backlash from certain groups. Importantly, these forms of uncertainty are not inherently negative, but rather are neutral features of central banks' social and political contexts and can also present opportunities.

**We offer three principles for central bankers to cope with political uncertainty in their work.** While some forms of political uncertainty can be somewhat reduced, they can never be entirely eliminated. The purpose of these principles is primarily to help central bankers better understand the challenges they face, and to move forward with action in the face of uncertainty rather than to necessarily seek to resolve it.

1. First, central bankers should not seek a seemingly stable political consensus ahead of action on any given issue relevant to their mandates if they are acting in pursuit of their legislated objectives, which are themselves the product of democratic processes. Dynamism is a feature of political systems, rather than a bug, and social and political preferences on any given issue are rarely permanently settled.
2. Second, while consensus is not a prerequisite for action, collaboration with other domestic political actors, as well as international counterparts, can serve to reduce some forms of political uncertainty. This could, for example, take the form of inter-agency committees (Tamez et al., 2024) or draw inspiration from the 'building blocks' set out by Reitmeier et al. (2025).
3. Finally, given that dynamism should be expected, central bankers should explicitly incorporate this into the ways that they think about their analytical work. One perspective on this is the

ongoing role of scenario analysis: given the uncertainty of social and political systems at all points of a transition pathway, there will always be a role for these and similar exercises in central bank toolkits. Another is elevating the importance of the role of diverse forms of expertise (Conti-Brown and Wishnick, 2021; Maechler and Graz, 2022).

Uncertainty is a familiar companion for all actors operating within political systems. While central banks may be independent from political institutions, they remain interdependent components of the broader system, as Draghi (2016) notes. The stakes are high: even as experts warn of escalating environmental and climate risks (Elderson 2025), the path towards a global transition to carbon neutrality remains uncertain, and some central banks are navigating increasingly complex political and institutional pressures. Although these uncertainties cannot be eliminated, we offer an initial framework to cope with them. Central banks that recognise their place within political systems can use this awareness to go forward with both humility concerning their limitations and confidence in their actions.

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