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TALKING POINT

Financing green growth in India

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\$200 billion is needed for 100 GW solar and 60 GW wind power installation by 2022

The climate change talks of the 21st Conference of Parties at Paris in December, though seemingly promising, are not legally binding. The meet has only culminated in discussions on financing climate change initiatives, especially for developing nations.

In its Intended Nationally Determined Contribution (INDC) India has proposed to reduce the emissions intensity of its GDP by 33-35 per cent by 2030 (from 2005 levels). To achieve these goals, India has to rely on external funds. The role of Indian banks and development financial institutions (DFIs) as a facilitator of green growth is critical.

There are three ways in which they can contribute to green growth. One, revamp their internal systems and processes to enhance energy and material efficiency by encouraging e-transactions and e-statements and converting their premises to 'green' buildings. Two, they must assess environmental, social and governance (ESG) risks while appraising projects for financing: currently, most banks and DFIs do not factor these in while evaluating project proposals.

Risk assessment

Environmental liabilities of projects are threats to bankers and financiers since lawsuits and heavy fines levied by courts — due to overlooking environmental or pollution control laws, emission benchmarks — eventually lead to reduction of projected cash flows.

Therefore, ESG risk assessment is quintessential to enhancing the asset quality of banks and to reduce the probability of loans getting converted into non-performing assets. Projects not adhering to industry standards in respect of emissions or process benchmarks can be eliminated outright — thereby, indirectly contributing to sustainable development.

According to the Global Sustainable Investment Review 2014, the proportion of sustainable investing (i.e., investing that integrates ESG assessment in asset valuation) relative to total managed assets in Asia is small — at about 0.8 per cent. In contrast, it is over 50 per cent in Europe and Australia, and 17-31 per cent in the US and Canada collectively.

Green financial products

Three, there is a need to introduce green financial products. India needs about \$200 billion to attain a target of 100 GW of solar power and 60 GW of wind power installation by 2022, according to Bloomberg. The government has approached lenders such as Rural Electrification Corporation, Power Finance Corporation, Indian Renewable Energy Development Agency and Yes Bank for low-cost, long-term funds.

To meet green financing need, DFIs and banks are expected to float 'green bonds' both in the domestic and international markets. For example, YES Bank has already raised ₹1,000 crore by floating green infra bonds and Exim Bank has obtained \$500 million through the issue of green dollar bonds. Two important RBI initiatives are noteworthy. One, renewable energy project financing was included under the priority sector lending category in July 2015.

Two, companies are allowed to sell rupee-denominated bonds overseas which, in turn, facilitates the institution to obtain overseas debt without exposure to currency risks.

Meeting global standards

Given the enormous quantum of climate finance requirement, India has to depend on funding from DFIs and international NGOs. This requires that Indian banks and DFIs rise to international standards to pitch in.

The UN supported Principles for Responsible Investment and the Equator Principles are internationally accepted frameworks for identifying and managing environmental and social risks in project finance. Currently, 81 Equator Principles Financial Institutions in 36 countries have adopted the principles, covering 70 per cent of international project finance debt in emerging markets. Only one Indian financial institution — the Infrastructure Development Finance Company — is a signatory to the same. It is high time our banks and DFIs internalise ESG risk management into project appraisal to become competent enough to obtain international funding.

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(This article was published on January 24, 2016)

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