MIGA Credit Enhancement: NHFO

The Non-Honoring of Financial Obligations (NHFO) is a credit guarantee offered by the Multilateral Investment Guarantee Agency (MIGA), a World Bank Group entity. The guarantee can protect the lender (or investor) against losses resulting from a sovereign, sub-sovereign or state-owned enterprise’s failure to make a payment when due. Under this coverage, if a borrowing entity fails to pay any installment covered by the guarantee, MIGA will pay the lender within six months of the date of loss, without the need for arbitration proceedings. This coverage is only applicable in situations where the obligation is unconditional and not subject to defenses.

Examples:
- Sovereign government or eligible sub-sovereign entity acts as borrower and is unconditionally obliged to repay a cross-border loan
- Sovereign government or eligible sub-sovereign entity unconditionally guarantees repayment of loan by sub-sovereign entity, state-owned enterprise, or private-sector project
- Sovereign government or eligible sub-sovereign entity assumes unconditional obligation to inject equity or other funding on demand or at a certain date (e.g. minimum revenue guarantee)
- Sovereign government or eligible sub-sovereign entity enters into a derivatives contract under which it is obligated to make payments to the counterparty

Potential structures

The NHFO can be structured in various ways to raise the required financing for a project, while reducing the exposure to default risk such as:
- Stand-alone MIGA NHFO to attract private sector financing
- IBRD loan + MIGA NHFO to support additional private sector funding
- IBRD credit guarantee covering first loss + MIGA NHFO covering long end of private sector financing

Benefits

The NHFO is tailored to meet the needs of both borrowers and creditors.

Borrowers: The NHFO boosts market confidence by mitigating the credit risk of a government or sub-sovereign entity. Benefits to borrowers include access to crucial financial resources, improved financial terms, opportunity to establish new lending relationships, and increased likelihood of project success. MIGA products are not subject to IBRD credit exposure limits. With the help of the NHFO, countries that are close to these limits can finance a project with less impact on their IBRD envelopes and receive better terms: maturity, cost-structure, volume.

Creditors: Commercial lenders and investors that provide funding to public sector entities for infrastructure and other productive investments are important beneficiaries of this product. If a borrower defaults, the NHFO will ensure that payments are made to the lender. By covering a large share of the default risk, the NHFO can help the lender reduce the potential for loss. The NHFO is also designed to be Basel II compliant, meaning that banks may receive more favorable capital treatment for loans that benefit from this form of coverage. Moreover, MIGA’s project monitoring and due diligence reduces project-specific risk to the lender, which is difficult to diversify. With the support of the NHFO, banks can prudently extend their risk horizons, potentially enter new markets, and offer financing at more competitive terms and conditions.

The World Bank’s involvement is not necessary for projects covered by MIGA. However, clients may benefit from leveraging the synergies of various World Bank Group entities. For example, partnering with IBRD allows MIGA to reduce administrative costs related to project preparation and monitoring, which can translate into lower premia for coverage of credit risk.
**Figure 1: Basic NHFO guarantee structure**

- Host country approval
- **MIGA**
- NHFO guarantee
- **Borrower: Ministry of finance or eligible sub-sovereign entity**
- **Sovereign government**
- **Commercial lender/investor**
- Commercial loan in major currency

---

### Major Terms and Conditions

<table>
<thead>
<tr>
<th>Purpose</th>
<th>To help emerging market sovereigns and sub-sovereigns access funding on more advantageous terms than may be available solely on the basis of their own international credit standing</th>
</tr>
</thead>
</table>
| **Value Added** | - Reduces exposure to default risk  
- Basel II compliant; banks may receive capital relief  
- Does not utilize countries’ credit limit with IBRD |
| **Eligibility** | - **Cross-border investment from one MIGA member country** (developed or developing) into another developing member country  
- Investment projects must be **financially and economically viable.** Cash flows must be identified to service the debt.  
- The underlying project must have a **development impact** and be consistent with IMF and World Bank country and sector strategies.  
- The NHFO covers payment default of **sovereign and sub-sovereign obligations.** |
| **Coverage amount** | Up to 95% of principal and interest |
| **Pre-approval Criteria** | - Obligations must be valid, enforceable and in full force and effect (not subject to legal defenses)  
- Compliance with MIGA/IBRD’s environmental and social guidelines, as applicable |
| **Tenor** | Minimum 1-3 years, up to 15 years (20 years on an exceptional basis) |
| **Pricing** | - Premium rates are determined on a per project basis and vary by country, sector, and transaction. Premium is paid by the lender or investor.  
- Premium may be paid annually or semi-annually and is calculated as a percentage rate applied to the amount of coverage. Premium may also be paid on an upfront basis.  
- A standby fee (between 25-30% of the premium rate) is charged on undisbursed amounts and future or “non-current” interest. |

**Contact:** (on structures involving World Bank projects): **Miguel Navarro-Martin,** Head of Banking Products, Mnavarromartin@worldbank.org, +1 (202) 458-4722; (on stand-alone MIGA guarantees): **Muhamet Fall,** Lead Underwriter, mfall3@worldbank.org, +1 202 458-2695

---

1. See list of MIGA member countries at http://www.miga.org/whoweare/index.cfm?stid=1789

---

Updated May, 2016