Inquiry: Design of a Sustainable Financial System

FICCI

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Delivering a Sustainable Financial System in India

FINAL REPORT



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EXECUTIVE SUMMARY

Financing India's goals for inclusive and sustainable growth requires the mobilization of additional low-cost, long-term capital. Raising incomes for the 800 million people living on less than US$2 per day, generating livelihoods for the 12 million people entering the workforce every year and generating the natural resource base at a time of climate change require innovative approaches to the challenge of sustainable finance.

This report presents the results of an 18-month process of dialogue and analysis in India to identify key steps to respond to this challenge through building a sustainable financial system. The private sector led this process, working closely with the government of India and key stakeholders, and in partnership with the UNEP at the international level.

The findings of the India Inquiry are based on the understanding of the real economy, growth imperatives, national priorities, financial system architecture and the gradual momentum on sustainable financing. India has a comprehensive approach to reducing the resource and pollution intensity of growth and delivering clean energy and water. India is also taking the lead globally, for example, through the new International Solar Alliance.

Section 2 sets out the strategic needs for sustainable finance across key sectors of India's economy, such as manufacturing, infrastructure, agriculture and small enterprises. Just in terms of basic infrastructure alone, at least US$1 trillion is required every five years, half of which needs to come from the private sector. Key challenges include overcoming the mismatch between long-term assets and short-term credit provision, as well as the imperative of attracting additional flows of foreign public and private capital.

Over the past decade, the pace of Indian innovation in sustainable finance has accelerated involving both a range of voluntary market-led initiatives as well as policy actions. Recent steps profiled in Section 3 include:

- the launch of national voluntary guidelines for responsible financing by the Indian Banks Association
- the decision by the Reserve Bank of India to include social infrastructure and decentralized renewable energy within the Priority Sector Lending requirements for banks
- the issuance by the Securities and Exchange Board of India (SEBI) of requirements for the development of the green bond market
- the approval of the Pradhan Mantri Fasal Bima Yojana initiative to extend crop insurance
- the increase in the coal cess, raising funds for the National Clean Energy Fund (NCEF).

The recommendations of the India Inquiry are based on this positive momentum – and the premise that the participation of the private sector and the availability of adequate finance are two of the framework conditions for India to achieve sustainable development.

The India Inquiry recommendations cover **six thematic areas** focusing specifically on action within the financial system:

1. **Developing a sustainable capital markets strategy:** Building on SEBI's recent market guidelines, credit enhancement, adjustment to risk weightings and fiscal incentives could help further scale up the green bond market. Infrastructure investment trusts – known as yieldcos in the US – also have considerable potential to raise equity capital for illiquid green assets.

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2. **Strengthening keystone financial institutions:** The pivotal role of the Indian Renewable Energy Development Agency (IREDA) could be further developed through building products for take-out, guarantees and loan-life extension. The NCEF's effectiveness could be improved through a well-articulated vision and revisions to operational guidelines.
3. **Aligning financial regulations with sustainability:** Further action can be taken to make additional sustainable finance projects admissible under Priority Sector Lending requirements. In addition, renewable energy could be given its own exposure limit outside of the overall power sector. Finally, the new Indian Financial Code (IFC) presents an opportunity to mainstream sustainability considerations in the regulation of India's financial system.
4. **Building financial sector capacities:** The capacity of the financial sector needs to be further developed in several areas, notably in financial ratings, financial disclosure and 'green credit' decision-making including for agricultural commodities and forestry.
5. **Increasing access to sustainable finance:** Access to sustainable finance is still lacking in many areas, notably for the Small and Medium Enterprises (SME) sector in terms of driving energy saving and adaptation to climate impacts. Further incentives are also required to channel finance into water, sanitation and waste management.
6. **Mobilizing international financial flows**: India has considerable opportunities to leverage the Green Climate Fund as well as the new International Solar Alliance. Finally, 'green credit' from overseas can be increased through changes to external commercial borrowing rules, while foreign institutional investors can be attracted through mechanisms such as the Green Infrastructure Investment Coalition, where India is strongly represented.

Within the contours of these six thematic areas of interventions, policymakers, regulators and financial market participants can embrace the beginning of a new design of the financial system that responds to the needs, challenges and opportunities arising out of India's sustainable growth objectives.

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