



**Green
Indian
Financial
System**



**GREENING THE
INDIAN FINANCIAL SYSTEM**

C O N F E R E N C E T A K E A W A Y S

January 28th, 2022

Inaugural Conference
of the Green Indian Financial
System Initiative

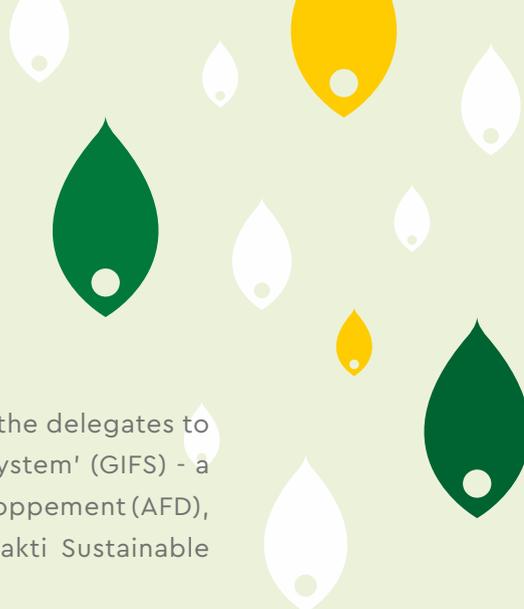
An Initiative By





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Ms. Kruthika Jerome from Shakti welcomed the speakers and the delegates to the inaugural conference 'Towards a green Indian financial system' (GIFS) - a joint multi-stakeholder initiative by Agence Française de Développement (AFD), Small Industries Development Bank of India (SIDBI) and Shakti Sustainable Energy Foundation.

OPENING REMARKS

Mr. Sivasubramanian Ramann,
Chairman, SIDBI

Commencing the GIFS initiative, Mr. Ramann began with a quote from Mahatma Gandhi - "The world has enough for everyone's need, but not enough for everyone's greed." He stressed upon the need for changing our high consumption lifestyle to save our environment. The growing frequency of severe natural events like cyclone and droughts indicates that climate change is real. In COP26, India has announced its NetZero targets and enhanced its 2030 commitments which establishes the countries contribution towards the global mission of greening the climate. India has committed to reduce its emission intensity of GDP to 45% by

2030 from the earlier target of 33-35% with respect to 2005.

The challenges to achieving the enhanced target is multi-dimensional and financing mitigation activities at scale remains a major barrier. According to some estimates, India needs around US\$2.5 trillion to achieve its nationally determined (NDC) targets by 2030 which is further enhanced in Glasgow. However, as of 2018, the climate and green investments in India represents only 13% of the required annual investment.

The MSME (micro small and medium enterprises) sector's contribution to India's gross domestic product (GDP) is almost 30% and is the second largest employer after agriculture. However, adverse impact of climate change is skewed towards the MSME sector as they do not have the resources and financial strength to overcome a complex problem like climate change. The MSME sector needs technical assistance, skill building support, supply chain innovation and enabling regulatory environment to build resilience and survive. SIDBI has identified energy efficiency, climate change and green ecosystem building as thrust area. SIDBI has setup dedicated vertical to provide advisory support to MSMEs to make them climate resilient and ensure their survival and competitiveness in the long run. SIDBI has customized global best practices to Indian context and financed energy efficiency loans to around 10,000 MSMEs in last five to six years. SIDBI believes in collaboration and works in tandem with its domestic and international partners.

As an accredited entity to Global Climate Fund (GCF), SIDBI will not only further its own green agenda but will help partner organizations raise

funds through GCF route. SIDBI plans to provide technical and financial assistance to over 100,000 MSMEs in coming 10 years in collaboration with international agencies like GEF, GCF, The World Bank, AFD, JICA, KFW, ADB etc. Another focus area for the country and SIDBI is green mobility. SIDBI will support development of charging infrastructure across the country.

SIDBI is developing an integrated credit rating model under which the units will be rated against their social and environmental performance along with financial parameters. Going forward this practice will be shared with the industry. Additionally, to reduce its own carbon footprint, SIDBI is working towards achieving carbon neutrality by 2024. SIDBI made its foray into development sector through its newly established entity SIDBI Swavalamban Foundation.

The Foundation will cater to the unserved and under-served areas to create rural entrepreneurs and promote sustainable value chain. SIDBI will continue to further India's sustainable development goals (SDG) through establishment of social stock exchange and issuing

green bonds. SIDBI believes that green financing to MSMEs will play a major role in the overall efforts to fight climate change and achieving India's NDC target set for 2030. SIDBI understand that ability to act

and inability to impact derails best of intensions. SIDBI's initiatives will always have an embedded theme of inclusive, innovative and impact aligned engagement.

OPENING REMARKS

Mr. Rémy Rioux,
AFD CEO

Welcoming the joint initiative by AFD, SIDBI and Shakti, Mr. Rémy Rioux, AFD CEO, stressed the importance of strengthening bilateral relationship and collaboration between India and EU. He reiterated the changing policy landscape as governments all over the world clarify long-term climate objectives, contributing towards (near) mid-century decarbonization. With India's COP 26 announcements, policy direction has been communicated to financial institutions – however, these must now be broken down into short-term objectives, complemented with decarbonization trajectories and roadmap. Banks and financial

institutions will play a major role in achieving climate neutrality through financing this huge and complex transition.

AFD, as an international actor, has committed to be fully aligned to Paris agreement. In keeping with this commitment, AFD has developed several methodologies and modelling systems to integrate climate change in their investment framework; wherein the institution would be happy to collaborate and share knowledge with Indian colleagues and financial community. Mr. Rioux emphasized on the vast potential that lies before India with regard to green markets, with India

being the second largest emerging green bond market today. AFD aims to be a strong project partner, where majority of the projects financed by AFD in India are already climate-focused.

Recognizing the relevance of global networks, AFD has been part of a vast movement among public development banks that are glued together by climate change and SDG financing. International Development Finance Club (IDFC), which also includes SIDBI as a member, has provided more than one trillion dollars in climate financing since COP21 and has committed another 3.1 trillion dollars in COP26. The members have taken many practical steps and commitments including stopping of coal financing along with training staff on climate change and SDG (Sustainable Development Goals) integration. Mr Rioux also highlighted the Finance in Common Summit as the 'gathering of all of us', with World Bank, ADB etc. working alongside a network of 530 public development banks. The volume of

activities by this coalition is around 2.2 trillion dollar per year which is equivalent to 10 percent of the total amount invested in the world every year by all public and private sources combined. The objective of the coalition is bridging the gap between public and private sector, in alignment with national commitments.

Mr Rioux closed his statement by highlighting the crucial role of public banks and international co-operation. Dialogue between various actors would be of paramount importance in opening pathways towards strategic finance with private actors. He also highlighted the role of networks like Glasgow Financial Alliance for Net Zero (GFANZ) in this regard. With the next two G20 summits in Asia, the region is well placed to become the focal point of future dialogue and progress.



Panel 1 Discussion

THE ROLE OF REGULATION IN FINANCIAL SYSTEM

PANELLISTS

Ms. Leena Nandan

Secretary, Ministry of Environment, Forests & Climate Change

Ms. Neha Chauhan

Deputy Director, Department of Financial Service, Ministry of Finance

Mr. Stéphane Cieniewski

Senior Adviser, French Treasury

Mr. Jean Boissinot

Secretary, Network for Greening the Financial System (NGFS)

MODERATOR

Mr. Koyel Kumar Mandal

Chief of Programme, Shakti Sustainable Energy Foundation

INTRODUCTION

Financial Institutions (FIs) around the world acknowledge misalignment with the 2015 Paris agreement to be a material financial risk. In line with this, several measures have been undertaken in the past five years. The Financial Stability Board issued recommendations for climate-related disclosure in 2017. NGFS was formed later that year and has spearheaded various initiatives to incorporate climate-related risks in prudential and financial supervisory frameworks.

Recently, in April 2021, the Basel Committee on Banking Supervision published two reports detailing

climate risk-related drivers along with a range of methodologies for climate risk assessment. With these developments, important questions lie before India today - Do we have the required data to form these assessments? Are the current modelling tools adequate? What can we learn from work done by Bank of Netherlands, Bank of France and Bank of England? What can central banks do to mitigate these risks? Within this panel discussion, the role of regulation was examined, in light of these questions and various ongoing initiatives.

ON INDIA'S PLAN FOR TRANSITION

The agenda has been set clearly following India's announcements at COP26. Various measures have been undertaken towards climate integration in the past few years. The Reserve Bank has been incentivising bank lending towards greener industries and projects and in April 2021 it has joined the Central Banks and Supervisors Network for Greening the Financial System

(NGFS). To lessen dependency on fossil fuels, right systems are being put in place, striving towards getting financing through concerted dialogue at every level. Concerted effort and support towards greening MSME (Micro Small & Medium Enterprise) sector, as emphasized by the SIDBI chairman, is also encouraging.

Additionally, there is a need to examine the regulatory ecosystem and incentives in entirety which could impede or advance India's transition. Ministry of Environment Forest & Climate Change (MoEFCC), for example, has been encouraging other efforts like ethanol - blending i.e. blending fuel with grain and molasses-based ethanol to reduce overall emissions. MoEFCC has also taken the lead in simplifying the process concerning the environmental clearances for setting up green energy plants. There is a need to encourage and

develop innovative climate-friendly industries. The next steps would be

ON INDIA ATTRACTING PRIVATE INVESTMENT AT SCALE, ESPECIALLY FROM INTERNATIONAL INVESTORS IN ORDER TO ACHIEVE 2070 NET-ZERO (~ TO THE TUNE OF 6 TRILLION).

The current challenge lies in providing the right incentives to FIs and other institutions in order to attract financial resources at scale. This can be achieved through climate change integration within the market – for example, through acknowledging the implicit carbon price associated with carbon-intensive activities. Green bonds are another avenue, where India forms the second largest emerging market. That

being said, it is important to channel resources keeping social development in mind. As reiterated in COP26, developed nations must contribute to the country's financing needs. Going forward, the adaptation financing needs are bound to increase. We need support from developed countries and at a much higher scale than that is happening at present.

ON THE ROLE AND WORK OF NGFS TILL DATE – IS NGFS SATISFIED WITH THE PROGRESS?

The NGFS was started four years ago by eight central banks, recognizing that progress would be faster on collaboration. Since then, the network has helped mainstream climate change integration through two key aspects. The first was through network expansion in itself. Currently, the NGFS has wide, global reach through 108 members - collectively they supervise all of the G6 along with two-third of the global systemic insurance companies. Majority of the main jurisdictions have joined the network, adding diversity of member input. Second, the network has looked to develop an understanding on how climate change will affect the financial systems, the price stability mandate and financial stability mandate, across all themes of central banks (monetary policy, macro-prudential policy, micro-prudential supervision, along with management of the non-financial part of the balance sheets of central banks). As better understanding was established, the network sought to develop tools/frameworks that members need for climate change integration. Recently, NGFS has released two progress reports detailing best practices with respect to supervision of climate change integration in bank and insurance related activity, which positively indicates climate becoming almost mainstream across the network. NGFS also came out with scenario analysis exercise, after building macro-financial climate scenarios. While these are complex, they will iteratively be improved and revised. Two-third of the members have taken actual climate commitments with regard to supervision, preserving stability, monetary policy and have incorporated practical steps like training and capacity building. In its role as an enabler, NGFS recognizes that while there is a lot more to be done, the ongoing momentum is impressive.



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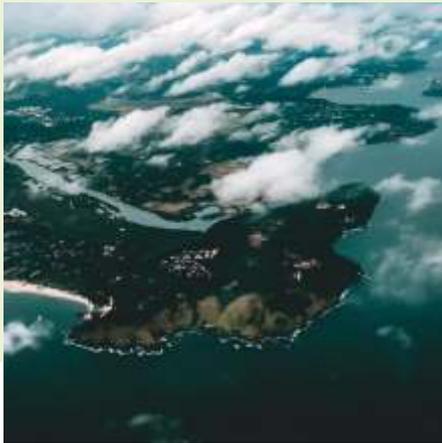
ON THE SUPERVISORY/REGULATORY MEASURES UNDERTAKEN BY FRANCE TO INTEGRATE CLIMATE CHANGE.

The French Ministry of Finance focused on a three-pronged strategy rooted in transparency, access to reliable data and peer pressure. Greening the financial system and mainstreaming climate change is grounded in government endeavor. To do that, the supervisory bodies aimed to provide private sector with a clear vision and detailed guidelines to achieve net zero by 2050. The commitment at EU and national level was broken down into indicative 5-year carbon budget, which was discussed at member level. At macro level, a combination of policy levers was used like CO₂ emission standard, energy efficiency standard and mechanisms like direct subsidies, cap-and-trade mechanism and carbon pricing which was first implemented at European Union (EU) level in energy sector (accounting for 40% of emissions).

The first pillar, transparency around investment decision, was targeted by making FIs accountable for climate change integration in portfolio allocation. In 2015, EU passed a directive for institutional investors to include Environment Social and Governance (ESG) factors in investment decision

making and risk management processes, along with disclosure required from FIs on how their strategy contributes to the Paris agreement. This formed the basis of the Sustainable Finance Disclosure Regulation (SFDR). This was taken one step further last year with climate law which broadened the scope for reporting entities to include exposure to biodiversity risks and portfolio exposure to fossil fuels. The second pillar, equipping FIs with tools to incorporate factors that will contribute to Paris agreement, shows impact at company level using reporting guidelines. Finally, dialogue was initiated between trade federations and Ministry of Finance - together they agreed on voluntary commitment to phase out fossil fuel investments (coal and coal-related divestment) in OECD (Organisation for Economic Co-operation and Development) countries by 2030 and rest of the world by 2040. One year later the implementation was assessed wherein the Ministry of Finance asked for detailed methodologies and commitment to non fossil-fuel investments. For continued improvement, government must be a key partner in greening the ecosystem.

ON INDIA BEING VULNERABLE WITH LONG COASTLINE, AGRICULTURE-DEPENDENT ECONOMY AND FREQUENT FLOOD OCCURRENCE LEADING TO HIGH ADAPTATION COSTS AND PHYSICAL RISKS AND THE REQUIRED MODELLING CAPACITIES.



It is imperative to come out with guidelines for industry on physical risks of climate change. Investments in enterprises that are located in vulnerable states will be at risk. Certain amount of handholding these organisations would be required to combat this risk. Conferences such as these can help us define roadmaps on what we will do on the ground. For India to anticipate these problems, proper mapping of enterprises vulnerable to physical risks and design of response mechanisms using a drilled down approach, must be done. Risk mitigation has to be factored in within business modelling. These conferences and

discussions can help us come up with an actionable plan on kind of methodologies that can be adopted, what kind of structures, institutions (institutional support systems) and mechanisms can help to know, assess, analyse and guide the disaster management plan. This must be complemented with technology-transfer and financing. Institutional structures can be initially funded and set up using this holistic approach; and they in turn can reach out to other organisations (domestic and international).

ON REGULATORY STEPS BEING TAKEN BY NGFS, BASEL COMMITTEE ON BANKING SUPERVISION (BCBS) ON IMPLEMENTATION AND CLIMATE CHANGE INTEGRATION *for eg. WOULD THERE BE CHANGES REQUIRED IN THE BASEL FRAMEWORK?*

There is a slight misconception that work is being done on only understanding climate change

implications and not integrating them. There will be regulatory action on the back of a stress test, for example. By running these exercises, NGFS is raising the attention of these institutions to the kind of challenges they can face and they need to address. If supervisors don't see progress, relevant policy levers would be used. Policy actions will be taken to make sure laggards keep up with the standards for management and measurement of these risks in the market. Going forward, it will be assessed if

additional capital must be kept aside to address climate risk (or a specific proportion of the capital must be kept aside for climate risk). However, there may not be a need to change the existing framework. Existing policy levers like specific buffers or readjusting the calculation of capital requirements can be used. It is a progressive journey. Most likely, this will be addressed through a policy package (rather than a one-size-fits-all approach), taking into account what is happening in rest of economy.

ON INDIA'S PLANS FOR OPERATIONALIZING THE COMMITMENTS.



From supervisory perspective, the thematic focus areas include capital allocation to carbon mitigating sectors, proper market functioning through disclosure/reporting and better assessment of climate risk. RBI has set up a sustainable finance group within the organization, which will be spearheading this. There is increased emphasis on building in-house capacities to assess these risks along with steps being undertaken towards coordination with other financial regulators to further understand transition and

physical risks. Efforts are being taken for advising regulated entities on developing a strategy along with proper governance mechanisms to address micro-prudential risks. RBI has also put in place an action plan. In recent years, they have incentivized lending to green projects and entities. In 2012, RBI included loans sanctioned by banks directly to individuals for setting up off-grid solar and other off-grid renewable energy solutions for households under PSL and in 2015, the PSL criteria was expanded to bank loans up to a limit of 15 crore

to borrowers for purposes like solar based power generators, biomass based power generators, wind mills, micro-hydel plants and for non-conventional energy based public utilities viz. street lighting systems, and remote village electrification. In 2020, the above limit for bank loans was doubled to 30 crore. These actions provide the right kind of policy signals. The government is also coordinating and engaging with other stakeholders so that sector specific needs are met and further capacity building is done on ground level.

WHAT CAN WE LEARN FROM THE FRENCH EXPERIENCE, BASED ON THE FOCUS AREAS HIGHLIGHTED FOR INDIA?



Supervisors must lead by example - effectiveness relies on peer pressure and consistency. In France, the greening of finance started with the greening of international financing instruments – specifically greening of Overseas Direct Investments (ODIs). This was then followed by greening of export financing instruments. Post the voluntary dialogue with trade federations, the French government committed to

phasing out coal export financing. The first sovereign green bond was issued in 2017, which kickstarted the green bond market in France. It set in motion mainstreaming of greening in policy instruments, laws along with promoting secondary issuances - currently outstanding at 40 billion euros. Two years ago, a green budget was released. The green budget included a more systemic and more encompassing approach, which also aligned public spending with climate priorities. Draft budget for 2022 is currently being worked on and is still an experimental project. Climate can be mainstreamed across ex-post evaluation (climate assessment) of draft laws. It is advisable to join peer groups, where best practices can be exchanged in conjunction with dialogue - These include IDFC, Finance in common network, NGFS, coalition of finance ministers for climate action, for example.

ON THE MONETARY POLICIES BEST SUITED TO MOBILIZE RESOURCES.

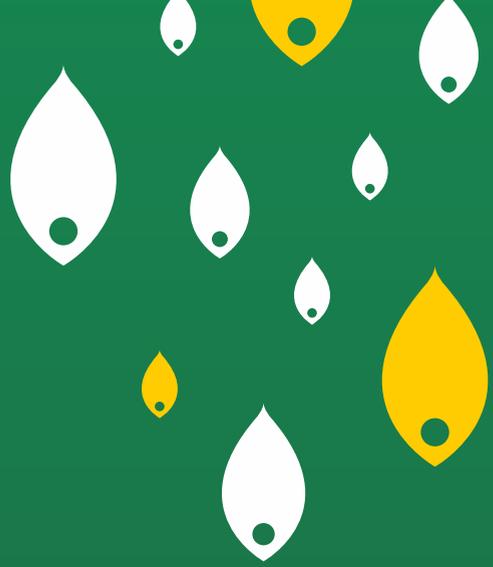
Not all economies face the same problems. They have different

financial systems and the solutions for them will be different in each case. That being said, two main discussions are important. One, to ensure that the balance sheet of central banks is climate-change proof - this is a common objective for all members of NGFS. It is also important to understand the macroeconomics of net zero transition and climate change. Earlier this was seen as a second order discussion, but it is likely to come to forefront sooner than imagined (2025-2030). In turn, this will affect monetary policy, such that the system has enough liquidity and the right conditions to go through the transition in a smooth manner. The actual policy depends on jurisdiction, context, mandate and the unique problems faced by the country. Overall, on development level, it involves not only huge amount of investment but more specifically, it concerns capital reallocation. The net cost must be accommodated from a macro perspective. The bigger the net cost, and the more fragmented and isolated the financial system is, the more kind of specific schemes / policy levers must be added like refinancing, green lending, direct incentives etc. The solutions should be tailored to each economy.

ON INDIA'S PLANS FOR CARBON PRICING AND IF THERE ARE PLANS TO CONVERT EXISTING MECHANISMS LIKE PERFORM ACHIEVE AND TRADE (PAT) AND RENEWABLE ENERGY CERTIFICATES (REC) INTO CARBON PRICING.

This is already being done. There are also taxes being imposed on petrol and diesel along with cutting down of subsidies. India is also participating alongside United Nations Framework Convention on Climate Change (UNFCCC) on designing a mechanism to come out with an institutional approach to

carbon pricing. There is a lot of scope in several industries for reduction in net emissions along with promotion of afforestation, green industries, which gives a good platform to come out with some mechanisms for actionable carbon pricing.



Panel 2 Discussion

ENHANCING THE RESILIENCE OF INDIAN FINANCIAL SECTOR

PANELLISTS

Mr. Saurav Sinha

Executive Director, Reserve Bank of India (RBI)

Mr. Sanjiv Chadha

Managing Director & Chief Executive Officer, Bank of Baroda

Dr. Rajiv B Lall

Ex-Chairman, IDFC First Bank & Professorial Research Fellow at Singapore Management University

Mr. Patrick de Cambourg

President, Project Task Force, European Financial Reporting Advisory Group

MODERATOR

Mr. Adama Mariko

Secretary General, Finance in Common Summit (FICS)

INTRODUCTION

Countries around the world are ramping up efforts to adapt and mitigate emerging climate risks. Building future-ready financial markets holds immense importance, which requires managing exposure towards climate risks within the financial system. This can be done via policy instruments such as establishing national guidelines for climate risk integration, stress testing approaches (focusing on physical climate resilience) along with building

awareness and capacity to address Climate and ESG aspects.

- In face of increasing climate risk - both physical and transition risk - what can financial sector regulators and policy makers do to ensure financial system stability?
- How can banks and financial institutions anticipate and integrate better climate risks in their processes?

THE PRIORITIES AND NEXT STEPS REGARDING THE INTEGRATION OF CLIMATE-RELATED RISKS IN INDIAN FINANCIAL SYSTEM.



Due to the unique and distinctive characteristics of climate change, the climate risks must be looked differently from the conventional financial risks. The uncertainty around climate risks is high and unevenly distributed across countries. Hence, historical data and backward-integrated risk assessment methods are often unable to capture the future impact of climate risk. Given that the climate risks impact financial stability, the central bank has envisaged certain measures. The RBI has set up a

Sustainable Finance Group which leads its efforts on climate risk and sustainable finance including coordination with other national and international agencies. The RBI has started a survey to evaluate the current level of understanding of national banks, the systems and processes instituted by these banks to minimize the impact of climate risk on their portfolio. The feedback from this survey will help RBI develop necessary regulatory policies. RBI is also developing a consultative discussion paper which covers governance, strategy, risk management and disclosure aspects related to climate risk. The consultative paper will sensitize the regulated entities to include climate and environmental risk in their business strategies, governance, and risk management frameworks. Based on the outcome of the consultative discussion paper and the work done by various standard setting bodies, the RBI will come up with appropriate guidelines in this regard.

To define what is 'green' and reduce the risk of greenwashing there is a need to come out with a taxonomy. In January 2021, a Task Force on Sustainable Finance has been set up by the Department of Economic Affairs, Ministry of Finance,

Government of India. The Terms of Reference of the Task Force include defining the framework for sustainable finance in India, establishing the pillars for a sustainable finance roadmap, suggesting draft taxonomy of sustainable activities and a framework of risk assessment by the financial sector. Once a taxonomy is developed there will be clarity for all stakeholders. RBI will going forward consider advising its regulated entities to come out with disclosures based on the Task Force on Climate Related Financial Disclosures (TCFD) framework. Some Indian banks have already started making voluntary disclosures following the TCFD guidelines which will help bring uniformity in comparing their performance with global counterparts. Along with this, capacity building within the bank and the regulated entities remains a priority. To summarize, RBI will continue to augment its in-house capacity on climate risk, create awareness on climate risk within the regulated entities, integrate climate related risks into financial stability monitoring and explore forward looking tools like climate scenario analysis and stress testing for assessing climate-related risks.

HOW DO YOU PERCEIVE THIS NEW DYNAMIC ON GREENING THE FINANCIAL SYSTEM, SET BY RBI AND THE INDIAN GOVERNMENT?



It is important for Indian banks to be aware of and adhere to the guidelines developed by the Reserve Bank of India. There are four to five ways through which climate risks impacts Indian banking system directly. Mitigating the impact of climate change is important for the bank. While we adopt mitigation levers, the climate change will continue to impact our customers, and the impact is disproportionately high on the customers from the poorer section of the society. The financial tool agenda is a powerful tool for the bank to mitigate this impact. For example, the Bank of Baroda has disproportionately

high number of customers belonging to the poorer section of the society. These customers will be seriously impacted by climate change. Deepening of interaction with these customers and ensuring financial resilience and survival of this customer base is one of the critical areas of work for the bank.

As asset managers, the bankers should plan their portfolios in a way that mitigates exposure of climate change on the customers directly and the portfolio indirectly. While designing portfolio, in terms of weightage, the climate risk is already factored in. For example, the bank has introduced caps on the exposure it can take on non - renewable energy related investments. The bank is consciously taking measures to make its portfolios more resilient and less vulnerable to climate risks. The bank also advises its customers, mainly from the MSME sector on the material and financial risk of climate change.

A lot of actions are taken by corporate customers; however, the vulnerable middle requires more attention. And there we must make sure that the climate commitment

needs to percolate from the boardroom to senior management and finally to the relationship managers. The Relationship managers must be fully conscious about climate risks and must evolve as trusted advisors to the clients.

Climate finance is also a huge opportunity to banks as commercial entity. Some estimates indicates that climate finance opportunity in India in next three to four years can be around 200 billion dollars. Construction,

building, waste management and drinking water are areas which will draw climate finance in days to come. The Bank must create internal capacity so that it can become an active player in these commercially viable emerging areas. The bank is actively engaging in multiple aspects to make sure that India's financial sector is resilient, and the bank is also proactive in terms of managing its own exposure to climate risk.



HOW COULD WE BETTER ADVOCATE THE CONCEPT - GREENING THE FINANCIAL SYSTEM?



There are two powerful potential advocates of greening the financial system. The obvious advocate for change is the regulator and the role of the regulator for changing behaviour and changing direction of travel for the financial sector is crucial. In Indian context, the work on this area is well in progress. The second advocate is the market itself. Globally and in India the investors and the consumers are shaping the direction the companies follow. With more investors appreciating the financial risk of exposure to climate change, the companies who

are slow in taking climate actions will soon have difficulty in accessing capital. Similarly, the corporates who fails to take climate action will find consumers abandoning them. These two advocates are gaining momentum globally as well as in India.

The first powerful actor, the Regulators can play a critical role in designing priority sector lending schemes with market friendly signaling. Pricing and capital requirements can be indirect signaling to help channel long-term and sustainable capital flow into newer green opportunities. There is a tendency among regulators globally to focus first on financial stability in the face of rising risk of climate change. The risk the financial system faces from climate change is itself endogenous. The risk we will face tomorrow is endogenous to how

much we invest today in mitigating and adapting to climate change. Hence, we must start taking proactive actions to eliminate the root causes of a climate risk instead of taking reactive measures after the risk arises. In the long-term we must actively channel more capital into green sectors, into innovation and for climate adaptation so that the real sector is better equipped to address the challenges of climate change. Along with the debt market, we also need to sensitize the regulators of capital markets. This will help sync these two markets on issues related to climate change. The capital market regulators should ensure detailed climate risk disclosure by listed entities so that the investors can take a better-informed decision on how to allocate the capital and facilitate the process of green transition.

WHAT ROLE THE EUROPEAN FINANCIAL REPORTING ADVISORY GROUP (EFRAG) PLAYS IN THE GREENING OF THE EUROPEAN FINANCIAL SYSTEM, AND IN THE ANTICIPATION OF CLIMATE-RELATED RISKS?

In European Union (EU), the sustainable finance has been integrated within the broader contours of sustainability reporting. There are several on-going programs

on sustainable finance in EU like taxonomy and regulation on sustainability-related disclosure in the financial services sector. To fully realize the potential, the



commission had to create a sustainability reporting environment to ensure the flow of information from business to the financial system (institutions). To enable this a Corporate Sustainability Reporting Directive (CSRD) has been tabled in April 2021. The CSRD is expected to be approved by the end of the first semester of 2022 (under French Presidency). Once, approved, CSRD will establish a robust system of corporate reporting on sustainability and will apply to all large undertakings (under EU definitions). For example, CSRD will be applicable to undertakings with more than 250 employees. This translates into around 50,000 reporting entities within EU who will be required to report on sustainability matters including climate under a standardized system. This will be also included in the company's management report (within a specific section) and will be subjected to an audit. The audit

requirement will start with a limited assurance and soon moving to a

AS A BANK, HOW DO YOU ASSESS THE RISK OF TRANSITION REGARDING CLIMATE FINANCE IN PORTFOLIO IN ORDER TO STRENGTHEN ITS SUSTAINABILITY?

The transition is inevitable, and we have started late. If we wait any further, then the time window available for transition will be shorter. To well manage the transition risk, we

must look at global development/ best practices and make appropriate plans to ensure that the time window available to banking institutions and its clients for transition is long enough.

A portfolio level analysis is required to identify the assets with higher risk. We must track development in these high-risk portfolios, put an investment cap if required and ensure an orderly transition.

The experience from last couple of years have proved that there is no

conflict between sustainability and commercial viability. For example, in energy sector the solar energy has become more viable over the years in comparison to non-renewable energy. Similar trends are emerging from the transport sector where electric mobility is progressively becoming viable and responsible. It is critical for banks to understand these trends and support these trends to prepare for future in a proactive manner. These are some ways through which the transition risk can be managed.

WHAT ARE THE EXPECTATIONS FROM INTERNATIONAL COOPERATION, ESPECIALLY FROM THE NGFS?



RBI is represented on the G20 Sustainable Finance Working Group, FSB's Working Group on Climate Risk and Work Stream on Climate-related disclosures, International Platform on Sustainable Finance and a Task Force on Climate-related Financial Risks set

up by the BCBS. Climate risk and sustainable finance being an evolving area, there is a need for international cooperation to share our experience and to learn from the experience of our peers.

RBI joined the NGFS in April 2021 and has begun participating in the workstreams of the NGFS. It would be making use of the NGFS platform to equip its officers with the necessary skills and knowledge on climate-related risks.

The workstream on bridging data

gaps is developed around three topics: identifying list of data items needed for the purpose of other NGFS workstreams, determining the availability, sources, and limitation for accessing relevant data and producing a public list of missing data items and calling for external stakeholders to bridge it.

The workstream on scaling green finance is structured around four main topics: promoting the adoption of sustainable and responsible principles in central bank's investment approaches, understanding, and fostering the market transparencies of green finance, providing a joint central bank view on the various challenges that climate change raises on the conduct of monetary policies and encouraging the adoption of climate related financial disclosures by central banks. This would help RBI understand how and at what stage other central banks are in term of their operations.

The Macroprudential workstream is currently developing the scenarios in a theoretical model to generate the effect of climate change on real sectors and the subsequent effects on the financial sector. The pathways through which these effects will manifest would also be charted based on these scenarios. Since the

scenario database of NGFS contains, scenario data for India as well, RBI

HOW CAN INTERNATIONAL COOPERATION HELP MAKE INDIAN FINANCIAL SYSTEM MORE RESILIENT?

The absorption and transfer of knowledge is vital. For example, the international models work on global frameworks and provide perspectives that are generic in nature for assessing impact at national or sub-national level. Whereas the physical risk associated to climate change varies dramatically across geographies. Hence, major work is needed for developing country specific scenarios and models. India fortunately has a large pool of talented researchers who are working on it. The coordination and collaboration between Indian researchers and international climate modelers in this regard is of vital importance. More importantly, the decision makers should start supporting these research works and use the modeling insights to inform their long-term planning process.

The current strategic and execution level capacity does not commensurate the challenge at hand and there is a serious need for building capacity at all levels starting from banks' board of directors to the working level.

Again, availability and transparency of data is critical. Banks will not be able to estimate the real risk to its portfolio without having access to information related to the financial risk faced by the borrowers due to their business's exposure to climate change. It will be unrealistic for the banks to uncover these data if borrowers do not mandatorily disclose these data. India can learn from the experiences and the best practices adopted by other countries in overcoming these challenges.



HOW COULD EFRAG'S WORK, AND MORE GENERALLY INTERNATIONAL NORMS, HELP TO BUILD PATHWAYS FOR A GREEN INDIAN FINANCIAL SYSTEM?



The framework will be aligned with the requirement under TCFD and International Sustainability Standards Board (ISSB) announced at COP26. However, more work is required in this regard as physical and transitional risks are often difficult to approach in a comparable manner.

An important step forward for India would be to develop a comparable climate disclosure standard. In this regard, the regulators are encouraged to review the working paper on CSRD released by EFRAG while they develop their own standards. The working paper tries to consolidate the global best practices and framework into something that can create a level playing field in terms of the information disclosed by the reporting entities. EFRAG has undertaken a double materiality approach (impact materiality and financial / risks and opportunities materiality) for conducting materiality assessment. In this respect, it is critical that the reporting entities disclose - scope 1, scope 2 and scope 3 emissions and provide necessary disclosures on their (low carbon) transitional plans.

THE COP26 DRAWN AMBITIOUS LINES FOR INDIA, AND THE G20 PRESIDENCY IS AHEAD. HOW DO YOU SEE THE ROLE OF THE FINANCIAL SYSTEM REGARDING THESE GOALS?

The regulators acknowledges that India has made ambitious commitment at the COP26 Summit, and India will assume Presidency of the G20 on December 1, 2022. Without doubt the financial system would have to play a key role with respect to these goals. The role of the central bank will be to develop policies and create an enabling environment based on the aforesaid

goals. Obtaining adequate financing would be key to fulfilling the national commitment at COP26. Bloomberg NEF has estimated a USD 648 billion financing gap across the power sector alone for India to reach its renewable energy targets by 2030. Therefore, it is important to mobilize significant amount of non-resident investments to India. As regards India taking over the G20 Presidency by December 2022, the Reserve Bank is internally brainstorming and identifying issues related to the finance track that can be taken up during India's Presidency.

As the country pivots towards a green future and sustainable growth, the banks and financial institutions would have to accelerate their focus on greening India's financial system. Therefore, integrating climate risk in their risk management framework and stepping up lending to green businesses would need to become a key aspect of their business strategy. Greening the Indian financial system would necessitate offering a range of products such as green savings

accounts and deposits, green and sustainability linked loans and tapping the opportunity of scaling up of lending for renewable energy projects, electric vehicles and charging infrastructures, rooftop solar, solar pumps and electricity storage from renewable sources, etc. The corporate sector has also started taking several initiatives towards greening their operations. Recently there was news of a large Indian corporate signing an MOU with a Norwegian company for manufacturing Hydrogen electrolyzers in India. This could be a first step towards gradually replacing the steam methane reforming process with green hydrogen in refineries and also could find use in the mobility sector as well. Banks would need to take proactive steps on green finance and engage with their clients to develop a better understanding of their plans for achieving Net Zero emissions and help them transition to a low carbon economy by providing sustainability-focused financing and other solutions.



Panel 3 Discussion

FRAMING CLIMATE FINANCE: FOCUS ON DISCLOSURE REQUIREMENTS AND GREEN TAXONOMY

PANELLISTS

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Whole Time Member, Security and Exchange -Board of India (SEBI)

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Ms. Caroline Wellemans

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Ms. Neha Kumar

India Programme Manager, Climate Bonds Initiative

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Partner and National Leader, Climate Change and Sustainability Services, Ernst & Young

MODERATOR

Dr. Dhruba Purkayastha

India Director, Climate Policy Initiative

HOW FAR DOES BUSINESS RESPONSIBILITY AND SUSTAINABILITY REPORTING (BRSR) SERVE THE PURPOSE OF GREENING FINANCE OR INTERMEDIATING CAPITAL TO GREEN SECTORS THROUGH CAPITAL MARKETS?

The regulation would be mandatory from 2023 for the top 1,000 listed companies (optional in 2021-22). From supervisory or regulatory perspective, some of the challenges faced include ensuring as much disclosure as possible, without any misrepresentation/misleading and investor protection. For any green products, these can be specific or generic (at entity level).

Currently corporate disclosure is being targeted through BRSR which covers about 400-500 data points; based on the nine responsible business principles. It is comprehensive and marks a departure from the Business Responsibility Reporting (BRR) structure. It will (aim to) allude to investors the ESG performance, ESG resilience, risks, perception, and adaptability - covering how business has aligned goals to sustainability objectives. In case of green instruments, however, there is a need to develop specific disclosure - for example, SEBI released the Green Bond Standards which provides guidance on use of proceeds. The details of the project and use of

proceeds must be continually assessed and disclosed. Last October, through a consultation paper on ESG themed products by mutual funds, SEBI has outlined the required disclosure in detail before they are launched. Therefore, (some) instrument-level disclosure guidelines exist, and entity-level disclosure is targeted through BRSR. In addition, a recent consultation paper was released on ESG rating for securities market.

From a supervisory perspective, standard methodologies and a well-linked regulatory ecosystem will be built upon, which will help investors. Green financing is dependent on multiple regulators and their regulatory architectures. For example, to encourage green lending, central bank may nudge the banks into increasing the green component of their private sector lending or there could be a basic minimum quantum of green lending in their portfolio along with development of sustainable finance taxonomy, integration of climate risk into investment decision processing, stress testing and

scenario analysis for climate risks by banks and FIs. This can also be targeted through developing appropriate products. Insurance regulator or pension fund regulators could nudge their regulated entities to invest more into green funds and provide guidance into the methodologies and tools required. At the end of the day, however, as an

investor considers a particular investment, the investee company or issuing entity must be assessed on ESG parameters and risk by ESG rating agencies and their ESG compliance should be present in front of all of us. The BRSR, being comprehensive with a huge climate component, will help provide that.

ON COMPARING TCFD FRAMEWORK (COMMONLY THOUGHT TO BE MORE AMENABLE FOR FIS) AND THE OVERARCHING BRSR FRAMEWORK FOR LISTED ENTITIES.



TCFD has more relevance to banks and FIs, given its specific focus on climate-related risks and disclosure. The four pillars of the framework form a subset of each other. TCFD is more committed to enable informed investment, credit, and insurance underwriting decisions, which enables the stakeholder to understand climate risk nuances better. However, the subject of climate risk is evolving with many continued changes and developments. RBI is yet to come

out with clear guidelines on what the banks and FIs must do to manage climate risk.

The Basel committee has brought out a consultation paper detailing principles of handling climate risks. RBI and other central banks are now in the process of giving feedback, based on which FIs might get an evolving regulatory structure with regard to climate risk. The paper is quite elaborate with various scenarios and risk management techniques, risk management

processes, management of liquidity and other operational aspects along with management of overall credit risk. 5 to 6 principles were denoted for climate financial risk. Many banks, including SBI, have voluntarily adopted its policy on climate risk management process as a start and set-out next steps, structured on the basis of TCFD report. Currently, there is a greater need for banks and FIs to adhere to TCFD. However, the Basel committee consultation paper will lead to more developments.

ON THE EU EXPERIENCE WITH TAXONOMY AND SUSTAINABLE FINANCE FRAMEWORK.

EU taxonomy is the frontline piece for building the EU sustainable finance ecosystem. This is because the regulator needs to provide guidance and direction for travel, provide tools and methodologies etc. Investors are increasingly asking for clarity on what can unambiguously be considered sustainable investment - EU taxonomy works on providing that clarity and is hence central to any sustainable financing framework.

EU taxonomy was designed keeping in mind the objective of becoming

climate-neutral by 2050. The only constraining element is that it includes disclosure requirements. Building a taxonomy takes time and is still in process. Until now, the EU Technical Expert Group on Sustainable Finance has created technical screening criteria for climate change mitigation and adaptation projects and is now developing criteria for the four other categories - water, pollution control, biodiversity and circularity. EU is also now looking at including social criteria in the taxonomy. The

taxonomy, will in any case, be viewed as a living tool as it needs to evolve with time and needs to reflect the developments in real economy, technology, and society. The framework would also be expanded to recognize transition efforts. The commission has proposed to include nuclear and natural gas in the taxonomy – The commission recognizes the role of these technologies in the transition, but it will come with retiring conditions associated with it and keeping in mind the Do No Significant Harm (DNSH) principle. Currently, this proposal is under consultation and is a draft proposal.

With regard to disclosure requirements, FIs have to disclose green asset ratio i.e. proportion of portfolio that is in compliance with the EU taxonomy. EU companies will also have to cover their non-EU activities and how compliant they are to the EU taxonomy. These developments with taxonomy and SDG gap financing should not be dealt with in isolation and must instead be developed together. It is encouraging to see the efforts of other countries on developing their taxonomy. However, to mobilize international investors and cross border sustainable capital flows, it is essential to coordinate our efforts



and have a coherent sustainable finance framework across the globe through the international community (G20 sustainable finance working group, international platform on sustainable finance).

The objective is not to have a single framework, as each country has its specificities but to provide a coherent framework and clarity around the differences so as to reduce the cost of transaction for cross-border flows. International Platform for Sustainable Finance (IPSF) has started this work based on the comparison between China and EU taxonomy, underlining the commonalities and differences. EU is promoting this by sharing technical expertise with other countries developing their framework. The same can also be said for the green bond standards, which have been key to mobilizing private investment.

GIVEN THAT INDIA DOES NOT HAVE A TAXONOMY YET, HOW DOES ONE SHIFT CAPITAL FLOWS TO GREEN ACTIVITIES, MEASURE IT AND HOW DOES IT LINK TO DISCLOSURE?



What we do within this decade will set the direction of travel. Current green investment flows are paltry in comparison of India needs. Green bonds have been able to make the initial foray, but this is still extremely low. India is batting much below its potential, with greater opportunities in place. Total issuances amount to only 20 billion dollars from 2015 onwards, 40% of which happened in 2021. The pandemic did bring ESG to the center.

Various technical groups are currently working with the department of economic affairs. We

can now expect a coordinated and concerted effort, anchored by Ministry of Finance and regulatory authorities. An important question is - How do we Indianize the work that has already happened? Do we adopt or adapt? The consensus was not to reinvent the wheel; the purpose was to draw offshore capital and to track it; which in itself forms an incentive basis.

The Indian taxonomy is currently in development, with general consensus to include science-based thresholds. Now that India has a 2070 NetZero goal, there will be exercises to determine what the transition pathway means. This further outlines the importance of quantitative thresholds in energy and other sectors. Concepts from the EU taxonomy have been taken and broken down to understand what it would mean in India. Binary thresholds will have to be defined with the help of sector transition pathways. The ESG and BRSR framework in India already follow an integrated approach. This will also be included in the taxonomy where there will be a green pillar, a social pillar and a green and social pillar.

There is a separate disclosure and verification aspect which comes from a third source.

With regard to disclosure, we must ask ourselves if the BRSR is complete in itself or can this be supplemented? The taxonomy would link to disclosure of CAPEX and OPEX alignment with the taxonomy, which adds a layer of complexity. This may not be integrated in the current BRSR framework, so we need to see what can be integrated or supplemented. There is also a lot of work that needs to be done in awareness building,

handholding, monitoring disclosures and how this can connect to a common finance international framework. We also face a data challenge in the beginning (due to low data availability), but that cannot be the reason to not go ahead. We can start small, start voluntarily - leaders have started voluntarily with TCFD/BRSR reporting and this will also be the endeavor with India's sustainable taxonomy. The idea would be to form a cohort of leaders and then make it mainstream.

ON THE PERCEPTION THAT ESG RATINGS LEAD TO GREENWASHING AS THERE IS NO PRIMACY OF CLIMATE OR ENVIRONMENTAL FACTORS. COULD THIS MASK THE ENVIRONMENTAL PERFORMANCE?



When the market is looking at ESG ratings, it tends to be based on the non-financial disclosures. The same providers have historically only looked at financial disclosure. Now, both financial and non-financial disclosure are being considered. For an investor, there is now an increased pool of information, which is a welcome thing. The problem arises because most of

these rating agencies work on a subscription model and therefore, each of them have their own model of evaluation based on their clientele. Weightages are different, what is considered public information is different, different technologies and scraping techniques are used to assess entities while some rely on information submitted by the entity.

Non-financial disclosure started from GRI standards in India, and it started a race over who will get A+ rating. Similar trends can be seen with ESG ratings. It is often difficult to ascertain why the differences in ratings occur and how to improve it. In this, what SEBI has done (with the

consultation paper) is commendable. However, while putting together the ESG framework, it should be careful to not be too prescriptive. This is relevant as the end-objective is to increase available funding. This objective can be hindered when, for instance, say rating given by a rating agency can be used to determine the coupon/interest rate. This is happening in the market right now.

While the rating agencies serve a purpose, there is a need of a coherent framework. It could also be highly sector-dependent and perhaps a sector-based approach as used by a few other countries may be relevant. There might be a combination of approaches that would work best for India and this would also evolve over time. Businesses, FIs and industry should support SEBI by providing comments and engaging in dialogue. Banks are also expecting their investments to flow into what would aid the net zero goal - in this process, if there could be concessional rates for investments into new technology, new energy domain, with improved net value, then that could also catalyze investment. All of this would be enabled if we have a good framework as a base.



ON THE NEED FOR GREEN RATINGS, TARGETING GREEN PRIMACY WITH QUALIFYING SOCIAL AND GOVERNANCE FACTORS

Indian ESG framework must follow an integrated approach as social factors are critical for the country's development. Social inclusion, gender, equity etc. remains primary to our developmental aspiration. Therefore, Indian approach has always been climate plus. By adopting an integrated approach, the investment characteristics of a company will get enhanced in the long run. The taxonomy and thresholds are also important for this framework. However, this will be long drawn process as the country adopt and adapt to these realities.

To lessen the burden of reporting compliance, there is an interoperability feature within BRSR as well. Having said that, there is a separate green bond regulation which aided green investments. The SEBI's consultation paper proposes creation of a pool of ESG ratings providers. After fulfilling the mandated selection criteria, the ESG ratings providers can also be engaged to rate other green schemes like green bonds. Such ratings can be envisioned for new green products launched in the market.

SYNTHESIS

There is now an overwhelming acknowledgement of the inevitability of climate change and how it impacts the financial sector and society. Through the conference, we saw this acknowledgement by policy makers, financial sector regulators, banks and capital markets alike. The policymakers, MoEFCC, MOF stressed upon India's enhanced climate ambition and elaborated on India's initiatives towards scaling up climate mitigation – through renewable energy, electric vehicles, transition trajectories- along with its investment in climate change adaptation efforts. The Financial sector players including the RBI, SEBI, NGFS, French Treasury and banks clearly alluded to climate risk present within the financial system. Ecosystem players are now understanding that climate change

related risks are endogenous and are embedded in the financial system. As physical risks become more prevalent, the concurrent risk of sudden transition also increases. Therefore, both, transition and physical risks must be managed concomitantly through strategic plans and holistic roadmaps.

As elaborated by the MoF, there is a need to shift market intermediation, capital allocation towards green activities. This requires design of market incentives, supporting regulations (for e.g. PSL), (interest) subventions and a mix of other relevant policy tools. The conference also delved into how climate risks affect individual financial institutions along with how it aggregates together on a macro-prudential level.



There is currently a lack of data, capacity, limited expertise, and frameworks that act as barriers towards greening of the Indian financial system and must be addressed in the coming year(s). Global networks like NGFS have been instrumental in bringing the globe together (through central banks), leading to increased awareness, development of tools and facilitation of peer learning. Such networks can be leveraged for knowledge transfer and capacity building.

The panels also highlighted that the existing regulation frameworks like Basel framework etc. do not necessarily need to change. The same pillars can be used for managing climate risks - for e.g., a layer of capital (requirement) could be

dedicated towards green activities. The discussions also brought green budgeting and green monetary policy to the fore - Can there be a greening of monetary policy such that the policy goes beyond conventional roles like inflation management and financial stability? Finally, the panels examined disclosure from the lens of ESG and 'green' along with the adoption of a sustainable taxonomy. Regulatory bodies and financial institutions acknowledged the need for carbon to be priced, owing to the negative externality generated. Regulators are currently in the process of developing guidelines for effective management of climate-related risks, ESG ratings and the the implications of these risks for the wider financial ecosystem.

CONCLUDING REMARKS

H.E. Mr. Emmanuel Lenain,
Ambassador of France in India

H.E. Mr. Emmanuel Lenain began by congratulating the GIFS initiative in its efforts to bring together a high level of expertise and specialists for these discussions. He highlighted that the conference marks the beginning of a process to continue such exchanges throughout 2022 between Indian and French experts. These discussions will inspire what our governments do this year, as France takes on the presidency for EU and India gears up to take presidency of G20. The

commitments made by India at COP26 - setting new targets for 2030 along with the 2070 Net-Zero pledge - were highly welcomed. India will now translate this announcement into strategy, in which the financial sector will have an important role to play. Through these conferences, there can be exchanges and dialogue on the greening of financial system, global sustainability and climate risk. This would need to be concretized into a long-term strategy.



India has showed renewed commitment through various initiatives in 2021 - first, with RBI joining the NGFS and by showing a commitment to integrating climate-related risks into financial stability monitoring and building awareness about climate-related risks among regulated financial institutions and spreading knowledge about issues relating to climate change and methods to deal with them accordingly. He concluded by

showing optimism for succeeding together and by reiterating France's commitment towards implementing a climate-integrated ecosystem, aiding climate finance and greening of the Indian financial ecosystem. He signaled that the French and European authorities would be eager and active in feeding this debate and will aim to build bridges between France, India and Europe.



Green Indian Financial System



An Initiative By