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INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT
INTERNATIONAL DEVELOPMENT ASSOCIATION

PROGRAM DOCUMENT

FOR A
PROPOSED LOAN

IN THE AMOUNT OF US$667 MILLION
AND A
PROPOSED NON-CONCESSIONAL CREDIT
IN THE AMOUNT OF US$83 MILLION

TO INDIA

FOR A

CATALYZING PRIVATE FINANCING FOR SUSTAINABLE RECOVERY AND GROWTH
DEVELOPMENT POLICY OPERATION

June 1, 2022

Finance, Competitiveness And Innovation Global Practice
South Asia Region

India

GOVERNMENT FISCAL YEAR

April 1 – March 31

CURRENCY EQUIVALENTS

(Exchange Rate Effective as of April 30, 2022)

US$1.00 = INR 76.42

INR 1 = USD 0.0131

ABBREVIATIONS AND ACRONYMS

AIF	Alternative Investment Fund	IMF	International Monetary Fund
AMFI	Association of Mutual Funds in India	InvIT	Infrastructure Investment Trusts
BEE	Bureau of Energy Efficiency	MFI	Microfinance Institution
BRSR	Business Responsibility and Sustainability Report	MFI	Microfinance Institution
CAG	Comptroller and Auditor General of India	MSE	Micro and Small Enterprises
CCB	Climate Co-Benefits	MSME	Micro, Small & Medium Enterprise
CPF	Country Partnership Framework	MoF	Ministry of Finance
CPI	Consumer Price Index	NaBFID	National Bank for Financing Infrastructure & Development
CGSMFI	Credit Guarantee Scheme for Micro-Finance Institutions	NBFC	Non-Banking Financial Company
CGTMSE	Credit Guarantee Fund Trust for Micro and Small Enterprises	NDC	Nationally Determined Contributions
DEA	Department of Economic Affairs	NHB	National Housing Bank
DPL	Development Policy Loan	NIP	National Infrastructure Pipeline
DFI	Development Financial Institution	NMP	National Monetization Pipeline
DFS	Department of Financial Services	NPA	Non-Performing Asset
ECLGS	Emergency Credit Line Guarantee Scheme	PforR	Program-for-Results
EIA	Environment Impact Assessment	PA	Prior Action
EPFO	Employees' Provident Fund Organization	PAT	Perform, Achieve & Trade
ESG	Environment, Social, and Governance	PTC	Pass through Certificate
FDI	Foreign Direct Investment	PFM	public financial management
FFC	Fifteenth Finance Commission	PSB	Public Sector Bank
FPI	Foreign Portfolio Investor	RAMP	Raising and Accelerating MSME Performance
FRBM	Fiscal Responsibility and Budget Management	RBI	Reserve Bank of India
FSR	Financial Stability Report	RMBS	Residential Mortgage-Backed Securities
HFC	Housing Finance Company	ROA	Returns on Assets
GDP	Gross Domestic Product	SIDBI	Small Industries Development Bank of India
GoI	Government of India	SEBI	Securities and Exchange Board of India
GRS	Grievance Redress Service	TA	Technical Assistance
IBRD	International Bank for Reconstruction and Development	WB	World Bank
IFC	International Finance Corporation	WBG	World Bank Group

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INDIA

CATALYZING PRIVATE FINANCING FOR SUSTAINABLE RECOVERY AND GROWTH

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SUMMARY OF PROPOSED FINANCING AND PROGRAM

BASIC INFORMATION

Project ID	Programmatic
P177985	No

Proposed Development Objective(s)

The proposed development objective is to catalyze sustainable private sector financing for India's economy, with the focus on infrastructure and MSMEs.

Organizations

Borrower:	INDIA
Implementing Agency:	Department of Financial Services, Ministry of Finance.

PROJECT FINANCING DATA (US$, Millions)

SUMMARY

Total Financing	**750.00**

DETAILS

International Bank for Reconstruction and Development (IBRD)	667.00
International Development Association (IDA)	83.00
IDA Credit	83.00

INSTITUTIONAL DATA

Climate Change and Disaster Screening

This operation has been screened for short and long-term climate change and disaster risks

Overall Risk Rating

Moderate

RESULTS

	Baseline	Target
Pillar 1: Catalyzing long term private sector finance		
Total volume of loans disbursed by the National Bank for Financing Infrastructure and Development (NaBFID) for the infrastructure sector (Rs. billion)	Rs. 0 (June 2022)	Rs. 1,000 billion (June 2024)
Total funds raised through monetization of brownfield assets included under the National Monetization Pipeline (Rs. billion)	Rs. 960 billion (FY2021-22)	Rs. 1,500 billion (FY2022-23)
Volume of Pass-through Certificate (PTC) Residential Mortgage-Backed Securities (RMBS) securitization transactions (Rs. billion)	Rs. 73.8 billion (FY 2021-22)	Rs. 100 billion (FY 2022-23)
Pillar 2: Developing the markets for green finance		
Volume of sovereign green bond issuances (Rs. billion)	Rs. 0 (March 2022)	Rs. 230 billion (June 2023)
Share of top 1,000 listed companies complying with enhanced environmental, social and governance (ESG) disclosure requirements (percent)	0 (March 2022)	100 percent (June 2024)
Trading Platform established to facilitate the National Carbon Market (Yes/No)	No (March 2022)	Yes (June 2024)
Pillar 3: Improving access to credit for Micro, Small & Medium Enterprises (MSMEs) and women entrepreneurs		
Volume of incremental guarantee covers under Credit Guarantee Fund Trust for Micro and Small Enterprises (CGTMSE) (Rs. billion)	Rs. 368.9 billion (FY 2020-21)	Rs. 500 billion (FY 2022-23)
Volume of guarantees under CGTMSE approved toward loan accounts of women entrepreneurs (Rs. billion)	Rs. 51.6 billion (FY 2020-21)	Rs. 75 billion (FY 2022-23)
Total lending under Credit Guarantee Scheme for Micro-Finance Institutions (CGSMFI) primarily to women borrowers (Rs. billion)	0 (July 2021)	Rs. 90 billion (July 2022)

IBRD PROGRAM DOCUMENT FOR A PROPOSED LOAN TO INDIA
CATALYZING PRIVATE FINANCING FOR SUSTAINABLE RECOVERY AND GROWTH

1. INTRODUCTION AND COUNTRY CONTEXT

1. **India's ability to rebound from the pandemic and to realize its ambitious growth targets critically depends on having a deep and efficient financial system, capable of meeting the country's large investment needs and catalyzing inclusive and sustainable growth.**[1] The proposed Development Policy Loan (DPL) of US$750 million to the Government of India (GoI) aims to support the continued transformation of the financial sector so that it catalyzes and intermediates sustainable private financing more effectively, in support of the real economy. Specifically, the policies supported by this operation are expected to help mobilize private finance for infrastructure and housing sectors, deepen the markets for green finance, and improve access to credit for Micro, Small & Medium Enterprises (MSMEs) and women entrepreneurs. The proposed DPL builds on extensive policy dialogue, analysis and Technical Assistance (TA) conducted by the World Bank Group (WBG) in these areas in recent years.

2. **India's financial sector is relatively stable and inclusive.** Over the past decade the GoI has pursued an ambitious reform agenda with the goal of deepening financial inclusion, enhancing the efficiency and stability of the financial sector, and strengthening domestic capital markets to attract long-term financing. The GoI has been making efforts to ensure that the financial sector is more efficient and resilient through the restructuring of large Public Sector Banks (PSBs), strengthening the oversight of Non-Bank Financial Companies (NBFCs), and using an improved insolvency framework and other measures to address the legacy of Non-Performing Assets (NPAs).[2] The financial sector has remained resilient in the face of COVID-19 and other shocks, in part due to a rapid and strong response of the GoI and the regulators, with banks and NBFCs being capitalized well above the regulatory threshold. At the same time, a series of ground-breaking initiatives (digital ID, fintech innovations) have resulted in much improved levels of financial inclusion, including for the poor and traditionally underserved. Finally, ongoing reforms in the capital market space focus on enabling new financing instruments, streamlining the regulatory environment to enable capital market liquidity, and attracting institutional investors to finance India's development needs.

3. **Notwithstanding this progress, credit growth has been decelerating in recent years, resulting in persistent financing gaps in critical sectors.** India has savings levels comparable to emerging market peers such as Brazil, Malaysia, and South Africa, but a much lower level of private sector credit, which means that the financial sector needs to be more effective in intermediating savings to support growth. Moreover, credit growth in India has been decelerating over the past decade, reflecting the risk aversion among lenders in the aftermath of a twin balance sheet problem and various structural impediments in the financial system.[3] This results in chronic financing gaps in sectors critical for growth such as infrastructure and MSMEs. The annual infrastructure finance gap in India is estimated at 4 percent of Gross Domestic Product (GDP), while the share of private sector finance in infrastructure has been falling, from 37 percent of total infrastructure financing to 25 percent between 2008 and 2019, and that gap has likely worsened following COVID-19. The financing gap for MSMEs is estimated between Rs.18–25 trillion[4], and almost half of all MSMEs do not have access to formal credit, with the situation worsened by the impact of the pandemic.

[1] The GoI's current medium-term goal is to make India a US$5 trillion economy by 2024–25 (compared to US$2.7 trillion in 2020).
[2] This includes the plans for potential divestiture of several state-owned financial institutions, announced in 2021.
[3] India's "twin balance sheet problem" refers to combination of over-leveraged companies and NPA-burdened bank balance sheets. During the boom period in the first decade of this century, companies saw rapid growth fueled by easy credit from PSBs. However, as credit conditions tightened in the early 2010s, corporates were left with high levels of debt, while PSBs struggled with a large stock of NPLs.
[4] Financing India's MSMEs: Estimation of Debt Requirement of MSMEs in India, IFC, 2018

4. **Although India has made remarkable progress in reducing absolute poverty in recent years, including due to the allocation of significant resources for social assistance programs, the COVID-19 outbreak has delayed the course of poverty reduction.** Between 2011–12 and 2020–21, India's poverty rate has declined from 22.5 percent[5] to values estimated between 9 and 12.3 percent. However, projections of GDP per capita growth suggest that this estimated decline also includes a reversal of poverty reduction due to the pandemic. Labor market indicators from high frequency surveys—including from the Centre for Monitoring Indian Economy—suggest that vulnerability has increased after the pandemic, particularly for urban households, with a moderate recovery in 2021. Overall, the pandemic and its economic impacts are estimated to have raised urban poverty, creating a set of "new poor" that is relatively more likely to be engaged in the non-farm sector and to have received at least secondary education. To respond to the pandemic, the GoI has deployed significant resources as part of the Prime Minister Garib Kalyan Yojana for social assistance, including for urban poor households and migrants.

5. **India is one of the countries most vulnerable to climate change.** The Global Climate Risk Index 2021 ranks India as the 7th most impacted nation. The country is expected to experience increasing climate variability with hazards projected to increase in frequency and intensity (such as floods, droughts, and cyclones), which will adversely impact human development, economic growth, and resources. In the context of the operation's goal to catalyze private finance and enhance financing for infrastructure and MSMEs, the mounting impacts of climate change pose substantial risks to the financial system's stability and could lead to massive economic losses, including losses incurred by MSMEs and damages to infrastructure. Thus, investments in enhancing finance for development should account for the impacts of climate change and ensure mitigation of such impacts.

2. MACROECONOMIC POLICY FRAMEWORK

2.1. RECENT ECONOMIC DEVELOPMENTS

6. **India's economy recovered in Fiscal Year (FY) 21/22, supported by a targeted macroeconomic policy response and a successful vaccination strategy.** After the deep recession in FY20/21, India was hit hard by the 'second wave' of COVID-19 last year. However, recovery, supported by increased vaccine deployment and a well-crafted fiscal and monetary response, has been quick. The real gross domestic product (GDP) in FY21/22 reached the pre-pandemic level in FY19/20. Growth is yet to be broad-based across all components. Growth in private consumption (7.9 percent year-on-year) remained sluggish, constrained by weakness in the labor market.[6] Frequent mobility restrictions have exacted a significant economic toll on low-income households, unskilled workers, and the informal sector. The recovery in investment (12.9 percent) was strong, bolstered by the surge in the GoI's capital spending.

7. **Headline inflation has increased on the back of oil and commodity price shocks, albeit within the tolerance range of the central bank (2–6 percent) in FY21/22.** Inflation averaged 5.5 percent y-o-y in FY21/22 largely due to cost-push factors: higher global oil prices, pandemic-related disruptions in the food supply chain, shipping container shortages and delay in the normalization of services due to successive waves of mobility restrictions. Core inflation remained elevated and sticky through FY21/22, averaging 6 percent, but demand-pull pressures were largely subdued. The government reduced import duties on edible oils and taxes on oil prices, which dampened inflation during the second half of FY21/22. Nonetheless, rising fuel prices and disruptions in domestic food supplies pushed inflation to 7 percent y-o-y in March 2022 and 7.8 percent y-o-y in April, significantly above the Reserve Bank of India's (RBI) tolerance range. India imports the bulk of its domestic crude oil requirement, but the high

[5] Consumption Expenditure Survey 2011-12, National Sample Survey Office (NSSO), Government of India.
[6] World Bank staff estimates.

global price of crude oil impacted domestic prices with a delay. India managed to use its strategic oil reserves and purchase oil at discounted prices from Russia. Food prices, which account for nearly half the Consumer Price Index (CPI) basket, remain elevated as supply chain problems related to the war in Ukraine disrupted global grain production, supply of edible oils and fertilizer exports.

8. **The RBI's policy focus has shifted toward managing inflationary pressures, but growth remains a concern.** To support the economy during the national lockdown from April to June 2020, preserve financial stability and stabilize borrowing costs for the central and state governments, the Monetary Policy Committee had cut the repo rate by a cumulative 115 bps and took additional regulatory measures to increase liquidity between March and May 2020.[7] Notwithstanding the increasing price pressures during FY21/22, the RBI maintained an accommodative stance and kept the policy rate unchanged to support growth. The RBI did, however, take steps toward policy normalization by winding down the government bond buying program (Government securities acquisition programme) and conducting operations in the term money market to realign the policy rate and the target overnight money market rate. In April 2022, the central bank reduced the size of the policy corridor to the pre-pandemic level by introducing a new instrument, the Standing Deposit Facility, which allows the RBI to borrow from commercial banks without collateral in place. In a mid-cycle decision meeting in early May, the RBI raised its key policy rate (repo rate) by 40 bps, to mitigate the second-round effects of supply constraints on inflation, keep long-run inflation expectations anchored and preserve macro-financial stability in view of increased volatility in global financial markets. However, the monetary policy stance remains accommodative with the focus on withdrawal of accommodation to manage inflationary pressures while supporting growth.

9. **The financial system remains stable, but vulnerabilities exist in some segments**. As per the RBI's latest Financial Stability Report (FSR, December 2021), the gross non-performing assets (GNPA) ratio of banks declined from 8.4 percent in March 2020 to 6.9 percent in September 2021. The performance of banks, particularly that of the public sector banks, has improved significantly with return on assets (ROA) and return on equity increasing across the board. Thus, the banks are in a better position to support credit growth, which turned around in the third quarter of FY21/22. However, the rebound in credit has not been broad-based. While the systemic risk in the banking sector is low, the forbearance measures related to COVID-19 (although mostly phased out by now) and the GoI's emergency support to MSMEs may have delayed the recognition of bad loans. As noted in the FSR, there are non-systemic risks in NBFCs and urban cooperative bank market segments due to dented asset quality and funding structure. The GNPA ratio of the NBFCs, which had declined in September 2020 due to regulatory forbearance, increased slightly to 6.5 percent in September 2021. Furthermore, the GNPA ratio in the industry sector, accounting for the largest share of the NBFC loan portfolio, rose from 6.7 per cent in March 2021 to 7.9 per cent in September 2021. However, the ROA of the NBFCs improved to 1.7 percent in September 2021 from 1.3 percent in March 2021. On the upside, the creation of an asset reconstruction company and further reforms in the insolvency process are expected to contribute to the faster resolution of bad loans, once these measures are operationalized. RBI is also seeking to mitigate the risks in the NBFC sector by tightening regulations for large NBFCs (effective October 2022), which is expected to lead to higher capitalization levels and improved governance.

10. **Rebounding economic activity turned the current account balance into a deficit but it remains adequately financed.** In contrast to a surplus of 0.9 percent of GDP in FY20/21, the current account balance showed a deficit

[7] The main steps include targeted long-term repo operations (TLTRO), cutting the cash-reserve ratio and increasing the overdraft limits for the central and state governments. The RBI also allowed for a 6-month loan moratorium and Non-Performing Loans standstill through August 31, 2020, followed by a special restructuring scheme. Post the "second wave", the RBI took new steps to aid Small Finance Banks, increase credit to MSMEs/Micro-Finance Institutions and to the healthcare sector, and introduced resolution framework 2.0 for stressed assets of small businesses.

of 1.2 percent of GDP in the Q1-Q3 FY21/22 (April-December), with import growth driven by rising commodity prices and a pickup in investment, outpacing export growth. The current account balance has been financed by a strong inflow of foreign direct investment (FDI) and portfolio flows, at least until the start of Q3 of FY21/22. The top sectors, receiving 49 percent of total FDI inflow in FY21/22, were services, computer hardware and software, telecommunication, trading, and automobile industry. In contrast, net portfolio investment worth US$ 21.5 billion (3.5 percent of foreign exchange reserves) has exited India's financial market since October 2021; initially due to the U.S. Federal Reserve's forward guidance on policy tightening, which intensified after the start of the conflict in Eastern Europe. The foreign exchange reserves, at around US$ 603 billion (about 14.8 months of import cover) as of mid-April, have cushioned domestic financial markets against global volatility and uncertainty since October 2021.

11. **The fiscal deficit narrowed despite higher capital spending.** A targeted fiscal stimulus supported the economy over the last two years. Since the beginning of FY21/22, the focus of fiscal policy shifted from mitigating the impact of the pandemic through targeted interventions, toward increased capital spending to crowd-in private investment. The capital expenditure of the central government grew by 27 percent y-o-y over the first three quarters of FY21/22, while growth in current spending was relatively modest at 8 percent. Supported by strong growth in revenue, the general government fiscal deficit is likely to decline to 10.9 percent in FY21/22, after peaking at 13.3 percent in FY20/21. Tax revenues growth was driven by income taxes, in particular corporate tax, as well as GST revenues on the back of improvements in the profitability of large corporates but also increased compliance. The public debt is estimated to have declined by 1.7 percentage points of GDP to 86.9 percent of GDP in FY21/22.

2.2. MACROECONOMIC OUTLOOK AND DEBT SUSTAINABILITY

12. **Spillovers from the war in Ukraine will impede economic recovery in India.** Amid the oil price shock, moderating global growth, and higher investor uncertainty, India's economy is expected to grow by 8 percent in FY22/23, one percentage point below the pre-conflict forecast. Private consumption growth will remain sluggish in FY22/23 due to slow growth in household disposable income, which in turn stems from incomplete recovery of the labor market and elevated inflation. Investment will benefit from increased capital spending by the government, a resilient financial sector, and government initiatives including the production–linked incentive scheme leading to a stronger multiplier effect on jobs and income, higher productivity. Net exports are expected to be a drag on GDP growth, with a high import bill and exports softening due to moderating global growth. However, if the current disruptions to energy supplies and negative impacts on confidence linked to the conflict persist and global growth and supply chains are significantly affected, India's growth will need to be further revised down. The recent and ongoing crises may also result in longer-term scarring and lowering of potential growth.

13. **There are considerable upside risks to inflation amid renewed supply disruptions.** Following a series of exceptional price shocks, the war in Ukraine implies that headline inflation is projected to remain at very high levels in the coming months, before easing toward the RBI's upper bound of the tolerance range at the end of the calendar year 2022. Compared with the pre-war forecast, inflation has been revised upward substantially, especially in 2022. While inflation is expected to average 5.5 percent for FY22/23 (April 2022–March 2023), there are significant upside risks to this forecast: (i) persistent upward pressures in prices of energy, food and other commodities; (ii) supply disruptions like shortages of crude oil and of key chemicals used in fertilizer production; and (iii) heightened inflation expectations and second-round effects from large commodity price shocks. These effects will more than offset the negative impact on inflation of a significant hike in the interest rates, the negative demand-related effects of the war in Ukraine and the central government's measures aimed at managing price pressures.

14. **The current account deficit will widen substantially amid moderating global growth and elevated commodity prices, but foreign exchange reserves will provide a cushion against external shocks.** Surging prices of crude oil and other commodities will push up the import bill while merchandise export growth is likely to soften as global growth moderates. This will only be partially offset by resilient services exports. Thus, the current account deficit is projected to widen from 1.2 percent in FY21/22 to 2.5 percent in FY22/23. Capital flows, especially foreign direct investment inflows, are expected to remain steady— given the reforms to improve the investment climate in India. The risk of large capital outflows appears to be moderate due to the relatively lower total accumulated portfolio investment liabilities (owed by India to the world) and a more stable mix of foreign capital inflows coming into the economy. India has maintained large foreign exchange reserves (see paragraph 10), which will cushion against external shocks. Lastly, the exchange rate which is largely market determined (but with the RBI intervening to manage volatility), will also help to absorb external shocks, particularly by supporting India's exports.

15. **Fiscal policy will chart a path of gradual fiscal consolidation with a greater focus on infrastructure spending.** Even as capital spending increases, the general government deficit is projected to decline by 1.3 percentage points of GDP to 9.6 percent of GDP in FY22/23. This is due to: (i) continued revenue growth (aided by domestic demand, excise and increased compliance); and (ii) a decline in current spending as a share of GDP (driven by lower spending on some welfare measures such as the rural employment guarantee program). India's Union Budget FY22/23 focuses on infrastructure development to stimulate growth and crowd in private investment. While the public sector borrowing requirement is high (it will increase in nominal terms in FY22/23), the risk of crowding out is low as there is still ample liquidity in the financial system and growth remains below potential. The budget for FY23 is based on credible revenue targets and the government continues in its efforts to improve budget transparency by keeping previously off-budget spending in the budget, limiting downside surprises. The fiscal deficit will be reduced only gradually, due to the expansion of public investment and likely absorption of a share of the increase in oil prices in the form of lower taxes on fuel. The domestic market's capacity to absorb a larger government borrowing program is also reflected in the relatively small increase in benchmark bond yields after the budget announcement on the size of the borrowing program. The budget has also provided additional capital in credit guarantee funds in anticipation of any calls on the credit guarantees issued as part of the stimulus packages in previous years.

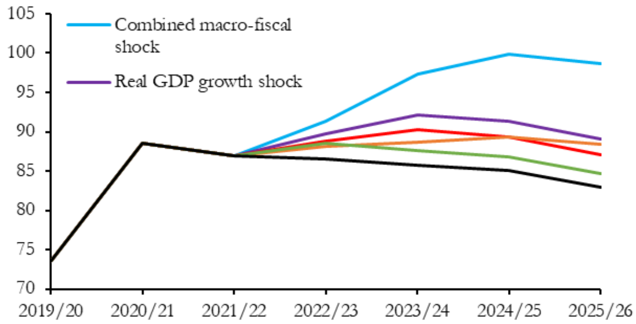
16. **The financial sector outlook remains stable, with credit growth expected to recover further, although asset quality may deteriorate somewhat reflecting the impact of the pandemic.** Bank credit growth is expected to rebound to 11–12 percent in FY22/23, compared to 9.7 percent in FY21/22, supported by recovering levels of economic activity, and launch of the Production Linked Incentive scheme for 13 key sectors. At the same time, the declining NPA trend over the past few years may reverse as the temporary effect of pandemic relief measures wears off, including moratoriums as part of debt restructuring. However, the latest available FSR by RBI forecasts a relatively moderate increase in NPAs to 8.1 percent in September 2022 (from 6.5 percent in September 2021) in a baseline scenario. The RBI furthermore estimates that all banks will be able to maintain capital adequacy above the regulatory threshold even under severe stress scenario, thanks to large amounts of capital raised by banks in the last two years.

17. **India's debt remains sustainable but is subject to heightened risks from macroeconomic uncertainty and contingent liabilities.** Under a baseline scenario, the general government debt-to-GDP ratio is projected to decline gradually to 85 percent in FY24/25 from 86.9 percent in FY21/22. In a combined macro-fiscal shock scenario, the debt-to-GDP ratio would increase steadily to nearly 100 percent (Figure 1). Contingent liabilities have also increased

substantially over the past two years[8] as the government announced credit guarantee programs amounting to over 4.5 percent of GDP to support vulnerable sectors like MSMEs. Notwithstanding these risks, the debt position remains sustainable. India's public debt is mostly domestic (only 4.5 percent of public debt is external), of medium- or long-term maturity, and held by residents. The weighted average maturity of central government debt is 11.7 years; only 4.6 percent is maturing within 1 year and 30 percent is maturing within 5 years. India's external debt is moderate at around 21 percent of GDP, and rollover risks are limited.

Figure 1. India Public Debt: Baseline and Stress-Test Scenarios

(General government debt-to-GDP ratio, percent)



Source: RBI, Ministry of Finance, WB staff calculations

Note: The combined macro-fiscal shock is the combined impact of the real-GDP growth shock (a decline of 4 percentage points in FY22/23 and FY23/24), fiscal shock (a 1.9 percentage point increase in FY22/23 and FY23/24) and interest rate shock (an increase by 2 percentage points throughout the forecast period).

18. **India's macroeconomic policy framework is considered adequate for development policy financing, reflecting solid fundamentals and capacity to respond.** The outlook for domestic activity and inflation has become very uncertain. It depends crucially on how the war in Ukraine unfolds, but the risks are mitigated by strengthening economic fundamentals and a robust policy framework. The financial sector entered the crisis well-capitalized, and the authorities took critical measures to ensure stability and liquidity. In recent years, the monetary policy framework has been strengthened, and while India is not immune to external financial developments, high reserve levels and limited external financing needs provide adequate buffers. In support of recovery, the government has used existing fiscal space prudently, accompanied by structural reforms. Public debt remains sustainable (and relatively resilient to different shocks) despite the large one-off increase in FY20/21 (see Tables 1–3). Thus, while significant risks remain, the GoI and the RBI have proven to have the capacity to respond swiftly and adequately.

Table 1. India: Selected Economic Indicators FY17/18–FY25/26

Key Macroeconomic Indicators	**FY17/18**	**FY18/19**	**FY19/20**	**FY20/21**	**FY21/22 Estimate**	**FY22/23 Forecast**	**FY23/24 Forecast**	**FY24/25 Forecast**	**FY25/26 Forecast**
Real Economy	(Annual percentage change unless otherwise Indicated)								
Nominal GDP (local currency)	11.0	10.6	6.2	-1.4	16.9	13.3	12.6	12	12.5
Real GDP	6.8	6.5	3.7	-6.6	8.3	8.0	7.1	6.5	6.8
Contributions to growth (percentage points)									
Consumption	4.7	4.7	3.3	-3.0	4.7	5.5	4.8	4.9	5.0
Investment	2.4	3.5	0.5	-3.3	3.9	3.2	2.7	2.8	3.0
Net exports	-2.8	0.3	-0.5	1.4	-2.9	-1.1	-0.7	-1.6	-1.2
CPI average	3.6	3.4	4.8	6.2	5.5	5.5	4.9	4.2	4
Fiscal accounts (General Government)	(Percent of GDP)								

[8] Data limitations do not allow for quantifying the total size of explicit and implicit contingent liabilities in India. The World Bank is working on this issue.

Overall balance	-5.9	-5.8	-7.2	-13.3	-10.9	-9.6	-8.5	-8.0	-7.5
Total Liabilities	69.8	68.6	73.7	88.6	86.9	86.5	85.8	85	82.9
Selected monetary accounts	(Annual percentage change unless otherwise indicated)								
Interest rate (Repo rate and period average)	6.1	6.3	5.4	4.0	4.0	4.5	5.0	5.0	5.5
Balance of payments	(Percent of GDP, unless otherwise indicated)								
Current account balance	-1.8	-2.1	-0.9	0.9	-1.2	-2.5	-2.0	-1.7	-1
Imports	22.1	23.8	21.4	19.3	23.1	22.7	23	23.5	22.9
Exports	19	20.2	18.8	18.8	20.6	20.3	20.8	20.9	20
Foreign direct investment (net)	1.1	1.1	1.5	1.6	1.6	1.5	1.6	1.6	1.7
Gross reserves (in US$ billion, end of period)	424.5	412.9	477.8	576.9	614	607.1	622.5	648.2	--
In months of next year's imports	7.9	8.2	11.1	9.7	9.5	8.3	7.4	--	
External debt	20.1	19.9	20.6	21.2*	—	—	—	--	
Other memo items									
Nominal GDP in Rs. (trillions)	170.9	189	200.7	198	231.4	262.2	295.2	330.6	371.9

Source: India National Statistics Office, Staff calculations.

Table 2. India: Selected Fiscal Indicators FY17/18–FY25/26

Key Fiscal Indicators	FY17/18	FY18/19	FY19/20	FY20/21	FY21/22	FY22/23	FY23/24	FY24/25	FY25/26
	Actual	Actual	Actual	Actual	Forecast	Forecast	Forecast	Forecast	Forecast
Central Government									
Overall balance	-3.5	-3.4	-4.6	-9.2	-6.9	-6.4	-5.5	-5.0	-4.5
Primary balance	–0.4	–0.4	-1.6	-5.8	-3.3	-2.8	-2.0	-1.6	-0.8
Total Receipts	*13.0*	*12.8*	*11.8*	*11.7*	*12.4*	*12.0*	*12.4*	*12.5*	*12.6*
Tax revenues, *in which*	11.2	11.0	9.9	10.3	10.6	10.7	10.9	10.8	10.9
Taxes on goods and services	*4.6*	*4.3*	*4.1*	*4.8*	*4.4*	*4.4*	*4.6*	*4.5*	*4.6*
Taxes on income and profits	*5.8*	*6.0*	*5.2*	*4.8*	*5.4*	*5.5*	*5.5*	*5.6*	*5.6*
Non-tax revenues	1.1	1.2	1.6	1.1	1.4	1.1	1.1	1.2	1.2
Expenditures	16.5	16.3	16.4	20.8	19.4	18.5	17.9	17.5	17.1
Current expenditures, *in which*	15.0	14.7	14.8	18.6	16.8	15.6	14.9	14.5	14.1
Interest payments	3.1	3.1	3.0	3.5	3.6	3.6	3.5	3.4	3.5
Others (salaries, supplies)	7.9	7.5	8.5	12.2	10.0	9.8	8.2	7.9	7.6
Capital expenditures	1.5	1.6	1.6	2.2	2.6	2.9	3.0	3.0	3.0
Central Government Financing	3.5	3.4	4.6	9.2	6.9	6.4	5.5	5.0	4.0
External (net)	0.0	0.0	0.0	0.4	0.1	0.1	0.0	0.0	0.0
Domestic (net)	3.5	3.4	4.6	8.8	6.8	6.3	5.5	5.0	4.0
State Governments									
Overall balance	-2.4	-2.5	-2.6	-4.1	-4.0	-3.2	-3.0	-3.0	-3.0
Revenues	13.8	14.1	13.4	14.2	15.0	14.8	14.6	14.5	14.5
Expenditures and net lending	16.2	16.6	16.0	18.3	19.0	18.0	17.8	17.5	17.5
Total Liabilities									
General Government	69.8	68.6	73.7	88.6	86.9	86.5	85.8	85.0	82.9

Table 3. India: BOP and external financing requirements

External financing requirements	FY17/18	FY18/19	FY19/20	FY20/21	FY21/22	FY22/23	FY23/24	FY24/25	FY25/26
	Actual	Actual	Actual	Actual	Proj.	Proj.	Proj.	Proj.	Proj.
(in percent of GDP)									
1. Financing Requirements (i-ii)	1.8	2.1	0.8	-0.9	1.2	2.5	2.0	1.8	1.0

i. Current Account Deficit*	1.8	2.1	0.9	-0.9	1.2	2.5	2.0	1.7	1.0
ii. Net Errors and Omissions	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
2. Financing Sources (i+ii)	1.8	2.1	0.8	-0.9	1.2	2.5	2.0	1.8	1.0
i. Capital Account Balance (a+b+c)	3.4	2.0	2.9	2.2	2.3	2.3	2.3	2.3	2.0
a. Net Foreign Direct Investment	1.1	1.1	1.5	1.6	1.6	1.5	1.6	1.6	1.7
b. Net Portfolio Investment	0.8	-0.1	0.0	1.4	0.1	0.2	0.2	0.2	0.1
c. Net All Other Flows**	1.5	1.0	1.4	-0.8	0.6	0.6	0.5	0.5	0.2
ii. Change in reserve assets (1-2.i)	-1.6	0.1	-2.1	-3.3	-1.1	0.2	-0.3	-0.6	-1.0
3. External Financing Gap (1-2)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0

Source: Reserve Bank of India and staff calculations.
Note: *: Includes merchandise and invisibles. **: All other flows include short- and long-term debt flows (external assistance, commercial borrowings and trade credits) and banking capital. Positive change in reserves indicates a decline.

Intergovernmental Relations

19. **India has a federal system of government with clear separation of taxation and spending powers.** The Constitution has demarcated the taxation powers of both levels of government, while borrowing and foreign exchange entitlements are controlled by the central government. [9] State governments are not allowed to borrow directly from foreign sources. States are fiscally dependent on the central government, and their borrowing is limited by the Fiscal Responsibility and Management Act, 2003. The fiscal relationship between the Center and the states is reflected in the devolution of central taxes and additional assistance in the form of grants from the Center to the states. Tax devolution (share of central taxes to states) is recommended by the Finance Commission.[10] Grants (to states) are composed of centrally sponsored schemes, block grants (additional central assistance for special and other programs), and grants (to states and local governments) as recommended by the Finance Commission.

2.3. IMF RELATIONS

20. **The International Monetary Fund (IMF) does not have an active lending program in India.** However, it carries out macroeconomic supervision and Article IV consultations twice yearly. The WB and IMF teams regularly exchange views and information. The most recent Article IV consultation report was completed on August 31, 2021. It commended the Indian authorities for advancing structural reforms despite the pandemic and stressed the need for steadfast implementation. These reforms would not only help maximize India's long-term growth and demographic dividend, but also help alleviate poverty and inequality, and deepen the country's integration into global value chains. India's progress toward transitioning to a greener and more inclusive economy is welcome.

3. GOVERNMENT PROGRAM

21. **The GoI's current economic program puts strong emphasis on fostering infrastructure development, as the sector has a high multiplier impact and is considered critical to achieve India's growth ambitions.** In the FY23 Union Budget, the government announced a 35 percent increase in capital spending to Rs. 7.5 trillion (US$100 billion), with the intention of leveraging the multiplier effect of infrastructure spending.[11] The boost in capital spending is part of the GoI's more comprehensive strategy for the infrastructure sector, which includes: (i) the

[9] Under Article 293(3) of the Constitution, "A State may not without the consent of the Government of India raise any loan if there is still outstanding any part of a loan which has been made to the State by the Government of India or by its predecessor Government, or in respect of which a guarantee has been given by the Government of India or by its predecessor Government".
[10] The 15th Finance Commission recommendations were submitted to Parliament in February 2021 for a five-year period starting April 2021. They recommended maintaining the states' share in the central tax pool at 41 percent and invoked greater horizontal equalization by compensating states with higher population and forest cover while rewarding better tax efforts and lower fertility rates.
[11] The multiplier effect indicates that an increase in capital expenditure by the central and state governments by one rupee each crowds in private investment, induces a more than proportionate increase in investment in the economy, and leads to an increase in overall output by 3.25 rupees and 2.0 rupees, respectively. Source: *https://www.rbi.org.in/Scripts/PublicationsView.aspx?id=18941*.

launch of the National Infrastructure Pipeline (NIP) to provide a clear roadmap to local and foreign investors for their participation in Indian infrastructure assets; (ii) the launch of the Prime Minister's GatiShakti National Master Plan for coordinated infrastructure planning and execution by GoI ministries; (iii) the establishment of a new Development Finance Institution (DFI) to act as a provider, enabler and catalyst for infrastructure financing; (iv) the launch of the National Asset Monetization Pipeline (NMP) to facilitate mobilization of funds by using innovative financing structures such as Infrastructure Investment Trusts (InVITs) for existing brownfield and operational infrastructure assets; (v) the launch of capacity building initiatives at the federal and state levels to facilitate better appraisal, financing, and implementation of infrastructure projects; and (vi) initiatives to deepen the corporate bond market to facilitate long-term financing and patient capital from institutional investors into the infrastructure sector.

22. **The GoI has taken multiple steps to enhance housing finance as part of its "Housing for All" agenda**. The role of the National Housing Bank (NHB), the housing finance DFI in India, has been rationalized by transferring regulation of Housing Finance Companies (HFCs) from NHB to RBI, which allowed NHB to focus on raising financing through innovative mechanisms for HFCs and other lenders, in particular for the affordable housing market. The NHB, with support from the WBG, is working on the development and operationalizing of a multi-originator RMBS platform to deepen the PTC market to allow HFCs and other lenders to access sustainable long-term funding from a wider base of institutional investors, as well as reduce dependence on bank funding.

23. **Climate change mitigation and adaptation is an important goal in the GoI's economic program, with increasing focus on mobilizing green and resilient financing.** The GoI has been working toward mobilizing funding for climate adaptation and mitigation objectives. In early 2022, the GoI has announced plans to launch sovereign green bonds to boost the development of the domestic green bond market through improved benchmark pricing and liquidity and a demonstration effect for local issuers. In parallel, the authorities are working on revamping the guidelines for issuance of corporate green bonds. These initiatives are being complemented by improved Environmental, Social, and Governance (ESG) disclosures by listed firms and financial sector participants, aimed at improving transparency and investor confidence.

24. **Another critical area of focus for the GoI is to support the resilience and recovery of the MSME sector, including women-led firms, from the impact of the pandemic**. The MSME sector is one of the largest non-agricultural employers in the country and its share in GDP is around 30 percent; yet it was hard hit by several waves of the pandemic. The GoI has relied on several established and new credit guarantee schemes to maintain vital flow of financing to these borrowers, with special attention to the worst-affected sectors, such as the contact-intensive sectors and women-led MSMEs. As per rapid surveys conducted in June and July 2021, during the pandemic, 11.5 percent of women-led enterprises were permanently closed, and 36 percent were temporarily closed. Even before the pandemic hit, women-led businesses in India experienced disparities in access to finance, business networks, skills, and technology. Estimates on lending from public sector banks indicate that of the total credit outstanding to micro and small enterprises, only 5.2 percent go to women-owned enterprises. Thus, to address such financial disparities, the GoI has been focusing on de-risking lending to women-led MSMEs through various guarantee schemes.

4. PROPOSED OPERATION

4.1. LINK TO GOVERNMENT PROGRAM AND OPERATION DESCRIPTION

25. **The proposed DPL aims to catalyze sustainable private sector financing for India's economy, with the focus**

on infrastructure and MSMEs. The proposed operation is comprised of three pillars:

- Pillar 1 builds on the GoI's strong commitment to crowd in private long-term financing for infrastructure and housing sectors through measures such as the creation of a catalytic DFI for the infrastructure sector, the launch of the NMP, and the establishment of a securitization platform for the housing sector. These measures are essential to address India's longstanding financing gaps in infrastructure and housing by crowding in private sources of financing to reduce pressure on public finances.
- Pillar 2 supports the GoI's Nationally Determined Contributions (NDC) and COP26 commitments by focusing on the financial sector as means of attracting capital and investment for green projects through a sovereign green bond; ensuring that investors are able to target their funding toward sustainable projects and firms; and developing the domestic carbon trading market.
- Finally, Pillar 3 reflects the GoI's commitment to assist productive MSMEs that were impacted by the pandemic, including women entrepreneurs. The objective is to ensure that financing continues to flow to viable firms, existing jobs are preserved, and new jobs are created.

26. **The policy initiatives supported under this DPL are complementary and interconnected.** In particular, the improved infrastructure financing mechanisms are expected to facilitate investments toward green projects consistent with India's newly formulated climate change mitigation and adaptation goals. For instance, the new infrastructure DFI should play an important role in the NMP implementation by helping to mobilize private capital for brownfield assets. Proceeds raised from the issuance of sovereign green bonds are expected to be primarily deployed toward resilient and environmentally sustainable infrastructure projects. The first sovereign green bond will also provide impetus to the private green bond market, thus leading to increased participation of long-term institutional investors in the NMP. The proposed results indicators for this operation reflect the WB team's estimates, made on the basis of the available official and market data, of the progress expected in the above-mentioned policy areas over the next two years.

27. **The reforms supported under the DPL build on the extensive prior policy dialogue and TA the WBG had with relevant counterparts**. In particular, the WB's work over the past two years with the Department of Economic Affairs' (DEA) Infrastructure and Financial Markets Divisions has helped in identifying key policy enablers that will be most critical for bringing long-term, local currency investors to India's infrastructure projects. Similarly, the reform program for MSMEs and housing finance is the continuation of a longstanding lending and TA program supporting the Small Industries Development Bank of India (SIDBI), the National Housing Bank and CGTMSE, and also stems from recommendations of the RBI Expert Committee on MSMEs and the RBI Committee on Housing Finance.

4.2. PRIOR ACTIONS, RESULTS AND ANALYTICAL UNDERPINNINGS

Pillar 1: Catalyzing long term private sector finance

28. **The reforms under Pillar 1 help address India's chronic long-term financing gaps in infrastructure and housing.** To this end, the main objective of the proposed measures is to support a shift in the financing composition from over-reliance on public sources (i.e., state budget and PSBs) to greater leveraging of private sector financing, including from long-term institutional investors. The establishment of a well-managed infrastructure DFI, with the mandate to crowd in the private sector, and the introduction of e new instruments such as NMP to mobilize private and institutional investor financing for infrastructure, are expected to make infrastructure projects more bankable and investor-friendly. At the same time, by enabling access to capital markets for the HFCs, this Pillar will support the scaling up of housing finance, including for the low-income and informal segments.

Prior Action #1: The Borrower has established the National Bank for Financing Infrastructure and Development (NaBFID), as a development financial institution with the mandate of offering credit enhancement products and mobilizing long term private finance for the infrastructure sector, pursuant to which (i) the Government of India has allocated capital; and (ii) NaBFID shall be regulated and supervised by the Borrower's central bank, RBI.

29. **Prior to the onset of the COVID-19 pandemic, India spent around 4–5 percent of its GDP on infrastructure (public plus private), well below the levels required which are estimated at about 7–8 percent of GDP.**[12] This gap reflects over-reliance on bank financing and a lack of adequate private sector participation. Due to asset-liability mismatches, India's commercial banking sector has been constrained in offering the long-term financing instruments required for infrastructure projects. In addition, a legacy of non-performing infrastructure assets and high-profile defaults over the past decade have resulted in risk aversion and a lack of confidence of the private sector to participate in infrastructure financing. Meanwhile, the Indian market currently lacks the credit enhancement products which could help improve the credit profile of infrastructure projects and mitigate investor concerns. A large infrastructure investment gap has hence been prevalent in India, with the country ranking low (70th out of 141 countries) in terms of infrastructure quality in the Global Competitiveness Index.

30. **Prior Action (PA) 1 supports the establishment of NaBFID, a national infrastructure development bank, which is expected to catalyze long term finance by de risking projects and leveraging private finance.** Based on the experience from other countries (e.g., Colombia and Malaysia), a well-established infrastructure DFI could help in leveraging private sector financing at scale, by assembling specialized expertise in a single institution, with a broad mandate (structuring, financing support, credit enhancement) of providing end-to-end support for making projects commercially viable and attractive to private sector investors. The design of NaBFID, as envisioned in its founding Act[13], seeks to establish a professionally run institution focused on mobilizing long term financing, including crowding in private sector. The institution must leverage its capital base to achieve existing targets this year, partly drawing from private sector sources of financing.

31. **There are several important design features in which NaBFID is expected to differ from the other DFIs in India, which is expected to help it leverage private sector financing more effectively.** Firstly, unlike other DFIs, NaBFID is expected to have diversified ownership in the long term and benefit from capacity building and higher standards of governance. Although NaBFID has been established as a fully state-owned entity, its founding Act envisages that the GoI's stake can eventually be reduced to 26 percent. Secondly, to ensure that NaBFID is achieving its objective, the Act mandates a performance review every five years by an external agency. Thirdly, the Act allows NaBFID to engage top-level experts at salaries and allowances guided by market standards, in contrast to other public DFIs whose ability to attract talent is constrained by salary differentials between the public and private sector. Lastly, while other DFIs focus mostly on lending and refinancing activities, NaBFID is also expected to play a role in facilitating the development of markets for interest rate derivatives, credit derivatives, currency derivatives and other innovative financial instruments, as may be necessary for infrastructure financing in the country.

32. **Following the approval of NaBFID's founding Act by Parliament in March 2021, the authorities have proceeded to establish the institution with the view to start operations during first half of the fiscal year 2022-23**. To this end, in February 2022 the GoI allocated Rs. 200 billion as initial share capital for NaBFID, while in March 2022 the RBI issued the decision to subject NaBFID to prudential oversight. The GoI has appointed highly

[12] As per the Economic Survey 2018-19 prepared by MoF, India needs to invest ~US$200 billion per annum in infrastructure, to be able to realize its growth potential and achieve its high-level development goals. Actual spending has been much lower at US$100–110 billion.
[13] The National Bank for Financing Infrastructure and Development Act, 2021.

experienced and reputable senior bankers to lead the new entity. The institution would have three independent directors of which two have been appointed, with the third appointment currently underway. The preparation of a business plan and selection of executive team are underway towards operationalization of the institution and is expected to be a significant contribution to the implementation of the NIP.

33. **Going forward, NaBFID is committed to work on a variety of instruments, including in the critical areas of credit enhancement and green financing**. Based on the WB team's review of the founding Act and discussions with NaBFID's senior management, the new entity's envisioned structure, product mix, and governance norms are broadly in line with global best practices. In particular, there is a broad consensus that NaBFID's focus on the development of credit enhancement products and other capital market instruments will one of the critical factors for the participation of private and institutional investors. The credit enhancement products are expected to be developed and offered by NaBFID to the market over the next two years, with the WBG standing ready to provide technical assistance, if need be, in this area. NaBFID management has also shown strong interest in promoting ESG-compliant investments and if required, seek assistance from the WB.

Prior Action #2: The Borrower (i) through NITI Aayog has launched the National Monetization Pipeline (NMP) to create greenfield infrastructure assets by recycling brownfield core assets of the Borrower; (ii) through RBI, has permitted FPIs to invest in debt securities issued by InvITs; and (iii) through the Ministry of Labour and Employment, has approved investments of up to 5 percent of EPFO's annual deposits in AIFs, including InvITs.

34. **PA2 supports a set of measures undertaken by the authorities in recent months with the goal to mobilize private, foreign and institutional investor financing for the infrastructure sector.** On the supply side, the creation of the NMP by the GoI (August 2021) is expected to provide visibility on the volume and type of assets to be monetized over a defined period. Asset monetization is an efficient approach widely used by many governments around the world to ease public sector fiscal constraints and free up government balance sheets for new greenfield infrastructure creation. There are significant existing public sector infrastructure assets in India that can be used to tap private sector capital while leveraging their operational efficiencies. The indicative value of the Central Government's infrastructure assets which can be monetized over a four-year period has been estimated at Rs. 6.0 trillion (US$80 billion), of which the government has already monetized projects worth Rs. 960 billion in FY2021–22, surpassing the target of Rs. 880 billion set for the first year. The funding raised from monetized assets can then be used to finance around 5.4 percent of the total infrastructure investment envisaged under the NIP. For conservative investors like pension funds (such as Employees' Provident Fund Organization (EPFO), India's leading pension scheme) or where private sector has had limited opportunities to participate, these brownfield operating assets represent ideal infrastructure investment opportunities. The new NMP will serve as a medium-term roadmap for the investors looking to participate in brownfield operational infrastructure assets, with clear estimates on revenue streams and investment potential. The private sector money that will be channeled into operational assets of the NMP would ultimately help in creating a fresh financing pool and in funding of new capital expenditure without creating pressure on government finances.[14]

35. **On the demand side, PA2 supports the review of investment rules and limits to promote participation of foreign and domestic investors in the NMP and in infrastructure financing in general**. As per the decision taken by EPFO's Central Board of Trustees in November 2021, the pension fund will now be able to invest up to 5 percent

[14] In a monetization transaction, the government is transferring revenue rights to private parties for a specified period in return for upfront money, a revenue share, and commitment of investments in the assets. The assets on the NMP list include roads, railway stations, train operations and tracks, power transmission lines, hydroelectric and solar power assets, and telecom assets.

of its incremental deposits (which are around Rs 1.8 trillion, or US$24 billion) per year in InvITs and other alternative funds. At the same time, based on November 2021 decision by the RBI, FPIs would be able to invest in debt securities issued by InvITs and real estate investment trusts (REITs) under the Medium-Term Framework or the Voluntary Retention Route of the RBI. The entry of FPIs into debt financing of InvITs is expected to open up a large source of fresh funding for the infrastructure and real estate sectors.[15]

Prior Action #3: The Borrower has taken steps to link housing finance companies to capital markets through securitization: (i) through RBI, by the issuance of the revised regulatory framework for Securitization of Standard Assets; and (ii) through NHB, by approving the setting up of a multi-originator Residential Mortgage-Backed Securities (RMBS) Pass through Certificate (PTC) securitization platform.

36. **India's housing finance market has reported high growth over the past decade, but still lags its peers on mortgage-loans-to-GDP ratio.** The affordable housing segment in particular has seen high growth, in part due to the government's *Housing for All* agenda. One of the key constraints for mortgage finance is the lack of access to sustainable long-term funding, particularly for HFCs, which account for around 40 percent of housing finance market assets, and play a critical role in financing affordable housing, including to borrowers in the informal sector. Securitization was identified by the RBI expert committee report on housing finance in 2019 as a suitable solution to improve long-term funding for housing finance. A vibrant PTC securitization market with a wide investor base will help HFCs and other lenders address asset-liability mismatches through longer tenure of instruments, enhanced participation of institutional investors such as insurance and pension funds, and scale-up of innovative lending products for affordable housing. However, market data suggest that around 63 percent of securitization transactions (for MBS securitization transactions, this figure is at around 85 percent) in India are currently carried out through the Direct Assignment route, which involves bilateral sale of loan portfolios instead of issuance of PTCs, as per international good practice. This constrains the potential impact of securitization in India since bilateral sales of loans limit the pool of investors, thus restricting potential funding sources for HFCs, and also does not allow efficient price discovery for loan portfolios.

37. **PA3 supports two important steps aimed at facilitating the access by HFCs and other mortgage lenders to capital market financing through improving the securitization framework.** Firstly, the revised guidelines on securitization issued by RBI in September 2021 will enable streamlined issuance of PTCs, including removing the bar on securitization of purchased loans, reducing risk retention requirements, and introducing Simple, Transparent and Comparable (STC) transactions which provide additional capital relief to lenders. Secondly, in November 2021, the Board of NHB, India's housing finance DFI, has taken a formal decision to proceed with establishing the national securitization platform. This NHB-led securitization platform would enable standardized securitization transactions involving banks, HFCs and investors, and thus provide sustainable long-term funding to lenders. In particular, the platform will allow the small and medium-sized lenders that lack the scale to participate in securitization transactions on a standalone basis to pool loan portfolios through the intermediary in order to issue higher-rated PTCs, which would improve their access to capital market funding and reduce funding costs. This initiative could be strengthened further by necessary regulatory interventions to develop the PTC securitization market. To date, the NHB has engaged a qualified consultant to develop the design of the securitization platform and help find quality investors (including potential participation by the International Finance Corporation (IFC)), with the goal to make the platform operational within 12-18 months (i.e., by December 2023).

[15] Even before this RBI decision, FPIs have been an increasing source of funding for India's financial markets, investing Rs. 500 billion (US$7.06 billion) in the calendar year 2021 alone.

Pillar 2: Developing the markets for green finance

38. **Pillar 2 supports the development of green finance markets and instruments for inclusive and resilient growth.** With India being highly vulnerable to impacts from climate change, both public and private sector finance need to be harnessed to support the economy transitioning to a more sustainable and resilient growth model. As per WB estimates, on energy transition alone, the economy will require a cumulative investment of 1.5 percent of GDP annually for the country to achieve its Intended Policy Scenario announced at COP26. This will be achieved through deepening of the financial sector, creation of new instruments for mobilizing funding for climate adaptation and mitigation objectives, as well as through greening of the financial system, ensuring that a national regulatory framework and financial infrastructure support such investments. Results from the reforms supported under this Pillar will include deepening of the green bond market through issuance of sovereign green bonds, as well as creating an operational framework for a domestic carbon market in India. In addition, disclosure of ESG risks by top-listed companies and mutual funds will be enhanced which, in turn, will promote sustainable investment.

Prior Action #4: The Borrower has taken steps for the launch of the country's first sovereign green bonds, as evidenced by: (i) the policy decision of the Union Government to issue sovereign green bonds in FY 2022-23 as part of the overall government borrowing; and (ii) the RBI's inclusion in the borrowing calendar for H1 FY2022-23 of their commitment to the issuance upon completion of the framework for issuance.

39. **PA4 supports issuance of the first sovereign green bond by GoI.** Green bonds are a commonly used tool for governments and companies around the world to raise capital in line with national climate mitigation and adaptation targets, consistent with NDC set in the Paris Agreement. India's first corporate green bond was issued in 2015, and the corporate green bond market saw significant growth since then, with issuance of US$6.11 billion in 2021 alone. In February 2022, as part of Federal Budget Announcement, the Minister of Finance announced that as a part of the GoI's overall market borrowing for FY 2022-23, the country's first ever sovereign green bonds will be issued for mobilizing resources for green infrastructure. The local currency bond proceeds will be deployed in public sector projects which help reduce carbon intensity of the economy. As stated in the public borrowing calendar for the first half of FY2022–23 (published in April 2022), the RBI and GoI are currently working on the framework for utilization of funds from sovereign green bond issuance. The WBG is sharing with authorities the best practices and lessons learned from recent successful issuances in other emerging markets. The GoI's first issuance of the sovereign green bond is expected to provide a strong signal of the country's commitment to a low-carbon economy and help bring down the cost of capital for green infrastructure projects by attracting new investors and catalyzing additional private capital toward sustainable development.

Prior Action #5: The Borrower, to ensure transparent and standardized disclosures on the ESG parameters, through its securities regulator, SEBI, (i) has revised the ESG reporting guidelines for the top 1,000 listed companies by market capitalization; and (ii) has, through AMFI, issued guidelines on disclosure norms for investments made by ESG mutual funds.

40. **PA5 supports transparent, standardized disclosures on ESG parameters and sustainability-related risks and opportunities by listed companies.** Detailed and reliable ESG reporting enhances corporate transparency, strengthens risk management, and promotes stakeholder engagement. It also helps investors direct financing to reputable and environmentally and socially sound companies, while avoiding companies that might pose financial risk due to their harmful environmental and/or social practices. This in turn will facilitate more climate friendly, sustainable, and inclusive growth. Recognizing the importance of ESG disclosures, the revised Business

Responsibility and Sustainability Reporting (BRSR) framework for the top 1,000 listed companies adopted by SEBI in May 2021 places a substantial emphasis on environmental compliances by mandating quantitative and qualitative disclosures with respect to energy consumption, water withdrawal, air emissions (including for greenhouse gas emissions), waste management, and sustainable sourcing. The revised BRSR framework includes elements from international standards such as the Task Force on Climate Related Financial Disclosures, as well as the National Guidelines on Responsible Business Conduct by the Ministry of Corporate Affairs. The result of this PA will be enhanced transparency in ESG disclosures as measured by the number of listed companies disclosing detailed ESG information as prescribed by the guidelines. The companies are required to comply with the new reporting framework starting from FY2022–23.

41. **In addition, PA5 supports improved ESG disclosures by the mutual fund industry.** With several new ESG themed mutual funds launched in India in the past year, SEBI asked AMFI to issue new guidelines on transparent disclosure norms for ESG investments in February 2022. To ensure proper labeling, the guidelines mandate ESG themed mutual funds to accurately disclose their stated objectives, documented investment policy and strategy, as well as their investments. This will encourage asset managers to take sustainability-related risks and opportunities into account in their investment decision-making and risk management processes.

Prior Action #6: The Borrower, through its Ministry of Power, has: (i) designated BEE as the nodal agency to set up a voluntary national carbon market and trading scheme to promote low-carbon alternatives; and (ii) through BEE, has prepared and disclosed a blueprint document laying out the rules and modalities for the functioning of a national carbon market overseen by a high-level inter-ministerial committee.

42. **PA6 supports the development of the carbon market and trading scheme in India.** Carbon markets are an instrument used in many jurisdictions to incentivize the decrease in emissions by enabling entities to reduce emissions at a lower cost to be paid by higher-cost emitters. The development of a domestic carbon market in India will provide necessary market support mechanisms to accelerate innovation toward low-carbon alternatives and simultaneously support momentum to drive the mobilization of private finance toward new climate mitigation opportunities. The WB's Partnership for Market Readiness has been providing support to Indian authorities since 2017 to pilot the use of carbon pricing instruments. This support included the preparation of three feasibility reports—two for piloting market-based instruments in the municipal solid waste management sector and MSME sector and the third to study the feasibility of setting up a Meta Registry to serve the dual purpose of ensuring emission reduction data management and acting as a transaction registry. India currently has two market-based trading schemes that put an implicit price on carbon—the Perform, Achieve & Trade (PAT) by the BEE which aims to promote energy efficiency and the Renewable Energy Certificate (REC) which supports clean energy. At the high-level inter-ministerial 'Apex Committee for Implementation of Paris Agreement' meeting held in March 2021, the authorities decided that BEE would be entrusted with the task of building on the PAT Scheme to develop a full-scale 'Domestic Carbon Market.'

43. **To kickstart this reform, the BEE prepared the blueprint for national carbon market development and formed a high-level steering committee to guide the process.** The BEE has released a "Roadmap of Sustainable and Holistic Approach to National Energy Efficiency" in October 2021 which covers critical elements of the proposed carbon market among other initiatives pertaining to energy efficiency. Thereafter, in January 2022, a stakeholder consultation was held on the Draft Blueprint of a 'National Carbon Market,' discussing the challenges and opportunities relating to developing a carbon market in India, and recommending a phased approach. In March 2022, the steering committee, comprised of high-level officials from various ministries, was constituted to provide

strategic direction for: (i) establishment of the carbon market & trading scheme; (ii) providing overall guidance on the functioning of the carbon market and trading of credits; (iii) overseeing the mechanism and its alignment with the national objectives and recommendations of the Apex Committee for Implementation of Paris Agreement; and (iv) monitoring the progress of establishing the mechanism. Building on the blueprint and stakeholder consultations, BEE will formulate a draft policy document on the domestic carbon market that will stipulate the rules and regulations of the proposed scheme. This document will form the basis for drafting the necessary amendments to the Energy Conservation Act and other relevant regulations and policies. Finally, it is anticipated that a trading platform to facilitate the operations of the national carbon market will be established by June 2024. Once the trading platform is established, a cap-and-trade mechanism will be introduced in a phased approach, and depending on the target-setting process, the size of the domestic carbon market will grow. Importantly, the financial sector is expected to play an important role in operationalizing the scheme by developing innovative instruments for monetization of future carbon receivables.

Pillar 3: Improving access to credit for MSMEs and women entrepreneurs

44. **Pillar 3 supports the flow of credit to MSMEs and women entrepreneurs impacted by the pandemic.** MSMEs, including women entrepreneurs, were disproportionately impacted by several waves of COVID-19 in India. As economic activity declined, credit to MSMEs, which had already been slowing, decreased further. To address the risk aversion of lenders, and to maintain the flow of funds in support of businesses and livelihoods, the GoI implemented a series of targeted emergency guarantee schemes, as well as overhauled the existing credit guarantee scheme for MSMEs. These measures, requiring relatively limited fiscal outlays, are shown to be successful in crowding in large amounts of funding from private banks and NBFCs, while demonstrating sound levels of asset quality. The credit guarantee schemes are also essential for post-pandemic economic recovery by allowing MSMEs to access credit without the need to provide additional collateral, while ensuring that funding costs do not rise significantly.

Prior Action #7: The Borrower, through CGTMSE, has strengthened the Credit Guarantee Scheme for Banks (CGS-I) and Credit Guarantee Scheme for NBFCs (CGS-II) for serving the needs of Micro and Small Enterprises (MSE) sector during recovery stage through: (i) expanding the limit for guarantee cover per borrower; and (ii) introducing guarantee cover for co-lending by banks and NBFCs.

45. **The CGTMSE is the largest permanent credit guarantee scheme in India which played a critical role in securing access to credit for MSMEs over the past two decades.** The CGTMSE scheme has been operating since 2000 and provides guarantees of 50–85 percent on loans to micro and small enterprises by banks and NBFCs for up to Rs. 20 million, to facilitate collateral free lending to micro and small enterprises. The scheme has been particularly instrumental in leveraging private financing for women-led MSEs, which typically face restrictive collateral requirements. The scheme includes provisions for lower guarantee fees and higher maximum guarantee coverage for women-led MSEs. The CGTMSE scheme maintains a strong financial position and is subject to oversight by its Board, comprised of representatives from SIDBI, Ministry of MSMEs, and Indian Banks' Association. The CGTMSE was evaluated against the WB Principles for Public Credit Guarantee Schemes for SMEs in 2020 and was found to have adequate arrangements for corporate governance, claims management process, and risk-based pricing.

46. **PA7 supports a number of important changes in the CGTMSE's operating model to make the scheme more effective in supporting the post-pandemic economic recovery.** As part of the federal budget announcement in February 2022, the GoI stated that the CGTMSE scheme would be revamped to enable additional lending of Rs. 2

trillion to the MSME sector over the next five years. Given the withdrawal of emergency support measures for most sectors, the CGTMSE scheme is being strengthened to support the MSME funding needs during recovery. This includes: (i) increasing the limit for the guarantee amount per borrower and (ii) introducing guarantee cover for co-lending by banks and NBFCs to reach new categories of borrowers. In the longer term, the CGTMSE plans to allow medium sized enterprises to benefit from guarantee cover under the scheme, complete the digitalization of the claims process to reduce turnaround time for claims, and introduce green guarantees (with support from the ongoing WB's Raising and Accelerating MSME Performance (RAMP) Program for Results (P4R), P172226).

Prior Action #8: The Borrower, through NCGTC, has revised the guidelines for the operations of the Emergency Credit Line Guarantee Scheme (ECLGS) to ensure MSMEs in sectors worst affected by COVID-19 have continued access to the Guaranteed Emergency Credit Line.

47. **The ECLGS scheme played a critical role in supporting MSMEs to access finance during the pandemic**. In response to the crisis in the MSME sector due to the impact of COVID-19, the GoI launched the ECLGS scheme in May 2020 to provide fully guaranteed additional credit to MSMEs. The scheme was designed as an emergency instrument to support the rapid disbursement of additional credit to eligible MSMEs, complementing the permanent CGTMSE scheme. Over the past two years, the scheme leveraged large amounts of funding for MSMEs from banks and NBFCs, with private banks disbursing a larger amount under the scheme than PSBs. The impact evaluation report estimates that the scheme prevented around 14 percent of MSME loans from becoming NPAs, and in doing so, prevented potential job losses for over 15 million workers.

48. **PA8 supports the reform of the ECLGS to respond to the funding needs of sectors affected by the second and third waves of COVID-19.** The National Credit Guarantee Trust Company (NCGTC), the public entity responsible for implementing the ECLGS scheme, issued revised guidelines for ECLGS in March 2022, specifying a list of eligible sectors (mostly contact-intensive ones) which were worst-impacted by successive waves of COVID-19 in India. The amount of additional credit under the scheme was previously linked to outstanding borrowings on February 29, 2020, which affected the eligibility of many borrowers, as they were excluded from the scheme if they had outstanding borrowings on that date. The revised guidelines allow enterprises in identified sectors to access additional credit based on the highest outstanding borrowings on any one of three dates (February 29, 2020; March 31, 2021; and January 31, 2022), and also allow more types of credit facilities to be included for calculating the eligible amount of additional credit. This will enable new borrowers to access the scheme and allow existing beneficiaries to mobilize additional financing. The ECLGS scheme is expected to end in March 2023, or as soon as the guarantee amount under the scheme is utilized, whichever is earlier.

Prior Action #9: The Borrower, through NCGTC, has implemented the Credit Guarantee Scheme for Micro-Finance Institutions (CGSMFI) in support of small borrowers and women entrepreneurs impacted by COVID-19.

49. **PA9 supports the establishment and implementation of CGSMFI, a dedicated guarantee scheme for microfinance institutions (MFIs) which maintains the flow of credit to smaller firms and women entrepreneurs during the pandemic.** The shocks emanating from COVID-19 led to liquidity issues for MFIs, as funding from banks and mutual funds decreased, the ability of borrowers to repay loans from MFIs also deteriorated significantly, and MFIs did not have direct access to RBI's liquidity facilities for financial institutions. This in turn led to reduced credit flow to the MFI sector's traditional clients, which are primarily women borrowing for microenterprises or livelihoods needs. Recognizing that MFIs are an important source of financing for small borrowers, in particular women entrepreneurs, the GoI established a dedicated credit guarantee scheme for MFIs in July 2021. The

objective of the CGSMFI scheme was to provide guarantee coverage to eligible lending institutions for the funding provided by them to MFIs for on-lending to eligible small borrowers in the context of COVID-19. The scheme provided a 75 percent guarantee for lending by banks to MFIs, and 80 percent of the funds under the scheme were mandated to be used for fresh lending to small borrowers. Also, 50 percent of the funds under this scheme were required to be channeled to lower-rated MFIs. The scheme was extremely successful and was fully utilized by October 2021 to facilitate lending of Rs. 100 billion to MFIs for on-lending to mostly women entrepreneurs. The share of women borrowers, in terms of the number of loans under the scheme as well as the volume of loans, is expected to be substantial. Further, the scheme supported 67 MFIs through 24 lenders, and lower-rated MFIs received around 50 percent of funds under this scheme.

Table 4: DPL Prior Actions and Analytical Underpinnings

Prior Actions	Analytical Underpinnings
Pillar 1: Catalyzing long term private sector finance	
PA1: The Borrower has established the National Bank for Financing Infrastructure and Development (NaBFID), as a development financial institution with the mandate of offering credit enhancement products and mobilizing long term private finance for the infrastructure sector, pursuant to which (i) the Government of India has allocated capital; and (ii) NaBFID shall be regulated and supervised by the Borrower's central bank, RBI.	WB TA to DEA on Infra finance (2019 – ongoing) **Key findings:** Infrastructure projects require long-term financing that commercial banks are unable to provide due to asset-liability mismatch. A well-run DFI could help in leveraging private sector financing at scale by offering a range of services (structuring, financing support, credit enhancement) to make projects commercially viable.
PA2: The Borrower (i) through NITI Aayog has launched the National Monetization Pipeline (NMP) to create greenfield infrastructure assets by recycling brownfield core assets of the Borrower; (ii) through RBI, has permitted FPIs to invest in debt securities issued by InvITs; and (iii) through the Ministry of Labour and Employment, has approved investments of up to 5 percent of EPFO's annual deposits in AIFs, including InvITs.	Ongoing WB TA on Infra finance; NMP reports by NITI Aayog[16] **Key findings:** Asset recycling and monetization, through NMP and innovative instruments such as InvITS, are the key to value creation in infrastructure by: (i) unlocking value from public investment in infrastructure; and (ii) tapping private sector efficiencies in operations and management of infrastructure.
PA3: The Borrower has taken steps to link housing finance companies to capital markets through securitization: (i) through RBI, by the issuance of the revised regulatory framework for Securitization of Standard Assets; and (ii) through NHB, by approving the setting up of a multi-originator Residential Mortgage-Backed Securities (RMBS) Pass through Certificate (PTC) securitization platform.	2019 RBI Expert Committee Report on Housing Finance; Ongoing TA on housing finance by WB and IFC **Key findings:** HFCs and other lenders need access to long-term funding to expand housing finance, in particular for affordable housing. Securitization transactions, including on the NHB-led platform, can support mobilization of long-term funding from investors.
Pillar 2: Developing the markets for green finance	
PA4: The Borrower has taken steps for the launch of the country's first sovereign green bonds, as evidenced by (i) the policy decision of the Union Government to issue sovereign green bonds in FY 2022-23 as part of the overall government borrowing; and (ii) the RBI's inclusion in the borrowing calendar for H1 FY2022-23 of their commitment to the issuance upon completion of the framework for issuance.	Ongoing WB TA on bond market development and climate finance; IFC support under Sustainable Finance Task Force **Key findings:** A sovereign green bond would be a key step in developing green finance markets in India, by providing a strong signal of the country's commitment to a low carbon economy and crowding in private capital for green investments.

[16] The NITI Aayog serves as the apex public policy think tank of the GoI, and the nodal agency tasked with catalyzing economic development, and fostering cooperative federalism through the involvement of state governments in India in the economic policy-making process using a bottom-up approach.

PA5: The Borrower, to ensure transparent and standardized disclosures on the ESG parameters, through its securities regulator, SEBI, (i) has revised the ESG reporting guidelines for the top 1,000 listed companies by market capitalization; and (ii) has, through AMFI, issued guidelines on disclosure norms for investments made by ESG mutual funds.	SEBI consultation papers on ESG Framework; IFC support under Sustainable Finance Task Force **Key findings**: ESG reporting by listed companies should be improved to enhance corporate transparency, strengthen risk management, and promote stakeholder engagement.
PA6: The Borrower, through its Ministry of Power, has: (i) designated BEE as the nodal agency to set up a voluntary national carbon market and trading scheme to promote low-carbon alternatives; and (ii) through BEE, has prepared and disclosed a blueprint document laying out the rules and modalities for the functioning of a national carbon market overseen by a high-level inter-ministerial committee.	WB TA on Partnership for Market Readiness **Key findings:** Carbon markets have successfully lowered the economic cost of reducing emissions by enabling entities to reduce emissions at a lower cost to be paid by higher-cost emitters. A domestic carbon market has the potential to succeed in India as several leading companies have already embedded an internal carbon price into their business strategies.
Pillar 3: Improving access to credit for MSMEs and women entrepreneurs	
PA7: The Borrower, through CGTMSE, has strengthened the Credit Guarantee Scheme for Banks (CGS-I) and Credit Guarantee Scheme for NBFCs (CGS-II) for serving the needs of Micro and Small Enterprises (MSE) sector during recovery stage through: (i) expanding the limit for guarantee cover per borrower; and (ii) introducing guarantee cover for co-lending by banks and NBFCs.	2019 RBI Expert Committee Report on MSMEs; FIRST TA to SIDBI; WB analysis under RAMP P4R preparation **Key findings:** The CGTMSE scheme plays a critical role in enabling MSMEs to access collateral-free funding. There is scope to make the scheme more inclusive/effective by adding new categories of borrowers and lenders, introducing new products, and digitizing claims.
PA8: The Borrower, through NCGTC, has revised the guidelines for the operations of the Emergency Credit Line Guarantee Scheme (ECLGS) to ensure MSMEs in sectors worst affected by COVID-19 have continued access to the Guaranteed Emergency Credit Line.	The ECLGS impact assessment reports; WB analysis on the impact of COVID-19 on financial sector and MSMEs **Key findings:** The ECLGS scheme helped preserve a large number of MSMEs and jobs during the pandemic. Further targeting the scheme toward sectors most severely impacted by COVID-19 is warranted as the economy enters recovery mode.
PA9: The Borrower, through NCGTC, has implemented the Credit Guarantee Scheme for Micro-Finance Institutions (CGSMFI) in support of small borrowers and women entrepreneurs impacted by COVID-19.	Reports by MFI industry associations and SIDBI; WB analysis on the impact of COVID-19 on financial sector and MSMEs **Key findings:** MFIs needed funding support during the pandemic to ensure that access to credit for small borrowers, mostly women, does not decline sharply.

4.3. LINK TO CPF, OTHER BANK OPERATIONS AND THE WBG STRATEGY

50. **The DPL is consistent with the WBG Country Partnership Framework (CPF) FY18–22 discussed by the Board on September 20, 2018 (Report 126667-IN).** The operation contributes to the CPF's Pillar 1 "Resource Efficient Growth" and Pillar 2 "Enhancing Competitiveness and Enabling Job Creation" by enabling an ecosystem where the critical sectors of infrastructure and MSMEs will be able to thrive and generate more employment. In addition, the DPL will support the de-risking of commercial investments in sustainable projects, creation of innovative products such as green bonds, and strengthening of ESG frameworks.

51. **This reform program will build on extensive TA and lending engagements in the financial sector**. The TA

to DEA has helped in identifying key policy enablers that will be most critical for bringing long-term, local currency investors to India's infrastructure projects. Similarly, the reform program for MSMEs and Housing Finance builds on long-standing lending and TA dialogue supporting SIDBI, the NHB, CGTMSE, including the ongoing RAMP P4R.

52. **The operation has substantial climate co-benefits (CCB) as it focuses on financing infrastructure (including low-carbon resilient infrastructure) and developing green finance markets**. The preliminary estimates suggest CCB of [25.18] percent. Being one of the most vulnerable countries to climate change and the third largest emitter globally, India faces significant climate-related physical and transition risks. Through its Pillar 1, this operation aims to catalyze financing to infrastructure, develop systems and tools to enable efficient implementation of the NIP and NMP to tap into long-term institutional and private investor capital. Both pipelines have significant renewable energy assets and infrastructure and further aim to integrate low-carbon and climate-resilient considerations into infrastructure planning, investment and spending. Through 'Pillar 2, the operation aims to further the development and attractiveness of the green bond market in India through the strong signaling effect of sovereign green bond issuances; improve the quality and granularity of ESG related disclosures; and develop carbon market and trading scheme in India. The credit guarantee schemes under Pillar 3, the operation will support, inter alia, the green MSMEs. The PA-specific climate adaptation and mitigation actions are detailed in the Climate Change Technical Note prepared for this operation.

53. **The operation is gender-tagged and it mobilizes financing for development.** PA7 and PA9 support MSME access to finance through credit guarantees schemes, with a focus on women-owned businesses. Two Results Indicators have been included to track the volume of financing and guarantees extended to women entrepreneurs, resulting in the operation having a gender tag. The operation also supports mobilization of financing for development through policy actions enabling private capital mobilization for infrastructure, housing and MSMEs as well as green initiatives, notably by establishing institutions (e.g., NaBFID, securitization platform) and mechanisms (e.g., credit guarantee schemes, sovereign green bonds).

4.4. CONSULTATIONS AND COLLABORATION WITH DEVELOPMENT PARTNERS

54. **The WBG and key stakeholders in India are closely coordinating with development partners on the reform agenda.** Various levels of consultations and technical discussions on the PAs were conducted between the WB and IFC teams on the one hand, and the Infrastructure Division at the DEA, RBI, SEBI, NHB and key development partners active in the MSME and infrastructure sectors on the other hand.

5. OTHER DESIGN AND APPRAISAL ISSUES

5.1. POVERTY AND SOCIAL IMPACT

55. **This operation will contribute to poverty reduction by ensuring continued flow of credit to MSMEs, including to women entrepreneurs, through credit guarantee schemes aimed at preserving flows of finance to MSMEs (PAs 7, 8 and 9).** The poverty impact of increased flow of funds to MSMEs attributed to credit guarantee schemes has already been quantified during the last financial sector DPL. Retrospectively, quantitative analysis demonstrated that firms that received credit as a result of an emergency credit guarantee scheme during the Government's first Emergency Response were less likely to lay off employees or cut their wages.[17] Analysis of the credit guarantee programs also suggests that they were reaching some vulnerable groups. Beneficiaries of the

[17] To better understand the impact of COVID-19 and mitigating measures on business owners, a module on MSMEs was added to the Consumer Pyramids Households Survey(CPHS) in the January-April 2021 wave.

credit guarantee program tended to be less educated (more likely to have less than primary education) and less likely to come from Other Backward Class castes. Additionally, there is evidence that the ECLGS increased business income derived from profits for MSME households in the six months following the national lockdown measures. By comparing MSMEs that obtained additional credit before and after the implementation of the credit guarantee scheme, the findings suggest that the expansion of credit guarantees have increased household business profits by 65 percent in August–November 2020. There is also suggestive evidence that the credit scheme prevented pay cuts for MSME employees. However, it also led to a decline in MSME owners' wages by 79 percent in August–November 2020 and by 118 percent in December 2020 to March 2021. This is likely due to MSME owners favoring paying suppliers and workers rather than paying wages to themselves. The ECLGS did not increase households' total income or consumption.

56. **The PA on the CGSMFI scheme (PA9) is particularly impactful for women.** Women are disproportionately vulnerable to the impacts of economic shocks in India, particularly those who are elderly, widowed or divorced. Women's mobility and survival options are affected by entrenched gender inequality, social norms, and reproductive responsibilities. Their adaptive capacity is constrained by lower relative access to capital and economic opportunities, and women have less ability than men to use urban migration as an adaptive strategy. Therefore, ensuring that MFIs continue to have access to liquidity for on-lending meant that their clients, who are almost exclusively women borrowers, were able to continue engaging in income-generating livelihood activities or could borrow to smooth consumption during the income shocks emanating from COVID-19 lockdowns.

57. **Citizen and stakeholder consultations.** The available literature on access to the ECLGS from the lens of the borrower is limited to the study undertaken by TransUnion CIBIL Ltd (December 2021). The study covered 756 respondents from 10 states. Engaging with citizens begins with information dissemination and 41 percent of respondents were informed by the lender. More than 50 percent of the borrowers who used the facility had a higher need for credit even before the pandemic. A lower proportion of respondents who either received no credit or credit below Rs. 10,000 were informed by the lender. However, 57 percent of respondents found it difficult to use the facility. Bigger entities found it easier to use the facility as compared to very small entities. At the same time, NBFCs as lenders had the highest negative response (66 percent) on the ease of availing the ECLGS across lender type. Sixty-five percent of respondents found the ECLGS to ease their financial problems and 68 percent of respondents had a positive future outlook for their business. Moving forward, the program will support stakeholder consultations specifically for PAs 7, 8 and 9 on access to credit, job market, and secured livelihood by women and socially excluded groups. Consultations will be conducted with the broader civil society, academia, and development partners.

5.2. ENVIRONMENTAL, FORESTS, AND OTHER NATURAL RESOURCE ASPECTS

58. **The reforms supported under this DPL are expected to have significant positive effects along with possible low negative impacts on the country's environment and natural resources.** Pillar 1 is expected to facilitate the mobilization of capital for infrastructure finance in the manner consistent with India's COP26 and NDC commitments, leading to positive environmental effects. However, there might be indirect negative environmental effects, including on forests, as a result of some of the downstream infrastructure investments that are currently not covered under GoI Environment Impact Assessment (EIA) policy. Under Pillar 2, issuing Indian sovereign green bonds would increase opportunities for institutional investors to support climate-smart investments. Moreover, enhanced ESG disclosure guidelines will enable Indian firms and mutual funds to attract more capital toward sustainable goals. Lastly, the development of carbon markets and trading schemes will provide strategic direction and will play a crucial role in catalyzing low-carbon investments in India. Under Pillar 3, considering the MSME

sector's compliance with environmental regulations is still moderate (although with the trend for improvement), there might be some low negative environmental impacts.

59. **To mitigate possible negative environmental effects under Pillars 1 and 3, capacity building and technical assistance to implementing agencies are being planned.** To manage the risks from Pillar 1, the relevant public agencies responsible for implementation are eligible to be recipients of the *WB Environment & Social Framework Client Capacity Building & Development Support*. Under this engagement, the WB plans to assist clients to deliver projects consistent with Environmental and Social Framework requirements across India over the next fiscal year (FY22–23) as well as provide capacity building to develop systems, enhance policies and procedures to align with international standards, and improve E&S performance during implementation. Importantly, the WB will seek to partner with the newly established NaBFID to ensure that global ESG standards are incorporated in its operating procedures to the extent feasible. The low risks emanating from Pillar 3 will be mitigated through support provided under the ongoing WB RAMP P4R, under which "Strategy to Strengthen Environment & Social Management" was developed. Under this engagement, capacity building assistance on environment and social management aspects is being provided to the Ministry of Micro, Small & Medium Enterprises, CGTMSE, and selected states.

5.3. PUBLIC FINANCIAL MANAGEMENT (PFM), DISBURSEMENT AND AUDITING ASPECTS

60. **The fiduciary risk of the proposed operation is moderate based on the current status of PFM systems, procurement systems and forex control environment.** A Public Expenditure and Financial Assessment for India was conducted in 2010 by the National Institute of Public Finance and Policy, with support from the WB, on the basis of which the team concludes that PFM systems are working adequately, and that the country fiduciary risk is moderate. The main strengths and weaknesses of the system are as follows:

- India has achieved a reasonably high level of fiscal transparency, and the comprehensiveness of the fiscal information available publicly has improved over the years.
- Adoption of the Fiscal Responsibility and Budget Management (FRBM) Act, 2003 has led to presentation of fiscal policy strategy documents and projected major fiscal indicators in the medium term. The General Government budget is publicly disclosed.
- The Constitution provides for the Comptroller and Auditor General of India (CAG) to act independently as a statutory auditor of the Union and States, and the audit reports are usually made available to the public within a year from the end of the FY and are submitted to the legislature.
- There is scope for: (a) further strengthening budgetary preparation and approval procedures and the manner in which they are controlled; (b) unifying and improving PFM systems that are currently disjointed;[18] and (c) further streamlining and enhancing financial rules for effective internal expenditure control.

61. **A substantive opportunity exists at the Union level to leverage earlier PFM reforms and further augment revenue collection, enhance expenditure efficiency, and create more headroom for undertaking larger productive investments.** Until now, India has not undertaken a comprehensive, coordinated PFM reform. Instead, reforms have occurred as standalone reform initiatives of individual Union or state government departments. Most states have launched PFM reforms, often in parallel, rarely in coordination with each other or with the Union. However, the scope for state-level reforms is also constrained by their dependence on GoI and CAG in setting the presentation of financial statements, accounting and reporting standards, reforms in budget orientation, and

[18] An Integrated Financial Management Information System (IFMIS) incorporating systems for management of personnel database and payroll records at central government level in India does not exist.

benchmarks for financial and fiscal transparency.

62. **The WB has been actively engaged with the 15th Finance Commission (FFC), Department of Expenditure and DEA in helping develop the next steps in PFM reform.** FFC has highlighted the need for a comprehensive plan and recommended that: (a) the FRBM Act be restructured and a timetable for defining and achieving debt sustainability be examined by a high-powered inter-governmental group; and (b) three mutually reinforcing pillars are strengthened to improve the quality and efficiency of public spending and financial management across all levels, namely (i) fiscal rules across all levels of government for fiscal sustainability; (ii) a PFM system which provides complete, consistent, reliable and timely reporting of the fiscal indicators; and (iii) an independent assessment mechanism to provide assurance and advice on the working of the other two pillars. While the government is in the process of examining these recommendations in detail, they have already included two critical reforms in the FY22 Budget, namely, bringing off-budget borrowings on budget (like food and fertilizer subsidy) and strengthening cash management in the GoI.[19]

63. ***Foreign Exchange Controls:* The WB has reasonable assurance that the control environment for foreign exchange in the RBI is satisfactory for the purposes of this DPL.** This assessment is based on RBI audit reports and the satisfactory outcomes of other operations, which have been disbursed and managed through the RBI. The IMF has not carried out a Safeguard Assessment of RBI. However, as part of the preparation for this operation, the RBI's audit report and published annual financial statements for the three financial years (FY19–21) were reviewed by the WB. The audit reports have a clean, unqualified opinion and were conducted by private firms of chartered accountants.

64. ***Disbursement:* The proposed operation will follow the WB's standard disbursement procedures for Development Policy Financing.** Upon effectiveness, the borrower - GoI, will submit a withdrawal application to the WB. The WB will disburse the US Dollar proceeds of the facility to the GoI's account with the RBI. This account is controlled by the Office of the Controller of Aid, Accounts, and Audit of the Department of Economic Affairs, GoI and is part of the GoI's general foreign exchange reserves. Once the amount is credited it will be added to the consolidated fund of GoI and will be available as part of the general budget proceeds. GoI shall, within thirty (30) days after the withdrawal of the Loan/Credit report to IBRD: (i) the exact sum received into the account; (ii) the details of the account to which the local currency equivalent of the proceeds will be credited; (iii) the record that an equivalent amount has been accounted for in the Borrower's budget management systems; and (iv) the statement of receipts and disbursement of the bank account at RBI. The loan proceeds for this operation do not finance specifically agreed activities. The proceeds may be used for any general purpose, in support of the program, other than for financing excluded expenditures (as defined in the legal agreement for the operation). If any amount of the proceeds is used to finance excluded expenditures, the legal agreements will authorize the WB to require India to refund the amount. The amounts so refunded shall be cancelled from the loan.

65. ***Procurement:* Public procurement is handled by GoI Ministries, States and Public Sector undertakings.** Public procurement is governed by General Financial Rules 2017 at Federal Level and similar Rules of respective states at State Levels. Some States have promulgated Public Procurement Acts. As part of COVID -19 response, the Federal Government has issued orders and instructions to streamline public procurement processes. These instructions have included designating agencies for procurement of goods for COVID response, greater use of Government e-marketplace Portal, removal of import duties for a period on key products and ingredients and

[19] Recommendations to strengthen cash management was made by the Bank in the note to the PM in 2014 and to the Expenditure Finance Commission in 2016. Based on pilots, these are being scaled up across the GoI.

simplified tender processes. Bank has carried out country procurement assessment using the Methodology for Assessing Public Procurement Systems (MAPS) and the final report is shared with the Ministry of Finance (MoF). Preliminary findings show that India has a moderately well-functioning public procurement system with islands of excellence. The majority of procurement is carried out through open competition procedures and e-procurement is extensively used by procuring entities throughout the country. The public procurement system of India may benefit from further improvement in complaints-handling mechanisms, more efficient procurement process from initiation to contract award, capacity building in contract management including dispute resolution mechanism, as well as strategic use of data for policy formulation and monitoring of the development expenditure.

5.4. MONITORING, EVALUATION AND ACCOUNTABILITY

66. **The Ministry of Finance of India is responsible for overall coordination and implementation of the DPL**. Data is generally available through the MoF and the RBI websites, as well as through the Ministry of Statistics and Programme Implementation and other government agencies.

67. **Grievance Redress**. Communities and individuals who believe that they are adversely affected by specific country policies supported as prior actions or tranche release conditions under a WB Development Policy Operation may submit complaints to the responsible country authorities, appropriate local/national grievance redress mechanisms, or the WB's Grievance Redress Service (GRS). The GRS ensures that complaints received are promptly reviewed in order to address pertinent concerns. Affected communities and individuals may submit their complaint to the WB's independent Inspection Panel which determines whether harm occurred, or could occur, as a result of WB non-compliance with its policies and procedures. Complaints may be submitted at any time after concerns have been brought directly to the WB's attention, and Bank Management has been given an opportunity to respond. For information on how to submit complaints to the WB's corporate GRS, please visit http://www.worldbank.org/GRS. For information on how to submit complaints to the WB Inspection Panel, please visit www.inspectionpanel.org.

6. SUMMARY OF RISKS AND MITIGATION

68. **The overall risk of the operation is assessed as Moderate,** based on the risk ratings in Table 5 below. The residual (other) risk stems from a potential weak response of the private sector in meeting the ambitious financing agenda. As the project intends to catalyze private financing for infrastructure, MSMEs, and green projects, the readiness of the private sector to contribute is essential in achieving this objective. The risk will be mitigated by strong commitment, and improved capacity of the GoI to work with the private sector to produce a bankable pipeline as highlighted in the Letter of Development Policy.

Table 5: Summary Risk Ratings

Risk Categories	Rating
1. Political and Governance	Moderate
2. Macroeconomic	Moderate
3. Sector Strategies and Policies	Moderate
4. Technical Design of Project or Program	Moderate
5. Institutional Capacity for Implementation and Sustainability	Moderate
6. Fiduciary	Moderate
7. Environment and Social	Moderate
8. Stakeholders	Moderate
9. Other	Low
Overall	Moderate

ANNEX 1: POLICY AND RESULTS MATRIX

Prior actions	Results		
	Indicator Name	**Baseline**	**Target**
Pillar 1: Catalyzing long term private sector finance			
Prior action #1: The Borrower has established the National Bank for Financing Infrastructure and Development (NaBFID), as a development financial institution with the mandate of offering credit enhancement products and mobilizing long term private finance for the infrastructure sector, pursuant to which (i) the Government of India has allocated capital; and (ii) NaBFID shall be regulated and supervised by the Borrower's central bank, RBI.	**Results Indicator #1:** Total volume of loans disbursed by NaBFID for the infrastructure sector (Rs. billion)	Rs. 0 (June 2022)	Rs. 1,000 billion (June 2024)
Prior action #2: The Borrower (i) through NITI Aayog has launched the National Monetization Pipeline (NMP) to create greenfield infrastructure assets by recycling brownfield core assets of the Borrower; (ii) through RBI, has permitted FPIs to invest in debt securities issued by InvITs; and (iii) through the Ministry of Labour and Employment, has approved investments of up to 5 percent of EPFO's annual deposits in AIFs, including InvITs.	**Results Indicator #2:** Total funds raised through monetization of brownfield assets included under the National Monetization Pipeline (Rs. billion)	Rs. 960 billion (FY2021-22)	Rs. 1,500 billion (FY2022-23)
Prior action #3: The Borrower has taken steps to link housing finance companies to capital markets through securitization: (i) through RBI, by the issuance of the revised regulatory framework for Securitization of Standard Assets; and (ii) through NHB, by approving the setting up of a multi-originator Residential Mortgage-Backed Securities (RMBS) Pass through Certificate (PTC) securitization platform.	**Results Indicator #3:** Volume of PTC RMBS securitization transactions (Rs. billion)	Rs. 73.8 billion (FY 2021-22)	Rs. 100 billion (FY 2022-23)
Pillar 2: Developing the markets for green finance			
Prior action #4: The Borrower has taken steps for the launch of the country's first sovereign green bonds, as evidenced by: (i) the policy decision of the Union Government to issue sovereign green bonds in FY 2022-23 as part of the overall government borrowing; and (ii) the RBI's inclusion in the borrowing calendar for H1 FY2022-23 of their commitment to the issuance upon completion of the framework for issuance.	**Results Indicator #4:** Volume of sovereign green bond issuances (Rs. billion)	Rs. 0 (March 2022)	Rs. 230 billion (June 2023)
Prior action #5: The Borrower, to ensure transparent and standardized disclosures on the ESG parameters, through its securities regulator, SEBI, (i) has revised the ESG reporting guidelines for the top 1,000 listed companies by market capitalization; and (ii) has, through AMFI, issued guidelines on disclosure norms for investments made by ESG mutual funds.	**Results Indicator #5:** Share of top 1,000 listed companies complying with enhanced ESG disclosure requirements (percent)	0 (March 2022)	100 percent (June 2024)

Prior actions	Results		
	Indicator Name	**Baseline**	**Target**
Prior action #6: The Borrower, through its Ministry of Power, has: (i) designated BEE as the nodal agency to set up a voluntary national carbon market and trading scheme to promote low-carbon alternatives; and (ii) through BEE, has prepared and disclosed a blueprint document laying out the rules and modalities for the functioning of a national carbon market overseen by a high-level inter-ministerial committee.	**Results Indicator #6:** Trading Platform established to facilitate the National Carbon Market (Yes/No)	No (March 2022)	Yes (June 2024)
Pillar 3: Improving access to credit for MSMEs and women entrepreneurs			
Prior action #7: The Borrower, through CGTMSE, has strengthened the Credit Guarantee Scheme for Banks (CGS-I) and Credit Guarantee Scheme for NBFCs (CGS-II) for serving the needs of Micro and Small Enterprises (MSE) sector during recovery stage through: (i) expanding the limit for guarantee cover per borrower; and (ii) introducing guarantee cover for co-lending by banks and NBFCs.	**Results Indicator #7:** Volume of incremental guarantee covers under CGTMSE (Rs. billion) **Results Indicator #8:** Volume of guarantees under CGTMSE approved toward loan accounts of women entrepreneurs (Rs. billion)	Rs. 368.9 billion (FY 2020-21) Rs. 51.6 billion (FY 2020-21)	Rs. 500 billion (FY 2022-23) Rs. 75 billion (FY 2022-23)
Prior action #8: The Borrower, through NCGTC, has revised the guidelines for the operations of the Emergency Credit Line Guarantee Scheme (ECLGS) to ensure MSMEs in sectors worst affected by COVID-19 have continued access to the Guaranteed Emergency Credit Line.			
Prior action #9: The Borrower, through NCGTC, has implemented the Credit Guarantee Scheme for Micro-Finance Institutions (CGSMFI) in support of small borrowers and women entrepreneurs impacted by COVID-19.	**Results Indicator #9:** Total lending under CGSMFI primarily to women borrowers (Rs. billion)	0 (July 2021)	Rs. 90 billion (July 2022)

ANNEX 2: FUND RELATIONS ANNEX

India—Assessment Letter for the World Bank

May 5, 2022

Recent Developments, Outlook, and Risks

1. Growth recovered in fiscal year (FY) 2021/22, while inflation rose. After a strong rebound in April-September 2021, real GDP grew by 5.4 percent (year-on-year) in 2021Q4, reflecting some softening in industries and an upward revision in historical growth. High frequency indicators in 2022Q1 suggest a temporary and milder-than-expected impact from the Omicron wave in the context of a high vaccination rate[1]. Consequently, real GDP growth is estimated at 8.9 percent in FY2021/22 (April-March), back to pre-pandemic levels, following a contraction of 6.6 percent in the previous fiscal year. While the recovery has become more broad-based, it is still lagging in contact-intensive services and in micro, small and medium enterprises (MSMEs). Headline inflation rose rapidly in recent months, reaching 7 percent in March 2022, and bringing the fiscal year average to 5.5 percent. Inflation is being partly driven by higher food prices, but core inflation has also risen. The authorities have to date refrained from using administrative measures to contain inflationary pressures with few exceptions.[2] The current account balance returned to a deficit estimated at about 1.6 percent of GDP in FY2021/22, which reflected the recovery in domestic demand and higher oil and commodity prices.

2. Growth is expected to soften in FY2022/23 on the back of external shocks. Growth is now projected at 8.2 percent in FY2022/23, with 0.6 percentage points of the deceleration reflecting projected headwinds from the impact of the war in Ukraine. The war in Ukraine and related sanctions on Russia are expected to affect the macro economy through multiple channels, most prominently through higher oil and other commodity prices and lower external demand. These price shocks are expected to adversely impact both domestic consumption and investment and increase inflationary pressures, with weaker external demand weighing on exports (partly offset by rising wheat and rice exports). In addition, financial and confidence effects due to high uncertainty are expected to weigh on domestic demand at least in the short term. Inflation is projected at 6.1 percent in FY2022/23, reflecting higher food prices and input costs, rising oil and commodity prices and sticky core inflation amid strengthening demand. The current account deficit is expected to widen to about 3.1 percent in FY2022/23, reflecting both higher international oil prices and pent-up domestic demand amid economic recovery from the pandemic.

3. The financial sector has been recovering but prospects remain uncertain. Bank credit growth has increased to 9.6 percent in March 2022, rising above pre-pandemic levels. However, the recovery appears uneven. On the demand side, the acceleration in bank lending is mainly driven by demand from MSMEs, while large corporations have been shifting towards funding from capital markets. On the supply side, credit growth by private banks continues to outpace

[1] As of mid-April, 98.3 percent of the population over 15 years has been vaccinated with at least one dose and 89.9 percent with two doses.

[2] The authorities had cut crude palm oil import duties before the outbreak of the Ukraine war in the face of rising prices on this important food staple in India.

credit growth by public banks. The aggregate gross NPL ratio across the banking sector has declined to 6.9 percent from over 8 percent in March 2020. However, this improvement may turn out to be temporary, and the Reserve Bank of India stress tests suggest that bank wide gross NPA ratio may increase to 8.1 percent by September 2022 under the authorities' baseline growth path, and 10.5 percent for public sector banks.

4. **Uncertainty about the economic outlook is exceptionally high, with near-term growth risks tilted to the downside**. The downside risks are driven in large part by the ramifications of the war in Ukraine and related sanctions on Russia, which can be amplified if other macroeconomic risks materialize—for example, future pandemic waves, including from the emergence of new variants that could put pressure on the health system and on the recovery; further or protracted disruptions to food supply chains; geopolitical tensions; or a widespread global risk-off event associated with faster-than-anticipated monetary policy normalization in advanced economies. On the upside, a successful implementation of the announced wide-ranging structural reforms could increase India's growth potential in the medium- and long-term. Given the recent volatility of inflation expectations and the significant risks of second-round effects in light of the protracted and large oil and commodity price shock, inflationary risks are on the upside.

Policy Response and Settings

5. **Fiscal policy is projected to remain accommodative in the near-term**. The general government fiscal deficit is projected to decline modestly from 12.8 percent of GDP in FY2020/21 to 10.4 percent in FY2021/22, reflecting strong growth in revenues and a partial withdrawal of support measures. The FY2022/23 budget is estimated to broadly maintain the accommodative fiscal stance from last fiscal year and emphasizes capital expenditure and infrastructure spending in particular, while current spending is projected to be contained (although food rations have been extended to September 2022). Heightened uncertainty around the outlook, reflecting the war in Ukraine, would require that policies remain agile and adjust swiftly to maintain macroeconomic stability. An accommodative fiscal stance, with additional support targeted to vulnerable households, is warranted given weaker growth prospects. The authorities' continued focus on public infrastructure also bodes well for supporting the recovery. In that context, implementation remains key. Education, health, and social safety nets are among the other long-standing expenditure priorities, which are critical for achieving the Sustainable Development Goals and boosting potential growth. The continued practice of enhanced fiscal transparency, and the budget's realism regarding macroeconomic and revenue projections are also welcome.

6. **A concrete medium-term fiscal consolidation plan remains critical to ensure credibility and reduce fiscal risks.** Medium-term fiscal space is more limited given the sharp increase in public debt—estimated to have reached 90 percent of GDP in FY2020/21 and

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expected to moderate slightly to 87 percent in 2022/23.[3] Public debt is projected to remain elevated over the medium-term, and a gradual fiscal consolidation will be critical for meaningful debt reduction. Fiscal risks have increased given the higher debt level, but India's public debt is denominated in domestic currency and predominantly held by residents, helping to reduce external financing risks. While a privatization program, if fully implemented, can provide fiscal space, a concrete medium-term consolidation plan anchored on revenue mobilization and improved expenditure efficiency will be needed to put debt on a durable downward trajectory, regain fiscal space, and reinforce market confidence.

7. **The Reserve Bank of India (RBI) has maintained an accommodative stance since early 2019 to support the economy through the pandemic but has recently appropriately shifted towards reduced accommodation.** Starting from March 27, 2020, the repo and reverse repo rates were gradually reduced by 115 and 155 basis points (bps), respectively, to 4 and 3.35 percent, building on the pre-COVID easing of 135 bps to further support the economy amid the COVID-19 shock. While maintaining the accommodative stance, and in light of inflationary pressures, the RBI signaled in April 2022 a pivot toward tighter policy. Furthermore, in an off-cycle MPC meeting in May 2022, policy rates were raised by 40 bps and the cash reserve ratio was raised by 50 bps, with forward guidance emphasizing the withdrawal of accommodation, while still supporting growth.

8. **Given the recent sharp increase in global commodity prices, higher domestic input costs and sticky core inflation, monetary policy needs to remain nimble.** Inflationary pressures remain elevated given rising commodity prices and sticky core inflation. Inflation has risen above the RBI's target bank of 4±2 percent and inflation expectations have remained elevated, with higher volatility. Over the near term, given the sizable and likely protracted shock, second round effects are highly likely. Monetary policy will need to respond nimbly, including through well-communicated expectations about the trajectory of inflation and the path of policy rate actions to address any second-round inflationary effects. Exchange rate flexibility should remain a shock absorber, while avoiding excessive volatility.

9. **A combination of near-term targeted support and structural reforms in the financial sector are important to ensure a speedy and sustained recovery of credit**. Borrower and lender relief measures adopted during the pandemic have expired except for a government guarantee scheme for MSMEs, which has been extended for FY2022/23. In this context, while targeted support can enhance the ability of the financial sector to sustain growth, policies should also facilitate the exit of nonviable firms and further strengthen the balance sheet of banks. By encouraging banks to increase capital buffers and to recognize problem loans, the authorities would prevent the potential increase in corporate insolvencies from negatively affecting credit supply. In this respect, an appropriate design of the recently established National Asset Reconstruction Company (NARCL) should follow best international practice to achieve

[3] Debt was projected to be sustainable in the Debt Sustainability Analysis for Market Access Countries last completed in September 2021, owing to a favorable debt dynamic. An update of the Debt Sustainability Analysis will be conducted in the context of the IMF's 2022 Article IV consultation with India.

effective loan loss recoveries and limit costs to taxpayers. Structural reforms in the financial sector, including governance reforms in public sector banks and continued efforts to reduce the government's presence in the sector, are also important to maximize medium term growth.

10. **India's external position is sufficiently strong to withstand external shocks in the near term, and the government is taking steps to promote trade and investment.** Pandemic-induced current account surpluses and large portfolio capital inflows in 2020-21 as well as the additional SDR allocation of about 0.6 percent of GDP allowed the RBI to replenish its international reserves. The current account balance returned to deficit from 2021H2, reflecting recovering domestic demand and rising oil and commodity prices. While FDI inflows remain steady, the portfolio investment flows are highly volatile. In 2022Q1, India experienced large speculative capital outflows, which reflected investors' concerns about the Omicron wave, the rise in U.S. yields and expectations of future U.S. Federal Reserve policy tightening, and the outbreak of the war in Ukraine. The exchange rate depreciated somewhat but remained broadly stable (and in line with fundamentals), and international reserves are at a comfortable level (covering about 8 months of prospective imports). The focus on bilateral trade agreements and the shift from direct export promotion to the development of export infrastructure (under the Trade Infrastructure for Export Scheme) is expected to support a sustainable increase in exports over the medium term. The authorities have eased limits on foreign portfolio inflows and have not resorted to any major capital flow measures (CFMs) on outflows or foreign exchange intervention (FXI) in recent months.

11. **A continued push for structural reforms is needed to achieve more inclusive and sustainable medium-term growth.** The authorities' structural reform package—including reforms to trade FDI regulations and privatization of non-strategic sectors—is an important step in the structural reform agenda. However, delays in other reforms—including agriculture, financial sector, and labor markets—could hurt growth over the medium term. It is also crucial that the social safety net adequately protect those who might be hurt during the transition. This may require expanding coverage through portable urban programs to scale up support for informal workers and vulnerable households, improving the identification and targeting of new beneficiaries, and ensuring that the job market can accommodate the people impacted by the reforms (including through active labor market policies). Overall, the growth benefits of these reforms will depend critically on the effectiveness, capacity, and timing of implementation. Looking ahead, long-standing priorities include infrastructure investments, land reforms, and labor reforms—including increasing female labor force participation and access to finance to create more and better jobs.

IMF Relations

12. India is on a standard 12-month Article IV consultation cycle. The 2021 Article IV consultation was concluded by the IMF's Executive Board on September 17, 2021. The next Article IV consultation mission is expected in September 2022. The IMF continues to engage closely with the Indian authorities through capacity development (CD) activities, including through the South Asia Regional Training and Technical Centre (SARTTAC).

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India: Selected Economic Indicators, 2017/18-2022/23

Population (2020/21):1.38 billion
Quota (current): SDR 13,114.4 millions/ 100 percent of quota
Per capita GDP (2020/21 estimate): 1927 USD
Literacy rate (2018): 74.37%
Poverty rate $1.90 a day PPP (2011): 22.5%
Main products and exports: Petroleum, chemical and primary products, business and IT services.
Key export markets: EU, USA, United Arab Emirates, China, Singapore, and Saudi Arabia.

FISCAL YEAR 1/	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23
					Est.	Projections
Output						
Real GDP growth (%)	6.8	6.5	3.7	-6.6	8.9	8.2
Prices						
Inflation, CPI-Combined (%)	3.6	3.4	4.8	6.2	5.5	6.1
General government finances						
Revenue (% of GDP)	20.0	20.0	19.9	18.3	19.7	18.9
Expenditure (% of GDP)	26.2	26.3	27.4	31.1	30.1	28.8
Fiscal balance (% of GDP)	-6.2	-6.4	-7.5	-12.8	-10.4	-9.9
Public debt (% of GDP)	69.7	70.4	75.1	90.1	86.8	86.9
Money and credit						
Broad money (% change)	9.2	10.5	8.9	12.2	9.1	7.2
Domestic Credit (% change)	7.8	11.7	8.3	9.2	10.9	10.8
Credit to the private sector (% change)	9.5	12.7	6.3	5.7	10.4	10.8
3-month Treasury bill interest rate (%) 2/	6.2	6.2	4.4	3.3	3.5	...
Balance of payments						
Current account (% of GDP)	-1.8	-2.1	-0.9	0.9	-1.6	-3.1
FDI, Net Inflow (% of GDP)	1.1	1.1	1.5	1.6	1.1	1.6
Reserves (months of imports)	7.9	8.2	11.1	9.0	8.1	7.3
External debt (% of GDP)	20.0	20.1	19.7	21.4	21.0	21.3
Exchange rate						
REER (% change) 3/	3.5	-5.0	3.3	-0.9	-1.0	...

Sources: Data provided by the Indian authorities; Haver Analytics; CEIC Data Company Ltd; Bloomberg L.P.; World Bank, World Development Indicators; and IMF staff estimates and projections.
1/ Fiscal Year is April to March (e.g. 2019/20 = Apr-2019 - Mar-2020).
2/ For 2021/22: Data provided is average of April 2021 to January 2022 to reflect fiscal year.
3/ For 2021/22: The change in the average for April-December 2021 from April-December 2020.

ANNEX 3: LETTER OF DEVELOPMENT POLICY

रजत कुमार मिश्र, भा.प्र.से.
अपर सचिव
Rajat Kumar Mishra, IAS
Additional Secretary

सत्यमेव जयते

75 Azadi Ka Amrit Mahotsav

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D.O. No. 19/02/2021/F.B-II

Date : June 01, 2022

Dear Mr. President,

I would like to thank you, and the World Bank Group for the timely and important support to the Government of India in the very important area of financial sector reforms and development. The proposed DPF will support India in its efforts to rebound from the COVID19 pandemic and to realize its growth targets by further strengthening the financial sector to support infrastructure development, private capital mobilization and catalyzing inclusive and sustainable growth.

2. The proposed DPF, supports the priorities of the Government of India (GoI) as announced through the national Budget and initiatives to support MSMEs and economic recovery from the COVID19. World Bank's programmatic engagement with the GoI over the last three years has been instrumental in bringing global best practices, knowledge and analytical support for advancing the financial sector reforms and infrastructure development. Firstly, the DPF builds on the technical assistance from the WBG to support the GoI in mobilizing private sector financing to address the infrastructure and housing finance gaps in India. The WBG has been assisting to deepen the debt-capital market and build capacity to prioritize projects (including through a climate lens) to deliver the ambitious National Infrastructure Pipeline (NIP) over next three years. Secondly, the WBG has been engaged with the GoI and other important stakeholders on climate finance, including through the Sustainable Finance Task Force. As India continues to identify the means to achieve its COP26 and NDC commitments, it is clear that private sector financing for the transformation of the economy will be critical, and thus green financing forms an important element of this DPF. Thirdly, the WBG's support to the MSME sector has been vital. The Emergency MSME Response DPL (2020), which supported important measures such as the Emergency Credit Line Guarantee Scheme (ECLGS) and Credit Guarantee Trust for MSEs (CGTMSE) has ensured that MSME sector is able to recover from the challenges posed by COVID-19. Through this DPL, support to the MSME sector continues and the financial sector is further reformed to be able to appropriately meet the needs of the sector. The GoI stays committed towards supporting the MSME sector through existing and new schemes, including the plan to allow medium sized enterprises to benefit from the guarantee cover available under the CGTMSE scheme in due course.

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3. Going forward, Infrastructure and Green Finance will remain important focus areas of the GoI, and we envisage this DPF as an important step among the broader programmatic engagement with the World Bank. We would like to further explore with the WBG other possible reforms and financing schemes to fund, as appropriate, the recently set up world class Development Finance Institution for the infrastructure sector, the National Bank for Financing Infrastructure and Development (NaBFID), with an objective to leverage and mobilize long-term financing from private sector, including through capital markets. Further, the GoI may revert with additional requests for capacity building and technical support, especially in the context of (i) the establishment of a securitization platform for the Housing Sector; and (ii) developing an efficient and sustainable framework for Sovereign Green Bonds.

4. The establishment of a well-managed infrastructure DFI with a mandate to crowd-in private sector and, introducing the credit enhancement products to mobilize private and public financing for infrastructure are expected to meet the infrastructure financing gap to large extent. The GoI is fully committed in making the new DFI (NaBFID) operational by the first half of the Fiscal Year 2022-2023, and would in due course assign performance indicators as appropriate. The new entity's envisioned structure, product mix, and governance would broadly be in line with the global best practices, and I am confident that by offering a variety of lending instruments, including green finance and credit enhancement products as appropriate, NaBFID would substantially help in leveraging private sector financing in the country.

5. The GoI is also focused on ensuring "Housing for All", and to meet this goal is implementing the PMAY Scheme (Pradhan Mantri Awas Yojana) and other initiatives. We recognize the need to further improve access to housing finance. The proposed National Housing Bank (NHB) led securitization platform, which has benefitted from the ongoing technical support from the World Bank and IFC, is a step towards enhancing sustainable long-term funding for housing. Strengthening the ability of lenders, including Housing Finance Companies (HFCs), to raise sustainable long-term funds through the securitization platform will allow them to introduce innovative housing finance products, and increase availability of affordable housing. We look forward to continued support from the WBG in operationalizing the securitization platform over the next twelve to eighteen months.

6. The focus of this DPF on Greening of the financial sector is well aligned with the government's priorities to make the financial sector resilient and build capacity to address risks arising from climate change. The recent national Budget has announced the issuance of India's first sovereign green bond, along with the framework for utilization and monitoring for these bonds, which reflects a strong

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commitment from the government to fund green investments in the country. The first issuance of the sovereign green bond is expected to be completed in the FY2022-23. These bonds will provide and improve benchmark pricing, liquidity and a demonstration effect for local issuers, helping to support the growth of a local market.

7. Further, the government intends to develop a national carbon market to catalyze low-carbon investments aligned with India's national climate goals. Government has set-up a high-level steering committee in March 2022, which will provide the strategic direction for India's climate goals, ensuring alignment with the National Objectives and recommendations of the Apex Committee for Implementation of the Paris Agreement (AIPA). Over the next 12-18 months, the Bureau of Energy Efficiency (BEE) will develop the policy on the national carbon market, including the regulatory framework, management of instruments, participation methodology etc. This policy will form the basis for amendments to the Energy Conservation Act, and setting up of a trading platform to facilitate the national carbon market. We would welcome World Bank Group's global expertise in climate finance to build capacity and alignment with globally accepted frameworks for climate finance.

8. Please let me reiterate that Government of India is fully committed to implement these policy and regulatory reforms in the most effective way, and to optimize the impact of this requested DPF operation which represents a very important support at a critical time of our sector engagement.

9. We look forward to the World Bank's continued support in this endeavor in meeting our overall Government developmental agenda.

With warm regards,

Yours sincerely,

(Rajat Kumar Mishra)

HE Mr. David Malpass
President
World Bank Group
Washington DC
USA

ANNEX 4: ENVIRONMENT AND POVERTY/SOCIAL ANALYSIS TABLE

Prior Actions	Significant positive or negative environment effects	Significant poverty, social or distributional effects positive or negative
Pillar One: Catalyzing long term private sector finance		
Prior Action 1: The Borrower has established the National Bank for Financing Infrastructure and Development (NaBFID), as a development financial institution with the mandate of offering credit enhancement products and mobilizing long term private finance for the infrastructure sector, pursuant to which (i) the Government of India has allocated capital; and (ii) NaBFID shall be regulated and supervised by the Borrower's central bank, RBI.	**Significant positive and possible negative environmental impacts**: The establishment of a financing facility through NaBFID will enable the unlocking of capital to finance projects supporting COP26 commitments and NDCs, having significant positive environmental effects. However, it might also pave the way for increased investment and implementation of medium to large infrastructure projects that would have significant physical footprints and could have negative environmental impacts. Some types of infrastructure are exempt from the national EIA regulation from securing environmental clearance. This might pose some uncertainty regarding the ability of the investors to assess environmental risk for some of the infrastructure projects. The capacity and the ESMS of the NaBFID as a financial intermediary that lends money to investors may need to be established, with relevant WB TA if required. .	**Expected positive effects**: Enhancing financing modalities to improve infrastructure facilities will benefit the society at large, including by improving the quality of the infrastructure facilities in underserved geographical regions.
Prior Action 2: The Borrower (i) through NITI Aayog has launched the National Monetization Pipeline (NMP) to create greenfield infrastructure assets by recycling brownfield core assets of the Borrower; (ii) through RBI, has permitted FPIs to invest in debt securities issued by InvITs; and (iii) through the Ministry of Labour and Employment, has approved investments of up to 5 percent of EPFO's annual deposits in AIFs, including InvITs.	**Low negative environmental impacts:** Both the NMP and the InvIT are avenues for the government to earn a substantial stream of revenue through monetizing already existing infrastructure assets. Therefore, no significant negative environmental impacts are expected.	No adverse social or poverty impacts are expected.

Prior Action 3: The Borrower has taken steps to link housing finance companies to capital markets through securitization: (i) through RBI, by the issuance of the revised regulatory framework for Securitization of Standard Assets; and (ii) through NHB, by approving the setting up of a multi-originator Residential Mortgage-Backed Securities (RMBS) Pass through Certificate (PTC) securitization platform.	**No environmental impacts**: Improving access to financing of HFCs and other primary lending institutions through securitization has no material environmental effects.	**Expected positive effects**: Improved assess to long-term funding by HFCs and other primary lending institutions is expected to increase access to housing finance products in various market segments, at more favorable terms, which should result in positive poverty and social impacts.
Pillar 2: Developing the markets for green finance		
Prior Action 4: The Borrower has taken steps for the launch of the country's first sovereign green bonds, as evidenced by: (i) the policy decision of the Union Government to issue sovereign green bonds in FY 2022-23 as part of the overall government borrowing; and (ii) the RBI's inclusion in the borrowing calendar for H1 FY2022-23 of their commitment to the issuance upon completion of the framework for issuance.	**Significant positive environmental impacts:** Issuing Indian sovereign green bonds would not only raise awareness of the challenges of climate change, but also demonstrate the potential for institutional investors to support climate-smart investments. This would stimulate more long-term institutional investors with a focus on ESG priorities and could catalyze more Indian corporate green issuances, thereby adding to the pool of global green bond market.	No adverse social impacts are expected. The funding raised through sovereign green bond will finance climate adaptation and mitigation investments, with expected positive social externalities.
Prior Action 5: The Borrower, to ensure transparent and standardized disclosures on the ESG parameters, through its securities regulator, SEBI, (i) has revised the ESG reporting guidelines for the top 1,000 listed companies by market capitalization; and (ii) has, through AMFI, issued guidelines on disclosure norms for investments made by ESG mutual funds.	**Significant positive environmental impacts:** Enhanced ESG disclosure guidelines for listed companies and mutual funds will enable the financial sector to attract more capital and investments towards sustainability and support regulators in introducing green finance taxonomy consistent with global practices on environmental management policies and regulations.	**Expected positive effects:** Disclosure of the ESG framework will strengthen systems on transparency and reporting for informed decision making by the investors.
Prior Action 6: The Borrower, through its Ministry of Power, has: (i) designated BEE as the nodal agency to set up a voluntary national carbon market and trading scheme to promote low-carbon alternatives; and (ii) through BEE, has prepared and	**Significant positive environmental impacts:** This structured approach to developing carbon markets will help harness synergies across different policy measures by various ministries to accelerate mitigation; thereby providing strategic direction to	No adverse social or poverty impacts are expected.

disclosed a blueprint document laying out the rules and modalities for the functioning of a national carbon market overseen by a high-level inter-ministerial committee.	develop the carbon market. This will play a crucial role in catalyzing low-carbon investments in India.	
Pillar 3: Improving access to credit for MSMEs and women entrepreneurs		
Prior Action 7: The Borrower, through CGTMSE, has strengthened the Credit Guarantee Scheme for Banks (CGS-I) and Credit Guarantee Scheme for NBFCs (CGS-II) for serving the needs of Micro and Small Enterprises (MSE) sector during recovery stage through: (i) expanding the limit for guarantee cover per borrower; and (ii) introducing guarantee cover for co-lending by banks and NBFCs.	**Low negative environmental impacts:** Considering the compliance of the MSME sector with the institutional, legal and regulatory framework for environmental protection is moderate (albeit significantly improving recently), there could potentially be low negative environmental impacts.	**Expected positive effects:** Access to credit facilities will increase the total number of women entrepreneurs and micro-entrepreneurs from socially excluded groups.
Prior Action 8: The Borrower, through NCGTC, has revised the guidelines for the operations of the Emergency Credit Line Guarantee Scheme (ECLGS) to ensure MSMEs in sectors worst affected by COVID-19 have continued access to the Guaranteed Emergency Credit Line.	**Low negative environmental impacts:** Considering the compliance of the MSME sector with the institutional, legal and regulatory framework for environmental protection is moderate (albeit significantly improving recently), there could potentially be low negative environmental impacts.	**Expected positive effects:** GoI's support to extend guarantee will increase opportunities for those who were pushed outside the job market during the pandemic to secure jobs and livelihood.
Prior Action 9: The Borrower, through NCGTC, has implemented the Credit Guarantee Scheme for Micro-Finance Institutions (CGSMFI) in support of small borrowers and women entrepreneurs impacted by COVID-19.	**Low negative environmental impacts:** Low negative environmental impacts are expected given the relatively low capacity of many MFIs to screen environmental risk.	**Expected positive effects:** The credit guarantee for MFIs enables women entrepreneurs to access credit and mitigate the poverty and social fallout from COVID-19.