Climate Risk Efforts of the Banks

Why in news?

On the heels of its monetary policy statement, the Reserve Bank of India has said that it would would issue a set of guidelines regarding climate finance.

What is the RBI announcement about?

- The Reserve Bank recognises that climate change can translate into climate-related financial risks for Regulated Entities which can have broader financial stability implications.
- The Reserve Bank of India's guidelines would be on three areas of climate finance
  - A broad framework for the acceptance of green deposits
  - A disclosure framework on climate related financial risks
  - A similar framework for climate scenario analysis
- It was based on the feedback received on a Discussion Paper (DP) on Climate Risk and Sustainable Finance.

> *A green deposit is a fixed-term deposit for investors looking to invest their surplus cash reserves in environmentally friendly projects.*
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> *In 2021, HDFC had launched green deposits directed towards financing of green and sustainable housing credit solutions and services.*

Why green or ESG funding has been in the limelight in recent years?

- ESG funds are those funds whose asset allocation mostly includes shares and bonds of companies that are evaluated based on the environmental, social, and governance factors.
- **Climate concerns** - The multilateral funds are not showing up the terrible climate scenario, thereby placing the onus on market solutions such as raising money through equities, bonds and deposits.
- India ranked 104th out of 192 countries in an **index of climate readiness** which measures a country's ability to leverage investments toward adapting to higher temperatures and extreme weather.
- **Non-tariff barrier** - ESG norms in the West could become a non-tariff barrier for Indian exports, creating knock-on effects for banks.
- Hence, banks need to be prepared to bake ESG/climate risk into their appraisals of projects.

What lies ahead for banks?

- **Need of the hour –** Green deposits can power desirable projects by delivering credit at low cost, provided investors are convinced that funds are put to good use.
- The banks need to develop expertise in three areas so that climate debt instruments attract funds even at lower tenures.
  - Climate assessment of regular projects
  - Appraising ESG projects
  - Creating confidence among investors
- **Challenges** – In order to create investor confidence, ESG should shrug off its global tag of being hijacked by the 'greenwashing'.
- Green bonds accounted for 1.7% of the $100 trillion bond market in 2020.
- However, a fifth of the over 600 bonds assessed between January 2021 and September 2022 were not truly green.

> RBI has announced issuance of sovereign green bonds worth Rs 16,000 crore.
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> RBI has decided to designate all Sovereign Green Bonds issued by the Government in the fiscal year 2022-23 as 'specified securities' under the fully accessible route (FAR)
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> Now, they will be opened fully for non-resident investors without any restrictions, apart from being available to domestic investors as well.

References

1. Businessline | Banks' climate risk efforts need to evolve
2. Live mint | No cap for foreign investors in sovereign green bonds
3. RBI | Statement on Developmental and Regulatory Policies