Planning for Net Zero: Best Practices for Indian Banks and NBFCs

A Discussion on Lessons Learned from Global Banks



Report / November 2024



RMI is an independent nonprofit, founded in 1982 as Rocky Mountain Institute, that transforms global energy systems through market-driven solutions to align with a 1.5°C future and secure a clean, prosperous, zero-carbon future for all. We work in the world's most critical geographies and engage businesses, policymakers, communities, and NGOs to identify and scale energy system interventions that will cut climate pollution by at least 50 percent by 2030. RMI has offices in Basalt and Boulder, Colorado; New York City; Oakland, California; Washington, D.C.; Abuja, Nigeria; and Beijing. RMI has been supporting India's mobility and energy transformation since 2016.

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Executive Summary



Indian banks and Non-Banking Financial Companies (NBFCs)[i] can help bridge the climate finance gap and ensure financial stability in a changing environment. India faces a considerable average annual investment need of USD 202 billion to achieve its net-zero greenhouse gas (GHG) emissions goal.[ii,1] As the largest available source of climate finance outside of government expenditure, India's banking sector has the potential to help address this financing gap.[2]



Regulators have implemented several initiatives to both support and nudge the sector to take action. Most recently, the Reserve Bank of India (RBI) released draft guidelines on climate-related disclosures for Regulated Entities (REs)[iii] in February 2024, highlighting the need to assess climate risks and plan for the transition.



Though banks are taking action, the sector is still early in its efforts and faces structural bottlenecks. A significant number of Indian banks and NBFCs lack the preparedness to comply with RBI's draft disclosure framework and provide confidence to stakeholders in their future-readiness. Key barriers identified through consultations include: the limited availability of high-quality, climate-relevant data needed to evaluate climate risks and opportunities; challenges building the capabilities needed to inform and implement transition strategies; and others.

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i. A **Non-Banking Financial Company** (NBFC) is an Indian company defined under the Companies Act, 1956 as engaging in the business of loans and advances, acquisition of shares/stocks/bonds/debentures/securities issued by government or local authority or other marketable securities of a like nature, leasing, hire-purchase, insurance business, chit business but does not include any institution whose principal business is that of agriculture activity, industrial activity, purchase or sale of any goods (other than securities) or providing any services and sale/purchase/construction of immovable property. Unlike a bank, an NBFC cannot accept demand deposits and is not part of the payment and settlement system. NBFCs are an important stakeholder to consider as they complement and supplement the banking sector through their grassroots-level presence and ability to deliver tailor-made products to meet the varied needs of customers.

ii. At the time of publication, 1 USD = 82 INR

iii. **Regulated Entities** are those entities that are directly regulated and supervised by RBI. These include Scheduled Commercial Banks, Payment Banks, Small Finance Banks, Urban Co-operative Banks (Tier III and IV), Non-Banking Financial Companies (NBFCs) – Upper and Middle Layer, Housing Financing Companies, Credit Information Companies, and All India Financial Institutions.

Banks and NBFCs can leverage integrated transition planning approaches to address barriers and meet evolving regulatory and stakeholder expectations. RBI's forthcoming climate disclosure framework presents a valuable opportunity for REs to demonstrate their commitment to climate action and enhance transparency for regulators, investors, and stakeholders. Beyond a compliance exercise, banks and NBFCs can leverage this opportunity to develop a holistic climate strategy.

This report highlights 10 lessons (See Exhibit ES1) from global banks' experience with transition planning and their potential application for Indian banks and NBFCs. Contextualising these global lessons and best practices to India and using them to inform transition planning can help REs better equip themselves to respond to RBI's final disclosure framework, identify and capture climate opportunities while addressing climate risks, provide stakeholders with confidence in future-readiness, and potentially attract greater foreign capital seeking climate alignment.

> **Beyond a compliance exercise, banks and NBFCs can leverage this opportunity to develop a holistic climate strategy.**

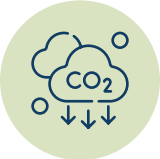


Exhibit ES1 Lessons From Global Experiences With Transition Planning



RMI Graphic. **Source:** RMI analysis.

Introduction



India will need significant financing to realise its net-zero target by 2070 and build climate resilience. India, which is the third-largest GHG emitter globally,[3] has taken steps to decouple economic growth from emissions,[4] but rising energy demand may double emissions by 2040.[5] Mitigation efforts needed to achieve net zero will be significant and are estimated to cost USD 10.1 trillion through 2070 or USD 202 billion per year on average.[6] Much of this investment will likely need to be front-loaded to build out critical infrastructure and invest in technology development, resulting in an immediate need for capital. In parallel, acute and chronic impacts of climate change are mounting. In 2021 alone, India is estimated to have faced an income loss of USD 159 billion as a result of such impacts.[7] In contrast, current estimates suggest that annual climate finance flows are close to USD 42 billion per annum, just 25% of what is needed to meet India's 2030 Nationally Determined Contributions (NDCs).[8]



Scheduled commercial banks, NBFCs, and other lending institutions will be critical to bridging this financing gap, giving them both an imperative for climate action and an opportunity to capitalise on green growth. India's banking sector, for example, is the largest available source of climate finance outside of government expenditure.[9] Banks and NBFCs are also increasingly recognising their vulnerability to disruptions from physical and transition climate risks. In fact, climate risk emerged as the highest risk category in the RBI's 2024 Systemic Risk Survey of its REs.[10] However, financing net zero is not just a "must-do" but also a significant opportunity for new business development. It will open up new sectors and clients for lenders and provide avenues for lenders to enhance their relationships with existing clients seeking to decarbonise and become climate resilient. The majority of banks in India, however, have yet to take necessary steps to align themselves with the climate transition.[11]



India's evolving regulatory environment for sustainable finance signals the need for banks and NBFCs to take an accelerated and holistic approach to the climate transition. The past few years have seen a series of regulations designed to improve transparency of corporate sustainability efforts (including climate) and incentivise greater action. The Securities Exchange Board of India (SEBI) introduced the Business Responsibility and Sustainability Reporting (BRSR) framework in 2021 and recently extended coverage to unlisted companies through the introduction of the BRSR Core in 2023.[12] Adding to this momentum, RBI released its draft disclosure framework for climate-related risks in February 2024, building on its initial guidance over the course of 2022 and 2023 and International Sustainability Standards Board's (ISSB) efforts. Though

not finalised, it recommends detailed disclosures on climate targets, relevant risks and opportunities, strategies and governance mechanisms for addressing the same, and performance against targets as a baseline, prompting REs to think holistically about their climate strategies.[13] SEBI and RBI have also been actively developing a market for credible green financing products, with the former laying out guidelines for thematic debt issuances and funds in line with global best practices and RBI implementing its Framework for Acceptance of Green Deposits in 2023.[14] Looking ahead, more is likely to come — for example, the development of a climate finance taxonomy, as mentioned in the 2024 Union Budget speech, holds the potential to have wide-reaching implications across fundraising, capital deployment, and disclosure.[15]



Banks and NBFCs can leverage integrated transition planning to help address climate change and related regulation. Transition planning and transition plans have been globally recognised as a critical tool to address climate risks, capitalise on climate opportunities, and unlock green financing.[16] Ultimately, integrated climate transition planning for banks can be understood as the comprehensive strategy development that a firm must pursue across business functions to ensure it can accelerate the deployment of transition capital and manage climate risk in a holistic way. It refers to a planning tool and strategic process that an organisation can undertake to support the low-carbon transition by setting out targets, actions, and resources.



Examining the lessons learnt by global banks that are navigating regulatory developments and engaging in transition planning can be particularly useful for Indian banks and NBFCs. The experiences of global banks, when contextualised for the Indian market, can provide insights into the process of transition planning, helping address key questions and bottlenecks early in the process. Accordingly, this paper intends to leverage global experiences to provide guidance to banks and NBFCs engaging in transition planning to holistically address climate risks and opportunities and stay in line with RBI's ongoing initiatives.

Bottlenecks to Unlock

Although some leading Indian REs have begun taking steps to address climate change and develop the capabilities necessary, the majority are still early in this journey.[17] This, in turn, suggests a lack of preparedness amongst many REs to not just comply with RBI's draft disclosure framework, but to also provide confidence to stakeholders in their future-readiness. Our consultations have identified a set of key challenges commonly faced by lenders. These both hinder them from engaging in integrated transition planning and from meeting RBI's proposed mandate credibly. Challenges include:

1. **Barriers related to the availability of high-quality, climate-relevant data needed to meaningfully evaluate climate risks and opportunities, develop appropriate strategies, and track performance.** Lenders require a wide variety of external data to inform their climate transition strategies. However, the availability of credible, climate-relevant data in India, for example the emissions of real-economy corporates, is lacking. While pioneering in many respects, BRSR is only applicable to the top 1,000 listed companies, with disclosure for micro-, small-, and medium-sized enterprises (MSMEs) limited to just the value chains of the top 250, leaving out a significant portion of companies. Furthermore, while BRSR asks for information on Scope 1 and 2 emissions, and Scope 3 on a voluntary basis, disclosures can vary in availability and reliability, particularly due to a lack of assurance.[18] This is further complicated by a lack of credible sector-level decarbonisation pathways and appropriate science-based climate scenarios tailored to India's context that could be used to inform transition strategies.[19]

2. **Lack of appropriate governance and oversight structures to drive transition planning.** Most banks have yet to lay out strong climate commitments, be it a focus on carbon neutrality or net-zero targets or active identification and management of climate risks. A major reason for this is the lack of internal structures and governance processes that would have oversight over an RE's approach to climate and could act as champions and drivers of integrated transition planning.[20]

3. **Challenges building the capabilities needed to inform and implement transition strategies.** Transition planning and the evolution of appropriate strategies to respond to climate risks and opportunities require individuals and teams with specific technical knowledge, as well as a strong understanding of relevant considerations at the leadership and board levels. At the level of execution, banks and NBFCs require tools and capabilities to design green products, assess the climate performance and transition plans of clients while executing appropriate engagement strategies, and measure and manage exposure to climate risks. They have repeatedly noted the need for support in augmenting capacity. Though a number of initiatives have begun, there still remains a prominent need for additional interventions, particularly for those behind the curve.[21]

4. **Existing regulatory norms can limit green financing flows.** As per BASEL III norms,[iv] the current regulatory framework does not differentiate between green and non-green finance. This, in turn, does not provide any specific incentive to finance green projects. For example, renewable energy falls under the power sector alongside fossil fuel sources. Due to the RBI's sectoral credit exposure limits, which do not separate types of power generation, banks may not be able to extend additional credit to renewable energy projects since they already have significant exposure to the power sector.[22]

> **Integrated climate transition planning for banks can be understood as the comprehensive strategy development that a firm must pursue across business functions to accelerate the deployment of transition capital and manage climate risk in a holistic way.**

While the above is not an exhaustive list of all bottlenecks facing Indian banks and NBFCs, these highlight some of the key obstacles that they need to tackle to comprehensively address climate risks and opportunities and position themselves well to meet RBI's proposed disclosure mandate. Global banks, especially those with multinational portfolios, have already faced and taken steps to address similar challenges. The following section lays out key lessons from their experiences in overcoming key challenges and developing holistic climate strategies. These best practices primarily focus on approaches banks have taken to address the first three bottlenecks, as structural limitations are unique to different contexts.



iv. The **BASEL III** norms are a set of minimum performance standards and practices that must be adhered to by internationally active banks. They were developed by the Basel Committee on Banking Supervision in response to the 2007–2009 financial crisis to strengthen macroprudential regulation and supervision and promote financial stability.

Best Practices

Early lessons from global banks can be tailored and useful in the Indian context to address current bottlenecks faced by banks and NBFCs and enable them to stay in tune with RBI's initiatives through comprehensive transition planning. While there is no one-size-fits-all solution for such barriers, especially considering the specific and constantly evolving context in India, we hope valuable lessons drawn from global experiences can help Indian banks begin to tackle some of these issues effectively. In this section, we summarise key lessons and insights related to data and metrics, stakeholder engagement, products, governance, and capacity building. Notably, some best practices help to address more than one bottleneck, as many of these topics are interrelated.

Data and Metrics

Data serves as a foundation of integrated transition planning as it underpins every aspect of transition strategies and actions. It enables institutions to comply with regulatory requirements by tracking and disclosing key climate indicators and progress, ensuring alignment with sustainability goals. It is also needed to assess and manage climate-related risks through stress-testing and scenario analysis, identifying risks and opportunity areas. Data is also essential for benchmarking portfolios, identifying investment opportunities, and engaging with clients. Moreover, it supports the development and monitoring of key performance indicators (KPIs) for green financial products such as sustainability-linked loans (see **Products** on page 20). Overall, identifying, accessing, and using transition-relevant data drives informed decision-making, enhances transparency, and enables financial institutions to navigate the complexities of transitioning to a sustainable future.[23]



LESSON 1

Measuring absolute financed emissions is a common first step to disclose banks' Scope 3 emissions and pinpoint hotspots of emissions in a bank's portfolio, but with limitations. Financed emissions are defined as the GHG emissions that are a result of a financial institution's financing activities, (e.g., lending and investment). In terms of the commonly accepted GHG protocol, these fall under Scope 3 category 15 emissions.[24] Calculating absolute financed emissions is a common first step for banks to measure and comparably disclose their overall climate footprint and can help banks identify emissions hotspots to prioritise within their portfolios. The Partnership for Carbon Accounting Financials (PCAF), an industry-led partnership, has developed a globally recognised accounting methodology to quantify emissions linked to financial portfolios and identify opportunities for decarbonisation.[25] PCAF is currently considered by many to be the industry-leading best practices, with 191 financial institutions globally having disclosed in alignment with its methodology.[26] That said, using absolute financed emissions has certain limitations, as described under Lesson 2.

Example:

- Nordea, the largest bank in the Nordic region, has calculated and leveraged data on its financed emissions to identify hotspots in its loan book at a sectoral level and align its lending activities with its net zero by 2050 target. It has done so using a proprietary tool called "Customer Brain" — a one-stop source for clients and portfolios that provides data on deals, loans, and financed emissions. The methodology for the same is based on PCAF, of which Nordea is a member. Using the tool, Nordea identifies clients with high emissions profiles and develops a structured engagement plan. As a result, Nordea was able to reduce its lending portfolio's financed emissions by 29% between 2019 and 2023.[27]



LESSON 2

Beyond financed emissions, other additional types of climate-relevant data are needed to help banks inform their transition strategy, monitor emerging transition risks, and guide lending activities. While measuring financed emissions can be useful as described, it has several limitations. For instance, the underlying quality and coverage of emissions data can be an issue, and PCAF's attribution methodology can distort the emissions impact allocated across asset classes.[28] Additionally, absolute financed emissions are inherently a backward-looking metric that may be disconnected from clients' forward-looking transition plans.[29] As a result, financed emissions must be further complemented by other types of data, such as emissions intensity data and forward-looking metrics, to provide a holistic picture of climate challenges and progress. For example, intensity metrics can help with comparability within a sector and provide a more nuanced view when assessing portfolio companies. Forward-looking data, such as production-based metrics (e.g., projected production volumes),[30] can further help financiers anticipate trends and future market conditions, better positioning banks to capitalise on opportunities and mitigate potential risks. This type of data enables financial institutions to assess transition risks and tailor their strategies to meet evolving challenges and expectations. As markets become increasingly complex, the ability to leverage forward-looking insights becomes a competitive advantage, driving more strategic and informed decision-making processes.

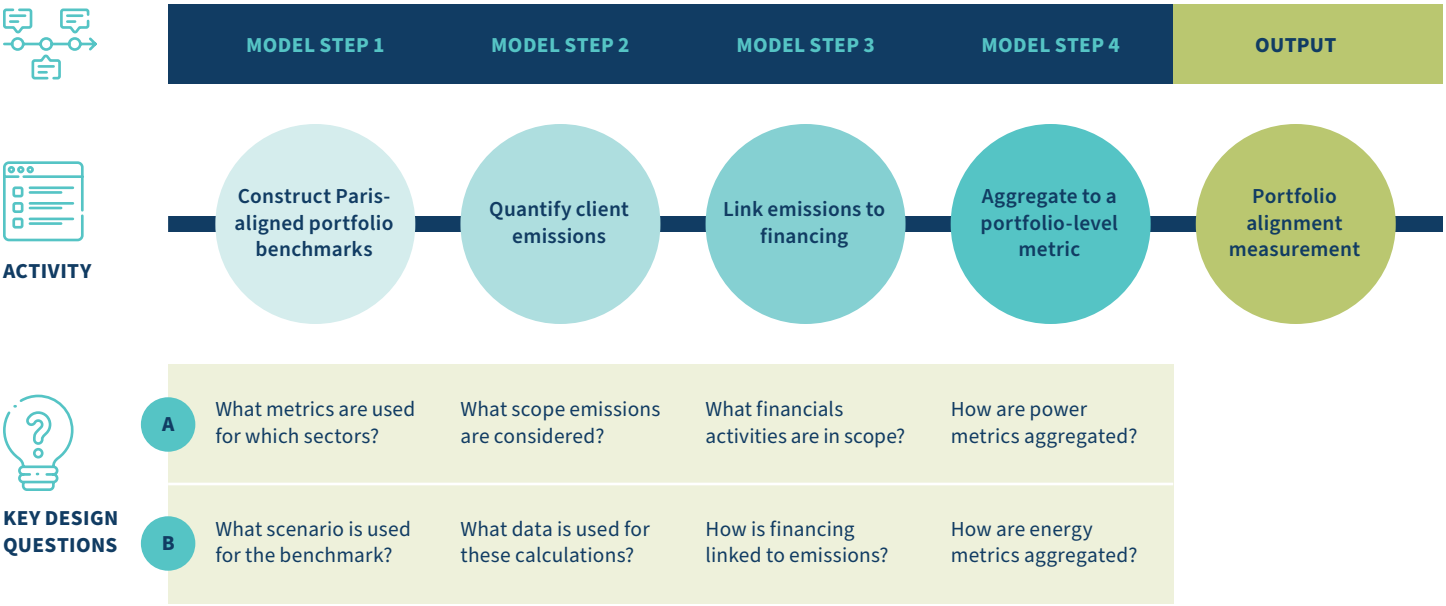
Examples:

- ING's Terra approach uses forward-looking metrics to assess and disclose its climate progress.[31] It bases its analysis on a version of the Paris Agreement Capital Transition Assessment (PACTA) alignment methodology developed specifically for banks. PACTA looks at the technology shifts that are needed across climate-critical sectors to slow global warming, as determined using sectoral pathways taken from credible, science-based scenarios, and then measures this against the actual technology clients are using or plan on using in the future. To do this, PACTA uses forward-looking data from specialist data provider Asset Impact that is based on the five-year production plans of companies in a financial institution's portfolio. This methodology can measure the alignment of a portfolio per sector or per technology, allowing institutions to identify sector-specific gaps and opportunities, as well as to target clients for engagement.[32]

The Terra approach focusses on nine sectors ranging from steel to shipping, and tracks how it needs to steer its financing portfolio to support climate goals and assess climate risks.[33]

- Barclays' BlueTrack methodology brings together multiple types of data and integrates them into the bank's decision-making process. BlueTrack estimates the emissions produced by its clients and assesses financed emissions across energy, power, aviation, agriculture, cement, and steel, monitoring these over time against a decreasing "carbon limit." BlueTrack also incorporates forward-looking data and metrics to measure the alignment of projected sectoral emissions attributed to its banking books; for example, by using datasets that combine external fossil-fuel asset and production databases with assumptions about emissions factors and asset utilisation rates, an approach also used by PACTA. It then integrates this data into the bank's risk management framework, helping to identify and monitor climate-related financial risks, including transition and physical risks. Progress is judged based on multiple parameters, including sector-level metrics such as power generation and capacity for its power sector portfolio. It further supports alignment with disclosure frameworks such as the Task Force on Climate-related Financial Disclosures (TCFD) and the aforementioned ISSB, ensuring transparency and informing decision-making on portfolio management and client engagement.[34]

Exhibit 1 Overview of Barclays' BlueTrack Methodology



RMI Graphic. **Source:** *Introducing Blue Track, Barclays.*

- Climate-aligned finance (CAF) frameworks have been developed by RMI for key sectors (shipping, steel, aluminium, aviation) to help financial institutions measure, benchmark, and disclose the emissions impact of their lending in these sectors. A key step of this process is setting boundaries around which emissions data should be included for each sector. CAF sector frameworks provide technical guidance for obtaining and processing emissions data to ensure bank disclosures are comparable. Importantly, banks then use net-zero roadmaps as benchmarks to contextualise emissions data, set robust and ambitious portfolio emissions targets, and inform engagement with clients to identify opportunities to deploy capital in support of their low-carbon transition. For example, the Sustainable STEEL Principles (SSP) provides a tailored measurement and disclosure framework for banks centred on an "alignment score" metric based on emissions intensity data and the scrap charge used in steel production.[35] This empowers lenders to support the decarbonisation of the steel sector and assess climate progress, compatible with Net-Zero Banking Alliance (NZBA) guidance.[36] Six banks currently utilise or have committed to the SSP, including Citi and Société Générale.[37]



LESSON 3

Banks can leverage existing data to uncover opportunities and design new financial instruments while working to alleviate barriers and improve data access. Despite the limitations they face, banks can access and utilise the data that is already available to them. Rather than waiting for perfect data, which increases exposure to growing physical and transition risks, banks can take an active role by collaborating closely with their clients to obtain more granular and accurate data on their environmental impacts (see **Client and Stakeholder Engagement** on page 16). They can also partner with third-party data providers to fill gaps with the best available data. Additionally, they can engage with policymakers and regulators to advocate for the disclosure and availability of higher-quality data in the future. For example, the Glasgow Financial Alliance for Net Zero (GFANZ) and One Planet are collaborating to create an open-data public platform.[38] By taking proactive steps, banks can enhance their decision-making processes and better align their financial strategies with sustainable outcomes.

Example:

- Banco Bilbao Vizcaya Argentaria (BBVA), a Spanish multinational financial services company, has integrated information from Asset Impact, a third-party data provider, as it works to align its lending portfolio with the climate goals of the Paris Agreement. Through its collaboration with Asset Impact, BBVA can utilise existing climate-related asset data to conduct analyses and inform decision-making, enabling them to monitor and reduce portfolio emissions. This includes setting targets for sectors like power generation, automotive, steel, and cement by 2040. Asset-based data also helps BBVA engage clients on decarbonisation, set KPIs, and inform investment strategies.[39]

Application to India:

REs have and will continue to face issues in securing credible data to identify their exposure to physical and transition risks, as well as the alignment of their lending book with net-zero targets.[40] However, clear progress is being made, and some Indian banks have already begun to take measures to assess the carbon footprint of their portfolios. In September 2024, Union Bank of India became the first Indian bank to join PCAF, committing to report the financed emissions of its lending portfolio by fiscal year 2027/2028.[41] Kotak Mahindra was the first bank in India to use the PACTA for Banks tool to assess the transition risk exposure of its power sector portfolio, with plans to undertake similar analyses on additional carbon-intensive sectors like oil and gas.[42] Such efforts will only continue to accelerate as REs prepare for RBI's final disclosure framework.[43] Emerging academic efforts to measure the financed emissions of India's banking sector may further provide useful lessons for domestic banks, particularly on the value of potential data sources.[44]

We are also seeing signs of increased data availability. Mandated BRSR Core disclosures are bringing in a vast swathe of unlisted companies and MSMEs into the disclosure paradigm. However, it will take time for this to be done in a robust manner, given SEBI's consideration of making this voluntary and requiring third party assessment rather than assurance.[45] Efforts have also been made to map out India's vulnerability to climate hazards down to the district level, providing a starting point for banks seeking to gauge the exposure of their own operations and that of their clients to climate change.[46] As data availability increases with time, banks will need to develop and evolve their use of tools, methodologies, and processes that can reduce the friction of data collection, processing, and integration into credit lending and risk management frameworks.

Client and Stakeholder Engagement

Financial institutions are not solely responsible nor solely capable of driving progress on real-economy decarbonisation. However, engagement with clients and other relevant stakeholders is well within the purview of bank operations and, when done strategically, enables a bank to manage its own transition risk and deepen its relationships with clients. In turn, this positions financial institutions to respond to both existing and latent demand for transition finance, identify long-term business opportunities, and can help them stand out from competitors by offering tailored products and services to support their clients (see **Products** on page 20).



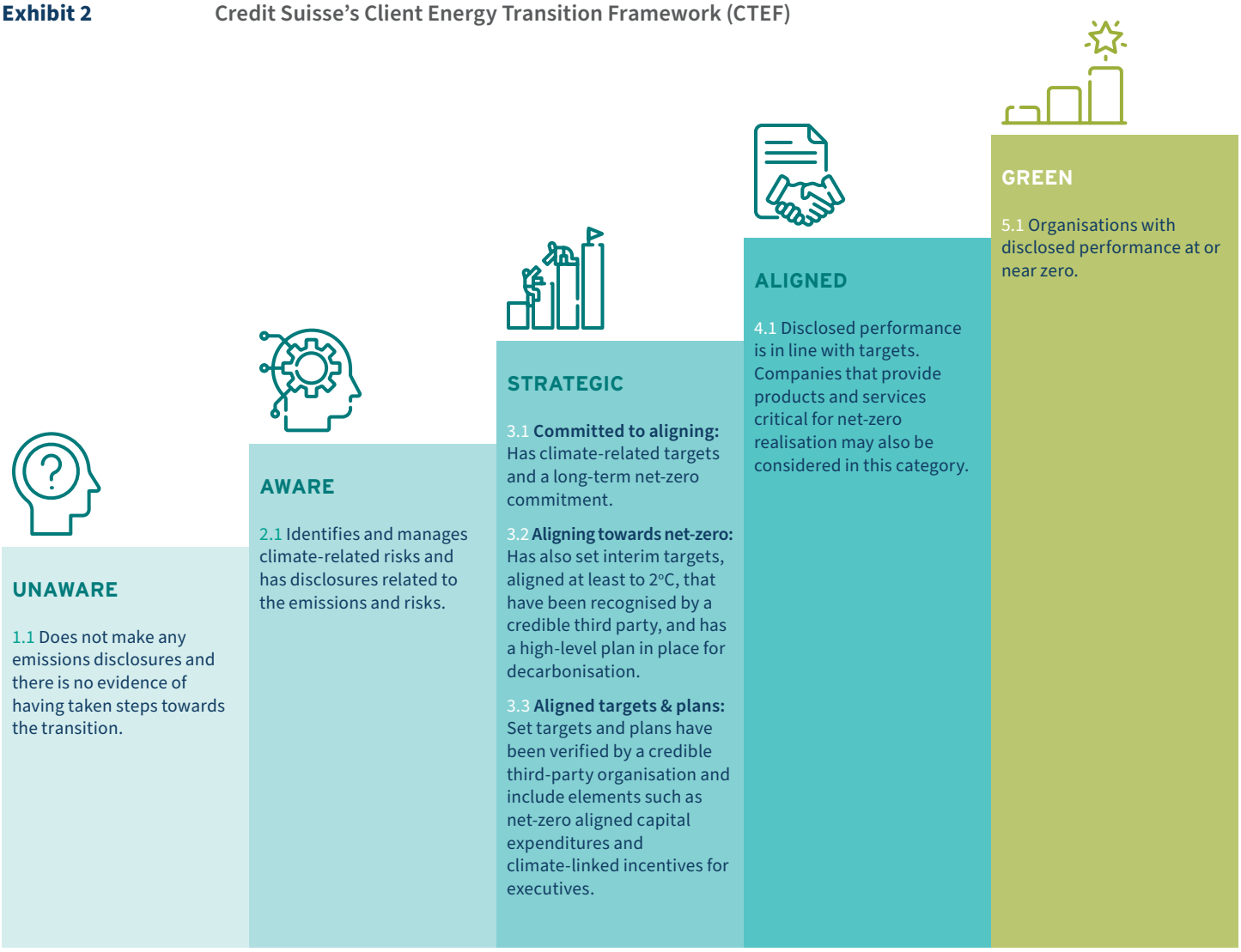
LESSON 4

Meet clients where they are in their transition journey and develop a tailored engagement strategy. Banks can see themselves as enablers and trusted advisors, providing support to clients on identifying transition ambitions and strategies while accounting for their capabilities and priorities. The first step to this is understanding where clients are in their journey. Developing a framework to assess clients and undertaking periodic assessments can not only help banks better target relevant client segments, but also give them a strong starting point in developing an engagement strategy. Following this, banks should create a structured engagement programme focussed on helping clients identify their transition finance needs and designing structured solutions for the same.[47]

Examples:

- Credit Suisse (a subsidiary of UBS) classifies clients in one of five categories in its Client Energy Transition Framework (CETF), each of which captures the extent to which the client is committed and aligned with the net-zero transition (see **Exhibit 2**). Assessment of clients is typically based on secondary research and disclosed information against a set of distinct performance indicators. Credit Suisse has implemented this classification for clients across sectors with the highest level of emissions intensity. These categorisations are used to guide Credit Suisse's sustainability discussions with clients. Though its focus is on engaging clients who are committed to or are already aligned with net zero, it is also committed to helping "unaware" clients gradually move up the framework to alignment through advisory and financing services.[48] However over time, Credit Suisse notes that it will eventually cease engagement with unaware clients after due consideration.[49]

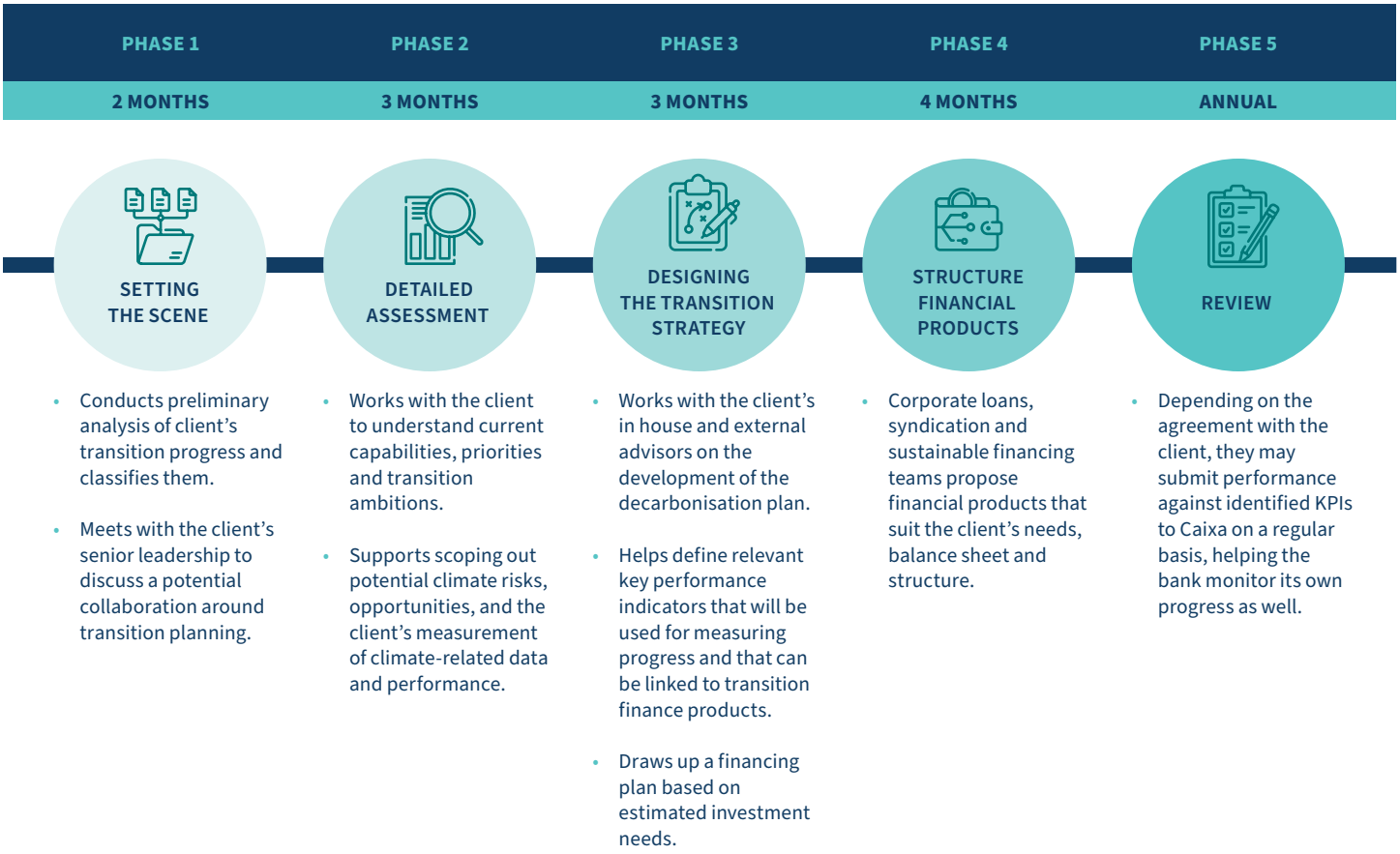
Exhibit 2 Credit Suisse's Client Energy Transition Framework (CTEF)



RMI Graphic. **Source:** Climate Action Plan." 2022. Credit Suisse. **https://am.credit-suisse.com/content/dam/csam/docs/esg/climate-action-plan-eng.pdf**.

- Caixa Bank, a founding member of the Net-Zero Banking Alliance (NZBA), has created a structured 12-month engagement process for assessing a client's transition ambitions, supporting it in developing transition plans, identifying financing needs and developing appropriate products, and engaging in annual follow-up to monitor performance (see **Exhibit 3**).[50]

Exhibit 3 Caixa Bank's client engagement process



RMI Graphic. **Source:** Leadership Strategies for Client Engagement: Advancing climate-related assessments, University of Cambridge Institute for Sustainability Leadership.

- Intesa Sanpolo, Italy's leading bank, has developed a set of standardised products through which it aims to increase the capabilities of corporate clients, particularly SMEs. It has created regional environmental, social, and governance (ESG) labs that bring together clients and industry experts to discuss pathways to improve ESG performance across their value chains. It has also developed a portal called Skills4ESG that clients can access to gain insights and inform their own transition towards sustainability.[51]



LESSON 5

Multi-level engagement — across clients, industry, and policy — leverages banks' resources in driving desired outcomes and maximising impact on climate in the real economy. Multi-level engagement refers to coordinating client, sector, and policy engagement to achieve specific, climate-aligned outcomes.[52] Under the current engagement paradigm — where different teams across a bank may pursue uncoordinated engagement—efforts are often siloed, hard to measure, and ultimately sometimes ineffective in driving desired outcomes. A multi-level engagement approach can help unlock system-level impacts by supporting policymakers and industries in promoting decarbonisation solutions and bolstering demand for transition finance. RMI published a how-to guide to help financial institutions jumpstart their engagement strategies by creating a roadmap to coordinate internally and engage externally at multiple levels.[53] For example, to support clients in the building sector to decarbonise, different teams within a bank (such as risk management and ESG) could work closely with regulators or industry groups through appropriate channels to support the development of an enabling environment for decarbonisation.

While this concept is relatively new and lacking in global best-practice examples in terms of disclosing and executing a fully multi-level strategy, banks have successfully engaged at the sector and policy levels.

Examples:

- Citi discloses its role in various climate-relevant trade associations and notes that it aims for any of its direct or indirect lobbying and public-sector engagement to align with supporting the net-zero transition.[54]

- Participation in CAF frameworks provides an opportunity for banks to work alongside industry. For example, the Pegasus Guidelines brought banks together with industry experts and groups in aviation to design an aviation-focussed climate finance framework.[55]

Application to India:

Transition planning for corporations in the real economy is still in an early stage in India, and proactive client engagement can risk overwhelming corporate clients, potentially impacting the relationship. This is particularly true for MSME clients, which account for a growing share of outstanding credit, but may be unwilling to engage in this process due to a lack of capabilities or incentives.[56] Some leading banks have recognised the value and need to engage clients, particularly smaller clients. For example, ICICI bank holds one-to-one sessions with senior management of smaller companies, helping them understand the need and value of transition.[57] However, a majority of banks lack a structured, climate-focussed engagement process with clients.[58]

As banks and NBFCs seek to increase their client engagement, it will be important to assess clients' transition readiness and willingness using a framework tailored to India's context, considering the broader decarbonisation readiness of the sector, their

priorities, and their broader performance on ESG efforts. Data from BRSR reporting provides a useful backbone for such an assessment but given its limited applicability relative to the diversity of borrowers, lenders will need to start early engagements with clients to gain deeper insight into their priorities. Banks and NBFCs should also consider developing engagement models and marketing campaigns for retail clients; an increased focus on retail lending across asset classes offers an opportunity to educate loan seekers on green assets such as electric vehicles (EVs) and green homes and associated financing products.[59] Lenders may also consider developing integrated engagement strategies, bringing together their existing policy, sectoral, and client engagement efforts under one unified approach to support systemic change.

Products

As financial institutions seek to decarbonise their balance sheets and support the economy, they will need to develop tailored financing products that can tap into the growing demand for green products and services. These can broadly fall into two categories:

- Green products that finance "green" assets or companies in alignment with or critical to net zero.
- Transition products that finance the transition of conventional assets or companies towards net zero.[60]



LESSON 6

Leverage existing regulatory and voluntary frameworks, engage key stakeholders and clients, and consider ecosystem synergies when developing green products.

Existing regulatory frameworks, taxonomies, and guidelines can provide strong policy signals, help banks identify emerging green sectors and technologies for investment, and offer tangible incentives. Banks can also consult and engage with clients proactively on their climate-related needs (see **Client and Stakeholder Engagement** on page 16) to inform their development of financial instruments that help those clients attract further transition finance and achieve their climate targets. Beyond client engagement, banks can consider how products and programmes can combine to enhance opportunities.

Examples:

- In 2021, ING, along with nine other banks, provided a USD 374 million sustainability-linked senior secured term loan linked to the Poseidon Principles, a framework for assessing and disclosing the climate alignment of ship-finance portfolios in line with the International Maritime Organization's goals,[61] to support Singapore tanker company Hafnia to incentivise lowering its emissions.[62]

- In 2023, Mizuho Financial Group underwrote JPY 41 billion (USD 267 million) of Japan's largest transition bond of the year, a JPY 80 billion (USD 521.4 million) offering offering from Chugoku Electric Power. One highlight is that beyond just bond issuance, Mizuho took one step further to engage and assist the utility company in developing its transition strategy, including a road map to net zero by 2050.[63]

- Bromford, a UK-based housing association, secured a GBP 200 million (USD 260 million) sustainability linked loan from NatWest that enables it to build 1,300 affordable and energy efficient homes by 2028.[64] NatWest also launched a Home Energy Hub to help homeowners make energy efficient changes to their properties and reduce their bills.[65]



LESSON 7

Products with robust KPIs or guardrails can both mitigate greenwashing risks and incentivise the realisation of a just transition. Ensuring a just transition is critical for the realisation of global climate commitments, particularly in emerging economies where many are dependent either directly or indirectly on carbon-intensive economic activities. While it is necessary to decarbonise and shift these activities away from business as usual, it is important to ensure that social harm is minimised and the benefits of the transition are applicable to all. Banks play an important role in ensuring this as the financiers of both green assets and transition efforts. Globally, banks in emerging markets have done so in a number of ways, such as by including social KPIs into their transition-linked loans or investments or instituting robust processes to ensure that all relevant stakeholders are consulted as industries decarbonise.

Similarly, a lack of sufficient guardrails can also pose risks to the environmental and climate impacts a product was intended to support. For example, DWS, the asset management arm of Deutsche Bank, overstated the integration of green or sustainability-related aspects into its financial products and investments and was fined USD 19 million by the US Securities and Exchange Commission (SEC) in September 2023.[66] Improving guardrails on such products can help ensure that these financial instruments meaningfully contribute to sustainable outcomes. This can entail developing and transparently reporting on clear and specific KPIs, having a second or third-party verification to enhance credibility, improving clarity on the use of proceeds for green bonds or loans and well-defining what activities qualify, and implementing robust but manageable monitoring and reporting frameworks.[67] Such practices can prevent greenwashing, foster investor confidence, and ensure that capital is directed towards projects that deliver tangible environmental and social benefits.

Examples:

- BNP Paribas has recently accelerated its deployment of sustainability-linked loans to microfinance institutions that can support micro and small enterprises in their climate transition in an inclusive manner. It issued three Inclusive and Sustainability-linked Financing credit lines in 2023 with specific indicators that will be used for monitoring and performance-based incentives. Indicators include incentive lending to specific segments (e.g., the number of loans to women, the number of loans to welfare recipients), lending for specific purposes (e.g., the volume or number of loans for environmental transition of clients), and shifting the borrower's own internal operations (e.g., the percentage of credit agents trained with regards to biodiversity, the number of loans informed by environmental and climate assessments).[68]

- Standard Chartered launched its first sustainability bond in 2019, attracting over EUR 2.4 billion (USD 3.67 billion) in investor demand. The bond issuance aligns with the United Nations' Sustainable Development Goals (SDGs) and focuses on supporting SMEs in emerging markets. The funds raised will be allocated to projects that support various SDGs, focussing on areas such as clean energy, health, education, and economic inclusion.[69]

- BNG Bank, a public bank owned by the Dutch government, issued a USD 856 million sustainability bond to encourage sustainable practices at local levels. This bond supports "best-in-class" municipalities in the Netherlands that excel in sustainability. The proceeds are used to finance general-purpose loans for these municipalities, chosen based on ecological, socio-cultural, and economic performance indicators developed by the Tilburg Sustainability Center. Key funded projects focus on sustainable energy sources, biodiversity, waste management, and social welfare improvements, aligning with the SDGs. This bond is innovative in encouraging municipalities to continuously improve their sustainability scores. For example, Bloemendaal has set a target to derive 15% of its energy from local, sustainable sources and implemented various housing and knowledge-sharing programmes for sustainability.[70]

Application to India:

Outside of supporting decarbonisation efforts, Indian banks and NBFCs should also view the development of tailored products with strong guardrails as a way to attract foreign and domestic institutional capital at concessional rates. This can be a powerful way to counteract some of the lagging growth in deposits that may constrain lending activities for banks and lower the cost of capital for NBFCs.[71]

SEBI and RBI have taken aggressive steps in the past few years to facilitate the development of green financing, namely through frameworks (SEBI's green bond framework and RBI's Green Deposit framework) that provide guardrails on use of proceeds and reporting and monitoring.[72] The climate taxonomy announced in the Union Budget 2024 should build on these and create economy-wide definitions and criteria for green activities and investments at a sector level.[73] Additionally, credit enhancement facilities have been set up to encourage green lending, such as the MSME Green investment and financing transformation scheme launched by the Ministry of MSMEs, and the SIDBI-Shell Risk Sharing Facility for EVs.[74, 75]

Green lending is growing in India, and banks have increasingly been deploying targeted financing instruments to raise and deploy green finance.[76] There has been an increase in green deposit offerings by both large and small banks over the past few years, supported by the release of RBI's guidance,[77] as well as the use of innovative performance-based products such as sustainability-linked loans.[78] However, there remains potential for greater product innovation and scale. A good example of the same is SBI bundling rooftop solar loans with home loans for residential projects financed through its long-term climate funds.[79] Additionally, it is important to consider ways to make these products more affordable by

either addressing elevated perceived risks or by implementing de-risking measures. For instance, despite rising EV penetration and credit enhancement availability, many banks either lack tailored EV loan products or offer less favourable terms than traditional automotive financing because of high-risk perceptions.[80] Furthermore, understanding how to integrate social considerations into new products is critical for India, where ensuring a just transition is considered vital to the path to net zero. This is particularly important for transition finance products for clients that may have to undergo significant structural shifts in their business models, where measures should be considered to mitigate negative impacts on livelihoods and surrounding communities.[81]

Governance

Governance is at the core of developing an integrated climate strategy. Globally, and increasingly in India, a growing number of banks have taken a positive step by establishing ESG or sustainability committees. However, taking board-level discussions to business-level implementation requires accountability at all levels.



LESSON 8

Ensure top level buy-in and execution across all management levels. Boards and executive committees play a critical role in setting the strategy of a bank and developing appropriate responses to emerging risks and opportunities. Embedding climate considerations across the organisation and appropriately managing risk requires boards to have a rich understanding of the relevant considerations and a commitment to effectively managing the transition, with high levels of accountability across management to ensure implementation.[82] One approach to ensure executives and boards are incentivised and accountable for climate and sustainability goals is to align compensation with climate metrics alongside traditional financial and business performance metrics. This trend is increasing, driven in part by new guidance by the Basel Committee on Banking Supervision, a global standard setter for prudential regulation.[83]

Examples:

- HSBC has elevated climate risk to the board level by defining it in a bank-wide Risk Appetite Statement and ensuring those risks are regularly reported to the board-level risk committee. To enhance the tracking of climate risk management at different levels, the bank developed risk appetite metrics that have been incorporated into the overall Key Management Information metrics, supporting more informed business and investment decisions at business and transaction levels.[84]

- NatWest Group Plc. began linking executive directors' renumeration to climate targets in 2020. In 2023, 10% of potential executive annual bonuses were based on achieving metrics linked to transition plan implementation and climate and sustainable financing goals. NatWest has increased the ambition level over time, with the financing goal increasing from GBP billion (USD 22.7 billion) in 2022 to GBP billion (USD 32.9 billion) in 2023. Incentives have also been extended to the wider workforce bonus pool within NatWest to further emphasise bank-wide actions that contribute to climate goals.[85]

LESSON 9

Ensure that climate and sustainability are integrated across business verticals and hierarchies. Beyond creating central ESG committees, banks should ensure sustainability departments do not operate in isolation. By working closely with departments such as risk management, credit, business operations, and strategy, sustainability teams can ensure that climate considerations are embedded into all business processes and decision-making, leading to more responsible and resilient financial practices.[86]

Example:

- ING has set up a distinct ESG committee to monitor and advise on ESG developments at the board level. To ensure its cross-departmental collaboration, the ESG committee consists of at least one member of each of the other committees such as the Risk Committee. At the senior management level, ING created the Steering Committee and Sounding Boards to involve senior leaders from across the bank and help guide the implementation of ESG strategies. At the business level, a Wholesale Banking Sustainability Steering Committee was set up to clarify ownership and accountability to implement wholesale banking's sustainability commitments.[87]

Application to India:

Many Indian banks have set up ESG divisions, providing oversight on integration of ESG considerations internally, as well as in lending activities and risk management.[88] Though these typically also cover climate considerations, a majority of banks lack dedicated oversight structures focussed on climate, despite the recognition of the need to take a clear stance on climate due to increasing risk.[89] However progress has been made by large banks and sustainability leaders such as State Bank of India (SBI), Axis Bank, and Yes Bank.[90]

Nevertheless, having board oversight does not necessarily translate into action. Indian banks, particularly small and medium domestic banks, may struggle to implement the changes needed to adequately integrate climate and ESG considerations into core business operations.[91] Though strengthening regulation will remain a key incentive to build capabilities, linkages to executive compensation may be necessary to develop a sense of internal urgency. While linkages to short-term incentive plans (STIPs) or long-term incentive plans (LTIPs) are yet to become a mainstream tool for corporate action, there is evidence that this is picking up among Indian corporates more broadly.[92]

Capacity Building

To incorporate the lessons above, banks need to invest in developing new competencies and skills, not just in siloed sustainability teams but across all levels of the organisation. For example, risk management teams need to be well-versed in transition and physical climate risks and their evaluation. Similarly, underwriting teams need to understand the nuances of emerging green sectors and the credibility of transition plans disclosed by potential borrowers. Client relationship managers need to be able to understand the challenges their clients face in trying to decarbonise to foster a deeper relationship. These capabilities are not purely a function of investing in training and hiring but in also ensuring that climate considerations are a part of the firm's culture, ethos, and performance review processes.



LESSON 10

Given limited resources, international capacity building initiatives should be leveraged while firm-specific efforts can be strategically tailored and targeted.

Building internal capacity is critical to enable financial institutions to make progress in areas such as those noted above. To help with this, many relevant tools and resources have been developed by groups such as CPI, CBI, and RMI that are publicly available.[93] Various global efforts exist, and more are being developed, to directly support banks to prepare for the climate transition. In addition to participating in such initiatives, banks can cultivate an organisational culture supportive of sustainability by providing internal, tailored trainings and workshops for employees, including senior leaders, to develop an enhanced understanding of regulatory requirements and transition planning best practices.

Examples:

- Over 450 global financial institutions participate in the GFANZ, which supports collaboration and provides resources and knowledge products to help the financial sector achieve the Paris Agreement.[94]
- FirstRand Bank has undertaken internal capacity building at multiple levels. It has rolled out an ESG training programme with a focus on climate change for allemployees, with intermediate and advanced trainings for relevant teams. For example, client-facing and credit-risk teams have received training on incorporating key climate risks and opportunities during credit appraisal.[95]
- NatWest sees education as a key enabler for enhancing the capacity and skills needed to drive change related to climate. In 2022, the bank invested EUR 1.5 million (USD 1.95 million) to partner with the University of Edinburg to offer a three-year climate education programme to all NatWest Group colleagues.[96] Additionally, NatWest created the Climate Centre of Excellence to not only provide technical support and resources for all NatWest employees but to also develop relevant climate strategies and integrate them in the bank's overall transition plan.[97]

Application to India:

There remains a significant need for capacity building of Indian banks. A 2022 survey of credit and risk officers across 10 leading Indian financial institutions revealed a significant lack of capacity and understanding of ESG and climate risks, as well as a lack of efforts to systemically integrate the same into risk management frameworks.[98] Efforts to bridge knowledge gaps have increased over the past few years. The UK PACT programme ran training programmes for staff across risk management and credit departments in 2022.[99]

More recently, the Indian Institute of Banking and Finance has stepped up its engagement on the climate transition. It recently partnered with the International Finance Corporation (IFC) to develop a course on Climate Risk and Sustainable Finance.[100] It has also partnered

with the United Nations Environment Programme Finance Initiative's (UNEP FI's) Principles of Responsible Banking (PRB) Academy to conduct capacity building on sustainable finance amongst Indian bankers.[101] Individual banks are also undertaking their own capacity building activities. For instance, SBI partnered with the Climate Policy Initiative's (CPI's) Centre for Sustainable Finance (CSF)[102] to run a training programme on Climate Change Risk Management.[103]

As RBI finalises its draft disclosure framework and Indian banks increasingly seek to implement global best practices, they will need to build capacity on sector-level decarbonisation pathways and financing opportunities as they identify emerging climate opportunities. They can do this by gathering and utilising climate-relevant data to assess their exposure to climate risks and guide their transition strategy, and by providing tools and technologies that can support banks in their transition planning and reporting.

Conclusion: The Value of Transition Planning for Indian Banks and NBFCs



RBI's draft climate disclosure framework presents a valuable opportunity for REs to signal their commitment to climate action and enhance transparency for regulators, investors, and stakeholders. Beyond a compliance exercise, banks and NBFCs can leverage this opportunity to adopt a holistic approach to assess climate-related risks and identify decarbonisation pathways.[104]

Undertaking such integrated transition planning can help lenders approach this challenge in a structured manner. Global best practice shows that transition planning is an organisation-wide effort. It is embedded within broader business strategy development and is an ongoing process, with key assumptions and decisions revisited in light of evolving regulation, stakeholder expectations, and business realities.[105] "Transition plans" are typically the outcome of this planning process.[106] These capture a firm's climate objectives and outline the approach it intends to take over a specified time horizon in order to align its business activities with the same. As with transition planning, these documents are not static. They reflect the approach to climate action the entity feels is best suited for the current environment and priorities, and can evolve as its strategies change.

While RBI's draft disclosure framework does not explicitly mandate banks to develop a transition plan, there are multiple benefits that Indian banks and NBFCs can unlock by completing a comprehensive transition planning process. Firstly, they will be better equipped to respond to RBI's disclosure framework, having taken structured steps to identify climate risks and opportunities and develop internal oversight structures to champion the transition. Secondly, transition planning can help banks and NBFCs identify and capture opportunities in new sectors and expand client relationships in hard-to-abate sectors like steel and cement. This process will also enable banks and NBFCs to identify the right approach to balance the need for climate and environmental action, with the need to ensure financing for India's economic growth and promotion of livelihoods in key sectors. Thirdly, this will provide stakeholders with confidence in the firms' readiness to navigate an evolving climate, economy, and regulatory landscape, and may help attract greater foreign capital as global investors undertake portfolio re-allocation in response to impact mandates and/or regulatory pressures.

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