cyril amarchand mangaldas
ahead of the curve

insight

Special Edition | November 3, 2021

India's Climate Ambition: The Role of Financial Institutions

Climate change is the biggest challenge facing humanity. By now it is clear that climate change not only impacts natural environment, but also poses serious risk to life and economy. Such risks have brought to the fore the role of the finance sector, including central banks, public & private sector banks, insurers, and the policy makers in guarding and managing risk to the financial ecosystem.

It's no surprise then that in India's fight to combat climate change and to attain its green goals, the finance sector has emerged as the pacemaker of its transitory phase. The transition to clean energy requires enormous investment and involves both physical and transitional risks. While physical risks are visible through extreme weather events, transitional risk contains compliance cost of transitioning to a carbon neutral economy. To overcome these, it is important that private investments are unlocked, project financing risks are evaluated from the economic and environmental standpoint, a standard reporting and disclosure framework is built and adhered to, and solutions are designed that are socially just and equitable. The stakeholders of finance sector believe that focussing on the long-term systemic shifts while charting out the post-pandemic recovery path can be an effective way to progress towards the UN Sustainable Developments Goals and transition to a green economy.

India's cost of transition from fossil fuel to clean energy

While India has often been made aware of its role in contributing to Green House Gases and has often been asked to commit to a net zero emission deadline, its point of view to facilitate access to green technologies has not really been heeded.

In the context of financing, developed countries had committed (during COP 16) to mobilize USD 100 billion per year by 2020 towards meaningful mitigation actions. To accelerate the pace of transition, developing countries like India count on this climate finance. According to Mark Carney, *UN Special Envoy for Climate Action and Finance also former governor of the Bank of England*, in addition to finance from public bodies, mainstreaming of private finance is also necessary to help companies decarbonize and be competitive in the green economy.

Supply of capital

The Network for Greening the Financial System is a voluntary group of central banks that aims to help members draw policies to make financial sector resilient to climate risks. The RBI has joined the group contribute to climate risk management strategies as well as to mobilise mainstream finance. However, the climate financing architecture is grossly inadequate for developing nations and the WEF projects an investment requirement of USD 5 trillion by 2020 in green infrastructure, which far exceeds USD 100-billion annual commitment.

Separately, a number of overseas funds have large pools of capital that they want to commit to companies embracing climate agenda and ESG principles. Global green bond issuances are expected to surpass USD 1 trillion by 2023.

Even domestic ESG funds are growing in number and green bonds worth USD 16 billion have been raised in 2020. Interestingly, according to RBI, India occupies second position in the cumulative emerging market green bond issuance in 2012-2020.

Measuring climate related risks

Despite posing serious risk to financial stability, climate change is difficult to quantify. The severity and frequency of natural disasters make it difficult to formulate a yardstick by using historical data to pre-empt unseen events. Thus, a large number of initiatives are underway to address financial risk through the formulation of effective reporting standards. Task Force on Climate Related Disclosures or TCFD is one such concept that has come a long way since it was first thought of during the Paris accord in 2015. It is a framework that recommends public companies to effectively disclose the metrics and targets used to assess climate related risks. Most of the financial sector is now demanding to make TCF disclosures mandatory. Additionally, there is a proposal to establish an International Sustainability Standard Board (**ISSB**) to focus on climate related reporting. Recently, market regulator SEBI has introduced Business Responsibility and Sustainability Report (**BRSR**) framework which is an elaborate and good measurement technique. Each of this techniques and metrics also rely on international coordination to promote relevant initiatives and synergies. In the context of India, it is hoped that all the regulators align to develop a common framework that would guide investors, banks, and corporates to measure climate risks residing in their companies or services.

Role of banks in the need to assess climate change risks

Notwithstanding the recent FDI and private capital inflows, much of India's industry and services are funded by financial institutions. Generally, banks release finances to projects that look viable in terms of generating future cash flows and have the necessary environmental clearances. But now that assessment has to go beyond basic environmental checks to include examination of carbon footprint and adoption of standard risk measurement parameters. As discussed above, projects in India still run on fossil fuel

and hence green financing must take into account the need to transition in a sustained manner. In fact, financial institutions are capable of creating an ecosystem on their own by incentivising projects that are climate-aware and disincentivising those that aren't. On the other hand, businesses also have to bear the responsibility of presenting a very granular strategy for the benefit of the project financier. Products coming out of carbon-emitting industries would find few takers in the coming decades, which means such businesses won't make a beeline for very long to procure funding.

Meanwhile, investment opportunities are gaining traction in in India, with investments coming to sectors such as infrastructure, construction, and energy. The RBI's inclusion of small renewable energy projects under the priority sector lending is helping the cause. Increasingly, resources are being made available for Green building, EVs, and rooftop solar projects.

India makes fresh commitments at COP 26

Prime Minister Narendra Modi announced a five-point agenda at the COP26 meet in Glasgow to show India's commitment to undertake climate initiatives. In his address to COP 26, the Prime Minister announced that India would:

i. Raise the non-fossil fuel based energy capacity to 500 GW by 2030;

ii. Cut the total projected carbon emission by one billion tonnes by 2030;

iii. The country would strive to achieve net zero emissions by 2070;

iv. Half of India's energy needs would be met using renewable sources by 2030;

v. The carbon intensity of the economy would be reduced to less than 45% by 2030.

In his speech, the Prime Minister made it clear that India's contribution to mitigate climate change is far greater than its role in emitting greenhouse gases. India has not only inched closer to meeting its ambitious energy target but also raised it. The Prime Minister drove home the point that just as India has raised its climate ambitions to achieve net zero carbon emissions by 2070, the developed world must also commit to smoothening the path through technology transfer and climate finance. Earlier, Indian Environment minister Bhupendra Yadav, who is representing the Indian delegation, has also stated he would press for climate justice and seek access to technology and finance necessary to achieve such a structural transformation.

Conclusion

The 26th edition of the United Nations Conference of Parties (COP 26) at Glasgow is getting the same attention, if not more, as the 2015 Paris Agreement on tackling climate change. The year 2021, recovering from a devastating pandemic, has the potential to move quickly to resolve climate-related challenges.

Developing countries like India, while being partners in achieving climate goals, must ensure they are not disproportionately impacted by climate talks. India is committed to transition to clean energy and is on track to achieve its 450 GW installed capacity of renewable energy target by 2030. But the net zero path is long and arduous. As of now, millions of jobs are dependent on fossil fuel and allied sectors, which is why, any transition plan must be socially just and inclusive. Embarking on an ambitious climate objective involves not only restructuring of economy & industry, but also workforce reskilling, repurposing of land & carbon sequestration, promotion of environment and social responsibilities, etc. Such transition is capital intensive, and therefore, India's assertion that capital be made available to it is both necessary and urgent.

In the run-up to COP 26 meet at Glasgow, distinguished voices from India as well as COP 26 presidency discussed 'Accelerating India's Climate Ambition: A Roundtable for Financial Institutions' in a webinar jointly organised by WWF, the IBA, CDP and Cyril Amarchand Mangaldas. The finance sector representatives engaged with L Viswanathan, Partner (Chair-Finance, Projects and Insolvency) at Cyril Amarchand Mangaldas. The link to the discussion is https://m.youtube.com/watch?v=KWiyttUT6p0&feature=youtu.be

Key Contacts:

L Viswanathan
Partner (Chair – Finance, Projects & Insolvency)
l.viswanathan@cyrilshroff.com

Arjun Goswami
Director (Public Policy)
arjun.goswami@cyrilshroff.com

Sucheta Bhattacharya
Principal Associate
sucheta.bhattacharya@cyrilshroff.com

Cyril Amarchand Mangaldas
Advocates & Solicitors

100 years of legacy | **750+** Lawyers | **Over 150** Partners

Peninsula Chambers, Peninsula Corporate Park, GK Marg, Lower Parel, Mumbai 400 013, India
T +91 22 2496 4455 **F** +91 22 2496 3666 **E** cam.mumbai@cyrilshroff.com **W** www.cyrilshroff.com
Presence in Mumbai | New Delhi | Bengaluru | Ahmedabad | Hyderabad | Chennai | GIFT City | Singapore