DEVELOPMENT IMPACT:
MIGA RESPONDS TO GLOBAL ECONOMIC CRISIS

"The one certitude we can draw from events over the past year is our inability to predict what is to come, and how it may trigger other unexpected events. To address the challenges ahead requires a spirit of innovation backed by action. We need to be fast and flexible. We need to be devising solutions to problems that draw together the resources and skills of multiple partners—governments, international institutions, civil society, and the private sector."

World Bank Group President
Robert B. Zoellick

Challenging Times

This has been an extremely difficult year characterized by challenges and uncertainty throughout the world. Looking back, it was less than a year ago that the financial crisis emerged and quickly transcended national borders to include most, if not all, of the developed world. The optimistic predictions that emerging and developing countries might escape the tsunami proved false and the situation soon turned into a global economic crisis.

Even before the emergence of a full-blown financial crisis in September 2008, we saw significant signs of weakening global growth. The world economy has been severely damaged and we are seeing the hard-won gains in growth of the past years being unwound. Again, it has been the world's poorest people who have been hardest hit by the crisis, many of whom were already battered by the food and fuel crises earlier in the year.

Prospects for the Global Economy

What began as a financial crisis in the United States became one of the sharpest global economic contractions in modern history reaching out and affecting everyone. The World Bank's economists updated their 2009 Global Economic Prospects predictions at the end of March due to the fast-changing circumstances. Their prediction of a highly uncertain possibility for slight recovery in 2010 did not augur well for prospects of sustainable development.

Their updated data showed global GDP will contract by 1.7 percent in 2009, which would be the first decline in world output on record, with OECD economies likely to contract 3 percent and other high-income countries 2 percent. They predicted that GDP among developing economies will ease from 5.8 percent in 2008 to 2.2 percent in 2009.

Virtually no developing country, be it an emerging market country in Eastern Europe or one of the poorest or emerging countries in Africa, has escaped the impact of the crisis. The World Bank estimates the recent food and fuel crisis already pushed more than 100 million people back into poverty and that the current crisis puts an additional 55 to 90 million people at risk this year due to the global recession.

Impact on FDI

The impact on foreign direct investment (FDI) has been significant, and has far-reaching consequences not just for MIGA, but more importantly for the member countries we serve. Over the past several decades, FDI—the largest component of international capital flows to the developing world—has increased in relevance to become a major source of funding for many developing countries. Among

other benefits, FDI brings job creation. It helps create fiscal space that allows governments to use scarce budgets and development assistance for meeting other critical needs for their people that may not lend themselves to private participation, such as education and health care.

It is also widely understood that investments in infrastructure, in mining, and other capital intensive activities—all heavily dependent on FDI—can yield huge benefits. They lead to real economic growth and development in ways that go far beyond the immediate project, such as bringing in roads that provide local populations with access to markets, and supporting all sorts of small and medium-size enterprises (SMEs). Foreign investors also typically bring in global knowledge and best practices that help develop domestic capacity.

Unfortunately though, here too the crisis has had a severe impact, and FDI levels this year have been sharply lower due to tighter liquidity in the developed countries and weaker growth prospects in developing countries. The World Bank estimates that FDI to developing countries will decline by some 30 percent to approximately $385 billion—down from an estimated $583 billion in 2008 and $520 billion in 2007.

The World Bank Group Response

Against this background, World Bank Group President Robert B. Zoellick has urged leaders around the world to define multilateral solutions to the global crisis. The World Bank Group, as well as other international financial institutions and other entities, has been working to lay the groundwork for a sustainable recovery and growth. We believe that, with shrinking access to private capital, everyone must play a larger role in channeling more resources to developing countries and helping countries to pursue their own policies on how to better manage and protect their resources.

As a group we are using all our resources, including financing, hedging products and guarantees, knowledge services, and partnerships to mobilize rapid assistance. The organization's commitment to client needs and innovative, flexible and rapid response is underscored by some very specific initiatives and scaled-up resources to assist countries hit by the crisis.

In this regard, the World Bank, MIGA, and IFC play complementary roles in facilitating growth and attracting private capital into the world's transitioning and developing countries.

MIGA's Response

In particular, MIGA's guarantees encourage responsible and sustainable FDI, which promotes growth, creates jobs, injects liquidity into markets, and improves the lives of people in developing countries. As we continue to move forward through this crisis, MIGA is proactively enhancing its operations and flexibility to help would-be sponsors of projects in developing countries better mitigate their risks, so that investment opportunities become more attractive and more good projects get done.

MIGA initiated some specific responses during the course of the year. With global financial pressures deepening, we announced a broadened initiative to support financial flows from banks to their subsidiaries in countries that have been hit by the global financial crisis. MIGA's guarantee support plays a critical role in enabling cross-border flows from financial institutions into their subsidiaries, at levels necessary to allow adequate capitalization and/or liquidity of these subsidiaries, especially during this turbulent time.

Under the initiative, we will be able to provide such guarantee support globally, of which up to $3 billion will be available for investments into the heavily affected economies of Europe and Central Asia. This follows and builds on the commitment made by MIGA in February this year, when we joined the World Bank and IFC, the EBRD, and EIB to design a coordinated initiative to help stabilize the financial sector in that region. We believe coordinated action among the financial institutions, governments across Europe and the European institutions will help the financial sector in the region emerge robustly from the current crisis.

In parallel, MIGA continues to actively establish framework and contractual arrangements with other financial institutions in order to create mechanisms that will allow rapid response to institutions in great need and channel liquidity to investors. In this regard, we entered into an innovative contract with the African Development Corporation (ADC) to develop a product that will facilitate private equity capital for new investments in sub-Saharan Africa. This is particularly important in an environment where investor confidence is lacking, and is highlighted later in this report.

In order to maximize the insurance capacity that MIGA can bring to a project, we are working closely with our private and public sector reinsurance partners. By "fronting" transactions, MIGA has provided access to insurance capacity that otherwise would not have been available to clients and host countries. MIGA's current ability to mobilize capacity is the result of long-term reinsurance relationships. For over a decade, we have been reinsuring projects with a panel of private and public sector insurers, forming relationships that now underpin our syndication ability. In addition, MIGA also cooperates with national entities of member countries, such as export credit agencies. Our reinsurance backing helps free up their capacity to facilitate further investments.

We also took steps this past year to enhance our product offerings and flexibility. In this regard, MIGA's Board approved a number of changes to our Operational Regulations that will

improve overall effectiveness. We will continue to look at smarter and better ways to serve our clients, especially given the challenges of today's environment and the vital need to restore the flow of productive capital.

MIGA's Business

We understand that we are living through a very difficult period, and that our clients, as well as our member country shareholders, are experiencing major challenges. In terms of our own business, which is highlighted in the "Operational Overview" of this report, we have seen our pipeline of upcoming projects significantly and adversely affected: many deals that we are looking to support are experiencing significant delays, being placed on hold, or being cancelled altogether, especially those that are relying on debt financing.

However, to the extent that projects are still moving forward—or for those being planned for once the markets ease up a bit—we have experienced a renewed emphasis on better managing risks of all types, whether they be commercial or political. We have also noticed that the rate of cancellations of our coverage has dropped dramatically year-on-year. It is not unusual for clients to cancel Political Risk Insurance (PRI) coverage after a few years, once a project is up and running and the sponsors are feeling more familiar with their local operating environment. The fact that this past fiscal year saw very little cancelling of in-place coverage sharply underscores the far more conservative approach to risk management by our existing guarantee holders.

Priority Commitments to the Developing World

The vision of the World Bank Group, which we share, is to contribute to an inclusive and sustainable globalization to overcome poverty, enhance growth with care for the environment, and create individual opportunity and hope. The agenda to meet the challenges faced by developing countries laid out by President Zoellick two years ago still holds true today, especially as countries try to cope with the challenges of the economic crisis that has had an impact on everyone.

As a group we have a role to play, particularly when it comes to six strategic priorities: the poorest countries, fragile and conflict-affected states, middle-income countries, global public goods, and the Arab world. Overarching these priorities is the Bank Group's ability to harness extensive knowledge and expertise to support its development work. Especially in today's climate, poor and middle-income countries alike need help to limit the damage caused by the economic crisis and prepare for recovery.

Over the last year, MIGA's focus was on supporting the Bank Group's immediate response to the financial crisis, while also providing its own unique set of tools and solutions to support the goal of inclusive and sustainable globalization. The six strategic areas are in line with our own operational priorities of supporting investments in the world's poorest countries, conflict-affected countries, complex infrastructure projects, and South-South projects (investment between developing countries).

Making a Difference

Many of the projects MIGA supported during the fiscal year are common to or cut across several of the strategic themes outlined above. Our experience on the ground in all regions of the globe confirmed what we heard from project sponsors and what we read in the headlines. Despite the fall-off in FDI, developing countries continued to rely on private sector investment to support their economic growth. But with liquidity drying up, the risk appetite of international investors for projects in emerging economies was tested. Even in this difficult climate, MIGA was able to play a critical role in helping these economies grow by supporting projects and initiatives that focused on improving liquidity, especially for SMEs, generating jobs and building essential infrastructure, allowing governments to focus funds on urgent social needs.

Regional Impact

Asia and the Pacific

MIGA has provided political risk insurance for a wide range of projects in this region that offers opportunities for foreign investors. To date, we have issued nearly $2.0 billion in guarantees for more than 90 projects, from support for microfinance in Afghanistan to the construction of a comprehensive solid waste treatment center in China. Though the region was initially less affected by the financial crisis, it has suffered due to the high export and FDI dependence of many of the countries which has left them vulnerable.

For example, MIGA has been active in the financial sector in Pakistan. The sector faces many challenges, including low banking penetration and limited access to finance, especially where SMEs and rural communities are concerned. To continue to assist underserved yet productive segments of the economy, we issued guarantees last year totaling $1.8 million for the establishment of the Kashf Microfinance Bank in conjunction with the Kashf Foundation, a foundation which uses group lending to provide finance to micro and small business owners, especially women, in regions across the country.

We know from experience that greater access to financial services helps reduce poverty and expand economic opportunity for low-income populations. Our support in establishing a for-profit, national, and fully regulated microfinance bank will help encourage new entrants and greater overall penetration to meet the vast need for financial services for Pakistan's poor.

We are also supporting progress in infrastructure and the environment in southwest China, where fast urbanization and industrial growth have led to severe wastewater issues. We supported a wastewater treatment project in Chongqing municipality which we anticipate will promote improved water quality as well as better environmental practices in a region that has lagged behind in attracting FDI.

MIGA's guarantees encourage responsible and sustainable FDI, which promotes growth, creates jobs, injects liquidity into markets, and improves the lives of people in developing countries.

Europe and Central Asia

The financial crisis has hit the countries in this region particularly hard, as mentioned earlier in this report, because of their integration into European financial markets. This resulted in the region being more vulnerable as the recession worsened and capital flows all but came to a halt. To assist in restoring liquidity, nearly all of MIGA's support to the region in fiscal 2009 went to financial sector projects. Going forward, we intend to continue to assist the financial sector in affected countries to meet their pressing capital and liquidity needs. (See Box 1)

Latin America and the Caribbean

Though this region has been affected by the financial crisis, particularly because of some country ties to the financial sector in the United States, we believe it will be an important part of investment portfolios and remain attractive to investors. In response to the crisis, MIGA joined the World Bank Group, the Inter-American Development Bank and the Inter-American Investment Corporation (IDB/IIC), Corporación Andina de Fomento (CAF), the Caribbean Development Bank (CBD), and the Central American Bank for Economic Integration (CABEI) in an initiative to help spur economic growth. The Bank Group's affiliates will provide $35.6 billion out of the total of $90 billion committed for the program.

We are pleased with the progress in some of the projects we have already supported, particularly in infrastructure. (See Box 2) Since inception, MIGA has issued $7 billion in guarantees for more than 160 projects in Latin America and the Caribbean, covering all sectors and spanning 20 countries.

In fiscal year 2009, we provided $34 million in guarantees, with the bulk going to an infrastructure project in Brazil that will support the construction, operation, and maintenance of new power lines along the north-south axis of the country. This project is expected to help alleviate the imbalance of electricity supply and demand caused by the geographic distance and climate difference across regions. At the same time, a more consistent energy source will help ensure that Brazil continues on a path of economic growth.

We also issued a guarantee for a microfinance project in Uruguay to support small business and help bring banking services to underserved communities. The country's existing financial infrastructure is dominated by large banks and does not meet the needs of some of the most vulnerable groups. The project, through support for small entrepreneurs, should help generate employment, improve living standards, and may encourage new entrants to Uruguay's microfinance market.

Middle East and North Africa

This region has been less severely affected by the global financial crisis hitting the banking sector in many regions, but the impact is still unfolding in the real economy. Over two decades, MIGA has issued nearly $1 billion in guarantees for 19 projects in 11 countries, covering investments in general banking, manufacturing, sanitation services, sewage systems, oil and gas, telecommunications, and tourism.

MIGA has also issued $886 million in guarantees to locally-based companies and banks investing in developing countries outside the region, in keeping with our commitment to support South-South investments. In 2009, we worked on underwriting a number of such projects, but they were delayed due to the global financial crisis.

Last October we welcomed Iraq as a new member. We participated in a fact-finding trip to the country in April 2009 aimed at getting a better understanding of the development needs and investment opportunities and to underscore World Bank Group commitment to assisting Iraq in its sustainable economic recovery. We are also exploring other ways in which MIGA can help facilitate sound and productive investment into Iraq outside of the agency's guarantee program.

Also last year, the World Bank Group officially re-launched a trust fund, administered by MIGA and co-sponsored by the EIB, the Government of Japan, and the Palestinian Authority. The fund is aimed at encouraging investment in the West Bank and Gaza and was expanded in fiscal year 2009 to offer coverage to local as well as foreign investors.

We also entered into discussions with the Dubai International Financial Center (DIFC) to identify a partnership arrangement that will work towards facilitating the development of regional securities markets. MIGA's

Financial Crisis and Support to Banks in Europe

As a result of the global financial crisis, banks in emerging economies faced the challenges of ebbing global liquidity and free-falling stock markets. We responded in a number of ways aimed at helping banks to sustain and expand their lending operations.

The perception of commercial and non-commercial risk in the Europe and Central Asia (ECA) region increased as a result of the economic crisis. To help address the challenges, the largest multilateral investors and lenders in the region—the EBRD, the EIB Group, and the World Bank Group—agreed to provide up to €24.5 billion ($31 billion) to support the banking sector in the region and to fund lending to businesses. The financial support includes equity and debt finance, credit lines, and political risk insurance. Within this package MIGA will provide political risk insurance capacity of up to $3 billion to help the banking sector meet its pressing capital and liquidity needs and back financing from parent banks.

The international investor/lender initiative complements and supports national crisis responses: it will deploy rapid, large-scale, and coordinated financial assistance from the international financial institutions to support lending to the real economy through private banking groups, in particular to SMEs.

In fiscal year 2009 MIGA issued 12 guarantees totaling $1.2 billion for ten projects in the financial sector in ECA.

Financial Sector Investments Supported in ECA in FY09

Host Country	Investor Country	Project Name	Guarantee Amount ($M)
Bosnia and Herzegovina	Austria	Raiffeisen Leasing d.o.o. Sarajevo	47.7
Hungary	Austria	UniCredit Bank Hungary Zrt.	133.8
Kazakhstan	Austria	ATF Bank, Kazakhstan	190.0
Latvia	Austria	AS "UniCredit Bank"	100.3
Moldova	Romania	I.C.S. Raiffeisen Leasing Moldova (RLMD)	6.2
Russian Federation	Austria	Closed Joint Stock Company UniCredit Bank Russia	90.3
Russian Federation	Belgium	Absolut Bank Russia	120.0
Serbia	Austria	UniCredit Bank Serbia JSC	134.2
Ukraine	Austria	Joint Stock Commercial Bank for Social Development Ukrsotsbank	247.0
Ukraine	Austria	Raiffeisen Leasing Aval LLC	142.5

demonstrated flexibility will enable us to tailor our products and provide coverage under both traditional finance as well as Islamic finance guidelines.

Sub-Saharan Africa

Africa continues to be one of our strategic priorities, especially as the financial crisis threatens to undo so many of the continent's recent gains. Since its inception, MIGA has issued nearly $2.6 billion in guarantees for investments in Africa, supporting over 100 projects in 29 countries. MIGA's support for projects on the continent also underscores our commitment to the poorest countries as well as our capacity to assist countries emerging from conflict and fragile states.

During the past year MIGA supported a number of projects in the region, from assisting the financial sector to agribusiness and tourism. Most of these projects were underwritten through the Small Investment Program. However, project size is not always an indicator of development impact, particularly in Africa where small investments can provide far-reaching spin-off effects that create jobs and spur economic growth. Here we highlight a few of these projects, all of which are discussed in more detail within our Regional Activities section.

One of the initiatives already mentioned is an innovative contract signed with ADC, a business development company capitalized by German investors, to facilitate up to $100 million of investments to SMEs in sub-Saharan Africa. As part of our ongoing response to the global financial crisis, this contract provides a blanket commitment of guarantee capacity and will help ADC raise risk capital at a critical juncture of limited global access to funds and slowdown in investment activity. We expect that this guarantee structure will be replicated for other similar funds or investors seeking to attract capital in today's difficult financial environment.

The first two ADC projects supported were in Rwanda, where fostering broad-based growth in economic activity and in the private sector is key to the country's continuing economic recovery. Both projects are expected to have a positive impact, especially at this critical time of financial turmoil, by injecting liquidity into the country's banking system.

We also issued a guarantee of $4.3 million for an agribusiness project involving the installation and operation of a vegetable oil refinery in Boma, a port town in the Democratic Republic of Congo. This project is expected to have a positive impact on the country's economy by creating jobs for the local population, generating significant annual tax revenues for the government, and leading to local procurement of goods and services.

Another key area of MIGA's work in the region is the agency's Environmental and Social Fund for Africa. Funded by a grant from the Government of Japan, it enables MIGA to provide technical assistance to existing and prospective projects in Africa to improve their environmental and social performance. Several of the Trust Fund supported activities that began in fiscal year 2008 achieved results this fiscal year. For example, an agribusiness project in Uganda completed a successful audit of environment, health, and safety management for ISO 14001 certification and a mining company in Mozambique completed and is implementing its malaria-prevention action plan. The fund also supported the development of a toolkit for implementing the Voluntary Principles on Security and Human Rights for major project sites. The toolkit was launched in fiscal year 2009 and received very good feedback from investors.

The Trust Fund is also collaborating with wider World Bank Group initiatives to provide additional training to support implementation and monitoring of a resettlement and livelihood restoration action plan within the oil and gas sector.

Initiatives in Knowledge and Learning

The World Bank Group views knowledge as the key to development effectiveness and the driver for a successful development institution. One of the group's biggest assets is its cumulative "brain trust" of development expertise and on-the-ground experience. MIGA continues to be at the forefront of gathering and sharing knowledge among the broader insurance and investment communities on political risk and foreign direct investment. This fiscal year, we again sponsored with Georgetown University the biannual symposium on international political risk management that has established itself as a leading forum for cutting-edge assessments of needs and capabilities within the industry.

MIGA has also been delivering high-quality information to the international investor community through its free online information services—FDI.net and PRI-Center. We are now intending to go a step further. In December 2009 we plan to launch our new report on world investment and political risk that will bring together experts in the field to analyze trends and conditions and provide an outlook on risk perceptions. We expect this report to become MIGA's annual flagship publication and a leading source of knowledge and information for our clients and the global investment community.

Toll Road Paves the Way in Costa Rica

The Latin America and Caribbean region has registered strong economic growth in recent years—but the global financial crisis has exacted a heavy cost. Even before the crisis, infrastructure spending by countries in the region had fallen sharply. In Costa Rica, outmoded infrastructure has impeded growth. The country needs to spend an average of $75 million annually in road maintenance alone.

A MIGA-supported toll road corridor between the capital San José and the port of Caldera on the Pacific Ocean could help to change that in a number of ways. The tolls paid will be used for ongoing road maintenance to ensure top-quality condition of the road, allowing the government to redirect scarce public resources elsewhere. Added to that is a psychological impact that comes when people see development, a feeling of being on the move towards economic growth. And with growing demand comes opportunity and the potential for improved livelihoods.

In this 2008 project, MIGA's guarantees of $158.5 million are covering an equity investment by FCC Construcción S.A. and Itinere Infraestructura S.A., and a loan by Caja Madrid. The partners associated with the project say it was MIGA's participation that helped negotiations between the government, the concessionaire, and the local councils achieve the first public-private partnership project in the country. According to David Gutierrez, a partner of BLP Abogados, the local law firm that represented Caja Madrid: "Everyone wanted the road and the partnership, but MIGA's contribution was critical to make it happen. It provided a degree of comfort and continues to do so, especially considering what has happened with financial markets."

Nonetheless, a complex infrastructure project can also face challenges, especially when it comes to people and their potential resettlement. In this project, according to all parties involved, MIGA's social and environmental safeguard practices helped create a new and innovative model for future infrastructure projects.

The new toll road will connect the industrial and business heartland of the country to one of the main ports and will provide easier access to the capital city. It is expected to ease transportation costs by reducing travel time by 1.5 hours for those who travel the full length of the corridor. The new road will lessen the costs associated with heavy traffic conditions, such as gasoline consumption and deterioration of vehicle parts and tires. By providing easier access to the port of Caldera, the investment will help improve the country's trade competitiveness and may reduce the price of imports.

The project is aligned with the government's own strategy, in partnership with the World Bank Group, of supporting, rehabilitating, and maintaining key trade corridors. It is also an important priority for MIGA given the estimated need for $230 billion a year for new infrastructure investment to deal with rapidly growing urban centers and underserved rural populations in developing countries.

Box 2