

OPINION: Green bonding for recovery

Green bonds could collectively set a precedent for India's climate-focused diplomacy.

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The 2021 Union Budget announced an institutional framework to instill liquidity into the corporate bond market. In sync with the pro-investor move, the country has an opportunity to scale up the green bond market, presently just under one per cent of the total domestic debt market. Green bonds are debt financing instruments for projects that involve renewable energy and energy efficiency, low-carbon infrastructure, and sustainable resource use (see Figure 1).



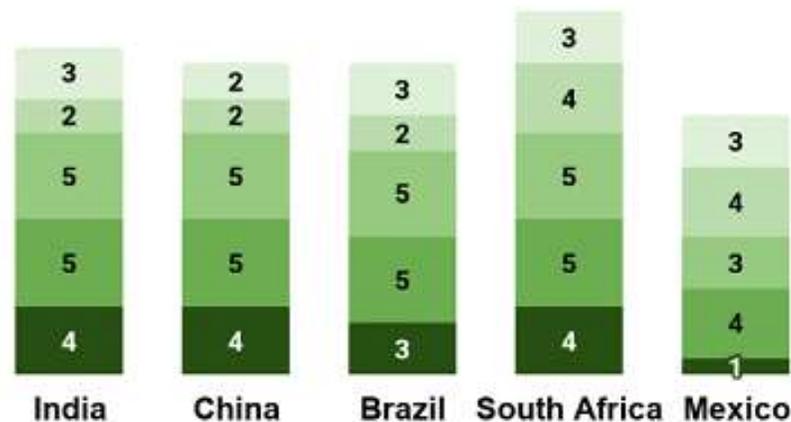
These bonds are growing in popularity as they offer investors the opportunity to tackle climate change while enjoying tax benefits. The European Union's recent decision to roll out around Dollar 240 billion worth of green bonds as a sustainable post-COVID economic measure to meet its clean energy demands is a case in point. It is a follow-up to Germany's first issuance in 2020, which saw sales of \$7.5 billion and pushed the green bond market beyond its initial one trillion dollar target. The EU's move is a testament to a bloc-level consensus towards climate-focussed financing and is expected to revive investor confidence in the near future. As a vital member of the G20, India would do well to follow the lead of the EU and raise its green capital.

The ebb and flow of green bonds in India

India issued its first green bond in 2015 and became the second-largest emerging market in 2019 with a \$10.3 billion worth transaction. This amount roughly equals half of India's green financing expenditure in 2019. However, these bonds have limitations. As per a study by TERI, green bonds that have been issued in India are small-sized (the issue size of bonds is a product of the number of bonds and the face value per bond), indicating selective issuance. The small issue size is courtesy project-centric risks, such as poor financial health of electricity distribution companies, non-adherence to contracts, asset quality risk, and payment failures at various instances. These risks have affected the overall sovereign rating of India's investment-grade bonds, bringing it closer to a low BBB. Foreign investors looking at large-sized bond issues and AA rating (or above) bonds have been reluctant to invest in India's green bond market. Another red flag is the greenwashing linked with projects. Limited regulation (Figure 2 indicates a low regulatory quality score for India) leads to misuse of green bonds for non-green outcomes, creating a reputational risk for projects.

Sustainability Banking Score (out of 5) to assess national sustainable finance policies

Political risk Regulatory quality Private credit
Market capitalisation Green bond issuance



Emerging markets

Moreover, green bonds have a very generic definition, leading to skewed perceptions among investors.

Towards greener pastures

So, how do we address these concerns? Let us look at a three-D approach: dialogue, demand, and direction. An ongoing study explores the feasibility of a multi-actor partnership (MAP) approach towards minimising India's RE financing challenges. The MAP approach brings in relevant stakeholders (governments, investors, industry players, financial institutions, and civil societies) to discuss challenges — such as financial risks in RE — and foster transformative solutions through dialogues. A similar approach could broaden the scope and, eventually, the scale of green bonds by deepening the investor pool beyond the initial government-based issuance. The recent bond issuance by Adani and CLP Wind Farms is undoubtedly an indication of the rekindling of market demand. However, long-term sustenance is possible only through a more well-defined framework (similar to the EU's proposed strategy). This framework could factor in country-specific and sector-specific challenges, offer more precise taxonomy (coupled with compliances and risk stress tests) across the project pipeline, and equip project players with the right skill set and direction. Green bonds could collectively set a precedent for

India's climate-focused diplomacy. With more nations pledging on collective multilateralism to achieve their Sustainable Development Goals, the world could witness more green recoveries in the future.

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