EXTRACT FROM:
WORLD BANK PORT REFORM TOOL KIT
Financial Implications of Port Reform, Part II,
Principles of Financial Modelling, Engineering and Analysis

The World Bank Guarantee Programme

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Since 1994, the World Bank promotes the use of political risk mitigation guarantees to address the growing demand from sponsors and commercial lenders contemplating financial investment in the infrastructure sectors of developing countries. The Bank's objective in mainstreaming guarantees is to mobilise private capital for such projects on a "*lender of last resort*" basis whilst minimising the host government's requisite indemnity to the Bank as a condition of providing the guarantee.

World Bank guarantees are provided to private lenders, for infrastructure financing, where the demand for debt funding is large, political and sovereign risks are significant, and long-dated financing critical to a project's viability.

The Bank offers commercial lenders a variety of guarantee products: Partial Risk, Partial Credit, Enclave and Policy-based guarantees in IBRD countries, and Partial Risk Guarantees in IDA-only countries. Broadly speaking, all guarantees provide coverage against debt-service default arising from sovereign risk events, each guarantee issued is tailored to match the specific need of an individual transaction.

IBRD guarantees are offered for projects in IBRD eligible countries, with the exception of certain foreign exchange earning projects in IDA-only countries. IBRD guarantees can be both Partial Risk and Partial Credit in nature. Bank guarantees are generally available for projects in any eligible country, irrespective of whether the project is in the private or public sector. The bank may, however, at times limit the availability of guarantees in certain countries, for example in countries undergoing debt restructuring.

IBRD Partial risk guarantees ensure payment in the case of debt service default resulting from the non-performance of contractual obligations undertaken by the government or their agencies in private sector projects. Sovereign contractual obligations vary depending on project, sector and circumstances. They typically include:

- Maintaining an agreed regulatory framework, including tariff formulas;
- Delivering inputs, such as fuel to a private power company;
- Paying for outputs, such as power or water purchased by a government utility;
- Compensating for project delays caused by political actions or events.

Partial risk guarantees may also cover transfer risks that may be caused by constraints in the availability of foreign exchange, procedural delays and adverse changes in exchange control laws and regulations.

Partial Credit guarantees cover all events of non-payment for a designated portion of the financing. While historically these guarantees have been used to encourage extension of maturity by covering the later years of the financing, the Bank recently structured a partial credit guarantee to cover a single coupon interest payment on a rolling basis throughout the life of the facility, plus the final bullet principal repayment.

Enclave guarantees are highly selective partial credit guarantees structured for export oriented foreign exchange generating commercial projects operating in IDA-only countries. Enclave guarantees may cover direct sovereign risks such as expropriation, change in law, war, and civil strife but may not cover third party obligations (such as those of an output purchaser or input supplier), nor will it guarantee transfer risk. In all cases, the scope of risk coverage under the guarantee would be the minimum required to mobilise financing for a given project.

Partial Risk guarantees are used in IDA member countries, in sectors undergoing significant reforms. IDA guarantees are offered on a pilot basis to private lenders against country risks that are beyond the control of investors and where official agencies and private markets currently offer insufficient insurance coverage. IDA guarantees are available selectively, where an IBRD Enclave guarantee is not available. IDA guarantees can cover up to 100 percent of principal and interest of a private debt trench for defaults arising from specified sovereign risks including government breach of contract, foreign currency convertibility, expropriation, and political violence.

Bank guarantees facilitate the mitigation of risks that lenders cannot assume, catalyse new sources of finance, improve borrowing costs, and extend maturity beyond what can be achieved without the bank guarantee. They also provide more flexibility in structuring project financing (currency, market, etc.).

Clearly, within the World Bank Group, IFC and MIGA are the preferred sources of support to the private sector. As such, sponsors and financiers should consult with IFC and MIGA as to their potential interest in financing or covering the project. IFC supports private sector projects through equity and debt financing, the syndicated B-Loan programme, security placement and underwriting and advisory services. MIGA provides political risk insurance primarily for equity investments, but it can also cover debt financing, as long as it is also covering equity finance for the same project. These agencies cannot accept host government guarantees.