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Yearly Rewind 2023

GREEN INVESTMENTS: THE 2023 INDIA STORY

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The year 2023 started with an outburst of green initiatives by the Indian government with the allocation of INR 3,500 billion (~USD 4.2 million) for investment towards energy transition and net zero objectives. In this section, we discuss the sectors that attracted investor interest in the ESG space in India and focus on the issues of greenwashing and reporting challenges faced by stakeholders. We also discuss, in brief, the developments with respect to credit rating entities, supply chain models and the establishment of carbon market in India.

Renewable energy and clean technology take the centre stage

In 2023, the most attractive sectors for green investments in India were renewable energy and clean technology. In January, India successfully issued its first sovereign green bond amounting to INR 80 billion (~USD 1 billion) for financing of public sector projects aimed at reducing the carbon emissions intensity and supporting renewable energy. In the private sector, start-ups in the clean technology space witnessed promising interest from venture capital investors despite the reported decline in venture funding in tech start-ups in 2023.[1] This can be attributed to India's raised commitments towards sustainability and achieving reduction of 33-35% in emissions intensity by 2030.[2] Resultantly, there is an increased demand for investments to meet such commitments.

In this sector, green hydrogen received considerable attention with the Indian Government deploying INR 197 billion (~USD 2.3 billion) on green hydrogen projects to facilitate transition from fossil fuels to clean energy. Many global financial institutions like the World Bank[3] and European Investment Bank[4], and institutional investors including Peak XV Partners (formerly known as Sequoia India)[5], Gruhas and Rainmatter Climate[6] have also invested towards production and use of green hydrogen. Electric mobility was another preferred sector for private equity investments both from domestic and foreign investors.[7] The sector has benefitted from government schemes such as exemption from customs duty on import of goods and machinery for manufacture of batteries used in electric vehicles up to 31 March 2024.[8] The Indian Government has also pushed towards achieving electric mobility by allocating USD 7 billion towards deployment of electric vehicles in India. In light of the favourable schemes and India's commitment towards electric mobility, large domestic corporations[9] as well as global giants like Foxconn[10] are already looking at investing in the Indian electric mobility market.

Greenwashing

Greenwashing continues to be a challenge for investors and regulators across jurisdictions. In 2023, there was a 70% increase in the greenwashing incidents globally.[11] India also witnessed a series of greenwashing incidents, some involving, as reported in the Economic Times, against large conglomerates like the Adani Group which were allegedly found to be contributing finance towards fossil fuels despite making carbon neutral commitments.[12] In a report by the Advertising Standards Council of India (**ASCI**), it was found that 79% of the environment related claims made by advertisements are exaggerating or misleading.[13] To increase transparency and accountability, ASCI proposed draft guidelines which include suggestions for a high level of substantiation for products marketing themselves as 'ecofriendly' or 'sustainable'.[14]

In April 2023, the Reserve Bank of India (**RBI**) also came up with a framework to address greenwashing concerns in deposits issued by regulated entities.[15] Within the framework, the RBI identifies greenwashing as the practice of marketing products as 'green' when they fail to meet the necessary requirements. One of the primary identifiers to qualify a product or service as 'green' is to determine the use of the finance proceeds i.e. determining the use of the finance to ensure that the funds are used for an activity that is categorized as 'green'. The use of proceeds test is consistently being recommended by global organizations and has been previously adopted in the Indian regulatory framework to mitigate the risk of misuse of funds.[16]

The next big steps for India in curbing greenwashing may be using artificial intelligence (**AI**) and technology to enable a robust system of verifiable and accurate data. AI and data analytics are already being used to assess real time performance of green projects in other parts of the world.[17]

Enhanced reporting obligations

On 12 July 2023, the Indian securities market regulator, Securities and Exchange Board of India (**SEBI**) introduced the 'BRSR Core' which seems to be an enhanced version of the existing reporting obligations under the Business Responsibility and Sustainability Report (**BRSR**). The BRSR Core outlines 9 key performance indicators which include water, energy and greenhouse footprint, embracing circularity, enhancing employee wellbeing and safety, and enabling gender diversity and inclusive development. Certain new indicators such as openness of business and gross wages paid to women are also included in the BRSR Core. Under the framework, the top 1000 listed entities are required to make disclosures of specified data points with respect to the key performance indicators, in their annual reports.

Amid global concerns on greenwashing and to bring credibility into the disclosures, SEBI has also required that the companies must obtain 'reasonable assurance' from an independent third party for the disclosures under the BRSR Core. This requirement is a higher threshold than other global regulators which only require 'limited assurance' which can be less costly and may better correspond to the current technical ability for assurance providers to undertake such assessment.[18]

With the increase in regulatory oversight, businesses will need to establish internal policies for collection and efficient reporting of information. One of the solutions to ensure accuracy and maintain standards is integrating technology enabled platforms into ESG reporting. In 2023, using technology to solve reporting issues has created investment opportunities for start-ups providing sustainability management software services to organizations for managing and reporting their ESG performance.[19] Going into 2024, we expect this trend to continue in India in line with the approach taken by companies across Europe and North America who are turning to AI and technology to simplify their reporting obligations.[20]

Supply chains at the frontier

A supply chain is the entire process which a product or service undertakes from its inception to the end user which includes the supply of raw materials, manufacturing and distribution. Globally, businesses are recognizing the importance of a sustainable end-to-end supply chain on parameters such as employee wellbeing and carbon emissions.[21]

India has also recognized the need for transformations in the supply chain and its impact on the overall ESG assessment of a company. SEBI through the BRSR Core has mandated disclosures for value chain, which encompasses the top upstream and downstream partners of the company, comprising of 75% sales or purchases by value. Indian start-ups have tapped this opportunity and have garnered investments for innovations in supply chains. For instance, Minfiti, a supply-chain financing platform aimed at digitizing the supply chain of corporations attracted investments worth USD 110 million in 2023.[22] Indian start-ups aimed at reducing carbon footprints in supply chains have also attracted funds from institutional investors like Omnivore.[23]

Regulatory framework for ESG Credit Rating Providers

The rising ESG landscape has led to the emergence of various service-related offerings, particularly the services provided by ESG rating providers which seek to objectively assess a company's performance on ESG metrics. The ESG assessments provided by such third-party agencies assume significance as they influence investor interests and opportunities. A recent study by Kroll surveyed over 13000 listed companies worldwide and observed that companies with higher ESG ratings generally experience better investment returns than companies with lower ratings.[24] In 2022, stakeholders raised concerns around the role and credibility of entities providing ESG ratings to companies. Issues such as lack of a common understanding of what constitutes ESG rating and use of different methodologies leading to varying results were identified.[25]

In 2023, India took steps to address such concerns in the securities market by bringing ESG rating providers (**ERPs**) within the ambit of the Securities and Exchange Board of India (Credit Rating Agencies) Regulations, 1999. It defines ESG ratings as products that are marketed as opinions about an entity regarding its ESG profile or exposure to ESG risk that are issued using a defined ranking system. On 12 July, SEBI issued a master circular requiring ERPs to obtain prior registration with SEBI. To ensure greater transparency, ERPs are required to provide ESG rating to companies on a scale of 0 (minimum) to 100 (maximum) and provide a detailed rational for the rating. As the demand for ESG related information is increasing, it is expected that the demand and use of ESG data related services and ERPs into business investment decisions will also increase. In view of this, the safeguards put forward by SEBI will prove to be consequential in ensuring investor protection.

Setting up the carbon market

The importance of international carbon markets to mitigate greenhouse gas emissions has already been realized by the international community under the Paris Agreement. India has also accepted the need for carbon markets but instead of participating in the international markets, it seeks to establish its own domestic carbon trading mechanism. To that effect, India introduced the Energy Conservation Amendment Act, 2022 (**Energy Conservation Act**) enabling the creation of a domestic carbon trading market. Under the aegis of the Energy Conservation Act, India launched its carbon credit trading scheme (**CCTS**) on 28 June 2023. The CCTS provides for a compliance mechanism under which industries in certain identified sectors will be required to maintain prescribed emissions targets and upon failing to do so, they can purchase credits to offset their increased emissions. The sectors have not been notified yet, but it is expected that fossil fuel intensive industries, iron, steel and cement may come under its purview.

However, achieving reduction in carbon emissions in such sectors can be challenging. These sectors are also hit by the European Union's Carbon Border Adjustment Mechanism (**CBAM**) which contemplates levy of higher import taxes on products whose production is carbon intensive. India is considering allowing overseas trading of carbon credits to facilitate such sectors in maintaining their emissions rates.[26] For instance, a framework for export of carbon credits to Japan is under deliberation.[27] Going forward in 2024, it is likely that India will collaborate with more countries for overseas trading of carbon credits.

India' s way forward

Globally, there is an increased awareness on the impact of human actions on the planet. Businesses and investors across sectors have been considering non-financial factors in their investment and business actions. Regulators around the world have also become increasingly stringent on regulating corporate behaviour and fixing accountability. Green finance investments in India have seen a significant increase in the previous two financial years, both from domestic and foreign investors.[28] However, in terms of contribution from the private sector, India still needs more participation to bridge the gap between the existing and required green finance. The conversation around 'blended finance' i.e. using concessional funding from public institutions and philanthropic sources to mobilize private commercial capital has already started in India.[29] To gather concessional funding, India needs to develop a predictable and transparent investment climate. The G20 Sustainable Finance Report emphasizes on combining public and private enterprises and improving the data and reporting infrastructure.[30] In 2024, we expect that the discussion on green investments in India will be inclined towards blended finance for shaping India's green economy.

ENDNOTES

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LEADERSHIP

SOUVIK GANGULY

MANAGING PARTNER & HEAD - CORPORATE PRACTICE

DENI SHAH

PARTNER- INDIRECT TAX & GLOBAL TRADE

VIDUSHI MAHESHWARI

PARTNER - DIRECT TAX

RENJITH NAIR

PARTNER - DISPUTES

CONTRIBUTORS

AKHIL RAMESH | BODHISATTWA MAJUMDER | KRISHNA NAIR | PARIDHI RASTOGI | SHRISHTI MISHRA | SUMIT NANDY | TANUJ MODI | VISHESH GUPTA

For any queries, please feel free to contact us at al@acuitylaw.co.in

506 Marathon Icon, Off Ganpatrao Kadam Marg,
Lower Parel, Mumbai 400013, India
+91 22 6666 7001
al@acuitylaw.co.in