This is a new section of the Public-Private Partnership Resource Center website and is currently in draft form. Your feedback is welcome: If you would like to comment on the content of this section of the website or if you have suggestions for links or materials that could be included please contact us at ppp@worldbank.org.

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Key-findings-to-scale-up private sector capital for ERC activities, Businessman holding coin with graph and tree grov

# Key Findings to Scale Up Private Sector Capital for ERC Activities

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***On this page:*** *An overview of three non-mutually exclusive options to scale up private sector capital for ERC activities. Read more below, or visit Strategic Guidance for Country System Assessments, Guidance for Countries in Assessing ERC Projects, or Mobilizing ERC Finance.*

DFI pilots to attract commercial investment to ERC activities have been highly informative but limited in their ability to scale. Instruments and funds designed to attract broad interest from financiers, beyond leading-edge buyers or specialist financial intermediaries, have been reliant on intensive DFI engagement to date, which is helpful for piloting, but will always be limited in scale.

Most financiers are still cautious about financing ERC activities. ERC markets have reached a level of maturity where some large lenders and bond investors are interested in investing further but still need to mitigate market and political risk exposure. Additionally, some banks are engaging with ERCs as a commodity play, but many are still not comfortable engaging in the market at all.

To scale ERC finance, the fundamental enabling environment for ERC transactions will have to improve. While there are numerous initiatives to improve the enabling environment and encourage greater ERC investment, the market is still relatively nascent. As such, several challenges remain pervasive, including a lack of consistent rules and regulations, standardized contracts and approaches, critical market infrastructure, mechanisms to ensure transparency and accountability, and—most importantly—an understanding of the legal nature of an ERC and what it represents. Knowledge and capacity building is required across the entire ecosystem—including governments, financiers, buyers and sellers, and ERC activities. Coordination amongst initiatives seeking to address these gaps will be critical to the long-term success and growth of the market.

Improving the ERC market fundamentals will be critical to scaling investment, but directly mobilizing capital is necessary too. The fundamental building blocks of the market need to improve to address critical market and political risks for investors. However, the market will remain stunted unless more investment happens now, and the market will never reach the anticipated necessary scale without immediately scaling up investment. It is essential to continue developing ERC financing solutions alongside establishing the market fundamentals to have any chance of mobilizing private sector finance at the scale required.

The next generation of ERC-backed structures should explore putting more principal at risk and offer different levels of ERC market exposure to attract greater investment. Early instruments and funds often relied on general credit enhancement through principal protection, credit guarantees, or first-loss capital. To deepen the capital base for ERC activities, a next generation of ERC-backed financing should be deployed on riskier but still investible counterparties (e.g., investment-grade sovereigns) and put more principal at risk against ERC performance. Recent “innovative” instruments and funds have experimented with better

matching ERC market risk and appetite either through optional ERC (-linked) returns or financial structuring to channel specific risks to specific financing parties, where those taking market risk also get delivery assurance.

Political risk insurance covering ERC activities should be brought to market and scaled. ERC markets are inherently policy driven and investment in ERC activities will be subject to a high degree of political risk while national policy frameworks are being established (e.g., carbon rights, authorization process). Political risk insurance is critical to help mobilize investment now while such policies are put in place.

Three non-mutually exclusive options to scale up private sector capital for ERC activities appear particularly promising at this stage of market maturity and given current investor appetite:

- Support ERC-backed debt issuance with targeted support. Debt instruments partially linked to or paid back in ERCs have been successfully piloted and could be scaled and replicated by non-multilateral issuers supported by the tailored use of concessional risk mitigation.
- Aggregate supply and mobilize capital to a broader set of ERC activities. Financial intermediation is common in the ERC market. With sufficient DFI support, both financial and technical, ERC activities from smaller or hard-to-reach markets that are not able to raise ERC-linked debt on their own could collectively raise capital.
- Establish an ERC club to pool demand and promote standardized approaches. Buyer's clubs can send a strong market signal and more practically reduce market risk and improve the expected cash flows of ERC activities, which helps to unlock debt capital, especially when other market participants are invited into the club. Those benefits can potentially be heightened through an Article 6.2 club that provides a government-sanctioned path to market.

#### Additional Resources

- UNCITRAL Legislative Guide on Public-Private Partnerships
- World Bank Guidance on PPP Legal Frameworks
- Climate-Smart PPP Legal and Regulatory Framework

*This section is intended to be a living document and will be reviewed at regular intervals. The Guidelines have not been prepared with any specific transaction in mind and are meant to serve only as general guidance. It is therefore critical that the Guidelines be reviewed and adapted for specific transactions. Unless expressly stated otherwise, the findings, interpretations, and conclusions expressed in the Materials in this Site are those of the various authors of the Materials and are not necessarily those of The World Bank Group, its member institutions, or their respective Boards of Executive Directors or member countries. For feedback on the content of this section of the website or suggestions for links or materials that could be included, please contact the Public-Private Partnership Resource Center at ppp@worldbank.org.*