

INFRASTRUCTURE DEVELOPMENT IN EMERGING ECONOMIES AND THE
ROLE PLAYED BY MULTILATERAL INSTITUTIONS

by

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(Under the Direction of Gabriel M. Wilner)

ABSTRACT

This thesis is a study of the development of long-term infrastructure projects in the emerging economies. The essay addresses the emerging economies' particular attraction to project finance to bring in much needed foreign investment for implementing infrastructure projects instead of the obtaining loans, grants and assistance from international institutions and wealthy donor countries. While the investors have found new opportunities to invest in the emerging economies, it is not without its own set of risks. To assist both the host nations and the investors, bilateral institutions as well as multilateral institutions provide risk insurances for long-term infrastructure projects. These institutions not only provide insurances but also foster and encourage investment by creating favorable conditions without infringing on the host nations' sovereign rights.

INDEX WORDS: Infrastructure, Emerging Economies, Developing Countries, Project Finance, Bilateral Investment Treaty, Overseas Private Investment Corporation, Multilateral Investment Guarantee Agency, BITS, MIGA, OPIC, Political Risk Insurance, Expropriation, Foreign Direct Investment.

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CHAPTER 1

INTRODUCTION

In this essay the author will address the financing of long-term infrastructure projects in the emerging markets. In particular, focus will be placed on the political risks faced by investors and the political risk insurance provided by multilateral institutions. Further as part of the study the essay will address project financing, and its appeal for investors interested in investing in long-term projects in the emerging markets. Finally the essay will highlight the positive role played by multilateral organizations, in particular the Multilateral Investment Guarantee Agency, hereinafter referred to as MIGA, which has had a very positive effect impacting the flow of investments to the emerging markets in an equitable fashion without exerting too much political influence.

In chapter two the author will briefly address the traditional methods through which infrastructure projects were financed. Financing primarily consisted of commercial lending, loans from international organizations such as the World Bank and grants from Developed Nations. These grants from the developed nations were political in nature as the granting country always attached various conditions to such grants. Further such assistance from the developed nations was really in place to facilitate their interests in the developing countries.

The developing countries depended on commercial loans from banks and other financial institutions to finance various development projects. However, commercial loans were recourse in nature, meaning, that in the event a country is unable to repay its loan, the bank would have access not only to the project towards which it extended the loan amount but also to the host countries capital resource for repayment of its loans. Since the developing countries subsidize essential services heavily, sufficient enough income was not generated and they invariably were unable to repay loans leading to debt crises such as in Asia and in Latin America in the recent past.

National institutions such as Overseas Private Investment Corporation (OPIC) and The Export, Import and Investment Insurance Department (EID), one of world's largest export-import insurers, a part of Ministry of International Trade and Industry (MITI) were specifically created for facilitating investments in developing countries. However, these institutions only promoted investments in few countries in specific parts of the world, mainly dictated by their relationship to the developing countries and their willingness to make changes to their national policies and to a certain extent give up sovereign rights in return. This form of investment though useful was not entirely successful. OPIC and other similar bilateral institutions were policy tools of the government which used them to reward friendly nations.

There is no multilateral investment treaty in place and Bilateral Investment Treaties (BITS) have been particularly effective in aiding countries attracting foreign investments. The investment climate in the emerging markets has been

very volatile and prone to sudden changes due to political instability. Bilateral agreements have reduced to a certain extent, the risks for foreign investors as the borrowing nation's accords such investors' favorable treatment pursuant to the BITS agreement.

In part three of the essay focus will be on project finance, as it has become the most preferred vehicle to transport foreign investments into emerging markets for long-term infrastructure projects. Earlier on, governmental institutions carried out all developmental work in the emerging markets. This was preferred by the governments of the emerging markets as it had sovereign control over such projects and also since these were highly political issues. However, with the recent liberalization and globalization of economies, the outlook toward such development projects has changed. More of long-term infrastructure projects are carried out by private enterprises. The governments play more of a supervisory role to ensure that such project do not erode environmental and social policies.

This essay will address why project financing is important and what is the role of the government /host nation. The essay will also address what is risk assessment and allocation and what are the safeguards built in the financing agreements. Further this chapter will also address the different methods of implementing projects, such as Build, Own & Operate and Build, Own, Operate & Transfer and how it benefits the emerging markets as well as the investors.

This chapter will deal with the risks faced by investors while investing in the emerging markets. In particular this chapter will focus on political risk as it

plays an important role in the lenders and investors decision in investing in long-term projects in such emerging markets. The writer will address what constitutes political risk and why it is important for investors to protect their investments against such risks.

Various institutions comprising of commercial banks and other multilateral institutions provide political risk insurance. This essay will provide a brief insight into the Multilateral Investment Guarantee Agency (MIGA), formed quite recently for the sole purpose of providing this kind of insurance, has played a very important role in fostering development in the emerging markets by providing them with access to foreign investments, which they might not have obtained earlier on. Further this essay will address why MIGA has been able to achieve this end and how it can continue to remain an important player in this field.

Finally the essay will conclude that foreign direct investment for infrastructure projects in emerging markets has increased in the recent years due to the change in the investment structure for such projects and due to the development role played by MIGA and other international and national developmental banks. The positive role played by multilateral organizations, in particular MIGA which provides political risk insurance for infrastructure projects have played a positive role impacting the flow of investments to the emerging market in an equitable fashion without too much political influence.

CHAPTER 2

INFRASTRUCTURE DEVELOPMENT IN THE EMERGING ECONOMIES

Traditional Methods of Financing Infrastructure Projects

A nation's socio-economic and political stability depends a lot on the needs of its citizens being met by the government. In particular, it is required of any government to ensure that basic infrastructure facilities are made available to its subjects. The availability of infrastructure ensures movement of people, goods and services, in addition to them having adequate access to electricity, transportation and communication services, which will enable them to compete in the global market. In today's globally interdependent world the existence of infrastructure determines a nation's ability to economically succeed and be a part of the economic revolution.

The availability of infrastructure is taken for granted in the developed countries.¹ In developed countries infrastructure development is typically carried out by the government utilizing its own capital resources. Such developmental work was either carried out by the either through public or private funding.² If the

¹ William M. Stelwagon, *Financing Private Energy Projects in the Third World*, 37 CATH. LAW. 45, 45 (1996).

² Id. at 62

government required additional funding it was raised through public offering of bonds and stocks.

However, in the developing countries there is a great need for infrastructure development. In many parts of the developing world they lack even some of the basic requirements such as proper roads and bridges to enable movement of goods and people.³

Traditionally infrastructure development was considered to be a bastion of the state or state agencies.⁴ Financing consisted primarily of loans and grants from developed nations and international and regional institutions specifically created to support development in the developing countries, such as the World Bank and commercial lending.

The grants from individual countries loans are very political in nature as the granting country always attached conditions to such grants, which were considered to encroach on the sovereign powers of the receiving nations. Further such form of financing was in place mainly to facilitate the developed countries interests in the developing countries.

Loans and Grants from International Organizations

The World Bank is one of the primary institutions, which foster development in the poorest and other developing countries in the world. Through the International Bank for Reconstruction and Development (IBRD) the World

³ See *supra* note 1, at 45.

⁴ Patrick D. Harder, *Infrastructure Privatization in South Asia*, 15 CONSTRUCTION LAW. 34, 34 (1995).

Bank assists in reducing poverty in middle-income and creditworthy poorer countries by promoting sustainable development through loans, guarantees, risk management products, and analytical and advisory services. The International Development Association (IDA) is another part of the World Bank that helps the world's poorest countries. Established in 1960, IDA assists in reducing poverty by providing interest-free credits and grants for programs that boost economic growth, reduce inequalities and improve people's living conditions.

The International Finance Corporation, another arm of the World Bank IFC promotes sustainable economic growth in developing countries by financing private sector investment.⁵ The IFC has helped develop debt and equity financing instruments that are applicable to the energy industry investments. Further the IFC has encouraged other investors and lenders to participate in long-term infrastructure projects.⁶

The IMF and the World Bank greatly influence the macroeconomic and monetary policies of the countries obtaining loans and financing from them.⁷ Though many countries have been critical of the IMF and World Bank's influence on their sovereign rights they have continued to avail of the loans provided by

⁵ D.L. Khairallah, *The Developmental Role fo the International Finance Corporation*, 2 SUM NAFTA: L. & BUS. REV. AM. 3, 3 (1996).

⁶ Christopher C. McIsaac & Lori A. Bean, *The Role of Multilateral and Bilateral Agencies in the Financing of Infrastructure Projects*, 749 PLI/COMM 165, 170 (1997).

⁷ David Blumental, *Sources of Funds and Risk Management for International Energy Projects*, 16 BERKELEY J. INT'L L. 267, 276 (1998).

them as they are the only ones extending them such assistance and also due to their inability to attract foreign direct investment.⁸

The International Monetary Fund is an international organization with 185 member countries. Article I of the Articles of Agreement of the IMF states as its purpose to promote international monetary cooperation, exchange stability, and orderly exchange arrangements; to foster economic growth and high levels of employment; and to provide temporary financial assistance to countries to help ease balance of payments adjustment.

Though the IMF doesn't directly undertake financing of development projects in the developing world its influence on developing countries' economic and monetary policies have had a great impact on their stability and in ushering in the required market reforms. By assisting the economies maintain the value of their currencies; the IMF helps installing stable conditions that are critical for the successful development, financing and operation of long-term infrastructure projects.⁹

Bilateral Investment Treaties

Bilateral investment treaties (BITs) are agreements entered into between two states that establish terms and conditions for investment by nationals and companies of one country in the jurisdiction of another.¹⁰ BITs have become one

⁸ See *supra* note 1, at 68.

⁹ See *supra* note 5, at 7.

¹⁰ Glen Kelly, *Multilateral Investment Treaties: A Balanced Approach to Multinational Corporations*, 39 COLUM. J. TRANSNAT'L L. 483, 488 (2001).

of the most important tools to support foreign direct investment (FDI) between developing and developed countries. Bilateral Investment Treaties (BITs) have greatly proliferated in the last two decades, and play an increasingly significant role in global trade and investment protection.¹¹ Further, bilateral and regional agreements have proliferated in all regions of the world not only between developed and developing countries as was the case earlier, but now also between developing countries.¹²

The main provisions of the BITs agreement cover the scope and definition of foreign investment; admission of investments; national and most-favored nation status; fair and equitable treatment clauses; compensation guarantees for expropriation, war and civil unrest; guarantees of fund transfers and the recuperation of capital gains; subrogation of insurance claims; and dispute settlement provisions.

The U.S. bilateral investment treaty (BIT) for example, helps protect private investment, develop market-oriented policies in partner countries, and promote U.S. exports.¹³

The basic aims of BITs are to protect investment abroad in countries where investor rights are not already protected through existing agreements; encourage the adoption of market-oriented domestic policies that treat private

¹¹ See *supra* note 10, at 488.

¹² Riyaz Datu, *A Journey from Havana to Paris: The Fifty-Year Quest for the Elusive Multilateral Agreement on Investment*, 24 *FORDHAM INT'L L.J.* 275, 277 (2000).

¹³ See Michael R. Reading, *The Bilateral Investment Treaty in ASEAN: A Comparative Analysis*, 42 *DUKE L.J.* 679, 690 (1992).

investment in an open, transparent, and non-discriminatory way; and support the development of international law standards consistent with these objectives.¹⁴

Developed nations have entered into a multitude of Bilateral Investment Treaties (BIT) with developing countries to promote and safeguard their investments.¹⁵ The BIT sets forth legally binding standards of treatment that one signatory must afford to the other signatory's investments. Breach of any of the terms contained therein can lead to legal actions by the aggrieved party.¹⁶

Organizations such as OPIC and EID/MITI were specifically created for facilitating investments in developing countries. As mentioned earlier this only promoted investments in few countries in specific parts of the world dictated by their relationship to the developing countries and their willingness to make changes to their national policies and to a certain extent give up sovereign rights in return. This form of investment though useful was not entirely successful.

There is no multilateral investment treaty in place and Bilateral Investment Treaties (BITS) have been particularly effective in aiding countries attracting foreign investments. The investment climate in the emerging markets has been very volatile and prone to sudden changes due to political instability. Bilateral agreements have reduced to a certain extent, the risks for foreign investors as

¹⁴ Mathew W. Barrier, *"Regionalization: The Choice of a New Millennium"*, 9 CURRENTS: INT'L TRADE L.J. 25, 26 (2000).

¹⁵ See *supra* note 13, at 682.

¹⁶ See *supra* note 13, at 680.

the borrowing nations' accords such investors' favorable treatment pursuant to the BITS agreement.¹⁷

Commercial Loans from Banks and other Institutions

Outside of the financing described above commercial loans were the primary sources of finance for the developing countries.¹⁸ This was always very expensive and the lenders were only interested in lending to countries whose economies were progressive. Though the commercial loans were expensive it did have certain advantages. Unlike the international organizations, commercial banks did not have to take into consideration if such development was sustainable or the impact it would have on the society and the environmental ramifications.¹⁹

Since the developing countries subsidize essential services heavily enough income was not generated and they invariably were unable to repay loans leading to debt crises such as in Asia and in Latin America in the recent past.

The development model where such development was carried out by the State or by state owned enterprises through financing obtained through commercial lending and loans from international organizations was very flawed for various reasons. Among them high interest rates, countries not being able to

¹⁷ See *supra* note 13, at 684.

¹⁸ Rumu Sarkar, *The legal Implications of Financial Sector Reform in Emerging Capital Markets*, 13 *Am. U. Int'l L. Rev* 705, 706 (1998).

¹⁹ See Marvin W. Tubbs, *Political Risk Insurance: The Potential Effects of Privatization on Credit Availability*, 16 *ANN. REV. BANKING L.* 553, 568 (1997).

service debts, increased amount of subsidization, poor management, lack of competition and protective policies. Consequences of such haphazard developmental policies did not lead to the expected growth or prosperity.²⁰ The indiscriminate borrowing only led to the collapse of many such developing countries.²¹

Recent developments

With the role of the private sector in providing and financing infrastructure development in the emerging economies expanding rapidly the role of the state has been redefined. The State or State owned enterprises, which were responsible for providing much of the required infrastructure development, have slowly been privatized due to the recent trend towards liberalization and market based economies.²² The change was brought about by the collapse of the many an economy in Latin America and Asia due to the policy of funding their growth by money borrowed from commercial sources, which was the prevalent method.²³ The borrowing countries were unable to service their debts and as a result their economies collapsed. Though the International Monetary Foundation and the World Bank have been criticized for dictating the policy changes to be

²⁰ Samuel K. Alexander, *Current Issues in Multinational Financing*, 89 AM. SOC'Y INT'L L. PROC. 19, 29 & 30 (1995).

²¹ Rumu Sarkar, *The legal Implications of Financial Sector Reform in Emerging Capital Markets*, 13 Am. U. Int'l L. Rev 705, 706 (1998).

²² See *supra* note 4, at 34.

²³ See *supra* note 21, at 707.

carried out by the borrowing countries it has to be said that the changes have been for the better.

A few countries situated in South America, Asia and also in Europe have experienced rapid economic growth in the recent past. These countries are all emerging markets or are otherwise known as developing countries. They are also called as transitioning economies. Most of these countries are newly independent and there has been a rapid increase in the inflow of Foreign Direct Investment into these Emerging Markets in the recent years. There are many factors contributing to the increase in the foreign direct investment from the developed countries to the developing countries. The most important factor is the liberalization of trade and economic policies of the newly independent nations which have for long maintained a protectionist policy.

With liberalization policies taking effect and the economy being on the rise there has been a great demand for financing infrastructure projects such as roads, bridges, power plants and telecommunications. However, these countries have realized that their earlier policies have not benefited them in the long run by making them competitive in the international market nor have they achieved the desired development within. The emerging markets, in order to achieve their desired growth must institute major institutional changes in the economic, administrative and legal front. Unless they make such changes they will be unable to attract the much needed foreign investment for development projects.²⁴

²⁴ Rumu Sarkar, *The legal Implications of Financial Sector Reform in Emerging Capital Markets*, 13 *Am. U. Int'l L. Rev* 705, 719 (1998).

CHAPTER 3

PROJECT FINANCE

The emerging markets have provided the developed countries with a new avenue to invest their capital.²⁵ Such increased need for capital has also led to new methods of financing.²⁶ The most popular and effective of these is Project Finance.²⁷ Project finance has become the most preferred vehicle to transport foreign investments into emerging markets for funding long-term infrastructure projects.²⁸ Examples of such large-scale projects include power plants, oil & gas pipelines, telecommunications network, airports and roads.²⁹

Typically the government or governmental institutions carried out all developmental work in the emerging markets. This was preferred by the governments of the emerging markets as they had more control over such projects and also since these were highly political issues.³⁰ It provided the

²⁵ Marvin W. Tubbs, *Political Risk Insurance: The Potential Effects of Privatization on Credit Availability*, 16 ANN. REV. BANKING L. 553, 553 (1997).

²⁶ David Blumental, *Sources of Funds and Risk Management for International Energy Projects*, 16 BERKELEY J. INT'L L. 267, 270 (1998).

²⁷ *Id.*

²⁸ See John Nibbelin, *Project Finance, a Legal Guide*, by Graham Vinter, 13 Int'l Tax & Bus Law, 326, 326 (1996).

²⁹ Christophe Dugue, *Dispute Resolution in International Project Finance Transactions*, 24 FORDHAM INT'L L.J. 1064, 1066 (2001).

³⁰ Patrick D. Harder, *Infrastructure Privatization in South Asia*, 15 CONSTRUCTION LAW. 34, 36 (1995).

governments the opportunity to balance their developmental needs and the social policies benefiting its citizens.³¹ Infrastructure, though not a primary concern in many of the developing nations were developed by existing public funds and borrowing from private financial institutions. The availability of funds was dependent on the creditworthiness of these countries and the prevalence of a stable political and economical atmosphere.³² However, with the recent trend in liberalization and globalization of economies, developing countries in Asia, South America and in the Eastern Europe have been experiencing economic growth resulting in great demand for all forms of infrastructure, including low-technology highways to high technology power generation plants to sustain growth.³³

With the role of the private sector in providing and financing infrastructure development in the emerging economies expanding rapidly, the role of the state has been redefined.³⁴ The State or State owned enterprises responsible for providing much of the required infrastructure development have slowly been privatized due to the recent trend towards liberalization and market based economies. The change was brought about by the collapse of the many an economy in Latin America and Asia due to the policy of funding their growth by money borrowed from commercial sources, which was the prevalent method. The borrowing countries were unable to service their debts and as a result their

³¹ See *supra* note 4, at 34.

³² Malcom D. Rowat, *Multilateral Approaches to Improving the Investment Climate of Developing Countries: The Case of ICSID and MIGA*, 33 HARV. INT'L L.J. 103, 103 (1992).

³³ See *supra* note 4, at 35.

³⁴ Don Wallace, Jr. *Uncitral Draft Legislative Guide on Privately Financed Infrastructure: Achievements and Prospects*, 8 Tul. J. Int'l & Comp. L. 283, 285 (2000).

economies collapsed.³⁵ Though the International Monetary Fund and the World Bank have been criticized for dictating the policy changes required to be carried out by the borrowing countries and influencing their internal national policies, it has to be said that the changes recommended have produced positive results for the developing countries.³⁶

The developing countries outlook toward such development projects has since changed and more of the long-term infrastructure projects are carried out by private enterprises and quasi government enterprises.³⁷ This method of privatized development of infrastructures is more appealing to emerging economies since it eliminates the need to use public funds or borrow from the lenders such as the World Bank, The Asian Development Bank or such other institutions specifically created for lending for such long-term projects.³⁸ The governments of host nations play more of a supervisory role to ensure that such projects do not erode environmental and social policies.³⁹

Project financing is an innovative and complex type of loan structure that relies only on the projects cash flow and the projects assets for repayment of

³⁵ Harold F. Moore, *Allocating Forseeable Sovereign Risks in Infrastructure Investment in Indonesia: Force Majeure and Indonesia's Economic Woe's*, 822 PLI/COMM 463, 466 (2001).

³⁶ Nicole Wendt, *The IMF and the World Bank Respond to Criticisms*, 9 TRANSNAT'L L. & CONTEMP. PROBS. 165, 166 (1999).

³⁷ Martin Stewart-Smith, *Private Financing and Infrastructure Provision in Emerging Markets*, 26 L. & POL'Y INT'L BUS. 987, 987 (1995).

³⁸ Patrick D. Harder, *Infrastructure Privatization in South Asia*, 15 CONSTRUCTION LAW. 34, 34 (1995).

³⁹ See *supra* note 37, at 988.

loan, rather than the borrowers assets.⁴⁰ Typically, such projects involve numerous parties including the host nation, investors or sponsors, banks or financial institutions that provide funding for the operation.⁴¹ The loans extended under project financing are mostly non-recourse loans. Non-recourse loans are, as described above, loans that are secured by the project itself and where repayment is through cash flow generated by the project.⁴²

In project financing a special purpose vehicle/project company is created for each project, which shields other assets owned by a project sponsor from the detrimental effects of a project failure.⁴³ As a special purpose vehicle the project company has no assets other than the project. "A project company is a group of agreements and contracts between lenders, project sponsors, and other interested parties that creates a form of business organization that will issue a finite amount of debt on inception; will operate in a focused line of business; and will ask that lenders look only to a specific asset to generate cash flow as the sole source of principal and interest payments and collateral". Project finance is often more complex than other types of financing methods due to the number of parties involved, the different nationality of such parties and the duration of such projects.

⁴⁰ David Blumental, *Sources of Funds and Risk Management for International Energy Projects*, 16 BERKELEY J. INT'L L. 267, 270 (1998).

⁴¹ Nan Zhang, *Moving Towards a Competitive Electricity Market? The Dilemma of Project Finance in the Wake of the Asian Financial Crisis*, 9 MINN. J. GLOBAL TRADE 715, 717 (2000).

⁴² *Id.*

⁴³ Carl S. Bjerre, *Project Finance Securitization and Consensuality*, 12 DUKE J. COMP. & INT'L L. 411, 415 (2002).

The development and operation of infrastructure under project financing is carried out either as a Build, Own and Operate enterprise or as a Build, Own, Operate and Transfer enterprise.

Build, Own and Operate

Under the BOO method the project is owned by the project company and it is responsible for building and completing the project as well as operating the project and services are rendered to the host nation under separate contracts entered into between the host nation and the project company as part of the project financing agreement. Since the host nation might not have the necessary knowledge to operate and maintain the newly developed project the sponsor is also responsible for providing training local employees of the host nation. There is no ultimate transfer of the project to the host nation and the project company after servicing its debt is entitled to continue to own the project. The host nation is usually entitled to a certain amount of shared revenue during a specific period of time.⁴⁴

Build, Own, Operate and Transfer

The Build, Own, Operate and Transfer is similar to BOO described above and consists of private financing, designing, constructing, operating and

⁴⁴ Patrick D. Harder, *Infrastructure Privatization in South Asia*, 15 CONSTRUCTION LAW. 34, 36 (1995).

ultimately transfer of the project to the host nation after a specified period of time set forth in the concession agreement.⁴⁵

In addition the host governments also require foreign investors to transfer advanced technology to local companies and train local people in the operation and maintenance of such technology. This in turn assists such emerging markets to enhance their own technological competitiveness in the world markets.⁴⁶

Risk Identification and Allocation

Risk identification and allocation is a key component of project finance. The success of a project is depends on the proper allocation of risks to each project participant who is best able to manage and mitigate the risk.⁴⁷ A project may be subject to a variety of technical, environmental, economic and political risks, particularly in developing countries and emerging markets. Financial institutions and project sponsors may conclude that the risks inherent in project development and operation are unacceptable. To cope with these risks, project sponsors are completed by a syndicate of companies operating in a contractual network with each other that allows for the allocation of risks in a way that will allow financing to take place.

⁴⁵ Patrick D. Harder, *Infrastructure Privatization in South Asia*, 15 CONSTRUCTION LAW. 34, 36 (1995).

⁴⁶ See Eric M. Burt, *Developing Countries and the Framework for Negotiations on Foreign Direct Investment in the World Trade Organization*, 12 AM. U. J. INT'L L. & POL'Y 1015, 1021 & 1022 (1997).

⁴⁷ See *supra* note 41, at 720.

The various patterns of implementation are sometimes referred to as project delivery methods. The financing of these projects must also be distributed among multiple parties, so as to distribute the risk associated with the project while simultaneously ensuring profits for each party involved.

A riskier or more expensive project may require limited recourse financing secured by a surety from sponsors.⁴⁸ The borrower will be liable with respect to breach of representations, warranties, undertakings and covenants contained in the credit agreement. A complex project finance scheme may incorporate corporate finance, securitization, options, insurance provisions or other further measures to mitigate risk.

As with any other commercial investments, foreign direct investment in infrastructure development in emerging markets has its own risk. The success of the project as well as the investments depends a lot on risk assessment and risk mitigation through allocation and the safeguards built into the financing agreements. There are several types of risks and they appear at the various stages of a project's life-time.⁴⁹ At the initial stages the project company faces severe developmental or feasibility risks. Since such projects are very expensive, the cost to even create a proposal for submission to a government entails huge expenses for the project group. The project company needs to be sure of the commercial viability of the project prior to embarking on a huge venture or risk abandoning the project midway and suffer a loss.

⁴⁸ See David Blumental, *Sources of Funds and Risk Management for International Energy Projects*, 16 BERKELEY J. INT'L L. 267, 271 (1998).

⁴⁹ See William M. Stelwagon, *Financing Private Energy Projects in the Third World*, 37 CATH. LAW. 45, 52 (1996).

Once the initial stages of proposal and acceptance has been completed and the contracts between the various parties have been executed the project company embarks on the construction part of the project. The project company usually will be supported in this venture by the host nation by providing all assistance in the form of acquisition of land, and power supply and most importantly a controlled labor force. Construction risks are usually borne by the contractor, who is often required to sign a fixed sum design agreement.⁵⁰ The contractor will also be required to provide completion and performance guarantees. The project company is also responsible at this stage to address all environmental and socio political issues involved in executing the project.

Operational risk

Operational risk is another one of the major risks faced in long-term infrastructure projects. It is quite common for operating contracts to be effective for a 20 or 30 year period. At this stage after completing of construction and effective functioning of the project, it is crucial for the project company to market the project product or output in an effective manner so as to recoup its investment and achieve profitability. The risks faced during this stage are similar to the ones described above under feasibility risk. The risk include inadequate demand for project product, disruption and delay in production due to labor

⁵⁰ See Nan Zhang, Moving Towards a Competitive Electricity Market? The Dilemma of Project Finance in the Wake of the Asian Financial Crisis, 9 MINN. J. GLOBAL TRADE 715, 721 (2000).

related problems, fuel shortage, and lack of local talent pool for required for the operation of the project.⁵¹

Legal System Risk

As discussed above the allocation of risks is a difficult and complex process in both the developed and developing countries. In the developing countries or emerging markets, the process is substantially more difficult as there is often a lack of precedents to build upon.⁵² Investors should take every measure to protect their investment should they run into disputes, which might include issues with the host nation or any of the multifarious parties to the various agreements. Since there are many parties belonging to various countries and subject to different laws,⁵³ settlement of disputes is complex in project financing.⁵⁴ It would be in the investors' best interest to incorporate arbitration clauses or agree to submit to the jurisdiction of a court which has sufficient knowledge about complex project finance matters instead of having to face a legal system which might be ill equipped to deal with matters of these magnitudes.⁵⁵ Since the legal system in many of the emerging markets is not

⁵¹ Patrick D. Harder, *Infrastructure Privatization in South Asia*, 15 CONSTRUCTION LAW. 34,37 (1995).

⁵² Nan Zhang, *Moving Towards a Competitive Electricity Market? The Dilemma of Project Finance in the Wake of the Asian Financial Crisis*, 9 MINN. J. GLOBAL TRADE 715, 724 (2000).

⁵³ Ian R. Cole, *The Julietta Gold Mining Project: Lessons for Project Financing in the Emerging Markets*, 24 FORDHAM INT'L L.J. 1052, 1055 & 1056 (2001).

⁵⁴ Christophe Dugue, *Dispute Resolution in International Project Finance Transactions*, 24 FORDHAM INT'L L.J. 1064, 1064 (2001).

⁵⁵ Peter Fitzgerald, *International Project Financing*, 822 PLI/COMM 407, 413 (2001).

similar to the more established systems of the developed countries the investors should ensure to include arbitration clauses whereby all disputes will be referred to arbitration with one of the international organizations such as UNCTRAL, ICSID or be subject to the laws of a state that is well versed with such types of complex transactions, such as New York, in the United States of America.⁵⁶

⁵⁶ Christophe Dugue, *Dispute Resolution in International Project Finance Transactions*, 24 FORDHAM INT'L L.J. 1064, 1072, 1073 & 1074 (2001).

CHAPTER 4

POLITICAL RISK INSURANCE

There is no clear definition for political risk as each event differs markedly.⁵⁷ As the world changes, the nature of political risk also changes. Political risk can be termed as the risk of loss of investment faced by the investor due to change in a country's political structure or policies relating to expropriation of assets, restriction on repatriation of profits, political violence and breach of contract. Among the more prominent of the political risks faced by investors in developing countries are expropriation, currency inconvertibility or non transfer and political violence.⁵⁸

Political Risk insurance against the above specified political risks can be purchased by investors before investing in long-term infrastructure projects in developing countries. Such insurance can be purchased from private banks, governmental institutions as well as multilateral institutions.⁵⁹

⁵⁷ George Thomas Ellinidis, *Foreign Direct Investment in Developing and Newly Liberalized Nations*, 4 D.C.L. J. INT'L L. & PRAC. 299, 314 (1995).

⁵⁸ Paul E. Comeaux & N. Stephen Kinsella, *Reducing Political Risk in Developing Countries: Bilateral Investment Treaties, Stabilization Clauses, and MIGA & OPIC Investment Insurance*, 15 N.Y.L. SCH. J. INT'L & COMP. L. 1, 4 (1994).

⁵⁹ *Id.* at 5.

Expropriation

One of the most common risks faced by investors in the emerging market is the risk of expropriation of the investors' assets by the foreign/host government. It is a risk that the host government will nationalize the assets or the equity of the project company in an arbitrary or discriminatory manner or without paying just compensation.⁶⁰ The investors have to be aware of the two typical types of expropriation, direct or outright expropriation and creeping expropriation.⁶¹ Expropriation by host governments has affected investments in varied field including oil and gas, mining, and power projects, etc.⁶²

It includes such actions by the host government that deprives the investor of its investments as well as profits and can be in the form of confiscation, nationalization, expropriation and deprivation. Under international law a host government has the legal right to seize a foreign owned asset as long as compensation is provided on a prompt, adequate and effective manner.

When expropriation occurs and the host government fails to compensate the investor or foreign owner the insurance provider compensates the investor based on the net value of the expropriate assets. Though there is no common definition for expropriation, most expropriation coverage requires that the expropriatory action continue for an extended period of time, usually at least for a

⁶⁰ William M. Stelwagon, *Financing Private Energy Projects in the Third World*, 37 CATH. LAW. 45, 58 (1996).

⁶¹ Peter Fitzgerald, *International Project Financing*, 822 PLI/COMM 407, 410 (2001).

⁶² See Id.

period of six months to one year at which point it is considered to be permanent and therefore eligible for compensation.⁶³

Creeping expropriation is however harder to identify, as it will be a series of hostile acts in the form of legal and administrative actions by the host government that will deprive the investor the enjoyment of its assets or profits.⁶⁴ Creeping expropriation is a series of hostile acts for which the host nation is responsible and which are illegal both under national and international laws.⁶⁵

Direct expropriation in the form of nationalization or seizure is easy to spot and the investor can submit a claim with the insurance provider. However, with creeping expropriation it is hard for the investor to identify when the expropriation began and how long it continued to cause permanent deprivation of property and constitute political risk as defined by the insurer.

Currency Risks

Any investor, prior to embarking on an investment in the emerging market must take into account the currency risks faced by them. It is a major risk faced by investors as they have to be able to transfer currency to and out of the host country in order to effectively execute the project and thereby profiting from it. Currency risk encompasses various issues relating to repatriation of profits, fees, capital and other proceeds from the insured project and such other problems as

⁶³ Peter Fitzgerald, *International Project Financing*, 822 PLI/COMM 407, 407 (2001).

⁶⁴ *See Id.*

⁶⁵ Marvin W. Tubbs, *Political Risk Insurance: The Potential Effects of Privatization on Credit Availability*, 16 ANN. REV. BANKING L. 553, 558 (1997).

inconvertibility, transfer and devaluations. It is crucial for an investor to be able to repatriate its profits, fees and capital out of the host country. However, when host governments implement measures which prohibit transfer of local currency into any other transaction currency or if they prohibit the export of the transaction currency the investor will be forced abandon the project leaving the property in the hands of the host government. Insurance can be purchased against such hostile actions by the host governments.

Currency devaluation on the other hand is not insurable, unless when an investor made the proper applications with the host government to convert local currency to a foreign currency and the host government's central bank failed to convert in a predefined period of time but also refused to return the local currency to the investor, then expropriation has taken place and the investor can file a claim with the insurance provider.

Political Violence

Political violence is a risk unlike the others described above which is neither precipitated by the host government nor is under the control of the host government. Political violence is not a risk that can be ascertained ahead of the investment as the events which constitute political violence such as civil disturbance, wars, revolutions, strikes and acts of terrorism are usually unexpected.⁶⁶

⁶⁶ Marvin W. Tubbs, *Political Risk Insurance: The Potential Effects of Privatization on Credit Availability*, 16 ANN. REV. BANKING L. 553, 553 (1997).

Breach of Contract

Another risk facing investors is the risk of breach of contract by the host government. As discussed in the previous chapter infrastructure project these days are carried out through project financing which is a set of contracts entered into between and amongst the multiple parties involved in the execution of the project. The Host governments enter into contracts with the investor to payments for services. In the event of a breach of such contract the investor must invoke its right for dispute resolution as per the term of contract. Usually arbitration is the preferred method of dispute resolution in such types of contracts. If after a pre-determined period of time the investor is unable to implement the outcome of the arbitration result, the political risk insurance provider will be called upon to pay compensation.

Investors in most cases will not be able to obtain third party financing if they have not obtained political risk insurance for the above specified risks.⁶⁷ Political risk insurance has been in existence for a long time. However, it has come to the forefront of the investment scene due to the increased flow of foreign investments in the recent years. Political risk insurance is provided by both private and public institutions. The private insurers are typically in the market with a profit motive. On the other hand the public players typically made up of specific governmental bodies and other multilateral organizations though profit form the this activity, their primary aim is to encourage the flow of foreign investment and

⁶⁷ William M. Stelwagon, *Financing Private Energy Projects in the Third World*, 37 CATH. LAW. 45, 50 (1996).

also create an investment friendly atmosphere in addition to providing forums for dispute resolutions.

Political Risk Insurance

Political risk insurance is coverage that protects the insured from loss due to various political perils which include confiscation, expropriation, nationalization, and government interference preventing repossession, currency inconvertibility or transfer risk, war, civil disturbance, acts of terrorism and breach of contract. Political Risk Insurance is a type of investment guarantee provided by multinational and private institutions to protect investments made by the developed countries in the developing countries.

In today's world, many countries which are on the verge of transitioning to western style capital economies, lack the much needed knowledge and an efficient legal systems to support such change. Further such countries face a very volatile unstable political system.⁶⁸ Faced with such uncertain prospects creditors and lenders will not provide financing unless the investor has obtained political risk insurance. Having political risk insurance increases the chance of obtaining better and improved financing terms from lenders. Political risk insurance is provided by many institutions both in the public and private sector.

Coverage against political risk insurance can be purchased from political risk insurers. Political risk insurance has traditionally been provided by Bilateral

⁶⁸ Claire A. Hill, *How Investors React to Political Risk*, 8 DUKE J. COMP. & INT'L L. 283, 293 (1998).

Organizations such as OPIC and Export Insurance Department of the ministry of International Trade and Industry of Japan.

Governmental organizations such as OPIC and Export Trade of Japan provide financing based on policy considerations. Private investors on the other hand are not bound by such policy considerations.⁶⁹ In addition, an institution known as Multilateral Investment Guarantee Agency was specifically created to provide insurance against the various political risks described above. Since its inception MIGA has played a very important role by supplementing the other providers of risk insurance and not competing against them.

Overseas Private Investment Corporation (OPIC)

OPIC is one of the largest public sector political risk insurance providers. OPIC was created by US Congress in 1971 with an aim to encourage private American investment in developing countries and its obligations are backed by the full faith and credit of the United States.⁷⁰ In addition to assisting American investment in developing countries it fosters economic development in new and emerging markets, complements the private sector in managing risks associated with foreign direct investment, and supports U.S. foreign policy. OPIC's political risk insurance covers, risks of war, revolution, insurrection, civil strife and

⁶⁹ Susan Mashkes, *Using Political/Credit Risk Insurance to Maximize Financing Opportunities*, 9 HASTINGS INT'L & COMP. L. REV. 451, 451 (1986).

⁷⁰ 22 U.S.C. §2197(c) (1988)

expropriation.⁷¹ OPIC insurance covers up to ninety percent of the investment to a maximum of \$100 million per project.

OPIC political risk insurance is available only to US citizens, US corporations and foreign corporations, if 95% or more of the shares are owned by US citizens.⁷² It is available only for investments in developing countries which are considered to be friendly by the United States government.⁷³ The US government constantly updates this list. Currently, OPIC services are available in more than 150 countries worldwide. Further OPIC insurance is based on the bilateral investment guarantee agreements entered into between the United States and the host country. OPIC's bilateral agreements are different from other bilateral investment treaties (BITS) negotiated by the United States Department of State. The BITs are agreements that are intended to protect all United States investors in contrast to the OPIC agreement which is intended to affect the relationship between OPIC and the host government.⁷⁴ Insurance is available only for new investments but includes the modernization or expansion of existing facilities. OPIC has been very successful in encouraging the flow of American investment to the developing countries. OPIC also promotes U.S. best practices

⁷¹ 22 U.S.C. §2194 (1988)

⁷² 22 U.S.C. §2198(c) (1988)

⁷³ 22 U.S.C. §2191 (1988)

⁷⁴ See S. Linn Williams, *Political and Other Risk Insurance: OPIC, MIGA, Eximbank and Other Providers*, 5 PACE INT'L L. REV 59, FN 40 (1993)

by requiring projects to adhere to international standards pertaining to environment and worker and human rights.⁷⁵

Since the OPIC insurance is provided by an US institution which is backed by the US government lenders and investors believe that it deters interference from host governments as they are unwilling to interfere with a “project sponsored by the US government”.⁷⁶

One of the important aspects of the OPIC political risk insurance is that the host government should agree to resolve any dispute by international arbitration in accordance with international law. The arbitration clause for resolution of disputes is crucial to protect the investment as in case of a dispute and in the absence of an arbitration clause the investor will be subject to the local laws of the host government which might be more favorable toward the host nation than the investor. Further most of the developing countries lack established legal systems capable of handling such complex issues and it is not in the investor’s best interest to subject itself to an unknown and untested foreign legal system.

OPIC insurance coverage is backed by the full faith and credit of the United States of America. Since it is accepted belief that the US government will not go bankrupt lenders assume that the US government will honor all claims and make compensation. This confidence in the US government enables investors to obtain financing from lenders

⁷⁵ Ana-Mita Betancourt, *OPIC Political Risk Insurance for Infrastructure Projects in Emerging Markets*, 745 PLI/COMM 179, 184 & 185 (1996).

⁷⁶ S. Linn Williams, *Political and Other Risk Insurance: OPIC, MIGA, Eximbank and Other Providers*, 5 PACE INT’L L. REV 59, 80 & 81(1993).

OPIC insurance coverage is available for projects up to twenty years. Since infrastructure projects typically are long-term in nature OPIC political insurance coverage is very advantageous to investors involved in the long-term infrastructure project in the emerging markets. Insurance coverage is provided up to \$200 million for potential investors.

However, there are limitations to OPIC's political risk insurance coverage. The primary and most significant problem with OPIC's coverage is the fact that it subject to foreign policy objectives of the US government. OPIC insurance is only available for investments in developing friendly countries. Many countries are termed as unfriendly nations based on its relationship to the US. American investors cannot obtain insurance from OPIC for investments in such unfriendly nations. This policy effectively reduces the investment to certain nations thereby affecting both investors as well as the nations requiring foreign aid. OPIC insurance is only available to US citizens and US corporations thereby limiting the availability to a wider circle of investors.

Keeping with its intention to promote American economic growth internationally, OPIC will not be able to assist in investment that would result in a significant lot of United States jobs and harm US economy.⁷⁷

OPIC continues to be a major force in this area and is instrumental in the development of various infrastructure projects in the emerging markets throughout the world. Though it is restricted by the US foreign policies, such measures have also proved beneficial in certain instances. The congressional mandate

⁷⁷ 22 U.S.C. § 2191(k), 2191 (l) (1988)

creating OPIC requires that OPIC offer insurance only to projects in a nation that complies with certain standards of environment and worker rights and human rights. Nations needing the inflow of foreign investment, particularly American investment will need to action to meet the best practice requirements set by the US government. This results in better policies being implemented in the developing countries.

Finally MIGA is one of the multilateral investment guarantee agency that provides political risk insurance. The following will highlight MIGA's political risk insurance and how it has affected the development of infrastructure projects globally.

Multilateral Investment Guarantee Agency (MIGA)

MIGA is an autonomous body⁷⁸ which, according to article 2 of the Convention Establishing the Multilateral Investment Guarantee Agency, was established to encourage the flow of investments for productive purposes among its member countries, and in particular to developing member countries.⁷⁹ MIGA will guarantee eligible investments against losses resulting from non-commercial risk and carry out research and promotional activities.

The MIGA convention provides for coverage against transfer risk resulting from host government restrictions on currency conversion and transfer, risk of loss of resulting from legislative actions or administrative actions or omissions of

⁷⁸ Ibrahim F. Shihata, *The Multilateral Investment Guarantee Agency*, 20 INT'L LAW. 485, 488 (1986).

⁷⁹ *See Id.*

the host government which have the effect of depriving the foreign investor of its ownership or control of or substantial benefits from its investment, the repudiation or breach of government contracts in the cases where the investor has no access to competent judicial or arbitral forum or faces unreasonable delays in such forum or is unable to enforce a judicial or arbitral decision in its favor and the risk of armed conflict and civil disturbance.⁸⁰

In the 1970's development was largely financed by commercial lending.⁸¹ The private banks loaned great sum of money based on the economic outlook of the developing nations. However, the outstanding debt of the developing countries grew astronomically and they were unable to service their debts, which in turn lead to the world debt crisis and prompted banks to reduce lending to the developing countries.⁸²

The world debt crisis also led to rethinking of ways to finance development in the emerging markets. Rather than extend loans to governments, which in the past had proven to be ineffective in addition to causing unstable economic conditions worldwide it appeared that the best way to promote development would be through investment where the repayment is through the revenue generated only by the investment project and not on the foreign government's balance sheet.⁸³

⁸⁰ 24 I.L.M. 1598, 1599

⁸¹ Ibrahim F. Shihata, *The Multilateral Investment Guarantee Agency*, 20 INT'L LAW. 485, 486 (1986)

⁸² *See Id.*

⁸³ *See supra note 81, at 487*

Though there are ample opportunities for investments in the emerging markets investors are wary of these markets due to the financial crises of the past, the inability of the developing countries in honoring their financial debts and the unstable political conditions prevailing in these regions. The emerging markets lack the confidence inducing political, economical and judicial structure that investors are used to in their own countries.

MIGA is essentially designed to overcome this hurdle by providing insurance against political risks and also contributing to the overall improvement and stabilization of investment conditions in the host countries.⁸⁴ The objective of MIGA is to encourage the flow of investments for productive purposes among its member countries and in particular to developing member countries. MIGA is intended to enhance mutual understanding and confidence between host governments and foreign investors, heighten awareness of investment opportunities and increase information, knowledge and expertise related to the investment process.⁸⁵

Infrastructure development is an area where MIGA has extensive experience. Since its establishment in 1988 the agency has issued more than \$5.6 billion in investment guarantees alone for infrastructure projects and facilitated roughly five times that amount in overall infrastructure investment.

⁸⁴ See Ibrahim F. Shihata, *The Multilateral Investment Guarantee Agency*, 20 INT'L LAW. 485, 487 (1986)

⁸⁵ 24 I.L.M. 1598, 1600

MIGA Coverage

The convention establishing MIGA specifically provides for four broad categories of non-commercial risks. They are the transfer risk resulting from host government restrictions on currency conversion and transfer; the risk of loss resulting from legislative actions or administrative actions or omissions of the host government which have the effect of depriving the foreign investor of its ownership and control of or substantial benefits from, its investment; the breach of contract in the cases where the foreign investor has no access to competent judicial or arbitral forum, or faces unreasonable delays in such a forum or is unable to enforce a judicial or arbitral decision issued in its favor; and the risk of armed conflict and civil disturbance.⁸⁶

Eligible Investments

To be eligible for MIGA insurance, investments will have to be new and of a medium or long-term nature. They must be determined by the agency to be sound investments, which contribute to the development of a host country, comply with its laws and are consistent with its declared development objectives and priorities.⁸⁷

To be eligible for the agency's guarantee the investors must be nationals of a member country or in the case of corporate investors, must either be incorporated and have their principal place of business in a member country, or

⁸⁶ Article 11 of the Convention Establishing the Multilateral Investment Guarantee Agency.

⁸⁷ Article 12 of the Convention Establishing the Multilateral Investment Guarantee Agency.

the majority of their capital must be owned by nationals of a member country or countries.⁸⁸

MIGA will not conclude any contract of guarantee before the host government has approved the issuance of the guarantee by the agency against the risks designated for cover. This is mainly due to MIGA's recognition of the host government's sovereign control over the admission of foreign investment into their territories and the treatment of such investment.⁸⁹

In order for the agency to issue an investment guarantee it must first be established that the investment meets certain conditions set forth in the convention. The reason why these conditions are in place is to reflect MIGA's developmental objectives and also to protect its financial viability. MIGA is very strict in screening an investment and it must be satisfied that the proposed investment complies with the host country's laws and regulations, is economically sound and contributes to development.

Further, the investment conditions of the host country must be assessed to ensure the availability of fair and equitable treatment and legal protection for the investment. If in MIGA's opinion, such conditions do not exist, MIGA would seek to enter into agreement with the potential host country on the treatment of investments guaranteed by it.

⁸⁸ Article 12 of the Convention Establishing the Multilateral Investment Guarantee Agency.

⁸⁹ 24 I.L.M. 1598, 1601

Claims and Settlement of Disputes

When an investor submits a claim alleging hostile actions by the host country MIGA will pay the claim and assume all the rights that the indemnified had acquired against the host country as a result of the event-giving rise to the claim. MIGA will have recourse to international arbitration unless otherwise agreed upon between the parties.

In the event of a conflict, MIGA's involvement facilitates an amicable settlement. MIGA will be able to depoliticize settlement of investment disputes.⁹⁰ In the past investment disputes between host countries and foreign investors have escalated into disputes between sovereign states, the host country and the state of the investor. MIGA essentially removes the foreign investor and the investor's home state from the dispute.⁹¹ MIGA has access to an immense resource of information and vast experience in dealing with claims made by investors.⁹² MIGA has to assess all claims prior to either settling the claim with the investor or denying it. This process provides MIGA with a better understanding of the entire situation both from the investors as well as the host countries perspective.⁹³ MIGA will utilize its position as an honest broker and

⁹⁰ Gregg B. Brelsford, *International Investment Insurance - The Convention Establishing the Multilateral Investment Guarantee Agency*, Reprinted in 24 I.L.M. 1518, 1605 (1985), 27 HARV. INT'L L.J. 735, 743 (1986).

⁹¹ See *Id.*

⁹² Ibrahim F. Shihata, *The Settlement of Disputes regarding Foreign Investment: The Role of the World Bank, with Particular Reference to ICSID and MIGA*, 1 AM. U. J. INT'L L. & POL'Y 97, 114 (1986).

⁹³ See *Id.*

assist in resolving disputes and increasing the likelihood of a settlement between the parties.

MIGA also settles investment disputes between parties by accepting the local currency of the host country and pay the investor out of its own funds in freely usable currency. Subsequently, MIGA under an agreement with the host country sell the local currency to the Bank or other international institutions or to the host government itself over a period of time and recover its position accordingly.⁹⁴

Private Insurers Providing Political Risk Insurance

In addition to the above mentioned risk insurance provided by bilateral and multilateral institutions investors can purchase political risk insurance from private insurers as well. The most experienced private insurer in this field is Lloyds of London while other insurers include American International Group, Citicorp International Trade Indemnity, Chubb Group and Poole d'Assurance des Risques Internationaux et Speciaux (P.A.R.I.S).

One of the most important benefits of obtaining private political risk insurance is that there are no policy mandates limiting availability as in political risk insurance provided by OPIC, EXIM Bank and other bilateral institutions.⁹⁵ It should also be noted that the private insurers are purely profit driven and hence

⁹⁴ Ibrahim F. Shihata, *The Settlement of Disputes regarding Foreign Investment: The Role of the World Bank, with Particular Reference to ICSID and MIGA*, 1 AM. U. J. INT'L L. & POL'Y 97, 114 (1986).

⁹⁵ Marvin W. Tubbs, *Political Risk Insurance: The Potential Effects of Privatization on Credit Availability*, 16 ANN. REV. BANKING L. 553, 553 (1997).

concern for sociological and environmental impacts are nonexistent in determining availability of insurance.⁹⁶ Private insurance providers evaluate each project, investor and country to determine risk level rather than making general restrictions based on policies. Since the private insurance providers are very risk averse, they usually provide political risk insurance only for short term investments.

Insurance coverage from private insurers ranges from \$5 million to a maximum of \$200-250 million per project provided by Lloyds. This is comparable to the risk insurance provided by both OPIC and MIGA.⁹⁷

⁹⁶ Marvin W. Tubbs, *Political Risk Insurance: The Potential Effects of Privatization on Credit Availability*, 16 ANN. REV. BANKING L. 553, 553 (1997).

⁹⁷ Malcom D. Rowat, *Multilateral Approaches to Improving the Investment Climate of Developing Countries: The Case of ICSID and MIGA*, 33 HARV. INT'L L.J. 103, 126 (1992).

CHAPTER 5

CONCLUSION

An emerging economy, in order to provide proper living conditions for its citizens, in addition to being economically successful and competitive in today's global market should have proper infrastructure in place. Project Financing is the most versatile and secure mode of transport of foreign direct investment from developed countries to emerging markets. It not only enables the implementation of the oft required large-scale infrastructure projects such as power plants, telecommunication, roads, etc., but also assists in transfer of technology, management skills and other goods and services which might otherwise not have been transferred. It should also be pointed out that in more recent times project finance has been used to implement all other kind of smaller projects such as installation of potable water facilities in Africa and construction of building in Asia and South America. This rapid development would not have been possible in the absence of the non commercial risk insurances such as political risk insurance and insurance against currency transfer issued by multilateral agencies.

The success of infrastructure projects in the emerging markets depends on the ability of both the host nation and the investor to identify, allocate and mitigate risk accordingly. Multilaterals such as MIGA have helped usher in the realm of safe and secure investment measures for the developed countries which have resulted in some vast amounts of international funds being invested in the

emerging markets. MIGA and other multilateral institutions encourage the flow of investment and along with it the flow of technology and training on terms acceptable to all parties. MIGA has had a catalytic effect on investment insurance programs, prompting nations to become more active and expand their programs. MIGA has played a vital role in depoliticizing investment disputes between sovereign states and enabling payments to investor nations.

Though the recent trend towards project financing of long-term infrastructure projects has proven very successful it should not be the only way for implementing such projects. The multinational financial institutions should continue to assist developing nations by providing them with grants for development where required. This ensures a balanced approach for the growth of the developing countries and assists them to sustain such growth.

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