



**Jim Yong Kim**  
President

March 23, 2017

**MEMORANDUM TO THE BOARD OF DIRECTORS**  
**Multilateral Investment Guarantee Agency (MIGA)**  
**Strategy & Business Outlook FY18-20**

As the World Bank Group enters on a new phase of development set forth by the Forward Look, one which recognizes and seeks to leverage more than ever before the transformative power of markets and private capital, MIGA's role in de-risking to promote private investment is more critical than ever before.

MIGA recognizes the increasing importance of its guarantees in achieving the World Bank Group's development goals and has sought to match that importance with a commensurate growth in the impact and scale of its offerings as described in its FY18-20 Strategy and Business Outlook. At the core of MIGA's strategy is a re-affirmed commitment to serving the poorest and most vulnerable populations through a focus on projects in IDA and FCS countries, and an expanded emphasis on projects that support climate change mitigation and adaptation.

The previous four years at MIGA were a time of unprecedented development impact. Since FY13, MIGA projects helped to mobilize close to US\$50 billion in private co-financing, which in turn brought power to over 50 million people, transport to over 177 million people and prevented the emission of 3 million metric tons of greenhouse gases. As MIGA expands its emphasis on supporting the most vulnerable through growth in IDA, FCS and climate-related projects, we expect MIGA's development impact to grow over the next 3 years.

To continue on this ambitious trajectory going forward, MIGA's FY18-20 strategy describes four pillars that will be key to growing our development impact: Grow Core Business, Innovate Applications, Create Projects for Impact, and Create Markets. These elements focus on the products, regions and sectors that have been MIGA's foundation while leveraging innovation and enhanced collaboration within the World Bank Group.

MIGA stands at a turning point in its history, when the demand from shareholders for increased development impact through private sector investment has never been greater. I have full confidence that this strategy will serve MIGA, its clients and the World Bank Group well. I look forward to the discussion and endorsement of its proposals.

A blue ink signature of Jim Yong Kim, consisting of several overlapping loops and lines.

Jim Yong Kim





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# **MIGA STRATEGY AND BUSINESS OUTLOOK FY18-20**



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## ACRONYMS AND ABBREVIATIONS

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%	Percent
ADB	Asian Development Bank
AfDB	African Development Bank
AIIB	Asian Infrastructure Investment Bank
BoC	Breach of Contract
BPR	Business Process Review
CSC	Corporate Score Card
CSL	Client Service Leader
CPF	Country Partnership Framework
DEIS	Development Effectiveness Indicator System
EBRD	European Bank for Reconstruction and Development
EC	Economic Capital
EPC	Engineering, procurement, and construction
EVP	Executive Vice President
FCS	Fragile and Conflict-Affected States
FDI	Foreign Direct Investment
FfD	Financing for Development
FY	Fiscal Year
GP	Global Practice
IBRD	International Bank for Reconstruction and Development
ICIEC	Islamic Corporation for the Insurance of Investment and Export Credit
IDA	International Development Association
IEG	Independent Evaluation Group
IFC	International Finance Corporation
IFI	International Financial Institution
IIC	Inter-American Investment Corporation
IsDB	Islamic Development Bank
IT	Information Technology
LEED	Leadership in Energy and Environmental Design
LIC	Low Income Country
LTIP	Long-term Investment Portfolio
MDB	Multi-Lateral Development Bank
MENA	Middle East and North Africa
MGF	MIGA Guarantee Facility
MIC	Middle Income Country
MIGA	Multilateral Investment Guarantee Agency, the “Agency”
NHSFO	Non-Honoring of Sovereign Financial Obligation
NHFO-SOE	Non-Honoring of Financial Obligations of State-Owned Enterprises
OC	Operating Capital

## ACRONYMS AND ABBREVIATIONS

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ODA	Official Development Assistance
OGM	Oil, Gas and Mining
P&P	Policy and Procedure
PPP	Public Private Partnership
PRI	Political Risk Insurance
PSW	Private Sector Window
RCM	Regional Coordination Mechanism
RMF	Risk Mitigation Facility for Infrastructure
SCD	Systematic Country Diagnostics
SDG	Sustainable Development Goals
SOE	State-Owned Enterprise
TTL	Task Team Leader
USD	US Dollars
WBG	World Bank Group



## INTRODUCTION

(i) This document presents MIGA's three year strategy for the period FY18-20. Chapter 1 discusses the external environment and the World Bank Group's response. Chapter 2 examines MIGA's products, business model, and results of the FY15-17 strategy. Chapter 3 considers the context and objectives for MIGA's FY18-20 strategy and the business and financial implications of the new strategy. Chapter 4 provides concluding remarks.

## EXECUTIVE SUMMARY

(ii) MIGA serves as the World Bank Group's risk mitigator, providing investors and lenders in the international investment community with the level of comfort necessary to invest in developing countries through its political risk insurance (PRI) and credit enhancement products.

(iii) MIGA's guarantees create significant development impact from the new cross-border private investments that MIGA facilitates through its de-risking products. Since FY13, MIGA estimates that its guarantees will have contributed to:

- 50+ million people having access to power;
- 177+ million having access to public transportation;
- 3+ million metric tons of CO<sub>2</sub> emission having been avoided;
- SMEs having acquired access to an estimated US\$6.1 billion in finance; and
- local governments having received about US\$ 1.8 billion in taxes and fees.

(iv) Through the disciplined execution of its FY15-17 strategy, MIGA has increased its activities in IDA, FCS and Climate-related finance. Since FY13, MIGA's gross exposure in IDA-eligible countries has grown by nearly 60%. Overall, MIGA's new guarantee issuance has expanded: new issuance in FY16 was 50% higher than in FY13.

(v) In the course of carrying out its FY15-17 strategy, MIGA has expanded and innovated its approach to creating broad development impact, achieving:

- **Expanded development impact where it is needed most** through refocusing PRI issuance on the highest-risk, highest-need environments, as evidenced by a tripling of MIGA's PRI market share in the riskiest countries (CCC and lower credit rating);
- **Direct, targeted contribution to achieving the Sustainable Development Goals**, including efforts in climate change mitigation, economic growth and infrastructure development;
- **Continued collaboration with the broader WBG**, resulting in some of MIGA's most impactful projects, for example a gigawatt-scale power project in Bangladesh, hundreds of kilometers of roadway in Brazil, and clean energy in Zambia; and
- **Significant mobilization of private sector investment, catalyzing six times the Agency's guarantee issuance**, or US\$27.3 billion dollars in private co-financing, in FY16;

- **Year-over-year operational efficiency improvements**, decreasing MIGA's income-to-expense ratio from 71% in FY13 to 52% in FY17H1; and
- **An expansion of MIGA's overall capacity through widened use of reinsurance**, enabling MIGA to do even more by leveraging public and private sector reinsurance to grow MIGA's guarantee capacity by >70% since FY13 thereby allowing greater capital efficiency.

(vi) MIGA's FY18-20 strategy is designed to capitalize on and accelerate these recent achievements to continue to scale MIGA's impact and grow its overall importance. At the center of the new strategy are three elements:

- A re-affirmed focus on the poorest through support for projects in **IDA countries**
- A continuing emphasis on **FCS**, where MIGA has opportunity to have impact where private PRI insurers are unwilling to go, and
- An expanded commitment to **climate change mitigation and adaptation, targeting 28% of new issuance related to climate change mitigation or adaptation in 2020**.

(vii) Understanding that MIGA's impact is correlated with the size of its issuance growth, MIGA aims to continue its ambitious trajectory of expansion, **targeting issuance growth of 40% between FY16 and FY20**. If achieved, MIGA's FY20 issuance would be four-fold what it was ten years prior and more than double what it was in FY13, despite more than five consecutive years of declining emerging market FDI flows. To deliver on these targets, MIGA's FY18-20 strategy has four pillars:

- **Grow core business:** MIGA will enable new investments across sectors and regions through building on past efforts to improve operations and delivery in current segments;
- **Innovate applications:** MIGA will continue to create new ways of using its suite of products to create impact, especially through the use of new vehicles, including the IDA 18 Private Sector Window;
- **Create projects for impact:** MIGA will develop, structure and launch new projects by playing a proactive role early in the pipeline through working with governments, state-owned enterprises, and investors; and
- **Create markets:** MIGA will drive comprehensive country solutions and spur private sector investment and development by working as part of the WBG's Cascade Approach.

## CHAPTER 1: EXTERNAL CONTEXT AND WBG RESPONSE

### EMERGING DEVELOPMENT AGENDA

1. In 2013, the World Bank Group (WBG) laid out its strategy to end extreme poverty by 2020 and to boost shared prosperity in a sustainable manner—collectively referred to as the “twin goals”. The number of people living in poverty was almost 1.1 billion fewer worldwide in 2013 compared with 1990 levels, and the incomes of the poorest people in 60 out of 83 countries reviewed had increased between 2008 and 2013<sup>1</sup>. Nevertheless, an estimated 767 million people remained in extreme poverty in 2013. The gap between the richest 60 percent and poorest 40 percent has widened in 34 countries. In addition, levels of global inequality (between countries) remain high. Further progress is threatened by weakening growth prospects and slowing trade. Climate change, fragility and violence, and pandemics also present systemic risks.

2. These challenges were forefront on the minds of leaders as they signed on to the Sustainable Development Goals (SDGs) in 2015. The SDGs are built on an understanding that sustainable development has economic, social and environmental dimensions; and that progress is fastest when governments, multilateral institutions, civil society and the private sector work in partnership. The WBG has adopted the twin goals and a 15-year Forward Look strategy to guide its efforts toward meeting the SDGs.

3. The WBG is well positioned to support shareholders as they pursue the SDGs. The Global Practices (GPs) – the structures of which closely reflect the SDGs – provide client services in pursuit of the twin goals. Cooperation across the World Bank (WB), the International Finance Corporation (IFC), and the Multilateral Investment Guarantee Agency (MIGA) positions the WBG to forge stronger partnerships for jobs and growth. Internally, priorities in the Forward Look seek to make the WBG better and stronger in serving its shareholders<sup>2</sup>. With its mandate to mobilize private investment, MIGA plays a key role in the WBG’s contributions towards achieving the relevant SDGs and the realization of the 2030 Agenda in both Low Income Countries (LIC) and Middle Income Countries (MIC). The private sector will help achieve development gains through investments in infrastructure, agribusiness, health and education, and access to finance and free up limited public resources to focus on delivery of services.

4. While the architecture of development finance has remained relatively unchanged, the resource landscape has shifted dramatically, calling for a new approach. Private capital flows to LICs and MICs have grown, now far exceeding the Official Development Assistance (ODA), as illustrated in Figure 1 below. Between 1990 and 2015, ODA nearly tripled, from around US\$55 billion to US\$161 billion per annum. Over the same period, net Foreign Direct Investment (FDI) to developing countries grew from US\$21 billion to nearly US\$650 billion, over 30 times 1990 levels. It has become clear that ODA is the scarcer resource, and the large financial costs of meeting the SDGs can only be achieved by leveraging this scarce resource to crowd in private investment. This represents a paradigm shift in development finance. The Multilateral Development Banks (MDBs) are committed to increasing mobilization and catalyzation of private investment as part of the Financing for Development (FfD) agenda to support achievement of the SDGs. This emphasis on mobilizing the private sector is linked to the recognition that public funding alone will never be sufficient to meet investment needs, as well as the fact that the private sector is the primary creator of jobs and growth.

5. Yet in most developing countries, markets are not developed well enough to enable the private sector to reach its full potential in achieving development outcomes. Perceptions of risk are often high,

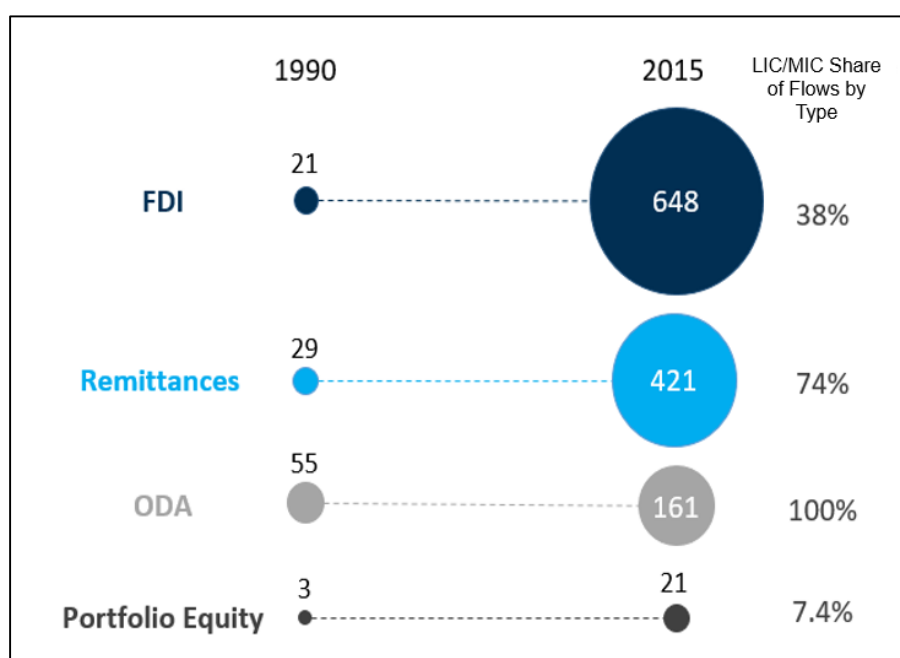
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<sup>1</sup> *Poverty and Shared Prosperity 2016: Taking on Inequality*. World Bank (2016).

<sup>2</sup> A progress report on the Forward Look will be presented to the Board and Governors at the 2017 Spring Meetings.

compounded by a lack of information, transparency, or limited price discovery. Investors have difficulty valuing new opportunities in developing countries, or are unable to price risk adequately. As a result, private capital does not flow at the scale required to meet the needs of the development agenda. In 2015, only 38% of global FDI flows and 7.4% of global portfolio equity flows went to LICs and MICs (see Figure 1). Leveraging the billions of dollars of ODA and private capital to attract the additional trillions of dollars of private sector investment required is an enormous challenge, and has become a core part of the WBG strategy. Attracting private investment will continue to require efforts to create the conditions that are critical for the private sector to thrive, including a business friendly enabling environment, strong institutions and sound regulations that balance public and private interests. Within this context, MIGA's guarantee products serve a valuable de-risking function, allowing the Agency to mobilize private sector investment in challenging environments that are often beyond the risk tolerance of commercial sources of capital.

Figure 1. Capital Resource Flows by Type to Low and Middle Income Countries  
(US\$ billions)



Sources: WB Staff calculations, World Development Indicators. ODA for 2015 represents 2014 actual but is expected to remain stable in 2015

## OPERATIONALIZING THE FORWARD LOOK

6. The Forward Look was endorsed by shareholders in FY17 and sets out how the WBG needs to evolve over the coming 10-15 years in order to meet global challenges. It defines three priority areas of focus to achieve the twin goals – promotion of inclusive and sustainable growth, investing in human capital, and fostering resilience. Implementation of the Forward Look will strengthen the WBG to address these priorities. It also sets out a number of initiatives to ensure the WBG remains fit for purpose including: (i) assisting all client segments, (ii) leading on global issues, (iii) resource mobilization, and (iv) improving the business model.

7. The Forward Look is now in place, serving as a roadmap for the WBG over the next 10-15 years. It is helping to shape a common view among shareholders on how the WBG can reach the twin goals and

support the 2030 development agenda, as influenced by the far-reaching and ambitious SDGs. It also reaffirms the WBG's role in promoting cooperation, integration, connectivity, private investment, trade, and collective action toward shared global goods and in helping member countries manage economic transformation, adopt advancing technologies, and realizing inclusive growth. Achieving the SDGs and implementing the FfD agenda will require global cooperation, including the need to strategically catalyze public and private sector investment to mobilize additional capital, especially private capital.

#### **PARTNERSHIP ACROSS THE WBG THROUGH THE CASCADE**

8. In 2017, the WBG introduced new principles for addressing development challenges and proposing solutions to its clients. Known as the “Cascade”, this hierarchical decision-making structure calls upon WBG staff to work with governments to prioritize private sector solutions wherever possible, expand reform and blended finance to de-risk markets, and crowd in commercial financing where it presents value for money. This will help ensure that scarce public resources, including ODA, are used more strategically, and that private sector investment is maximized.

9. In practice, the starting point for investment decisions under the Cascade approach will be that if a development project or program can be financed on commercial terms without government guarantees while remaining affordable and offering value for money, then that investment is not a priority for concessional or public financing. Where commercial financing is not cost-effective or viable due to perceived risks or market failures (including social or environmental externalities), support will be focused on addressing these through reforms to strengthen country and sector policies, regulations, and institutions, and, where justified, well-targeted subsidies. Where risks remain high and raise the cost of commercial capital beyond that which can be afforded by project or corporate revenue generation, the institution would explore the potential for lowering the financing cost by deploying concessional and public resources in risk-sharing instruments. Finally, where commercial financing is not cost-effective or viable despite sector reform and risk mitigation, public and concessional resources will be applied, including on a commercialized sub-sovereign basis.

10. The Cascade approach involves two key innovations from existing WBG practice. First, it puts an emphasis on “mainstreaming the upstream” with substantially scaled-up efforts at sector and utility reforms, broader governance and budgetary reforms, as well as standardized and wholesale solutions to reduce transaction costs for private investments and create a pipeline of attractive projects. Second, it aims to “shift the default” by deploying scarce public resources to catalyze commercial financing, expanding existing financial instruments to reach new institutional investor capital, and pursuing debt and asset recycling to free up fiscal space for new investments. Operationalizing the Cascade is expected to be a key driver of WBG activities going forward, and will likely place a renewed emphasis on collaboration at every level of the WBG to ensure complementary actions and approaches to the private sector in order to encourage the use of the entire WBG tool-kit to make sure that private sector mobilization is optimized.

11. MIGA will work alongside IBRD/IDA and IFC in helping to operationalize the Cascade. Its guarantee products are a natural fit for the de-risking which is central to the Cascade approach, and its position at the intersection of private and public solutions has given rise to its key role in the Cascade approach. The MIGA guarantee product is especially powerful in expanding the pool of private sector investors in countries or sectors where perceived non-commercial risk are high, especially in IDA and post-conflict countries. Deepening of the cooperation across the WBG and expanding synergies for public reforms and private sector mobilization will be central to maximizing the overall developmental impact of these new principles.

12. Currently focused on infrastructure projects, the Cascade will be piloted within a set of priority countries. It will eventually be expanded to sectors such as finance, education, health and agribusiness. The list of countries is expected to cover a mix of income levels, including FCS, with promising reform and investment conditions.

## **FINANCIAL SUSTAINABILITY**

13. MIGA's strategy depends on a strong World Bank Group. Due to external factors and strong client demand, IBRD and IFC face financial capacity constraints which, if not resolved, could adversely impact performance over the medium-term. At the same time, the success of IDA 18 and MIGA's increase in guarantee capacity leave both IDA and MIGA in strong financial stead to contribute to tackling the ambitious agenda ahead.

14. Notwithstanding the successful implementation of measures to increase revenues and contain expenditures through savings and efficiencies, external factors including a strong demand for IBRD lending and continued low interest rates have resulted in a quicker decline than originally forecast in the Equity to Loan ratio toward the 20% policy minimum. As a result, without remedial measures to further strengthen IBRD's equity capital, the WB will need to scale back lending from around US\$25 billion in FY17 to US\$20 billion and below in FY20 and onward to ensure equity-to-loan ratio stays above the 20% level.

15. The IDA replenishment discussions concluded in December with a US\$75 billion replenishment, 50% higher than IDA17. This will enable IDA to scale up interventions over the next three years, including a doubling of lending to FCS countries, and to support climate change, gender equality, governance and institution building, and jobs and economic transformation. The US\$2.5 billion IDA PSW has been created to scale up private sector involvement.

16. MIGA is managed to be financially self-sustaining. The Agency's activities are supported by a strong capital base and a comprehensive risk management framework. In the context of its statutory underwriting capacity, the Agency is able to support significant amounts of gross exposure and contain risk, through the use of reinsurance, in order to manage net guarantee exposure and the related capital utilization.

17. MIGA's economic capital consumption currently stands at approximately 44%, well within sustainable levels. In order to support MIGA's enhanced reinsurance strategy for prudent capital management and management of concentration risk, MIGA's Board of Directors recently approved an increase in the portfolio reinsurance limit. As a result, MIGA's reinsurance capacity has risen from US\$10.1 billion to US\$33.8 billion as of December 31, 2016. This increase in MIGA's guarantee capacity will allow MIGA to respond effectively to increasing client demand while preserving the Agency's financial sustainability in the context of its growth strategy.

18. MIGA's strong financial position will facilitate its ability to support the goals of the Forward Look and to implement the Cascade approach. Through the IDA PSW, MIGA's existing financial capacity will be supplemented to spur sound investments in the poorest countries through de-risking private sector projects.

## CHAPTER 2: STRATEGIC DIRECTIONS – LAYING THE FOUNDATIONS FOR MIGA2020

### MIGA’S PRODUCTS AND BUSINESS AND FINANCIAL MODEL

19. When MIGA was established in 1988, its original mandate was to extend political risk insurance (PRI) to investments with an equity participation. MIGA’s Operational Policies<sup>3</sup> and Convention changes since 2009 have paved the way for the Agency to expand coverage to lenders such as banks and some capital market investors. These changes have also allowed MIGA to introduce two new credit enhancement products: non-honoring of sovereign financial obligations (NHSFO) in 2010 and non-honoring of financial obligations of state-owned enterprises (NHFO-SOE) in 2013 (See Box 1). Through these changes, MIGA has expanded its product line as well as its client base, a source of growth for the Agency.

#### Box 1. Product Offerings

##### TRADITIONAL POLITICAL RISK INSURANCE

- **Transfer restriction and inconvertibility**  
Provides coverage for the risk of inconvertibility of local currency into foreign exchange for transfer outside the host country. Currency depreciation is not covered.
- **Expropriation**  
Protects against losses attributable to measures taken or approved by the host government that deprive the insured of its ownership or control over all or a substantial portion of its investment.
- **War and civil disturbance**  
Covers the risk of damage to, or the destruction or disappearance of, tangible covered assets caused by politically motivated acts of war or civil disturbance in the host country, including revolution, insurrection, coups d’état, sabotage and terrorism.
- **Breach of contract**  
Covers the risk of being unable to obtain or enforce an arbitral or judicial decision recognizing the breach of an obligation by the host government or a state-owned enterprise.

##### NON-HONORING OF FINANCIAL OBLIGATIONS

- **Non-honoring of a sovereign financial obligation (NHSFO)**  
Covers the risk that a sovereign or sub-sovereign fails to honor an unconditional financial payment obligation or guarantee, where the underlying project meets all of MIGA’s eligibility requirements. Unlike MIGA’s breach of contract coverage, this credit enhancement coverage does not require a final arbitral award or court decision as a condition of payment of a claim.
- **Non-honoring of financial obligation by a state-owned enterprise (NHFO-SOE)**  
Covers the risk that a state-owned enterprise fails to honor an unconditional financial payment obligation or guarantee, where the underlying project meets all of MIGA’s eligibility requirements. This coverage does not require a final arbitral award or court decision as a condition of payment of a claim.

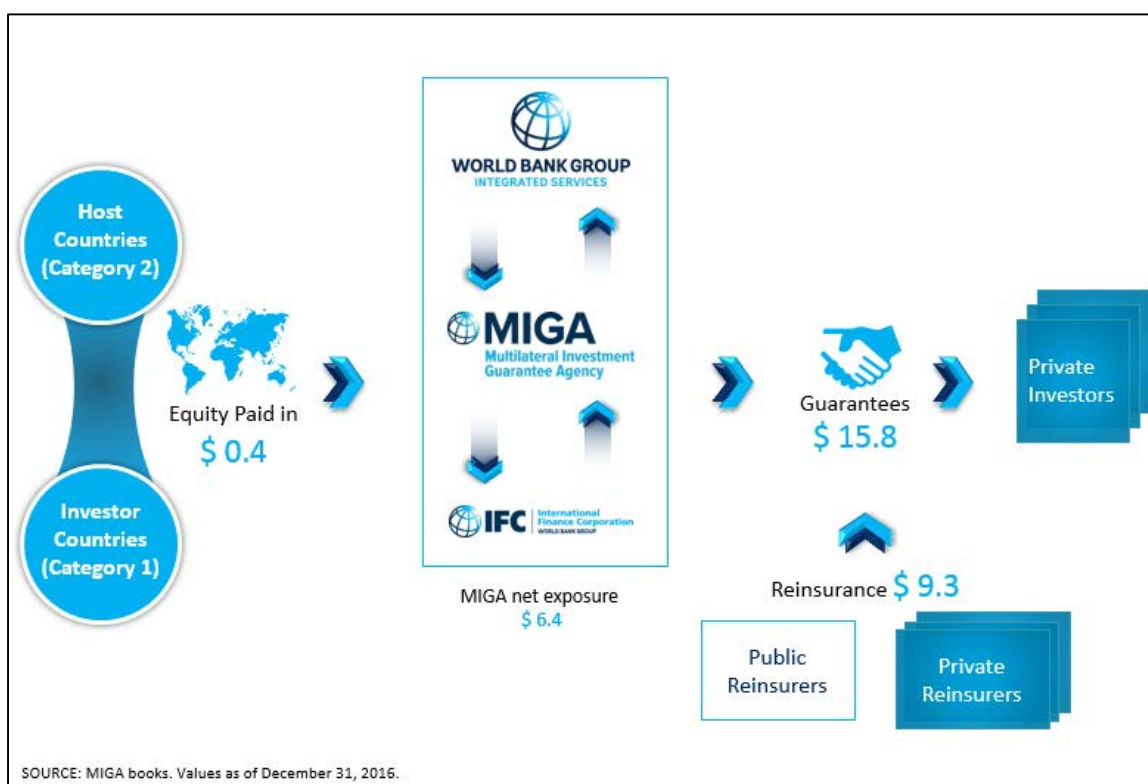
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<sup>3</sup> In FY15, MIGA replaced its Operational Regulations with MIGA’s Operational Policies in conformity with MIGA’s Policy and Procedure Framework approved by MIGA’s Board of Directors in FY13.

## Business Model

20. MIGA's business model leverages the full World Bank Group, along with public and private reinsurers, to multiply the impact of its member countries' investments. As shown in Figure 2, MIGA utilizes prudent operating practices to create billions in guarantees from just a small amount of paid-in equity. As of December 31, 2016, the Agency supported US\$15.8 billion of gross exposure with a paid-in equity capital base of US\$0.4 billion, which translates to a support of \$43 of gross exposure for every \$1 of paid-in equity capital. Coupled with reinsurance capacity, MIGA is able to further leverage its capital base to maximize its development reach. MIGA has expanded its financial capacity by raising its reinsurance and overall guarantee limits. By more than doubling reinsurance levels from US\$4.3 billion in FY13 to US\$9.3 billion in the first half of FY17, along with increasing its guarantee limits, MIGA has been able to increase its guarantees capacity and, by doing so, making more efficient use of its existing capital.

Figure 2. **MIGA's Business Model**  
(US\$ millions)



## Financial Model

21. In fulfilling its mandate, MIGA seeks to operate in a financially sustainable manner by generating sufficient revenue from its guarantee and investment portfolios, to cover its operating and claims-related expenses and contribute to the growth of its capital base.

22. MIGA's business revenue base is represented by net premium income from its guarantee portfolio which is comprised of gross premium income less premium ceded to reinsurers net of ceding commissions and less brokerage costs. Positive operating income, defined as net premium income less administrative expenses, combined with earnings from the investment portfolio and after claim loss

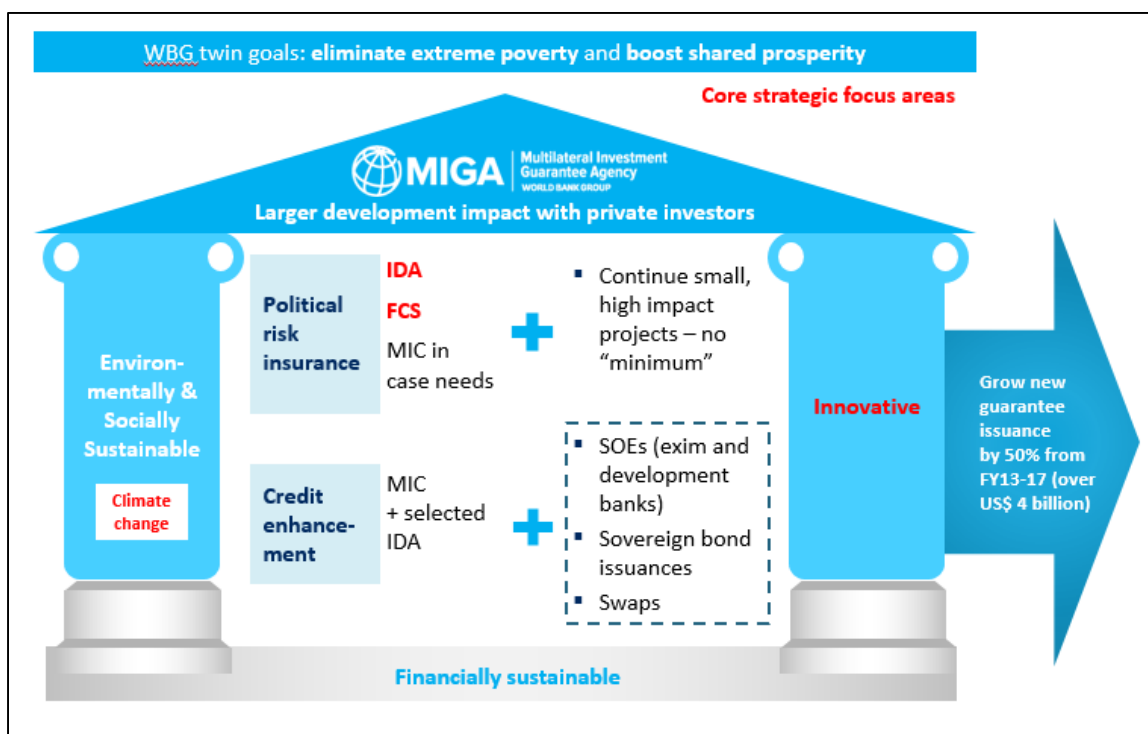


provisioning, has enabled MIGA to increase its capital resources in the form of retained earnings and insurance portfolio reserve to strengthen its ability to support existing and new guarantee exposures.

### MIGA'S FY15-17 STRATEGY

23. MIGA's FY15-17 Strategy laid out the Agency's goal of maximizing development impact by partnering with the WBG to focus on IDA, FCS and climate finance through innovative transactions and supporting projects with higher development impact. With this focus, in seeking to deliver more foreign direct investment to its member countries using its expanded product line and broader client base, the Agency targeted an increase of 50% in annual volume by FY17. See Figure 3.

Figure 3. MIGA's FY15-17 Strategy



24. The implementation plan for attaining these business objectives and attaining a larger development impact were anchored around six change initiatives that MIGA undertook:

- (a) Business Development;
- (b) Non-Honoring Product Management;
- (c) Reinsurance;
- (d) Investment Management;
- (e) Pricing; and
- (f) Operational Effectiveness

## Business Development

25. A key element of implementing its FY15-17 strategy was MIGA's proactive approach to business development. MIGA cultivated closer relationships with client country governments in order to identify key development priorities that these governments would like to see MIGA involved in through PRI (e.g., PPPs) and credit enhancement products. MIGA forged partnerships with governments, conducted targeted outreach, took advantage of the WBG Annual and Spring Meetings and carried out aggressive outreach and mission travel at all levels of the Agency, all with the objective of seeking guidance from governments on their priority sectors and potential projects. By identifying early on the priorities for host governments, MIGA has been more effective in linking this information with potential investors thereby enhancing the impact of the new client-serving model.

26. In parallel, MIGA also engaged actively in the Bank's Regional Coordination Mechanisms (RCMs), Systematic Country Diagnostics (SCDs), and Country Partnership Frameworks (CPFs). Over the past three years, MIGA's input into these WBG documents has become standard procedure, including MIGA EVP approval of all SCDs and CPFs. This is a significant expansion of the earlier notion of selective engagement by MIGA in CPFs. There remains much potential to yield more project opportunities from this process, especially as the Cascade and creating markets go into full swing.

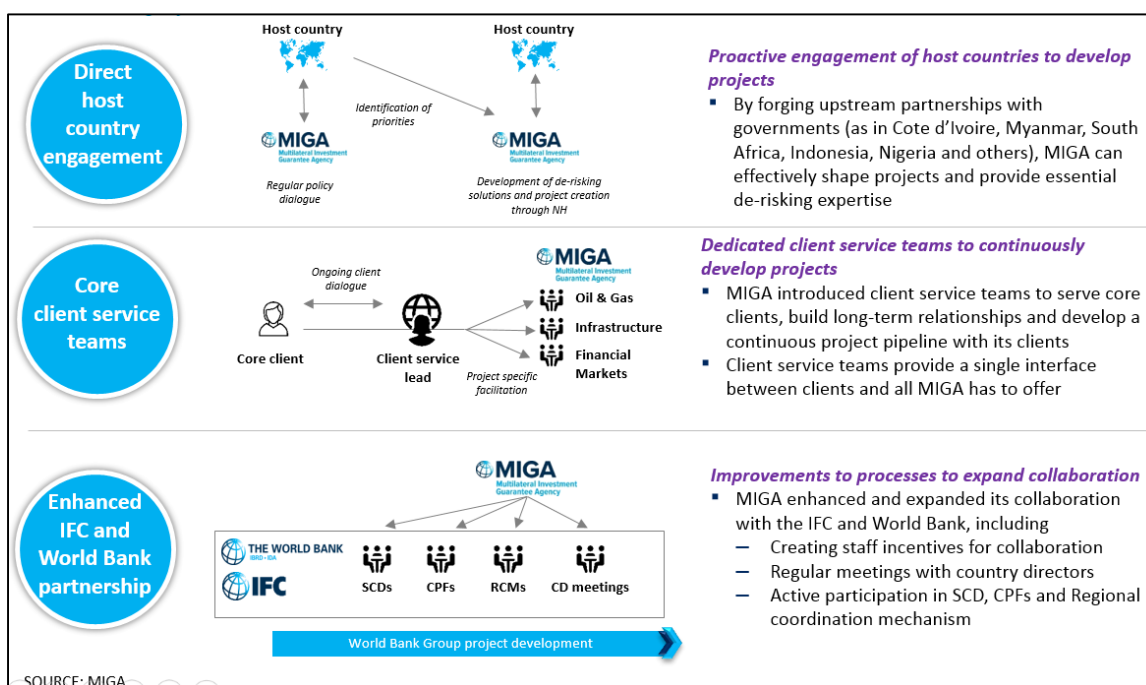
27. MIGA's repeat business was concentrated within a manageable group of top clients, both banks and corporate sponsors, with 15 investors accounting for 70% of gross new guarantee issuance in FY11-13. From this core group, MIGA has cultivated strategic relationships that have helped identify additional areas for collaboration. By assigning small client service teams to support important clients, MIGA's has expanded its role as a client advisor, helping investors prioritize objectives, and guide the direction of the investments to more closely align with MIGA's and WBG's strategic priorities.

28. A Client Service Leader (CSL) model was also designed and launched as part of the FY15-17 implementation plan. The plan called for assigning a CSL to each of MIGA's top clients to serve as the main point of contact and to better understand the client's unique business needs. Under this model, the CSL coordinated all client interaction by MIGA staff, including Management, from both headquarters and the regional hubs, to ensure a consistent message and to leverage the relationship to generate the type of business that is of greatest strategic value to the Agency. The CSL's interface with clients is informed by the results of the country outreach efforts described earlier that allows identification of the opportunities that MIGA should pursue in line with the priorities from the country.

29. In addition, MIGA's business development approach is designed to fully leverage the power of the full World Bank Group. Unlike MIGA, IFC has the scale to maintain a global footprint, with investment officers talking to potential project sponsors and investors around the world. The Agency's agreement with IFC has led to a steadily growing volume of guarantees from clients referred by IFC. The agreement, signed in 2009, revised in 2010 and revised again in 2014, formalizes the relationship for IFC to provide marketing support to MIGA. Under the agreement currently in place, IFC provides two types of support: (1) introduction of new clients to MIGA; and (2) sharing of information on client and project due diligence, credit analysis, and environmental, social and integrity due diligence. In return, MIGA pays IFC a share of the premium income. As of end-December 2016, MIGA has incurred cumulative fees of US\$12.1 million under this agreement since it first went into effect.

30. This enhanced business development through targeted country and client service, combined with enhanced IFC and WB partnership, were designed to expand MIGA's coverage of its country clients. With the achievement of 50% growth from FY13 issuance levels by FY16, and a robust pipeline of future projects, the results showed that these efforts have paid off. These successes have come despite five consecutive years of steady declines in emerging market foreign direct investment – a decline that MIGA expects to continue in the near term.

Figure 4. MIGA's Proactive Business Development Approach



## Non-Honoring Product Management

31. In 2009, MIGA's Board of Directors approved a new cover for non-commercial risks leading to the introduction of a new product line for MIGA: credit enhancement. Through the non-honoring of sovereign financial obligations (NHSFO), MIGA assists credit-worthy sovereigns in reducing their cost of financing when borrowing from cross-border lenders. This product can also be applied to credit worthy municipalities and sub-sovereigns without the requirement of a sovereign guarantee.

32. In 2013, the non-honoring of financial obligations by state-owned enterprises (NHFO-SOE) was introduced which has allowed credit-worthy state owned enterprises to receive MIGA guarantee coverage without the requirement of a sovereign guarantee.

33. Since its introduction, MIGA's credit enhancement products have proven to be very attractive to both investors and country clients. The success of this product can be seen in its increasing share in MIGA's product mix. While NHSFO and NHFO-SOE transactions show strong development impact, from a risk-return assessment, there is an increase in MIGA's economic capital utilization.

34. To manage the risk presented by credit enhancement products, MIGA has put in place enhanced risk management and monitoring procedures. In particular, MIGA has adopted an internal framework which sets internal risk limits and processes, thereby formally articulating the Agency's risk appetite in different rating categories. These risk limits and process framework are relevant both to NHSFO and to the NHFO-SOE product, with the NHFO-SOE limits reflecting the relatively higher risk characteristics of the product compared with the NHSFO product. In addition, given that the NHFO-SOE cover requires a risk assessment framework that combines corporate credit analysis and sovereign support analysis, MIGA has created and staffed a dedicated SOE credit team to conduct this analysis, as well as the monitoring of NHFO-SOE transactions that have been - and will be - added to MIGA's portfolio.

35. MIGA does not yet have experience with claims for its credit enhancement products and has put in place robust mechanisms to monitor countries and manage claims and pre-claims situations through

close collaboration and consultations with the World Bank. Frequent collaboration and exchange of information between MIGA and WB colleagues is allowing MIGA to be aware of those client countries experiencing deteriorating conditions and at higher risk of default. Should a claim situation arise, by virtue of its status as a multilateral development institution and a member of the WBG, MIGA would be in a considerably stronger recovery position compared to private creditors.

### Reinsurance

36. Since 1997, MIGA has successfully used reinsurance to grow its investment guarantee capacity by >70% since FY13, manage the risk profile of its portfolio and foster the growth of the private PRI market. Significant benefits have accrued both to MIGA's investors, who have gained access to larger levels of coverage for projects in developing countries, and to the host countries that have benefited from much higher levels of productive cross-border investment. In order to support the Agency's growth, MIGA has continued to augment its reinsurance programs<sup>4</sup>, by enhancing their capacity to absorb high insurance exposures for longer tenors through the following:

- Seeking new private sector reinsurance partners outside the American and European insurance hubs: MIGA concluded its first reinsurance contract with an Asian private sector reinsurer in FY16 and currently has reinsurance programs with three Asian reinsurers. In Europe and the United States, MIGA added four new reinsurers to its panel.
- Encouraging its private sector reinsurance partners to accept longer tenor projects in challenging markets: whereas up to FY15 private reinsurers would generally not accept tenors beyond 15 years on a facultative basis, MIGA currently has five private sector reinsurers that will offer 20-year facultative capacity. In addition, three companies moved from ten to 15 years and two moved from seven to ten years.
- Where necessary, adjusting reinsurance program structures and terms: MIGA has increased its ceding commission income and augmented the amount of reinsurance capacity provided by its treaty reinsurers without additional restrictions in respect of the application of that capacity.

37. In addition to enhancing its reinsurance programs, MIGA proposed an Exposure Exchange Agreement to IBRD and concluded a pilot exchange in FY16. The agreement helps both institutions to manage their risk more efficiently. IBRD has since expanded this initiative to include other Multilateral Development Banks.

### Investment Management

38. An important component of total net income, investment income has contributed to the growth in MIGA's capital base. MIGA's investment portfolio has produced an average total return of 2.7% over FY11-16 since the implementation of the Long-term Investment Portfolio (LTIP) in FY11. LTIP consisted of U.S. Government bonds with 5-10 year maturities (and global equities, although there are currently none in the portfolio). In recent years, returns have been tracking lower driven mainly by the

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<sup>4</sup> MIGA cedes risks to its reinsurers under both treaty and facultative reinsurance. Under treaty reinsurance, the ceding company and the reinsurer conclude an agreement, usually for periods of one year or longer, which stipulates the conditions under which the ceding company has agreed to cede and the reinsurer has agreed to provide reinsurance for a portion of the ceding company's insurance liabilities, premiums and losses. Facultative reinsurance is concluded on an individual risk basis. While a relationship may exist between the ceding company and the reinsurer, there is no obligation on the part of the ceding company to cede a particular risk and no obligation on the part of the reinsurer to accept a risk when it is offered by the ceding company.

generally lower interest rate environment that has prevailed since the onset of the global financial crisis. During this period, MIGA's short term liquidity holdings earned close to a 0.0% return.

39. MIGA asset holding allocations have remained steady over the last three years with 53% in short-term liquidity (deposits, repos and non-U.S. government and agency bonds), 17% in short-term U.S. Treasuries and 30% in Agency Mortgage Backed Securities – AAA rated US government guaranteed instruments. Given that MIGA's portfolios are passively managed, where the investment holdings track index benchmarks, to the extent the market performs well or suffers decline, MIGA has the same experience as the market benchmark.

40. Over the last two years, MIGA has been examining options to improve the on-going performance of its investment portfolio. Contact with the largest institutional asset management firms has provided MIGA opportunities to benchmark itself against a peer group of reinsurers. MIGA is in the process of concluding its analysis and is considering adjusting its allocation to further diversify its portfolio. MIGA will discuss this with the Audit Committee and provide a review of the Agency's investment policy.

### **Pricing**

41. Premium income is the main driver of MIGA's revenues and retained earnings. With an objective of assuring financial sustainability and additionality, and to strike a balance between premium income and portfolio risk, MIGA follows a "risk plus administrative cost" approach to pricing. The premium rate for each contract of guarantee thus includes components for risk and administrative cost. The pricing model and/or its parameters are reviewed on a regular basis to reflect MIGA's evolving experience and developments in the markets where MIGA is active.

42. The premium components for risk are based on internal country risk assessments for each of the PRI covers (transfer restriction, expropriation, breach of contract, war and civil disturbance) and for NHSFO. Ratings for state-owned enterprises (SOEs) are prepared at the obligor level. As discussed above, MIGA's Finance and Risk Management department created and staffed a dedicated unit with the necessary credit analysis capability to support the NHFO-SOE product. The unit was formed in FY17 Q1 and has been operational since FY17 Q2, informing and supporting MIGA's credit and pricing decisions. Ratings represent a forward-looking estimate of risk in the medium term and feed into MIGA's economic capital and pricing models to determine the premium component for risk, effective for the duration of the contract. Through an integrated risk modeling framework, similar assumptions and parameters are used for pricing as for capital adequacy assessment and portfolio reserving for potential claims losses.

43. The model-based premium rate is a key input to the pricing decision, and is supplemented with market data and other benchmarks where available. The final rates for guarantee contracts are approved by MIGA's Project Review Committee, whereby consideration is given to the PRI market at large and MIGA's strategic positioning, to ensure that pricing is consistent with the Agency's strategic focus areas in terms of host country and product mix.

44. A review of the parameters was undertaken in FY13-14, in conjunction with the development of a new EC model. Given the use of new products as well as changes in the political risk environment, business dynamics and approaches to risk management, a new simulation-based model engine was developed to ensure MIGA employs a flexible model that is appropriate for measuring its risks given current and anticipated future needs. The new EC model has enhanced capability to capture contract structures such as first loss and portfolio coverage, and allows for better flexibility and transparency. The new model and parameters resulted in some changes in the relative differentiation of claims risk levels and risk premiums across MIGA's different cover types and along the rating scale; however, NHSFO and NHFO-SOE covers continue to command higher risk premiums than PRI covers for similar ratings. The new model and parameters were tested in FY15-16, followed by an independent third-party validation

exercise in FY17Q1. Management's final review and sign-off was received in FY17Q2 and the model and parameters were fully implemented as of December 2016.

45. Prior to the implementation of the new economic capital model, MIGA commissioned a review of its pricing mechanics and framework by a consulting firm in FY15. The work was completed in Q1 of FY16. The review found that MIGA's pricing strategy was appropriate and the technical approach sound. In particular, four principles of MIGA's pricing strategy were confirmed and strengthened: (i) facilitating investments for development impact and additionality, (ii) ensuring MIGA's financial sustainability, (iii) clearing the reinsurance market, and (iv) optimization of risk and return for all parties in the transaction. Recommendations included refinement of allocation of administrative expenses and updating of parameters for calculation of risk premiums. A detailed approach to addressing the recommendations was developed and further internal analysis was done by MIGA in FY16. The recommendations from the pricing review for both administrative cost recovery and calculation of risk premiums were fully implemented in FY17 Q2 and focused on (i) adjustments to modeled premium for administrative costs, to ensure that MIGA receives adequate compensation for small projects, guarantees with exposure on standby, and in situations of early cancellations, and (ii) refinements to risk premiums by fully implementing the new EC model and its risk parameters.

### **Operational Effectiveness**

46. MIGA has also made important changes to its operational practices, aimed at generating more development impact with fewer resources and creating a work environment that helps MIGA employees flourish. These efforts were three-fold, (1) improved operational efficiency realized in part through a business process review, (2) closer partnership with the other entities within the WBG, and (3) a multi-pronged effort to enhance staff capabilities and motivation

#### ***Improved operational efficiency***

47. In order to optimize the opportunities presented by its two product lines, improve its ability to respond to its clients quickly, and increase productivity, MIGA initiated a business process review (BPR) in FY15. The BPR focused on the underwriting procedure and key decision points in the process. Based on the analysis, opportunities for greater efficiency and elimination of non-value-adding inputs were identified. This resulted in new procedures that were implemented on a pilot basis in FY16 that helped to streamline the decision-making and approval process for projects.

48. MIGA also focused on identifying ways by which the Agency could reduce its administrative costs. By reducing its footprint at office headquarters through space compression by 20%, MIGA was able to achieve savings in office rental, convert into a more collaborative open space environment, and co-locate with the WBG's PPP practice. Further cost savings were also realized from the WBG-wide expenditure review which resulted in reductions in field benefits and unit travel costs, and a review of shared service arrangements. These savings have, in turn, been redeployed to fund the Agency's operational needs. In addition, MIGA's field presences have been focused on co-location in order to ensure a one WBG-identity and to leverage economies of scale given the relatively small size of MIGA's field-based teams. This commitment towards cost containment, while accompanied by a growing business, has led to a consistent improvement in MIGA's expense to premium income ratio, reducing it by 19 percentage points from 71% of premium income in FY13 to 52% in FY17H1.

#### ***Closer partnership with the other entities within the World Bank Group***

49. For MIGA, collaboration is not just a worthy goal but an operational necessity. MIGA benefits greatly from working in partnership with the IBRD/IDA and IFC because of its comparatively small size<sup>5</sup>

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<sup>5</sup> As of end-December 2016, MIGA's total number of active direct hire staff was 119.

and complementary product offerings. Over the years, as pre-claims issues arise, WBG collaboration has been critical to MIGA's low claim loss ratio. In addition, given MIGA's more limited capacity due to staffing constraints, the MIGA-IFC business development agreement has allowed the Agency to leverage IFC's resources around implementation of environmental and social performance standards in return for a fee paid by MIGA.

50. MIGA also receives support directly from the WB in finding new project opportunities, similar to the origination support the Agency receives from IFC. Both the WB and IFC involve MIGA early in projects where de-risking services may be necessary, allowing MIGA to provide both early advisory services to project stakeholders as well as de-risking services once projects reach the financing stage.

***Multi-pronged effort to enhance staff capabilities and motivation***

51. MIGA has taken several steps with the intent of ensuring that employees are in an environment where they can flourish. The measures include:

- A renewed training program, ensuring that new staff members receive effective training and capability building on an ongoing basis (see Box 2 for more details);
- Launch of a career workshop program, aiding employees in career path planning;
- Revised job titles that better reflect employees' skills and responsibilities;
- The opportunity to participate in strategic development assignments in collaboration with WBG partners, expanding the experiential learning and career opportunities of MIGA employees through rotational assignments in other WBG entities; and
- Work changes for improving the experience of staff stemming from the business process review.

**Box 2. New Training Opportunities for MIGA employees**

Innovation, new staff members and a changing landscape for development finance demand on-going opportunities for MIGA personnel to expand their suite of skills and capabilities. New training opportunities introduced over the last several years include

- A 2-week intense induction program for new hires
- A core credit training program, specifically designed for MIGA in partnership with the University of Virginia
- Multiple new leadership training opportunities
- Chartered Financial Analyst training
- Formal underwriting best-practice exchange program
- Business applications and skills training (Excel, PowerPoint, communications)

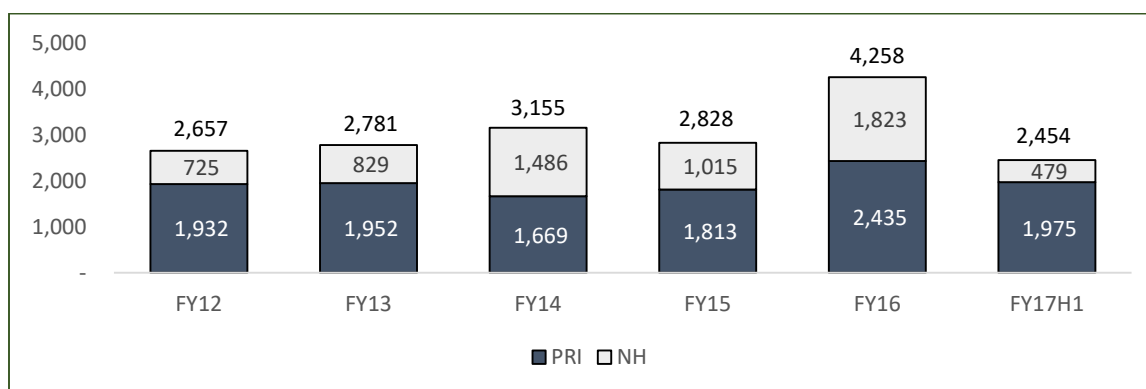
## HISTORICAL TRENDS

### Guarantee Program and Portfolio

52. FDI flows to emerging markets have declined steadily since 2011 and current forecasts project negative FDI growth through 2018 before accelerating in the medium-term. In spite of this, MIGA has been able to meet its FY15-17 aspiration of growing 10% annually and reach its goal of increasing guarantee issuance by 50% from its FY13 level. MIGA has continued to facilitate foreign direct investment into developing countries by tailoring its guarantee products to the unique needs of each project and investor. During the first two years of the FY15-17 strategy period, MIGA issued new business of US\$2.8 billion in FY15 and US\$4.3 billion in FY16, significantly increasing the new business volume compared to US\$2.7 billion issued in FY12. Much of this growth came from the credit enhancement product line, which has generated significant interest from private lenders, governments and investors. During FY17H1, MIGA issued US\$2.5 billion in support of 19 projects, reflecting a growth of 20% over the similar period in the previous fiscal year. MIGA expects to issue new business of US\$4.1 billion by FY17 year-end.

53. The demand for the credit enhancement products continues to grow. New business volumes for credit enhancement products have grown from US\$0.7 billion in FY12 to US\$1.8 billion in FY16. Figure 5 below presents the new business issuance over the past six fiscal years by product type.

Figure 5. New Business Issued by Fiscal Year and by Product  
(US\$ millions)

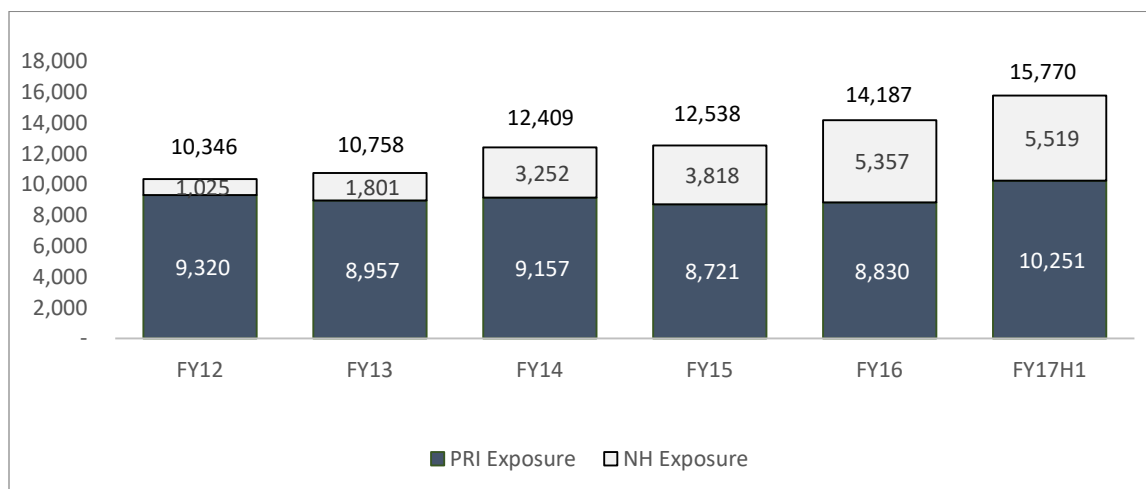


54. MIGA's gross outstanding portfolio has also increased substantially over the FY15-17 strategy period from US\$12.4 billion as of end-FY14 to US\$15.8 billion as of end-FY17H1. The increase in gross outstanding exposure over the period is primarily due to the sustained new business volume achieved over the past three fiscal years i.e., US\$2.8 billion in FY15, US\$4.3 billion in FY16, and US\$2.5 billion in FY17H1, offset by portfolio runoff (inclusive of translation adjustments) of US\$2.7 billion in FY15, US\$2.6 billion in FY16 and US\$0.9 billion in FY17H1.

55. While the credit enhancement or non-honoring product types have a lower share in the gross outstanding portfolio, they have displayed significant growth over the past few fiscal years. This product line's share of the gross outstanding portfolio increased to 35% as of end-FY17H1 when compared to end-FY14's share of 26% and 10% as of end-FY12. **Figure 6** below shows the evolution of the gross outstanding portfolio over the past six fiscal years by product type.



Figure 6. **Gross Outstanding Exposure by Fiscal Year**  
(US\$ millions)



### Priority Areas

56. MIGA's FY15-17 strategy identified IDA-eligible, FCS, innovation, and Climate and Energy Efficiency as priority areas and MIGA has shown over the last few fiscal years a clear commitment and support towards these priority areas.

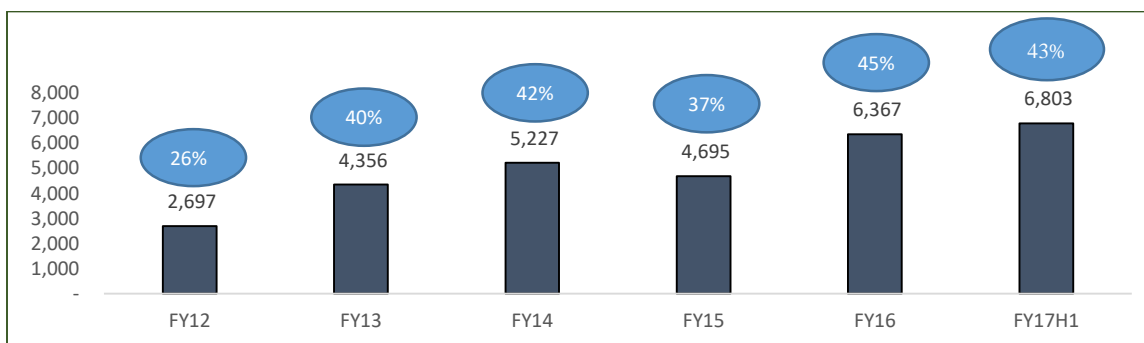
#### *IDA Countries*

57. Promoting investments in IDA-eligible countries is a strategic priority area in MIGA's FY15-17 strategic directions and will remain a priority through its FY18-20 strategic period. MIGA's support of new projects in IDA countries has continuously increased since FY12. During the FY15-17 strategy period, MIGA issued a total of US\$3.7 billion in new business volume to IDA-eligible countries as of end-FY17H1, or 38% of total guarantees issued.

58. As a result of the significant new business volumes written over the FY15-17 strategy period, MIGA's gross outstanding exposure in IDA-eligible countries increased from US\$5.2 billion as of end-FY14 to US\$6.8 billion as of end-FY17H1, representing a US\$1.6 billion increase or 30% (see Figure 7). Despite the overall expansion by 27% of MIGA's outstanding gross portfolio from US\$12.4 billion as of end-FY14 to US\$15.8 billion as of end-FY17H1 and the graduation of certain IDA-eligible countries with large exposures<sup>6</sup>, MIGA has been able to maintain the share of IDA-eligible countries at over a third of the overall portfolio, even increasing slightly from 42% at end-FY14 to 43% in FY17H1.

<sup>6</sup> For instance, MIGA has an outstanding exposure of about US\$400 million in Angola which was IDA-eligible until FY14. MIGA's IDA exposure would be closer to 46% had Angola remained IDA-eligible.

**Figure 7. Gross Outstanding Exposure in IDA-eligible countries**  
(US\$ millions and % of total gross outstanding exposure)

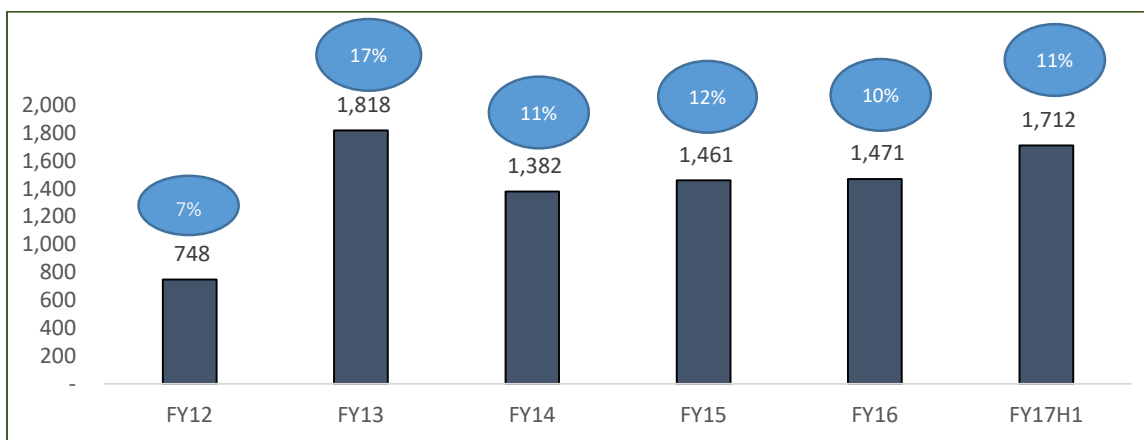


### *Fragile and Conflict-Affected Situations*

59. Support for investments in fragile and conflict-affected situations remains a key priority area for MIGA. Over the FY15-17 strategy period, MIGA's support of projects in FCS totaled US\$0.7 billion. In the first half of FY17, 17% of the US\$2.5 billion of guarantees issued supported investments in fragile and conflict-affected situations.

60. Gross outstanding exposure in FCS countries grew from US\$1.4 billion as of end-FY14 to US\$1.7 billion as of end-FY17H1, representing an increase of US\$0.3 billion or 24% (See Figure 8).

**Figure 8. Gross Outstanding Exposure in FCS**  
(US\$ millions and % of total gross outstanding exposure)



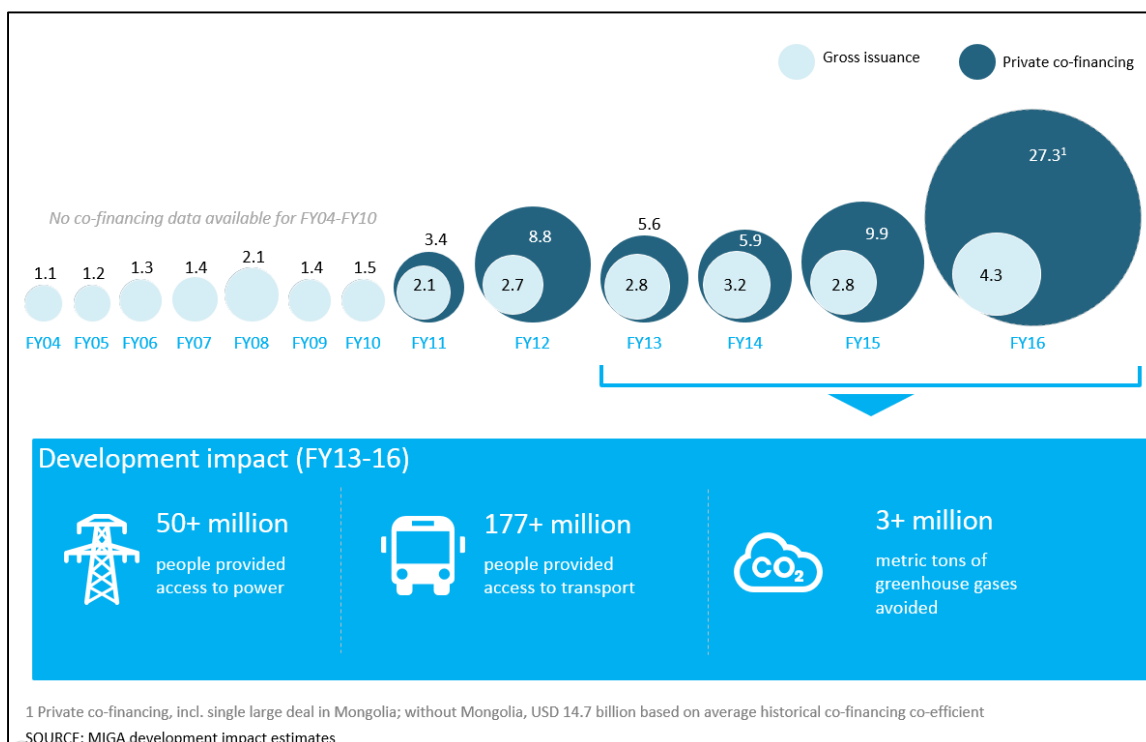
### *Climate Change and Energy Efficiency*

61. MIGA has committed to the WBG's climate change targets of 28% in new business annually by 2020 and continues to focus on projects that contribute to this target. Over the last three fiscal years, gross outstanding exposure has grown substantially. As of end-FY17H1, MIGA supported climate change and energy efficiency projects with an outstanding gross exposure of US\$4.0 billion or 26% of the total gross outstanding exposure.

## DEVELOPMENT RESULTS

62. MIGA's guarantees create significant development impact. By de-risking investments through MIGA's PRI and credit enhancement products, the Agency has facilitated cross border investment that led to transformative development impact beyond the face value of its guarantees (see Figure 9).

Figure 9. **Development Impact Highlights from Investments Mobilized by MIGA**  
(US\$ billions)

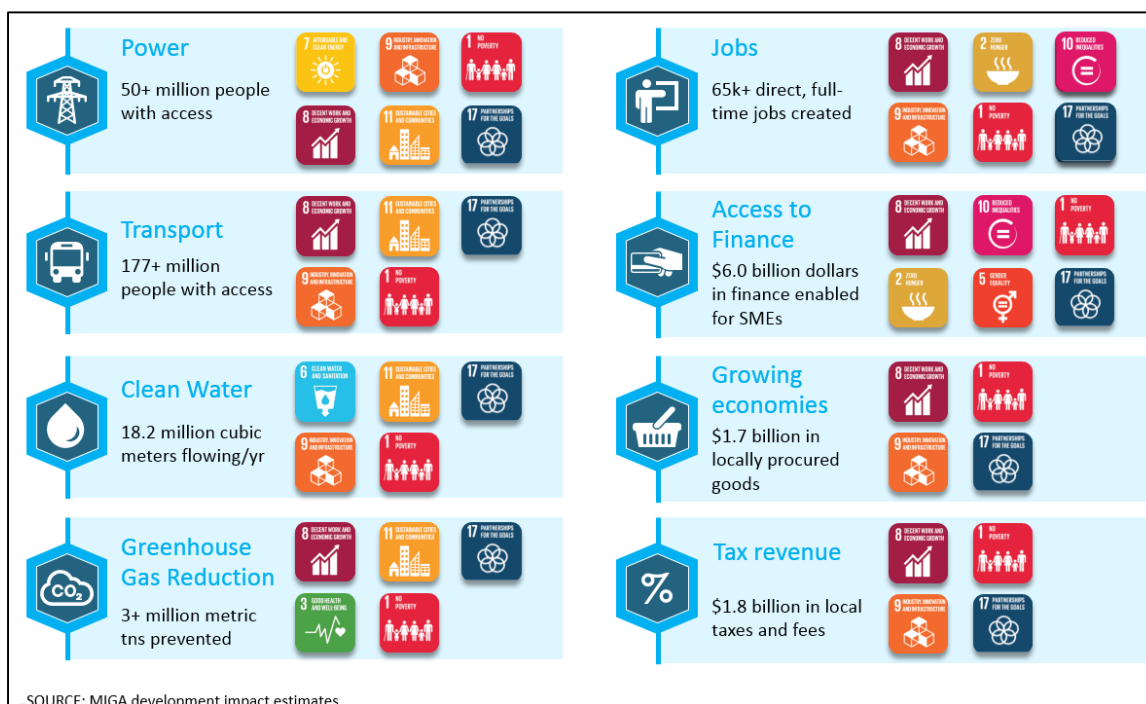


63. Since FY13, MIGA estimates that the gains from its guarantees will have contributed to:

- 50+ million people having access to power;
- 177+ million having access to public transportation;
- 3+ million metric tons of CO<sub>2</sub> emission having been avoided;
- SMEs having acquired access to an estimated US\$6.1 billion in finance; and
- Local governments having received about US\$ 1.8 billion in taxes and fees.

64. More importantly, with 43% of MIGA's gross exposure in IDA countries and 11% in FCS as of the first half of FY17, a significant portion of these developmental gains are expected to benefit people in countries of greatest need. Furthermore, these benefits contribute directly towards helping MIGA's client countries advance towards several SDGs (see Figure 10).

Figure 10. Core Areas of Development Impact, FY13-FY16



## ENHANCING RESULTS MEASUREMENT AND EVALUATION

65. MIGA's efforts in development data gathering through the Development Effectiveness Indicator System (DEIS) has progressed steadily since its launch in 2011. MIGA routinely estimates ex-ante development results from projects supported and then follows up with an annual exercise of collecting actual ex-post results from across the entire portfolio. Collated results data is published through MIGA's website.

66. MIGA continues to seek ways to further improve its results-measurement and evidence system to better reflect the Agency's priorities and demonstrate its impact. MIGA is engaged in dialogues with IFC's VP of Economics and Private Sector Development to learn from their experience and improve the Agency's ex-ante/ex-post development impact framework, especially to assess the market creation contribution of MIGA's projects. MIGA is also engaged with the International Investment Corporation of the Inter-American Development Bank on their development effectiveness learning, tracking, and assessment tools that seek to align country and corporate priorities with project selection and disseminate knowledge and sharing of learning.

67. Since 2008, MIGA has participated in a forum of multilateral and bilateral development institutions to help foster collaboration among IFIs to enhance development impact through common development indicators. The Harmonized Indicators for Private Sector Operations is the first tangible result of this partnership.<sup>7</sup> MIGA ex-post development results data is reported as part of the World Bank Group Scorecard (Tier 2) as well as in MIGA's own Scorecard.

<sup>7</sup> <https://indicators.ifipartnership.org/>

68. MIGA has a robust program of evaluation which provides both an accountability and learning function. Since FY12, all MIGA guarantee projects are evaluated either by MIGA staff, referred to as 'self-evaluations' which are then validated by the World Bank's Independent Evaluation Group (IEG), or by IEG staff. MIGA also participates actively in relevant IEG WBG macro (sector, thematic) and corporate and process evaluations. The success rates of MIGA guarantee projects are reported in the WBG Scorecard (Tier 3) and MIGA's own Scorecard.

69. MIGA has also made progress in nurturing feedback loops between evaluation and learning. IEG's Results and Performance Report 2016 notes that MIGA has consistently used its self-evaluations and validations mechanism in recent years to identify lessons and has used the knowledge gained in its new business reviews through a combination of information systems and knowledge events. Also, IEG's 2016 Report on Self-Evaluation Systems identified MIGA's Seminar series on Learning from Evaluations as good practice within the WBG for learning from evaluation.

### **Corporate Scorecard**

70. MIGA developed its own Corporate Scorecard (CSC) in FY15, fully aligned with WBG, WB, and IFC Scorecards. MIGA's CSC reports on development results, financial sustainability, client satisfaction and workplace metrics. MIGA has actively participated in the CSC discussions with the Board and collaborates closely with WB and IFC to align reporting.

## CHAPTER 3: MIGA’S FY18-20 STRATEGY

### CONTEXT AND OBJECTIVES FOR MIGA’S FY18-20 STRATEGY

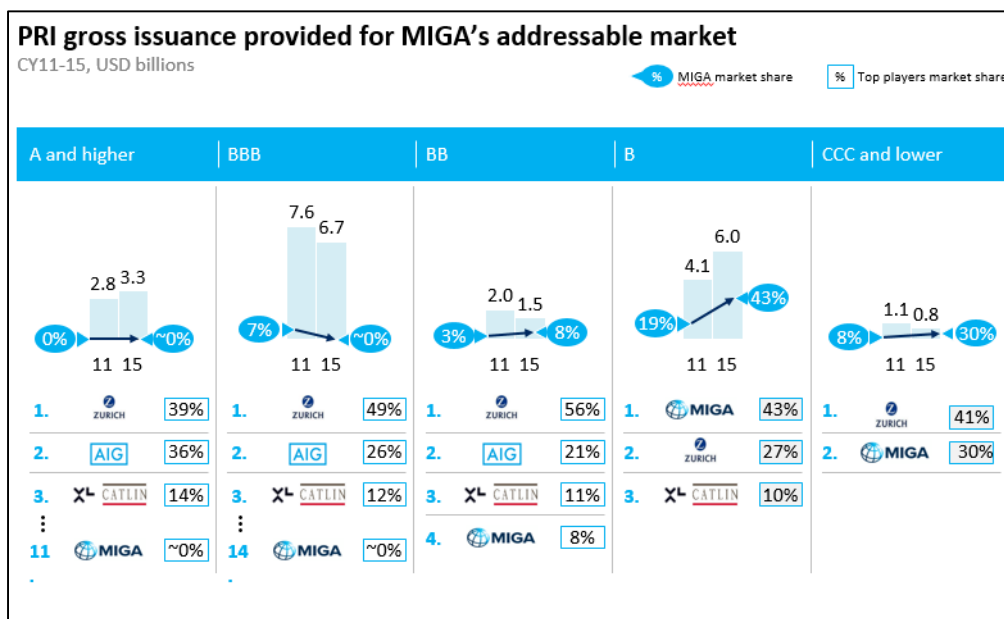
71. The core of MIGA’s objective remains unwaveringly focused on the WBG twin goals: eliminating extreme poverty and boosting shared prosperity.

#### MIGA’s Position in the PRI Market

72. MIGA examines its position in the overall PRI market in order to confirm that it is delivering its products to those markets where the Agency brings greatest value and additionality. Compared to its market position in 2011, MIGA has increased its share in core risk categories (BB and lower). MIGA saw a 24 percentage point increase in the B category rising from 19% market share to 43% of the market placing it as the top PRI provider in this market segment<sup>8</sup>, while reducing its share in categories where the private sector can actively provide financing (BBB and up). Furthermore, MIGA is the second top provider in the CCC and lower rated countries, growing its market share from 8% in 2011 to 30% in 2015 in the addressable market (see Figure 11).

73. The market position of MIGA confirms that the Agency has increased its focus on riskier markets. At the same time, MIGA’s portfolio of PRI business has managed to keep a low claims loss ratio. This is not just a reflection of MIGA’s underwriting standards, but also, and most importantly, MIGA’s access to governments as a member of the WBG, which enhances its ability to facilitate the resolution of investment disputes and help resolve issues that can occur over the duration of the project’s guarantee coverage.

Figure 11. MIGA's Market Position



<sup>8</sup> Market share analysis is conducted on the addressable market which includes IDA, Blend, and IBRD countries except those few countries with an insufficient WBG relationship. It also excludes those segments of the PRI market in these countries that are “captured” by leading state-sponsored PRI providers.

## Weak Investment Outlook for Emerging Markets

74. Investment growth in emerging markets has slowed down significantly since the 2010-2011 period, as highlighted by the WB's Global Economic Prospects (2017). The weakness has been worsened by shocks in the commodities markets, slowing FDI, weak industrial production, depressed domestic demand, rising public and private debt, and growing policy uncertainty.<sup>9</sup>

75. Despite the sluggish FDI levels, MIGA has managed to increase its volume of business by 50% in four years. In the process, MIGA has grown its exposure in IDA and FCS countries—markets that need cross-border investment the most.

76. Although growth prospects vary by region, overall FDI forecasts remain in the negative in the near term. And yet investment needs in many developing economies are large, particularly given sizeable infrastructure and human capital deficits and high unemployment. Macroeconomic factors, such as geopolitical uncertainty and exchange rate volatility will influence future growth. MIGA's strategy is designed around positioning itself where the projects are designed and financing structures are considered, an active role in the context of limited bankable projects.

## World Bank Group Forward Look

77. Over the past three years, MIGA has not only seen greater engagement with the World Bank and IFC but has, in fact, been fully integrated into the Forward Look exercise (see para. 6). This year marks the first time that MIGA has participated in IDA replenishment meetings and, going forward, will be a key implementer as the IDA 18 IFC-MIGA Private Sector Window (PSW) becomes operational.

78. MIGA has focused aggressively on building greater knowledge among WBG staff and management about MIGA's products. With its mandate to mobilize private investment, MIGA plays a key role in the WBG's support for both LICs and MICs. The MIGA guarantee product is especially powerful in expanding the pool of private sector investors in countries or sectors where perceived non-commercial risk is high, especially in IDA and post-conflict countries. De-risking in this manner can mobilize private capital to precisely those areas where investment is needed, while simultaneously allowing scarce public resources, including ODA, to be used more strategically. With almost half of MIGA's portfolio in IDA countries and about 11% in FCS countries, MIGA plays a key role among the WBG's client countries in greatest need.

## MIGA will focus on IDA, FCS, and Climate Finance while building on 4 strategic pillars

79. In order to pursue business issuance in its strategic priority areas of IDA, FCS and climate finance, and grow guarantee issuance by 40% from FY16 to FY20, MIGA will build on the following four pillars:

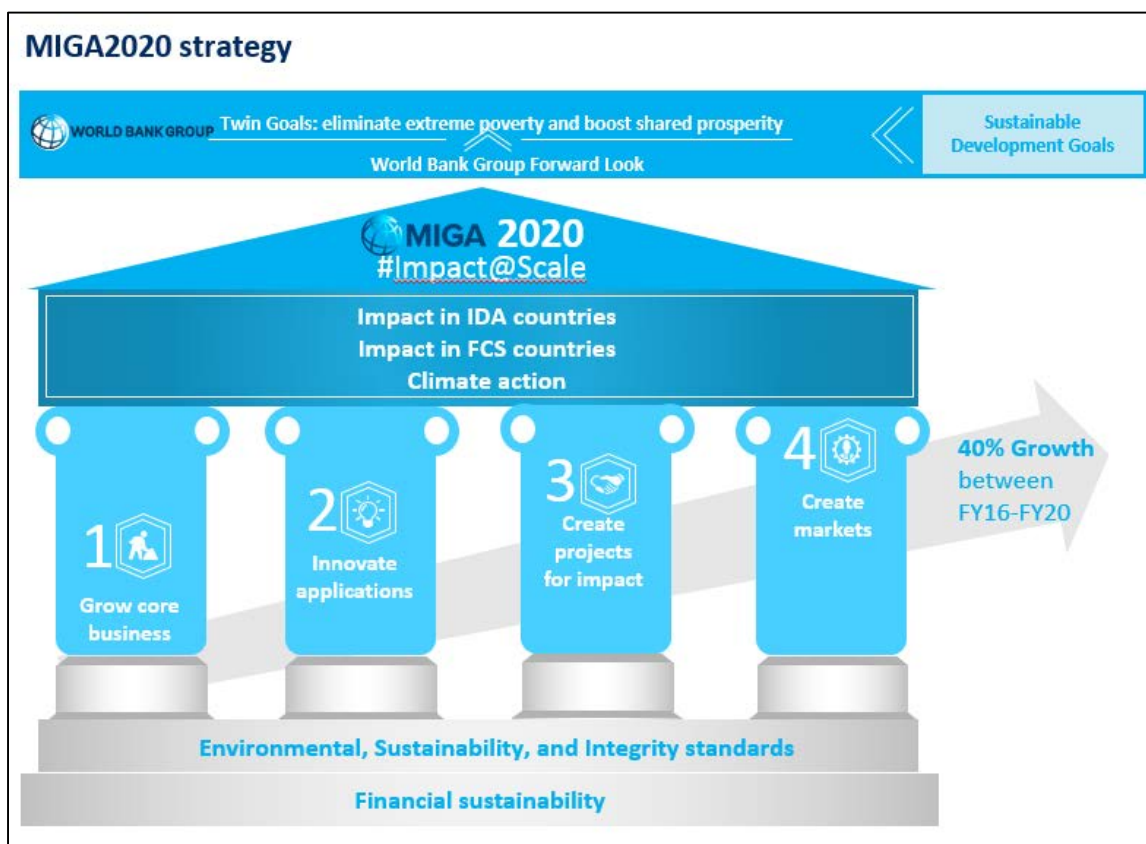
- **Grow core business:** Enable new investments across sectors and regions through building on past efforts to improve operations and delivery in current segments;
- **Innovate applications:** Continue to develop innovative ways of applying its broad suite of products to de-risk development projects and create unique impact, especially through the use of new facilities, including the IDA18 IFC-MIGA PSW;
- **Create projects for impact:** Develop, structure and launch new projects by playing a proactive role early in the pipeline with governments, SOEs and investors; and

<sup>9</sup> Global Economic Prospects: Weak Investment in Uncertain Times. World Bank, December 2016.

- **Create markets:** Drive comprehensive country solutions and spur private sector investment and development by working as part of the World Bank Group.

80. Through this multi-faceted approach, MIGA can enable new opportunities for development impact and drive growth, while maintaining financial sustainability and adhering to the Agency's environmental, social and integrity standards. See Figure 12.

Figure 12. MIGA FY18-20 Strategy



## The Four Pillars

### *First Pillar: Grow Core Business*

81. MIGA will build on the success of its enhanced business development approach, cultivating and nurturing relationships built with top clients and with client country governments to increase the impact and scale of the projects it supports. MIGA will continue to engage at all levels to exchange information on priority projects and expand outreach to those markets that are less familiar with MIGA's products to demonstrate the value in de-risking through the Agency's guarantee products.

82. Internally, MIGA will remain focused on streamlining its processes and ensuring that it is able to respond quickly to client needs. Experience gained from the BPR recommendations and pilot will be used to determine whether more opportunities exist to increase efficiency. Management will also operationalize a new staff organizational configuration that will facilitate deployment of staff between business development functions and underwriting in order to enhance the Agency's agility.



### *Second Pillar: Innovate Applications*

83. In recognition of the key role innovation has played in driving growth and in serving development goals, MIGA has set product application innovation as the second core pillar of its strategy. Despite MIGA's limited product mandate, the Agency has continuously grown and expanded its product offerings and applications. Over the years, MIGA has sought new ways to apply and customize its products to meet the needs of its clients, including through the (i) introduction of the credit enhancement (or non-honoring) product line; (ii) the expansion of the NH product to cover state-owned enterprises to ensure that middle income countries also benefit from MIGA coverage; (iii) application of its products to new types of clients (private equity firms and pension funds); (iv) collaboration with other parts of the WBG (such as IFC, WB units working on guarantee instruments, and PPP) or other international financial institutions (such as ADB, AfDB, AIIB, EBRD, IIC and IsDB-ICIEC).

#### **Box 3. MIGA-EBRD Partnership leads to Innovative Project Elazig Integrated Health Campus PPP**

MIGA's third Turkish Hospital PPP project represents an important milestone in sustainable infrastructure development and provides an example of recent innovation. MIGA and EBRD collaborated to offer the first liquidity-backed political risk insurance for a greenfield project bond, making possible a 288 million Euro long-term project bond issuance to support 1000+ new hospital beds.

**Background & Project Description:** The Elazig Integrated Health Campus is part of Turkey's flagship Health Transformation Programme, a 15+ billion Euro investment plan to deliver ~30 hospital campuses throughout Turkey. Elazig, in Eastern Anatolia, will have a bed capacity of 1,038 and include a general hospital, women's & children's hospital, as well as dental and psychiatric facilities.

**Rationale:** Elazig will be built in a region with limited access to high-quality healthcare services. Given Turkey's long-term infrastructure financing needs, traditional financing sources were unlikely to match Turkey's needs. However, given Turkey's sovereign risk rating (Ba1) and construction risk due to the EPC contractor's credit risk, the bond was unlikely to receive an investment grade credit rating.

**Key Features:** MIGA's support of Elazig has many important and innovative features. (1) MIGA's PRI coverage in conjunction with the EBRD liquidity facility is credited with Moody's promotion of the Elazig bond to investment grade (Baa2), two notches above Turkey's sovereign ceiling. (2) This was facilitated in part by the innovative nature of the risk mitigation structure, with MIGA's BoC cover providing lump sum payment to bond holders following arbitration while EBRD provides interim liquidity allowing for timely debt repayments during arbitration. (3) This innovation, Turkey's first project bond for a PPP and the longest maturity in the Turkish market sets a replicable market benchmark for similar projects elsewhere. (4) It will be constructed with strong local partners who have significant experience and expertise. Finally, (5) The building itself will also be LEED certified, adding a clear climate benefit to MIGA's support for the project and making Elazig Turkey's first "Green and Social" project bond, adhering to Green Bond principles and verified by Vigeo EIRIS.

84. Other examples of MIGA's ability to innovate are through the capital optimization product which allows MIGA's clients to address regulatory requirements and receive capital relief, and PRI for bonds which have led to upgrades in the credit rating of the client's underlying project. Such innovations allow MIGA to do more with its range of products, creating broader development impact while providing more creative solutions for its clients and mobilizing greater private sector investment into developing countries. The investment market for developing economies has changed radically over the last few years, and MIGA has found itself evolving in turn to better serve this market. MIGA will look to cultivate and reward an internal culture of innovation, one where new approaches are encouraged, but also where the evolving needs of the client country are kept in clear focus, even as the global market environment shifts.

85. The new IDA 18 IFC-MIGA PSW will play a key role in enabling the next wave of product application innovation. MIGA expects to make full use of the US\$500 million set aside under the MIGA Guarantee Facility (MGF) of the IDA 18 IFC-MIGA PSW. Over the FY18-20 period, through structures with first loss and risk participation akin to reinsurance, every dollar of MGF resources deployed is expected to result in up to five dollars of private sector investment mobilized and co-financed through MIGA. MIGA has adopted a similar approach before with its donor-supported Conflict Affected and Fragile Economies Facility. In comparison, the level of financing for the MGF is higher and the focus on higher risk markets or higher risk transactions will be great. The MGF will be utilized when existing MIGA PRI instruments are necessary for the project to move forward but there is insufficient MIGA or market capacity to provide the coverage required (e.g., where MIGA has reached exposure limits, or private market capacity does not exist, is insufficient or cost prohibitive). The MGF is expected to be particularly useful in the case of large-scale, systemically important transactions, programmatic approaches to sectors involving multiple projects, or multi-sector approaches.

### ***Third Pillar: Create Projects for Impact***

86. MIGA will leverage relationships with investors, host countries, and other development institutions early in the deal origination process to co-develop catalytic projects and unleash private sector investment to create projects for impact, particularly through its credit enhancement product line.

87. Based on MIGA's recent experience in significantly expanding its business to enhance its development impact, six success factors stand out and will guide MIGA project creation initiatives:

- (a) Early shaping of agenda of investor towards development priorities, and upstream identification of high development impact priorities for investor;
- (b) Broader World Bank Group alignment and strong relationship with government entity or financial institution (e.g., potential past collaboration, and/or major WBG investment);
- (c) Proof of critical country issues that can be solved via MIGA risk mitigation (e.g., client financing gaps aligned with MIGA's priorities and strengths and significant benefit from MIGA pricing and tenor);
- (d) Alignment and collaboration at all levels between MIGA and client on best use of funds, environmental, social and integrity standards;
- (e) Strong government or financial institution support for project (e.g., within strategic sector / citizen service) and high demand for financing; and
- (f) Sufficient credit worthiness of target SOE / sovereign / sub-sovereign to ensure financial sustainability of the project.

### ***Fourth Pillar: Create Markets***

88. There is WBG-wide recognition that growing private sector involvement in development requires an expansion to the pipeline of bankable private sector projects through upstream reforms that address market failures and other constraints to private sector investment. MIGA, like IFC, will work in limited, targeted ways with the WB to drive comprehensive country solutions that can spur private sector investment and development, leveraging its private sector experience to support the WBG's policy reform efforts and institution building in a sub-set of priority countries and sectors. Although MIGA does not have the staff resources to formulate policy prescriptions and provide substantial advisory work, the Agency will participate actively in the broader WBG country diagnostic work to identify country and sector priorities, and play a support role in assessing trends in private sector risk and investment. MIGA

will do this through as-needed participation in the Systematic Country Diagnostic, the development of Country Partnership Frameworks and the creation of Joint Implementation Plans

89. MIGA will also play a pivotal role in the Cascade at the project level as a provider of de-risking solutions when commercial financing and upstream reforms alone are insufficient to engage the private sector. The Agency will work in coordinated ways to ensure that WBG country directors, TTLs, host countries and investors are familiar with the de-risking tools available to clients through MIGA. Through its close contact with WBG and host country personnel in Cascade priority countries and by leveraging its relationships with investors, MIGA will help ensure that its de-risking products play a productive role in bringing private sector involvement to bear in the countries that would benefit from it the most.

## FINANCIAL SUSTAINABILITY

### Capital Usage and Income Outlook FY18-20

90. MIGA's FY18-20 Strategy targets a 40% increase in new guarantees issued by FY20 over FY16 levels. The Agency's financial position can support this activity under normal market conditions. However, if reinsurance capacity becomes limited or unavailable entirely, or if large unexpected claims payouts were to occur, capital utilization could sharply increase and lead to a capital constraint.

91. **Base Case Portfolio Growth and Assumptions.** Growth in MIGA's new business volumes by 40% from FY16 levels forms the base case projection. Total new issuance is projected to be in the range of US\$4.1 billion in FY17, US\$5.0 billion in FY18, US\$5.5 billion in FY19 and US\$6.0 billion in FY20 (see Table 1). Other assumptions include: (i) new business reinsurance levels at 60%<sup>10</sup>; (ii) average premium rates of 0.97% for PRI business and 1.25% for NHSFO; and (iii) runoff: portfolio cancellations at 8% based on long-term averages of FY06-FY16; scheduled repayments estimated at 7%; expiries at 2% of portfolio gross exposure, resulting in total annual runoff at 17% of portfolio gross exposure. The capital utilization ratio, as measured by guarantee portfolio economic capital to net exposure ratio (Guarantee Portfolio EC/NE) for new business is projected at 8.4%.

Table 1. Base Case Financial Data and Key Ratio (US\$ millions)<sup>11</sup>

	FY17 Forecast	FY18 Forecast	FY19 Forecast	FY20 Forecast
Gross New Issuance	4,125	5,038	5,480	5,961
Ending Gross Exposure	16,602	18,598	20,885	23,363
Ending Net Exposure	6,714	7,273	8,263	9,323
Gross Premium	174.8	188.0	203.4	225.6
Net Premium Income	93.6	100.6	109.2	122.3
Administrative Expense	55.6	57.3	59.0	60.8
Operating Income	38.3	43.4	50.2	61.5
Guarantee Portfolio EC	522	579	679	781
Total Economic Capital (EC)	596	662	770	879
Operating Capital (OC)	1,374	1,439	1,519	1,612
<b>Key Ratios</b>				
Total EC/OC	43%	46%	51%	55%
Administrative Expense/ Net Premium Income Ratio	59%	57%	54%	50%

<sup>10</sup> Based on MIGA's New Business Pipeline Report

<sup>11</sup> FY17 new business issuance based on MIGA Strategic Directions FY15-17, April 17, 2014 (MIGA/R2014-0011/1)

92. **Income.** Net premium income over the Strategy period is expected to increase in line with the growth in the average portfolio net exposure over FY16-20. At FY20, net premium income is projected to be US\$122.3 million, a 40% increase from FY16 levels.

93. **Capital Utilization.** Under normal conditions for the base case scenario, the capital utilization ratio defined as total economic capital<sup>12</sup> over operating capital (EC/OC) is projected to reach 55% in FY20, below the guideline that MIGA management team set of 70%-80% in total economic capital usage that MIGA's management team views as being acceptable. Figure 13 shows the EC/OC ratio under the base case and the scenarios discussed next and their related effect on capital utilization.

### Scenario Analysis

94. **New Business Volumes.** A new business volume scenario for a high case and the resulting impact on the Agency's financial sustainability was considered over FY18-20. In this scenario, a 60% increase in new guarantees issued by FY20 over FY16 levels is assumed versus the 40% in the base case. Higher average capital utilization of 52% over FY18-20 results, with capital utilization growing to 57% by FY20. New business volumes would average US\$5.9 billion over the period.

95. **New Business Reinsurance Levels.** In addition, two scenarios around the levels of new business reinsurance were considered to further assess impact on MIGA's capital utilization. A reduced availability in the reinsurance marketplace would require MIGA to hold higher levels of newly underwritten exposure. If MIGA were only able to reinsure 50% of its new business issued, an increase in capital utilization would result and the projected EC/OC ratio would be 62% in FY20 (see Figure 13). In the case of large scale transaction sizes of around US\$1.0 billion, MIGA would be required to reinsure at consistently higher levels.<sup>13</sup> Reinsurance at 70% for new business results in slightly lower capital usage of 46% in FY20.

96. **Claims Payout.** Claim payout scenarios were examined to assess impact on MIGA's capital utilization. A hypothetical cumulative claim of US\$250 million over a four year period starting in FY17 represents a payout on MIGA's contracts of guarantee covering equity and debt investments in a top exposure country. Under this scenario, even with a reduced capital base, MIGA is able to continue to implement its base case business plan after the payout, where the EC/OC ratio rises from 52% in FY17 to 64% in FY20.

97. A second more severe claims scenario adds an additional immediate claims payout of US\$240 million, in year one, from two of MIGA's largest net exposure contracts covering equity investments. This results in a hypothetical total claims payout of US\$490 million. The EC/OC ratio increases to 65% in FY17 and reaches 79% in FY20. If MIGA were to incur a claims payout of this magnitude, MIGA would seek a discussion with the Board on the need for potential capital support.

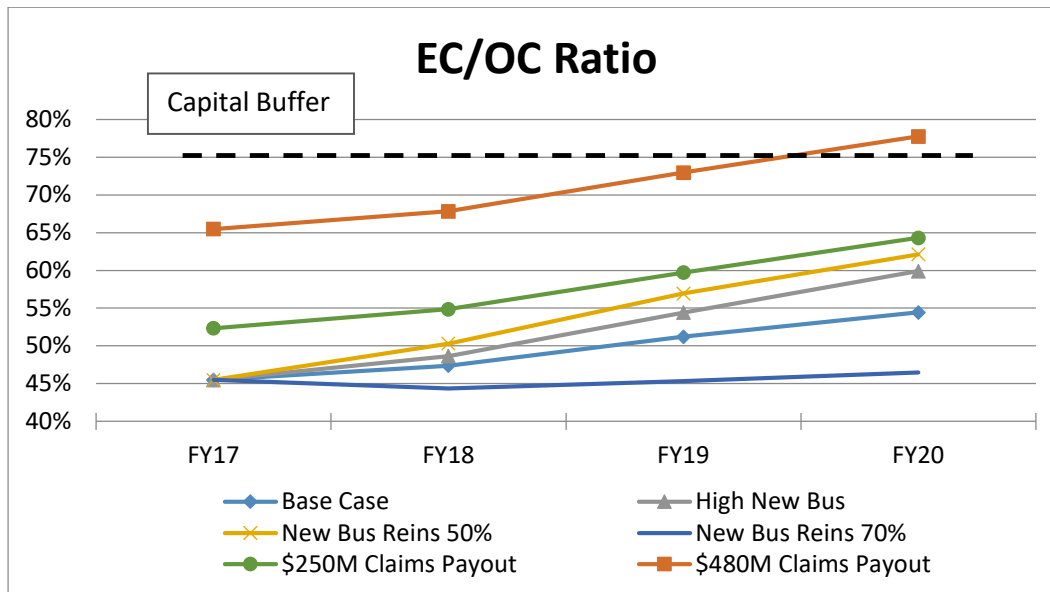
98. The base case and scenarios show that MIGA can withstand various types of stresses, including those associated with reduced reinsurance market capacity and potential claims payout. A combination of these events could lead to a significant increase in capital utilization. If a capital constraint were to materialize, a reevaluation of the planned new business volumes would be warranted in consideration of any claims recovery MIGA expected over time.

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<sup>12</sup> MIGA's total economic capital usage includes the EC consumed by the guarantee portfolio, EC for operational risks, and EC for investment portfolio risks.

<sup>13</sup> MIGA's Board approved per project net exposure limit maximum is US\$250 million.

Figure 13. Economic Capital to Operating Capital Ratio



## BUDGET TRAJECTORY

99. MIGA has demonstrated its commitment to cost efficiency. In the FY15-FY17 period, MIGA has grown its guarantee issuance while steadily improving its administrative expense to premium income ratio over a quarter in four years from 71% in FY13 to 52% in FY16. In order to continue to expand its business, widen its reach, and extend its developmental impact across its priority areas of IDA, FCS and climate finance for FY18-FY20, MIGA will require slight increases (estimated at 3-4% per year) in its administrative budget. The four pillars will require investments in business development, recruitment of new expertise, such as in climate finance and FCS. Additional costs will also be incurred as the IDA PSW facilities become operational, namely the MGF and the RMF which MIGA will be administering on behalf of IDA and IFC. The administrative budget request, with details on the implementation of the FY18-20 strategy, will be brought to the Budget Committee in FY17 Q4.

## **CHAPTER 4: CONCLUSION**

100. In order to deliver on its objectives to provide development impact at scale and additionality in the context of the WBG's development goals and the SDGs, MIGA is positioning itself to fully leverage the resources of the WBG and the private sector through effective partnerships. MIGA's ability to generate business in its strategic priority areas of IDA, FCS, and climate finance will rest on the four core pillars around which the strategy will be pursued. These pillars are designed to improve its ability to serve countries, and deliver development results, engaging clients earlier in the project formulation process.

101. Given the assumptions for future business volume presented in this FY18-20 strategy, combined with the Agency's increased portfolio reinsurance limit and the recently approved increase in MIGA's guarantee capacity, MIGA will continue to more effectively utilize its capital. While the risk level of the guarantee portfolio may increase, continued growth in the portfolio would result in higher income earned, which in turn adds to a growing capital base supporting the guarantee business, absent any significant claim payouts. Overall, MIGA's ability to deliver on its strategic objectives, and be a reliable de-risking partner for the private sector, remains strong.