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Published in Sustainability Karma
Nov 28, 2024

Developing a green taxonomy for climate financing in India

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Article Content:

India's green taxonomy should be designed in harmony with international standards, such as the Task Force on Climate-related Financial Disclosures (TCFD) and the International Platform on Sustainable Finance (IPSF).

As the world grapples with the growing impacts of climate change, nations are reassessing their economic models to transition toward more sustainable and green economies. India, being one of the fastest-growing economies, is uniquely positioned to lead this transition.

The Need for a Green Taxonomy in India

A green taxonomy is essentially a classification system that outlines which economic activities are considered sustainable or "green." It serves as a guide for investors, policymakers, and financial institutions, helping them channel funds into activities that contribute to climate mitigation and adaptation. It fosters greater transparency, reducing the risk of greenwashing (i.e., falsely marketing activities as sustainable).

The Importance of Clarity and Standardisation

The central challenge in developing a green taxonomy is creating a balance between clarity and flexibility. The taxonomy must be robust enough to ensure that projects claiming to be green are genuinely sustainable, but it must also be adaptable to India's unique developmental and economic needs.

The EU's taxonomy defines six environmental objectives: climate change mitigation, climate change adaptation, water resources protection, transition to a circular economy, pollution prevention, and biodiversity protection. It also outlines a "do no significant harm" principle, ensuring that activities aligned with one objective do not undermine others.

Adopting a similar principle could be beneficial for India. It is important to note, however, that India's green taxonomy should consider the developmental and socioeconomic challenges

that the country faces. Therefore, it should focus on poverty reduction, access to clean energy, sustainable agriculture, and water security.

For instance, a solar energy project may contribute to climate change mitigation, but if it leads to excessive water use or habitat destruction, it should not be classified as green. Similarly, activities largely dependent on imports of goods (e.g. solar panels, batteries, etc.) should be disincentivized. A new EV manufacturer may be reducing emissions of our country, but unless he generates significant number of jobs, his work may not be considered green.

An appropriate approach is necessary, where green investments are also directed towards gender equity and inclusion, re-skilling workers and providing alternative employment opportunities. It is commendable that the National Adaptation Plan (NAP), worked on by Ministry of Environment, Forest and Climate Change (MoEFCC) clearly addresses gender and inclusion as part of the overall framework.

The Role of Financial Institutions

Currently, financial institutions face challenges in assessing the environmental impact of projects due to a lack of clear guidelines. A green taxonomy would standardise the evaluation process, making it easier to identify and fund sustainable projects. It could also influence lending rates, with green projects potentially receiving lower interest rates or more favourable financing terms compared to projects with a high carbon footprint. As a matter of fact, there are multiple investors as well as donors (both domestic and international) who are looking to fund such green initiatives.

Additionally, the taxonomy would enable financial institutions to develop new green financial products, such as green bonds, green loans, and sustainability-linked loans. This would not only help meet the financing needs of green projects but also tap into the growing demand from investors for sustainable investment options.

India's green taxonomy should be designed in harmony with international standards, such as the Task Force on Climate-related Financial Disclosures (TCFD) and the International Platform on Sustainable Finance (IPSF). This would make it easier for foreign investors to assess and invest in Indian projects, thereby increasing the flow of international climate finance into the country.

Challenges and the Way Forward

While the development of a green taxonomy is an essential step for India, it is not without challenges. The complexity of India's economy, with its high dependence on fossil fuels and large informal sector, makes it difficult to implement a one-size-fits-all framework.

A phased approach could be a solution, where the green taxonomy is initially applied to sectors where sustainable alternatives are more established, such as renewable energy, waste management, and water conservation. Over time, the framework could be expanded to include more complex sectors, such as agriculture and heavy industry.