2003 Report on Operations Evaluation in MIGA

July 11, 2003

Document of the Operations Evaluation Unit (OEU)
Abbreviations and Acronyms

CAO  Compliance Advisor/Ombudsman  
CODE  Committee on Development Effectiveness  
COSO  Committee of Sponsoring Organizations of the Treadway Commission  
CUP  Cooperative Underwriting Program  
DGO  Director General, Operations Evaluation  
EMS  Early Management Screening  
ERM  Enterprise Risk Management  
EVP  Executive Vice President  
FDI  Foreign Direct Investment  
FGPC  Finance and Guarantees Portfolio Committee  
FRR  Financial Rate of Return  
FY  Fiscal Year  
IAD  Internal Audit Department (WBG)  
IDA  International Development Association  
IBRD  International Bank for Reconstruction and Development  
IFC  International Finance Corporation  
IMS  Investment Marketing Services Department (MIGA)  
MDGs  Millennium Development Goals  
MIGA  Multilateral Investment Guarantee Agency  
MIGFR  Finance and Risk Management Department (MIGA)  
MIGPE  Policy and Environment Department (MIGA)  
OED  Operations Evaluation Department (IBRD/IDA)  
OEG  Operations Evaluation Group (IFC)  
OEU  Operations Evaluation Unit (MIGA)  
PRI  Political Risk Insurance  
RAROC  Risk-Adjusted Return on Capital  
RMC  Risk Management Committee  
ROE  Report on Operations Evaluation  
ROW  Risks and Opportunities Workshop (COSO)  
SME  Small and Medium-sized Enterprise  
WBG  World Bank Group (IBRD/IDA, IFC and MIGA)
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1. PURPOSE, SCOPE, AND METHODOLOGY

Purpose and Scope

1.1 This first Report on Operations Evaluation (ROE) in MIGA is presented by the Operations Evaluation Unit (OEU) in discharging its responsibility to report on the evaluation processes in MIGA. The report reviews the quality assurance, monitoring, and evaluation systems in MIGA, and the current strategies, policies, systems, processes, and practices to meet its development mandate while operating as a financially sound institution. It takes stock of what is currently in place, describes new initiatives underway, and identifies areas to be addressed in the future.

Methodology

1.2 This report reviews MIGA’s evaluation processes relative to the achievement of its core objectives of development effectiveness and financial sustainability, with a focus on monitoring and evaluation of development effectiveness. In FY03, new methodological requirements were introduced in MIGA for assessing the developmental impact of new guarantee applications during underwriting. In this context, a sample of FY03 guarantee projects was reviewed to assess the quality of the ex-ante development impact analysis prepared by MIGA during the underwriting of guarantees. The desk review also examined the progress made in applying the new methodology in its first year of application to identify strengths and weaknesses. The sample consisted of 19 projects approved by MIGA’s Board between July 1, 2002 and June 27, 2003. It comprised 53 percent of all projects approved and 65 percent of the maximum aggregate liability approved during that period and is representative across sectors and regions.

1.3 Additionally, OEU reviewed recent reports and audits that analyzed various aspects of MIGA’s operational processes and systems, the results of which are currently being considered by MIGA Management.

1.4 The report is organized as follows. Section 2 summarizes MIGA’s mandate, operating environment, and business model. Section 3 describes the current status of MIGA’s quality assurance, monitoring and evaluation, and risk management systems and policies. It addresses the strategic effectiveness, developmental effectiveness, financial sustainability, and management and performance measurement in MIGA. Section 4 presents the findings of the review of ex-ante development impact assessments during underwriting of MIGA guarantee projects. Section 5 summarizes the report’s findings, makes recommendations for MIGA Management and identifies future work for OEU.

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1 The desk review focused on development effectiveness and did not review the assessments of the projects’ environmental aspects.
2 Documents reviewed include Definitive Applications, Underwriting Papers, and Reports of the President to MIGA’s Board of Directors (“President’s Report”).
2. MIGA’S MANDATE, OPERATING ENVIRONMENT, AND BUSINESS MODEL

Mandate

2.1 MIGA was created in 1988 to promote foreign direct investment (FDI) in developing member countries. MIGA offers political risk guarantees (insurance) to private investors—its main product—as well as providing technical assistance (TA) and advisory services to developing countries, and information dissemination tools and legal and mediation services to both host countries and investors. MIGA’s development mandate derivest from its Convention, which states that MIGA’s objective is to “encourage the flow of investments for productive purposes among member countries and in particular the developing member countries.” The Convention also requires that MIGA satisfy itself that the eligible investments to be guaranteed are “economically sound and contribute to the development of the host country” and that they are “consistent with the declared development objectives and priorities of the host country”. These together form the basis of MIGA’s role for contributing to the development of the host countries, as part of the World Bank Group (WBG). Its developmental mandate sets MIGA apart from most other political risk insurers and has implications for its business model.

Operating Environment

2.2 The long-term success of MIGA depends on its ability to remain financially viable, adaptive, and attractive to clients by offering relevant products cost-effectively to private sector investors. However, unlike most other political risk insurance (PRI) providers, MIGA needs to align its activities closely with the development priorities of the WBG, in its role as a development institution. Sustained support from stakeholders is important for MIGA’s long-term viability and hence, the Agency has to demonstrate to its stakeholders its relevance and contribution to development.

2.3 MIGA’s business environment has been changing rapidly, becoming more volatile in recent years. Following a period of strong growth in the late 1990s, FDI flows to developing countries have declined over the last few years. Reasons included the general slowdown of the global economy, regional economic crises, terrorism and conflict, and disappointing experiences of many private investors during the 1990s, especially in infrastructure (see Figure 1 on trends in FDI flows).

Figure 1. FDI Net Flows to Developing Countries 1992-2002

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3 Article 2 of MIGA’s Convention.
4 Article 12 of MIGA’s Convention.
2.4 These developments also resulted in lower demand for MIGA guarantees—in terms of the volume of new coverage—and increased cancellations of existing guarantees (see Figure 2). On the supply side, private political risk insurers have reduced the tenor (duration) and amounts of coverage, and increased pricing (in part due to the terrorism events of 2001), resulting in a hardening of the insurance market. These changes, which followed a (pre-2001) period of sustained growth in MIGA’s business, have important implications for MIGA’s short-term performance and its strategies to position itself in the political risk insurance market and to remain financially sound.
2.5 MIGA’s TA programs, capacity building tools, and information products and services, which are geared towards helping investment promotion intermediaries in host countries attract FDI for productive purposes, have seen an increase in demand in the wake of lower foreign investment in developing countries.

MIGA’s Business Model

2.6 MIGA’s business model for guarantee activities differs from that of the World Bank and the IFC in important respects. As a provider of political risk guarantees, MIGA is less involved with its clients and the projects it insures than a lender or an equity-holder. It is largely detached from the project once the guarantee is issued and it does not routinely supervise or monitor the projects’ developmental and financial performance. Thus, updated information on the achievement of development objectives is scarce. Normally, MIGA relies on representations from its clients for various aspects of the investments it guarantees (which, if found to be material misrepresentations, could lead to a termination of the guarantee or the rejection of a claim by MIGA). However, MIGA has been monitoring projects it considers environmentally and socially sensitive.

2.7 The nature of MIGA’s interest in a project, as an insurer, also differs from that of a lender or an equity-holder. From an insurer’s perspective, the level of profitability of guaranteed projects is largely the concern of the investor, while MIGA’s concerns are the capacity of guarantee holders to pay premiums, and the Agency’s appropriate management of the risk of potential claims. Currently, MIGA generally relies on investor analyses of the projects’ expected profitability and longer-term viability, as these are considered primary concerns of the investor. However, the viability of investment projects ultimately matters to MIGA because, unlike most political risk insurers, MIGA is
concerned with the existence and sustainability of the long-term development impact of guarantee projects, for which sound financial performance is important.

3. QUALITY ASSURANCE, MONITORING, EVALUATION AND RISK MANAGEMENT

3.1 Over time MIGA has adopted strategic tools, policies, systems, and processes to meet its development mandate and maintain its financial soundness. These help MIGA to balance its developmental and financial goals while staying relevant to both clients and stakeholders.

Strategic Effectiveness

3.2 The most recent documents articulating MIGA’s strategic directions and priorities are the Strategic Focus Paper (1999) and the MIGA Review 2000. The Strategic Focus Paper outlined four guiding principles for MIGA activities to foster investment in developing countries: development impact, financial soundness, client orientation, and partnerships. The MIGA Review 2000 confirmed these principles and stressed that the developmental impact of MIGA’s activities is quintessentially important to fulfilling its mission (see Annex 1). The guiding principles and findings of the MIGA Review 2000 were reiterated in MIGA’s business plan and administrative budget document for FY04.

3.3 Strategic Priorities. The MIGA Review 2000 identified a targeted (“multi-niche”) strategy to deliver significant developmental impact to developing member countries through guarantees and technical assistance. The priority areas of this strategy are:

In guarantees:
- Projects in IDA-eligible countries and African countries;
- Investments related to small- and medium-sized enterprises (SMEs);
- South-South investments; and
- Complex infrastructure projects.

In technical assistance and information services:
- Capacity-building that delivers actual investment flows; and,
- Continued upgrading of knowledge activity through Internet-based services.

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5 This section presents a brief overview. OEU has not reviewed the relevance and efficacy of MIGA’s strategy, or the processes by which the Agency updates and adjusts these strategies.

6 MIGA Review 2000. A periodic review of the Agency’s activities and results “with a view to introducing any changes required to enhance [its] ability to serve its clients” (MIGA Convention Art. 67).
3.4 Progress has been made in priority areas for guarantees over the last three fiscal years.\textsuperscript{7} Tables 1a and 1b show that MIGA’s net exposure in IDA-eligible countries and in Africa increased, and its infrastructure portfolio grew between FY01 and FY03, despite the adverse FDI environment. In FY03, MIGA introduced simplified procedures and pricing indicators for SMEs (in addition to projects in certain other sectors) on a pilot basis.

3.5 Progress made towards the objectives for technical assistance and information services is more difficult to measure as there are no reliable tools to establish causality between technical assistance and information dissemination services and actual investment flows.\textsuperscript{8} MIGA continues to expand its repository of online information resources and to develop new websites in response to client demand. The demand for MIGA’s Internet-based services is evidenced by the number of users, hits, and page views, as well as content partners providing information through these services, all of which increased during FY03.

<table>
<thead>
<tr>
<th>Table 1.a</th>
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<tr>
<td>Share of Cumulative Net Exposure in Priority Areas, FY01-FY03</td>
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</table>

<table>
<thead>
<tr>
<th>As % of net exposure</th>
<th>FY01</th>
<th>FY02</th>
<th>FY03*</th>
</tr>
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<tbody>
<tr>
<td>IDA Countries</td>
<td>29.6</td>
<td>34.8</td>
<td>35.5</td>
</tr>
<tr>
<td>Africa</td>
<td>13.0</td>
<td>17.1</td>
<td>19.8</td>
</tr>
<tr>
<td>Infrastructure</td>
<td>28.8</td>
<td>36.0</td>
<td>36.6</td>
</tr>
</tbody>
</table>

* Figures for FY03 are as of March 2003.

\textsuperscript{7} OEU has not reviewed the classification of projects in priority areas and has not evaluated the underlying definitions for project classifications by MIGA.

\textsuperscript{8} To establish links between investment promotion capacity and actual FDI flows, MIGA is examining recent research and evidence such as “The Effectiveness of Promotion Agencies at Attracting Foreign Direct Investment.” FIAS, January 2003.
Table 1.b
Number of New Projects in Priority Areas, FY01-FY03

<table>
<thead>
<tr>
<th></th>
<th>FY01</th>
<th>FY02</th>
<th>FY03</th>
</tr>
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<tbody>
<tr>
<td>IDA Countries</td>
<td>18</td>
<td>14</td>
<td>18</td>
</tr>
<tr>
<td>Africa</td>
<td>8</td>
<td>9</td>
<td>8</td>
</tr>
<tr>
<td>Infrastructure</td>
<td>11</td>
<td>16</td>
<td>8</td>
</tr>
<tr>
<td>SME</td>
<td>18</td>
<td>11</td>
<td>10</td>
</tr>
<tr>
<td>South-South</td>
<td>8</td>
<td>11</td>
<td>12</td>
</tr>
<tr>
<td>Total new projects</td>
<td>38</td>
<td>31</td>
<td>36</td>
</tr>
</tbody>
</table>

Source: MIGA Underwriting Department

3.6 **Managing Strategic Risks.** The most recent risks and opportunities workshops held in January – February 2003 brought to Management’s attention risks associated with market downturn, relevancy, stakeholder support, strategy, and alignment, and also highlighted the limited progress made in addressing issues raised in previous workshops. In 2003 MIGA, as recommended by the Internal Audit Department (IAD), began preparations to introduce the Enterprise Risk Management framework (ERM) as part of an effort to identify and manage risks and opportunities to achieve its business objectives and aid its strategy work. Furthermore, internal discussions have begun on how MIGA can contribute to the Millennium Development Goals (MDGs). For example, MIGA is exploring ways to expand its support to the private sector in areas (such as water and sanitation) critical for the MDGs.

3.7 While MIGA has pursued the same strategy since 2000, with some modifications through the annual budget document, the next formal periodic review of MIGA’s strategies and activities is due in FY05. Responsibility for strategic work was assigned to a specific unit (Policy and Environment Department, MIGPE) in February 2003, which is expected to take the lead in updating the Agency’s strategy. The internal risks and opportunity workshops indicated staff uncertainty about the strategic direction in MIGA and an expectation for a new strategy—to be prepared in a participatory way and clearly communicated to staff at all levels—which also captures potential synergies between MIGA’s guarantees and TA activities and addresses risks and trade-offs to better respond to new challenges.

**Development Effectiveness**

3.8 Ideally, quality assurance, monitoring, and ex-post evaluation systems complement each other and work together forming a continuous cycle to improve the effectiveness of future operations, as set out in Figure 3. Operational departments are to ensure quality at entry/approval. Systematic monitoring and self-evaluation of the active portfolio (for financial and fiduciary requirements, development impact, and compliance with environmental and social safeguard policies) is to provide management with timely information for early warning and operational actions and strategic decisions.
Information from reviews of quality at entry and from monitoring and supervision, together with the findings of ex-post independent evaluation, then provide a base for accountability and learning. When quality assurance at entry, monitoring, supervision, and self-evaluation systems are well established, the role of independent evaluation could primarily be to verify and validate results of self-evaluations. At the project level, both the World Bank (with OED) and IFC (with OEG) have systems in place addressing the three pillars of the accountability and learning cycle, as depicted in Figure 3. In the absence of systematic monitoring and self-evaluation, as is the case in MIGA, independent evaluation has to play a broader role as the predominant source of lessons of experience.

Figure 3: Accountability and Learning Cycle

3.9 MIGA’s quality assurance, monitoring, supervision, and evaluation systems for development effectiveness have evolved over time, reflecting its business model and thus differing in important ways from those of the World Bank and IFC (in particular with respect to post-approval monitoring and supervision). Initially consisting of modest and informal arrangements, MIGA’s quality assurance, monitoring, and evaluation processes have become more formal, as more components of the accountability and learning cycle have been put in place. While doing so, MIGA has also tried to be cost-effective and maintain the advantages of being a small and less bureaucratic organization. Currently, MIGA does not have in place all the components of the three pillars of this cycle for either guarantees or technical assistance and information services. The independent evaluation pillar has only recently been introduced to fill one important gap, while some other components are either under consideration or remain to be addressed (e.g., more systematic monitoring of project and TA performance).

3.10 **Quality Assurance in the Underwriting Process.** MIGA needs to complete its underwriting process within a short time period in order to respond to clients quickly and
to keep costs down. The main steps for selecting projects, ensuring quality, and managing risks during underwriting include project assessment, country risk assessment, environmental and social safeguards clearance, Risk Management Committee (RMC) review of the guarantee proposal, and review by the EVP before the guarantee is submitted to the President and Board of Directors.

3.11 For guarantee project assessment during underwriting, the investor often prepares and submits to MIGA the financial rate of return (FRR) analysis and additional information needed for describing the potential development impact of the project. In most cases, a project site visit is not carried out during project underwriting. Development impact analysis is conducted by guarantee underwriters as part of the underwriting process based on information from clients and other readily available sources. Country risk assessments provide country context from the perspective of potential risks to be covered by the guarantee (see paragraph 3.25). Project teams typically consist of one or more underwriters, a country risk analyst, a lawyer, a syndications officer when required, and an environmental specialist, but not an economist.

3.12 Ex-ante assessments of guarantee projects inform MIGA decision-making on whether or not to support a guarantee proposal. “De-selected” (or turned down) guarantee applications, and the reasons for de-selecting them, would be an indicator of the robustness of quality assurance/project screening in MIGA. However, there are no systematic records of applications rejected at the initial stages. Guarantee applications de-selected at later stages (e.g., at the Early Management Screening (EMS) stage, which takes place before the receipt of a Definitive Application and before underwriting begins) are being tracked, although it is not always possible to distinguish those de-selected due to developmental impact considerations (including environmental and social aspects) versus those turned down for reasons of underwriting risk. De-selection in late stages of underwriting, i.e., during the RMC review, is very rare.

3.13 **Pre-approval Environmental and Social Safeguard Clearance.** MIGA is required to satisfy itself that the projects it supports are environmentally and socially sound. It assesses projects in terms of its own environmental and social safeguard policies and guidelines as part of the underwriting process. MIGA’s framework for assessing the compliance of its guarantee projects with these policies and guidelines has evolved significantly over time. Prior to adopting its own policies and guidelines, MIGA was subject to World Bank environmental and social policies and guidelines. The

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9 According to its Operational Regulations, as a business standard, MIGA is required to reach a decision on issuing a guarantee within 120 days from the receipt of a Definitive Application.
10 The RMC was established in FY00.
11 MIGA does not have staff specialized in economic and development impact analysis to review guarantee project proposals; similarly, there is no head of an economic unit in the RMC.
12 Information available from MIGA on 17 projects de-selected at the EMS stage since FY01 indicates that the reasons included high underwriting risk levels, sponsor-related issues, deficient policy environment related to the project, and environmental concerns in a few cases, or a combination of these factors.
13 MIGA’s Convention (Art. 12) and MIGA Environmental and Social Review Procedures, paragraph 5.
creation of an in-house environmental unit by MIGA in late 1997 improved the Agency’s capacity to address environmental issues. This unit is responsible for setting up procedures, formulating and revising policies, project environmental assessments, and selective monitoring.\textsuperscript{15} In May 1999, the Board approved MIGA’s own environmental assessment (EA) and disclosure policies and procedures that reflect its business as an investment insurer for the private sector. In May 2002, MIGA’s Board approved the adoption of its own interim issue-specific safeguard policies.\textsuperscript{16}

3.14 MIGA’s website\textsuperscript{17} notes with respect to its safeguards review: “In carrying out its review and evaluation, MIGA considers:

- the project’s ability to comply with the appropriate guidelines found in the World Bank Group’s \textit{Pollution Prevention and Abatement Handbook};
- compliance of the project with host country environmental requirements; and
- consistency of the project with MIGA’s safeguard policies regarding the following specific issues: natural habitats; forestry; pest management; dam safety; projects on international waterways; involuntary resettlement; indigenous peoples; and physical cultural resources.”

3.15 Currently MIGA’s review procedures and the application of its safeguard policies primarily aim at avoidance of environmental and social harm. A December 2002 review of recent MIGA projects by the Compliance Advisor/Ombudsman’s Office (CAO) for compliance with the 1999 Environmental and Social Review Procedures found that MIGA has made “strenuous efforts to consistently adhere to its procedural requirements”.\textsuperscript{18} It also referred to the need for MIGA to “ensure that projects meet MIGA’s commitment to environmentally sustainable and socially responsible projects.”

3.16 \textbf{Post-approval Monitoring, Supervision, and Self-evaluation.} MIGA currently does not have a system to monitor development impacts of its projects during the active guarantee period. The main check points for development impact are therefore the ex-ante assessment at the underwriting stage and the ex-post (independent) evaluation, which takes place when the guarantee is “mature” and still active. While data on anticipated development impacts gathered during underwriting is stored in a database, no

\textsuperscript{15} Shortly after MIGA obtained its in-house environmental expertise, a review of the portfolio was conducted to identify high-risk projects from an environmental and social standpoint, as well as priorities for potential monitoring site visits.
\textsuperscript{16} MIGA has adopted its own versions of eight issue-specific safeguard policies: \textit{Involuntary Resettlement, Indigenous Peoples, Natural Habitats, Safety of Dams, Cultural Property, Projects on International Waterways, Forestry, and Pest Management}.
\textsuperscript{17} In its description of \textit{Framework for Safeguard Policies at MIGA}.
\textsuperscript{18} Compliance Advisor/Ombudsman: Insuring Responsible Investments? A review of the application of MIGA’s Environmental and Social Review Procedures, December 2002. The CAO’s report covered procedural issues such as environmental categorization, variances from policies, identification of environmental and social issues, etc.
systematic and periodic tracking of project performance during the life of a guarantee is undertaken by MIGA. Any follow-up is often limited to safeguard issues (which may cover some development impacts as well), financial obligations of the guarantee holder, and possible claim situations.

3.17 MIGA’s practice has been to follow up with a project only when circumstances warrant it, such as in a pre-claim situation,\(^\text{19}\) when the Agency learns of a potential problem through a variety of sources, or when it receives a complaint from stakeholders, particularly regarding the project’s environmental and social aspects. Since 1998, MIGA has been monitoring\(^\text{20}\) selected projects it considers “sensitive” with regard to compliance with environmental and social safeguard policies. The environmental unit also tracks contractual obligations included in contracts of guarantee for compliance with safeguard policies. It periodically provides a list of active projects considered to be sensitive to the CAO’s office for an informal briefing, including monitoring information of active projects when available. While the criteria used for identifying sensitive projects and the required steps for follow-up and mitigation are not spelled out as part of MIGA’s operational procedures, CAO briefings indicate that MIGA informally considers certain criteria to determine the list of sensitive projects. MIGA visits a small number of these sensitive projects each year and also uses information available from partners and clients.

3.18 As part of a FY03 evaluation of MIGA activities in extractive industries,\(^\text{21}\) OEU reviewed the consistency of a sample of extractive industry projects with MIGA’s environmental and social safeguard policies. One of the findings was that 73 percent of projects were substantially consistent with policies at the time of approval, and that consistency improved to 88 percent while projects were under implementation. The review identified weaknesses in the application of social safeguard policies, consultation and disclosure, and monitoring requirements. OEU recommended that MIGA should add value to projects by providing proactive environmental and social advice in the post approval stage, and that it should strengthen systematic monitoring to ensure compliance with policies.

3.19 Apart from environmental monitoring described above, there are no other general monitoring or supervision activities to systematically track the performance of the guarantee projects in its portfolio on a regular basis. This makes it difficult for MIGA to know to what extent its projects have fulfilled their development objectives. In recognizing this issue, the *MIGA Review 2000* noted that MIGA should consider designing a performance measurement and evaluation system that would explicitly recognize and reward development impact, and that MIGA’s Underwriting Department would explore a more systematic framework for balancing development impact against risk-taking concerns. During the 2003 COSO workshops, staff also identified the need to

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\(^{19}\) A pre-claim situation refers to an instance where MIGA has been notified of a potential claimable event, however, a formal claim notification has not been filed.

\(^{20}\) Monitoring includes a site visit by a MIGA environmental staff to selected “sensitive” projects to ensure compliance with environmental and social safeguard policies and implementation of action plans identified in the contracts of guarantee.

introduce measures that clearly demonstrate MIGA’s effectiveness in achieving its mission. Currently, no self-evaluation is done when a guarantee expires or is terminated or cancelled—such as a “guarantee closing or conclusion note”—to record, however briefly, the results and experiences on key aspects, i.e., with respect to MIGA’s finances, value added, or developmental impact.\textsuperscript{22}

3.20 Independent Ex-Post Evaluation. An independent ex-post evaluation function was introduced in MIGA in FY03. Prior to July 1, 2002, MIGA undertook ex-post evaluation of guarantee projects beginning in 1996,\textsuperscript{23} initially at a modest level within the Guarantees Department, then moving to a separate MIGA unit in FY01. From FY97 through FY02, MIGA undertook ex-post (self-) evaluations of 75 active guarantee projects. To harmonize evaluation standards across the WBG and strengthen the analytical foundation of guarantee project evaluations, MIGA and the DGO jointly prepared a note setting out an evaluation method for MIGA. In FY02, CODE endorsed the new evaluation method described in the Methodological Note as well as a Multi-Year Evaluation Framework: FY03-07, which defined the scope of evaluation work for OEU, including guarantee projects, technical assistance and information services, joint country, sectoral and thematic evaluations, and institutional strategy, efficiency and effectiveness.

3.21 In FY03, OEU assumed the ex-post evaluation function for MIGA. One of OEU’s core responsibilities is to evaluate a sample of mature active guarantee projects each FY.\textsuperscript{24} As noted in the Methodological Note, OEU’s target is to evaluate, during a five-year period, 50 percent of all active guarantees issued between FY96 to FY02. In FY03, OEU evaluated a sample of guarantee projects and will report its findings to the Board in a Report on Development Effectiveness in FY04.

3.22 Technical Assistance and Information Services. MIGA’s technical assistance activities (such as capacity-building for investment promotion intermediaries) are largely demand driven; in this regard MIGA suffers from the common challenge to develop criteria to ensure quality assurance and effective resource allocation for what often prove to be ad-hoc interventions. In FY03, MIGA initiated a self-evaluation of major technical assistance activities and conducted four self-evaluations of completed technical assistance projects to date. It is also tracking the usage of its Web-based information dissemination tools. In FY03 MIGA began to develop a new system to systematically monitor its TA and information services activities. Independent evaluation of these activities by OEU will begin in FY04, complementing the evolving self-evaluation and monitoring framework. To this end, in FY03, OEU began developing an approach for evaluating these heterogeneous services and products. Apart from an external assessment conducted in 1998, there has been no independent evaluation of MIGA TA or information services.

\textsuperscript{22} MIGA’s Underwriting Department keeps an internal list of cancelled guarantees noting the reason for cancellation given by the client.
\textsuperscript{24} A project is considered mature after a minimum of 18 months of operations, or 4 years after guarantee approval. Given cancellations of guarantee contracts and other departures from MIGA’s portfolio prior to the maturity date, any initial cohort of guaranteed projects will shrink over time.
3.23 MIGA’s systems, processes, and organization to manage its financial sustainability as an insurer have evolved as the Agency’s portfolio grew over the last decade. The need for a more integrated risk management framework was identified in the MIGA Review 2000. MIGA introduced COSO in 2000 in order to strengthen its control framework. The most recent (2003) COSO workshops brought to attention several key issues, including risks related to financial sustainability, which included market downturn, relevancy, and strategic alignment. An IAD review of MIGA’s Enterprise Risk Management (ERM) processes conducted in 2002 confirmed that MIGA has established several risk management processes for individual risks, but that there is a general need to strengthen the existing processes and to integrate them into an ERM framework. As recommended by IAD, MIGA is currently considering steps to strengthen its risk governance structure and implement an integrated risk management framework. Specific areas for further focus and strengthening identified by the IAD ERM review were underwriting, liquidity, market, and credit risks.

3.24 **Underwriting Risk and Pricing.** Assessing political risks associated with a project correctly and assigning appropriate risk ratings and pricing are the cornerstones of MIGA’s business as an insurer. MIGA has taken steps in the past several years to improve its risk rating and pricing system. A business process review carried out in FY99, and the subsequent reorganization of the Underwriting Department in FY00, brought substantive changes in the underwriting process. The RMC was introduced and is intended to play a key role in reviewing guarantee proposals, particularly from the underwriting risk perspective. In FY02, the country risk and portfolio management functions were moved from the Underwriting Department to a separate unit (Finance and Risk Management Department, MIGFR), which has made progress in standardizing the risk rating system across countries, enhancing transparency of the risk assessment process.

3.25 At present, MIGFR provides an independent country risk assessment for each guarantee proposal. The country risk assessment methodology has been revised to improve the rigor and consistency of assessments across all countries (see Annex 2). Individual ratings are assigned for each country in each of the political risk dimensions MIGA guarantees (i.e., transfer restriction, expropriation, breach of contract, and war and civil disturbance), which in turn indicate an applicable premium range. Project-specific risk ratings, which may deviate from country ratings, are proposed by the underwriting team to the RMC for discussion and approval. The risk rating and country risk assessment systems (and processes to ensure transparency in assigning risk categories)

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25 Liquidity risk is the risk of defaulting on financial obligations due to inability to liquidate assets or obtain adequate funding. Sub-risks include: claims reserves-risk of not maintaining adequate levels of reserves to cover potential claims; and asset liability management – risk resulting from difference in the maturities or re-pricing dates of assets and liabilities, both on and off the balance sheet. (IAD, MIGA FY03-01).

26 Credit risk to MIGA arises if counterparties – other insurers and companies with which MIGA has reinsurance and coinsurance agreements - fail to make payments of such as premiums or claims when due, and by market players through which MIGA invests its liquid assets portfolio.
are still being fine-tuned. Given the volatile external environment, they also need to be easily updateable to ensure MIGA’s market responsiveness.

3.26 While an individual project’s potential impact on the risk composition of MIGA’s portfolio with regard to country risk is well documented in the underwriting report, some of the analytical tools to review a project’s impact on the overall portfolio—such as estimated revenue from and cost of a potential guarantee, and its implication for MIGA’s provisioning—are not yet in place. A methodology is currently being developed by MIGFR to begin addressing these issues. The overall status of MIGA’s guarantee portfolio and financial position are discussed and reviewed by the Finance and Guarantees Portfolio Committee (FGPC). The FGPC addresses: (i) current and projected guarantee exposure and limits, portfolio composition by sector and by host and investor country; (ii) reinsurance27 levels and associated credit risks of reinsurance partners; (iii) cancellations of guarantee contracts; (iv) use of the Cooperative Underwriting Program (CUP),28 and (v) Board concerns as they may arise.

3.27 Regarding premium ranges and pricing structure, in light of recent developments in the PRI market and premium structures, in FY03 MIGA introduced, on a pilot basis, standardized premiums for certain sectors.29 It is also now working on a new costing/pricing methodology,30 which would enable the easy estimation and updates of portfolio risk, costing, and pricing of guarantees.

3.28 Claims and Provisioning. In MIGA’s history, only one claim of US$15 million was paid, of which US$4.5 million was for MIGA’s own account. The claim has subsequently been repaid by the government of the host country. In FY03, MIGA received a new claim (for US$5 million), which is under consideration. Several other pre-claims were also addressed in the past year (in Africa, Asia, Europe and Central Asia, and Latin America and the Caribbean). The Legal Department (MIGLC) is the focal point for handling claims and the General Counsel chairs the Claims Committee, which is convened as needed.

3.29 Since FY98, MIGA has been using a risk-based provisioning method to establish reserves for potential claims sufficient to cover the present value of estimated future losses, net of estimated future premium income from MIGA’s outstanding guarantee portfolio. MIGA’s claim determination process follows several steps, which are reflected in the current provisioning method.31 In FY03, MIGA began developing a new

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27 MIGA uses both treaty reinsurance (specific quotas of each guarantee contract are automatically assumed by reinsurers with which MIGA has concluded reinsurance treaties) and facultative reinsurance (arranging reinsurance for specific deals on an ad-hoc basis).
28 CUP is a form of coinsurance whereby MIGA acts as the insurer of record for other coinsurance partners.
29 Pilot sectors are manufacturing, agribusiness, and services for guarantees up to US$5 million, and SMEs.
30 The methodology will use a Risk-Adjusted Return on Capital (RAROC) based model.
31 The methodology distinguishes between (i) general claims reserves which provide for potential future claims, (ii) specific claims reserves which consist of notified claims, and claims which have been incurred but not yet reported, and (iii) special reserves, under specific claim reserves for contracts in countries that are experiencing heightened risk and for which MIGA Management believes that claim notification may be imminent.
provisioning methodology to address the limitations\textsuperscript{32} of the current method. Since the implementation of the new methodology, and the supporting tools and systems is likely to take some time, MIGA will continue using the current provisioning method in the interim.

**Management and Performance Indicators**

3.30 Given its dual mandate of development effectiveness and financial sustainability, MIGA needs an integrated set of indicators that would support its management in making strategic and operational choices in meeting these goals. Currently MIGA does not have an integrated management information system and much of the information needed for decision-making is provided on an ad-hoc basis. MIGA recognizes the importance of this issue and has allocated resources in the FY04 budget to establish the capacity for providing real-time data on a variety of operational and risk indicators.\textsuperscript{33} A related, important area is the measurement of unit costs of its primary products and services by developing metrics and standards, together with a reliable way to monitor them. Adopting an institutional scorecard was suggested in the *MIGA Review 2000*, to serve as a tool to integrate financial, cost, developmental, and other relevant information for management decision-making, which is still under consideration.

4. **REVIEW OF EX-ANTE DEVELOPMENT IMPACT ANALYSIS**

4.1 OEU analyzed the quality of ex-ante development impact assessments in a desk review of a representative sample of 19 MIGA guarantee projects selected from the 36 approved in FY03 through June 27, 2003.\textsuperscript{34} Of those 36 guarantee projects, 11 were submitted by four investors (each of whom had similar investment projects in different countries). The study included one representative project from each of these investors’ subsets of similar projects. Of the remaining 25 projects (from other investors), 15 were selected on the basis of sectoral and regional representativeness. The sectoral and regional distribution of the 19 projects reviewed is shown in Annex 3.

4.2 Because applications for some of the guarantee projects approved during FY03 originated in the previous fiscal year, only 10 out of 19 sampled projects were subject to the new methodological requirements for assessing the potential development impact of

\textsuperscript{32} One limitation of the current method is the use of a sample of countries and regions, as opposed to the whole portfolio, as the basis for evaluating possible systemic losses for provisioning.

\textsuperscript{33} OEU will begin developing metrics for the evaluation of MIGA’s effectiveness and efficiency, which would build on MIGA’s own measures.

\textsuperscript{34} Excludes seven projects classified as modifications of existing guarantee projects (i.e. prior concurrence) that have been approved by the Board during the same period.
projects. The main objective of this review is therefore to establish a baseline for future OEU evaluations, and to assess the degree to which MIGA already incorporates the new methodological requirements in its ex-ante analysis of development impact.

The New Methodology

4.3 The Methodological Note, agreed by MIGA and the DGO and endorsed by CODE, sets different analytical requirements for assessing: (1) financial sector projects; (2) SME projects and/or south-south investments; and (3) all other projects (i.e., non-financial sector, non-SME, and non-South-South investments). For financial sector projects, which are not subject to FRR calculations, the Methodological Note requires that the project’s ex-ante appraisal should consider the project’s effect on the structure of the financial sector, the resources provided and the resource allocation of the intermediaries supported among other factors. Projects classified as SME and South-South investments would continue to be evaluated under the pre-FY03 methodology unless there is evidence that significant distortions or externalities exist. If such significant distortions or externalities are found, SME and South-South projects would undergo an economic cost-benefit analysis.

4.4 All other guarantee project applications (i.e., for non-financial, non-SME, and non-South-South projects) have more stringent appraisal requirements. The Methodological Note states that for these projects “MIGA will examine the financial rate of return for all prospective Guarantees” and also prepare a tax-adjusted FRR. In those cases where “there is reason to suspect that substantial distortions or externalities might cause the quality of the economic impact to differ from the project’s commercial quality,” an in-depth economic cost-benefit analysis is required. For all non-financial sector projects, MIGA would request from the project sponsors the details of all possible distortions and externalities affecting the project and any subsidies that are being provided by the host government. Once these are identified and quantified and the FRR is determined, the project’s financial flow would be adjusted for taxes paid, which would represent the project’s anticipated quantifiable economic costs and benefits.

4.5 In addition, MIGA would evaluate the development impact for all three categories of projects in terms of the benefits accruing to non-financiers and according to their consistency with the PSD strategy as well as with MIGA’s environmental, health, and social policies. The new methodology (summarized in Figure 4) is applicable to all new Definitive Applications for guarantees received after July 1, 2002.

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SME projects are defined as projects that meets two of the following three criteria: (a) up to 300 employees; (b) total assets of up to US$15 million; and (c) up to US$15 million in annual sales.

In order to be able to investigate the project’s distortions and externalities, MIGA underwriters will receive training and the information provided by the investors will be supplemented by information from the IBRD/IDA, IFC and the IMF.
4.6 **The Sample of Projects.** The sample of 19 projects included 15 non-financial sector projects, of which six were either SME projects, South-South investments, or both. The remaining nine projects, of which five have Definitive Applications submitted after July 1, 2002, required an adjusted FRR and were candidates for an in-depth cost benefit analysis under the new requirements. (See Table 2 for sample composition.)
Table 2: Composition of Sample of Reviewed Projects

<table>
<thead>
<tr>
<th></th>
<th>Definitive Application received Before July 1, 2002</th>
<th>Definitive Application received after July 1, 2002</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Distortions Listed</td>
<td>Distortions Not Listed</td>
<td>Distortions Listed</td>
</tr>
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<td>Non-financial sector, non-SME and/or South-South projects</td>
<td>2</td>
<td>2</td>
<td>3</td>
</tr>
<tr>
<td>Financial sector projects</td>
<td>Not applicable</td>
<td>1*</td>
<td>Not applicable</td>
</tr>
<tr>
<td>SME and South-South projects</td>
<td>4</td>
<td>1**</td>
<td>1</td>
</tr>
<tr>
<td>Total Sample</td>
<td>6</td>
<td>4</td>
<td>4</td>
</tr>
</tbody>
</table>

Note:  Definitive Applications for 9 projects were received before July 1, 2002 (which are not subject to new methodological requirements) and Definitive Application for 10 projects were received after July 1, 2002.

* Financial sector projects are not subject to cost-benefit analysis and do not require an analysis of distortions.

** SMEs and South-South investments are subject to the pre-FY03 methodology if no significant distortions are identified.

Application of the Methodology

4.7 The review found that MIGA assessed the development impact of prospective guarantee projects on the basis of several qualitative and quantitative indicators (such as the number of jobs created, tax revenues, possible demonstration effects, or downstream and upstream linkages). These anticipated impacts are described in the development impact section of the Underwriting Paper and President’s Report (which were reviewed), and separate from the other sections of the document (such as environmental assessment, underwriting structure, and risk assessment). Individual findings for the 19 projects are summarized in Annex 4.37

4.8 OEU identified three good practice examples in the sample in terms of the quality of the ex-ante assessment. The first example had integrated most of the important elements required to adequately assess the project’s financial viability and economic sustainability in the underwriting paper, despite less stringent requirements due to its

37 A control group of six IFC projects approved during the same period, and in similar sectors and regions, was used to compare the scope and quality of ex-ante analysis of development impacts undertaken by MIGA and IFC.
categorization as an SME project and South-South investment and even though the project’s Definitive Application was submitted before July 2002. The second, also a South-South investment project, cogently provided coherent sectoral, economic, and financial analyses, which convincingly argued that the project has sufficient potential development impacts even though the enterprise had been facing short-term financial difficulties. The third good practice example reflected the robust due diligence performed by the underwriters in verifying the project’s financial viability. The sector analysis they provided highlighted the project’s economic contribution. Both the second and third good practice examples were submitted after July 1, 2002 and were therefore covered by the new method.

4.9 Across the 15 non-financial sector projects, FRRs were provided for 14 projects, including the majority of SME and South-South projects. In the reviewed projects MIGA used FRRs and cash flow projections furnished by investors, except in three cases where underwriters differed from those projections—indicating additional in-house analysis and verification. Among the 14 projects for which FRRs were provided, nearly three-quarters did not specify the underlying assumptions used.

4.10 The files did not indicate that MIGA had identified a detailed list of possible distortions and subsidies or solicited such information on a systematic basis from project sponsors. In 10 projects wherein MIGA identified distortions or subsidies, these tended to be limited to tax and import duty exemptions. Trade protection or distortions implicit in concession agreements or government guarantees, especially in the infrastructure or agribusiness projects contained in the sample, were not identified or investigated.

4.11 A detailed economic cost-benefit analysis was not carried out for any of the sampled projects. In five cases (two submitted before, and three after the new methodology was introduced), MIGA provided an adjusted FRR to capture the viability of the investment projects based only on the absence of any tax exemptions or tax holidays received. No adjusted FRRs were calculated for other types of distortions inherent in certain types of projects (e.g., cost recovery and tariff rates for projects with concession agreements with the host country, and trade protection in agribusiness). In none of the cases (including applications received after July 2002) has MIGA calculated an FRR adjusted by payments to the host country governments (taxes and duties), as required by the Methodological Note.

4.12 The Underwriting Paper generally did not discuss (or quantify) the projects’ negative impacts or costs. In cases where such impacts were discussed, this was usually in the context of its environmental impact, or occasionally the project’s risk profile, but such discussions were not integrated into the development impact assessment. The development impact section tended to discuss the project’s potential benefits without

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38 In the cases of the seven infrastructure and one oil and gas projects reviewed, their potential costs were not measured nor discussed, notwithstanding the host governments’ varying contingent liabilities as part of the concession contracts provided to the project sponsors. For six projects in infrastructure or oil and gas involving concession contracts with the host governments only one included both the agreed wholesale and retail tariff prices, even though tariffs are crucial in determining the financial viability and economic sustainability of infrastructure projects.
noting any potential negative impacts or costs. In the reviewed projects, they could have included lost revenue due to import substitution, implicit or explicit subsidies, possible job losses in privatization projects, relocation/resettlement cost, and losses to local industries as the project enterprise captures additional local market share.

4.13 Sectoral analysis was inadequate in the documents for 10 of the 19 reviewed projects, making it difficult to verify the assumptions underpinning the project’s financial viability. Assessment of investor’s demand projections, investment or marketing plans, and capital expenditure programs were usually not presented even among the sampled projects that involve capacity expansion. Only three projects in the sample incorporated nearly all of the elements listed in the President’s Report and Underwriting Paper format by presenting a concise and coherent market and sector analysis and therefore supported the recommendation that these projects are financially viable.

4.14 The analyses of the three financial sector projects covered by the new methodology—which do not require an FRR/adjusted FRR or cost-benefit analysis—did not adequately reflect sectoral and developmental considerations. The Methodological Note requires that resource allocation policies of the financial intermediaries, the rationale for choice of particular sectors for the intermediaries’ on-lending program, and its impact on the structure of the financial sector must be assessed.

4.15 While impacts on the host country for projects promoting South-South investments were measured, little analysis was done on the benefits that the investor country might gain from the project. Although not required under the new methodology, this is likely to result in under-reporting of developmental impact. Of the six projects that entailed South-South investments, there was only one instance in which some information on the nature of potential benefits accruing to both the host and investor countries was included. The others noted only the macroeconomic benefits to the host country.

4.16 As this review of the quality of ex-ante project assessments shows, the Methodological Note was implemented partially with three good practice examples (among them two exempted projects) that demonstrated the underwriters’ ability to undertake the analysis required under the new method. Areas for greater attention and improvement include: (1) creating a check-list of potential distortions, positive or negative externalities for each sector or type of project, and verifying these items with the project sponsors; (2) undertaking an in-depth cost-benefit analysis for non-exempted projects with distortions beyond taxes paid; (3) conducting economic cost-benefit analysis for SME and South-South investments with significant distortions, especially infrastructure projects and/or projects with concession contracts from the host government; (4) identifying clearly the assumptions used in calculating the FRR and

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39 An example is a financial sector project which did not provide a rationale for choosing a sector experiencing overcapacity and weak performance world-wide for its on-lending activity.
40 In one case, a project was classified as a south-south investment even though it was sponsored by the regional sales headquarters of a multinational corporation, which was registered in the “investor” country but whose shares are 100% foreign-held.
adjusted FRRs; and (5) improving skills to undertake in-depth economic cost-benefit analysis.

5. CONCLUSIONS AND RECOMMENDATIONS

Findings and Conclusions

5.1 MIGA has a dual mandate of development effectiveness and financial sustainability that differentiates it from other insurers. The Agency’s long-term success depends on its ability to remain financially sustainable and to fulfill its development mandate to the satisfaction of its stakeholders, while operating in an increasingly volatile environment. The development mandate sets the Agency apart from other investment insurers, but the nature of its guarantee business also has implications for its business model—which embodies a more detached relationship with its guarantee projects than lenders or equity holders have with their projects. While not a critical issue to MIGA during underwriting, the profitability of guaranteed projects is an important indicator for the sustainability of the development impacts they generate.

5.2 MIGA has adopted strategies, policies, tools, and processes to meet its developmental and financial objectives and has implemented a strategy focusing on promoting investments in priority areas. Recent changes suggest that the Agency’s strategy needs updating. MIGA has identified guiding principles and a targeted strategy to increase foreign investments in priority areas that deliver significant development impact. The Agency has made some progress in achieving those strategic objectives. New strategic initiatives have been embraced more recently. However, MIGA’s rapidly changing external environment, new strategic alignment of the WBG, developments in risk management, and staff concerns about the strategic direction of the Agency point to a need for a new strategy, capturing potential synergies between guarantees and technical assistance activities, to better respond to new challenges.

5.3 MIGA has established some elements of a quality assurance (at entry), monitoring and supervision, and ex-post evaluation cycle. Such a cycle ensures learning and accountability for results during all phases of the life of a project. The quality assurance pillar is well established and structured. There is a lack of economics skills in underwriting teams, and development economics expertise is not well represented in decision-making. Under present practice, development impact analysis is done by underwriters based on information provided by clients. MIGA assesses each candidate project according to its own environmental and social safeguard policies.

5.4 After issuing a guarantee, MIGA does not conduct monitoring and supervision of its projects beyond compliance with safeguard policies. MIGA has no
systematic post-approval monitoring of developmental, financial, or risk aspects of projects; hence, there is little measurement of the achievement of MIGA’s development mandate beyond information provided by clients.

5.5 **MIGA’s independent evaluation function was established in FY03** with a mandate to evaluate ex-post the development effectiveness of MIGA guarantee, technical assistance, advisory, and information dissemination services. OEU’s target is to evaluate 50 percent of active projects guaranteed in FY96-02 by the end of FY07.

5.6 **New initiatives in the area of risk assessments, pricing, and provisioning are underway to strengthen MIGA’s financial sustainability.** Ensuring that MIGA has appropriate tools and processes for assessing its underwriting risks is critical to its financial sustainability. The risk function was reorganized in FY02 and progress has been made in standardizing risk ratings across countries. The Agency will need to continue to update its tools for risk management, implementing the key recommendations made by IAD, consider new developments such as the Enterprise Risk Management framework, and move forward with its systems renewal. Similarly, MIGA has begun to design monitoring tools for its investment marketing activities.

5.7 **MIGA has made only partial progress in implementing the new methodology for appraising the developmental impacts of guarantee projects.** The new methodology was to be implemented for guarantee applications received after July 1, 2002 and called for an economic cost-benefit analysis to be conducted on prospective guarantee projects except those specifically exempted. An OEU desk review found that, while some elements of the new methodology were in place, MIGA had not yet fully implemented some key requirements. The Agency conducted development impact analysis on the basis of quantitative and qualitative indicators, and, in most cases, provided an FRR. The desk review identified three good practice cases, which provided integrated financial, economic, and sector analyses.

5.8 **Financial flows were not adjusted for economic factors; distortions, subsidies, and externalities were not systematically taken into account.** MIGA does not yet routinely request a detailed listing of applicable distortions from its clients at the application stage. While in some cases an analysis of distortions was done, non-tax or non-tariff distortions were often not identified. While some FRRs were adjusted for tax holidays and some sensitivity analysis was done, MIGA has not yet undertaken a detailed cost-benefit analysis in a case where substantial distortions might cause economic benefits to diverge from financial ones. Furthermore, costs or negative impacts were often not captured in the analysis of development impacts.

**Recommendations**
5.9 **Application of new methodology for ex-ante assessments of development impact.** MIGA should apply the new methodological requirements to all guarantee projects in the underwriting process, except where specifically exempted.

- In particular, MIGA needs to identify relevant distortions systematically and analyze their potential impact and implications for a project’s benefits, costs, and overall development impacts, using cost-benefit analysis.
- MIGA should build on current good practices, to improve quality at entry and mainstream the new methodology.

5.10 **In order to strengthen the analytical basis of ex-ante assessments of development impact, MIGA should build capacity in this area,** including by providing training to underwriters in calculating adjusted FRRs, undertaking economic cost-benefit analysis, and integrated/holistic development impact analysis, as envisaged in the Methodological Note.

5.11 **Guarantee Closing Reports.** MIGA should introduce a cost-effective system of “guarantee closing” reporting.

- MIGA staff should prepare a closing note when a guarantee contract ends, either because it expires, is cancelled, or terminated. This note should summarize the achievement of project objectives, lessons learned, and developmental and other impacts for institutional learning, analysis, and accountability, and to aid strategy formulation.
Annex 1

MIGA Review 2000 Guiding Principles

1. Development Impact

- MIGA will seek to increase foreign direct investment flows to developing countries with a view to optimizing its developmental impact through the provision of guarantees and technical services, which complement other activities of the World Bank Group.
- MIGA will continue to ensure that its projects are developmentally and financially sound, and that its portfolio is balanced.
- MIGA will broaden the range of its Investment Marketing Services’ products and deepen the level of its assistance, to ensure that it is moving its clients up the “ladder of effectiveness.”
- MIGA will be more proactive in the Country Assistance Strategy process.

2. Financial Soundness

- MIGA will maintain its financial soundness through prudent underwriting, sound risk management, strong internal controls, and continued portfolio diversification.
- MIGA will improve its financial resilience through the accumulation of reserves and the maintenance of claims-paying liquidity.

3. Client Orientation

- MIGA will be more client-oriented by improving responsiveness to client risk mitigation needs, and streamlining its operations to ensure delivery of its products and services to clients in the most timely way possible.
- MIGA will develop a comprehensive marketing/communication strategy, which entails the collaborative efforts of Guarantees and Technical Assistance.

4. Partnership

- MIGA will seek further partnerships with multicultural development banks, national insurers, private sector entities, civil society and international development agencies.
- MIGA will continue its effective mediation services in investment disputes. MIGA will maintain its reputation both within the investor community and among member countries as an objective mediator.

Annex 2

MIGA Country Risk Assessment Methodology

**MIGA: Country Risk Assessment Methodology**

**COUNTRY REPORT**
"filter", in-depth Background Assessment
(focus on fundamentals of the country)

- Economic Fundamentals & Outlook
- Political System
- Legal System
- Claims History & Experience

**COUNTRY RISK ANALYSIS**
(RMC Annex VI & Rating Opinion)

- Probability of a claim in the next 3-5 years
- Expropriation rating
- Breach of Contract rating
- War & Civil Disturbance rating
- Potential for Recoveries & or Severity of Loss

**RATING COMMITTEE**
- underwriters recommend rating to committee
- all countries rated per risk, using standard comparators and country assessment
- committee comprises of CDG members, consensus based decision making

**NBI FRAMEWORK**
To provide transparent and consistent NBI guidelines to be used as a base for sector underwriters. Work still in progress; NBI database updated and improved; Data is being analyzed
Annex 3

Sectoral and Regional Distribution of the Sample of Reviewed Projects
Sample Size = 19

Sectoral Distribution

- Agriculture: 5.3%
- Infrastructure: 42.0%
- Manufacturing: 5.3%
- Finance: 21.1%
- Oil & Gas: 5.3%
- Others: 21.1%

Regional Distribution

- Africa: 31.6%
- Asia-Pacific: 15.8%
- FSU: 10.5%
- EC Europe: 21.1%
- MENA: 5.3%
- LAC: 15.8%
### Annex 4
#### Review of Consistency of Entry with the New Methodology

<table>
<thead>
<tr>
<th>FY03 Sample Projects</th>
<th>DA Received before or after July 1, 2002?</th>
<th>Financial Sector Project</th>
<th>SME Category</th>
<th>South-South Investment</th>
<th>With FRR</th>
<th>Evidence on file for distortions, externalities, subsidies.</th>
<th>Included adjusted FRR</th>
<th>Sensitivity analysis included or mentioned</th>
<th>Econ cost-benefit analysis for non-SME, non-South-South projects conducted</th>
<th>Economic cost-benefit analysis for SME projects or S-S conducted</th>
<th>Performed required analysis to assess financial sector project</th>
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