



FII to Invest in India's Sovereign Green Bonds

For Prelims: [Reserve Bank of India \(RBI\)](#), [Foreign Institutional Investors](#), [Sovereign Green Bonds](#), [Securities and Exchange Board of India](#), [Statutory Liquidity Ratio](#), [Comptroller and Auditor General](#)

For Mains: Sovereign Green Bonds, Status of Green Bonds, Green Finance initiatives.

[Source: TH](#)

Why in News?

The recent decision by the [Reserve Bank of India \(RBI\)](#) to allow [Foreign Institutional Investors \(FIIs\)](#) operating within the [International Financial Services Centre \(IFSC\)](#) to invest in [India's Sovereign Green Bonds \(SGrBs\)](#) marks a significant step towards financing the nation's transition to a **low-carbon economy**.

Note

- FIIs are institutional investors that invest in assets belonging to a different country than where the organizations are based.
- The [Securities and Exchange Board of India \(SEBI\)](#) regulates FII investments in the country, while the RBI maintains the investment ceilings to keep FII participation in check.

What are Sovereign Green Bonds (SGrBs)?

- **About:**
 - In the [Union Budget 2022-23](#), the FM announced the government's decision to issue **SGrBs**, a kind of government debt that specifically funds projects attempting to accelerate **India's transition to a low-carbon economy**.
 - Funds raised through SGrBs are earmarked exclusively for **green projects**, ensuring transparency and accountability in fund utilization.
 - SGrBs typically offer **lower interest rates compared to [Government-Securities \(G-Secs\)](#)**, reflecting their alignment with sustainable development objectives.
 - Issuance of SGrBs requires adherence to internationally recognised green standards and certification processes to ensure the credibility of funded projects.
- **Classification:**
 - SGrBs are classified under the [Statutory Liquidity Ratio \(SLR\)](#), a liquidity rate set by the RBI for financial institutions.
 - Financial institutions must maintain SLR with themselves before lending to customers, affecting the availability of funds for other purposes.
- **Greenium:**
 - As SGBs typically yield lower interest rates compared to conventional G-Secs, the

difference in interest rates between SGrBs and G-Secs is called a greenium.

- Central banks and governments globally encourage embracing greeniums to support the transition to a greener future.

▪ **Sovereign Green Bonds Framework:**

- The Finance Ministry released [India's first SGrB Framework in 2022](#) detailing the kind of projects that would receive funding through this class of bonds.
- **Funding Projects:**
 - Funds will be directed towards **nine green project categories:** [renewable energy](#), energy efficiency, clean transportation, climate adaptation, [sustainable water management](#), pollution control, sustainable land use, [green buildings](#), and biodiversity conservation.
- **Excluded Projects:**
 - Projects involving [fossil fuel](#) extraction, [nuclear power generation](#), and direct waste incineration. Additionally, projects related to alcohol, weapons, [tobacco](#), gaming, or palm oil industries are also excluded.
 - Furthermore, **renewable energy projects using biomass** from protected areas, landfill projects, and [hydropower](#) plants larger than 25 MW are **not eligible**.
- The Indian government sought validation from **Norway-based validator Cicero** to enhance credibility. Cicero rated India's framework as a "**green medium**" with a score of "good governance," showing alignment with global green standards set by the **International Capital Market Association (ICMA)**.

▪ **Features of the SGrB:**

- issued through **Uniform Price Auction** (a public sale where a fixed number of similar items are sold for the same price).
- eligible for [Repurchase Transactions \(Repo\)](#).
- reckoned as eligible investments for SLR purposes.
- **eligible for trading in the secondary market.**

▪ **Management:**

- Sovereign green bond proceeds will be deposited into the [Consolidated Fund of India](#) and managed by the **Ministry of Finance's Public Debt Management Cell**.
- Allocation and utilization of Green Bonds will be audited by the [Comptroller and Auditor General \(CAG\) of India](#).

▪ **Advantages:**

- Indian green bonds not only support sustainability goals but **also strengthen the Indian currency** by attracting investors and increasing funds within the central bank.
- The growing demand for socially responsible investments and the limited supply of **green bonds can raise their price and yield.**

How do FIIs' Investments in Green Bonds Boost India's Green Transition?

- FIIs investing in India's green projects **expands the capital pool** for funding the country's ambitious [2070 net zero goals](#), which aim to derive [50% of India's energy from non-fossil fuel sources](#) and **reduce the nation's carbon intensity by 45%**, as promised at [United Nations Climate Change Conference\(COP 26\) in Glasgow 2021](#).
- FIIs provide an alternative source of funding, lessening the pressure on domestic lenders and freeing up capital for other uses.
- The recent inclusion of foreign investors has **expanded the pool of potential investors for India's SGrBs**, potentially leading to more funds for green projects that aim to reduce the [carbon footprint of the Indian economy](#), and contributing to India's [Sustainable Development Goals](#).
 - The government aims to raise Rs 20,000 crore through SGrBs in FY24 and **plans to borrow Rs 12,000 crore in the first six months of FY25.**
- Foreign investors bring valuable knowledge and experience in **green technologies** and project management, which can benefit Indian green infrastructure projects.

What are the Challenges Regarding India's SGrBs?

▪ **Lack of Green Taxonomy:**

- The absence of a green taxonomy or standardized method to assess an investment's

environmental credentials poses a challenge.

- Without clear criteria, there is a risk of **greenwashing**, where projects falsely claim to be environmentally friendly to secure funding.

▪ **Framework Implementation:**

- While the Finance Ministry released India's first SGrB Framework, its implementation and enforcement remain critical.
- Ensuring that funded projects align with the defined criteria and contribute to environmental sustainability requires robust monitoring and evaluation mechanisms.

▪ **Project Selection and Impact:**

- Identifying **new green projects with credible audit trails** and high impact is crucial for optimal deployment of SGrB proceeds.
 - Projects with limited private capital, such as Distributed Renewable Energy and clean energy transition finance for MSMEs, may face challenges in attracting sufficient funding.

▪ **Availability of Suitable Projects:**

- Securing a pipeline of eligible green projects may be challenging, particularly in sectors like offshore wind, grid-scale **solar power production**, and **Electric Vehicles (EVs)**.
 - The government needs to actively **encourage and incentivize** the development of such projects to ensure a steady flow of investment opportunities.

Way Forward

- Augment **transparency in green bond** issuance and viability to overcome existing challenges.
 - Implement specialized awareness programs to promote the advantages of investing in green projects.
- **Reduce legal, default, liquidity, and other risks** by establishing a favorable environment for private investors.
 - Implement robust legal frameworks regarding defaulters to instill investor confidence.
- Prioritize the establishment of a **green capital pool** to stimulate domestic demand.
- Integrate green projects into institutional investors' portfolios, potentially involving Indian institutions like the **Insurance Regulatory and Development Authority of India (IRDAI)**.

Drishti Mains Question:

Q. Assess the policy measures required to promote investments in green projects and stimulate the growth of India's green bond market.

UPSC Civil Services Examination, Previous Year Questions (PYQs)

Prelims

Q. Indian Government Bond Yields are influenced by which of the following? (2021)

1. Actions of the United States Federal Reserve
2. Actions of the Reserve Bank of India
3. Inflation and short-term interest rates

Select the correct answer using the code given below.

- (a) 1 and 2 only
- (b) 2 only
- (c) 3 only
- (d) 1, 2 and 3

Ans: (d)

Mains

Q. Explain the purpose of the Green Grid Initiative launched at the World Leaders Summit of the COP26 UN Climate Change Conference in Glasgow in November 2021. When was this idea first floated in the International Solar Alliance (ISA)? **(2021)**

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