



**Independent Evaluation Group-MIGA
2008 Annual Report**

Evaluating MIGA's FY05-08 Strategic Directions

April 15, 2008

Abbreviations and Acronyms

ABS	Asset-backed security
AMS	Agribusiness, manufacturing, and services
AR	Annual Report
ARDE	Annual Report on Development Effectiveness (IFC)
BU	Berne Union
CAS	Country Assistance Strategy
CODE	Committee on Development Effectiveness
CRM	Customer relationship management
EA	Environmental assessment
ECA	Europe and Central Asia
EHS	Environmental, health & safety
EIA	Environmental impact assessment
EMS	Environmental management systems
EROIC	Economic return on invested capital
ERR	Economic rate of return
FDI	Foreign direct investment
FIAS	Foreign Investment Advisory Service
FRR	Financial rate of return
FY	Fiscal year
GDP	Gross Domestic Product
HR	Human Resources
IBRD	International Bank for Reconstruction and Development
IDA	International Development Association
IDS	Information Dissemination Services
IEG-MIGA	Independent Evaluation Group – MIGA
IFC	International Finance Corporation
LAC	Latin America & the Caribbean
M&E	Monitoring and evaluation
MBS	Mortgage-backed securities
MENA	Middle East and North Africa
MIGA	Multilateral Investment Guarantee Agency
OPIC	Overseas Private Investment Corporation
PFG	Project Finance and Guarantee (WB)
PPP	Public-Private Partnership
PRI	Political risk insurance
PwC	PricewaterhouseCoopers
RDE	2004 Review of Development Effectiveness in MIGA (OEU)
RM	Resource management
ROC/ROOC	Return on operating capital
ROE	2003 Report on Operations Evaluation in MIGA (OEU)
SIP	Small Investment Program
SME	Small and medium-sized enterprise
SMI	Small and medium-sized investor
TA	Technical Assistance
TRS	Time Recording System
WB	World Bank
WBG	World Bank Group
XPSR	Expanded Project Supervision Report

Acknowledgments

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Executive Summary

MIGA is at an important juncture as it reviews its role and strategy. The past five years have seen foreign capital flows to developing countries soar to record highs. The distribution of these flows, however, has been highly concentrated, and political risk has been a factor in determining these flows. Global demand for political risk insurance - an important instrument to mitigate the aversion to investing in difficult settings - has also increased significantly since 2002. Much of this increase has been met by private insurers and national insurance agencies, while MIGA's market share has declined.

This IEG-MIGA 2008 Annual Report evaluates key aspects of MIGA's FY05-08 Strategic Directions. This was the Agency's first comprehensive strategic exercise, and it emphasized MIGA's development mandate and collaboration with other parts of the World Bank Group (WBG). Yet the strategy document had structural weaknesses, with links missing between different strategic levels. During implementation, MIGA began project level consultation with the World Bank to ensure the consistency of its projects, put in place improved policies and analytics, and has also shown considerable support for innovative projects. But IEG notes lack of progress in important areas such as general product innovation, systematic business development, and performance monitoring.

The ultimate test of a strategy lies in results. MIGA's operational results during FY05-08 have shown a steady increase in new business from the nadir of FY04, even though, except for FY08, it was short of the business targets in the strategy. The Agency has supported projects in the priority areas identified in the strategy. MIGA's ability to insure complex projects in difficult markets continues to be a key strength. The crucial challenge will be to adopt a more integrated vision and strategy, and to develop products to better serve clients, while strengthening processes and performance metrics.

The 2005 Strategy

The FY05-08 strategy integrated business, development impact, and risk management aspects. The strategy had important gaps in linking MIGA's objectives (development, risk, and growth) and operational priorities at the client, internal process, and human capital levels. The operational priorities were aligned with WBG priorities and mainly reflected MIGA's internal strengths and continuity with previous priorities. Implications for MIGA's financial situation, risk profile, and development impact were not made clear. Similarly, although MIGA identified resource needs to implement the strategy, it has not been clear how these resources would be allocated to achieve performance outcomes and how these outcomes would link to the organization's macro level performance objectives. The strategy also had a significant gap in the area

of performance metrics that would allow monitoring and evaluation of achievement of objectives.

Strategy Implementation

Limitations of a strategic framework can be corrected by strong and adaptive implementation. In this respect, MIGA has emphasized several aspects during the implementation of its strategy. In a significant departure from past practice, it has changed its business model to better align its operations with Bank Group strategies and policies, and has in this regard scaled up consultations and collaboration at the project level with the World Bank. Increased coordination and collaboration with the WBG, while an important and positive aspect of MIGA's effectiveness as an insurance agency valued by clients, has

entailed increased transaction costs for the Agency.

Decision making has been modified. MIGA has made progress in developing its methodology for assessing development impact, and in using this methodology in its project assessments, but this has not yet reached consistent application. The Agency has also harmonized its policy and performance standards on social and environmental sustainability with those of IFC: it is too early to assess the results of this shift.

Processing times for guarantees have increased, due at least in part to MIGA now undertaking more complex guarantee operations with longer gestation periods.

In addition, the Agency has improved its risk and finance analytics underpinning its decision making with respect to pricing, provisioning, reinsurance, and capital deployment. More work remains in this area—including the need to further refine MIGA's pricing vis-à-vis insurance market business cycles. Performance management, internal reporting, and monitoring continued to be weak during implementation. MIGA should build on its recent improvements in this regard and systematize its efforts.

MIGA's internal organization has become more aligned functionally. Some improvements have been made in client relationship management, but it is important to do much more to improve and clarify roles and responsibilities of individual staff in business origination, including a business development plan, performance incentives, and measures of effectiveness, and to systematize client relationship management.

The Agency has underwritten innovative projects within its limited product range. But, partly due to constraints in its Convention, MIGA has not been able to make progress in more general and systematic product development as envisioned in the Strategic Directions.

Adapting and developing its product would be vital for the Agency to serve its clients better.

MIGA requested additional resources to support implementation of the strategic directions. However, the connection between expected increases and planned business growth was not explicit and actual administrative costs remained flat during implementation.

Results

The 2005-08 Strategic Directions anticipated business growth targets and announced an increased focus on the four operational priority areas: frontier countries, conflict-afflicted countries, infrastructure, and south-south investments. MIGA has steadily increased its business volume from the very low level of FY04, but it has fallen short, until this fiscal year, of the annual business target range of \$1.6-\$1.8 billion. At the same time, the international political risk insurance industry has seen rapid growth—tripling in size since 2004— and consequently, MIGA's share in the market declined from 6 percent to 4 percent during 2004 and 2007. This in part reflects growth in business lines of PRI that MIGA cannot offer at present. The growth in MIGA's annual business volume has come from an increase in the average size of guarantees; during FY05-07, the number of projects supported annually by MIGA has declined compared with its level in FY00-04.

MIGA has supported projects in its operational priority areas and has increased the share of new business in Africa and in IDA countries (within the frontier country priority), with much continuity seen in patterns of its business volume in priority areas compared with the previous strategy period. Efforts were made to diversify the portfolio, which was highly concentrated in terms of regions and sectors in FY04-FY05, and MIGA achieved significant improvements during FY06-FY07. Yet,

more recent results indicate a return to a higher level of concentration.

MIGA has a strong capital base and an excellent claims record to date. However, its net premium income has declined and effective premium rates remain above industry averages. With net premium income declining since FY04, the ratio of administrative cost to net guarantee income has increased to 80 percent in FY07--up from 68 percent in FY04. Should this trend continue, it could raise concerns about financial sustainability. MIGA has been recovering administrative costs through its premium income. It has priced guarantees consistent with its pricing model, although larger projects were more likely to be under or overpriced relative to MIGA's model.

It is too early to assess the development outcomes of MIGA projects approved during the FY05-08 period. Quality at entry assessments suggest MIGA has strengthened several aspects of its work quality at entry.

The Agency retains strengths due to its ability to underwrite complex projects in difficult markets, and there is room for it to grow. However, MIGA faces challenges in its business environment due to a proliferation of risk mitigation instruments and thus, its regulations, product, and processes need updating. The Agency can also strengthen its responsiveness to clients and its client relationship management. The challenge is to take advantage of growing demand for risk mitigation instruments and find solutions to address institutional constraints.

MIGA's support in some evaluated projects was crucial for investments to go forward. It has provided comfort to investors dealing with local communities and those entering a new country. The Agency's role has been especially important for investments in post conflict countries. The Agency has the potential to play an important development role.

Recommendations

In order to i) fortify its long term viability; ii) ensure the sustainability of recent operational results; and iii) strengthen its development results, MIGA needs to:

1. On MIGA's long-term viability:

a) Develop a new strategic directions framework that carefully considers the external and internal context in which MIGA is involved, the proposed performance dimensions and the linkages between the latter, the expected value to its customers, the necessary changes in internal processes, and the human capital and technological demands of the strategy.

Aspects to be considered include: the potential demand and appetite for risk mitigation products, the agency's market position vis-à-vis other providers of political risk mitigation tools, the changing international market conditions, the effectiveness of delivering guarantee instruments and potential synergies across the World Bank Group, remedies to address institutional and external restrictions imposed by MIGA's Convention, its competitive advantage, potential areas of growth and high development impact, and factors affecting the achievement of the objectives of the FY05-08 strategy. It would need to address the weaknesses of the current strategy by linking objectives, resource allocation, processes, and expected development results.

As part of this strategic exercise MIGA management would need to consider:

- Tackling the issue of administrative costs, as reflected by the increasing ratio of administrative costs to net premium income;
- Improving the effectiveness of its business development and client relationship functions; and

- Continuing enhancing the value added and the efficiency of business processes and decision making to ensure impact and cost-efficiency in underwriting.

b) Ensure that the new strategic directions make explicit the link between risk levels, pricing, and financial, operational, and development impact objectives. The strategy should include a portfolio perspective that would consider net guarantee income across risk, financial performance, and development objectives to facilitate decision making and performance monitoring of indicators such as expected income, costs, risk, and development impact. Similarly, MIGA should obtain more accurate unit cost data for underwriting individual guarantees. Finally, it should clarify further its pricing relative to market pricing throughout the insurance business cycle.

c) Ensure that the new strategy identifies the set of performance indicators to track progress in implementation. The strategic exercise needs to include the development of a framework of strategy metrics as well as the further improvements in internal systems for performance measurement, reporting, and monitoring.

2. On sustainability of MIGA's recent growth:

a) Strengthen systematic support to innovative projects and improve product innovation and internal processes to meet investors' changing risk mitigation needs. The Agency needs to strengthen innovation through systematic support to innovative projects and for new product development and innovation. It should address changes to its eligibility requirements not demanding amendments to the Convention. In the medium term, ensuring MIGA's innovation capability, vital for its relevance and sustainability, may require changes to the Convention.

b) Build on recent developments to improve tracking and management of progress during implementation. MIGA should systematize its recent efforts to develop metrics to monitor progress for improving management decision making, allocating resources to the desired areas of growth and impact and communicating results to the Board and other stakeholders.

3. On strengthening development results:

Make significant progress in implementing initiatives related to development impact assessment and monitoring, recommended in previous evaluations of the Agency by IEG, including the development of self-evaluation.

i) The test of a sounder strategic and implementation framework will be in the accomplishment of development results in supporting inclusive and environmentally sustainable growth. In this respect, to ensure that projects MIGA supports are economically sound and have positive and sustainable development impact, the consistent application of MIGA's development impact assessment guidelines is crucial: it will underscore the Agency's unique role.

ii) Likewise, the Agency should give high priority to continuing the steps it is initiating to implement a monitoring and self-evaluation system that would allow it to gauge, understand, manage, and report the development impact of its interventions.

1. INTRODUCTION

Background

1.1. The Independent Evaluation Group—MIGA (IEG-MIGA)¹ has prepared annual reports to the Committee on Development Effectiveness (CODE) and the Board of Directors since 2003, to update them on its evaluation findings about MIGA, and to present relevant information on issues critical to MIGA’s performance as a development institution and insurance agency. This 2008 Annual Report is IEG-MIGA’s first with a thematic focus. It evaluates some key aspects pertaining to the design, implementation, and results of MIGA’s three-year strategy (FY05-08).

1.2. The Multilateral Investment Guarantee Agency (MIGA) contributes to the mission of the World Bank Group by promoting foreign direct investment for the purpose of economic development in its developing member countries. MIGA fulfils its mandate mainly through offering political risk insurance to private investments in developing countries, complementing the services of private and public insurance agencies.

1.3. In 2005, MIGA proposed new strategic directions for the Agency for FY05-08 in order to enhance its insurance business and financial sustainability, strengthen the development effectiveness of its projects, and improve risk management. The purpose of this Annual Report is to present a forward-looking evaluation that will inform the formulation of MIGA’s new strategic directions for FY09-11.

Approach

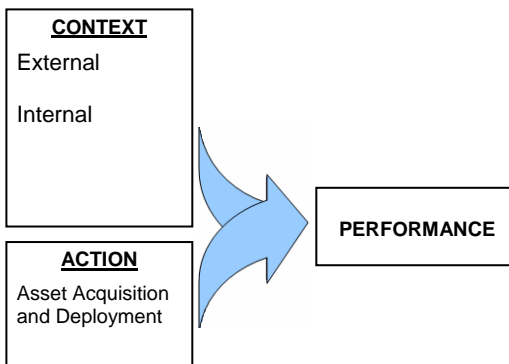
1.4. For its evaluation, IEG has drawn on analytical frameworks commonly used in strategic management.² The role of strategy is to guide the specific decisions an organization takes as it moves forward. Strategies do not generally involve particular actions, but rather define a framework for taking actions. In the framework presented in Figure 1, the ability of an organization to achieve its objectives (performance) depends on both the actions it takes and on the context in which these steps are taken.³

¹ IEG-MIGA is hereafter referred to as “IEG” unless the full acronym should be required by context.

² See Saloner, G., A. Shepard, and J. Podolny. *Strategic Management*. 2001. The links between performance and actions are examined using concepts developed in Kaplan, R., and D. Norton. *The Strategy-Focused Organization*. 2000, which described a balanced scorecard to measure the achievement of strategic objectives.

³ In this framework, the external context describes industry characteristics such as competitors, buyers, and non-market factors (e.g., the regulatory and political environment in which the organization operates), while internal factors refer to the assets and resources of an organization and the way in which it is organized. Actions the organization takes involve deploying and acquiring assets (such as knowledge, processes, organizational structure, and resources).

Figure 1: Strategic Management



Objectives and Scope

1.5. This Annual Report provides evaluative material to address key aspects of MIGA’s current strategy and the extent to which MIGA has been effective in implementing it and in achieving its strategic objectives over the FY05-07 period.⁴ The evaluation identifies issues and lessons relevant for MIGA going forward. Where appropriate, findings and recommendations are forward-looking and actionable to inform MIGA’s future strategy in the context of its changing business environment and the ongoing World Bank Group-wide strategy development. Using the framework noted above, the report assesses three main issues: (i) design, or strategy formulation, (ii) strategy implementation, and (iii) results MIGA has achieved so far from an operational and development perspective, identifying how results can be strengthened going forward.

Methodology

1.6. IEG has followed where possible an objectives-based approach, evaluating the relevance and implementation of the strategy using a strategic management framework. The effectiveness of implementation was assessed primarily against MIGA's indicators of progress identified in the 2005 Strategic Directions and supplemented by indicators from other relevant documents.

1.7. The evaluation has included a review of literature on the political risk industry and analyses of MIGA strategy, policy, and work program documents, and has drawn on structured IEG interviews with senior MIGA staff, as well as market studies and client surveys commissioned by MIGA in FY05 and FY08. Using data from MIGA Annual Reports and databases, the evaluation has analyzed characteristics of MIGA guarantees issued under the current strategic directions and of its overall guarantee portfolio to identify shifts during FY05-08, compared with the previous strategy period (FY00-04). The findings from this review have been complemented with material from existing and some new IEG project-level evaluations to identify issues and trends.

1.8. The assessment of aspects of MIGA's operational income, overall financial sustainability, and implementation of risk analytics tools was based on a review of financial statements, Board papers, other documents, an analysis of MIGA databases, and

⁴ While the focus is on MIGA operational results in FY05-07, available trend data and information from FY08 (up to March 31, 2008) have also been used where appropriate.

interviews with MIGA staff. Finally, the report draws on findings from previous or ongoing evaluations where appropriate, such as the parallel IEG evaluation of the use of WBG guarantee instruments.

1.9. The report is organized as follows: Section 2 describes MIGA's 2005 Strategic Directions, and Section 3 analyzes the way the strategy was designed. Section 4 presents key aspects of the implementation of the strategy, and Section 5 discusses findings on results so far from MIGA's operational and development perspective. Section 6 provides an outlook of MIGA's role and potential. A summary of findings and recommendations to MIGA management is contained in Section 7.

2. BACKGROUND: THE 2005 STRATEGIC DIRECTIONS

2.1. **The 2005 Strategic Directions were the first comprehensive strategy exercise since MIGA's inception.** Although the earlier MIGA 2000 Review proposed directions for the Agency, the 2005 document was the first to articulate a forward looking strategy and business model for the Agency with an integrated view on operational performance, development results, and risk management. The strategy also represented a first serious effort to thoroughly review MIGA's market environment, comparative advantage, and the Agency's strengths and weaknesses, in consultation with MIGA's partners and clients. It presented an important turning point for the Agency to move from an institution operating largely in isolation from the rest of the World Bank Group (WBG) to one that redefined MIGA first and foremost as a member of the WBG, emphasizing synergies, coordination, and collaboration with the Bank and IFC.

2.2. **The strategy defined MIGA as a development institution.** MIGA issued a mission statement in May 2004 defining the Agency as a development institution firmly grounded in the mandate of the World Bank Group by aiming "to support economic growth, reduce poverty, and improve people's lives."⁵ The statement further noted that MIGA was "committed to promoting projects with the greatest development impact, that are economically, environmentally, and socially sustainable."

2.3. **MIGA's 2004 business model reflected its development mandate, and emphasized marketing, risk management, and collaboration with the WBG.** In 2004, MIGA revised its business model both to emphasize its development mandate as laid out in the Convention and to address the significant decline in guarantees activities since FY02.⁶ This work culminated in the formulation of the MIGA 2005 Review for FY00-04 and Strategic Directions for FY05-08, which was discussed by CODE and the Budget Committee on March 16, 2005 and by the Board of Directors on May 10, 2005. The strategy confirmed a new business model with three elements: 1) proactive marketing and complementary product lines; 2) a comprehensive risk management framework; and 3) stepped-up collaboration with the WBG. Proactive marketing was part of the strategy especially in order to build a stronger and more diversified pipeline, thus giving MIGA a better chance to implement its strategic priorities by focusing on the sectors, regions, and themes where it saw a comparative advantage. Another related aspect of the business model was to remain more engaged with clients downstream.⁷

2.4. **At the core of the FY05-FY08 strategic directions were four operational priorities, which largely reflected underserved markets:** investment in infrastructure development, investment in frontier countries, investment in conflict-afflicted environments, and investment among developing countries ("south-south").⁸ In addition, the strategy identified sub-Saharan Africa as its most important regional priority and emphasized work in support of small and medium-sized enterprises. The strategy

⁵ MIGA. *Mission Statement*. May 2004.

⁶ IEG-MIGA. *Operations Evaluation Unit 2005 Report*. April 8, 2005. P. 3.

⁷ IEG-MIGA. *Operations Evaluation Unit 2005 Report*. April 8, 2005. P. 3.

⁸ A series of consultations and studies helped inform MIGA's FY05-FY08 strategy. Among these were a PRI Client Survey and a Technical Assistance Client Survey which provided some insight into the external environment and MIGA's comparative strengths and weaknesses.

document linked these priorities directly to expectations of increasing overall business volume and guarantees in the priority areas over the three-year strategy cycle, to a strengthening of MIGA's development mandate, and of its financial results. MIGA identified for each priority several planned results (including both outputs and outcomes in the results chain) with indicators of progress but did not identify specific targets for each of the priority areas. Selectively, these have served as benchmarks against which to evaluate implementation.

2.5. Among other outcomes, **MIGA's 2005 strategy document recognized the need to enhance the *quality* of its interventions as well as the *quantity* of foreign direct investment** it facilitates in order to stay relevant as a development institution. It expected to improve quality by an increased focus on development impact both at appraisal and project implementation, greater selectivity, and a clear demonstration of the value added of MIGA's involvement for the projects it supports. In particular, MIGA's strategic directions encompassed the following operational implications:

- MIGA would take the lead on non-commercial risk guarantees within the WGB in order to ensure its core competitive advantage and to avoid client confusion;
- Business volume would increase to between \$1.6-1.8 billion over the three year period (FY06-08), with further scaling up from expanded product offerings and closer alignment with the WB guarantees programs;
- The three elements of MIGA's new business model --proactive marketing, comprehensive risk management, and collaboration with the WBG-- would leverage its comparative advantages and reinforce each other;
- MIGA would focus on higher risk markets and other areas where it has a comparative advantage;
- Scaling up of business volume would need to be balanced with portfolio quality (development impact);
- MIGA would focus on projects that reinforce the agenda of the WBG, working with the Bank, investors, and governments to identify projects that would fit within the context of the CAS;
- MIGA Technical Assistance and other services would increasingly be part of tailored risk mitigation solutions;
- MIGA would pursue four operational priorities, based on MIGA's core competencies and comparative advantage (see Section 5);
- Initiatives in support of SMEs would be an integral part of the frontier strategy;
- In the infrastructure sector, MIGA would engage early in concessions processes and work upstream with clients to develop a pipeline;
- In frontier markets MIGA would apply its due diligence and effective risk management to encourage FDI;
- MIGA would continue efforts to mobilize investments with high demonstration effect in conflict-affected countries; and

- MIGA would market its products proactively to developing countries with a solid base of investors to increase south-south investments.

2.6. As MIGA now reviews its experience with its strategic directions and formulates new directions and operational priorities, this Annual Report seeks to provide evaluative feedback on the relevance and effectiveness of key aspects of the implementation of MIGA's strategic directions during the FY05-08 period. It also responds to a request from CODE members for IEG to conduct further work to contribute to the consideration of MIGA's future strategic directions.

3. ANALYZING THE DESIGN OF THE STRATEGY

3.1. This section seeks to assess key aspects of the 2005 strategy and its alignment with relevant World Bank Group strategies and with MIGA's market situation, comparative advantage, and resources. It reviews the extent to which the design reflected MIGA's internal and external environment; was conceptually complete (including objectives, resource and organizational requirements, and performance metrics); and provided a logical structure for achieving the strategy's objectives. It also addresses the evaluability of the strategy (the degree to which it contained monitorable actions and objectives).

Mapping MIGA's Strategy: An Analytical Framework

3.2. One approach to analyze the structure of strategies and describe relationships between overarching performance goals for the organization, its value proposition to its customers/stakeholders, and its internal initiatives and activities is to map the relationships among these strategic building blocks. IEG adopted Kaplan and Norton's approach for Strategy-Focused Organizations and Strategy Map⁹ and used it as a lens through which to view and help analyze MIGA's FY05-FY08 strategy. The approach is further described in Annex 1.

3.3. Such an analytical tool is useful (even if it was not applied during the initial strategy design) to identify systematically components and relationships in the logical structure of the FY05-FY08 strategy. Thus, this evaluation organizes the presentation of analysis according to four perspectives of strategy analysis identified by using this approach. These are (i) financial and development perspective, (ii) customer perspective, (iii) internal perspective, and (iv) human capital and resources perspective.

3.4. As indicated above, the 2005 Strategic Directions (described in more detail in Section 2) was MIGA's first comprehensive exercise to develop strategic directions and to firmly articulate the Agency's mission as a development institution. The strategy also emphasized MIGA's role as a member of the World Bank Group and its implications for increased alignment and collaboration among the institutions. The strategy was informed by analysis of the different aspects of MIGA's business environment and its operations. The remainder of this section examines the structure of the strategy in more detail according to each of the aforementioned perspectives.

Context

3.5. MIGA has a unique status within the WBG and among investment insurers alike in that it offers only one narrowly defined product: political risk insurance. This has a number of operational implications. First, it has to fully recover its costs and cover its risks from the guarantees it underwrites and does not have the ability to cross-subsidize one business line with revenues from another during a time of declining demand or price

⁹ Robert Kaplan & David Norton. *The Strategy-Focused Organization: How Balanced Scorecard Companies Thrive in the New Business Environment*. Harvard Business School Press, September 2000. The strategy map is a way to view the relationships between the four components of the traditional balanced scorecard.

for its insurance product (while national insurance agencies or private insurers typically offer a portfolio of financing or insurance products). Its administrative costs are also higher compared to many competitors due to costs associated with fulfilling its development mandate and complying with World Bank Group policies. Second, due to the nature of its business, MIGA's approach is necessarily largely reactive to market demand rather than proactive as can be the case for a financier. Third, MIGA's ability to offer products is constrained by its Convention and Operational Regulations, which make MIGA guarantees a more restrictive product than those offered by the World Bank and IFC.

A. Financial and Development Perspective

At the highest level, the strategy depicts MIGA's dual mandate as a development institution and as an insurance agency. MIGA's strategic directions emphasized the need to enhance its development impact and strengthen its financial sustainability.

3.6. In FY04, MIGA had faced challenges in its operating environment and performance. At the time of its strategy formulation, MIGA had been experiencing a substantial decline in guarantees issued from a high of \$2.0 billion in FY01 to \$1.08 billion in FY04. MIGA had also experienced an increase in cancellations,¹⁰ and return on operating capital (ROOC) had declined over the same period from 6.7 percent to 3.2 percent. Despite these challenges, MIGA's only explicit performance objective at this highest level of the strategy related to the growth of its business.

3.7. It is difficult to determine the assumptions underpinning MIGA's growth projections. The strategy indicated that MIGA would increase its business substantially from an average of \$1.27 billion in the three years preceding the strategy to between \$1.6 and \$1.8 billion in FY06 to FY08. The strategy also stated that if MIGA were able to expand its product offerings, it could further extend its business by up to 100 to 150 percent over its average performance during FY01-04 to a level of \$2.5-3.0 billion. The assumptions that resulted in these projections were not explicitly stated.

3.8. MIGA's four operational priorities appear to have been derived largely from internal (supply side) factors and provided continuity with MIGA's previous strategic objectives. The operational priorities were similar to and extended MIGA's priorities from its FY00 strategy and they reflected MIGA's access to capital, its development focus, and its relationship with the World Bank Group (WBG). They were also aligned with research showing that risks for projects in conflict areas favor public or multilateral providers, particularly for large or salient investments in a poor country, or projects across international boundaries.¹¹ MIGA's analysis of the external environment suggested a direct relationship between increased FDI flows and increased insurance demand, despite research showing a more complex relationship.¹² The strategy surmised

¹⁰ There is a management point of view that cancellations are a positive indicator.

¹¹ West, Gerald T. and Kristofer Hamel. P. 220.

¹² West, Gerald T. and Kristofer Hamel. "Whither the Political Risk Insurance Industry?" in *International Political Risk Management, Vol. 3: Looking to the Future*. World Bank Publications. June 30, 2005. P.

that projected increases in FDI flows would not be enough to harden market conditions for public insurers, but noted that the projected FDI flow increase was encouraging for the industry.

3.9. **MIGA’s capital is a significant resource that has been underutilized during the period under review.** MIGA’s strong capital base is consistently highlighted as one of MIGA’s strengths by clients and competitors. The decline in return on capital during FY00-04 and MIGA’s subsequent implementation of an economic capital model indicated that its capital was not fully deployed. MIGA’s FY05-08 strategy document stated that it was in the process of implementing an economic capital model in order to strengthen its ability to analyze and assess its balance sheet strength and deploy its capital on the basis of risk considerations (see paragraph 4.24 ff. on risk management), but it did not address how it would more effectively deploy its operating capital or improve its return on operating capital (ROOC).

B. Customer Perspective: MIGA’s Comparative Advantage and Operational Priorities

From this perspective, which refers to the components of MIGA’s customer value proposition that differentiates it from other providers, MIGA’s strategy defined a concentration on customer segments in high risk member countries with an emphasis on infrastructure development. The strategy defined some of the value proposition components for each customer segment by operational priority.

3.10. **MIGA’s definition of its core competencies and comparative advantage was informed by perceptions and feedback provided by market participants and consequently had a sound supply side view of its strengths in the global market.** MIGA’s FY05-FY08 strategy described its core competencies as understanding risk and providing protection; resolving disputes and leveraging World Bank Group relationships; financial strength; and integrated technical assistance. It identified its comparative advantage for its private sector clients as its deterrence effect, mediation abilities, certification effect (compliance with environmental and social best practices), financial strength, country knowledge, and lower borrowing costs. A recent study for MIGA on the PRI industry has confirmed that MIGA remains at the top of its peer group with respect to its reputation, knowledge and expertise, financial strength, environmental and social standards requirements, ability to pay claims, and capacity to resolve disputes.

3.11. **The analysis of the external environment to support the rationale for the operational priorities was useful but had some contradictions.** MIGA research had identified several demand side factors affecting the PRI industry such as an increasing reliance on self-insurance and commercial banks questioning the value of political risk insurance and preferring comprehensive insurance instead. Its analysis of the external environment also observed that its ‘deal flow’ had fallen for the second year in a row, market capacity was in oversupply, and the political risks market was continuing to

215. This study found that there is no direct relationship between FDI flows and demand for political risk insurance.

soften. However, its analysis did not reflect the fact that Berne Union had reported a surge of overall PRI business in 2004.¹³

3.12. The operational priorities could have been strengthened by defining complementarities, the relative size of the opportunities they presented and how the portfolio as a whole would be managed. It was not evident if MIGA expected to generate more of its business from infrastructure or from south-south investment. The strategy did not explicitly discuss whether MIGA wanted to pursue other business in addition to its operational priorities in order to support its financial viability and balance its portfolio. Given MIGA management's observations about the market conditions overall and the challenges of developing business inherent in some of the operational priorities, there was a gap in explicit analysis and rationale as to how MIGA expected to manage the complement of operational priorities and meet performance objectives (risk management, growth and development impact) for its portfolio.

C. Internal Perspective

The strategy describes internal capabilities and initiatives needed to deliver MIGA's customer value proposition, and consequently its financial and development impact performance. Thus, MIGA's strategy identified objectives and initiatives such as a better internal alignment, coordination and collaboration within the WBG, product development, improved marketing and business development, and improved risk management.

Internal Processes, Methods and Alignment

3.13. The 2005 Strategic Directions called for a number of changes in MIGA's internal processes and organization, including:

- Closer and more collaborative relationships with host countries to address constraints holding back foreign investment;
- A more proactive approach to marketing and business development involving investor targeting and deepening relationships with key clients, better understanding of investor business strategies, which require the development of new client relationship approaches and systems;
- Expanded MIGA product offerings to better meet the needs of the marketplace, including new tools such as trust funds for SME investors, and covering different types of investments such as stand-alone debt, existing investments, local investments, and portfolio treaty reinsurance for developing country insurance agencies;¹⁴

¹³ Berne Union. In the press release *Business Volumes Up 21 Percent to \$788 Billion For Berne Union Members—Record Year for Export Credit and Investment Insurers*. October 6, 2005.

¹⁴ MIGA noted that it was studying these areas and would revert to the Board with a proposed approach, including changes to the Convention.

- Institutionalized coordination between the Bank’s Project Finance Guarantees unit and MIGA to establish a complementary basis for management and deployment of the instruments;
- In the area of finance and risk management, implementation of the economic capital model to strengthen risk-based analyses, mitigate and hedge insurance portfolio risk (including a review of the reinsurance program), set risk-based portfolio management policies (country and project exposure limits), and manage MIGA’s assets;
- An improved underwriting process aimed at advancing the project selection process; and
- Creation of a coherent and integrated monitoring and evaluation system across the Agency.

The document did not explicitly refer to further organizational alignment within MIGA as a result of the strategy, in addition to the changes implemented as part of the new business model (see paragraph 4.9).

Alignment within the World Bank Group

3.14. **MIGA’s operational priorities aligned with the Bank’s anti-poverty strategy.** At the institutional level, MIGA’s FY05-FY08 strategy articulated the necessity of aligning with the World Bank/IDA and IFC. In particular, MIGA’s strategy aligned with the Bank’s focus on improving investment climates, which included a focus on revitalizing infrastructure and tackling risks and uncertainties affecting developing countries. Regionally, MIGA’s focus on Africa aligned with the Bank’s priorities for that region.¹⁵

3.15. MIGA’s FY05-FY08 strategy stated that MIGA would focus on projects and activities that supported the agenda of the WBG and that it would work closely with the Bank, investors, and host governments in a selected set of countries to identify projects and programs that would fit with country assistance strategies (CAS).

3.16. The strategy document also indicated that during the strategic review exercise, MIGA had considered whether it should remain a stand-alone entity or be incorporated into the World Bank or IFC. MIGA had concluded that it would remain independent and also noted that “. . . it is essential that the agency must find ways to work with the World Bank and the IFC in a more systematic and coordinated way, to realize the benefits that can be achieved through complementary activities, and that this commitment must come from the top management of each of the institutions.”¹⁶

Structure to Link Objectives, Outcomes, and Performance Metrics

3.17. **Some links and relationships between components of the strategy were not made explicit.** For example, MIGA could have linked the customer perspective (value proposition by operational priority) to the financial perspective to make clear which operational priorities MIGA expected would contribute more to its development mandate,

¹⁵ World Bank. *Annual Report 2005*. P. 32.

¹⁶ MIGA. *MIGA 2005 Review for FY00-04 and Strategic Directions for FY05-08*. May 10, 2005.

which was expected to drive growth and whether there was an additional, implicit priority to underwrite projects for portfolio risk management purposes. In this regard, MIGA would also have benefited from linking financial, growth, and developmental objectives.

3.18. **MIGA’s FY05-08 strategy had few explicit targets against which to measure achievement of its objectives, with the exception of a growth target for overall business volume and projections for operating income.** The strategy presented a broad range of activities and initiatives to address its business model, four operational priorities, and a focus on Sub-Saharan Africa. The business plan supporting the strategy provided some additional targets such as increasing the share of new business in infrastructure by 30-35 percent and building new business in the Africa region by 20-25 percent. IEG recognizes that setting such business targets will always imply uncertainties given the primarily demand-driven nature of much of MIGA’s guarantee business. However, difficulties do not imply impossibilities. The strategy had set some targets for overall business growth (see paragraph 5.3). The strategy’s approach of listing activities against the operational priorities did not provide insight into the outcomes expected from these activities such as how achievement in implementing activities would help the Agency reach its strategic objectives. Although the strategy outlined by fiscal year a list of planned actions, outcomes, and indicators, the relationships among them were not clear. Structuring a clear and direct relationship among actions, outcomes, and indicators would have better informed an understanding of the interdependencies and priorities among the activities that the strategy identified.

3.19. **Moreover, the strategy provided only partial indicators for the Agency’s performance.** With only a growth target and projections for operating income, it is difficult to determine the expected and realized contributions of actions to the Agency’s strategy. This also makes it difficult to consider where management could later have changed course if initiatives were implemented but the expected outcomes were not achieved.

Evaluability of the Strategy

3.20. The only apparent way to monitor the strategy’s implementation would have been against the overall growth targets (by volume of guarantees) and by the completion of initiatives. The strategy did not clearly define a prioritized or interdependent set of outcomes and indicators and did not make evident how resources were to be allocated. Therefore, it is difficult to clearly identify or address areas of strategic underperformance.

D. Human Capital and Resources Perspective

Concerning this perspective, MIGA would use its resources and enable delivery of the other components of the strategy, including capabilities and skills, staffing, and technology applications to support information tracking, analysis, and reporting. MIGA’s strategic directions document addressed some of these needs.

3.21. **The strategy contained little information or analysis to describe the resource requirements for each of the operational priorities and for ‘scaling up the business’, including for required staff capacity and capabilities.** From the strategy and its accompanying business plan and administrative budget, it was not clear how the budget

was allocated in order to yield which expected results, what were the ‘big ticket’ items, which activities were new investments or multi-year investments, and which allocations were dependent on or of higher priority than others. Similarly, as described in paragraphs 4.27 ff., the skills and staffing required to support delivery of the operational priorities were not evident.

Conclusions

3.22. MIGA’s 2005 Strategic Directions document was the first for the Agency to incorporate development, business, and risk management aspects. It stated objectives, priorities, and some of the resource requirements for achieving those objectives, but it lacked a complete logical structure that would allow an understanding of how overall objectives would be reached. The strategy did not connect effectively the two levels of the organization’s financial and development impact objectives to the operational priorities and subsequently to the many initiatives and activities identified. It did not adequately link achievement of individual activities and progress in priority areas to overall performance objectives. Doing so would have allowed a further focus on a clear and prioritized list of actions, outcomes and indicators for how to achieve its macro (financial and developmental) objectives. Similarly, although MIGA identified resource needs to implement the strategy, it was not evident how these would be allocated to support strategic priorities and actions such as business development or development of new products, how these would fulfill the organization’s operational priorities, and ultimately lead to its financial and development impact performance goals.

4. IMPLEMENTATION OF THE STRATEGY

4.1. This section assesses whether MIGA has been consistent in implementing the concepts proposed in its strategy from the customer, internal, and human capital perspectives or whether it adjusted the implementation process in response to gaps in the conceptual strategic framework or as a reaction to changes in the context. Implementation from the financial and development perspective is examined in section 5. Accordingly, this section focuses on changes in organization, resource allocation,¹⁷ skills mix, processes, and procedures, assessing whether they were consistent with and strengthened MIGA's ability to implement its strategic objectives, and whether MIGA's core functions were aligned with the strategy. This section also describes changes in risk analysis and risk management relative to MIGA's business objectives.

A. Customer Perspective

Product Development and Leadership

4.2. **MIGA has underwritten innovative projects and shown adaptability within its limited product range.** During the FY05-08 strategy period, MIGA has supported several innovative deals. In FY05, for example, MIGA issued guarantees to the first cross-border issuance of mortgage-backed securities, and supported two large cross-border projects. In FY06, MIGA provided coverage to its first carbon credit finance project and to a residential mortgage-backed securitization, the first such transactions in the host countries. The Agency also issued its first guarantee of an international private placement (bond issue) to support the financing of a toll-road project. In FY08, MIGA also issued its first guarantee for an Islamic financing facility to benefit a new container terminal. These projects involved guarantees covering multiple countries, difficult environmental or social issues, and the participation of other multilateral donors or insurance agencies.

4.3. **Despite considerable support to innovative projects, MIGA has made little progress on more general product development, which is constrained in part by its Convention and Operational Regulations.** MIGA's basic product range for PRI has not changed since its Convention was adopted in the mid-1980s, under very different conditions in the global financial markets. MIGA's Convention and Operational Regulations restrict the eligibility requirements and the types of risks MIGA is able to cover, which hinders its adaptability to new market trends. A PRI study commissioned by MIGA in 2005 noted that PRI providers were looking at a range of new products in response to changing market conditions. It outlined in particular that respondents had suggested a leadership role for MIGA in assessing the risk of sub-sovereign transactions, and solutions to address regulatory risk. Respondents also suggested new types of political risk for which there would be demand such as comprehensive non-payment coverage, sovereign non-honoring coverage, existing equity and acquisitions, and stand-

¹⁷ Resources are defined to include financial resources, human resources, know-how, processes, procedures, and organizational structure.

alone debt coverage. The 2005 strategy noted the limitations MIGA faced such as its inability to engage in certain types of transactions due to its Convention and indicated that new products could produce significant growth, but that the necessary studies would take some time. It outlined several options for new product offerings including a trust fund to provide matching funds to SME investors, coverage for stand-alone debt, coverage for existing investments, portfolio treaty reinsurance for developing country insurance providers, and coverage for local investors in joint ventures with foreign partners. In addition, the FY08 business plan reiterated the critical need for MIGA to remain relevant and the importance of product development in this regard, but its progress on developing and innovating its product has been limited over the current strategy period.

Client Relationship Management and Business Development

4.4. **MIGA has made some progress in its efforts to improve its client relationship management (CRM) but the role of and responsibility for business development is not clearly defined.** The FY05-FY08 strategy highlighted the need for improved client relationship management approaches and systems and described a number of activities to better understand and target investors as well as to implement a CRM system. In its FY08 business plan, MIGA stated its intentions to implement a more systematic process of identifying key investors in each sector, cultivating relationships to encourage repeat clients and attract potential key clients. Recent IEG discussions with staff indicated that the roles and responsibilities with respect to managing client relationships and engaging in business development activities continue to require improvement and could be more systematic.

4.5. **Staff also noted the absence of business development plans for underwriting sector teams to help improve planning and coordination, which would include objectives, responsibilities, and resources, and would allow MIGA to measure at the end of each period its effectiveness in business development and origination.** Similarly, there was an absence of performance incentives for individual staff to improve business origination and client responsiveness. MIGA has devoted some efforts and resources to improve its CRM function during the implementation period, and is undertaking a multi-year effort to upgrade its management information system, which is expected to become operational in FY09 and will include a database linking all aspects of CRM. But more efforts are needed in terms of assigning and clarifying responsibilities of individual staff for managing specific clients and key accounts.

Small Investment Program

4.6. **MIGA established a Small Investment Program (SIP) in FY06 to increase its business in the SME market and to streamline its procedures for small guarantees.** The program, with an initial per project coverage limit of US\$5 million, targets small and medium investors (SMIs) investing in SMEs, offering standardized terms at lower fixed premium rates and a streamlined underwriting process to make it more accessible to

small investors and cost efficient for MIGA. IEG evaluated in 2007 the implementation of this program.¹⁸

4.7. SIP projects reflected MIGA's operational priorities, but the program's implementation has had some shortcomings. Most projects were in the program's target sectors and regions, and in some cases, MIGA had played an important role by assisting the investor in structuring successfully the deal for the project. There were some inconsistencies between the program's stated objectives, the eligibility criteria, and the type of projects underwritten under the SIP. The streamlined process, which intended to reduce underwriting costs and the burden on small investors, also resulted in little documentation on project financial viability and the analysis of expected development impact.¹⁹

4.8. The results of the SIP and its projects have not yet been evaluated. In January 2008, the Board approved the expansion of the SIP program, increased the coverage limit to \$10 million, and clarified some eligibility criteria. Of the 15 projects that were provided coverage under SIP until December 2007, four had been cancelled after one or two years, a somewhat higher rate of cancellation than for regular MIGA projects--several of them due to the project not going forward or financial difficulties. The higher cancellation rate reflected the program's focus on high risk markets such as frontier and conflict-afflicted countries and also meant that those projects that were not implemented have had no measurable development impact.

B. Internal Perspective

Alignment of Core Business Functions within MIGA

4.9. To support implementation of the 2005 strategy, the internal organization has become more functionally aligned. In FY04 MIGA adopted a new business model and a flatter organizational structure. The number of departments was reduced from nine to six as was the number of senior managers. In FY04 an Economics and Policy Group was created along with the new role of Chief Economist. Country risk analysis, policy work, developmental assessments, and environmental and social analysis was centralized in this group. In FY04 MIGA's Online Services were moved to the External Outreach and Partnerships Department where marketing resided. Some initiatives to streamline the Agency did not increase synergies (see Box 1).

¹⁸ See *IEG – MIGA 2007 Annual Report*. The review focused on the design of the program and whether these first projects have met the original intent, objectives and eligibility requirements. It is not an evaluation of project or program outcomes since these projects are very recent and their development impact cannot yet be assessed. The assessment includes all 13 SIP projects underwritten since FY06 through the third quarter of FY07, corresponding to 20 contracts of guarantee, for a net exposure of US\$30 million.

¹⁹ IEG recommended that MIGA should tighten the SIP eligibility criteria to ensure that the program is fully focused on its intended clients—small investors and small and medium sized enterprises. IEG also recommended that the program should exclude projects with concessions as well as those in the infrastructure, oil, gas and mining sectors, and that MIGA strengthen the quality and documentation of the development impact analysis of SIP projects.

Operational Alignment with WBG

4.10. **Although MIGA selectively participates in joint Country Assistance Strategies (CASs) and Country Partnership Strategies, this may not be the most effective instrument of coordination for a small agency.** MIGA provides inputs in CASs based on whether the country is important in terms of MIGA exposure or there are issues with MIGA projects.²⁰ In its strategy, the Agency stated it would be playing an active role in the development of country assistance strategies (CASs), being proactively involved in analytical work and ongoing policy dialogues, and tailoring interventions to support and complement World Bank Group operational work. Given the agency's size and the nature and magnitude of MIGA's business in each country, and the Agency's size, providing inputs to the CAS may not be the most effective way of coordinating its operations with World Bank Group strategies. During the FY05-08 strategy period, MIGA has become much more proactive in consulting with Bank staff to ensure that the projects it underwrites are consistent with and support Bank priorities in the country or sector. This project level coordination approach may in fact be a more relevant way for MIGA to ensure alignment, reserving participation in the CAS process for those countries where MIGA's participation in the policy dialogue with the host country is considered essential.

4.11. **MIGA has changed its business model to ensure its operations align well with Bank strategies and policies.** The *IEG-MIGA 2004 Review of Development Effectiveness* found that at that time "guarantee projects fit MIGA's mandate and the host country's priorities for most of the cases, but could be better linked with the CASs."²¹ The *IEG-MIGA 2007 Annual Report*, which looked at new MIGA projects underwritten between January 1, 2005 and June 30, 2006,²² stated that "the projects are well aligned with country and WBG strategic priorities. In almost all cases, MIGA indicated how the project fit with the Country Assistance Strategy (CAS), and consulted with the Bank and IFC on macroeconomic and sector issues as needed."²³ With respect to middle income countries, IEG noted that, "Since 2004 MIGA has stepped up collaboration [with the World Bank] at all three levels [strategic, institutional and operational]."²⁴

4.12. **MIGA has implemented systematic project level coordination with the World Bank.** During the implementation of the FY05-FY08 strategy, MIGA began systematic consultations with the Bank on the projects for which MIGA is providing support. Although there are no formal mechanisms to structure these interactions, staff indicate that this coordination happens systematically as part of the regular course of work.²⁵ Staff describe these as working relationships with both the country teams and the Bank sector specialists. In practice, consultations on whether a MIGA project fits within the Bank program has clearly increased since 2004; MIGA also seeks and benefits

²⁰ Interviews with select MIGA staff. February 11, 2008.

²¹ IEG-MIGA. *2004 Review of Development Effectiveness in MIGA*. August 19, 2004. P. 2.

²² IEG-MIGA. *IEG-MIGA 2007 Annual Report*. June 18, 2007. P. 2. In this period there were 77 guarantee contracts underwritten for 46 guarantee projects.

²³ IEG-MIGA. *IEG-MIGA 2007 Annual Report*. June 18, 2007. P. 12.

²⁴ IEG-MIGA. *IEG-MIGA 2007 Annual Report*. June 18, 2007. P. 12.

²⁵ Interviews with select MIGA staff. February 11, 2008.

from the Bank's country, sector, and policy knowledge.²⁶ More systematic consultations between Bank country and sector departments have helped ensure that MIGA-supported projects are consistent with Bank Group strategies. All MIGA projects underwritten during FY06-07 were consistent with WBG country strategies or policies, based on a desk review/profiling of new MIGA projects. While coordination with the Bank is an important way for MIGA to manage risks and to leverage its relationship with the WBG in projects, this has come at a cost in terms of time spent by MIGA staff on completing a transaction.

Box 1: Realignment of MIGA's Technical Assistance (TA) Function

In 2004, MIGA merged the guarantees and TA departments into the Operations Group to capitalize on the potential synergies between TA and the guarantees function, although MIGA thought at the time that linkages between TA and guarantees were typically indirect. The Strategy did not articulate the expected benefits for the underwriting teams or MIGA's clients and partners from the realignment.

According to staff, in retrospect the integration of guarantees and TA failed because linkages between the two were quite weak in practice. TA helped MIGA's understanding of country dynamics particularly in Africa but did not work as well as was hoped in linking TA work and business development for MIGA guarantees.²⁷ Accordingly, in FY07 MIGA TA was integrated into the Foreign Investment Advisory Service (FIAS). The integration with FIAS, which had traditionally been working further upstream from MIGA TA but addressing similar investment-related issues, seems to be a step towards greater alignment of WBG entities offering complementary services, and a better fit for MIGA's TA services.

4.13. **However, the principles governing the relationship between IFC and MIGA products have not been clear.**²⁸ The relationship between MIGA and IFC has not always been free of friction. MIGA and IFC have been jointly involved in about 10 projects over the last 10 years. However, staff indicate that coordination and collaboration with IFC has not been at the level of interaction reached with the World Bank. This may be due to perceived competition between the products the two institutions offer. IFC has emphasized with clients and in justifying its role in projects the substitutability of the implicit risk cover of its lending and equity investment instruments with MIGA's political risk insurance.²⁹

4.14. **Infrastructure is one area of MIGA operations that was identified as an opportunity to align with and support the WBG's work.** According to IEG's project reviews, a significant share of the number of new MIGA projects (25 percent) underwritten in FY06 and FY07 involved partners, and all of these joint projects were undertaken in conjunction with either IBRD/IDA, or the IFC, or both. Five out of the 13 projects undertaken jointly were in infrastructure.

²⁶ Interviews with select MIGA staff. February 11, 2008.

²⁷ Interviews with select MIGA staff. February 11, 2008.

²⁸ IEG. *The World Bank Group Guarantee Instruments 1990-2007: An Independent Evaluation*. 2008. (Forthcoming)

²⁹ IEG found that in approximately 10 percent of IFC projects (FY05-07), implicit political risk cover was indicated as the primary reason for IFC's involvement (IEG. *The World Bank Group Guarantee Instruments 1990-2007: An Independent Evaluation*. 2008. (Forthcoming))

4.15. **A proposal to more closely align MIGA's PRI and the Bank's PRG instruments did not move forward.** In FY05 MIGA proposed the full integration of the Bank's Project Finance and Guarantee (PFG) Unit into MIGA. PFG was to continue to operate as a World Bank program, but administratively it was to be managed by MIGA. The supporting business plan provided detail about the anticipated benefits of the integration including optimal service delivery to private sector clients and government, enhanced coordination of product offerings, closing of potential product gaps, and creating an enhanced platform for knowledge sharing and innovation. The integration was to include co-locating PFG staff with MIGA underwriters. However, this proposal was initially delayed by changes in the Bank Group's senior management and the integration never materialized. Given the potential for overlaps in political risk mitigation products between the two institutions, such an approach could still be a viable proposal to strengthen product delivery across the WBG, but a subsequent World Bank reorganization resulting in the disbanding of the PFG unit may have made organizational integration more challenging. IEG's forthcoming evaluation of WBG guarantee instruments notes that while several Bank Group products offer political risk mitigation in some form, these were originally conceived as complementary. In practice, however, there have been overlaps and competition among WBG institutions in the delivery of political risk mitigation, driven by innovation and flexibility of policies, especially in IFC and the Bank. Competition for MIGA has come in particular from traditional and new non-guarantee products offered by IFC, which incorporate explicit or implicit risk cover.³⁰

Performance Management & Internal Reporting and Monitoring

4.16. **MIGA lacks an enterprise performance management approach to guide its management of resources relative to the implementation of the strategic plan, and is now beginning to address seriously its internal reporting gaps.** As far back as 2000 MIGA identified that it needed to improve its performance management and that it required technology systems and infrastructure to support this goal. One of the gaps where MIGA has made progress is addressing (through the use of Time Recording System) the lack of information on MIGA's unit cost of underwriting and managing a guarantee.³¹ The FY08 business plan states that for the agency to be efficient and effective it is crucial that it strengthen the links between resource allocation and work program deliverables. The plan states that MIGA will start using program budgeting methods in order to have the policies, procedures, systems, and necessary costing information in place. MIGA can build on recent efforts made in FY08 to systematize performance management and reporting going forward.

4.17. **Performance monitoring of MIGA projects has been consistently weak throughout the implementation period.** IEG's annual reports since 2004 have identified the need for MIGA to introduce monitoring in order to have a better understanding of whether MIGA's projects meet their development objectives. In its

³⁰ IEG. *The World Bank Group Guarantee Instruments 1990-2007: An Independent Evaluation*. 2008. (Forthcoming)

³¹ IEG-MIGA. *IEG – MIGA 2006 Annual Report*. May 31, 2006.

FY06 business plan MIGA indicated that it intended to develop an integrated monitoring and evaluation system across the agency. The IEG-MIGA 2007 Annual Report noted that MIGA's project monitoring framework to track project outcomes had made little progress in implementation and remained a challenge; no activities were highlighted to address project monitoring in the FY07 or FY08 business plans, and a monitoring framework is still lacking in MIGA.

Decision Making

4.18. **MIGA has modified its processes, but these changes have not significantly improved client perceptions of MIGA's service.** MIGA modified some underwriting and decision making processes in order to support implementation of its new business model and strategy. It introduced a Project Review Committee to provide guidance to underwriting teams early in the process, thus making underwriting more efficient. A PRI study that provided input into the FY05-FY08 strategy identified that among the areas MIGA could improve were its decision making and transaction processes, which were perceived as slow and requiring extensive documentation. MIGA simplified its contract of guarantee in 2004, and in 2005, MIGA approved new guarantee procedures to clarify the division of responsibilities among underwriting teams.³² A PRI study recently completed for the 2008 strategic planning exercise indicated that MIGA continues to be perceived as performing below its peer group in time needed to process applications and in customer service, and MIGA's internal business process review also highlighted the need to improve client responsiveness through more efficient processes, improved decision-making, and delegation of authority while ensuring accountability and quality control.

4.19. **Average processing times for MIGA's guarantee portfolio have increased during FY05-07.** MIGA's processing times vary widely between sectors and according to the type of project. Larger projects and those with more complex environmental and social issues require the longest processing times.³³ Processing times increased in all sectors in the period FY05-08 when compared with processing times in the period FY01-04. The growth in average processing times reflects in part MIGA's move into more complex projects, including those undertaken together with the World Bank, and other projects with longer gestation periods and requiring increased MIGA due diligence.

Development Impact Analysis

4.20. **The new business model helped to refocus the organization on its development impact.** In 2004 and 2005, MIGA shored up its capabilities in this regard by creating a new Economics and Policy Group and creating a Chief Economist position. It built up its team and developed sound guidelines for underwriters (December 2004), which reflected the Board-endorsed methodology, to assess development impact, and support this dimension of its critical 'quality at entry' process.

³² IEG-MIGA. *IEG – MIGA 2007 Annual Report*. June 18, 2007. P. 5.

³³ Measured from submission of a Definitive Application for a guarantee to the date when a guarantee contract became effective. In its Operational Regulations, MIGA is called upon to make prompt underwriting decisions, to be completed within 120 days from the receipt of a Definitive Application.

4.21. **MIGA adopted a sound methodology to assess development impact, and its implementation is improving.** In its 2007 Annual Report, IEG-MIGA found that MIGA's performance had improved since 2004 in rigorously applying its assessment methodology spelled out in its guidelines for new projects. However, its ability was still uneven to consistently analyze development issues. Out of 18 projects for which a cost-benefit analysis was applicable, only five complied with presenting a full analysis in the decision documents, including an analysis of potential economic costs, and the remainder demonstrated varying degrees of quality of analysis.³⁴

4.22. **Staff awareness on development impact is still limited.** The IEG report also found that a majority of staff preparing the decision documents were not fully familiar with all aspects of specific requirements for development impact analysis. Underwriters considered the guidelines more as a general framework and saw the cost-benefit analysis required by MIGA's own guidelines as optional.³⁵

Environmental and Social Standards

4.23. **MIGA has improved its performance in ensuring the application and monitoring of safeguards, and adopted in 2007 a new policy on social and environmental sustainability.** MIGA's attention to environmental and social standards has yielded more consistent results. Consistent with IEG recommendations to improve its performance in this regard, MIGA upgraded the role of environmental and social specialists by requiring site visits for all category A and most category B projects and issued a guideline to ensure their early involvement. MIGA has also recently (2007) adopted a new policy on social and environmental sustainability and performance standards, which are harmonized with those of IFC. In its 2007 Annual Report, IEG observed that 86 percent of all assessed projects (including SIP) adhered satisfactorily to MIGA's review procedures for addressing environmental and social issues at entry.³⁶ IEG highlighted that there were notable improvements in the way MIGA ensures that relevant specific safeguard policies are addressed, with the greatest improvement in social safeguard policies.³⁷

Risk Management Methods and Tools

4.24. **MIGA has supported its business model and operational priorities by developing and applying risk and finance methods to improve its decision making with respect to pricing, provisioning, reinsurance, and capital deployment.** MIGA implemented a new pricing methodology in FY04, which was amended in FY07. In FY05, it implemented an economic capital model to help management gain a better understanding on the deployment of capital on the basis of risk considerations and to achieve consistency with MIGA's cost/pricing methodologies and provisioning. This model continues to inform MIGA's risk-related approaches and the FY08 business plan highlighted MIGA's role in reporting on the exposure and capital consumption of

³⁴ IEG-MIGA. *IEG-MIGA 2007 Annual Report*. June 18, 2007. P. 14

³⁵ IEG-MIGA. *IEG-MIGA 2007 Annual Report*. June 18, 2007. P. 16.

³⁶ IEG-MIGA. *IEG-MIGA 2007 Annual Report*. June 18, 2007. P. 17.

³⁷ IEG-MIGA. *IEG-MIGA 2007 Annual Report*. June 18, 2007. P. 18.

segments of the guarantees portfolio and to evaluate the financial attractiveness of new products. Throughout the implementation period, MIGA continued to improve its risk methods to provide management insight into performance and inform decision making.

4.25. **MIGA has updated and refined its pricing method.** In 2007, MIGA implemented several changes in its pricing model, including the integration of the economic capital model, updating of model parameters such as administrative cost allocation method, based on a review of MIGA's cost structure, and a review of cancellation parameters. The pricing model modifications also more accurately reflected actual economic risk by replacing actual capital with economic capital utilization.

4.26. **Revisions to the allocation of MIGA's administrative costs were guided by an effort to better understand MIGA's fixed and marginal costs.** A better understanding by MIGA of the recovery of cost (or profitability) from underwriting different types of projects should facilitate a more comprehensive decision-making process for determining underwriting strategy. Going forward, MIGA management needs to formulate clearer pricing principles and objectives that reflect this understanding of marginal and fixed costs. Such principles could address the expected consequences of transferring cost burdens from projects with certain characteristics to others, and how these consequences fit into MIGA's strategic underwriting objectives. To follow up, MIGA needs to monitor carefully the implementation of the modified pricing model to see if there are any unintended consequences, such as penalizing certain types of projects, sectors, or affecting overall cost recovery.

C. Human Capital and Resources Perspective

Resource Allocation

4.27. **MIGA received a budget increase to support the implementation of its strategic directions.** In the FY00 to FY04 period, MIGA's real administrative expenses had risen 27.8 percent while guarantee income had stagnated. Based on its strategy, MIGA submitted a work program and budget request for FY06 with three options where the difference was in the pace at which the strategy would be implemented. The Board approved the high budget scenario (real budget increase of 6.12 percent), with an expectation that MIGA would expeditiously implement its planned directions.

4.28. **However, MIGA did not make explicit the connection between the expected increase in expenditure and areas of planned business growth.** In its FY06 Business Plan and Administrative Budget that supported the strategy, MIGA indicated that its requested budget increase would be allocated to additional travel related to marketing and outreach to build its pipeline in priority areas, travel costs to support scaling up its infrastructure business, staff and travel costs to deploy TA, retaining specialized legal counsel for complex infrastructure projects and additional publications. These are largely variable costs and are not linked to specific performance objectives or outcomes, while MIGA's overall budget is largely fixed in terms of staff costs and World Bank Group charges.

4.29. **During execution, MIGA has contained expenses and its actual administrative costs have remained flat.** After an increase in FY06, MIGA's

subsequent budget requests involved decreases in real terms by 3.0 percent (FY07) and 4.5 percent (FY08). Actual administrative costs have remained largely flat during FY05-07, registering underruns of on average just under 20 percent per year compared to the approved budget envelope in each of the years.

Human Capital

4.30. **Overall staffing numbers do not appear to reflect changes expected in the strategy document.** MIGA estimated in that document that it would need to hire approximately 10 additional professional staff over the implementation period to support its growth, without connecting this to specific business needs that warranted strengthening. This anticipated increase does not appear in the subsequent supporting budgets. Instead, the number of internationally recruited staff remained constant between FY05 and FY07, and total staff levels declined between 2004 and 2006 by 14, in part due to transferring MIGA staff in areas such as Human Resources and Information Technology to central units in the Bank.

4.31. **MIGA has not yet articulated an explicit human resources strategy, but it has in practice invested in training and skills upgrading, and hiring has been targeted towards new and current skills needs.** Although MIGA recognized at the time the strategy was developed that there were areas where the organization needed to develop its human capacity, focusing on training and skills development for addressing a broader range of risk mitigation issues, this does not appear to have been planned or followed through systematically. Such a strategy could have also linked recruitment and retention and incentives to support implementation of the strategy and the operational plans.

4.32. Throughout the period, concerns were raised on MIGA's ability to retain institutional knowledge, as it faced staff turnover and experienced in some instances difficulties in filling vacancies. Staff surveys have pointed to areas of consistent underperformance in MIGA's HR management relative to the rest of the Bank Group, such as staff morale, staff performance evaluations and rewards, innovation, and managerial effectiveness.

Conclusions

4.33. Consistent with its new business model, MIGA has implemented systematic project level coordination with World Bank and has significantly scaled up its efforts to ensure its operations align well with Bank Group strategies and policies. MIGA has also increased collaboration at the strategic and project level with the World Bank and increased the number of products supported jointly with the WB and IFC. While positive and beneficial to MIGA, increased alignment and coordination has involved costs to the Agency.

4.34. MIGA has adapted its existing product to underwrite innovative deals, but has yet to make progress on more general development of its product range, which would benefit from amendments to its Convention and Operational Regulations, in order to meet its potential and meet demand from private investors.

4.35. MIGA's improvements of its processes and procedures were uneven and it has made little progress in some important areas. It has recently made some progress in improving performance management, monitoring, and internal reporting, and stronger attention is needed in this area.

4.36. MIGA has made progress on improving its ability to assess development impact. It developed its methodology in this regard but has not yet been consistent in its implementation. MIGA has harmonized its policy on social and environmental sustainability and performance standards with those of IFC. In particular, MIGA has also improved how it ensures that relevant specific safeguard policies are addressed.

4.37. MIGA has improved its client relationship management function, but more can be done to improve the effectiveness of its business development, by drafting annual business development plans, clarifying the roles and responsibilities of individual staff and aligning performance incentives with agreed outcomes.

4.38. MIGA has also improved its risk and finance analytics, culminating in a modified pricing model implemented in FY08 which has addressed some shortcomings resulting in pricing distortions. During implementation of its strategy MIGA has improved its decision making with respect to pricing, provisioning, reinsurance and capital deployment although some work remains in this regard.

5. RESULTS OF THE STRATEGY

5.1. This section presents some findings on the results that MIGA has achieved so far from the financial and development perspective. The section intends to shed some light on the question of the extent to which the implementation of MIGA's strategy has led to expected results. It presents findings in terms of growth, portfolio shifts, progress made on meeting some monitorable objectives and indicators established in the MIGA strategy document, trends and characteristics of projects underwritten during FY05-07, and alignment at appraisal of individual MIGA projects with World Bank Group country or sector strategies. It does not include development outcomes of projects underwritten during the FY05-08 period. This assessment recognizes the time lags involved with the implementation of changes to the business model, policies, and guidance discussed in Section 4, and that it would take time for changes to be reflected in MIGA's operational performance.

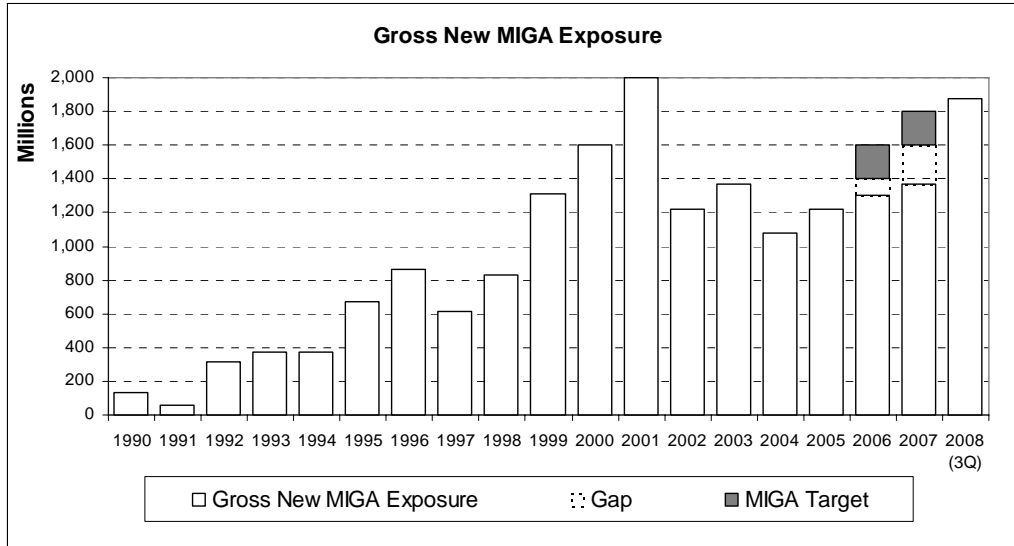
A. Operational Results

Portfolio Growth and Composition

5.2. **MIGA's strategy document anticipated overall growth targets for the Agency during FY05-08 and an expectation of increased focus in four operational priorities.** In addition to overall growth targets (paragraph 2.5), the identified operational outcomes included (i) increased level of SME transactions through the SIP in Africa and MENA (see 4.6 ff.); (ii) growth and diversification of the portfolio; (iii) growth of portfolio in African post-conflict countries; and (iv) increased investor interest in non traditional sectors/markets. Among the key indicators were total amounts of new MIGA business in infrastructure, new SIP business in Africa and MENA, proportion of new business going to frontier countries, increased volume of SME and post-conflict business, and number of new sub-national projects supported and in the pipeline. However, the strategy largely did not set expected target ranges for these indicators (see paragraph 3.17), other than in broad, qualitative terms, and there was clearly an expectation of directional changes in MIGA's new business volume towards the four priority areas.

5.3. **MIGA's business volume has increased steadily since its low point in FY04 but did not reach its expected annual business levels until FY08.** (See Figure 2). MIGA's business volume fell by almost half between FY01 and FY04, and during FY04 relied on one financial sector client for its business. Since FY05, business volume has increased but until FY08 MIGA has not reached the growth targets laid out in the strategy document, which called for a range of \$1.6-1.8 billion. The change registered in FY08 may reflect the time lag from actions adopted by MIGA during the last three years, as examined in Section 4, including the change in the pricing model. Sustaining the recent business growth will be important for MIGA's institutional sustainability in the future.

Figure 2. MIGA Guarantee Volume (FY90-08)



FY08 figure is actual business volume between July 1 and March 31, 2008.

5.4. **MIGA’s outstanding portfolio has remained constant.** On a gross basis (i.e., before reinsurance) MIGA’s outstanding portfolio was \$5.2 billion at the end of FY04 and \$5.3 billion at the end of FY07, and net exposure (after reinsurance) showed a small decline from \$3.3 billion to \$3.2 billion over the same period. Both numbers have been remarkably stable since FY01.

5.5. Table 1 presents some key characteristics of MIGA’s guarantee activities during FY05-08 and the previous strategy period. It points to an increase over time in the average size of projects insured by MIGA, reflecting the rise of “mega-deals” in MIGA’s portfolio.

Table 1: Key Characteristics of MIGA’s Guarantee Activities FY00-08

	FY00-04	FY05-07	FY08 (Q3)
Average volume of guarantees issued per year, gross (\$ billion)	1.455	1.296	1.874
Number of Projects Supported p.a.	40	35	18
Average Number of Contracts of Guarantee p.a.	58	58	30
Average Project Size (exposure per project, in \$ million)	36.371	36.688	104.100

5.6. **MIGA’s share of the political risk industry has decreased in recent years,** while there was increased demand for PRI overall as MIGA’s business has remained flat. MIGA’s share in 2007 was approximately 4 percent of the relevant market, a decline from 6 percent in 2004, during a period when the insurance market has recovered from the conditions following the September 11, 2001 attacks and the fallout of the Argentine crisis. The relative decline for MIGA also reflects increased supply of political risk insurance, with capacity increasing as a result of new market entrants and expanding offerings by existing providers. MIGA’s share of PRI in frontier countries has been

volatile, falling from 10 percent (2005) to 4 percent in 2006 before it rebounded to 9 percent (2007).

5.7. **Despite the variety of risk-mitigation products available to investors, the demand for PRI products continues to be robust**, as reflected in the rapid growth of new investment insurance business observed in the PRI market from 2004 through 2007. Total new business rose from \$16 billion in 2001 to \$44 billion in 2006 as investors prepared for the resurgence of traditional political risks, especially expropriation risk, which until early in this decade had been largely discounted. Recent episodes of expropriations and nationalization in Bolivia, Ecuador, Venezuela, and Russia have underlined the continued need for traditional PRI.

5.8. **MIGA's share in the PRI market has been eroded by private insurers offering a wide range of tailored guarantee and finance products and lower premiums.** Private insurers offer tailor-made financial products that MIGA and some national insurers are unable to offer because of the limitations in their charters. In MIGA's case, it can only insure eligible investments consisting of equity or quasi-equity but its coverage of debt is limited to loans with a link to equity. Competition from private insurers has also pushed down the premiums for PRI coverage, many suppliers of which have a different cost structure than MIGA with its development mandate. Private insurers have also expanded their business into higher risk countries, especially in Africa.

5.9. **Over the FY05-08 period,³⁸ MIGA has made important efforts to diversify the regional and sectoral distribution of the portfolio**, following a sharp increase in portfolio concentration in the Europe and Central Asia (ECA) region and in the financial sector during FY04-05 (due to reliance on two financial sector clients in ECA). Significant improvements were achieved in FY06 and FY07 in terms of sectoral and regional diversification (Figures 3 to 6), yet partial results for FY08 indicate a return to high concentration levels.

³⁸ Business numbers include MIGA's results for FY08 up to March 31, 2008 (3rd quarter).

Figure 3: Share of New MIGA Guarantees by Region and Sector (in Percent of Exposure)

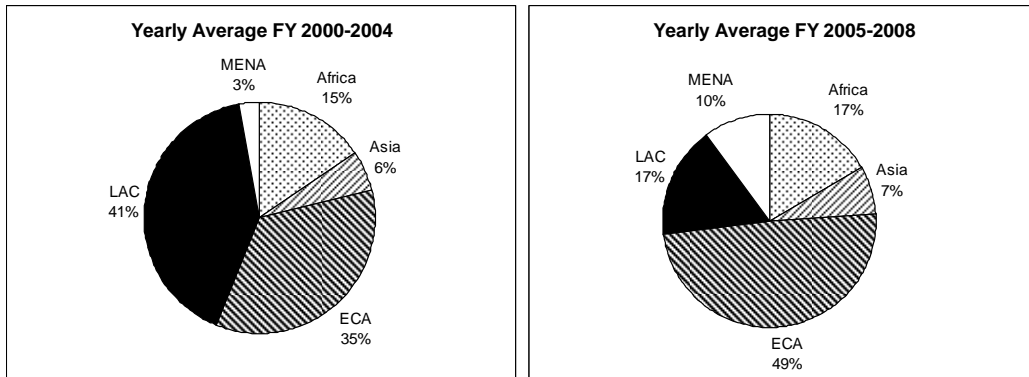


Figure 4: Share of New MIGA Guarantees by Region, by FY (in Percent of Exposure)

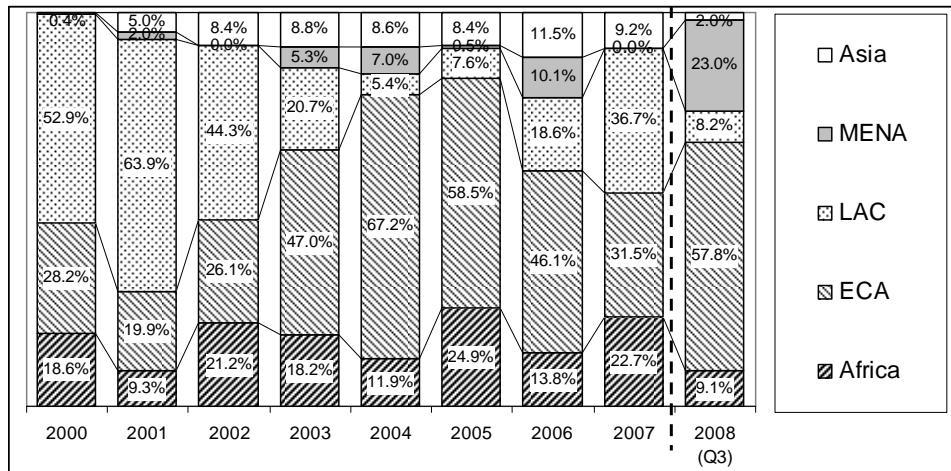


Figure 5: Share of New MIGA Guarantee Exposure by Business Sector

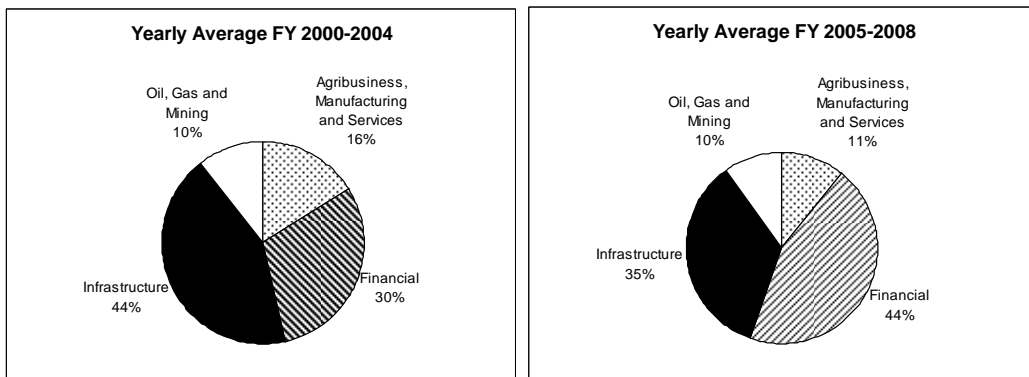
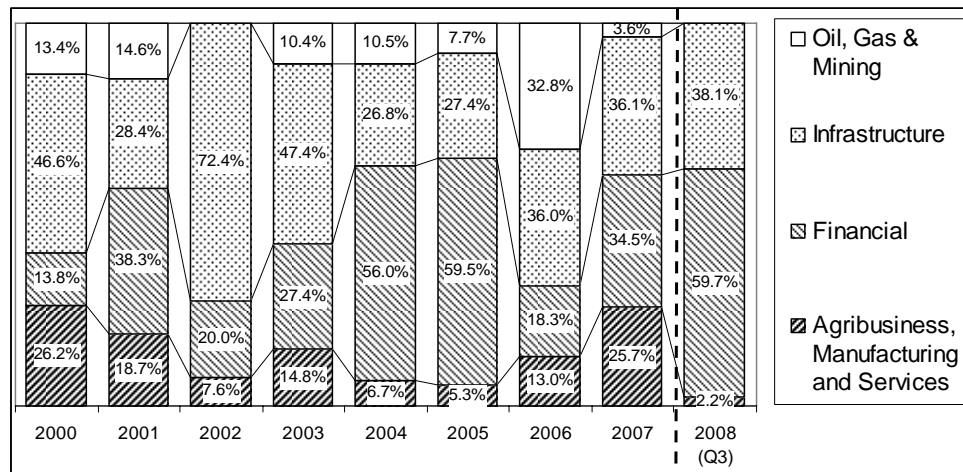
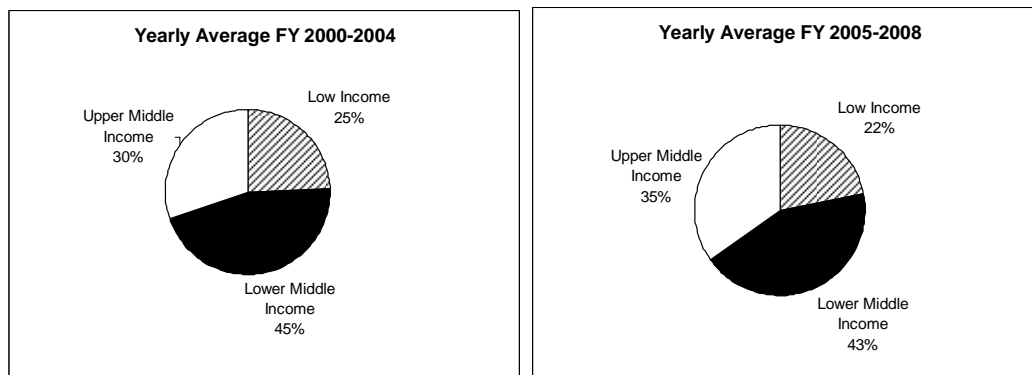


Figure 6: Share of New MIGA Guarantee Exposure by Sector, by FY (in Percent of Exposure)



5.10. **MIGA’s exposure tends to be concentrated in lower middle income countries (43 percent).** MIGA also continues to meet demand for coverage in upper middle income countries, accounting for 35 percent of exposure. This is consistent with trends in the FY00-04 period (see Figure 7).

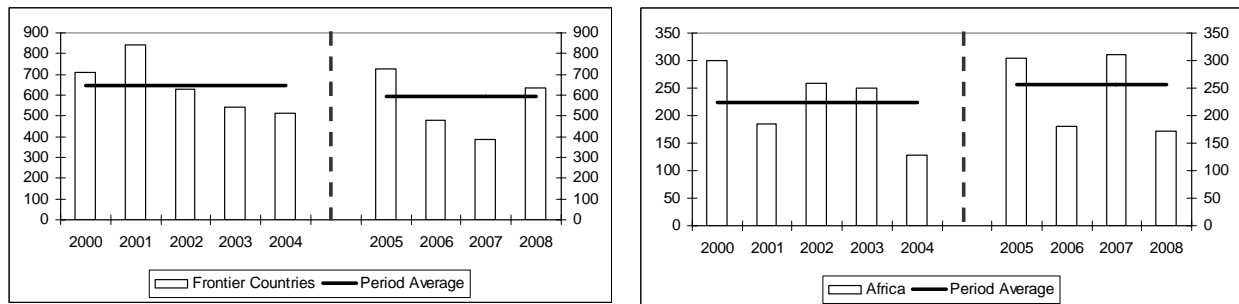
Figure 7: Share of New MIGA Guarantee Exposure Middle Income and Low Income Countries



5.11. **MIGA has pursued opportunities in each of its operational priority areas and its portfolio composition has shown continuity.** MIGA has directed significant shares of its new guarantees activities to priority areas. The portfolio composition shows a large degree of continuity rather than changes in direction following approval of the new strategy, when compared to MIGA’s performance under the preceding strategy period (FY00-04). IEG reviewed shifts and trends in MIGA’s new guarantee issuance for FY05-07 (including FY08 where available) to assess how MIGA’s portfolio aligned with its strategic priorities. This is shown in paragraphs 5.12 to 5.17 below.

5.12. In terms of MIGA’s support for **frontier countries**,³⁹ about 39 percent of MIGA’s exposure (and more than half of new projects) underwritten in FY05-08 went to countries that are characterized as either high risk or low income (see Figure 8). This share has declined since FY05, and is below the average achieved in FY00-04 (44 percent). The relative decline may be due to reclassifications of countries no longer considered frontier, and where MIGA has been active in both periods, such as Serbia or Ukraine.⁴⁰ MIGA’s new exposure in frontier countries in FY05-08 decreased in Africa and declined sharply in both the ECA and LAC regions, compared with the earlier strategy period.

**Figure 8: MIGA Guarantees in Frontier Countries and Africa
(Annual new exposure by FY, US\$ millions)**



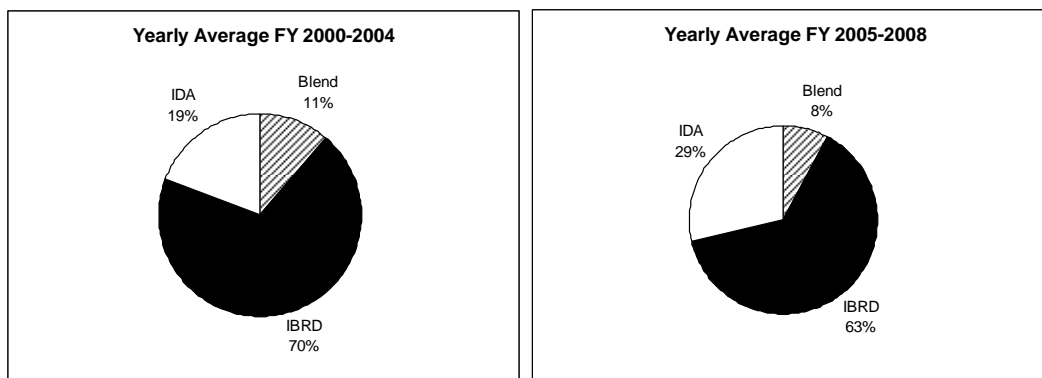
5.13. Within this group, however, MIGA has made substantial efforts to increase its activities in Sub-Saharan Africa, another focus area (see Figure 8), from 15.4 percent of new exposure (FY00-04) to 16.8 percent (FY05-08). MIGA achieved an increase in business volume in Africa from an average business volume of \$225 million p.a. (FY00-04) to an annual average of \$265 million (FY05-07), although it has not yet reached its target of quadrupling new business in Africa by FY08 (from a base in FY04). Similarly, MIGA increased the share of projects supported in Africa from just under 20 percent (FY00-04) to 33 percent (FY05-08).

5.14. **MIGA has increased its guarantees volume in IDA or IDA-eligible countries** (see Figure 9). New exposure in IDA countries accounted for 29 percent during FY05-08 (compared with 19 percent in the earlier strategy period). Together with blend countries, MIGA commitments in IDA-eligible countries rose to 36 percent from 30 percent earlier in the decade. In terms of the numbers of projects supported, a significant share (40 percent of new projects during FY05-08) were in IDA countries, compared with 23 percent during FY00-04. While guarantee volumes in both IBRD and blend countries declined in absolute and relative terms, MIGA increased its new guarantee exposure in IDA countries. The increase in exposure in IDA countries is due to the increases in the Africa and Asia regions, which offset a sharp decline of exposure in Latin America. The MENA regions’ increase can be attributed to one large project.

³⁹ Using MIGA’s definition of frontier countries.

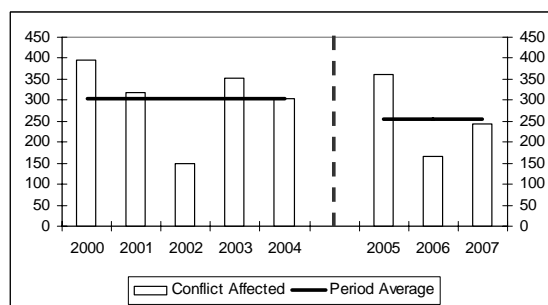
⁴⁰ The number of countries considered frontier declined from 98 (FY00) to 91 (FY08).

**Figure 9: Composition of MIGA Guarantees in IDA, Blend, and IBRD Countries
(Annual new exposure by FY, USD millions)**



5.15. **New exposure in conflict-afflicted countries has remained constant.** The share of MIGA’s new exposure in conflict-afflicted countries⁴¹ has remained constant at around 20 percent of MIGA’s new exposure between FY00-04 and FY05-07 (see Figure 10). In this regard, the strategy had stated that MIGA would work on establishing a trust fund for underwriting guarantees in post-conflict countries in Africa. The initiative did not materialize. MIGA’s new exposure for conflict-afflicted countries declined in Africa over the FY05-08 period compared with FY00-04, as did exposure in ECA, while exposure to conflict-afflicted countries in the LAC region decreased dramatically. Asia registered a moderate increase and the MENA region a significant improvement due to a mega-deal.

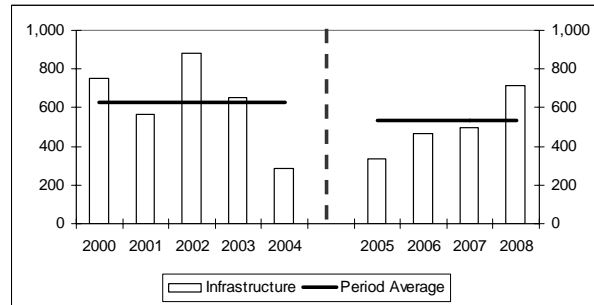
**Figure 10: MIGA Guarantees in Conflict-Afflicted Countries
(Annual new exposure by FY, US\$ millions)**



5.16. MIGA has pursued a focus in **infrastructure development**, which was already a priority area during FY00-04, as evidenced by the large share (35 percent vs. 43 percent during FY00-04) of new guarantees volume in infrastructure projects (see Figure 11). When considering the number of projects, the share of infrastructure remained flat at 31 percent, for FY00-04 and FY05-08, respectively. Within this sector focus, the Agency has increasingly supported more complex projects in new sub sectors, such as water and sanitation.

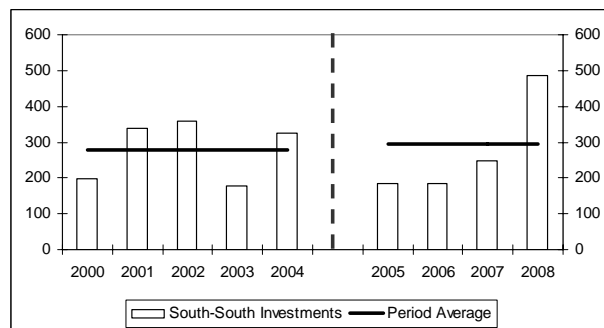
⁴¹ Using an IBRD definition of Conflict-Affected Countries.

**Figure 11: MIGA Guarantees for Infrastructure Projects
(Annual new exposure by FY, US\$ millions)**



5.17. **MIGA support for south-south investments has stayed constant between the two periods, with an upward trend registered since FY07.** In this priority area, MIGA continues to support a share of 19 percent of its guarantee volume to investors from MIGA Part II countries (see Figure 12).⁴² (The share of projects originating in developing member countries increased from 21 percent to 34 percent.) However, when considering only investments among developing countries (excluding investments from MIGA Part II countries classified as high income, such as Cyprus, Israel, Singapore, Slovenia, and United Arab Emirates), the shares of exposure drop to 15 percent (FY00-04) and 12 percent (FY05-08). In terms of the origin of insured investment flows, the recent strategy period involved for the first time MIGA guarantees for investments from emerging economies in Africa, the Middle East, and Asia. They also showed a relative decline of insured investments originating in Latin America and ECA and from some traditional MIGA client countries such as Singapore, Mauritius, or Brazil.

**Figure 12: MIGA Guarantees for South-South Projects
(Annual new exposure by FY, US\$ millions)**

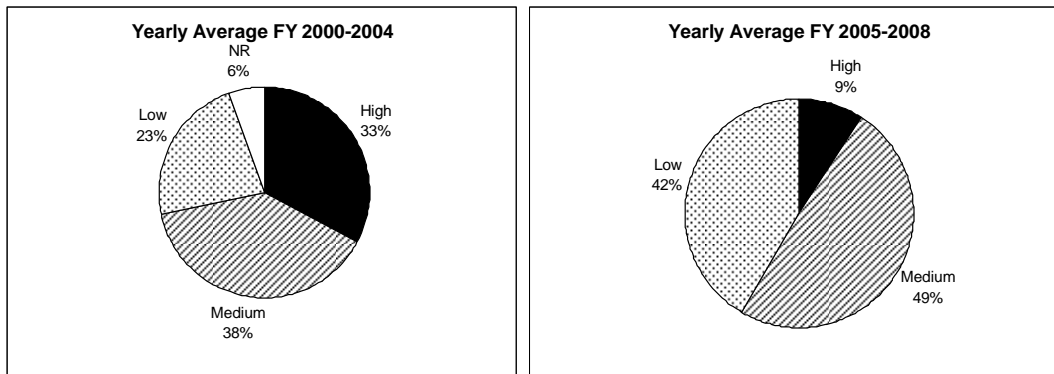


5.18. **According to some country risk indicators, MIGA exposure is increasingly concentrated in countries with low risk profiles.** Changes in the risk profile of MIGA’s exposure are an important indication of MIGA’s added value in supporting investments in the most risky and underserved markets. IEG mapped the volume of MIGA’s new exposure to a suitable risk indicator and classified countries in three categories as per this indicator: high risk, moderate risk, and low risk (see Figure 13). Many indicators approximating investment climate or country risk have shown an

⁴² Investments from MIGA developing member countries to other developing countries.

improving trend over the last 10 years.⁴³ Parallel to this, MIGA's exposure has become heavily concentrated in countries rated as low risk (42 percent of exposure during FY05-08, compared with 23 percent during FY00-04). A relatively small share now goes to projects in high risk countries (9 percent vs. 33 percent in the previous period). During FY05-08 most of MIGA's portfolio in countries classified as high risk has been concentrated in Africa and MENA, whereas during FY00-04 the highest exposure in high risk countries was in the ECA region, followed by Africa. Most of MIGA's low risk exposure is concentrated in ECA and medium risk is dominated by the Latin America and Caribbean region.

Figure 13 : Risk Profile of Countries with MIGA Exposure

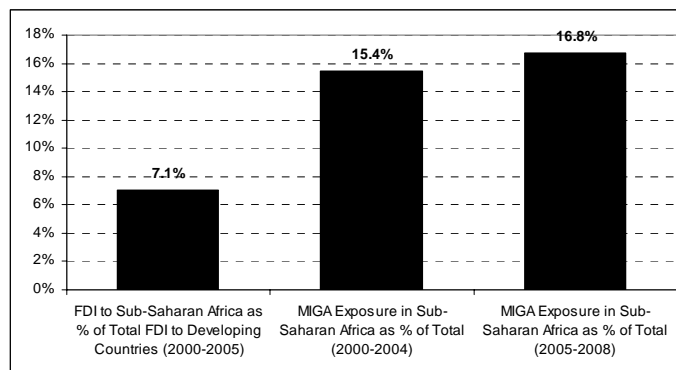


5.19. **MIGA has been successful in supporting investments to underserved markets, rather than mirroring international FDI flows.** Measured by the share of MIGA's new exposure going to the top 10 developing country recipients of FDI, MIGA has well diversified its portfolio. The top 10 FDI recipients attracted 58 percent of FDI flows to developing countries⁴⁴, but accounted for just 24 percent of MIGA exposure during FY05-08 (34 percent for FY00-04). MIGA is notably more exposed to sub-Saharan Africa than the share of FDI this region is receiving—it accounted for just over 7 percent of FDI to all developing countries during 2000-2005, while MIGA's new business volume in Africa has averaged 17 percent of total new business during FY05-08.

⁴³ See for example: World Bank. *Improving Investment Climates*. 2006. P. 66 ff.

⁴⁴ Based on FDI inflows during 2000 to 2005, top recipient countries were China, Brazil, Russian Federation, Poland, India, Chile, Hungary, Colombia, Turkey, and Romania.

Figure 14 : FDI Flows vs. MIGA's New Exposure in Sub-Saharan Africa



5.20. **MIGA's client concentration has been a concern.** In the period FY00-04 four financial sector clients accounted for 30 percent (31 new projects) of MIGA's new gross exposure. Client concentration increased in the period FY05-08 as two financial sector clients accounted for 35 percent of new exposure and the top four clients accounted for 49 percent of new guarantees issued in the same period (18 new projects). While client concentration has thus remained high, the composition of the top ranked clients has changed. MIGA has reduced its reliance on one financial sector client from FY04 and FY05 (accounting for 43 percent and 54 percent of gross exposure, respectively) to 10 percent in FY07. Also, the year-to-year trend shows that the proportion of new guarantee volumes of the two clients with the largest yearly exposure went up from 17 percent in FY00 to 62 percent in FY05 and then declined to 25 percent and 43 percent in the next two years.

B. Financial Results and Sustainability

5.21. As noted in paragraph 3.9, **MIGA's strategic directions did not incorporate financial objectives and targets**, or reflect explicitly the need for MIGA to pursue a balanced portfolio to ensure its financial sustainability and manage risks prudently.

5.22. **MIGA has a strong capital base, but its income side is less solid.** MIGA's capital base gives clients comfort in MIGA's ability to pay out claims, one of the comparative advantages as identified through client surveys. However, its income side is less healthy. MIGA has had a positive net income each year. As a result, net premium income peaked in FY04 and has since declined; in FY07 it was 11.3 percent lower than in FY04. At the same time, administrative costs are relatively high, after having grown by 54.9 percent between FY00 and FY04 in nominal terms, and then, (as noted in paragraph 4.29), staying flat since FY06. However, the ratio of actual administrative cost to net premium income was 80 percent in FY07, up from 61 percent in FY00 and 68 percent in FY04.⁴⁵ If this trend should continue, MIGA's cost could exceed its net guarantee income in the medium term. MIGA's earlier increases in administrative cost are relatively well understood and partly reflect MIGA's development mandate and its role as

⁴⁵ MIGA Financial Statements (several years).

a member of the World Bank Group, but MIGA needs to manage better the dynamics on its revenue side in order to reach a better balance between costs and revenues. (See Table 2.)

5.23. MIGA's net premium income depends on (i) the effective premium rate, and the (ii) average size of its portfolio (including the size of reinsurance). As noted above, MIGA's total portfolio remained relatively flat throughout FY07. It is determined by new guarantees issued, but also by the run-off from the portfolio (cancellations, reductions, and expiries). Cancellations play a particularly important role. The reasons for contract cancellations differ and may be consistent with MIGA's development mandate and value added in fostering investment. However, a high share of cancellations affects MIGA's revenues.

5.24. Effective premium rates declined during FY05-07 compared to earlier this decade. The recent PRI study for MIGA's upcoming strategy found MIGA to be among the PRI providers with the highest premium rates. The downward trend in effective premium rates for MIGA may well reflect market pressures given a "soft" insurance market (see paragraph 5.6 f.). There has been a general improvement of risk and business environment indicators over the past few years, which can also explain the lower average effective rates. The decline in MIGA's premium income may also reflect an increasing share of financial sector projects with fewer risk coverages per project and projects exiting from the portfolio that were underwritten when MIGA's average premium rates were higher.

5.25. **Premium:** As noted in paragraph 4.25 f., MIGA's pricing model has recently been modified to incorporate more rigorous assumptions, which should improve its ability to accurately reflect in premium rates a systematic recovery of administrative cost on a portfolio level. IEG has analyzed the consistency of MIGA's pricing practice since implementation in January 2004 of the current pricing model and through FY07, comparing non-binding indications generated by the model with actual pricing in the contracts. A consistent pricing would indicate that MIGA systematically attempted to recover administrative cost, a risk premium, and return on capital through its new business. IEG observed that projects are priced consistent with model benchmarks up to a certain hurdle but as they increase in size, over and underpricing increases significantly.

5.26. MIGA has little flexibility in changing its pricing over the medium term since its pricing model is based on recovery of administrative cost (on a portfolio basis) plus a risk component. Changes in expected and outstanding business volume can drive changes in pricing. As a development institution, MIGA has a mandate of "complementing" private insurance companies and export credit agencies rather than competing with them for business. However, if MIGA's pricing should diverge significantly from that of other providers, it could erode its comparative advantage and business volume or, alternatively, crowd out other PRI providers in certain market segments. MIGA can further clarify its pricing strategy vis-à-vis insurance business cycles and market prices. As prices largely reflect administrative costs and its cost drivers are derived from expected volume of new and outstanding business, premiums would tend to decrease when the expected and outstanding business volume rises, and would tend to increase when expected demand for MIGA's product falls. This aspect

would require further attention in future pricing model adjustments, to ensure alignment between pricing and MIGA's strategic objectives.

**Table 2: MIGA's Guarantee Activities FY00-07 and MIGA Financials
(in US\$ thousands)**

Outstanding Portfolio (as of June 30th)	2000	2001	2002	2003	2004	2005	2006	2007
Guarantees Issued (MAL)	1,605,398	1,999,780	1,194,256	1,351,977	1,054,738	1,206,631	1,299,764	1,355,377
Number of Contracts (issued)	59	67	58	59	56	63	66	45
Gross Outstanding Guarantee Portfolio	4,364,812	5,179,040	5,256,599	5,082,778	5,186,017	5,094,443	5,362,405	5,301,190
Reinsurance	1,548,856	2,022,603	2,055,148	1,878,789	1,927,255	1,956,147	2,052,228	2,091,776
Net Outstanding Guarantee Portfolio	2,815,956	3,156,437	3,201,451	3,203,989	3,258,762	3,138,296	3,310,177	3,209,414
MIGA Financials	FY00	FY01	FY02	FY03	FY04	FY05	FY06	FY07
Premium Income	37,443	46,341	57,043	53,878	57,947	57,140	52,879	48,960
Premium Ceded	(13,037)	(18,078)	(24,376)	(21,371)	(23,225)	(23,864)	(20,488)	(17,289)
Fees and Commissions	5,128	8,203	7,700	6,990	6,194	6,354	4,772	4,617
Net Premium Income	29,534	36,466	40,367	39,497	40,916	39,630	37,163	36,288
Income from Investments	23,473	30,356	28,708	25,298	14,241	16,842	11,352	42,747
Others (Translation gains + income from staff retirement plan)	2,717	2,999	2,187	16	4		2,673	8,848
Total Other Income	26,190	33,355	30,895	25,314	14,245	16,842	14,025	51,595
Total Income	55,724	69,821	71,262	64,811	55,161	56,472	51,188	87,883
(Release of) provisions from claims	26,625	29,734	43,891	(20,672)	(62,440)	(106,849)	(3,374)	(3,726)
Release of provisions due to withdrawal of claims								(837)
Administrative Expenses	18,065	19,772	21,939	25,523	27,985	30,330	30,846	29,103
Other Expenses	130	745	943	1,144	1,612	1,995	484	995
Total Expenses	44,820	50,251	66,773	5,995	(32,843)	(74,524)	27,956	25,535
Net Income	10,904	19,570	4,489	58,816	88,004	130,996	23,232	62,348

5.27. **Claims and pre-claims: MIGA has had an excellent claims record over 19 years of operation.** MIGA's net income and financial sustainability is also dependent on its claims record. In the nearly 19 years since its inception, MIGA has accepted and paid only three claims for a total of \$5.2 million (net, i.e., after reinsured amounts); one claim paid was subsequently recovered from the host country government. Two claims were brought under expropriation and one under a war and civil disturbance coverage. The latest two claims were paid in FY05.

5.28. Between FY03 and FY07, 21 MIGA projects involved claims or pre-claims. Infrastructure projects accounted for the largest share among them (57 percent), somewhat higher than the share of infrastructure projects in MIGA's portfolio. Agribusiness, manufacturing, and services projects accounted for 19 percent, whereas relatively few financial sector projects encountered disputes. Sixteen projects involved either Public Private Partnerships (PPPs) or a project with a concession. Based on the low number of investment disputes in its portfolio that resulted in the payout of a claim, MIGA has had a good track record in helping resolve such disputes.

5.29. In sum, with respect to financial performance and sustainability, MIGA's strategy lacked a full discussion of the interdependencies between growth, financial, and development objectives. MIGA has a strong capital base for underwriting guarantees, but its net premium is declining and the ratio of administrative cost to premium income is high. Due to several factors, including market trends, MIGA has seen its effective premium rates decrease over recent years. At the same time, MIGA has maintained a strong record in mitigating investment disputes, resulting in a very low incidence of claims paid.

C. Expected Development Results

5.30. **It is too early to assess development outcomes of MIGA projects supported during the FY05-08 period.** However, IEG-MIGA evaluated a sample of 12 projects that reached maturity during the strategy period (i.e., projects underwritten by MIGA between FY96 and FY02), the results of which are presented in this section. Prior IEG-MIGA evaluations have found an association between work quality and development outcome.⁴⁶ (This is a finding that has been confirmed by IEG-IFC evaluations of IFC investment projects.) MIGA's performance in projects prior to its current strategy period is used as a benchmark against which to assess progress during FY05-08, using IEG-MIGA's more recent assessment of the quality at entry of the population of MIGA guarantees underwritten between January 1, 2005 and June 30, 2006. These findings are complemented by an IEG project profiling of all new MIGA projects during FY06 and FY07 (see Box 2).

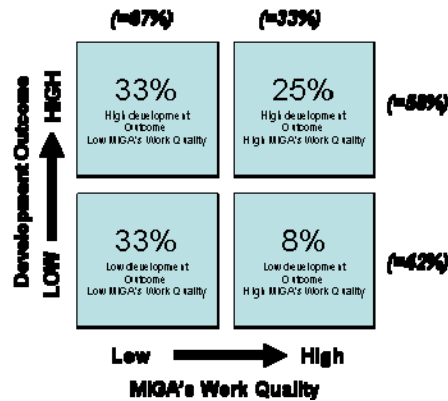
5.31. **Findings from Ex-post Evaluations of Projects Preceding the Current Strategy:**⁴⁷ Figure 15 shows an association between MIGA's work quality and development outcomes for this sample of 12 projects. Three-fifths of evaluated projects had high ratings for development outcomes, while the rest were rated partially unsatisfactory. Half of the projects were rated as high for MIGA's effectiveness⁴⁸ (consisting of three components: strategic relevance, MIGA's role and contribution, and MIGA's assessment, underwriting and monitoring), with all projects rated high for their strategic relevance and all but one rated high for MIGA's role and contribution. However, only 33 percent of projects rated high for MIGA's work quality (assessment, underwriting, and monitoring; see Figure 16).

⁴⁶ IEG-MIGA. *IEG – MIGA 2006 Annual Report*. May 31, 2006.

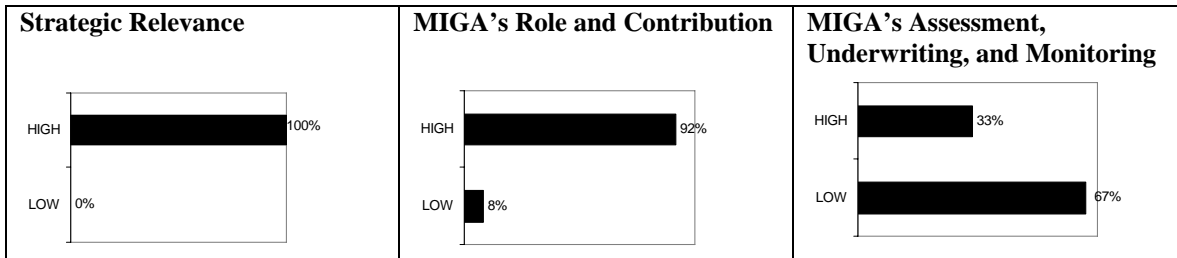
⁴⁷ Based on IEG evaluations of 12 MIGA projects that were underwritten in the period FY97-02.

⁴⁸ Ratings of Excellent and Satisfactory correspond to "high", whereas partially satisfactory and unsatisfactory correspond to "low" for the purposes of showing associations in the graph.

**Figure 15: Development Outcome and MIGA's Effectiveness
(Sample of 12 Most Recent Projects Evaluated)**



**Figure 16: MIGA's Effectiveness Results
(Sample of 12 Most Recent Evaluated Projects)**



5.32. IEG identified the following issues in this cohort's adequacy of project assessment, underwriting, and monitoring, which preceded guidelines and processes of the current strategy period:

- MIGA's analysis of projects' financial viability had shortcomings. Due to a strong reliance on investor's representations, MIGA did not verify assumptions on information provided by the guarantee holders.
- MIGA's analysis of development impact was not satisfactory. In many cases ex-ante project impacts were not adequately discussed by MIGA in the underwriting documents and were based on overly optimistic assumptions and incomplete analysis.
- Although the agency had scaled up the environmental and social supervision of its projects since 2004, adequate monitoring arrangements associated to compliance with environmental and social policies and safeguards were still not in place at the time of evaluation. Some of these problems were associated to MIGA's practice of not requiring monitoring reports for Category B projects.

5.33. **IEG Quality at Entry Assessments of Projects Underwritten during Current Strategy Period:** MIGA's work quality to ensure strategic alignment, ex-ante assessment, and due diligence of guarantees has improved for recent projects reviewed by IEG. The IEG-MIGA 2007 Annual Report assessed 23 new regular

projects to determine improvements in MIGA's work quality. These guarantees were issued by MIGA during the period January 2005 to June 2006.⁴⁹ The results are summarized in paragraphs 5.34-5.38 below.

5.34. MIGA's strategic relevance and value added: Nearly all of the MIGA projects were aligned with the host country, WBG, and MIGA's strategic priorities. The quality at entry assessment confirmed that MIGA's collaboration with the World Bank and IFC had increased since 2004.

5.35. Assessment of expected business performance: Since 2004, MIGA has strengthened analysis of the projects' ex-ante financial performance, a key determinant of expected development outcome. The business objectives and scope of these projects are also better defined, which previous IEG reports found often lacking in earlier MIGA projects.⁵⁰ However, the underlying assumptions and risks affecting a project's financial viability are not always provided.⁵¹ Relevant sector issues are now taken into consideration more systematically, especially for financial sector projects.

5.36. Assessment of Expected Contribution to Economic Sustainability: MIGA had made progress in determining the economic soundness of projects through the application of a cost-benefit approach, but this method had not yet been mainstreamed and requires further attention by MIGA. In 2004⁵² IEG had not found any projects that presented an ERR⁵³ or a full cost-benefit analysis to aid MIGA's decision on whether a project would be beneficial to society or not. In contrast, in the latest analysis, five out of the 18 real sector projects for which cost-benefit analysis was applicable presented a full cost-benefit analysis in the decision documents. Projects with concessions have to indicate "positive social return" because of their potential to affect a range of stakeholders but only three out of 14 complied.⁵⁴ Most projects involving concessions were still not assessed adequately, particularly their implications for consumers affected by the projects, especially the poor. Among the four financial sector projects only one had an economic return on invested capital (EROIC) as required by MIGA's guidelines.

5.37. Assessment of Environmental and Social Issues: MIGA's assessment of environmental, health, and safety (EHS) and social issues showed strong improvement as most (86 percent) of the assessed projects, including SIP, adhered to MIGA's requirements for addressing environmental and social issues. MIGA adequately addressed EHS issues of Category A and C projects but there were shortcomings in four Category B projects, three of which were SIP projects. The shortcomings related to the use of outdated environmental audits, EIAs not covering the full scope of the project,

⁴⁹ IEG also reviewed 13 new projects under the Small Investment Program (SIP) but these projects have different requirements and procedures and thus excluded from the analysis below.

⁵⁰ This improvement was facilitated by the recent inclusion of a clause in MIGA's contract of guarantee, requiring a legal description of the investment project.

⁵¹ Only a third of the projects specified FRR assumptions in a manner consistent with the project's business plan and the sector context while a third of the projects discussed commercial risks adequately.

⁵² See IEG-MIGA. *2004 Review of Development Effectiveness in MIGA*. August 19, 2004.

⁵³ Paragraph 3.05 of MIGA's Operational Regulations is explicit in its requirement that a reasonable economic rate of return should be established based on the projects costs and benefits regardless of any distortions due to trade, tax, pricing and other concessions offered by or have been agreed with the host government.

⁵⁴ Ten projects had concessions and four projects had the government as its direct client.

absence of environmental and social assessments prepared by guarantee holders, and lack of investors' environmental management systems.⁵⁵ Notable improvements have been achieved in the way MIGA ensures that relevant specific safeguard policies are addressed, with the greatest improvement in social safeguard policies. MIGA has also made better use of its contracts of guarantee to reference appropriate safeguards and guidelines⁵⁶ since 2004, consistent with an earlier IEG recommendation, although it also needs to include EHS reporting requirements. Modest progress has also been made in adapting IEG's earlier recommendation to key reporting requirements for EHS monitoring in the contract of guarantee for relevant projects. However, upstream attention to setting up Environmental Management Systems (EMS) has remained insufficient.

5.38. IEG's risk profiling of recent MIGA projects confirms a strengthening of underwriting quality (see Box 2).

Box 2: IEG Project Risk Profiling

IEG has profiled recent MIGA projects underwritten during FY06 (32 projects) and FY07 (20 projects) to determine their risk factors against success drivers IEG-MIGA adapted from IEG-IFC evaluation findings.⁵⁷ A total of 52 projects were profiled, excluding contracts linked to modifications of prior projects. The review was based on information contained in MIGA's underwriting papers, President's Reports, and using independent indicators (such as for business environment). This exercise covered: (i) changes in the quality of a country's business climate following project approval; (ii) type of industry sector in which the investment is made; (iii) quality of the project sponsor; (iv) level of product market, client company and project type risks; and (v) work quality (in this case by MIGA).⁵⁸ Absence of a success driver means higher risk.

Based on these findings, MIGA appears to have made further progress in the depth of its underwriting. For FY07, 45 percent of projects contained information on concessions or Public-Private Partnerships. Of these projects, more than half contained references to competitive bidding. MIGA also strengthened its analysis of sector issues in its underwriting: More than half the projects referred to sector reforms, restructurings, or policy changes. Of the 20 projects, 12 analyzed whether there was a presence of market distortions or circumstances impeding competition, which may affect the economic viability of projects. Eight of these projects affirmed the presence of such distortions. 60 percent of projects where this information was referenced in MIGA's documents involved sectors with claims or disputes in the host country.

⁵⁵ IEG-MIGA. *IEG-MIGA 2007 Annual Report*. June 18, 2007.

⁵⁶ Contracts of guarantee were used in 54 percent of the projects to explicitly reference relevant MIGA safeguards.

⁵⁷ IEG-IFC has for a number of years used its large annual samples of IFC's Expanded Project Supervision Reports (XPSRs) to identify key results drivers for the quality of development outcome and IFC's investment outcome, and the identified drivers have been shown to be quite robust across sectors and regions. IEG-MIGA does not yet have a corresponding data base for MIGA projects, but it seems likely that findings for IFC projects will be at least reasonably valid also for MIGA projects, and IEG-MIGA has also in the past been able to identify some similar associations for the quality of MIGA project outcomes.

⁵⁸ See IEG-IFC: *Independent Evaluation of IFC's Development Results 2008*, p. 12 f.

Conclusions:

5.39. MIGA's strategy anticipated business growth targets and an expectation of an increased focus in the four operational priority areas. There has been a consistent increase in business volume since the nadir of FY04, following a steep decline of MIGA business and high portfolio concentration. But MIGA did not reach until FY08 the business volumes expected for the FY05-08 period. At the same time the political risk insurance has experienced significant growth, due to the entrance of new market participants and expansions of offerings from existing PRI providers.

5.40. MIGA has been successful in pursuing opportunities in each of its operational priority areas: frontier countries, conflict-afflicted countries, infrastructure, and south-south investments. Its operational results for business volume in each of these areas show some continuity with the patterns observed during the previous strategy period. MIGA has improved its focus on Africa and in IDA countries.

5.41. MIGA's exposure continues to be concentrated in lower middle income countries and analysis also suggests MIGA is increasingly active in countries with low risk.

5.42. MIGA has a strong capital base, but net premium income has declined due to a largely flat outstanding portfolio, market pressures, and changes in MIGA's portfolio composition—although MIGA's premiums remain above industry averages. The ratio of administrative cost to net guarantee income has increased. Overall, MIGA is recovering its administrative cost through premium income but instances of under- and overpricing have had an impact on guarantee income.

5.43. It is too early to assess the development outcomes of MIGA projects approved during the FY05-08 period, but findings from IEG ex-post evaluations and quality at entry assessments suggest a strengthening in many aspects of MIGA's effectiveness, ensuring the strategic relevance and MIGA's value added, and improving MIGA underwriting and, to a lesser extent, monitoring. In particular, MIGA improved attention to the financial viability of its projects, an important predictor of development outcome; made progress in assessing the economic soundness of projects; and scaled up the assessment and supervision of environmental, health, safety, and social issues.

5.44. IEG evaluations point to an important role MIGA has played for a sample of ex-post evaluated projects, ranging from MIGA's support being critical for the investment to go forward, its environmental and social requirements providing comfort to investors dealing with local communities, and to investors entering a new country. MIGA's role was considered especially important for investments in post-conflict countries. There is, however, a need to address more systematically MIGA's additionality in its projects.

6. OUTLOOK: MIGA'S ROLE AND THE POTENTIAL FOR MIGA GUARANTEES⁵⁹

6.1. **The challenge facing MIGA in the next five years is to take advantage of the demand for political risk insurance given its strengths and to find solutions to constraints** hindering its ability to adapt to a rapidly changing global investment environment. Notwithstanding the array of risk mitigation products offered to investors and the number of investors opting to self-insure, demand for PRI had been strong since 2004.⁶⁰ The resurgence of expropriation and nationalization risks and the increasing incidence of non-honoring of sovereign guarantees has revived awareness of political risks. Demand for PRI products continues to be robust indicated by the rapid growth in the new business of the Berne Union (BU) investment insurance members from 2004 through 2006. A June 2007 global survey of 602 executives by the Economist Intelligence Unit affirmed the positive outlook for PRI in the next five years, noting that companies with better political risk assessment capabilities experienced fewer cases of expropriation, government payment default, or currency transfer restriction compared to those without PRI coverage.⁶¹

MIGA's strengths:

6.2. **MIGA is known in the PRI market for offering long-term tenors, its excellent claims record, ability to provide coverage to difficult projects in high risk countries, large underwriting capacity, and, as part of the WBG, it has good relationship with host governments.** MIGA is also a trusted party in resolving investment disputes. Its comparative advantage vis-à-vis other market players has been consistent and reaffirmed by the 2008 and past client studies commissioned by MIGA. The 2005 conceptual framework presented in the strategy document capitalizes on these strengths which identified the two areas where MIGA can deploy its resources for maximum development impact: (1) countries that are relatively low risk but still underserved by private insurers due to country capacity limits; and (2) high-risk, frontier markets and conflict-affected countries for maximum value-added and development impact. These identified segments remain relevant at the present time as confirmed by a 2008 MIGA client study. However, MIGA has faced increasing competition from private insurers even in high risk countries in the last four years. In 2005, private insurers accounted for 50 percent of new PRI business in Africa, which has most of the high-risk, frontier countries. In 2007, its share was estimated to have been increased to 70 percent. Private insurers are also offering long-term tenors (10 to 15 years) for their PRI.

6.3. **MIGA has the most mainstreamed, flexible, well-defined and tested guarantee product within the WBG.** MIGA has the most unbundled and narrowly defined product within the WBG, thus allowing clients to purchase exactly what they

⁵⁹ IEG. *The World Bank Group Guarantee Instruments 1990-2007: An Independent Evaluation*. 2008. (Forthcoming)

⁶⁰ Reported new exposure by Berne Union members has increased from \$18 billion to \$44 billion between 2004 and 2006.

⁶¹ Economist Intelligence Unit. *World Investment to 2011. Foreign Direct Investment and the Challenge of Political Risk*. 2007.

need. There is clear demand for this flexibility. MIGA's insurance is also the least disruptive to a project's financing structure, compared with other risk mitigation tools offered by the WBG. MIGA has been able to enhance its capacity despite limitations imposed by its Convention. MIGA's product is also the most standardized among WBG guarantees, which allows for quick deployment. Thus it appears that MIGA's comparative advantages over other WBG instruments is in situations where (i) certain political risks can clearly be identified, isolated, and managed; (ii) the project is at an advanced stage of development and possible funding has been identified; and (iii) the client wants specific, narrowly defined risk mitigation.⁶²

MIGA's Constraints:

6.4. **MIGA faces challenges in its business environment due to a proliferation of political risk mitigation instruments offered by private insurers, which MIGA is unable to match due to limitations in its Convention.** The business environment for MIGA has become more difficult because it can only provide coverage against four types of 'traditional' political risks. It can cover loans (non-shareholder loans) if these are equity-linked and the guarantee coverage must be related to new investments. Private insurers, such as AIG, Chubb, Lloyds, and Zurich do not have these constraints and can insure stand-alone debt and provide coverage to new and existing investments. Business growth also came from tailor-made guarantee products and by offering a wider range of guarantee products including comprehensive coverage. Their PRI products include coverage against non-honoring of sovereign guarantees, trade credit insurance, terrorism cover, all of which are ineligible under the MIGA Convention and Operational Regulations.

6.5. **The soft PRI market since 2004 has pushed premium rates of private insurers lower than MIGA's prices, making MIGA's product less competitive, partly due to different cost structures.** Among the 73 survey respondents of companies from developed countries for the 2008 MIGA client study, price considerations ranked top among the five most important factors for selecting a PRI provider, followed by the scope/terms of coverage, size of project and country limit, the financial strength of the provider, and insurer reputation. Investors from developing countries had similar responses. As discussed in paragraph 5.8, MIGA's cost structure reflects its mandate as a development institution and its policies, processes, and procedures which are aligned more with the WBG's than with the PRI industry. Average administrative cost represented 80 percent of average net premium income during FY07. While MIGA has made efforts to improve its cost-efficiency, it bears higher costs associated with fulfilling its role as a development institution, as well as related to the provision of complementary services mandated by its Convention (such as disseminating information on FDI and PRI, technical assistance and mediation activities).

6.6. **Alignment, coordination, and collaboration with the WBG has benefits for MIGA but is also associated with transaction costs.** The strategic direction for FY05-08 clearly stated that "MIGA's mission is to promote foreign direct investment (FDI) into

⁶² IEG. *The World Bank Group Guarantee Instruments 1990-2007: An Independent Evaluation*. 2008. (Forthcoming)

developing countries, to promote economic growth, reduce poverty, and improve people's lives." MIGA's underwriting requirements reflect this development mission and partly explain its low claims record but these requirements also prolong the due diligence process. MIGA's deterrence effect, which is valued by investors, comes from its close alignment with WBG's policies, process and procedures but alignment, coordination and collaboration with the WBG have also increased transaction costs for MIGA and the client in recent years. Underwriters and some risk management officers were concerned that such collaboration undermines MIGA's competitiveness.⁶³

MIGA's Potential:

6.7. **MIGA has supported several innovative projects but must ensure that these are replicated to grow business and for development impact.** An example is a FY05 biomass project seeking carbon credits, which MIGA could build upon by offering to assist investors to tap carbon credit offsets for their renewable energy projects. In FY2005, MIGA insured its first private placement in support of a toll-road project, which allowed the project to obtain a single notch rating above the sovereign risk. These are particularly suitable for PPP structures in high risk countries where the project rating needs enhancement to obtain a higher project rating than sovereign risk. It had more success in replicating support for projects involving securitization of mortgage-backed securities (MBS) and accounts receivables. MIGA's eligibility requirement for an equity-linkage also posed a problem for investors in asset-backed securities (ABS). Its experience with the providing coverage under Shariah Laws for a port facility is another first for MIGA which it could build on to support projects with Islamic financing.

6.8. **Within its eligibility criteria, there is some room for MIGA to grow by taking advantage of the space allowed by its Convention and Operational Regulations.** While the Convention and the Operational Regulations specify the eligibility requirements, these documents allow for a range of risks and underlying assets that MIGA could cover (e.g., any tangible or intangible assets with monetary value such as machinery, patents, processes, technical services, and trademarks). Other types of investments can also be covered provided that the Board approves by a special majority under Article 12(b) and MIGA's Operational Regulations Section 1.08. Article 13(c) also allows the Board, through a special majority, to extend eligibility to a national of the host country or to a company which is incorporated in that country.⁶⁴ Although fraught with high procedural hurdles, the Convention and the Operational Regulations also allow the Board, by special majority, to add any other non-commercial risks, including acts of terrorism or kidnapping specifically directed against the guarantee holder to be eligible for coverage except for currency depreciation or events that occurred before contract signing.⁶⁵ A 2008 MIGA market study identified expanding MIGA eligible investments to include the entire portfolio, intellectual property, qualifying MIGA's PRI coverage for favorable regulatory capital treatment under Basel II requirements, sovereign non-

⁶³ IEG-MIGA interviews of underwriters and risk management officers for the *IEG-MIGA 2007 Annual Report*.

⁶⁴ *MIGA Convention*, Article 13(c) includes a proviso that the assets invested must be transferred from outside the host country and that the investor and the host country must jointly apply for Board approval.

⁶⁵ *MIGA Convention*, Article 11(b) and *MIGA Operational Regulations*. Paragraphs 1.53 to 1.57.

honoring guarantee -- which may require only amendments to the Operational Regulations.

6.9. **Updating MIGA's Convention to reflect changes in the global investment environment would improve the Agency's ability to achieve its objective of helping foster the flow of FDI to developing countries.** Investment insurance trends and market feedback indicate demand for stand-alone debt coverage, comprehensive non-payment coverage, coverage of existing equity and acquisitions which all requires changes in the Convention. Flexibility in the guarantee contracts' terms and conditions was also identified in a 2008 MIGA market study as a constraint, which requires a change in the Operational Regulations or the Convention. In the long run, MIGA's business growth and relevance would depend in part on amending the Convention to provide it with more flexibility to react to the demand for coverages in support of projects where the Agency can add value.⁶⁶

6.10. **The emergence of new investors from developing countries (south-south investors) provides MIGA with an opportunity to increase its activities in this growing market segment.** FDI flows among developing countries are now growing more rapidly than investments from developed countries. While MIGA has made strides in supporting south-south investments (paragraph 5.17), there are several member countries whose nationals have not taken advantage of what the Agency can offer. A business development or shareholder relationship plan could cultivate business links with MIGA shareholders in developing countries, who could be potential new clients given the lack of national insurance agencies in many of these countries.

6.11. **MIGA has the potential to play an important role and provide additionality in its projects.** In 2006 IEG evaluated a sample of 21 mature MIGA projects⁶⁷ to assess *MIGA's additionality* as an insurer, its role in leveraging and complementing partners, as well as its contribution to its clients, and found that in the majority of projects (18 out of 21) MIGA made important contributions. The high ratings reflect investors' perceptions that MIGA's involvement in many cases was critical for the investments to proceed, or provided comfort to clients entering new markets or new sectors (especially private provision of public infrastructure). MIGA's insurance was particularly crucial for investors in post-conflict countries. In one evaluated project, MIGA provided a tailored product that was not available from private insurers for the term required by the investors, and in six cases, MIGA coverage was a condition for lenders to provide funds. However, MIGA does not always explicitly define the value it adds to a given project. An IEG review of the quality of underwriting of new projects (FY05-FY06) showed that in more than half of the cases MIGA did not define the particular value it brings to the project which would distinguish it from other possible insurance providers.

⁶⁶ IEG-MIGA. *The World Bank Group Guarantee Instruments 1990-2007: An Independent Evaluation*. 2008. (Forthcoming)

⁶⁷ IEG-MIGA. *IEG – MIGA 2006 Annual Report*. May 31, 2006.

Conclusions

6.12. There continues to be a role and demand for MIGA's political risk insurance. MIGA's main strength lies in its ability to underwrite difficult projects in difficult markets, and there is continued demand for traditional PRI as offered by MIGA. However, its business model, product range, and processes need updating, and it needs to address its shortcomings in communicating with clients and more general manage client relationships. There are indications that the potential for MIGA guarantees may increase, given that political risks may increase in the medium term, and due to the emergence of south-south investors.

7. SUMMARY OF FINDINGS AND RECOMMENDATIONS

7.1. MIGA was established to offer political risk insurance and was created with a specific role and narrowly defined product. MIGA has the most mainstreamed, flexible, well-defined and tested guarantee product within the WBG. Its product is the most unbundled of the guarantee instruments within the WBG, allowing clients to purchase exactly what they need. MIGA has been able to enhance its capacity despite limitations imposed by its Convention. MIGA's product is also the most standardized among WBG guarantees, which allows for quick deployment. At a time of an important juncture for MIGA to review its role and strategy, this report evaluated key aspects of the design and implementation of MIGA's FY05-08 Strategic Directions, and results to date.

7.2. ***The Strategy Design:*** The 2005 Strategic Directions were MIGA's first comprehensive exercise to develop a strategic framework and to firmly articulate the Agency's mission as a development institution. The strategy also emphasized MIGA's role as a member of the World Bank Group and its implications for increased alignment and collaboration among the institutions. Its four priorities aligned with WBG strategies.

7.3. The FY05-08 strategy incorporated development, business, and risk management aspects. However, the strategy had weak links between its overall objectives and operational priorities, and planned initiatives, and it did not explicitly link objectives and outcomes with performance measures or resource needs.

7.4. ***Implementation:*** During implementation MIGA has emphasized several aspects of the strategy. There has been a significant departure from its past business model and practice in coordinating and collaborating with the WBG on both the strategy and operational (project) levels to ensure consistency across the WBG, and MIGA has supported more projects jointly with the WB and IFC. While consultations with Bank sector or country staff have been systematic, the relationship with IFC has not shown such a degree of interaction. Coordination is an important way for MIGA to manage risks and to leverage its role in projects, but has also increased the cost to underwrite projects.

7.5. MIGA has improved its risk and finance analytics, and has modified its pricing model to better reflect its current cost structure in pricing. There have also been improvements in the way the Agency assesses the development impact and environmental and social aspects of its projects. Despite considerable progress in project-based adaptation of its product, it has made little progress in more general product development, a focus on the 2005 strategy. MIGA also made improvements in its client relationship management. It has not yet instituted a business development plan, and clear responsibilities and performance incentives for business origination. More efforts are needed to improve performance management, internal reporting, and monitoring to add value to MIGA's development mandate.

7.6. ***Results of the strategy:*** The business volume of new guarantees has increased steadily, but did not reach until FY08 overall targets for the FY05-08 strategy period. During this time, MIGA's market position in the PRI industry declined. The portfolio has been concentrated on areas stated in the strategy, and has in particular increased its

focus on Africa and IDA countries within its frontier markets priority area. There has been continuity in patterns of business volumes among the operational priorities compared with the previous strategy period.

7.7. The Agency has a strong capital base with a solid claims record. However, net premium income from guarantees has declined and although administrative costs have been contained in recent years, the ratio of cost to net income has increased.

7.8. While it is too early to assess the development outcomes of MIGA projects underwritten during the strategy period, the Agency has strengthened the work quality in its projects, such as ensuring better alignment of projects with WBG strategies and policies, and improving project assessments and due diligence during underwriting, which have been found to be associated with outcomes.

7.9. There is a role and demand for MIGA's political risk insurance product, based on key strengths such as its ability to insure difficult projects in difficult markets. MIGA faces some challenges in its operating environment and constraints in its Convention and regulations. It needs to take advantage of the growing demand for risk mitigation instruments and find solutions to address institutional constraints. The Agency has the potential to play an important development role.

Recommendations

In order to i) consolidate its long term viability; ii) ensure the sustainability of recent operational results; and iii) strengthen its development results, MIGA needs to:

1. On MIGA's long-term viability:

a) Develop a new strategic directions framework that carefully considers the external and internal context in which MIGA is involved, the proposed performance dimensions and the linkages between the latter, the expected value to its customers, the necessary changes in internal processes, and the human capital and technological demands of the strategy.

Aspects to be considered include: the potential demand and appetite for risk mitigation products, the agency's market position vis-à-vis other providers of political risk mitigation tools, the changing international market conditions, the effectiveness of delivering guarantee instruments and potential synergies across the World Bank Group, remedies to address institutional and external restrictions imposed by MIGA's Convention, its competitive advantage, potential areas of growth and high development impact, and factors affecting the achievement of the objectives of the FY05-08 strategy. It would need to address the weaknesses of the current strategy by linking objectives, resource allocation, processes, and expected development results.

As part of this strategic exercise MIGA management would need to consider:

- Tackling the issue of administrative costs, as reflected by the increasing ratio administrative costs to net premium income;
- Improving the effectiveness of its business development and client relationship functions; and

- Continuing enhancing the value added and the efficiency of business processes and decision making to ensure impact and cost-efficiency in underwriting.

b) Ensure that the new strategic directions make explicit the link between risk levels, pricing, and financial, operational, and development impact objectives. The strategy should include a portfolio perspective that would consider net guarantee income across risk, financial performance, and development objectives to facilitate decision making and performance monitoring of indicators such as expected income, costs, risk, and development impact. Similarly, MIGA should obtain more accurate unit cost data for underwriting individual guarantees. Finally, it could clarify further its pricing relative to market pricing throughout the insurance business cycle.

c) Ensure that the new strategy identifies the set of performance indicators to track progress in implementation. The strategic exercise needs to include the development of a framework of strategy metrics as well as the further improvements in internal systems for performance measurement, reporting, and monitoring.

2. On the sustainability of MIGA's recent growth:

a) Strengthen systematic support to innovative projects and improve product innovation and internal processes to meet investors' changing risk mitigation needs. The Agency needs to strengthen innovation through systematic support to innovative projects and for new product development and innovation. It should address changes to its eligibility requirements not demanding amendments to the Convention. In the medium term, ensuring MIGA's innovation capability, vital for its relevance and sustainability, may require changes to the Convention.

b) Build on recent developments to improve tracking and management of progress during implementation. MIGA should systematize its recent efforts to develop metrics to monitor progress for improving management decision making, allocating resources to the desired areas of growth and impact, and communicating results to the Board and other stakeholders.

3. On strengthening development results:

Make significant progress in implementing initiatives related to development impact assessment and monitoring, recommended in previous evaluations of the Agency by IEG, including the development of self-evaluation.

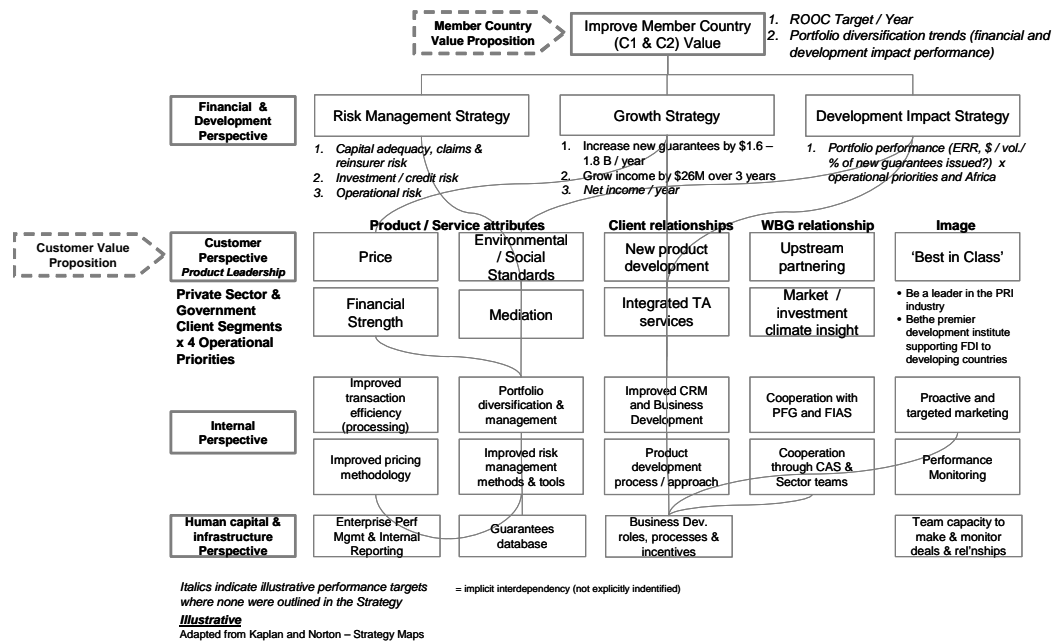
i) The test of a sounder strategic and implementation framework will be in the accomplishment of development results in supporting inclusive and environmentally sustainable growth. In this respect, to ensure that the projects MIGA supports are economically sound and have positive and sustainable development impact, the consistent application of MIGA's development impact assessment guidelines is crucial: it will underscore the Agency's unique role.

ii) Likewise, the Agency should give high priority to continuing the steps it is initiating to implement a monitoring and self-evaluation system that would allow it to gauge, understand, manage, and report the development impact of its interventions.

Annexes

Annex 1: An Illustrative Strategy Map

An Illustrative View of MIGA's 2005-08 Strategy



MIGA's strategy can be mapped to four different perspectives:

- **Financial and Development Perspective:** At the highest level, the strategy would depict MIGA's dual mandate as a development institution and as an insurance agency. MIGA's strategy highlighted a need to enhance its development impact and strengthen its financial sustainability.
- **Customer Perspective:** This perspective would describe components of MIGA's customer value proposition that differentiate it from other providers. In MIGA's case its focus is on product leadership.⁶⁸ MIGA's strategy defined its customer segments as its private sector clients and member country governments. The strategy defined some of the value proposition components for each customer segment by operational priority.
- **Internal Perspective:** The strategy would describe internal capabilities and initiatives needed to deliver MIGA's customer value proposition, and consequently its financial and development impact performance. MIGA's strategy identified initiatives such as product development, coordination and collaboration within the WBG, and improved marketing and business development.

⁶⁸ Kaplan and Norton use Treacy and Wiersema's research (1995) to describe three distinct types of customer value propositions: product leadership, operational effectiveness, and customer intimacy. While most organizations do some of all three, strategically, the customer value proposition is focused on delivering only one.

- ***Human Capital and Infrastructure Perspective:*** This layer reflects how MIGA would use its resources to enable delivery of the other components of the strategy. This would include capabilities and skills, additional staff, and technology applications to support information tracking, analysis, and reporting. MIGA's strategy included a section on 'scaling up the business' which addressed some of these needs.

IEG considers this to be a useful approach to analyze and logically structure a strategy. Further refinements could include more attention to clarifying and defining the performance objectives, defining the 'sub-strategies' and outcomes at each of the 'layers', and analyzing in more detail the interdependencies among initiatives and activities.

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