HSR (LONDON),
HOUGHTON STREET REVIEW JOURNAL
ISSN: 2058-5519|Impact factor-15.9
http://houghtonstreetreview.com/index.php/hsr

CONTEMPORARY SOURCES OF INVESTMENT PROJECT FINANCING: BANK CREDIT, PRIVATE CAPITAL AND INTERNATIONAL FINANCIAL INSTITUTIONS

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doi:https://doi.org/10.5281/zenodo.23182670

Abstract. This article examines how three major categories of external capital – commercial bank credit, private capital, and international financial institutions (IFIs) – differ in their ability to finance investment projects, and how they can be combined in a coherent capital structure.

The study uses an integrative, theory-driven review of the corporate finance, financial intermediation and development finance literature. Sources are compared against six analytical criteria: cost of capital, tenor, risk allocation, information and monitoring requirements, accessibility, and non-financial value added.

Bank credit remains the most accessible and best-monitored source but is constrained by short tenors, collateral requirements and maturity mismatch in long-term projects. Private capital (venture capital, private equity, infrastructure funds and project-level equity) offers risk-bearing capacity and governance expertise at a higher required return. IFIs provide long tenors, concessional pricing and a signalling effect, yet involve stringent eligibility, environmental and procedural requirements. The comparison shows that the three sources are complementary rather than substitutable.

Effective project financing depends on matching the source of capital to the project's life-cycle stage, risk profile and cash-flow pattern. Blended structures in which IFI participation mobilises commercial and private capital offer the most promising route for capital-intensive projects in emerging markets. The article concludes with a decision framework and directions for empirical research.

Keywords: project finance; investment financing; bank credit; private equity; international financial institutions; blended finance; capital structure.

Introduction. Investment projects – in infrastructure, energy, manufacturing and services – are the primary channel through which savings are converted into productive capacity, and the way they are financed shapes their cost, resilience and ultimate success. Since Modigliani and Miller (1958) established the irrelevance of capital structure under perfect markets, a large literature has shown that real-world frictions – asymmetric information, agency costs, taxes and incomplete contracts – make

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the choice of financing source consequential (Jensen & Meckling, 1976; Myers & Majluf, 1984; Stiglitz & Weiss, 1981).

The financing landscape has changed substantially over the past two decades. Post-crisis banking regulation has raised the capital cost of long-dated bank lending (Basel III), while institutional investors, private equity and infrastructure funds have expanded their role as providers of long-term capital (Kaplan & Strömberg, 2009). At the same time, multilateral development banks and other international financial institutions have moved from being direct lenders to acting as catalysts of private investment, through guarantees, co-financing and blended finance instruments (Mazzucato & Penna, 2016; Gatti, 2018). Firms and project sponsors, particularly in emerging and transition economies, therefore face a broader but more complex menu of financing choices.

Existing research typically studies each source in isolation: the bank-lending channel, venture capital and private equity, or development finance. Comparative treatments that evaluate the three sources against a common set of criteria, and that address how they interact within a single project's capital structure, are comparatively rare. This gap matters for practitioners, who must decide not only which source to use but also when and in what combination.

Aim. The article aims to develop a comparative framework for selecting and combining bank credit, private capital and IFI financing for investment projects.

Research questions. The study addresses three questions: (1) what are the distinguishing economic characteristics of each source of financing, and what theoretical mechanisms explain them; (2) how do the sources compare in terms of cost, tenor, risk allocation, monitoring and accessibility; and (3) under what conditions do the sources complement one another, and what does this imply for structuring project finance.

The remainder of the paper is organised as follows. Section 2 describes the analytical design. Section 3 presents the results for each source and their comparison. Section 4 discusses implications, blended structures and limitations. Section 5 concludes.

Materials and Methods.

1. Research design. The study adopts an integrative, theory-driven review design combined with a structured comparative analysis. This design is appropriate because the research questions concern the relative properties of financing sources and the mechanisms behind them, rather than the estimation of a single causal effect. The unit of analysis is the financing source as an institutional arrangement, evaluated in the context of a long-lived investment project.**2. Theoretical foundations.** Three strands of theory structure the analysis. The first is financial intermediation and credit rationing: banks reduce information asymmetry through screening and monitoring, but adverse selection and moral hazard can lead to credit rationing (Stiglitz & Weiss, 1981; Berger & Udell, 1998). The second is capital structure and agency theory: the pecking-order and agency-cost frameworks explain why internal funds, debt and outside equity carry different costs and control implications (Jensen & Meckling, 1976; Myers & Majluf, 1984; Fazzari, Hubbard & Petersen, 1988). The third is project

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finance and development finance: non-recourse structures, contractual risk allocation and the catalytic role of public and multilateral institutions are analysed in the project-finance and development-finance literature (Esty, 2004; Yescombe, 2013; Gatti, 2018; Mazzucato & Penna, 2016).

3. Source categories. The three categories are defined as follows. Bank credit covers senior and syndicated loans, credit lines and leasing provided by commercial banks, including project loans with limited recourse. Private capital covers venture capital, private equity, infrastructure and private-credit funds, and direct equity from strategic or institutional investors. International financial institutions are multilateral and bilateral development banks and agencies providing loans, equity, guarantees and technical assistance.

4. Comparative criteria. Each source is assessed against six criteria, derived from the theoretical strands above and commonly used in project appraisal.

Cost of capital is the return required by the provider, including fees and collateral costs. Tenor and flexibility refers to maturity, grace periods and the repayment profile relative to the project's cash flows. Risk allocation is the degree to which the provider bears construction, market and completion risk. Information and monitoring requirements cover due diligence, covenants and reporting obligations. Accessibility reflects eligibility conditions, transaction costs and the time required to close. Non-financial value added covers governance, technical expertise, signalling and access to networks.**5. Analytical procedure.** For each source, the mechanisms identified in the theoretical literature were mapped to the six criteria. The sources were then ranked ordinally (low / medium / high) on each criterion. These ratings are analytical judgements grounded in theory and in the institutional characteristics of each instrument, not statistical estimates; they describe typical rather than universal conditions and vary across countries and market cycles. The comparison was used to derive a decision framework matching sources to project life-cycle stages.

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6. Scope and sources of evidence. The analysis draws on established theoretical and empirical contributions in corporate finance, banking and project finance, and on the published characteristics of financing instruments. The scope is limited to external sources of long-term financing for real investment projects; short-term working-capital finance, internal funds and public budget financing are outside the scope, although they may complement the sources examined here. The framework is intended to be general, with particular relevance for bank-dominated financial systems in emerging and transition economies.

Results

1. **Bank credit.** Bank credit is the most widely used external source because banks combine screening, monitoring and liquidity provision within one relationship (Berger & Udell, 1998). Its principal strengths are accessibility for established borrowers, predictable pricing and relatively fast execution. Lenders typically obtain seniority and security over project assets, so the required return is lower than for equity.

Three limitations recur in the literature. First, maturity mismatch: banks fund themselves with short-term liabilities, so long-tenor loans are costly and, since Basel III, capital-intensive. Second, collateral and covenant dependence: firms lacking tangible assets or credit history are exposed to rationing (Stiglitz & Weiss, 1981) and to investment–cash-flow sensitivity (Fazzari et al., 1988). Third, limited risk-bearing: lenders are paid a fixed return and therefore avoid construction and demand risk, transferring it to the sponsor. Syndicated and limited-recourse project loans partly relieve these constraints but require robust contractual structures (Yescombe, 2013).

2. Private capital. Private capital comprises venture capital, private equity, infrastructure funds and private credit. Its defining feature is the willingness to bear residual risk in exchange for an equity-type return and control rights. Research on private equity documents that active governance, staged financing and performance-linked incentives can reduce agency costs and improve operating performance in portfolio companies (Jensen & Meckling, 1976; Kaplan & Strömberg, 2009).

The corresponding costs are a higher required return, dilution of ownership and control, and an exit horizon that may not match the project's natural life. Private capital is therefore best suited to projects with high growth potential, innovative content or a need for managerial upgrading, and to infrastructure assets with stable long-term cash flows where funds seek yield. In many emerging markets the supply of private capital is thin, and deal flow is concentrated in a small number of sectors.

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3. International financial institutions. IFIs, including multilateral development banks, provide long-tenor loans, equity participations, guarantees and technical assistance, frequently at pricing below that available commercially because of their preferred-creditor status and access to low-cost funding. Beyond finance, their participation has a signalling and certification effect: due diligence and adherence to environmental, social and procurement standards reassure commercial lenders and investors (Mazzucato & Penna, 2016).

The main constraints are procedural. IFI financing entails extended appraisal, strict safeguard and reporting requirements, minimum project size, and often a sovereign or quasi-sovereign counterpart or guarantee. Eligibility and priorities are also set by institutional mandates rather than by the borrower's preferences. As a result, IFI funds are most valuable for large, long-gestation, socially beneficial projects and for early demonstration of markets where private capital is initially reluctant to participate (Gatti, 2018).

4. Comparative assessment. Table 1 summarises the assessment of the three sources against the six criteria defined in Section 2.4. Ratings are ordinal and reflect typical conditions.

Table 1. Comparative assessment of external sources of project financing

Criterion	Bank credit	Private capital	International financial institutions
Cost of capital	Low to medium (senior, secured)	High (equity-type return)	Low to medium (long-term, sometimes concessional)
Tenor and flexibility	Short to medium; limited grace periods	Medium; exit-driven (typically 5–10 years)	Long; extended grace periods
Risk allocation	Low risk-bearing; recourse to sponsor or assets	High risk-bearing; residual claimant	Medium to high; can absorb political and early-stage risk via guarantees
Information and monitoring	Medium; covenants and periodic reporting	High; board involvement, milestones	High; safeguards, procurement and impact reporting
Accessibility	High for established borrowers	Medium; selective, deal-dependent	Low to medium; eligibility, size and time constraints
Non-financial value added	Low; banking relationship	High; governance and networks	High; technical assistance and signalling

Source: authors' analytical synthesis based on Berger & Udell (1998), Kaplan & Strömberg (2009), Yescombe (2013), Mazzucato & Penna (2016) and Gatti (2018).

No source dominates on all criteria. Bank credit is strongest on accessibility and price but weakest on tenor and risk-bearing; private capital is strongest on risk-bearing and governance but most

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expensive; IFIs are strongest on tenor and signalling but least accessible. This pattern of offsetting strengths indicates complementarity rather than substitution.

5. Matching sources to project stages. Because the risk profile changes over a project's life, the appropriate source changes too. Table 2 presents the resulting decision framework.

Table 2. Suggested matching of financing sources to project life-cycle stage

Stage	Dominant risks	Most suitable primary source	Supporting sources
Concept and development	Technical and market uncertainty	Private capital (venture or sponsor equity)	IFI grants and technical assistance
Construction	Completion, cost overrun, political	IFI long-term loans and guarantees; syndicated bank loans	Private equity for the equity tranche
Operation and ramp-up	Demand, operating performance	Bank credit (term loans, working capital)	Private credit; IFI guarantees
Maturity and refinancing	Interest rate, refinancing	Bank credit, bonds and institutional investors	Private capital for exit or recycling

Source: authors' analytical synthesis.

6. Interaction effects and sequencing. Comparing the sources separately understates the extent to which they condition one another. Senior lenders rely on the equity cushion provided by sponsors and private investors: a substantial equity tranche lowers the probability of default and therefore the spread demanded by banks (Yescombe, 2013). Conversely, the availability of long-term debt raises the return on equity through leverage, which lowers the hurdle for private investors. The cost of each source thus depends on the presence and terms of the others, and the financing plan should be optimised as a whole rather than source by source.

IFI participation affects this system through three channels. The first is the direct funding of tranches that commercial markets are unwilling to finance at the required tenor. The second is risk mitigation through guarantees and political-risk instruments, which transfers risks that commercial lenders cannot price. The third is the demonstration and certification effect described above. Through these channels an IFI can move a project from an unfinanceable to a bankable position even when its own share of total funding is small (Gatti, 2018).

Sequencing also matters. The risk premium is highest during development and construction, when cost overruns and delays are most likely, and declines once the asset demonstrates stable cash flows. Refinancing operating assets with cheaper long-term debt then releases equity that can be recycled into new projects. This logic of staged financing explains why the same project may rely on equity and IFI support at the outset and on bank or capital-market debt in its mature phase.

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Discussion

1. Interpretation of the findings. The results are consistent with the view that financing sources specialise in different segments of the risk–return–maturity space. Banks exploit their comparative advantage in monitoring secured, cash-generating activities; private capital is the natural bearer of residual and growth risk; and IFIs fill the long-tenor, high-externality segment that markets under-supply. The pattern is also consistent with pecking-order reasoning: sponsors prefer cheaper, less dilutive debt where feasible and turn to outside equity when debt capacity is exhausted or project risk is too high for lenders (Myers & Majluf, 1984).

2. Blended finance and the catalytic role of IFIs. The complementarity documented in Table 1 explains the growing use of blended structures. In a typical arrangement, an IFI takes a subordinated or guaranteed position, commercial banks provide senior debt, and private investors supply equity. The IFI's participation lowers perceived risk, extends effective tenor and imposes governance and safeguard standards, which in turn reduces the cost of the commercial tranches. The design challenge is to ensure additionality – that public or concessional resources genuinely mobilise capital that would not otherwise be invested – and to avoid crowding out private lenders (Mazzucato & Penna, 2016).

3. Emerging-market considerations. The relative importance of the three sources differs across financial systems. In bank-dominated economies with shallow capital markets, commercial banks supply most external finance, but their funding base is typically short-term, which limits the availability of long tenors. Private capital markets are thin, and exit options for equity investors, such as public listings or sales to strategic buyers, are limited. In such settings IFIs often play a proportionately larger role, both as providers of long-term funds and as a source of standards and know-how.

Currency mismatch is an additional concern. Loans from IFIs and foreign investors are frequently denominated in hard currencies, whereas project revenues may be earned in local currency. Unless hedging instruments or local-currency lending are available, exchange-rate depreciation can erode debt-service capacity. The quality of legal institutions, creditor protection and contract enforcement also conditions the willingness of all three types of providers to commit capital for long periods (Levine, 2005). These considerations reinforce the case for blended structures that combine local bank funding with foreign long-term capital and risk-mitigation instruments.

4. Implications for practice and policy. For project sponsors, the analysis suggests treating financing as a sequence rather than a single decision: secure early-stage risk capital, use IFI support and syndicated loans through construction, and refinance with cheaper bank or capital-market debt once operating performance is demonstrated. Early engagement with IFIs is advisable because of long appraisal times.

For commercial banks, participation in co-financing with IFIs and the use of guarantees can extend the tenor and volume of lending within prudential limits.

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For policy-makers, the priorities are to develop domestic long-term capital markets, strengthen creditor rights and contract enforcement, standardise project documentation, and build project-preparation capacity, since weak preparation is often a more binding constraint than the availability of funds (Levine, 2005).

5. Limitations. The study has four main limitations. First, the ratings in Table 1 are ordinal judgements derived from theory and institutional characteristics; they are not estimated from a primary dataset, and actual terms vary by country, sector, sponsor quality and market cycle. Second, the review is integrative rather than a formal systematic review with a pre-registered search protocol, so selection bias in the literature cannot be excluded. Third, the analysis treats each category as homogeneous, whereas instruments within each category (for example, mezzanine finance or green bonds) can have hybrid features. Fourth, the framework does not model taxation, exchange-rate risk or sanctions and regulatory constraints, which may be decisive in specific jurisdictions.

6. Directions for future research. Future work could (i) test the framework empirically using project-level data from transaction databases and IFI disclosures; (ii) estimate the mobilisation ratio of blended structures and the conditions under which additionality is achieved; (iii) compare financing patterns across countries at different levels of financial development; and (iv) examine how sustainability-linked and green instruments change the relative attractiveness of each source.

Conclusion. This article compared bank credit, private capital and international financial institutions as sources of investment project financing against six criteria: cost, tenor, risk allocation, monitoring, accessibility and non-financial value added. Three conclusions follow.

First, each source has a distinct comparative advantage rooted in a specific economic mechanism – monitoring for banks, risk-bearing and governance for private capital, and long-term, catalytic finance for IFIs. Second, because these advantages are offsetting, the sources are complementary, and the optimal financing plan combines them according to the project's life-cycle stage and risk profile. Third, blended structures in which IFIs mobilise commercial bank and private capital are a promising instrument for capital-intensive projects, provided that additionality and transparent risk sharing are ensured.

The main contribution of the paper is a unified comparative framework and a stage-based decision matrix that can support project appraisal and financing strategy. Its main limitation is that it is conceptual; empirical validation using project-level data is the natural next step.

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