

CROWDING IN OR CROWDING OUT?

Why rising public debt may reshape the financing of energy and infrastructure

By Gustavo Vera, CFA, FRM

The world needs more infrastructure just as governments are finding it harder to finance it. Power generation, grids, transport, water and digital infrastructure all require large amounts of capital. Public balance sheets are increasingly constrained, while private capital remains available. The apparent solution is straightforward: if governments cannot finance the next generation of infrastructure, institutional investors can.

Private capital can replace part of the financing provided by the state. It cannot necessarily replace the state itself. A privately financed toll road may still depend on a concession agreement. A power plant may depend on a regulated tariff, a long-term offtake contract or a government-backed utility. A transmission asset may earn returns established by a regulator. A public-private partnership may replace upfront public expenditure with availability payments extending decades into the future.

This distinction matters more as fiscal conditions become tighter.

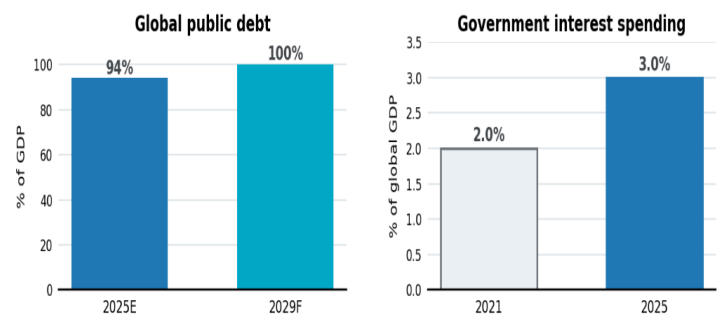
The IMF estimates that global public debt reached nearly 94% of GDP in 2025 and, under current policies, will reach 100% by 2029. At the same time, global government interest payments have risen from roughly 2% of GDP four years ago to almost 3%. The fiscal problem is therefore not only the stock of debt. It is the increasing competition for the next dollar of public expenditure.

That competition is arriving just as infrastructure capital requirements remain enormous. The IEA expects global energy investment to reach a record US\$3.4 trillion in 2026, including approximately US\$2.2 trillion across renewables, nuclear, grids, storage, low-emissions fuels, efficiency and electrification.

The investment question may therefore be more subtle than whether private capital can bridge the infrastructure gap.

What happens when governments need private infrastructure capital precisely when their own balance sheets become less able to support the commitments that make some of that capital investable?

Exhibit 1. Fiscal space is becoming more expensive



Source: IMF, *Fiscal Monitor*, April 2026. 2029 debt figure is a projection; interest-payment figures are rounded as stated by the IMF.

The infrastructure bill is arriving at the wrong time

There is nothing unusual about governments facing competing spending priorities. What is unusual is how many of those pressures are converging at once.

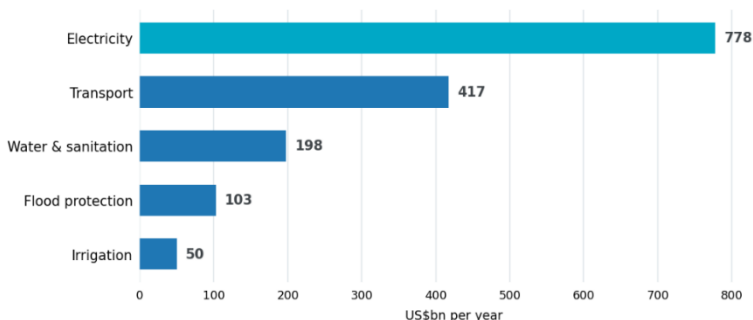
The IMF's April 2026 *Fiscal Monitor* describes public finances as being under pressure from rising interest costs alongside spending demands related to social programs, defense and strategic priorities. The global fiscal deficit remained around 5% of GDP in 2025. These pressures do not imply that governments will stop investing in infrastructure. They do mean that infrastructure increasingly has to compete against expenditures that can be politically or contractually difficult to reduce.

Meanwhile, infrastructure demand is not particularly sensitive to the fiscal cycle. Electricity demand can rise regardless of the budget deficit. Congested transport systems still require expansion. Water systems still need maintenance. Existing grids need reinforcement

even when sovereign borrowing becomes more expensive.

For low- and middle-income countries, the World Bank's *Beyond the Gap* framework estimates annual investment needs of approximately US\$1.5 trillion, or 4.5% of GDP, for new infrastructure investment consistent with infrastructure-related development objectives. Electricity represents the largest component of that estimate, at roughly US\$778 billion per year, followed by transport at US\$417 billion. These are planning estimates rather than observed 2026 expenditure, but they illustrate the scale of the capital requirement relative to many public balance sheets.

Exhibit 2. Infrastructure needs do not disappear when fiscal space contracts



Source: World Bank Group, *Beyond the Gap* / infrastructure-needs framework. Preferred scenario annual average over 2015-2030. Planning estimates, not observed 2026 spending.

Bridging the gap

The obvious response is to bring in private capital.

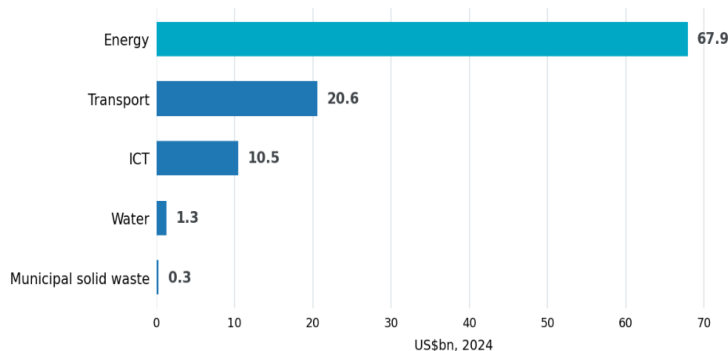
Private participation in infrastructure is hardly new. But the logic becomes particularly attractive when fiscal space is scarce: let private investors provide upfront capital, transfer selected risks to them and recover their investment through user charges, regulated revenues, concessions or contractual payments over time.

World Bank data show that investment commitments in infrastructure projects with private participation across low- and middle-income countries reached US\$100.7 billion in 2024, up 16% from US\$87.1 billion in 2023 and above US\$100 billion for the first time since the pandemic. Energy accounted for US\$67.9 billion across 217 projects, by far the largest sector.

That sounds like crowding in.

But the definition matters. The World Bank's PPI database measures total investment commitments in projects with private participation, not simply dollars of private equity or debt. Projects can contain public participation as well. That distinction points toward the deeper issue: infrastructure financing rarely separates neatly into public and private capital.

Exhibit 3. Private participation is already concentrated in energy



Source: World Bank, *Private Participation in Infrastructure 2024 Annual Report*. Investment commitments at financial close in low- and middle-income countries; not private equity or debt alone.

The growth of private participation is therefore real. What is less obvious is whether fiscal pressure necessarily makes those opportunities more attractive.

Consider a government that can no longer afford to finance a highway directly. A concession may eliminate much of the upfront public capex. But if traffic revenues are insufficient, the project may require minimum-revenue support. An availability-payment structure may replace construction expenditure today with contractual payments over the next twenty or thirty years. A power project may be privately financed but depend on an offtaker whose financial position is ultimately linked to tariffs or public support.

The asset can move off the government's construction budget without eliminating the underlying public-sector exposure.

The IMF and World Bank explicitly treat PPPs this way. Their fiscal-risk framework recognizes direct obligations such as availability payments and subsidies, as well as contingent liabilities including revenue, exchange-rate and debt guarantees. PPPs can transfer risk and improve efficiency, but they can also transform an immediate fiscal cost into a longer-dated commitment.

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For an infrastructure investor, sovereign fiscal conditions can enter valuation through more than one channel.

The most obvious is the discount rate. When sovereign or risk-free borrowing costs rise, the hurdle rate for a long-duration infrastructure project may rise as well, all else equal. That affects both financing costs and the present value of distant cash flows.

But the second channel may be more important: cash-flow credibility.

An airport concession ultimately depends on the concession framework. A regulated utility depends on the durability of tariff-setting rules. An availability-based PPP depends on the capacity and willingness of the public counterparty to make payments years into the future. A power purchase agreement can shift market risk away from the generator while introducing counterparty exposure elsewhere.

Private capital therefore does not simply substitute for sovereign capital. In many infrastructure structures, it is layered on top of sovereign, regulatory or contractual credibility.

Structure	Private capital can provide	May remain public-linked
Regulated energy / grids	Equity, debt, construction and operation	Tariffs, allowed returns, regulation
Contracted generation / power PPP	Capital, construction and operating risk	Offtaker quality, tariff policy, guarantees
Transport concession	Upfront capex and operations	Concession rights, tariffs, termination
Availability-payment PPP	Financing and delivery	Long-term government payment obligation
Asset Recycling	Upfront monetization	Regulatory framework and use of proceeds

Source: Conceptual framework based on IMF/World Bank PPP fiscal-risk guidance and World Bank asset-recycling guidance.

This creates an interesting paradox.

Countries with less fiscal space may have a stronger incentive to monetize assets, recycle capital, grant concessions and structure PPPs. That can create opportunities for infrastructure investors. Yet the same fiscal pressure can also weaken the economics of those projects: higher financing costs, less capacity for subsidies or guarantees, greater scrutiny of long-term

payment commitments, and potentially weaker public counterparties.

Fiscal scarcity can therefore crowd private capital in by creating more investment opportunities, while at the same time making those opportunities more expensive or difficult to finance.

That tension may be more relevant to investors than the headline size of the infrastructure financing gap.

Crowding out or crowding in?

There is an important counterargument.

Infrastructure is not simply another expenditure competing for scarce fiscal resources. Well-selected infrastructure can increase productive capacity. The relevant question is therefore not only how much debt is incurred, but what that debt is used to finance.

Recent IMF analysis illustrates the distinction. Based on a sample of 174 economies, the Fund estimates that reallocating expenditure equivalent to 1% of GDP from lower-impact government consumption toward infrastructure could raise long-run output by approximately 1.5% in advanced economies and 3.5% in emerging and developing economies over about 25 years. These are model-based estimates rather than guaranteed project returns, but they highlight why reducing productive investment mechanically in response to fiscal pressure can also carry a long-term economic cost.

Private participation is therefore not simply about making public expenditure disappear. The most effective structures combine the state's ability to define and support essential public services with private capital, operating expertise and risk-bearing capacity.

A PPP that merely hides a fiscal obligation is not necessarily creating fiscal space. A concession that genuinely transfers construction, operating or demand risk may. An asset-recycling transaction can release capital from a mature asset and redeploy it into new infrastructure, but the economics depend on the price received, the revenues surrendered and what is done with the proceeds.

For investors, this means that infrastructure underwriting increasingly requires an understanding of the sovereign, regulatory and contractual framework behind the project's cash flows.

The question is no longer simply whether a project is 'public' or 'private.' It is which risks have actually moved, which remain with the state, and whether the public commitments supporting the cash flows remain credible over the life of the asset.

That distinction could matter considerably in energy. The IEA expects US\$3.4 trillion of energy investment in 2026. Mobilizing that capital is one challenge. Creating structures capable of absorbing it at acceptable risk-adjusted returns is another.

Public debt does not imply that governments will retreat from infrastructure. It may instead change the way they participate: less direct ownership in some cases, more concessions or asset recycling in others, and potentially greater reliance on regulation, contracts and risk-sharing mechanisms to mobilize private capital.

The more the world asks private capital to bridge the infrastructure gap, the more important it may become to understand the balance sheet standing behind the bridge.

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