

Terrifying Insurance

When bridges, hotels, and other structures are hit by bomb blasts, not only do media show up but also insurance adjusters as more and more political risk policies now cover terrorism

By Keith Rosenblum



Illustration by Gerry Castro

In conflict zones, few investors are eager to back the building of roads, bridges, and other vital infrastructure needed to bring peace and stability. Not only are such harsh investment climates unpredictable, but they are also literally deadly.

Political risk insurance, an increasingly important part of the portfolio of major international financing organizations worldwide, was designed to address these problems by protecting investors against every kind of ominous scenario that might plague an unstable host country, except the vagaries of the market.

After the terrorist attacks of September 2001 in the United States, political risk insurance was expanded. Today, when bridges, hotels, and other structures are hit by bomb blasts, not only do media show up, but also insurance adjusters are increasingly likely to be on the scene as more and more political risk policies now cover acts of terrorism.

One example is the 5-year-old Afghanistan Investment Guarantee Facility (AIGF). The \$60 million fund, offered through the Multilateral Investment Guarantee Agency (MIGA), which is part of the World Bank Group, is one of a few of its type. Covered under the plan are expropriation, sabotage, terrorism, civil disturbances, war, inability to convert local currency, and, in some cases, breach of contract.

“We are saying to investors, ‘Don’t worry about the political situation or any events that may lead to a loss—just come and concentrate on your merchant abilities,’” says Nabil Fawaz, MIGA’s sector leader for agribusiness, manufacturing, and services. “Our job is to create the same comfort level the entrepreneur feels elsewhere. People swoop in and sell 10,000 air-conditioning units, but what we want is the assembly plant.”



TERRORISM RISK PROTECTION Pakistani bystanders and rescue workers are seen beside a huge crater outside the burning facade of The Marriott Hotel in Islamabad on September 20, 2008, following a powerful bomb blast. The blast triggered a variety of claims associated with political risk insurance that covers acts of terrorism.

Political Violence

MIGA and its US counterpart, Overseas Private Investment Corporation (OPIC), as well as some private insurers, have settled numerous claims for terrorist acts; the types and amounts of settlements are rarely disclosed.

Some confusion persists regarding the classifications of settlements. OPIC, for example, pays its political risk insurance under the following categories: inconvertibility (of currency), expropriation, war damage, and political violence.

In the broad “political violence” category, OPIC has paid out about two claims a year over the past decade or so. Included are those specifically classified as “terrorism”—sabotage of a gold mine by Revolutionary Armed Forces of Colombia, or FARC, and a rash of vehicles destroyed in Iraq and Afghanistan.

Political risk insurance was first offered in Afghanistan in July 2004, a year after the country joined MIGA. Its initial sponsors included the International Development Association, a World Bank entity that contributed \$5 million; the Asian Development Bank, which contributed a

\$5 million “soft loan”; and MIGA, which contributed \$10 million. With additional support from private insurers, coverage tripled to \$60 million.

In addition to the International Home Finance & Development, LLC (see sidebar), beneficiaries of the plan to date include MTN Group Limited, a cell phone enterprise based in South Africa; the Afghanistan Project for Cotton and Oil Development, a French cotton gin project; and ShoreCap International Ltd., a banking venture based in the Cayman Islands.

Investments under AIGF may originate in any of MIGA’s 168 member countries and may extend to additions to ventures and acquisitions of state industry. Coverage is available for 7 years, though longer terms may be obtained through MIGA coinsurance. MIGA insures up to 90% of equity investments and 450% of an initial investment to cover earnings directly attributable to it.

Coverage has made a difference in investment possibilities in Afghanistan, as signs of expatriate and newcomer investment alike have appeared throughout the country of 30 million people.

Afghans have logged record advances in living standards since 2001, largely due to the fact that conditions bottomed out for most people. Afghans dispersed throughout the West have led the charge both in numbers and dollars to help rebuild what the World Bank labels a “post-conflict” nation.

The business climate, for most, hardly suggests a “post-conflict” society. Even MIGA will not back loans in many of Afghanistan’s 34 provinces. Officials from the World Bank and international organizations, including the US Department of State, depict a dangerous atmosphere with a tenuous investment climate, where investors are subject to physical danger, corruption, excessive bureaucracy, and few legal guarantees. Some official briefs even warn investors against flying into Kabul, let alone investing.

Drinking a Lot of Tea

A key to bringing foreign investment to Afghanistan is making the right pitch to the public ideologically and business-wise—emphasizing that investments will be protected, says Jeff Raleigh, who

OPIC Political Risk Insurance Payments (FY2000–FY2009)

Types of Claims: ■ - Inconvertibility ■ - Expropriation ■ - War Damage ■ - Political Violence

Investor	Country	Type of Claim	Industry	Settlement Amount
FY2000				
MidAmerican Energy Holdings	Indonesia	■	Power	\$217,500,000
F.C. Schaffer & Associates	Ethiopia	■	Manufacturing	\$9,563
Citibank, N.A.	Sudan	■	Banking	\$1,055,607
TOTAL				\$218,565,170
FY2001				
Citibank, N.A.	Sudan	■	Banking	\$3,750,000
TOTAL				\$3,750,000
FY2002				
Sector Resources/Sector Capital	Colombia	■	Mining	\$2,369,736
TOTAL				\$2,369,736
FY2003				
Sector Capital Corp.	Colombia	■	Mining	\$514,410
Bank of America	India	■	Banking	\$28,139,505
TOTAL				\$28,653,915
FY2004				
Ben Dabhol Holdings Ltd.	India	■	Power	\$31,744,922
GE Capital Project Finance	India	■	Power	\$31,803,775
Sector Capital Corp.	Colombia	■	Mining	\$265,757
Shelter for Life International	Afghanistan	■	Services	\$29,857
Bank of America, NA a/b/	Colombia	■	Power	\$7,600,000
Bechtel India Power Investment a/c/	India	■	Power	\$9,995,000
GE EFS India Holdings a/c/	India	■	Power	\$9,995,000
Offshore Power Production CV a/c/	India	■	Power	\$400,000
Scientific Applications International Corp.	Venezuela	■	Services	\$5,875,000
AES Corporation a/	Colombia	■	Power	\$3,200,000
TOTAL				\$100,909,311
FY2005				
Ponderosa Assets LP	Argentina	■	Oil and Gas	\$50,000,000
TOTAL				\$50,000,000
FY2006				
Western Wireless International Corp.	Haiti	■	Telecom	\$54,209
Team Technology Inc.	Eritrea	■	Manufacturing	\$91,875
ABI Group, Ltd.	Afghanistan	■	Manufacturing	\$19,970
Caterpillar Financial Services Corp.	Venezuela	■	Transportation	\$2,644,989
TOTAL				\$2,811,043
FY2007				
Sector Resources, Ltd.	Colombia	■	Mining	\$75,548
TOTAL				\$75,548
FY2008				
Uniworld Holdings, Ltd.	Serbia	■	Services	\$1,980,000
TOTAL				\$1,980,000
FY2009				
International Rescue Committee	Democratic Republic of Congo	■	Services	\$36,232
International Rescue Committee	Afghanistan	■	Services	\$38,257
International Rescue Committee	Chad	■	Services	\$130,680
International Rescue Committee	Afghanistan	■	Services	\$1,000
TOTAL				\$206,169

Source: Overseas Private Investment Corporation (OPIC), www.opic.gov

a/ Without determining that expropriatory action had occurred, OPIC and the investor agreed on a negotiated sum in settlement of the claim, avoiding a contest over complex, ambiguous legal and factual issues.

b/ The settlement amount includes a provisional payment in the amount of \$4,372,492 made on 27 November 2002, which was made final by the terms of the settlement.

c/ These three payments were all in settlement of the claim of Offshore Power Production CV, an affiliate of Enron Corp.

MIGA War and Civil Disturbance Payments

Guarantee Holder	Country	Industry	Settlement Amount
FY2005			
Undisclosed	Nepal	Power	\$144,600
FY2009			
Kibos Sugar and Allied Industries Ltd.	Kenya	Manufacturing	\$491,100
Louvre International Ltd.	Madagascar	Tourism	9,273 euros (\$12,824)
TOTAL			\$648,524

Note: MIGA has paid only five claims since its inception in 1998.

Source: Multilateral Investment Guarantee Agency (MIGA), www.miga.org

recently returned to the US after 4 years in Afghanistan, first as a foreign service officer then as a private communications worker.

“We have done a terrible job in explaining the invasion and liberation. We need to learn from that and do a better job explaining why the country now needs foreign investment,” he says. Mr. Raleigh has developed a fondness for the country’s highly personal business networking. “I drank a lot of tea and made new friends while I was waiting and waiting and waiting.”

One area not ripe for new investment is online commerce, he cautions. “Once people online see an internet protocol address from Afghanistan, you’re basically blocked out: no one will ship to you.”

Regardless of incentives, there are limits to what political risk insurance alone can accomplish in a nation’s development.

Louis T. Wells, a Harvard Business School professor and coauthor of *Making Foreign Investment Safe: Property Rights and National Sovereignty*, notes that MIGA and OPIC help create initial investment and pave the way for private risk providers.

“There are two simple questions: ‘Will it work and at what cost?’ There are potential moral hazards here. An investor can find himself in trouble for whatever reason, political or otherwise, and then move in and collect,” he explains.

Since public risk insurance providers have the backing of government, they can instruct the host government to reimburse claims paid out, which can create the potential for fraud, he explains. “It’s the commercial equivalent of burning down your own house.”

Robert E. Svensk is a political risk insurance veteran who started his career at OPIC, then built AIG Political Risk Inc. from a \$500,000 annual business at inception to a \$55 million business in 7 years. He sees the current public risk insurance entities as good pilot projects.

Adjusting for inflation, the amounts guaranteed by MIGA or OPIC are actually less than decades ago, he says, pointing to the inevitability of business going to the dozens of political risk insurers that have sprung up in the past 20 years. Nothing will ever replace the “nimbleness” of the private sector, he says, because private companies “don’t have to prepare 800 politically mandated labor, environmental, and workplace studies before taking action.”

In the public sector, Rod Morris, OPIC’s current vice-president of insurance, says a government-backed insurance entity can be especially vigilant at

guarding against contract violations by foreign governments, including “creeping expropriations.”

“There are lots of ways to deprive you of your investment rights,” he says. “Breaches don’t always [occur] suddenly with a gunboat.”

For development prospects in Afghanistan and other fledgling free-market economies, however, the public versus private insurers debate is a moot point.

These countries offer “bonanzas” and “heartbreak,” says Emily L. Walker, a London-based consultant who has held positions in financial services, government, and humanitarian agencies.

“One of the best ways to combat terrorism is job creation—even if it’s in a dangerous area,” says Ms. Walker, who has served on a Department of Homeland Security (DHS) advisory council. “Jobs give kids something to do other than plan killing kids on the other side of a border.”

If a problem arises with a MIGA-backed project, she says, “They pick up the phone and have a direct line with a secretary of finance. That’s an excellent mechanism.”

Businesspeople are in deals to make money—not to collect on insurance, Ms. Walker explains. “Afghanistan is a long way to Tipperary. No one is there to make what they can make at home; they want to be rewarded.” ●



RECOUPING LOSSES A massive bomb ripped through the downtown area of the troubled Afghan city of Kandahar in August 2009. Some bombings in Afghanistan are being covered by an innovative form of political risk insurance that covers acts of terrorism.

Answering the Plea

Political risk insurance helps bring Afghans home to invest

Rafaat Ludin has answered the plea that invariably finds its way across continents to the ears of every member of the Afghan diaspora.

The messengers are as varied as diplomats and nongovernment organizations, chambers of commerce and religious organizations. But the plea is always the same: come back and give the homeland a boost.

In Mr. Ludin’s case, answering the plea means a trek every other month that begins with Los Angeles traffic and, 48 to 60 hours later, ends in Kabul—home to “The GreenMachine” and the 45-year-old entrepreneur’s dreams of lifting beleaguered-but-eager compatriots up another notch.

The odyssey has paid dividends: business is good. The GreenMachine, a patented, 1-ton, diesel-powered brick-making device, is a hit with Kabul home-builders and United States military personnel alike. The GreenMachine has built a small mosque at the Ministry of Education. Response to production from the three existing machines, airlifted to Afghani-

stan from the US, has been so enthusiastic that Mr. Ludin plans to manufacture another 10 in Kabul, he says. “With a trained workforce, there should be no difference whatsoever in quality.”

The challenges of doing business in a country devoid of services, lacking in training programs, and scarce of infrastructure, is nothing new for Mr. Ludin. In fact, the German-educated businessman, whose family left Afghanistan when he was 12, has embarked on his own Afghan reconstruction mission as a less stressful alternative to his former career in German industry, which he blames for a mid-life stroke.

Today, Mr. Ludin and partners hold interests in an array of Afghan renewable energy projects, and he moves, always with his Blackberry, from the West to Afghanistan and back like a migratory bird.

In many ways, The GreenMachine venture is the embodiment of the project so desperately sought by architects of Afghanistan’s reconstruction. In a single package, the machine weds a wanting population to affordable housing, manufacturing jobs, and ecologically sensitive technology.

Yet, for as smoothly as this venture has gone, the remarkable truth is just how close a logical, commercially viable project came to never existing at all.

Were it not for political risk insurance—which adds from 1.75% to 3.5% to the cost of doing business—there would be nothing today. “I might have looked at doing this myself, but it was going to take the insurance to convince investors,” he explains.

Mr. Ludin says the machines in Kabul and at a US military base could be targeted by militants at any time. Knowing they are financially protected is “a relief,” he says, that allows him to concentrate on the tasks of running the business.

He rattles off a list of daily concerns: low temperatures freeze The GreenMachine’s oil in the winter; software issues have repeatedly crippled one of the machines; silt, clay, and cement supply issues always crop up in Kabul....

These problems—and not potential loss of patrimony—are the issues that happily concern Mr. Ludin. ●