

Q2•2024

Every deal is
a blended
finance deal

Blended finance
for first-of-a-kind
nature-based
solutions

Unlocking the
potential of blended
finance in Asia

CrossBoundary
QUARTERLY



**Blended
Finance**



**CrossBoundary
Group**



We are recruiting

At the heart of CrossBoundary is our purpose to unlock capital for sustainable growth and strong returns in markets that are often overlooked. We're not just advisors; we're a driving force—navigating the investment landscape in underserved markets and directly deploying capital through our investment platforms.

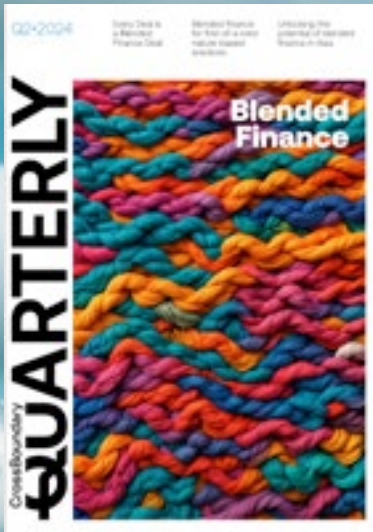
None of this would be possible without our strongest asset: our people. The CrossBoundary team comprises a unique set of individuals who come from diverse backgrounds but share core qualities: curiosity, humility, integrity, a drive for excellence, and a bias for action. They're genuinely excited about making a considerable impact on underserved markets across the globe.

Together, ten core virtues shape our culture and guide our actions:

- We expect excellence
- We can all belong here
- We act like the owners we are
- We are relentlessly curious
- We prioritize results
- We authentically care
- We think deliberately
- We act with humility
- We are biased to action
- We never compromise on integrity

Learn more
about working
with us:





**CROSSBOUNDARY
QUARTERLY
Q2 2024**

EDITORS
MIKE CASEY
KYMBERLY BAYS

DESIGNER
DAVE LLOYD

DISCLAIMER

The views and opinions expressed in this magazine are those of the authors and do not necessarily reflect the official policy or position of CrossBoundary Group or any of its affiliates. The magazine is intended for general information purposes only and does not constitute investment, legal, tax, or other professional advice. Readers should consult their own advisers before making any decisions based on the content of this magazine. CrossBoundary Group does not assume any liability for any errors or omissions in the content of this magazine.



About the CrossBoundary Group

CrossBoundary Group is a mission-driven investment and advisory firm that unlocks the power of capital for sustainable growth and strong returns in underserved markets. CrossBoundary Group has advised on over US\$11 billion of closed transactions in impactful sectors, such as agriculture, health, education, manufacturing, ICT, infrastructure, and clean power. CrossBoundary Group also directly deploys capital through its investment platforms, such as CrossBoundary Energy, CrossBoundary Energy Access, CrossBoundary Real Estate, and The Fund for Nature. CrossBoundary Group has a global presence with 23 offices and over 180 professional staff. For additional information, visit www.crossboundary.com.



Table of contents

03 Letter from the Editor

06 Every deal is a blended finance deal

22 Blended finance for first-of-a-kind nature-based solutions

32 How can innovation in funding models unlock energy access in emerging markets?

42 Unlocking the potential of blended finance in Asia

48 Reducing transaction costs and information asymmetries to mobilize capital effectively



This interactive document has been optimized for use on screens in portrait orientation.



Bold blue words will link you to the reference associated with the text.





Every Deal is a Blended Finance Deal

Blended finance, as [Convergence](#) defines it, is the use of catalytic capital from public or philanthropic sources to increase private-sector investment in sustainable

development. In practice, we believe the definition extends a bit broader to include pioneering transactions in firms that exhibit the ability to graduate from grants and subsidized capital to commercial sources of financing.

CrossBoundary Energy is a great example. When we first articulated a vision for a commercial and industrial (C&I) solar vehicle for Sub-Saharan Africa, the value proposition was clear: cheaper and more reliable clean energy addressed a critical pain point for local businesses. Local electric grids were unreliable and expensive, and businesses' dependence upon back-up diesel generators was not only expensive but also contributed to emissions of noxious carbon dioxide.

Despite identifying a business model that had strong unit economics—and, in fact, grew stronger each year as solar input prices declined—the scalability of C&I solar remained an open question. And this uncertainty meant that the volume of commercial capital available to us was not only *de minimis*, but also that the investors who bought into our vision sought ways to de-risk their capital commitments.

We approached USAID with the concept of a repayable grant, which was used as the first-loss tranche of subordinated equity for the CrossBoundary Energy fund. While the US\$1.3 million grant was contingent on us raising at least US\$6.5 million in equity funding, the first-loss facility enabled us to crowd in family offices and reach a final close of US\$8.8 million.

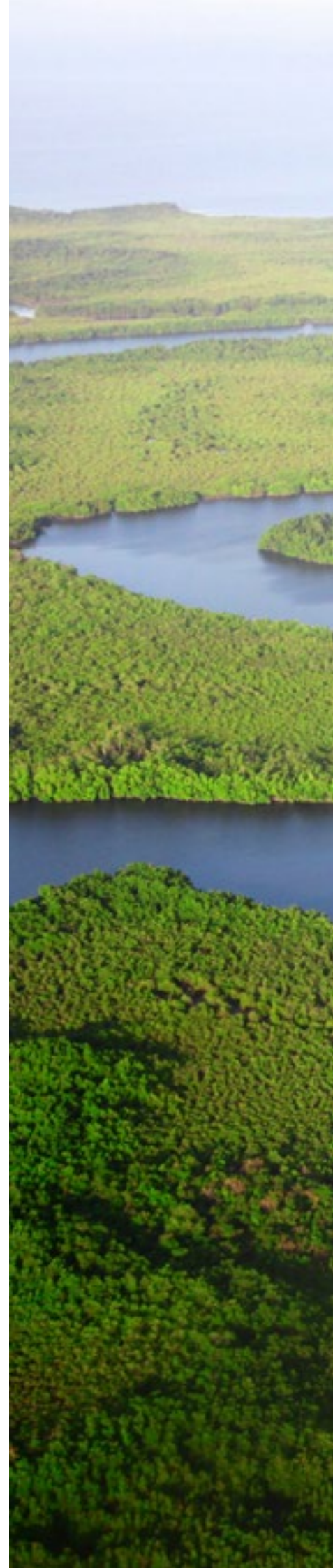
More to the point, we fully realized an exit from this pilot fund at a price that delivered a net IRR of 15% and enabled us to fully repay the grant funding that USAID extended as first-loss funding. Since then, CrossBoundary Energy has been able to raise funding from commercial banks and investors, and scale its operations across Africa and to Australia.

Since that initial pilot project, blended finance has graduated from a relatively niche capability to one that the world's largest asset managers employ—oftentimes, though not exclusively—in climate-related investments. In fact, blended finance

is one of the core capabilities CrossBoundary employs to mobilize capital in underserved markets. The suppliers of capital that we work with are seeking greater security to offset risks, while from the demand side, governments are exploring the effectiveness of tools to entice capital flows.

For this reason, our Co-Founder and Managing Partner Jake Cusack recently advanced the argument that every deal is a blended-finance deal. In his estimation, recognizing that every deal is a blended finance deal normalizes discussions of policy incentives and a differentiated cost of capital, rather than artificially shunting deals into “commercial” and “non-commercial.” Moreover, it forces investors and stakeholders to consider the externalities of their investments and how they impact the public good.


In this issue of the CrossBoundary Quarterly, Kate Wharton, Rose Farah, and Ian Ndegwa from our Natural Capital team





explore the role that concessional capital can play in accelerating “first-of-a-kind” transactions in the nature-based solutions space. We also share insights from our Head of South and Southeast Asia Advisory, Nandini Chaudhury, on the potential of blended finance in Asia. Nathan Kelly, who heads our US Underserved Markets practice, explores why subsidies and guarantees are necessary—but ultimately insufficient—to mobilize capital, and argues that what’s really needed to accelerate

capital flows that can address transaction costs and reduce information asymmetries. Finally, Kate Pallett, Senior Marketing Communications Manager for CrossBoundary Energy, interviews Nchimunya Chipo Hamukoma from the Global Energy Alliance for People and Planet (GEAPP) to explore how innovations in funding can advance inclusive energy access.

We hope you enjoy this issue and please reach out to us with your comments and questions. 

Every deal is a blended finance deal

One of the many nice surprises of returning to in-person conferences post COVID was finding that “blended finance” has entered the common vernacular. In 2019, it still felt like a new term that warranted a quick explanation with each use; now, it seems like even the most staid of financial institutions are bandying it about with casual abandon.



Written by:
Jake Cusack





Read *Every Deal is a Blended Finance Deal* here:



*That said, it is worth quickly revisiting the definition. Our friends at **Convergence** provide the following:*

Blended finance is the use of catalytic capital from public or philanthropic sources to increase private sector investment in sustainable development¹



We might propose an even simpler, yet more comprehensive framework:

every deal is
a blended finance
deal.

¹ The full Convergence definition goes onto to say: “The actors in a deal come together to achieve social impact and financial return (the relative importance of each to the actors may vary). Blended finance frameworks typically focus on a subset of deals that have a very clear social impact and have public or philanthropic money in the core capital stack that finances the investment.”



Every deal has externalities

Every deal has positive or negative externalities that are not fully captured in its financial returns.² Business and investing invariably affect the climate, or biodiversity, or public health, or a society's civic cohesiveness, and/or many other attributes of the world we live in.

A blended finance process acknowledges these externalities and asks whether any actors have decided those externalities warrant either additional compensation (such as revenue subsidies or a lower cost of capital) or penalty (e.g., taxes, fines, et cetera).³

Even if seemingly not financial relevant today, there is always a question of whether new mechanisms (such as a carbon tax) may reward or punish these externalities in the future, and/or whether the business may face competition from a substitution good that better addresses these externalities.

From this, we can imagine at least three relevant archetypes of deals:

1

Deals where the desired public or social goods are already internalized and amplified by the core business model. This is the sweet spot where purpose and profit overlap; where we can achieve our sustainable development goals by simply pushing investment professionals and C-suites to better realize the intrinsic relevance of these factors to their pursuit of shareholder returns. Examples could include companies that lower their costs by investing in renewable energy, or goods that have measurable marketing benefits from social factors such as net-zero commitments or certified fair supply chains.⁴

² Note that to be a "deal", there must be external revenue. Public goods that should be provided at no-cost (e.g. police/public safety or emergency humanitarian assistance) are not suitable for blended finance.

³ While beyond the scope of this essay, it is important to note that there are additional justifications for public/philanthropic capital to subsidize activities that interconnect to externalities. For instance, affordability and equity/inclusivity.

⁴ The paper "Are Business Ethics Effective? A Market Failures Approach to Impact Investing" provides some thinking on which sectors and countries are likely to have more opportunities with this natural social/financial returns overlap, noting that addressing renewable energy, infrastructure, financial services, and agriculture may be initially more attractive to private investors than water and sanitation, biodiversity and natural resources, housing for the poor, malnutrition, literacy, etc. Further research on sector selection comes from Matthieu Pegon's "A Strategic Approach to Blended Finance", which among other points argues that "leverage" (private dollars mobilized divided by public dollars used) isn't always the best metric for choosing impactful transactions, but rather it should be total social benefits vs. the public cost/blended finance required to make the deal possible. Also see CrossBoundary's paper with Tony Blair Institute on sector selection and facilitation for blended finance deals. <https://crossboundary.com/wp-content/uploads/2023/09/Tony-Blair-Institute-with-CrossBoundary-Scaling-up-Investment-for-Covid-19-Economic-Recovery-and-Jobs-in-Africa.pdf>

2 Deals where public or philanthropic actors are already acting to appropriately incentivize business and investment. The Inflation Reduction Act (IRA) in the US is an example of almost \$1 trillion in various subsidies and industrial policies that will incentivize massive investment into climate-relevant technology. Another example would be rural electrification in developing countries, where the World Bank or country governments have appropriately decided that expanding access to electricity generates benefits beyond the private consumers' initial ability to pay, and therefore provide new connection "top-ups" or energy charge subsidies. (Similar incentives often exist for rural agriculture/farmers.)

3 Deals that have material externalities but no incentives yet. These situations warrant policy/regulatory change and/or philanthropic intervention to address appropriately. Many natural capital factors fall into this area as, for example, the potential depletion of ecosystem health is often not adequately noted and discouraged. Our imaginations here must be broad, as it is easier to think first of mitigating existing negative externalities (e.g. incenting lower energy consumption for operating facilities) than to conceive of the possible positive externalities of production that has not yet been established. For example, having local value-added agri-processing in developing countries improves price stability and self-sufficiency; having a local pharmaceutical industry improves domestic supply and resilience to pandemics; having relevant vocational schools improves equality, human capital, and labor market flexibility; and so on. Yet, there are only occasional public/philanthropic incentives for these "greenfield" projects to be undertaken. Of course, appropriate allocation of new incentives between different sub-sectors or deal opportunities must be considered thoughtfully as both public and philanthropic resources are scarce.





Opportunities through a broadened blended finance lens:

Deal archetype	Description	Financial incentive
<p>1 Public good externalities already linked to core business</p> <div style="border: 1px solid #f08080; padding: 5px; margin-top: 10px;"> <p>Core Business</p> <p>Internalized externalities</p> </div>	<p>Majority of public goods are fully internalized and amplified by core business model – sweetspot of overlap of purpose and profit</p>	<p>Amplify awareness of relevance of internalized externalities in the pursuit of shareholder returns – e.g. climate resilience</p>
<p>2 Public or philanthropic incentivization of externalities</p> <div style="border: 1px solid #f08080; padding: 5px; margin-top: 10px;"> <p>Core Business</p> <p>Philanthropic or public subsidy</p> </div>	<p>Public or philanthropic actors are already actively incentivizing business – e.g. U.S. Inflation Reduction Act, connection subsidies for rural electrification</p>	<p>Compensate business for positive externalities for which there is no current market mechanism</p>
<p>3 Non-incentivized externalities</p> <div style="border: 2px dashed #f08080; padding: 10px; margin-top: 10px;"> <p>Unpriced positive externalities</p> </div>	<p>Positive externalities are not yet incentivized, and so are under-produced, resulting in sub-optimal social outcome</p>	<p>Need for new financial incentives or public policy changes (regulation)</p>





Most deals already use blended finance tools

The majority of deals—even those considered “purely commercial”—use the instruments of blended finance. Coldly numerate financiers who might dismiss discussions about social outcomes should realize that they use these tools too, just usually in a different legal and rhetorical frame.

For instance, a venture investor who takes a 2x liquidation preference (meaning they receive twice their money back before sharing pro-rata with other investors) is using the tools of blended finance. So, too, is a lender who takes warrants (embedded equity instruments) to capture upside in addition to their strongly covenanted senior debt positions.

Optically, such tools might seem different from those used in social-impact deals, but they exist on the same plane: subordinated “first loss” from a philanthropic player to encourage new private capital is just a rhetorical difference away from management’s common equity being subordinated to a new investor’s liquidation preference. Or, put another way, instruments of blended finance are no different than structured finance, a long practiced methodology for having a “wedding cake” of different tranches of risk & return.

Moreover beyond a deal by deal approach, there are cross-cutting types of blended finance. Targeted tax breaks are essentially a blended tool for crowding commercial investors into markets. Consider the revitalization of American neighborhoods through opportunity zones, or the moves of carbon capture companies to the United States on the heels of the IRA.

So, it’s erroneous to think terms like “first loss” mean a non-commercial transaction. Structures that have a different balance of risk/return for different capital providers are logical in every deal. And notably, structures themselves can have externality implications — an overly levered debt deal can create adverse incentives, or conversely, bringing along new participants into a transaction could enhance demonstration or ecosystem activation effects.⁵

⁵ Delilah Rothenberg and others at the Predistribution Initiative have done excellent work on system level risks/ externalities that can emerge from asset allocation strategies and deal structures. For example, see their paper “ESG 2.0: Measuring & Managing Investor Risks Beyond the Enterprise Level”.





Our hope is that—by demonstrating that every deal is a blended finance deal—we will widen the external audience for these conversations while helping investment teams be appropriately thorough in their investment processes and policy discussions, rather than treating only a narrow set of deals or products as “blended finance.”⁶

A blended finance framework creates opportunities for savvy and responsible investors

Investors should always think about the positive and negative externalities of their investments, and how those externalities surface potential subsidies/taxes and catalytic/concessional structuring opportunities.

By using this frame, we can imagine discovering that a philanthropic capital partnership would enable a healthcare business to reach not-yet economic customers, growing the customer base and providing access to care sooner than otherwise possible. Or, an investor might realize that she should be advocating strongly in the policy arena, because her investment is delivering substantial public goods (such as carbon removals) that are not rewarded in the current government framework.

Even the “ruthlessly commercial” investor must acknowledge that public externalities could have future economic consequences for them. Such investors can choose to believe a looming subsidy or penalty will be immaterial to their business—but choosing to ignore something is itself a due diligence and investment decision, possibly one with unforeseen consequences.

⁶ For a similar argument that ESG should be treated as a process rather than a ‘product’, see George Serafeim, “ESG: From Process to Product”, Working Paper 23-069, Harvard Business School, 2023. I would note that I am not attempting to argue that every deal will in fact have blended finance directly within it or immediately adjacent to it, but that virtually every deal has externalities that could directly or indirectly interact with public / philanthropic financial incentives or disincentives at some point, and responsible investment and policy processes should think through this lens.



This dynamic is even more true with the rise of modern “industrial policy,” which has blended finance tools at its core. In fact, a recent study found that 96% of climate tech venture capitalists are two degrees or less away a government grant, and that the US government is the most central co-investor in American climate-relevant companies.

Economic growth is private sector led, but it is becoming ever more government enabled.⁷ Ideally, new industrial policy approaches are based on bottom-up iterative public-private cooperation and coordinated tools specific to the prioritized sectors and locations. This is far preferable than the unrealistic extremes of top-down five-year plans or completely hands off “let the market decide” approaches.⁸

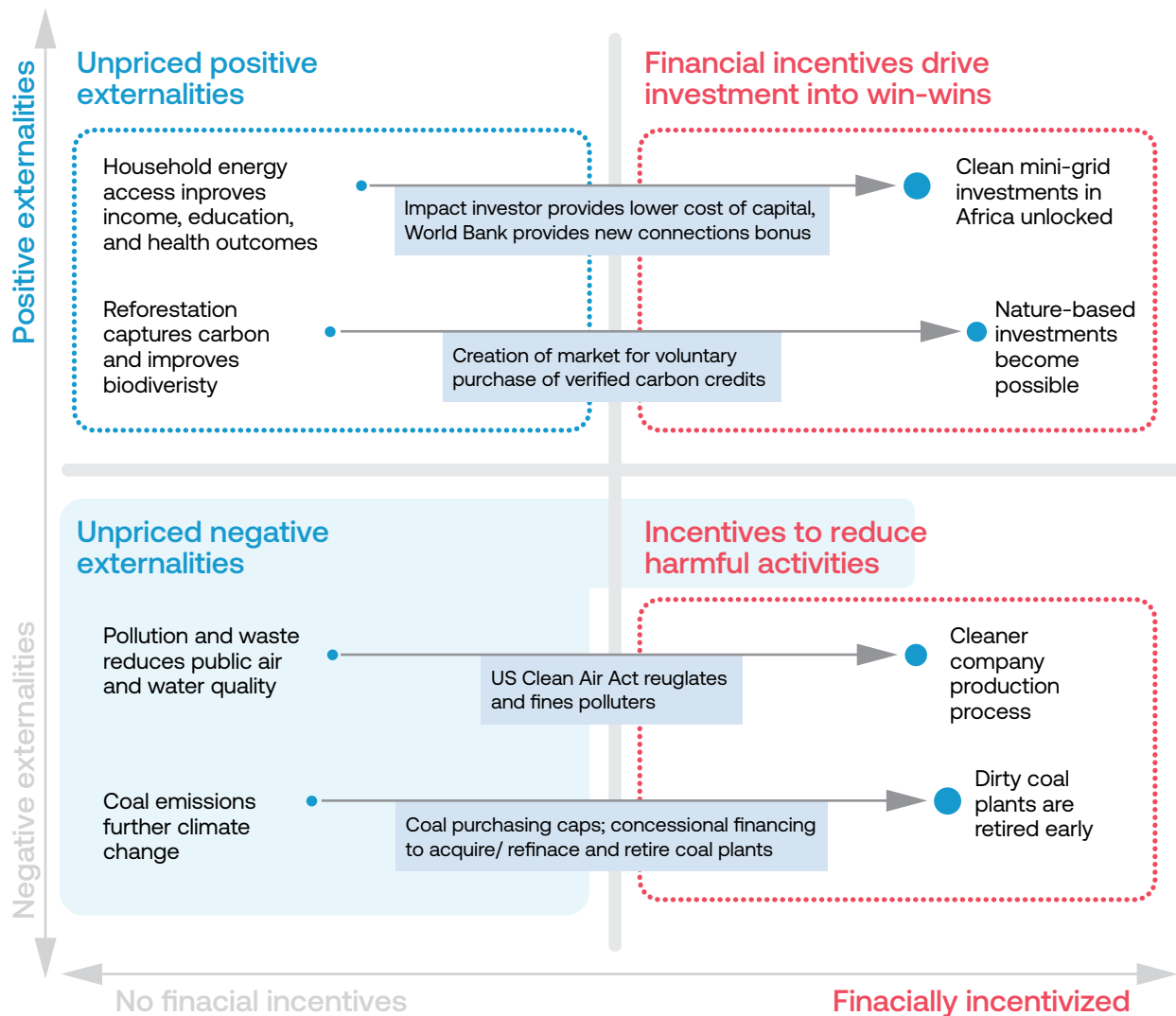
Moreover, if an investor determines externalities are material but “someone else’s problem,” this logically must correlate to what they personally advocate for the public and philanthropic sectors to do. For example, while it is possible for someone to believe that climate change is a problem but not an inherent corporate responsibility, surely this same person must then argue for public or philanthropic intervention.

The following graphic provides a way to consider this framework: opportunities are mapped in four quadrants, based on whether they have positive or negative externalities, and the degree to which the externalities are financially incentivized. Changes in public policy and the resulting incentives can move whole subsectors between quadrants. If policy can not or will not move fast enough, blended finance structures on a deal-by-deal basis can move specific needs and opportunities between quadrants.

⁷ This is the phrasing often employed by the Biden Administration, such as by Jigar Shah, director of the Loan Programs Office at Department of Energy.

⁸ These new approaches are detailed well in “The New Economics of Industrial Policy” from Dani Rodrik and others. Additionally, a recent essay in Time by Rohan Sandhu emphasizes the importance of supporting local intermediaries to address the coordination failures that can often limit logical investments. Finally, our own work on investment facilitation argues that supporting locally based advisory intermediaries can help lower transaction costs and information asymmetries, unlocking the private investment desired by a government or philanthropic third party in a relatively light-touch and cost-effective way.





Importantly, this landscape is not static. Pioneering transactions that leverage subsidized capital to create new market opportunities can illuminate a path for follow-on investments, foster the development of an ecosystem of participants in the pioneering firm’s value chain, and encourage innovations that increase consumer surpluses. Blended finance, in short, can inject dynamism and create virtuous circles of change which eventually reduce or eliminate the need for direct or indirect “subsidy”.

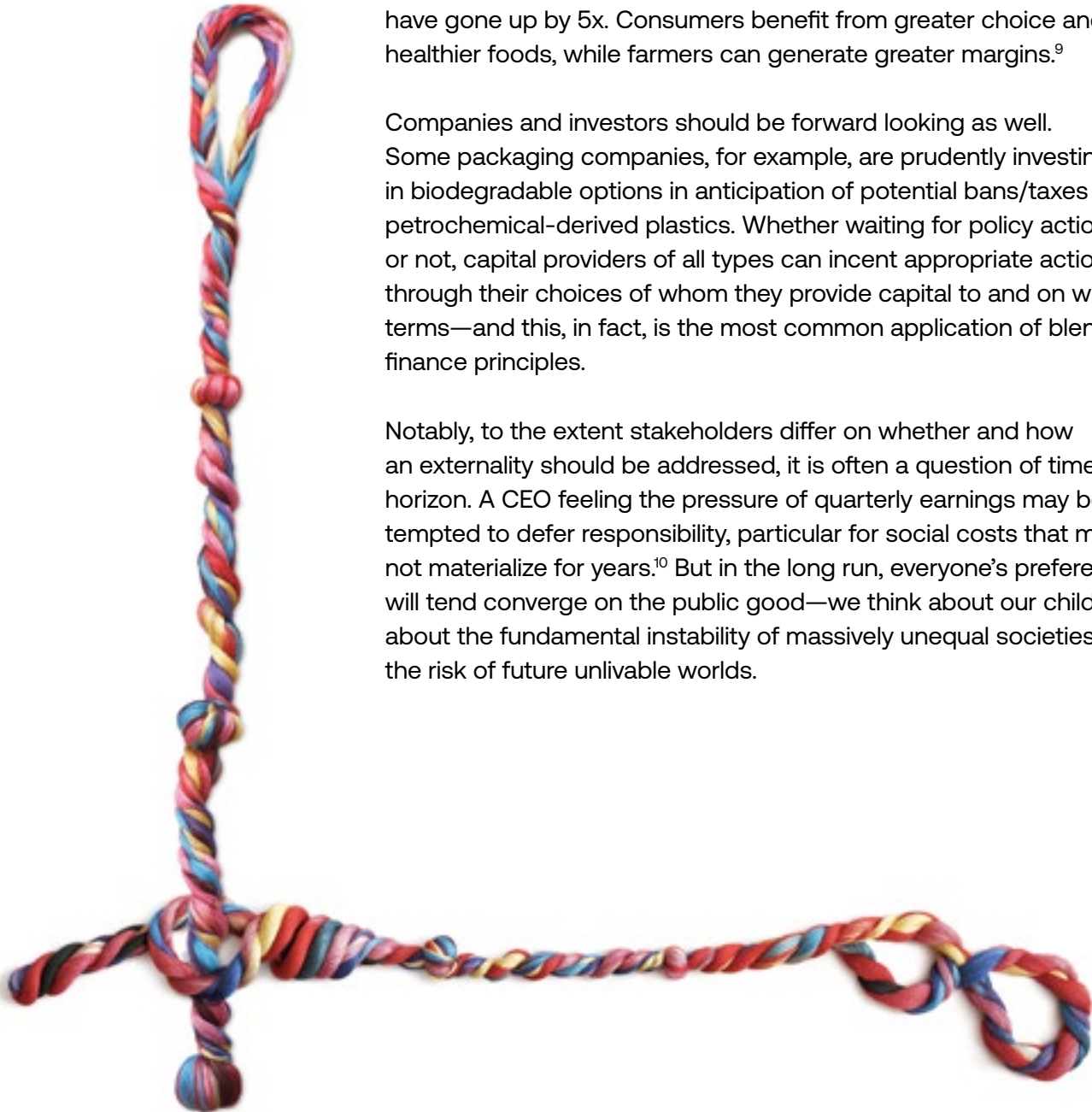
A few further examples might help reinforce the point. For starters, while increased scrutiny of the voluntary carbon credit market is appropriately elevating the importance of high-integrity projects, its existence has enabled the growth of rural companies in Africa that previously struggled due to low consumer ability to pay. For instance, Koko Networks, which switches customers from coal to clean

cooking ethanol fuel, now receives the majority of its revenue from the monetization of carbon credit streams, while also passing on a reduction in price to consumers.

Or, take organic farming: since US government standards were first implemented in 2002—creating clear certification pathways and customer awareness—organic acres under cultivation (and sales), have gone up by 5x. Consumers benefit from greater choice and healthier foods, while farmers can generate greater margins.⁹

Companies and investors should be forward looking as well. Some packaging companies, for example, are prudently investing in biodegradable options in anticipation of potential bans/taxes on petrochemical-derived plastics. Whether waiting for policy action or not, capital providers of all types can incent appropriate action through their choices of whom they provide capital to and on what terms—and this, in fact, is the most common application of blended finance principles.

Notably, to the extent stakeholders differ on whether and how an externality should be addressed, it is often a question of time horizon. A CEO feeling the pressure of quarterly earnings may be tempted to defer responsibility, particular for social costs that might not materialize for years.¹⁰ But in the long run, everyone's preferences will tend converge on the public good—we think about our children, about the fundamental instability of massively unequal societies, of the risk of future unlivable worlds.



⁹ See, for example, Conventional and Organic Enterprise Net Returns - Center for Commercial Agriculture

¹⁰ Put another way, the difference in time horizon or in who is seen as responsible/benefiting from a return/cost can create a mispricing in scarce assets such as biodiversity.



The way ahead

So, where does this bring us?

Recognizing that every deal is a blended finance deal normalizes discussion of policy incentives and a differentiated cost of capital, rather than artificially shunting deals into “commercial” and “non-commercial.” It provides a more useful, nuanced taxonomy for asset allocation and investment theses. And, it forces regular consideration of externalities impacting the public good and their current and possible future financial consequences.

But while it’s natural to focus on the “blending” of instruments in the capital stack of a deal, in our experience it is often the transaction costs before and during a deal’s execution that are an even bigger barrier than structuring an adequate return. At CrossBoundary, we routinely see opportunities with commercial risk/return economics that could deliver strong returns and public goods, but the costs of finding, diligencing, structuring, and executing the investment are not easily absorbed—particularly for pioneer transactions.¹¹

This is even more true for blended finance deals, which often involve a fragmented universe of capital providers with distinct impact/return preferences and mechanisms for deploying their capital, thus raising the initial structuring burden.¹²

For philanthropic or public actors that would like to take a light touch with the private sector, providing initial facilitation for investments can be less interventionist than taking long-term ownership position in the company or project. Therefore, relevant assistance can include not just providing low-cost investment capital, but also funding to lower transaction costs and reduce information asymmetries, and to construct the opportunity so that it is bankable. The funding of investment facilitation platforms that help construct and package opportunities, or institutions providing funding to cost-share the burden of early-stage origination and diligence, can play a critical role in fostering the growth and development of sustainable businesses.

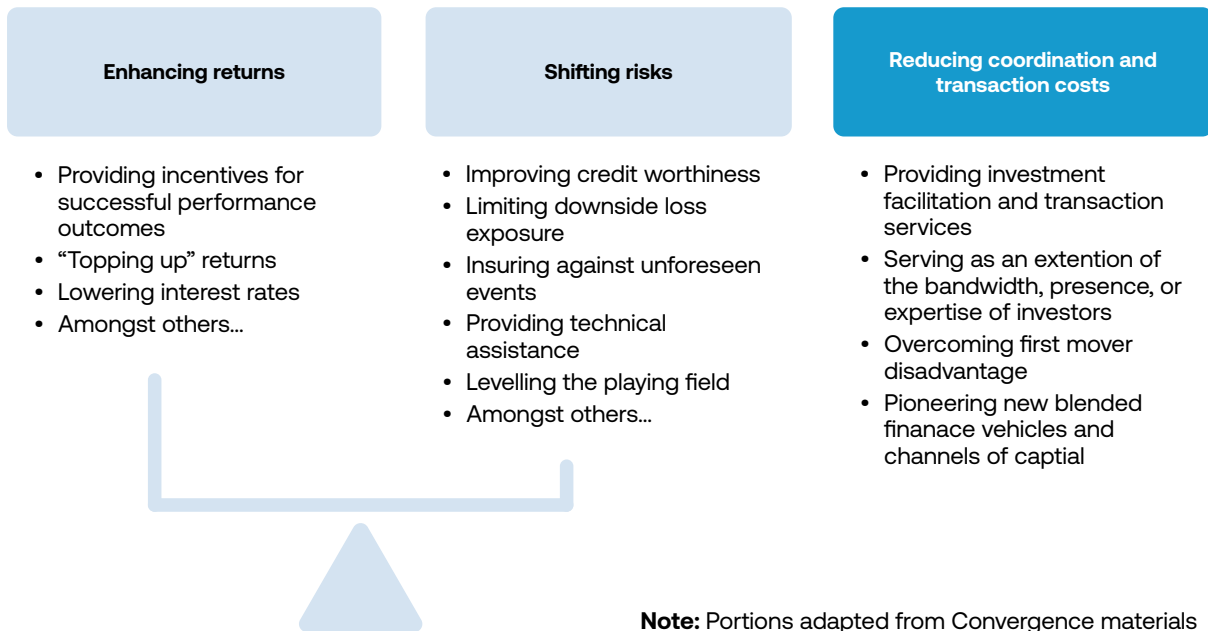
¹¹ Impactful pioneer transactions, even small ones, are particularly important to support as they create demonstration effects, knowledge spillovers, and value chain complementarity (as argued by Paul Collier, Dani Rodrik, Matthieu Peon, and Paddy Carter in various papers, among others).

¹² We should be careful to keep the transaction cost implications of seemingly innovative multi-layered blended structures in mind, we have seen small investments derailed by overly complicated structuring disproportionate to the size of deal. The simplest viable structures should be pursued.

A suite of blended finance tools across public, philanthropic and private sectors...




... can be used to incentivized positive externalities and unlock capital by...



Note: Portions adapted from Convergence materials

More fundamentally, beyond the tactical mechanics of unlocking these deals, there are important personal and industry-wide implications of this essay’s thesis. Lengthening our time horizons and widening what we perceive as our relevant spheres of responsibility will create greater convergence in cost/benefit decision-making, for all stakeholders.

And for each of us as individual allocators of our capital and time, heightened sensitivity to externalities reminds us that our business, philanthropic, and policy beliefs must work in combination rather than as distinct domains.

Trade-offs of course sometimes remain. But when every deal is a blended finance deal, investors can see better risk-adjusted returns, governments can link policy to tangible outcomes, and all of us can enjoy greater access to public goods while experiencing fewer negative externalities. 



Acknowledgments

Thank you to Joan M. Larrea, Michael Casey, Jonathan Said, Eliza Erikson, Nathan Kelly, Pooja Yadav, Matthieu Pegon, Kate Wharton, Marília dos Reis Martins, Carey Buxton, Michael Hankin, Andrew Herscowitz, Matt Tilleard, Thomas Flahive, James Harding, Gabriel Davies, Kirtika Challa, Stuart Fairclough, Armin Peter, Sayle Evarts, Kymberly Bays — among others — for their thoughtful ideas and comments on this piece.




Blended
finance for
first-of-a-kind
nature-based
solutions

**Written by:**

Kate Wharton, Managing Director and Head of Natural Capital, CrossBoundary Group
Rose Farah, Associate, CrossBoundary Advisory
Ian Ndegwa, Associate, CrossBoundary Advisory



There is an important conversation happening in climate tech circles around the challenges of financing first-of-a-kind (FOAK) projects. FOAK projects carry a unique set of risks, and not just technology risk – it's also risk around the business model, project execution, and country context. Not surprisingly, these conversations center almost exclusively on hardware like direct air capture and green hydrogen production.



Natural climate solutions (NCS) are notably absent from the conversation, yet they represent a critical category of scalable infrastructure projects needed for the climate transition. While the underlying biotechnology, photosynthesis, is not new, the other FOAK risks of NCS are just as real as for any other climate project.



Photosynthesis transforms carbon dioxide and water into oxygen and biomass. If it were discovered in a lab today, no doubt it would be the darling of Silicon Valley. But it's our good fortune that this solution has, over millions of years, bypassed R&D, prototyping, and piloting, and arrived at our doorstep in its familiar form.



If photosynthesis is truly such a low-cost, scalable, and de-risked climate mitigation solution, why is it so difficult to finance reforestation projects?

We would argue that the fundamental investment challenge has been unpriced externalities – in short, there historically has not been a market for ecosystem services because there was no "product" and no demand. But as positive externalities move from being unpriced to priced, the business model for nature is evolving. We see this most clearly with the development of carbon credit markets.

While public and philanthropic actors are increasingly incentivizing development of and investment into novel climate technologies, natural climate solutions have not received the same attention. To mobilize greater investment into climate mitigation, we need greater collaboration across the capital stack for NCS. This means targeted use of public and philanthropic funding and incentives that are ultimately linked to commercial investment into replicable, scalable projects.

The FOAK challenge for climate tech

In the last 50 years, the price of solar modules has declined by 99.6%. The decline in the cost of solar is a function of several factors – one of which was the use of public policies and incentives, including R&D grants, concessional loans, subsidies, and tax credits. Like many climate innovations, solar PV benefitted from public and philanthropic incentives that helped address key risks – including high upfront costs, long payback periods, and uncertain demand – to bring the technology to commercial scale.

In fact, a recent study found that 96% of climate tech venture capitalists are two degrees away or less from a government grant, and that the US government is the most central co-investor in American climate-relevant companies. In short, public and philanthropic incentives have been critical to climate tech innovation.

FOAK projects test the commercial potential of pioneering technologies, methodologies, and processes – and if successful, they create replicable models that can scale.

Figure 1: Key Characteristics of FOAK Projects



Pioneering:

Projects advance new technologies, processes, and methodologies



Commercial risk:

Projects seek to prove the commercial potential of a solution, typically after a successful pilot



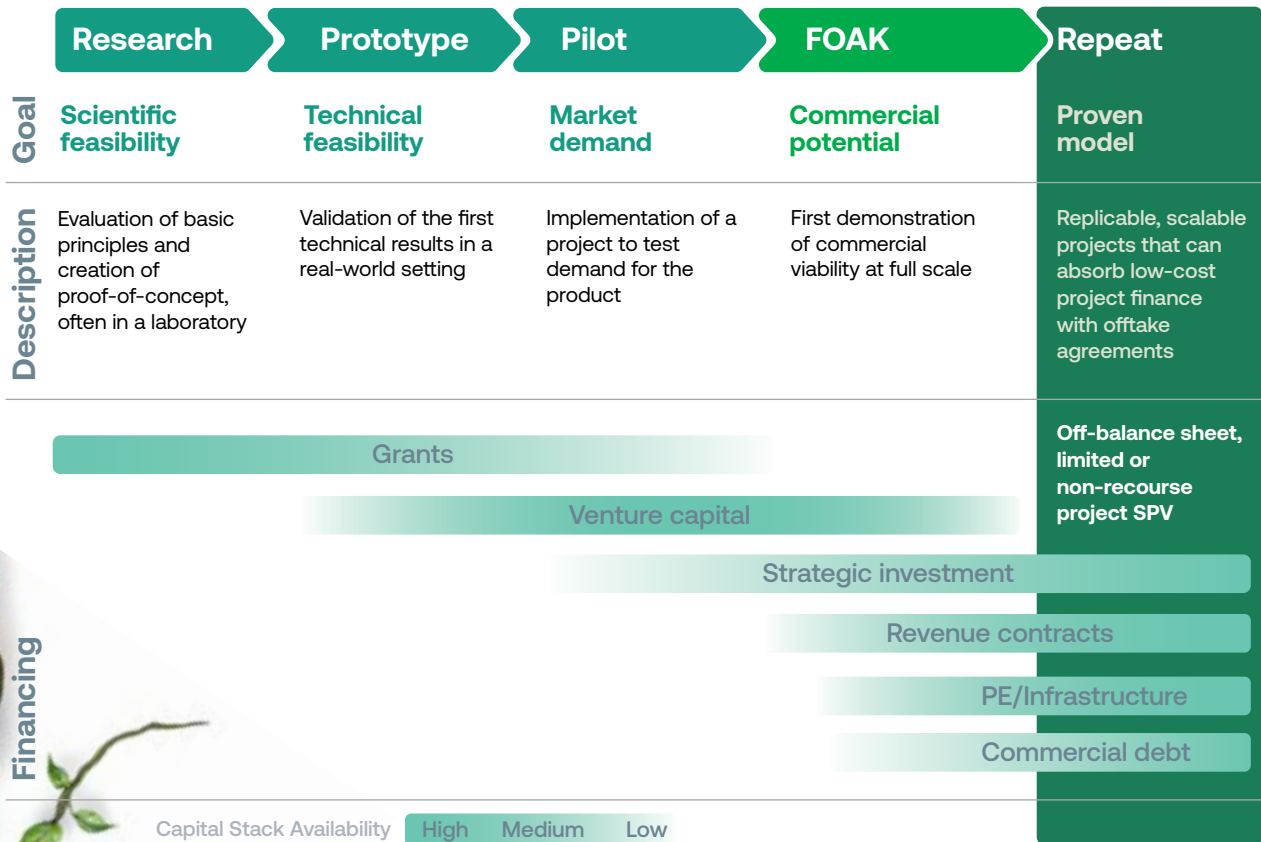
Replicable:

Successful projects reduce future risk and create models that can be replicated and scaled

There is a critical gap in funding for FOAK projects. To get the first proof-of-concept and test market demand, funding typically comes from grants, angel investment, or early-stage venture capital. But to launch the first full-scale commercial project, companies are looking for low-cost, large-scale financing that neither venture capital nor infrastructure funders are well-positioned to provide. FOAK projects may be too large or have returns that are too low for venture capital, yet they are perceived as too risky or one-off for infrastructure funders looking for the kind of deal that can be repeated multiple times, not just once.

The FOAK stage is also when a project can move off balance sheet and be funded through a project SPV rather than with use of proceeds of a corporate capital raise. This can present another challenge to founders and early investors, who know how to raise grants and rounds of venture capital, but not necessarily how to raise large-scale project finance, or from whom.

Figure 2:
Financing
First-of-a-Kind
and Beyond



Nature-based carbon projects as FOAK projects

Natural climate solutions have high climate impact but are critically underfunded. NCS remove and avoid carbon emissions through ecosystems in nature – take, for example, afforestation, reforestation, and revegetation (ARR) projects, which restore forest ecosystems to sequester carbon from the atmosphere. NCS hold enormous potential for climate mitigation, with the capacity to remove one-third of the emissions needed to meet global climate targets¹ – yet they receive less than three percent of climate funding.²

Historically, the investment challenge for nature has been that the benefits, or positive externalities, of NCS were not priced, and so there was not a reliable business model to mobilize private capital for projects. The growth of carbon markets has changed this by internalizing nature's positive externalities to unlock new, reliable revenue streams throughout the life of the project.³ As carbon has gone from being unpriced to priced, there is an opportunity for commercial investors to participate in natural climate solutions and therefore to mobilize funding at scale.

The term "FOAK" is typically a reference to projects with first-of-a-kind technology risk. But the FOAK financing challenge applies to nature-based carbon removal projects, too. Of course, nature-based carbon projects aren't pioneering new technologies – they use naturally occurring processes, such as photosynthesis, to remove carbon from the atmosphere. But they are pioneering new methodologies for sequestering carbon emissions at scale, in a new global market for carbon credits.

We can categorize the risks of FOAK nature-based carbon projects as business model risk, execution risk, and country risk, each of which has a set of mitigation strategies – from negotiating offtake agreements to guard against uncertain future demand, to investing in advanced data collection technologies to support



¹ Griscom et al. 2017

² CPI, 2023. Global Landscape of Climate Finance 2023. Climate Policy Initiative, London.
<https://www.climatepolicyinitiative.org/publication/global-landscape-of-climate-finance-2023/>

³ Carbon markets require that projects meet criteria of additionality, permanence, avoidance of leakage, robust quantification of emission reductions and removals, and no double counting.

Figure 3: Risks and Mitigants for FOAK Nature-based Carbon Projects

accurate measurement, to purchasing political risk insurance to protect against breach of contract that results in late or non-delivery of credits. Figure 3 details select risks for FOAK nature-based carbon projects.

Category		Risk	Select Mitigants
Business Model	Demand	Uncertain future demand of carbon credits	<ul style="list-style-type: none"> ● Secure long-term offtake agreements from blue-chip customers ● Align with industry-leading quality guidance such as ICVCM's Core Carbon Principles ● Incorporate co-benefits
	Price	Uncertain future price of carbon credits	
	Reputation	Exposure to reputational risks and negative publicity	
Execution	Community	Complexities with community engagement, including education on carbon markets	<ul style="list-style-type: none"> ● Engage credible local partners to undertake robust process for Free, Prior, and Informed Consent (FPIC) ● Invest in training and development programs to build local expertise ● Purchase insurance ● Conductive extensive due diligence of potential partners
	Talent	Insufficient specialized talent in an ecosystem	
	Physical risk	Asset destruction or degradation due to fire, drought, hurricane, or other physical risks	
	Financial	Inability of self or key partners to fundraise	
Country	Carbon markets regulation	Uncertain or changing carbon market regulation, including taxes, benefit-sharing, and Corresponding Adjustments	<ul style="list-style-type: none"> ● Purchase political risk insurance ● Proactively engage with relevant policymakers and other government stakeholders
	Political risk	Risk of political violence, currency inconvertibility, expropriation, breach of government contract, etc.	

Blended finance for nature-based carbon removal projects

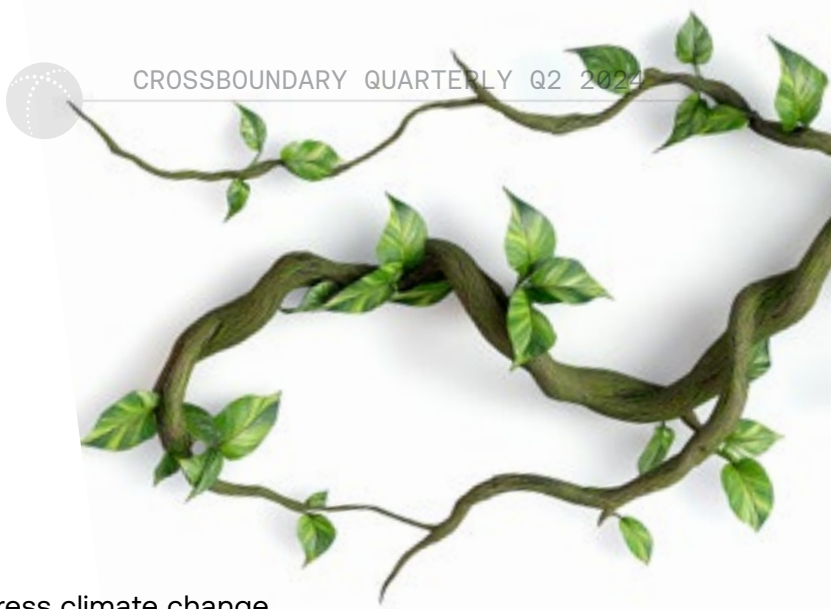
There is more than enough money to address climate change, and certainly more than enough to fund the nature-based solutions that are needed to meet the Paris Agreement targets. Climate Policy Initiative estimates US\$8.6T of global climate finance is needed annually until 2030. This is less than the US\$11.7T COVID-19 emergency spend in 2020, and it is less than the combined global public expenditure on military (US\$2.2T) and fossil fuel subsidies (US\$7T).

Capital is not the problem. The problem is getting the right capital to the right projects at the right time.

This is where blended finance approaches can help move the needle – especially in new sectors, new markets, and of course for FOAK projects. Blended finance is the use of public or philanthropic capital to improve the risk-return profile of a deal in order to crowd in private, commercial investment. Blended finance can take many forms, including upstream grants to de-risk a project, design funding to bring a new investment vehicle to market, technical assistance vehicles alongside funds, technical assistance to reduce transaction costs during the investment process, first-loss capital or other junior capital within the investment structure, and guarantees on invested capital.

Concessional capital is limited, and it is precious; its use should be carefully tailored to the specific problem that needs to be solved.

In scaling nature-based carbon projects, the case for targeted use of concessional funding is two-fold. First, it addresses one-time costs of pioneering transactions that pave the way for fully commercial opportunities. Unlike in developed markets, in new markets and underserved geographies, first movers often face a penalty rather than a reward. In the case of nature-based solutions, first-movers must test demand for carbon credits from new project types, educate investors and buyers, navigate and inform

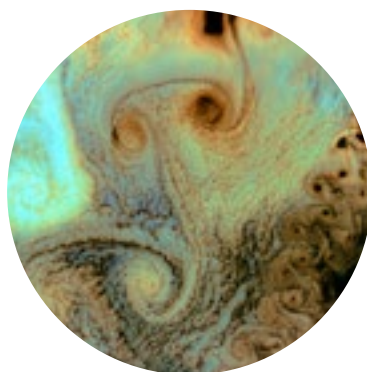




development of an evolving regulatory landscape, upskill the local workforce, and often vertically integrate operations. These are all additional costs of doing business that benefit those that follow. This broader market development impact builds the case for subsidy of first-movers.

Second, concessional funding recognizes that nature-based projects generate positive externalities – public goods – that are still unpriced in the market today. For example, biodiversity benefits and livelihoods benefits can increase the price of carbon credits in the voluntary market, but this does not necessarily fully compensate the project for the additional costs of achieving these higher impact outcomes. Likewise, climate adaptation outcomes, as well as other ecosystem services beyond carbon sequestration, are not part of the investment case for nature today. Philanthropic funding can be used to help address the costs of achieving this impact, and in doing so also make the project more attractive to investors.

Finally, while conversations around blended finance often focus on first-loss instruments, we find that often deals can be done on commercial terms but face high transaction costs in getting the deal over the line. This is especially the case when global investors are looking at opportunities in emerging markets for the first time, or when they are looking outside the few large countries that receive the majority of investment today. Getting to know the regulatory environment, local actors, and unique risks and opportunities in a new geography is costly, especially without a full-time team on the ground. Likewise, there are high search costs for projects to connect with the right investors, and to build trust between all parties involved. Donor or philanthropic funding of neutral, third-party



investment facilitation services can help mutually beneficial deals to close – setting important precedent in the market.

To move the market from pilots to repeatable, scalable projects – past the FOAK valley of death – we see four key areas where funding is most needed:

1

Feasibility - and development-stage philanthropic or donor funding to understand the business case and help projects meet specific milestones for investability

2


Early-stage equity for FOAK projects and first phases of greenfield projects, proving out execution, demand, and commercial viability

3

Philanthropic or donor funding for investment facilitation targeting pioneering transactions with market-level impact

4

First-loss or other junior capital to de-risk specialized nature funds that can prove out the investment case and create attractive, aggregated opportunities for commercial capital at the fund level

The gravity of the climate crisis demands that we find ways to mobilize large-scale investment into both climate tech and natural climate solutions. At CrossBoundary, we are committed to leading this movement by building the pipeline of bankable, high-impact, and high-integrity carbon projects. With support from development partners, we help nature-based project developers in emerging markets design projects and structure financing agreements that are mutually beneficial for developers, investors, buyers, and local communities; and we ourselves invest in high-impact projects – with the ultimate objective of establishing the proven, replicable models that we so urgently need. 

Q&A

How can innovation in funding models unlock energy access in emerging markets?

Moving beyond traditional blended finance models can spark market activity and reduce bottlenecks to clean energy provision in Africa





Written by:
Kate Pallett, Senior Marketing
and Communications Manager
at CrossBoundary Energy



Nchimunya Chipo Hamukoma is the Senior Associate for Demand Jobs and Livelihood (DJL) at GEAPP, based in South Africa. She leads GEAPP SA's Just Transition portfolio and supports the DJL Africa team on operations and project management for the Energizing Women & Youth in Agri-Food Systems Program (EWAS) in Nigeria and Ethiopia.

She has worked as an implementor, a donor, and a policy advisor to institutions and governments on issues such as youth employment, urbanization, and the future of work, most notably in Morocco, South Africa, Nigeria, and Ghana. She was previously the Head of Funder Partnerships & Strategic Projects Harambee Youth Employment Accelerator, a South African-based youth employment organization.



High energy costs and the instability of electricity provision are two major hindrances to African businesses and investment on the continent. The global move toward decarbonized forms of energy is crucial in mitigating climate change, yet progressing without addressing the energy access challenges in Africa will render this energy transition unfruitful. I sat down with an old friend and peer, Nchimunya Chipo Hamukoma, the Senior Associate for Demand, Jobs and Livelihood at the [Global Energy Alliance for People and Planet \(GEAPP\)](#), to hear her thoughts on how innovations in funding can propagate inclusive energy access.



Thanks for speaking with me, Chipo –

As a starting point, please describe GEAPP and your work?



GEAPP is an alliance of partners bringing their unique offerings together to accelerate the transition to renewable energy in emerging markets to power inclusive, sustainable economic growth for millions of people. Our overarching ambition is to reduce 4 gigatons of future carbon emissions while providing 1 billion people with clean energy access and creating 150 million new jobs and sustainable livelihoods. My work focuses on the intersection of policymaking, philanthropy, and social impact organizations, working to unify multiple stakeholders around bold visions to deliver pragmatic results. In South Africa, I lead the Just Transition portfolio and I also work with the GEAPP Africa team on Energizing Women and Youth in Agri-Food Systems in Nigeria and Ethiopia.



Our overarching ambition is to reduce 4 gigatons of future carbon emissions while providing 1 billion people with clean energy access and creating 150 million new jobs and sustainable livelihoods.



You mentioned the intersecting roles of policymakers, philanthropy, and social impact organizations. Within this picture, what role does blended finance play in enabling a just energy transition in Africa?



The energy transition in emerging markets (excluding China), requires around US\$1.4 trillion - US\$1.9 trillion¹ annual investment, of which two-thirds will need to come from the private sector. To attract private capital at this scale will require an estimated US\$80 billion of concessional capital per annum, yet concessional capital is scarce. Because we have access to a philanthropic capital base, GEAPP is uniquely placed to lay the foundations required to bolster models that are on the brink of commercial viability. As such, we think about the role of philanthropic capital as a type of funding innovation that can de-risk investments into strategic markets. Blended finance isn't the only tool in our arsenal, but it is an effective tool to catalyze investments within the markets and sectors that will affect the most change.

The energy transition in emerging markets (excluding China), requires around US\$1.4 trillion - US\$1.9 trillion annual investment, of which two-thirds will need to come from the private sector.



¹ <https://www.iea.org/reports/scaling-up-private-finance-for-clean-energy-in-emerging-and-developing-economies/executive-summary>





From your perspective, how has the deployment of blended finance for energy infrastructure changed, and what does this say about the sector?



There have certainly been big changes in the funding landscape for renewable energy in the past few years. Where renewable energy was once a “fringe” investment, governments and pension funds are starting to recognize the value of these investments, and the increased scale has changed the blended finance picture, with larger and more diverse projects being funded. For example, the second round of the Nigeria Electrification Project (NEP2) attracted more than double the funding from the World Bank (US\$750m vs US\$350m). The increased scale, and innovative funding models, have gone a long way to make renewable energy recognized in the market as a potential competitor with fossil fuels.





You mentioned innovative finance solutions. In what way can traditional blended finance be broadened to enhance its impact?



Whilst blended finance has been an important part of the growth in renewable energy infrastructure, it can have drawbacks. Often, the main obstacles point to the availability and dependability of donor funding, which can be intermittent. However, in some cases, overcrowding of concessional capital can also be an issue, discouraging private investments due to the expectation of low capital costs and hesitation for private investment.

When it comes to renewable energy investments, these challenges point to the need for innovative, carefully structured finance models that can bring out the best environments for market activity. Part of this includes risk mitigation instruments like guarantees, insurance, and first-loss capital that will enhance the attractiveness of private capital in the energy sector. Another such innovation is a decoupled approach: the provision of philanthropic capital and private finance running in parallel or in complementary roles, rather than in a blended model. This allows for private capital to focus on creating commercially viable operations, whilst philanthropic capital can provide support for high social impact activities with low returns, such as the regulatory support and advocacy that creates an enabling environment for commercial activity.

A decoupled financing approach allows for private capital to focus on creating commercially viable operations, whilst philanthropic capital can provide support for high social impact activities with low returns, such as the regulatory support and advocacy that creates an enabling environment for commercial activity.

An example of an innovative funding approach, with philanthropic capital bolstering a sector that supports commercial operations, is the GEAPP-supported Demand Aggregation for Renewable

Technology (DART) program, which created a partnership model that allows distributed renewable energy companies to procure equipment at affordable prices and with attractive financing terms. The program, launched in 2022 and now expanded, has had success in accelerating renewable energy access in Nigeria by providing cheaper energy components to businesses supplying renewable energy, making them more profitable and thus sustainable.





What are the factors that GEAPP considers when enabling successful renewable energy investments?




To be a good steward of philanthropic capital, it is important to think about the impacts – not only those that are immediate, but also any unintentional consequences of bringing capital into a market and the charitable outcomes of investing. When designing a project or model, we take care to ensure that we are working with trusted market partners. Philanthropic capital can have very different objectives from private investment, yet creating commercial viability is a solid way to ensure the sustainability of projects, so understanding what a capital injection might unlock in terms of attracting additional commercial funding is a really important decision factor in where to deploy the most investment.



Any closing thoughts?



The interplay among private, concessional, and philanthropic capital is an important factor in enabling a renewable energy transition in Africa and emerging markets. For participants in this space, asking important questions about what meaningful support should look like is essential. Financing, both from private and non-private sources, should carefully consider additional value when developing blended or parallel approaches. Asking, “What can this investment bolster, and how can it create value that will further the just energy transition?”, is an important starting point to ensure that value is derived and that projects are sustainable. 



CrossBoundary Energy



Inauguration of the Rio Tinto QMM, CrossBoundary Energy and Madagascar partnership solar power plant at Ehoala Park

Rio Tinto QMM (QIT Madagascar Minerals) took an important step towards decarbonizing its ilmenite mine in Fort-Dauphin in April. The Ehoala Solar Park, a partnership with CrossBoundary Energy, was inaugurated under the high patronage of His Excellency Mr. Andry Rajoelina, President of the Republic of Madagascar.

Isabelle Wabete, Managing Director of QMM: “This project is in line with QMM’s ‘Sustainable Mining’ vision, and demonstrates QMM’s commitment to achieving Rio Tinto’s decarbonization objectives. The initiative is intended not only as a contribution but also as us recognizing the direct role we have to play in addressing climate change in Madagascar.”

Richard Stanford, Chief Technical Officer of CrossBoundary Energy (CBE): “We are delighted to finance, own and operate this exciting project, whose importance

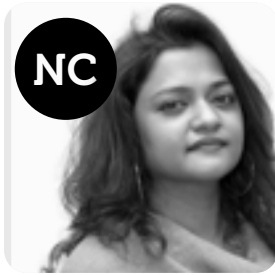
in the fight against climate change is well established. Our partnership with Rio Tinto, and through it the Government of Madagascar, is exemplary, and we are delighted to note the recent development of renewable energies in Fort-Dauphin and Madagascar. CrossBoundary (CBE) remains a partner both available and committed to bringing renewable energy solutions to our customers.”

President of the Republic of Madagascar, Andry Rajoelina: “Madagascar aspires to be a model of resilience in the face of climate challenges, particularly in the industrial sector. The Malagasy Government recognizes the vital importance of an adaptable industry that contributes to the effort to combat climate change. As a nation, we are committed to being pioneers in this transition, demonstrating our determination to protect our country and offer a sustainable future to our fellow citizens.”

Unlocking the potential of blended finance in Asia

A Conversation with Nandini Chaudhury,
Head of South and Southeast Asia Advisory



**Featuring:**

Nandini Chaudhury, Head of South and Southeast Asia Advisory, CrossBoundary Advisory



Blended finance is a powerful tool for addressing funding gaps and driving sustainable development in regions like Asia.

The Money Meets Mission podcast, brought to you by [AVPN](#), the largest social investing community in Asia, features business, philanthropy, and impact investing leaders sharing stories of tackling some of the largest and most complex social and environmental issues facing Asia today.

In this Q&A excerpt, we highlight their recent Impact Investing Musings conversation with CrossBoundary Advisory's Head of South and Southeast Asia Advisory, Nandini Chaudhury, who breaks down blended finance as a concept and how it can be structured to mobilize private capital and support sustainable development goals (SDGs).



Read on for the interview and listen to the full podcast [here](#).

Disclaimer: This interview has been edited for length and clarity.

Taimur Nabili, AVPN:

Let's begin by discussing your definition of blended finance in the Asian context.

Nandini:

Blended finance is essentially a structuring method in which catalytic capital or development funding from various public or philanthropic sources is utilized to increase private sector investment in sustainable development goals. The essence of blended finance

is to help organizations, sectors, or countries move from an early stage to a matured, able-to-absorb commercial capital stage.

The Asia Pacific region is geographically and economically diverse, with a fair mix of developing, developed, and transition economies. The region is considerably exposed to climate and macroeconomic risk, and quite often, the gap between the perceived and the actual risk is very high.

The UN estimates that for the Asia Pacific region to realize its Sustainable Development Goals by 2030, an annual additional investment of about US\$1.5 trillion is required. So here we are dealing with a region of considerable perceived risk that needs this massive capital inflow to realize the Sustainable Development Goals. And we are faced with a classic chicken and egg problem.

Does capital flow in first to create a demonstration effect for these markets to reduce the perceived risk? Or do we spend time intelligently crafting risk mitigation solutions and exploring them first to crowd in private capital? Well, the answer lies in balancing both. Blended finance is one of the best tools available to create that balance.

AVPN:

You talk of perceived risk, but you've also said it's an extraordinarily diverse region. The perceptions in each country within that region must be somewhat different.

Nandini:

Yes, exactly. It is not only about country perception, right? Even if you look at the

sectoral perception within these countries, it is different. For example, if you look at the commercial and industrial solar market or the solar rooftop market, it is perceived as a very safe market in India. At the same time, if you look at neighboring Bangladesh, there are barely two years' worth of projects that you can look at to see how they have performed. So, there is a layer of country-level risk and sector-level risk.

AVPN:

Are there some fixed principles that guide your work in blended finance? What imperatives do you keep in mind when you're structuring a transaction?

Nandini:

When considering a blended finance transaction, you overarchingly examine a few concepts. Number one is leverage—how much of your philanthropic or development capital can mobilize private capital? Typically, we talk about 3x leverage, 7x leverage, and 10x leverage. This means that if you pool US\$1 of philanthropic capital, you can mobilize 7 times or 10 times the amount of commercial capital.

The second is impact. It has to be measurable. It has to be additional. And unless you have a measurable impact from the transaction, the blended finance intervention can fall through.

Third, we look at returns. Ultimately, the goal is to deliver market-based risk-adjusted returns to the private sector, which is achieved by allocating the risks in part or full to the development finance tranches on non-commercial terms.

AVPN:

Give me a sense of some models that have worked in real life in your experience.

Nandini:

I can give you an example of one of CrossBoundary's investment platforms, CrossBoundary Energy—which focuses on commercial and industrial renewable energy in Africa. When CrossBoundary launched this fund in 2013, we were able to pull in commercial capital by using a junior tier of funding through USAID. This transaction created a pioneering demonstration effect for the sector that these projects can be commercially viable in a geography that investors are not generally comfortable with. It has grown into a multi-million dollar investment platform that owns and operates renewable energy assets across Africa.

AVPN:

What are some examples of challenges and barriers to implementing policies and plans like this?

Nandini:

I can give you an example from a blended finance transaction in Bangladesh. The first and foremost challenge is understanding the concept. Many are unfamiliar with blended finance. In this case, we were working with a financial institution and helping them understand the methods of structuring the transaction, monitoring, and evaluating.

Another challenge we typically face is tailoring blended finance to the local context, and this was particularly true in the Bangladesh case. When we were applying

the typical blended finance archetypes to Bangladesh, we had to consider country-level idiosyncrasies.

Another point to keep in mind is the monitoring and evaluation of the blended finance transaction. Quite often, we have seen insufficient attention paid during the structuring stage. What happens in that case are outcomes that are not measurable, impactful, and, most importantly, additional.

The idea of blended finance is to pool development capital so that it has a mobilizing effect on commercial capital. It should demonstrate additionality for the sector. But if you do not structure it correctly, the additionality concept can sometimes be lost.

AVPN:

How much explaining do you have to do to investors to let them know that the solution you implement is appropriate to their needs?

Nandini:

That depends on the class of investors you are reaching out to. Right now, blended finance is mainstream in the Western world. Most understand the concept. If you can translate the opportunity into clear investment terms, it is not an uphill battle. The major challenge we have seen while executing transactions, especially in Asia Pacific, is socialising the concept for the regional actors.

For example, regional donors and family offices have significant pools of capital that can be mobilized for such interventions in the region. Most of our effort goes into

helping these players understand how to shift from their traditional impact investing or grant-making mentality to a more holistic blended finance approach.

AVPN:

Where is the interface between the needs of a country where blended finance is the answer and then the process of generating interest amongst those players who need to get involved in the deal?

Nandini:

The answer lies in structuring the transaction effectively. On the structuring side of things, first, it needs to be robust. It needs to be aligned with the development principles of the non-commercial funders who will be contributing to the transaction. It needs to be aligned with their ultimate goals. And then it also needs significant marketing. If considerable time and effort is spent to pool in the necessary resources and maybe advisors to structure it correctly, they will be able to market it correctly to the necessary partners.

A lot of this requires considerable understanding of the nuances of the transaction. If you go to a traditional commercial investor or a pension fund and say, hey, will you invest in a solar project in Bangladesh? The answer will be no.

But suppose you can numerically and theoretically explain how you've secured development actors into the transaction and the significant names anchoring the transaction and mitigating the risk. In that case, the transaction becomes interesting to this commercial player. A lot of the effort also goes into translating this development or impact angle, translating this concept into a language that commercial investors will understand. And that language is essentially the language of risk and return: What am I doing at a transaction level to reduce the risk? What am I doing at a transaction level to increase the returns? It's as simple as that.

We must simplify it and ensure the commercial investors understand that concept. 



Podcast

For more insights, listen to the full podcast here

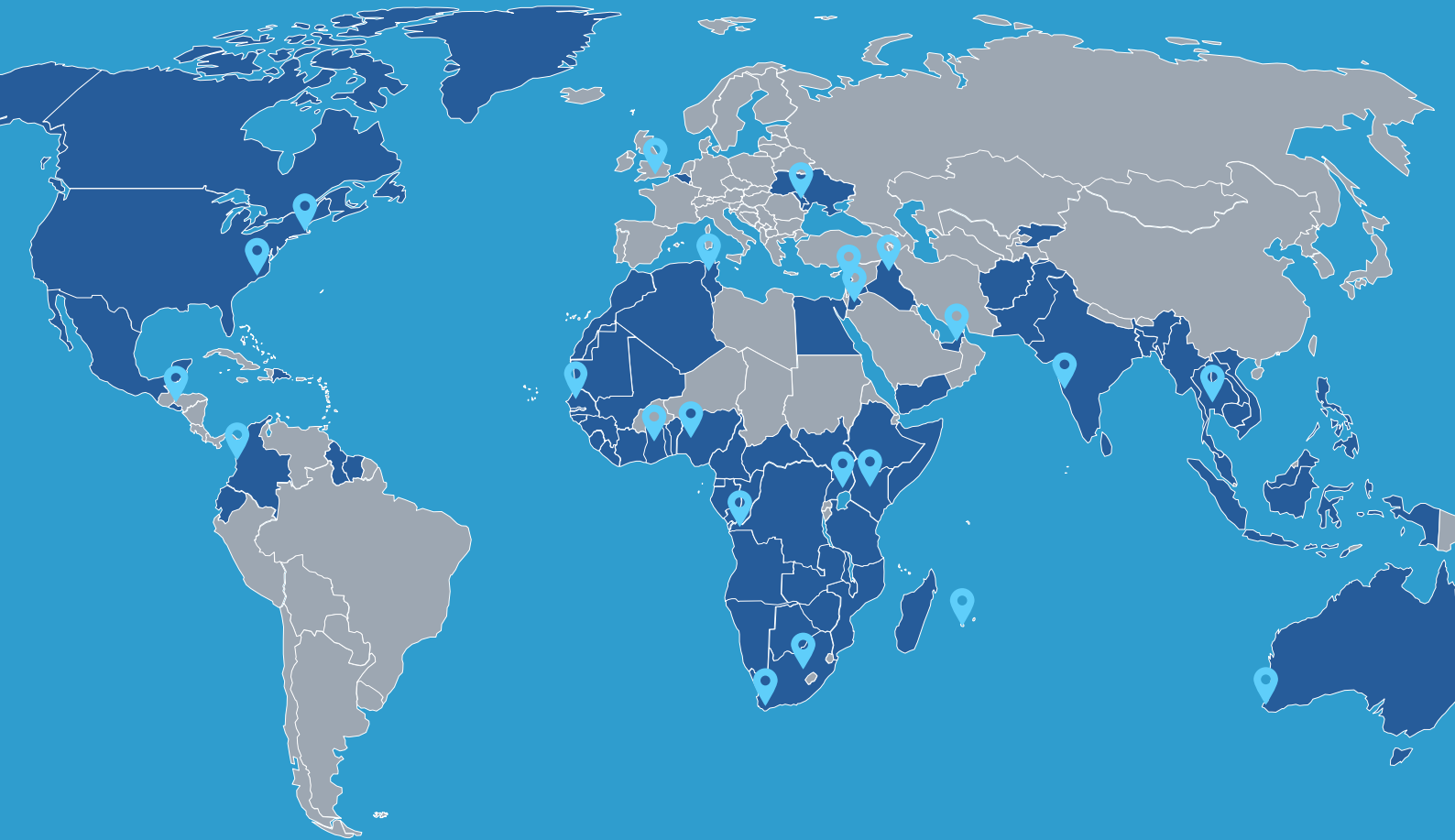


Nandini Chaudhury is CrossBoundary Advisory's Head of South and Southeast Asia Advisory and a member of the CrossBoundary Group Council. She holds an MBA in Finance and a Bachelor of Science in Economics. She has 13+ years of experience and specializes in energy transition investments, the voluntary carbon market, and the oil and gas market. Before CrossBoundary, Nandini worked with Trafigura Group, where she developed and managed a

US\$200M+ investment platform of renewable energy projects for Puma Energy (subsidiary and retail arm of Trafigura), focusing on emerging economies of Africa, Central America, and South-East Asia. She was instrumental in carving out the energy transition strategy for Puma Energy's Future Energies' by formulating viable business models to align with the company's current footprint and future ambitions. Nandini is based in our Mumbai office.



CrossBoundary
Group



Our geographic focus

We have offices in more than
23 locations across underserved
markets and global financial centers

- NY
- DC
- San Salvador
- Bogota
- London
- Chişinău
- Tunis
- Dakar
- Accra
- Lagos
- Kinshasa
- Nairobi
- Kampala
- Johannesburg
- Cape Town
- Ébène
- Amman
- Erbil
- Beirut
- Dubai
- Mumbai
- Bangkok
- Perth

Reducing transaction costs and information asymmetries to mobilize capital effectively in US underserved markets

The following is a preview of a white paper by CrossBoundary Advisory's US Underserved Markets team. Find out more about CrossBoundary Advisory's work in US Underserved Markets on our website.



Written by:
Nathan Kelly,
Head of US
Underserved
Markets,
CrossBoundary
Advisory
and Hannah
Mae Merten,
Advisor, US
Underserved
Markets,
CrossBoundary
Advisory



In the wake of George Floyd's murder in May 2020, the 50 largest US public companies pledged nearly US\$50 billion to address racial inequality, more than 90% of which was allocated as loans or investments into Black institutions and communities. However, in the nearly four years since their pledges have been made, 37 companies have confirmed disbursing only US\$1.7B of the total pledged, and most of those dollars have been disbursed in the form of grants.

We do not think this is an anomaly. Since the introduction of empowerment zones in the 1990s, a litany of government and private programs have sought to promote investment in US underserved markets. Yet most of these programs have achieved middling results, with (by our count) none having reached the lofty goals set out for them.

Despite the political will, availability of public/philanthropic funding, and best intentions of these programs, there is no inevitability to the flow of capital to opportunities in underserved markets. Two unique characteristics of underserved markets prevent programs and policies from reaching their objectives: high transaction costs and deep information asymmetries.



We argue there is a need to address the underlying barriers that prevent capital flows to underserved markets.

- **Transaction costs**—both at the deal level and for intermediaries—are an under-addressed friction to capital flows.
- **Transaction costs** can be higher in small deals in underserved markets relative to larger deals in deeper markets due to novelty and complexity; investors know that when transaction costs are too high, even otherwise commercially viable deals die.
- **Information asymmetries** between investors and capital seekers breed distrust and cause markets to deteriorate. Without ways to

reliably signal quality or credibility, capital providers avoid risk, while capital seekers are wary of investor exploitation. Both investors and capital seekers thus lose out on viable deals.

- **Investment facilitation** provides expertise, resources and an “honest broker” role to reduce these barriers.

- Without **efficient and effective capital formation**, underserved markets in the US will struggle to grow, deepening inequality and depriving individuals of the opportunity to build businesses.



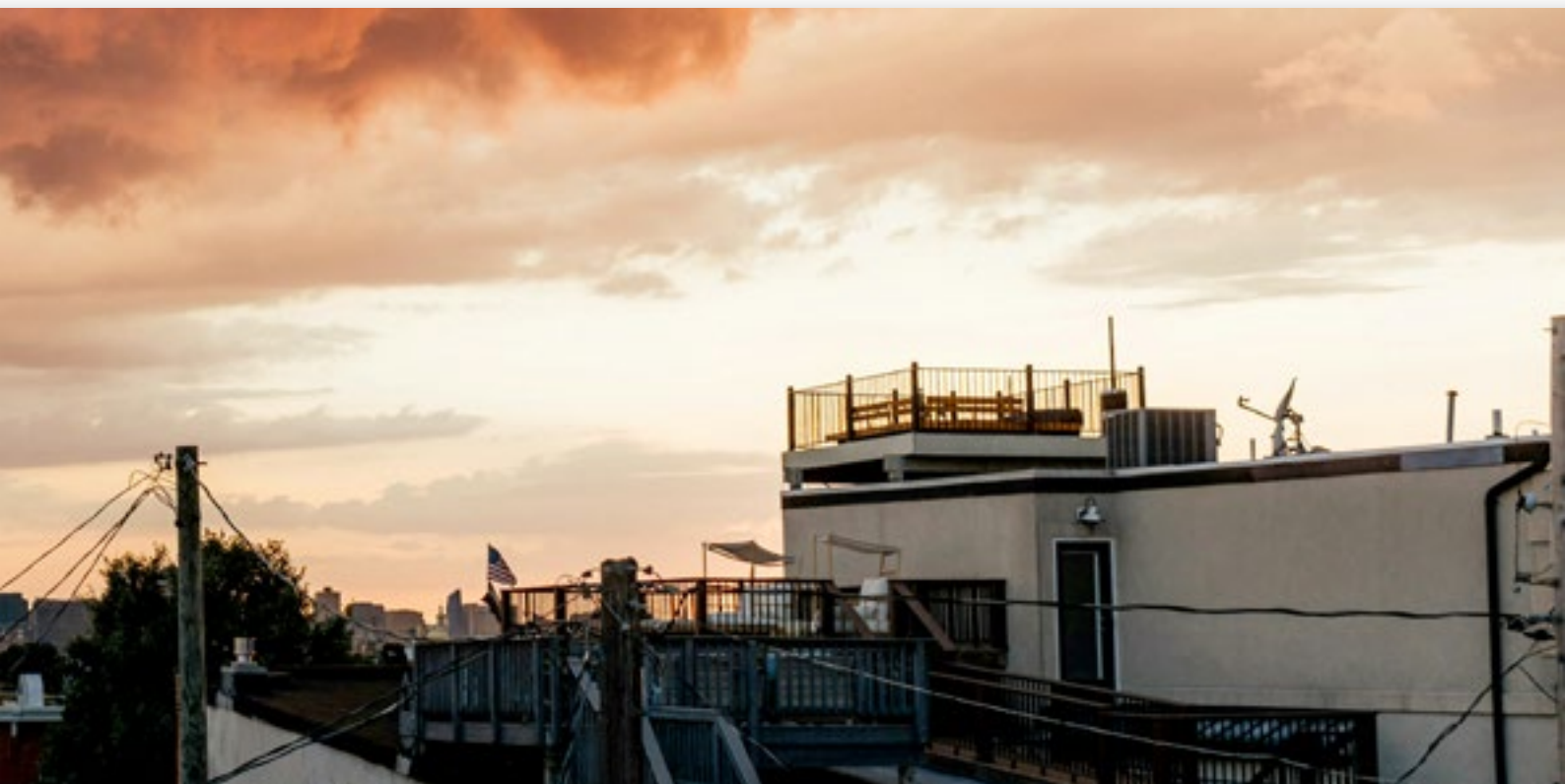
Economic theories of transaction costs and information asymmetries explain why these frictions are not minor irritants, but rather are major impediments that can cripple capital flows if left unaddressed. According to these theories, current programs overly focus on de-risking investments through subsidies and guarantees that increase gross returns, and they fail to solve for mutual distrust between capital providers and capital seekers in underserved markets.

To be effective, solutions must directly tackle transaction costs and information gaps. Based on our decade of experience in emerging and frontier markets, we propose that investment facilitation is an ideal approach for doing so. Investment facilitation provides expertise, resources and an “honest broker” role to reduce these barriers at both the intermediary level, such as establishing new funds, and the direct investment level.

Removing barriers to capital flows into underserved markets requires a holistic solution that addresses both market failures and micro-level obstacles to investment.

For the past decade, CrossBoundary has implemented and refined investment facilitation as a targeted approach to address transaction costs and information asymmetries in underserved markets around the world. We believe investment facilitation has a critical role to play in driving economic growth in underserved markets within the US.

As practitioners of blended finance—a term used to describe the combination of commercial capital (often from the private sector) and concessional capital (often from the public sector) to unlock investment in underserved markets—we believe that until the barriers of high transaction costs





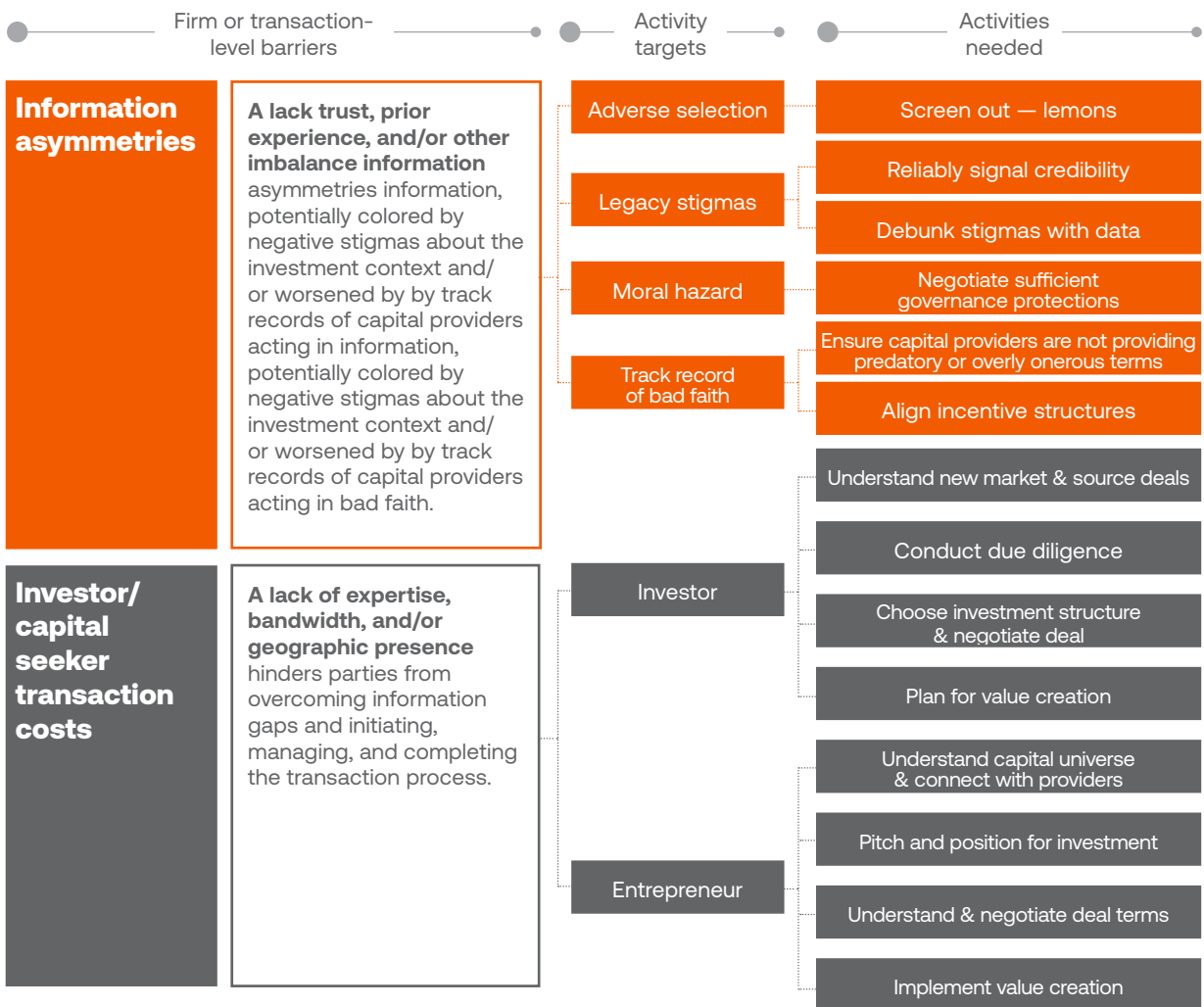
and deep information asymmetries are addressed, these programs will continue to underperform their targets.

Investment facilitation takes on numerous critical tasks that reduce information asymmetry and transaction costs, and enable transactions to close using the best-suited capital providers. Importantly, investment facilitation does not just work

with one type of investor or vehicle, but rather seeks to match the source of capital with its end uses, ensuring an alignment of interests, mission, and values.

Figure 1 highlights several of the activities that an investment facilitation team undertakes to overcome information asymmetry and transaction costs.

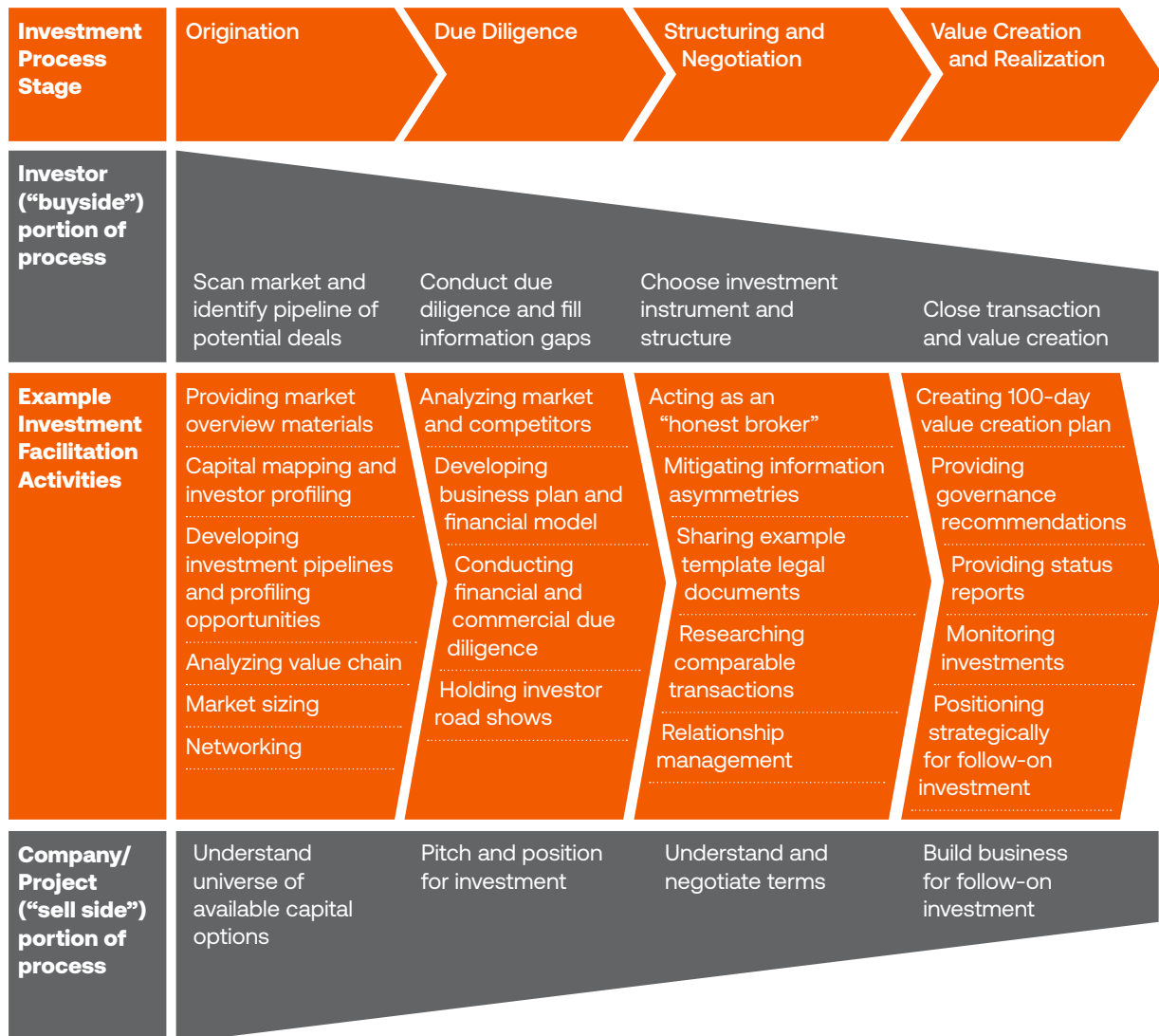
Figure 1: Activities to overcome information asymmetries and transaction costs



In our experience at CrossBoundary, we have found that these activities are best executed on a platform that can advance multiple transactions at once within a given market for several reasons. First, these transactions can take a long time from origination through to execution and value creation. Second, they can have inconsistent workloads (a transaction might require

significant amounts of bandwidth one week, and then be in a period of stasis as investors review materials, or a company, project, or fund executes specific initiatives to prepare for raising outside capital). Finally, investment facilitation is most effective when it can address each stage of the transaction process, supporting both investor and capital seeker in moving through each stage.

Figure 2: Investment facilitation through the investment cycle

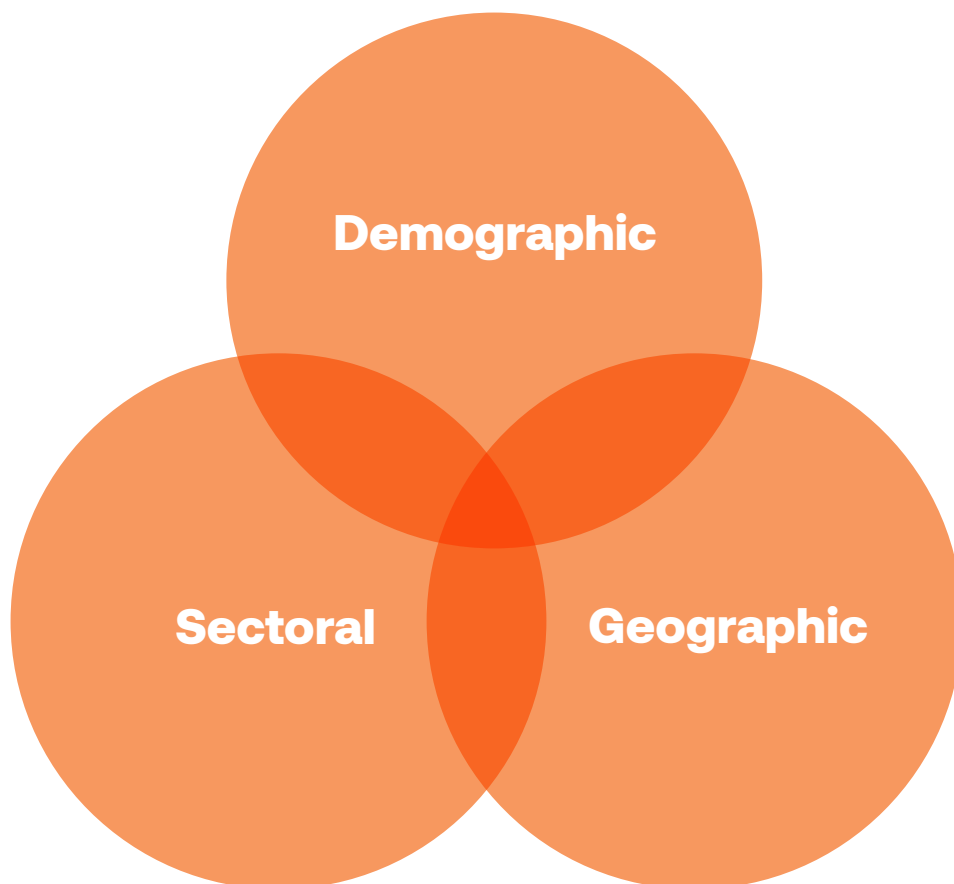


What constitutes an underserved market?

At a very basic level – underserved markets are those in which the amount of capital invested in a market is less than the market opportunity. Some of these are easy to identify by the outcomes – only 2% of venture capital goes to women, the DRC receives less investment despite greater market opportunities. But some are harder to see – especially in the US where underserved markets might be hidden behind a strong market (e.g. a city like Minneapolis seems to punch above its weight in terms of capital invested, but certain neighborhoods seem impervious

to capital flows; farmland seems to be heavily invested in, while organic farmland struggles to raise capital despite strong financial returns).

In order to better see underserved markets we break them into three categories – demographic, geographic, and sectoral. Each has their own problem and solution sets – and while they often overlap (e.g. a certain demographic is concentrated in a certain geography) breaking them down into their respective components allows us to better design solutions for each.¹



¹ Not all investment data is public or easily aggregated. In the below breakdown we use venture capital investments relative to population size as a proxy for how underserved a given market is.

Demographic underserved markets

Venture capital investment in the US is relatively highly concentrated among males, and is underrepresented in Black, Latino, and Native American populations as indicated in the graphic below.

There are lots of reasons for this – with some of them overlapping with geography and sector. For instance, most Native American Reservations are located away from the deepest capital markets of New York, Boston, San Francisco, and Los Angeles which increases the transaction and management costs for capital providers located in those major financial markets. But many are specific to a demographic – redlining may have been defined geographically, but it was a proxy for race. And for Latino businesses, the concern of undocumented workers

and lack of data on the market because of a lack of available market research is a specific challenge that both keeps entrepreneurs from approaching the formal channels of capital, and prevents investors from entering the market.


Geographic underserved markets

Geographic underserved markets are – in many ways – the easiest to define. Investing data is often disaggregated by geography, providing a window into how capital overlooks certain geographies. A quick breakdown of venture capital investment by geography shows that the Midwest and Southeastern US are more challenged to raise investment capital than businesses in the Northeast, West Coast, or Mid-Atlantic.



Capitol Hill B

BURN
Plants




But – investing data by geography depends highly on its granularity. Certainly, the United States is not an underserved country, but Louisiana is. Pennsylvania is not an underserved state, but Erie County is. So, what is the right focus level to evaluate a geography? The Economic Innovation Group has broken down US underserved markets by geography in what we have found is the most granular, well thought through analysis of US geographically underserved markets in their Areas of Persistent Poverty report. Using this lens reveals a long history of areas that have been overlooked by capital, leading the extreme economic underperformance by these geographies over many years.

A careful review of these areas reveals histories of injustices, specifically against Black and other minority groups, that have left critical areas under invested in, as well as key corridors that have lost ground as our economy has become “financialized” with capital increasingly concentrated on the coasts.

Sectoral underserved markets

Underserved sectors are harder to define than underserved demographics or geographies. Investment capital within the US is used to evaluating sectors so finding those that are overlooked for something other than their fundamental economics can be challenging, but they do exist, and typically they exist as a result of unintended structural challenges. The best example that we have found of an underserved sector is regenerative agriculture and organic agriculture. Despite promising long-term economics based in cost and risk reduction (reducing inputs and creating farms that are more resilient to weather shocks) as well as a price premium in the case of organic agriculture, the structure of crop insurance and the existing loan infrastructure fails to take these into account, leaving the sector underserved.

But why should we care?

Much of the research on development economics has taken place abroad, comparing a country's per capita income with the amount of outside investment received. Robert Solow's original growth curve has remarkably predicted the impact of investment on country economies. The same is true of underserved markets in any form – without efficient and effective capital formation, the demographic, geographic, and sectoral economies that we care deeply about will struggle to grow. Of course there are other factors that are necessary for economic growth – and capital formation can both an outcome and a driver of those factors (e.g. an educated workforce can attract outside investment, but outside an investment can also increase the education level of a workforce). But, without accurately identifying underserved markets, we can do little to address the very human problems that exist within them. 







CrossBoundary
Group

CrossBoundary is honored to be included in the ImpactAssets 50 2024 list

The ImpactAssets 50™ (IA 50) 2024 is a free publicly available, searchable database of impact investment fund managers globally. The IA 50, now in its 13th year, is designed to offer a simple way to identify experienced and emerging impact investment firms and explore the landscape of potential investment opportunities across diverse impact areas, maturity levels and geographies. This year's list is composed of 155 impact fund managers selected from an unprecedented 343 applications, a submission volume that is 15% higher than last year. This growth signals increased interest in the IA 50, alongside expansion and maturation of the impact investing industry at large. The increasing traction also points to a broader shift that embraces impact investing's critical role in shaping a sustainable future.

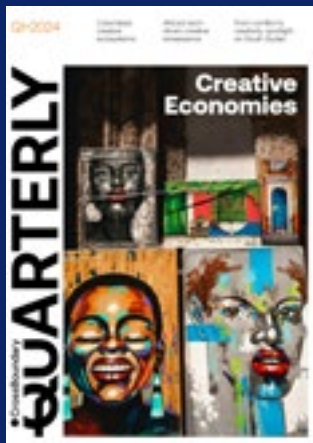
“Year after year, the IA 50 stands as an essential guide for everyone in the financial ecosystem — from individual investors to global corporations — enabling them to discover and engage at the forefront of impact investing. The database encapsulates the pulse of the industry, providing a snapshot of the firms poised to make a significant difference through their investments,” said Malaika Maphalala, CPWA®, IA 50 Review Committee Member, and Wealth Advisor and Trust Steward, Natural Investments PBLLC.



Our next *CrossBoundary Quarterly* will focus on Localization and Decentralization

Localization and decentralization are two mega-trends that are shaping the investable landscape across underserved markets. The donor community and global investors are seeking greater participation from local partners, partly to drive greater impact, but also to capture more granular insights on market developments. Notably, these

approaches are not confined to emerging and frontier markets, but rather are gathering attention within OECD economies as well. Our Q3 *CrossBoundary Quarterly* will explore the “Localization and Decentralization” theme through the lens of our teams based in more than 20 locations across underserved markets and global financial centers.



It's not too late!

Did you miss our launch issue on Creative Economies?

The creative economy—also known as the “orange” economy—is vital in helping countries to diversify the composition of their output while enabling new sources of growth. The inaugural edition of the *CrossBoundary Quarterly* explored the theme of “Creative Economies” with highlights on creators across Africa, the intersection of sports and creatives in South Sudan, and the role that creative industry ecosystems are playing in revitalizing Colombia’s municipalities. Explore the issue on our website.



CrossBoundary
Group



CrossBoundary
Group