USAID
FROM THE AMERICAN PEOPLE

DCA PHILIPPINES LGUGC EVALUATION

REPORT

DCA PHILIPPINES LGUGC EVALUATION

REPORT

OCTOBER 2009

This publication was produced for review by the United States Agency for International Development. It was prepared by SEGURA/IP3 Partners LLC under the SEGIR Global Business, Trade and Investment II Indefinite Quantity Contract (IQC), Number EEM-I-00-07-00001-00 Task Order # 04, Development Credit Authority Evaluation.

TABLE OF CONTENTS

TABLE OF TABLES

TABLE OF FIGURES

ACKNOWLEDGEMENTS

The evaluation team gratefully acknowledges the assistance and support received from many sources during the conduct of this evaluation. Specifically, the team would like to express its sincere appreciation to the following:

- Sashi Selvendran, EGAT/DC, who accompanied the evaluation team on the field trip to the Philippines and whose information and observations were invaluable during the entire process of the evaluation;

- Mary Joy Jochico, USAID's Philippines Mission, who participated in many of the interviews conducted during the evaluation, and provided useful background and insight into the developments affecting the Philippines DCA guarantee during the in-country data collection phase, as well as the other personnel of the USAID Philippines Mission who contributed their time and experience to the benefit of the evaluation, particularly Maria Cynthia Nona M. Razo of the Financial Management Services Division;

- Lydia N. Orial, President and CEO of LGUGC, who generously shared her extensive knowledge of the private financial sector in the Philippines, and the organization's operations;

- The staff of the LGUGC for their assistance and cooperation, especially Thelma Sansales for her tireless efforts to timely respond to the data requests of the evaluation team, and Aileen Castro for her valuable information on the marketing and outreach efforts of the enterprise;

- Alma Porciuncula who provided important background and data regarding the development of the Philippines Water Revolving Fund;

- Celia Soriano whose expertise in water sector financing was of significant assistance to the evaluation team, and Jesus Tirona who provided helpful information on the evolution of LGUGC;

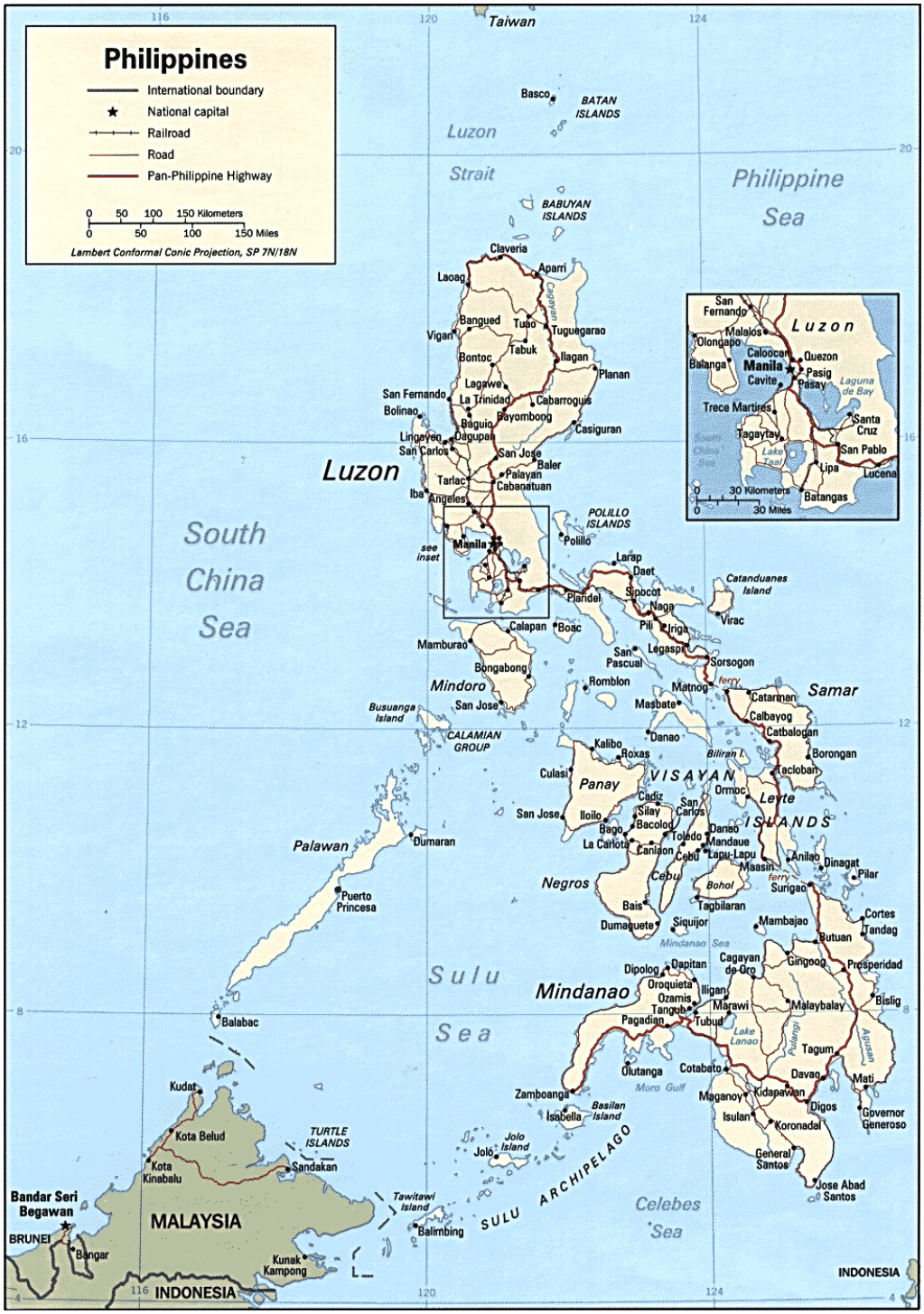
- Chie Cruz who arranged meetings and organized in-country logistics for the evaluation team; and

- The many key informants from the Government of the Philippines, private and government financial institutions, local government units and water districts who took the time to meet with and supply data to the evaluation team.

ACRONYMS

ADB	Asian Development Bank
BAP	Bankers Association of the Philippines
CMS	USAID Credit Management System
DBP	Development Bank of the Philippines
DCA	Development Credit Authority
EGAT/DC	USAID Economic Growth, Agriculture and Trade Bureau's Office of Development Credit
GFI	Government Financial Institution
IFI	International Financial Institution
IRA	Internal Revenue Allotment
JBIC	Japan Bank for International Cooperation
JICA	Japan International Cooperation Agency
LBP	Land Bank of the Philippines
LGU	Local Government Unit
LGUGC	Local Government Unit Guarantee Corporation
LWUA	Local Water Utilities Administration
MDG	Millennium Development Goals
ODA	Official Development Assistance
PFI	Private Financial Institution
PNB	Philippine National Bank
PWRF	Philippines Water Revolving Fund
TA	Technical Assistance
USAID	United States Agency for International Development
WD	Water District

MAP OF THE PHILIPPINES



I. EXECUTIVE SUMMARY

By the late 1990s it had become apparent that the needs for capital investment in local infrastructure for the rapidly urbanizing Philippines exceeded that which could be provided by the central government and international donors, and that private capital would have to be mobilized to permit the population access to essential services. Much of the responsibility for local infrastructure rested with local government units (LGUs), which had the authority to borrow for such purposes. However, LGUs were reluctant to borrow, and when they had borrowed, they had done so almost exclusively from government financial institutions (GFIs). Private financial institutions (PFIs) in turn had been reluctant to lend to LGUs due to a lack of information about and familiarity with LGUs, skepticism about their creditworthiness, and a tradition of conservative lending practices.

To bridge the gap between potential and actual private LGU financing, the Philippines Department of Finance launched an initiative to develop a municipal bond market that led ultimately to the formation of the Local Government Unit Guarantee Corporation (LGUGC) with the assistance of the United States Agency for International Development (USAID). Incorporated on March 2, 1998 and initially capitalized at approximately US$6 million, LGUGC is a private financial credit guarantee institution created with the initial objective to make private financial resources available to creditworthy LGUs through its credit enhancement facility. LGUGC is jointly owned by the Bankers Association of the Philippines (BAP), Development Bank of the Philippines (DBP or Development Bank) and the Asian Development Bank (ADB).

In June 1999, USAID entered into a Development Credit Authority (DCA) agreement with LGUGC (DCA Guarantee Number 492-99G-001) to re-guarantee 30% of the principal and interest LGUGC is obligated to pay in the event of default of an eligible loan. The original purpose of the DCA agreement was "to strengthen the LGUGC's ability to mobilize private capital lending for local government infrastructure services and facilities in the Philippines." However, over the course of the agreement, its purpose evolved.

With the launch of the Clean Water for People initiative in 2002 by Japan and the U.S. and the release of Executive Order 279 (EO 279) by the Philippines government in 2004, the Philippines water sector assumed a high priority for all three governments. EO 279 mandated sweeping reforms in the financing of water service providers and laid the groundwork for the private financing of water projects. In response to these developments, the DCA Guarantee Agreement was amended in October 2004 to focus on revenue generating water infrastructure projects of LGUs. The DCA Guarantee Agreement was again amended in January 2006 at the behest of LGUGC to add revenue generating water projects of water districts (WDs) as eligible for credit enhancement under the DCA guarantee.

EVALUATION OBJECTIVES

USAID's Economic Growth, Agriculture and Trade Bureau's Office of Development Credit (EGAT/DC) commissioned SEGURA/IP3 Partners LLC to conduct this evaluation of the DCA agreement with LGUGC in the Philippines. The evaluation assesses the performance of the DCA guarantee with respect to its objectives as articulated in the Action Packages and Guarantee Agreement related to the mobilization of private, commercial lending to (initially) local government units (LGUs) and (later) water districts. The evaluation was guided by an Evaluation Framework—developed by SEGURA/IP3 in conjunction with EGAT/DC and adapted to the Philippines context—that investigates results at three levels:

Output Level—Did LGUGC's use of the DCA guarantee conform to guarantee objectives as described in the Guarantee Agreement?

Outcome Level—Did the DCA guarantee influence behavioral changes at the LGUGC-level, and did LGUGC's experience with the DCA guarantee improve access to credit for entities in the target sectors outside of the DCA guarantee coverage?

Impact Level—Did the guarantee have a demonstration effect that improved access to credit for entities in the target sectors by increased lending from the private banking sector without use of the guarantee?

The scope of this evaluation extends only to LGUGC and its behavior at the output, outcome, and impact levels. The evaluation does not extend to EGAT/DC's management of the guarantee nor to the impacts of the loans on borrowers or on USAID/Philippine's objectives. At the request of EGAT/DC, the evaluation presents only findings and conclusions and does not discuss lessons learned or make recommendations.

EVALUATION METHODOLOGY

A two-person team conducted the evaluation during July 2009. The team met initially in Washington, D.C. to refine evaluation objectives and procedures, develop an evaluation framework, and to interview USAID personnel. Field work took place in Manila and outlying areas during July 8-17. Information sources for the evaluation included in-depth interviews with stakeholders; collection and review of documents related to the DCA guarantee; and information on loans and guarantees to LGUs and water districts from the USAID Credit Management System (CMS), provided by LGUGC, PFIs, and GFIs, and through independent research.

KEY FINDINGS AND CONCLUSIONS

At the **output** level, the purpose of the DCA guarantee as finally amended – *"to strengthen the LGUGC's ability mobilize private capital lending for local government infrastructure services and facilities and for water districts in the Philippines"* -- corresponded to LGUGC's strategy to facilitate private financing for infrastructure projects. The DCA guarantee, particularly the formal commitment of USAID and the U.S. Government, played a central role in helping the LGUGC achieve credibility

among PFIs and other stakeholders and in providing a measure of comfort and safety to the PFIs that appears to have been pivotal in overcoming their traditional hesitancy to lend to LGUs and water districts.

The DCA guarantee helped LGUGC mobilize a modest volume of private financing to the target sectors. Although the volume of lending was less than anticipated due to adverse external influences, LGUGC guarantees were critical in providing LGUs and water districts access to private investment where little or none had previously existed, and allowed PFIs to gain experience in new markets with substantial potential. Evidence also suggests the DCA guarantee had a positive effect on demand for water district loans by PFIs and contributed to a lengthening of tenors for loans to water districts.

Specific findings in support of these conclusions include:

- LGUGC placed 11 LGU and water district loans under DCA guarantee coverage totaling US$28,521,273, including six LGU bond issues and five water district loans.

- LGUGC's success in mobilizing private LGU and water district financing was abbetted by several other factors, including its extensive marketing and education efforts, its close and cooperative working relationship with PFIs, monitoring and evaluation suppport from USAID/Philippines and EGAT/DC, and its sound operations buttressed by technical assistance (TA).

- There were no significant differences in interest rates or the collateral required between DCA guaranteed loans and other LGUGC guaranteed loans.

- The trend of tenors under all LGUGC guaranteed loans to water districts has rapidly moved to the maximum tenor permitted under the Guarantee Agreement. The first DCA guaranteed water district loan had the same seven year tenor as all the previous DCA guaranteed LGU bond floats. Of the LGU bond issues/loans that were outside of DCA coverage, all but one had tenors of seven years or less, and the first non-DCA guaranteed water district loan had a five year tenor. Thereafter, all LGUGC guaranteed loans to water districts, whether covered by the DCA or not, carried a ten year tenor. This suggests that experience lending to LGUs and water districts under the DCA guarantee was a factor.

- PFIs have begun to understand the potential value of the water district market as a result of the lending experience gained under LGUGC guarantees as well as the above mentioned marketing and education efforts. There now appears to be substantial appetite among PFIs to increase their volume of water project loans once (if) market distortions recently caused by the Local Water Utilities Administration (LWUA) are resolved.

At the **outcome** level, LGUGC opened the municipal bond market in the Philippines, and initially enjoyed success. However, when the demand for private financing in the municipal bond market slowed, USAID leveraged the relationship with LGUGC to target water sector finance. The

existence of the DCA and LGUGC also opened opportunities for collaboration by USAID and Japan in the facilitation of private investment in the water and sanitation sectors. This eventually led to the creation of the Philippines Water Revolving Fund (PWRF), an initiative to coordinate and combine donor and PFI financing for water infrastructure projects.

LGUGC relied on the direct technical assistance provided by USAID to strengthen its technical capacity, which enabled LGUGC to enter the water district sector, improve its risk management and accounting, and monitor its guarantees effectively. The relationship begun with the DCA that led to additional technical assistance from USAID/Philippines eventually grew LGUGC into a recognized entity in the Philippines.

The LGUGC actively served the target sectors by guaranteeing loans outside of the DCA guarantee. It has begun to expand its guarantee activities outside of the target sectors, and has broadened its services by becoming program manager of three other guarantee funds for other organizations.

The findings on which the conclusions are based include:

- All stakeholders interviewed stated that LGUGC essentially launched the municipal bond market in the Philippines.
- LGUGC was strengthened and its credibility enhanced through the rigorous monitoring that accompanied the DCA.
- Interviews with PFIs repeatedly affirmed the importance of LGUGC and its perceived backing by USAID as critical to the decision of PFIs to enter the new areas of LGU and water district financing.
- Interviews with management and staff indicated that experience with the DCA guarantee for bonds/loans to LGUs prepared LGUGC to expand the scope of its guarantees to another sector beyond credit enhancement of LGU financing—the water district market.
- LGUGC's energetic marketing activities interested and encouraged PFIs to enter into water district financing.
- At least half of all of LGUGC'S guaranteed loans, in both number and volume, flowed to the target sectors without a DCA guarantee.
- LGUGC has guaranteed eight bond issues and loans to LGUs without the DCA guarantee with a value of PhP1,728.05 million (US$34,265,094), and three water district loans without DCA guarantee with a value of PhP361.25 million (US$7,855,496). Additionally, at the time of the evaluation, LGUGC had three private water financing transactions in the loan guarantee pipeline outside DCA coverage, and had no fewer than six water financing transactions cancelled or suspended through the interference of the LWUA.
- LGUGC has extended its guarantee beyond the target sectors by guaranteeing one loan to a renewable energy company for a mini-hydroelectric plant, and two loans to bulk water suppliers, with another bulk water supply loan among its proposed guarantees.
- LGUGC currently serves as program manager for three energy sector guarantee programs of other donors/IFIs.

- LGUGC is currently evaluating the feasibility of instituting a credit rating system and a guarantee mechanism for energy cooperatives.

At the **impact** level, any assessment of market demonstration effect within the evaluation framework resulting from a partial re-guarantee of a partial guarantee is tenuous, at least quantitatively. This is particularly true when the financial partner's function is to encourage and facilitate the entry of private financing services to sectors in which borrowers have essentially had no access or exposure to private investment.

The impact of the DCA guarantee as a demonstration model has been modest to date. However, the DCA guarantee was a key factor, in combination with a number of elements, in initiating private lending to the target sectors where there had been little or no prior activity. The true impact may be what was begun—the process of introducing private investment in the target sectors. The process is continuing with the PWRF, which will utilize the LGUGC with a new DCA guarantee, building on what has been done. Indeed, the willingness of PFIs to participate in the PWRF is likely due in part to the DCA agreement. Additionally, the World Bank is planning a program to complement the PWRF. In the long term, the impact of the DCA as a demonstration model could be significant.

Findings supporting these conclusions include:

- Prior to the LGUGC, there was virtually no access to private sector financing in the target sectors.
- One PFI has made a loan to a water district without the LGUGC guarantee, which it would not have made without its experience with LGUGC, and is currently looking at lending to LGUs without a guarantee.
- LGUGC, using both DCA and non-DCA guarantees, channeled approximately PhP 3.5 billion (US$70.6 million) in private financing to the target sectors.
- LGUGC participated in a pilot project, which served as a prelude to the PWRF.
- Based on experience with the DCA guarantee and LGUGC, a new DCA guarantee with LGUGC was approved by USAID for use in the PWRF launched in October 2008.
- Several donor and IFI projects are under development directed toward either urban infrastructure generally or the water sector specifically, including the World Bank's project aimed at assisting less-than-creditworthy water districts to complement the PWRF.

II. BACKGROUND

Local governments in the Philippines were assigned greater responsibility for the provision of basic services under the Local Government Code of 1991 (or the Code)[1], in return they were able to start borrowing from banks or to issue bonds to finance such services and entitled to receive new revenues from the central government through the internal revenue allotment (IRA)[2].

The Code's authority for local governments to borrow was accompanied by a restriction on their borrowing capacity, by providing that the debt taken on by a local government cannot exceed 20% of its regular revenues, which are essentially the amount received through central government transfers. Typically, however, LGUs have been reluctant to exercise the authority granted them to borrow, preferring to finance current operating expenditures and infrastructure improvements with current revenues and budget surpluses. Nevertheless, use of credit by local governments has increased. Borrowings by LGUs as a percentage of their total income net of borrowings grew from 1.9% in 1999 to 3.5% in 2005.[3]

When LGUs have borrowed, they have done so almost exclusively from government financial institutions (GFIs) and other government on-lending institutions, principally the Municipal Development Fund Office. LGUs naturally looked to GFIs—of which there are now two, the Land Bank of the Philippines (LBP or Land Bank) and the Development Bank of the Philippines (DBP or Development Bank)—for loan financing since they are the authorized depository institutions for the LGU IRAs. Additionally, official development assistance (ODA) is channeled through the GFIs and other government on-lending institutions. Accordingly, private capital has traditionally played little or no part in LGU financing.

A 1997 study[4] on the potential market demand for LGU borrowing estimated an effective annual LGU loan market at between PhP4.5 to PhP25 billion (US$170.0 million to US$948.9 million),[5] depending on the policies of the LGUs and the marketing efforts of the banks. This study, and the potentially substantial market for LGU borrowing it forecasted, helped form the rationale for the creation of a private LGU debt guarantee facility to promote private financing of LGUs.

To bridge the gap between potential and actual private LGU financing, the Philippines Department of Finance launched an initiative to develop a municipal bond market. This led ultimately to the

---

[1] Republic Act No. 7160

[2] The internal revenue allotment is a local government's share of 40% of the central government's internal revenues (income and value added tax revenues). The IRA is allocated to local governments according to a formula based primarily on population and land area. Local governments also have local revenue sources, principally property, business and vehicle taxes.

[3] Bureau of Local Government Finance (BILG) (as cited in ADB Report and Recommendation of the President to the Board of Directors. 2007. *Republic of the Philippines: Local Government Financing and Budget Reform Program Cluster (Subprogram 1).*

[4] Saldana, Cesar G. (February 20, 1997). "Study for the Design of a Viable Private LGU Debt Guarantee Institution." The dollar equivalents are calculated using the exchange rate prevailing on the day the study was published (1 US Dollar = 48.11064 Philippine Pesos).

[5] Most US$ values contained in this report are approximations based on available exchange rate information.

formation of the LGUGC with the assistance of the Governance and Local Democracy project (Project Gold)[6] of the United States Agency for International Development (USAID). LGUGC has had deep ties to donors and private financial institutions (PFIs) since its inception in March 1998. This is evidenced by the fact that the Bankers Association of the Philippines (BAP),[7] a non-stock, non-profit trade organization of licensed commercial banks in the Philippines, is the largest equity holder in LGUGC reflecting the interest of its members in risk mitigation measures to permit PFI participation in the LGU market. Initially capitalized at approximately PhP250 million (approximately US$6 million), LGUGC is owned 38% by BAP, 37% by the Development Bank of the Philippines (a GFI), and 25% by the Asian Development Bank (ADB).[8] The original purpose of LGUGC was to make private financial resources available to fund infrastructure projects of creditworthy LGUs primarily through credit guarantees. However, LGUGC later expanded its guarantee facility to cover private financing of infrastructure improvements of water districts (WDs), as well. Three primary factors contributed to the decision to extend LGUGC guarantees to water districts.

The first factor was that, despite some early LGUGC success with municipal bond floats, the growth in private LGU financing failed to materialize as envisioned, owing to a variety of market and other external influences (described in Section VI).

The second factor was the selection of the Philippines as one of the countries to receive assistance in achieving its Millennium Development Goals (MDG) for water supply and sanitation under the Clean Water for People Initiative (a partnership between the U.S. and Japan begun in 2002). The increasing of access to safe water and sanitation, previously declared a national priority by Presidential Decree 198, assumed an even higher profile after this partnership. Presidential Decree 198[9] had authorized the establishment of independent water districts,[10] empowered them to borrow money for authorized public improvements, and created the Local Water Utilities Administration (LWUA) to serve as a specialized lending institution for the development and financing of local water utilities[11] and water districts. It, also, importantly prohibited water districts with outstanding loans from LWUA from borrowing money from other sources without a waiver from LWUA.

---

[6] From 1995 to 2001, Project GOLD assisted local governments to manage revenues and resources, strengthen the Leagues of Cities and Municipalities and improve local government performance measurement.
[7] According to the Executive Director of the BAP, it currently has 36 member banks, including 14 foreign bank branches. Both GFIs (the Land Bank and the Development Bank) are among its members.
[8] LGUGC was incorporated with an initial ownership composed of 51% BPA and 49% DBP. From February 28, 2005, when ADB purchased a 25% interest for US$1.3 million, to present LGUGC has been owned as stated above.
[9] The "Provincial Water Utilities Act of 1973," as amended by PD 768 (promulgated August 15, 1975), and PD 1479 (promulgated June 11, 1978).
[10] WDs are government-owned and controlled corporations, which can be formed by resolution of any city, municipality, province, or combination thereof. Once created WDs are theoretically beyond local political control, and, unlike LGUs receive no IRA.
[11] Local water utilities were defined as any district, city, municipality, province, investor-owned public utility or cooperative corporation that owns or operates a water system serving an urban center, excluding the Metropolitan Waterworks and Sewerage System (serving Metro Manila) and any system operated by the Bureau of Public Works.

The third factor was the issuance of Executive Order (EO) 279 in February 2004. Consistent with the heightened priority of water supply and sanitation, in EO 279 the Philippine government announced sweeping financing reforms for water service providers, including water districts, LGU-run water utilities, and other local water utilities. Given its position as a specialized lending institution, LWUA had become the primary lender (and until recently the only lender) to the water and sanitation sector, although its lending had focused on larger and more creditworthy water districts.

To remedy this situation, EO 279 called for comprehensive reform involving all government agencies involved in the water and sewerage sector with a particular emphasis on the LWUA to rationalize its financing of water service providers. Of particular note, EO 279 established a financing classification system for water service providers with four categories that determined eligibility of water service providers for various sources of financing: (1) creditworthy, (2) semi-creditworthy, (3) pre-creditworthy, and (4) non-creditworthy. LWUA was specifically directed to classify water service providers into one of the four categories beginning with the classification of water districts and to provide financing primarily to the less-than-creditworthy water districts. EO 279 further directed LWUA to develop a monitored graduation plan providing incentives for less-than-creditworthy water districts to transition to creditworthy status.

Creditworthy water districts were to be eligible for financing at commercial rates from GFIs and PFIs, and LWUA was to streamline its waiver procedures for consent to such financing. Semi-creditworthy water districts were eligible to source lending at concessional rates from LWUA, as well as GFIs and PFIs if possible. Pre-creditworthy water districts were eligible for deep concessional financing from LWUA, while non-creditworthy water districts continued to be eligible for LWUA financing with technical and financial support from the Department of the Interior and Local Government and the Municipal Development Fund Office.

EO 279 was the paramount policy guideline on which the U.S. and Japan relied in establishing the Philippine Water Revolving Fund (PWRF). The PWRF, launched in 2008, is an important co-financing scheme for creditworthy water supply and sanitation projects. It combines funds from private banks, partially backed by LGUGC and supported by a new USAID DCA guarantee, with concessionary ODA loan funds from Japan yielding a blended rate to water service providers.

III. DEVELOPMENT PROBLEM AND USAID'S RESPONSE

PROBLEM STATEMENT

Access to basic services dramatically affects the living conditions, health and economic wellbeing of the Philippine people. However, infrastructure in the Philippines to support basic services is lacking, leaving many of the countries' poor without access. Funds required for needed infrastructure improvements and expansion far outstrip current financing sources including external donor resources. Addressing the huge financing constraints is one approach USAID/Philippines has taken to span the breach between those that have access to essential services and those that do not. The funding gap between available funds and the amount needed for the Philippines to meet water and sanitation targets of the Millennium Development Goals (MDG)[12] by 2015 has been estimated to be PhP92.2 billion (US$1.8 billion).[13] The large funding needs were recently confirmed by an ADB study, which estimates approximately US$95 billion will be needed in the period from 2008 to 2025 to satisfy urban infrastructure requirements in the Philippines,[14] including US$5.7 billion for water supply and US$13 billion for sanitation. Any attempt by LGUs and water districts to meet the capital demands for water supply and sanitation requires that financing be mobilized from private, domestic lenders through more efficient credit markets.

USAID'S INTERVENTION IN RESPONSE

Originally, USAID's response to this market imperfection of greater demand than supply of credit was focused on LGUs,[15] and the potential for creating a municipal bond market. The challenge for USAID was to provide LGUs access to private finance to help meet their infrastructure needs and to encourage PFIs to enter the market. According to the Development Credit Authority Action Package,[16] the constraints to private sector financing of needed revenue generating infrastructure improvements included: (i) lack of information availability to commercial financing sources, (ii) lack of market confidence regarding enforcement of LGU repayment obligations, (iii) weak financial capability of most LGUs, and (iv) conservative lending practices of the commercial banking sector.

To address the challenge, USAID sought to accelerate LGUGC's ability to gain the confidence of the Philippines credit market and expand LGUGC's early credit enhancement efforts by application of its Development Credit Authority (DCA). The DCA is a guarantee mechanism, available to USAID Missions since 1999, to mobilize private financing with the goal of unleashing large reserves

---

[12] MDG Target 10 is to halve by 2015 the proportion of people without sustainable access to safe drinking-water (and sanitation).

[13] Murata, Osama. March 19, 2006. Presentation to the Fourth World Water Forum, Mexico City. *Mobilizing Private Funds to the Water Sector.*

[14] ADB Technical Assistance Consultant's Report (financed by the Japan Special Fund), prepared by GHK International Ltd. UKG for the Department of the Interior and Local Government, Philippines. March 2009. *Philippines: Preparing the Philippine Basic Urban Services, pg.20.*

[15] In the Philippines, LGUs consist of 80 provinces, 120 cities, and 1,511 municipalities, not counting the 42,008 barangays (basically neighborhood groups). Source: National Statistical Coordination Board of the Philippines, June 2009.

[16] Action Packages are internal USAID documents, which set out the rationale for and objectives of a Development Credit Authority guarantee.

of dormant local capital in less-developed countries for activities that have a development impact. DCA guarantees are built on the principle of true risk sharing, with USAID guaranteeing only a fraction of the loss to encourage private financial institutions to take more risk while still lending prudently.

USAID signed a 15 year DCA Guarantee Agreement with LGUGC on September 15, 1999 (DCA Guarantee Number 492-99G-001). Under the DCA guarantee, USAID agreed to re-guarantee 30% of the principal and interest LGUGC is obligated to pay in the event of default of a loan qualifying for coverage under the agreement. The primary purpose of the DCA was to increase the number and value of loans guaranteed by LGUGC, which would in turn incentivize PFIs to increase their lending to LGUs for local infrastructure projects. It was expected that, in the long term, the performance of the DCA guarantee would create a demonstration effect that LGUs are creditworthy, leading to a further expansion of LGUGC guarantees and PFI financing (both guaranteed and unguaranteed) for LGU infrastructure projects.

To qualify for coverage under the DCA, the loan had to meet specified criteria, the most important of which are identified in Table 1.[17] The DCA Guarantee Agreement also called for the development of a credit rating procedure and risk assessment system approved by USAID to provide a credible process for assessing and verifying the credit risk associated with LGU infrastructure lending. The initial facility size of US$28,500,000, allowed for US$8,550,000 in USAID's guarantee ceiling, and the maximum loan size was capped at US$5,700,000.

The final date for placing loans under DCA guarantee coverage initially was September 30, 2004, with September 30, 2014 as the final date for submitting claims under the DCA guarantee. While the end date of the DCA guarantee has not changed, the deadline for placing loans under the guarantee has been repeatedly extended by amendment, most recently to September 30, 2008.

There have been eight amendments to the DCA guarantee since its inception. Most relate to extending the date for placing loans under coverage or other relatively minor matters. Two amendments, however, responded to the changing market conditions and led to a faster utilization of the guarantee.

Amendment 3, effective October 1, 2004, modified the DCA Guarantee Agreement by restricting loans eligible for guarantee coverage to water projects, meaning LGU infrastructure facilities and services for the supply, treatment and distribution of potable water, including sewerage and sanitation systems, that otherwise meet the underwriting criteria.[18] Amendment 5, effective January 2006, expanded the borrower cohort to include water districts. Owing to the greater risk of water

---

[17] Additional criteria include: requirements that the project be capable of meeting operating and debt service costs, serve a public purpose, be accessible to low income families, improve availability and quality of infrastructure services, and comply with applicable planning and environmental regulations; certain types of projects that conflict with USAID policy are excluded; and borrowers must successfully undergo a credit rating procedure. The original DCA agreement also mandated the LGUGC increase its percentage of private ownership.

[18] Amendment 3 also eliminated the requirement in the DCA Guarantee Agreement that the percentage of private ownership of LGUGC be increased.

district financing, the guarantee agreement was amended to reduce the maximum portfolio amount to US$24,453,000, and the DCA guarantee ceiling to US$7,335,900. Given the outstanding enrolled principal amount as of January 2006 (US$9,789,000), new principal disbursements placed under the DCA guarantee were limited to US$14,664,000. Table 1 summarizes the original DCA Guarantee Agreement and the changes made by amendments.

TABLE 1. SUMMARY OF LGUGC DCA AGREEMENT AND AMENDMENTS

	ORIGINAL 1999 DCA	DCA AS AMENDED TO 2009
Authority	DCA	Same
Type	Loan Portfolio Guarantee (LPG)	Same
Guaranteed Party	LGUGC	Same
Term of DCA Guarantee	15 years	Same
Start date	September 15, 1999	Same
End date	September 30, 2014	Same
Final date for placing loan under DCA guarantee	September 30, 2004	September 30, 2008
Maximum portfolio amount	US$28,500,000	US$24,453,000
LGUGC maximum loan guarantee %	85% of loan principal, 100% for bonds	Same
USAID re-guarantee %	30% of the principal and interest LGUGC is obligated to pay in the event of default of an LGUGC guaranteed loan	Same
DCA guarantee ceiling	US$8,550,000	US$7,335,900
Maximum principal amount of loans to single borrower	US$5,700,000	Same
Interest rate of guaranteed loan	Consistent with prevailing market rates for similar risk	Same
Maximum loan tenor	10 years	Same
Loan collateral	Project revenues and IRA	Same for LGUs; Assignment of water billings and portion of reserve fund for WDs
Qualified borrower	LGUs	LGUs and WDs
Qualified project	Revenue generating LGU infrastructure projects	Revenue generating water infrastructure projects of LGUs and WDs
Qualified lender	An accredited member bank of the BAP, not owned or controlled by the government; or an individual or a private firm	Same
LGUGC loan guarantee fee	Dependent on credit rating of borrower	Same
DCA origination fee	0.5% of DCA guarantee ceiling	Same
DCA biannual utilization fee	0.5% of the portion of the aggregate outstanding principal and interest of all loans guaranteed by USAID	Same

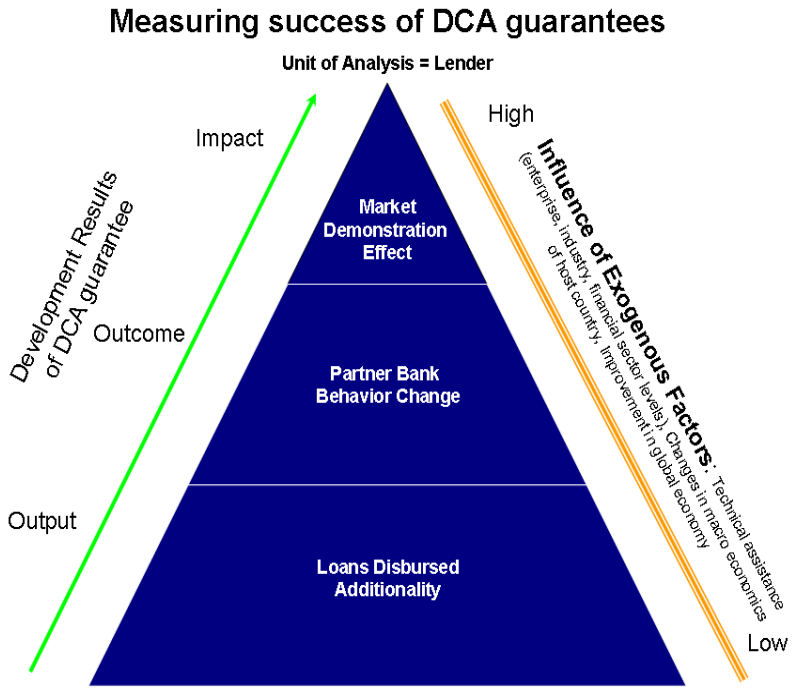
IV. PURPOSE OF THE EVALUATION

USAID's Economic Growth, Agriculture and Trade Bureau's Office of Development Credit (EGAT/DC) is carrying out a series of evaluations of partial credit guarantees made under the auspices of its Development Credit Authority. USAID will use evaluation findings for the following purposes:

- Demonstrate and communicate to DCA stakeholders (OMB, Congress, USAID Missions, etc.) the contributions of DCA loan guarantees to the achievement of development results in the countries in which guarantees are provided.
- Contribute to the dialogue about how to engage financial sector institutions as partners in development.
- Strengthen USAID's application of DCA as a tool for achieving development results.
- Influence the project design of new guarantees.[19]

This report deals only with the 1999 Philippines DCA guarantee. Like the other evaluations, this evaluation was carried out in accordance with an Evaluation Framework developed by SEGURA/IP3 in conjunction with EGAT/DC that measures development results at three levels (Figure 1):

FIGURE 1. DCA EVALUATION PYRAMID



[19] The DCA evaluation will not address borrower issues, such as what happens to borrowers as a consequence of getting loans under guarantees, what they do with the loans, and what development results accrue from their use of the loans. These are seen as issues for the missions to address, depending on the nature and purpose of the guarantees, mission assistance objectives, and other factors. As such, they are outside the scope of the instant evaluation.

Output—Did LGUGC's use of the DCA guarantee conform to guarantee objectives as described in the Guarantee Agreement (*i.e.,* "to strengthen the LGUGC's ability mobilize private capital lending for local government infrastructure services and facilities and for water districts in the Philippines")?

Outcome— Did the DCA guarantee influence behavioral changes at the LGUGC-level, and did LGUGC's experience with the DCA guarantee improve access to credit for entities in the target sectors outside of the DCA guarantee coverage?

Impact— Did the guarantee have a demonstration effect[20] that improved access to credit for entities in the target sectors by increased lending from the private banking sector without use of the guarantee?

The scope of this evaluation extends only to LGUGC and its performance at the output, outcome, and impact levels under the 1999 DCA guarantee. The evaluation does not extend to EGAT/DC's management of the guarantee nor to the impacts of the loans on borrowers or on USAID/Philippine's objectives.

[20] According to the Concept Paper for DCA Evaluation, the demonstration effect "…refers to the longer term goals that occur well after a guarantee has expired. The credit guarantee alone is not responsible for change at this level, but the confluence of factors [associated with the DCA guarantee] can have a lasting effect on the landscape of financial markets and products in a given country or market. …This is the furthest level of impact that relates to the USAID credit guarantee, and as such is the hardest to attribute to the guarantee itself." The demonstration effect typically involves one financial institution showing by use of a guarantee that a market or product is profitable, and other institutions following, creating more robust and competitive market conditions.

V. EVALUATION METHODOLOGY

A two-person team conducted the evaluation in Manila during July 8-17, 2009.[21] Preparation for the evaluation began in June when the evaluation team met in Washington, DC with representatives from the Office of Development Credit to discuss the evaluation objectives, review the evaluation framework, conduct initial interviews with relevant USAID staff, and gather background documents related to the Philippines DCA agreement. Following this initial meeting, the evaluation team worked to tailor the Evaluation Framework to the Philippines context (see Annex C), prepare a desktop analysis, and create a work plan in preparation for the ensuing field trip to the Philippines.

The desktop analysis included a summary of the Philippines DCA agreement and history along with a description of its objectives and possible exogenous factors that could affect the evaluation findings. The Evaluation Framework, evaluation questions, desktop analysis, and work plan were submitted to EGAT/DC by June 26, 2009.

The evaluation methodology consisted of three primary sources of information: (1) in-depth interviews with key informants representing different DCA stakeholders in and around Manila; (2) collection and review of documents pertaining to the DCA; and (3) secondary information on loans and guarantees to LGUs and water districts found in the USAID Credit Management System (CMS), provided by LGUGC, PFIs, and GFIs during interviews or in response to requests for information from the evaluation team, and through additional research. (Annex A presents a complete list of persons interviewed, along with their institutional affiliations.)

DATA LIMITATIONS

The evaluation team dealt with a number of limitations related to the type and quality of data available to conduct the evaluation. These included:

- Incomplete data from PFIs, GFIs and LWUA;
- Lack of a baseline for LGUGC operations;
- Limited number of PFIs and target sector members available for interviews;
- The relatively small number of guaranteed loans to the target sectors.

The inability to establish a counterfactual—what would have happened in the absence of the DCA agreement—makes attributing any findings to the DCA guarantee tenuous. Within the context of the evaluation scope of work, there was no possibility to create a valid counterfactual (which would have required a control group).

---

[21] Randolph Bruton served as Team Leader for the evaluation, and Gary Woller served as Evaluation Specialist. Sashi Selvendran of the Development Credit Office and Joy Jochico of USAID/Philippines participated with the evaluation team in several of the key informant interviews. Melissa Brinkerhoff and Anne-Sophie Samjee of SEGURA/IP3 Partners LLC and Adam Saffer and Nazrawit Medhanie of Management Systems International assisted the team with technical and administrative support throughout the evaluation.

Attributing findings to the DCA agreement is further complicated by the fact that the DCA agreement is a partial *re-guarantee* of the partial loan guarantee granted by the LGUGC. While the PFIs knew which loans were backed by LGUGC, they did not know which of these loans were backed by the DCA. The effect of the DCA guarantee on their behavior is thus both less direct than that of the LGUGC guarantee (and other DCA guarantees) and more difficult to discern. To the extent the DCA has influenced PFI behavior, the effect is likely to be a second-order or even third-order effect. To a large extent this means that to evaluate the impact of the DCA guarantee requires, first, determining the effectiveness of the LGUGC guarantee and, second, determining what incremental impact the DCA guarantee had on the effectiveness of the LGUGC guarantee. There is no straightforward way to attribute results to the DCA agreement in a quantitatively objective manner. Any claims of attribution to the DCA agreement must, therefore, be subjective.

The evaluation team was unable to get complete information on PFI and GFI outstanding loans and pipeline of loans to LGUs and water districts in terms of amounts, interest rates, tenors, and collateral, despite repeated requests for information. As a result, the quantitative data on loans and loan terms outside the DCA and LGUGC guarantees presented in this report is often limited.

Prior to the launch of the DCA agreement in 1999, there was virtually no PFI lending to LGUs or water districts. At the signing of the DCA agreement, only two PFI loans to LGUs were outstanding in the entire country, both bond floats and both backed by the LGUGC. The result is that there was no baseline to which the evaluation team could compare the evolution of LGU and water district loans and loan terms in the presence of the LGUGC and DCA guarantees.

Due to time limitations and scheduling conflicts, the evaluation team was only able to interview three PFIs that have been involved in the financing of LGUs or water districts[22] and three of the LGUs and water districts that have received PFI financing since 1999. The evaluation team could not be certain, therefore, that the experiences and perspectives of the sample PFIs, LGUs, and water districts were generalizable to their respective populations.

Finally, the small number of PFI loans to LGUs and water districts under the LGUGC and DCA made the relative importance of LGU and water district loans to the PFIs overall lending portfolios, as called for in the Evaluation Framework, comparatively insignificant.

---

[22] Four private banks made direct loans guaranteed by LGUGC (Philippines National Bank, Bank of the Philippine Islands, Allied Bank, and Metrobank). With respect to municipal bond issues, the LGUGC can identify the trustees (Philippine National Bank, and the Development Bank) and underwriters (RCBC Capital Corporation, PCI Capital Corporation, Solidbank, Multinational Investment Bancorporation, Investment & Capital Corporation of the Philippines, PNB Capital, Allied Bank, and Unicapital, Inc.), however, it does not have a record of the bondholders.

VI. EXOGENOUS INFLUENCES ON GUARANTEE PERFORMANCE

In the absence of a counterfactual, it is important to consider external influences that can help account for the observed results. This section addresses three external influences that appear to have had significant influence on the observed results: commercial lending rates, political interference of LWUA, and aggressive GFI competition.

COMMERCIAL LENDING RATES

When the DCA agreement was finalized in 1999, the average nominal commercial lending rate was 11.8% and, after some up and down fluctuations, had fallen to 8.8% by 2008 (see Figure 2). This mild volatility in the nominal lending rates, however, masked a more pronounced volatility in the real commercial lending rates, which fluctuated from 5.8% in 1999 to a high of 12.4% in 2001 and lows of -0.9% in 2002 and -0.5% in 2008. (The real lending rate equals the nominal lending rate minus the inflation rate.)

FIGURE 2. SELECTED INTEREST RATES IN THE PHILIPPINES 1999-2008

The volatility in real interest rates was important in at least two ways. First, it made long-term planning riskier. LGU administrators are largely debt averse to begin with, and uncertainty about the movement of interest rates probably only served to reinforce this tendency. On top of that, once interest rates appeared to be falling (as was the case after 2005), LGU administrators may have chosen to hold off borrowing hoping for interest rates to fall further.

The fall in interest rates, moreover, made bond floats comparatively less attractive to LGUs given the additional (real or perceived) costs of the bond float due to the guarantee fee, increased due diligence, collateral, and enhanced monitoring. Thus as interest rates started to fall, LGUs increasingly saw direct GFI loans as the lower-cost option, and (as the evaluation team learned) cost is the most important factor LGUs consider in borrowing decisions.

POLITICAL INTERFERENCE OF LWUA

As discussed earlier, EO 279 decreed that LWUA should realign its lending practices to focus on less-than-creditworthy water districts, while PFIs could lend to creditworthy water districts. LWUA could finance creditworthy water districts when no other sources of funds were available, but it was to give priority to non-creditworthy water districts, as well as to allocate any concessionary loan or grant funds it received from the central government, international financial institutions (IFIs) or other sources to the less-than-creditworthy water districts. Implementation of this policy was relied on by donors and IFIs in the preparation and implementation of projects, including the PWRF of the U.S. and Japan, and a planned World Bank program supportive of the PWRF but geared to concessionary loans to non-creditworthy water districts.

LWUA initially complied with EO 279 and even entered into a Memorandum of Agreement with LGUGC to co-finance water loans. However, with assumption of the LWUA Chairmanship by Mr. Prospero Pichay, Jr. in August 2008, the administration of LWUA abruptly and dramatically changed its approach and role in the water district finance market. Mr. Pichay is a former member of Congress who some suggest is using LWUA as a populist platform to launch a political comeback. The evaluation team was expressly told by LWUA that it considers EO 279 no longer relevant in the current situation where market interest rates have fallen, even though PFIs appear willing to lend to creditworthy water districts (with an LGUGC guarantee). LWUA is now aggressively expanding its water district loan portfolio to creditworthy water districts by offering concessionary terms (e.g., 9.2% over ten years) in combination with grant funding. (The default grant-to-loan ratio is 50/50, although the ratio can vary, with the highest grant ratio going to "waterless" communities.)[23] Additionally, not only is LWUA ignoring the EO 279 mandate to expedite waivers to permit water districts access to private financing, it is denying waivers. It is also using its authority to review water tariffs of water districts with outstanding LWUA loans to discourage increases in water tariffs necessary to allow them to service private debt obligations.

According to LWUA, it has applications for water infrastructure projects in the pipeline amounting to approximately PhP3 billion (US$63.7 million). To finance its lending expansion, LWUA is slated to receive PhP10 billion (US$212.5 million) from the national government on top of which it is seeking an additional PhP10 billion. LWUA also recently purchased a 60% stake in a thrift bank located in Laguna with three branch offices (and plans an expansion of branches) to serve as a Water Development Bank. LWUA intends to require water districts with outstanding loans, which it

[23] "Waterless" communities are defined as those where less than 50% of the total households have access to piped water.

estimates to be well over 90% of water districts, to deposit their funds in the Water Development Bank, although some water districts question the legality of LWUA's subsidiary bank serving as a depository.

As a result of its activities, LWUA has managed to crowd private lenders completely out of the market for water district financing. Key informants (aside from LWUA) were unanimous in citing LWUA's recent policies as the single biggest impediment to private water district financing.

AGGRESSIVE COMPETITION FROM GFIs

The demand for private financing has declined significantly for LGUs since the original design of the DCA, which relied on initial estimates of an annual LGU loan market of US$170.0 million to US$948.9 million. Reasons for this include:

- aggressive competition from GFIs together with a weak appetite for private infrastructure financing arising from the paucity of creditworthy LGU projects;
- the high perceived costs of private bond floats/loans; and
- the incompatibility of relatively short PFI tenors with the long term needs of large infrastructure projects.

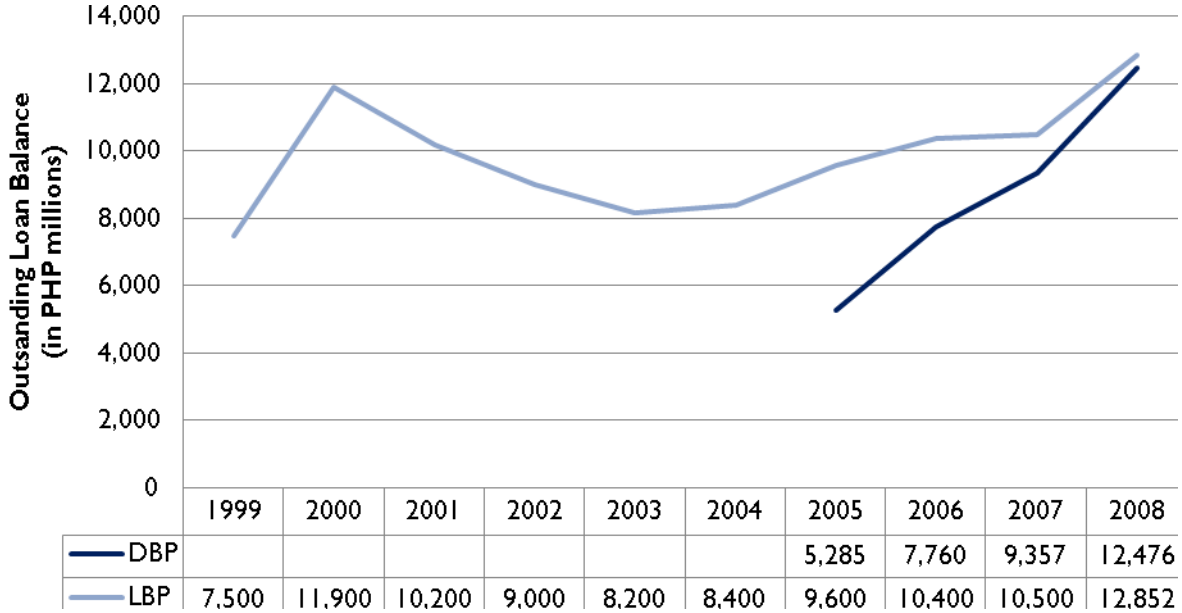
Philippine law allows GFIs to hold a number of competitive advantages over PFIs in the LGU lending market. Even though it is unclear whether such an approach is sustainable over the long-term, the central government has not curtailed GFI domination in the financing of creditworthy LGU infrastructure projects. To begin with, Philippine regulation and policies stipulate that, with limited exceptions, LGUs must hold their depository accounts at GFIs. This means that virtually all LGUs have long-standing, pre-existing relationships with the GFIs. Further, GFIs typically can simply debit LGU IRA deposits with the GFI in the event of loan default, thereby diminishing reliance on project generated revenues and eliminating the need for collateral. Finally, GFIs often benefit from highly concessionary ODA financing, which in turn allows them in certain circumstances to offer concessionary financing to LGUs.[24] In contrast, PFIs have few existing relationships with LGUs, require permission from the Department of Finance to accept deposits from LGUs, may not easily intercept IRAs, and do not receive concessionary ODA financing.

Figure 3 depicts the outstanding balances of loans by GFIs to LGUs based on data provided by LBP and the Development Bank of the Philippines.[25] As can be seen, LGU loan balances of LBP (the largest lender to LGUs) declined from 2000 to 2003. Beginning in 2004, the LGU loan balances of both GFIs have risen steadily through 2008, reaching their highest level in over a decade. This

[24] The evaluation team found evidence, however, to suggest that GFIs frequently fail to pass on their concessionary financing terms to LGUs.
[25] Data was unavailable from DBP for LGU loan balances for the period prior to 2005.

increase in the outstanding balances of LGU loans of the GFIs coincides with the increased competition experienced by LGUGC.

FIGURE 3. OUTSTANDING BALANCE OF LOANS BY GFIS TO LGUS



The GFIs have exploited their inherent competitive advantages to compete aggressively for LGU loans, managing to crowd private financing out of the LGU loan market.[26] The evaluation team heard numerous accounts from LGUGC and other key informants describing cases in which GFIs had poached LGU loans from the PFIs. Indeed, the first 10 bond floats backed by the LGUGC (including three guaranteed by the DCA) were redeemed early by the LGUs having in each case been refinanced by a GFI.

The competitive advantages enjoyed by the GFIs have made them the low-cost alternative for LGU financing, particularly in the current era of low interest rates. Each of the LGUs and water districts interviewed by the evaluation team identified cost as the most important factor in deciding where to borrow. In each case, moreover, private financing was seen as more expensive than GFI financing due to higher underwriting and monitoring costs, additional due diligence and documentation, and the guarantee fee. The Commission on Audit evaluated the City of Pasay bond float and concluded that the bond float cost the city approximately US$850,000 (PhP50 million) more than if had

[26] On June 9, 2009, President Arroyo, by EO 809, directed implementation of the LGU financing framework previously adopted in 2007 by the Department of Finance to rationalize and segment LGU financing with the ultimate goal of graduating LGUs to private investment. The EO further allowed the most creditworthy LGUs to directly contract loans with "multilateral financial institutions created by multilateral treaties or agreements to which the Philippines is a signatory," without national government guarantee. Whether EO 809 will be enforced and the effect of direct multilateral investment on private financing of LGUs remains to be seen.

borrowed from a GFI. The City Administrator estimated an 80% likelihood that next time the city would borrow from a GFI.

A significant component of the weak demand for LGU financing is the dearth of infrastructure projects being undertaken by LGUs stemming in turn from the LGUs' tradition of fiscal conservatism. The political structure of LGUs is not conducive to undertaking large infrastructure development projects. Mayors serve three-year terms, and the short election cycle creates disincentives to invest in expensive and long-term infrastructure projects. Investing in large infrastructure projects also requires the approval of both the Mayor and Vice Mayor, who are frequently political opponents and thus disinclined to agree on large investments of this nature. In addition to the political obstacles to project development, LGU personnel frequently lack capacity and experience in properly designing, prioritizing and packaging economically viable projects.

Moreover, loans from private financial sources (which rely on their deposit base) and the lack of a secondary bond market (investors tend to hold the bonds to maturity) result in relatively short tenors that do not match the long-term tenors needed for infrastructure projects with extended lives. The short maturities of loans from private investment require a recovery of principal in a brief period, which radically escalates LGU debt service.

As a group, LGUs are highly liquid having large budget surpluses in the aggregate averaging nearly US$491.5 million from 2002-2007, the last year when data was available (Table 2).[27] During the same period, LGUs average US$76.4 million per year in borrowing from all sources with a debt service totaling on average only 4.0% of IRA revenues. LGUs clearly have substantial opportunity to increase their borrowing and debt service, but they are not taking advantage of the opportunity. This fact has alarming implications for the delivery of key services. The unwillingness to borrow translates into loss of the benefits that could be gained through investment in public infrastructure, including increased local revenues, income generation, job creation, improved access to clean water and sanitation, and the reduction of poverty.

TABLE 2. MEASURES OF LGU LIQUIDITY

	2002	2003	2004	2005	2006	2007
Budget Surplus (US$ millions)	$355.2	$375.3	$320.7	$510.7	$671.0	$716.3
Loans and Borrowings (US$ millions)	$26.6	$59.1	$59.6	$62.5	$126.1	$124.5
Debt Service / IRA	3.1%	3.9%	3.8%	4.5%	4.4%	4.3%

[27] BLGF, (June 2008), Moving Towards a Positive and Sustainable LGU Financial Performance: Statement of Income and Expenditures CY 2005-2007.

VII. FINDINGS AND CONCLUSIONS

This section presents the evaluation findings and conclusions. Findings at the output, outcome, and impact levels are presented in separate sub-sections. Each sub-section begins with a summary of the evaluation questions followed in order by the conclusions and the findings supporting the conclusions.

OUTPUT FINDINGS AND CONCLUSIONS

At the output level, the evaluation examined whether LGUGC used the DCA guarantee to improve access to credit for LGUs and water districts. The Evaluation Framework specified four questions at the output level.

Question 1: How did the DCA guarantee fit into LGUGC's ongoing strategy? What market potential did the DCA guarantee help open for LGUGC?

Question 2: How did LGUGC implement the DCA loan guarantee program, and did implementation of its loan guarantee program change over the course of the DCA guarantee? Why?

Question 3: Did LGUGC's use of the DCA guarantee improve access to credit for the target sectors? If so, how much local private capital was mobilized?

Question 4: To what extent, if any, did the DCA guarantee influence changes in characteristics of LGUGC's guarantee portfolio?

Findings And Conclusions For Question 1

Question 1: How did the DCA guarantee fit into LGUGC's ongoing strategy? What market potential did the DCA guarantee help open for LGUGC?

Conclusion: The purpose of the DCA guarantee—to mobilize private capital lending for water infrastructure services and facilities of local governments and water districts in the Philippines—complemented the LGUGC mission of providing credit enhancement for private financing of local public infrastructure projects. Therefore, the DCA guarantee fit well with LGUGC's ongoing strategy. The DCA guarantee played a critical role in helping LGUGC achieve credibility among PFIs and other stakeholders.

Findings: The evaluation team found the DCA helped boost the confidence of PFIs in lending to LGUs and water districts through LGUGC. As a result, the DCA was a significant factor in building the credibility of LGUGC as a viable guarantor. It was the formal commitment by USAID that gave the assurance of oversight and U.S. government endorsement of LGUGC (rather than the monetary amount) which established the credibility of LGUGC to PFIs and other sector participants (what one informant called "intangible goodwill.") The DCA guarantee was, according to one informant "a strong statement to the banks that thorough due diligence had been done, and it gives the assurance of quality." Prior to the creation of LGUGC, there was no private bond/loan

market for LGUs, nor was there a market for private water district financing. LGUGC was instrumental in creating both. LGUGC through its guarantee provided a measure of comfort and safety to the commercial banks that appears to have been pivotal in overcoming their traditional hesitancy to lend to LGUs and water districts, and permitted it to forge loan transactions with little precedence in the Philippines up to that point in time.

Findings And Conclusions For Question 2

Question 2: How did LGUGC implement the DCA loan guarantee program, and did implementation of its loan guarantee program change over the course of the DCA guarantee? Why?

Conclusion: Overall, LGUGC has implemented the DCA guarantee professionally, competently, and in a manner consistent with the terms of the DCA agreement. LGUGC staff members demonstrated a high level of knowledge on all issues related to the DCA agreement. Supporting information systems are well-developed, accessible, and relevant to ongoing program operations. The high quality of guarantee implementation is in significant part attributable to the technical assistance (TA) and monitoring that accompanied the DCA guarantee. Given that municipal bonds were a somewhat novel method of financing public projects, the utilization of the DCA guarantee for LGU financing was rather slow, and became slower as the bond market crumbled and GFI competition for loans to local governments grew. Accordingly, LGUGC shifted its focus from LGU financing to water district financing in 2006 in response to such external forces and to take advantage of market opportunities, and DCA utilization quickly increased.

Findings: The professionalism demonstrated by LGUGC in its operations and its initiative in promoting private financing of water district infrastructure projects have earned it the respect of the financial community, and it has assumed a high profile in the financing of water supply. This conclusion is not only borne out in interviews with key informants but also by the number of collaborative products (e.g., guarantees, loan instruments, documents, memoranda of understanding, information systems, databases, credit rating systems) produced with the assistance of USAID over the course of the DCA agreement. Its cooperation with and standing among other stakeholders is evidenced as well by LGUGC's participation in the Philippines Development Forum Sub-Working Group on Water Supply and Sanitation, and its Task Force on Financing and Infrastructure Investment. The Philippines Development Forum, formed in 2004, has grown into an important instrument of the Philippine government for facilitation of policy dialogue, the advancement of development plans and the coordination of the activities of all stakeholders.

LGUGC has carried out extensive efforts to market its guarantee program and the DCA guarantee. Specific marketing activities pursued by LGUGC are highlighted in Box 1. Since the issuance of municipal bonds was a relatively new method of financing of local government infrastructure in the Philippines and neither borrowers nor lenders were experienced in the process, the utilization of the DCA guarantee was somewhat slow. Local government political and capacity limitations rendered strong revenue producing projects scarce and prized as investments. In 2004-2005 when competition through direct loans from GFIs began to increase, such projects were tempting targets

and the municipal bond market withered. To date LGUGC's marketing efforts for the most part have been unable to overcome the various factors working against private LGU financing.

However, once it had become apparent that the market for private LGU financing was drying up, LGUGC moved first deliberately and then aggressively into water financing. A USAID commissioned report issued in September 2004 provided the market rationale for LGUGC to facilitate PFI lending to water districts,[28] while EO 279 provided the market opportunity. With USAID encouragement, LGUGC's transition into water district financing was formalized in Amendment 5 to the DCA agreement.

After amendment of the DCA agreement to include water districts, the associated marketing efforts to promote private financing of water projects appeared to be bearing fruit. Private banks began to recognize the potential in water district lending and DCA guarantee utilization rapidly accelerated (ultimately reaching 86.3%) until the distortion in the market caused by LWUA.

Box 1: Marketing Activities Undertaken by the LGUGC

Marketing to financial advisors: Prior to 2006, the LGUGC focused much of its marketing efforts on the financial advisors. Financial advisors work closely with LGU officials on financial planning and management. They play a key role in convincing LGUs to consider private financing.

Marketing to LGUs and WDs: The LGUGC maintains an extensive data base of 506 LGUs, which it ranks by creditworthiness into groups A, B, C, and D. Every year the LGUGC initiates contact with each LGU in groups A-C, in addition to LGUs and water districts identified in a demand analysis carried out by DAI and JICA, via phone or mail. Where possible it makes follow-up marketing visits to LGUs and water districts throughout the country. To date, it has talked to all LGUs and water districts identified in the DAI/JICA demand analysis.

Marketing to water associations: The LGUGC markets directly to water district associations in each province. It presents to association members at various plenary sessions of the associations' general assembly held monthly in each province.

Marketing to PFIs: The LGUGC provides briefings to PFIs on issues related to LGU and water district financing. The LGUGC's marketing efforts to the PFIs is supplemented by extensive PFI outreach and instructional activities carried out by USAID's FORWARD Project, including seminars for PFIs on how to evaluate water districts and water projects. Marketing efforts to PFIs reflect the lesson learned during the early years of the DCA agreement that it is critical to build both demand and supply for private financing.

Findings And Conclusions For Question 3

Question 3: Did the LGUGC's use of the DCA guarantee improve access to credit for the target sectors? If so, how much local private capital was mobilized?

Conclusion: The DCA guarantee was used by LGUGC to improve credit access in the target sectors. Starting essentially from scratch, the LGUGC and DCA guarantees were instrumental in mobilizing 22 LGU bond floats and water district loans of which 11 totaling approximately US$28.5 million[29] were covered by the DCA guarantee.

---

[28] Florento, Hector. September 2004. "Analysis of Constraints to Mobilizing Sector Financing for Water Supply and Sanitation Projects in the Philippines." Development Alternatives, Inc.

[29] The mobilization of funds under the DCA guarantee is higher than the DCA maximum portfolio amount previously stated because until 2002 the facility was treated as revolving, permitting reuse of funds after repayments.

Findings: Given the absence of private LGU and water district financing prior to the creation of the LGUGC, any increase in private LGU and water district financing under the DCA agreement can be reasonably attributed to the LGUGC and to a significant extent (based on the evidence presented above) the DCA guarantee. From September 15, 1999 to June 30, 2009, the LGUGC helped mobilize private sector financing to 11 LGUs and water districts under DCA guaranteed loans totaling US$28,521,273.

The 11 DCA guaranteed loans included six bond floats totaling US$17,207,074 and five water district term loans totaling $US11,314,199 (see Tables 3 and 4). Three of the six bond floats were fully redeemed in 2005.

Table 3 summarizes each of the 11 DCA guaranteed loans while Table 4 summarizes the number and value of DCA guaranteed loans made over the course of the DCA agreement.

TABLE 3. SUMMARY OF DCA GUARANTEED LOANS

BORROWER	YEAR	TYPE	PURPOSE OF LOAN	LOAN AMOUNT (PHP MILLION)	LOAN AMOUNT (US$)	LOAN TENOR (YEARS)	INTEREST RATE[30]
City of Puerto Princesa	2000	Bonds	Low cost housing	256.27	$5,700,000	7	182-day T-bill +2.5%
Municipality of Daraga	2002	Bonds	Public market	75.00	$1,486,974	7	182-day T-bill +3.0%
Municipality of Bayambang	2002	Bonds	Public market	42.00	$810,435	7	13.1692%
Municipality of Carmona	2004	Bonds	Housing	150.00	$2,665,814	7	6-month MART1 +3.0%
City of Pasay	2004	Bonds	Public market and commercial center	317.32	$5,700,000	7	6-month MART1 +3.25%
Municipality of Imus	2004	Bonds	Slaughterhouse	47.00	$843,852	7	6-month MART1 +3.25%
Metro Iloilo WD	2006	Term Loan	Rehabilitation, improvement and expansion of water system and refinancing of LWUA loan	39.29	$770,370	7	3-month MART1 +3.0%
Silang WD	2007	Term Loan	Repair and expansion of water system	160.65	$3,565,009	10	10.5%
LagunaWD	2008	Term Loan	Expansion of water system and financing of LWUA loan	85.00	$2,072,210	10	3-month PPDST-F +3.0%
City of San Fernando WD	2008	Term Loan	Rehabilitation and expansion of water system	192.10	$4,605,831	10	3-month PPDST-F +2.5%
Indang WD	2008	Term Loan	Expansion of water system	12.75	$300,778	10	3-month PPDST-F +2.5%
TOTAL				1,377.38	$28,521,273		

[30] The 182-day T-bill rate represents the average bids for the 182-day government treasury bills. (www.bsp.gov.ph/). The 3-month and 6-month MART1 rates represent the average bids for government securities submitted by fixing banks. They represent the average rates for money in the Philippines. (www.mart.com.ph/). The 3-month PDST-F rate replaced the MART1 rates under the new infrastructure for trading securities (www.pdex.com.ph/).

TABLE 4. DCA GUARANTEED LOANS

	2000	2001	2002	2003	2004	2005	2006	2007	2008
Number of LGU Loans	1	0	2	0	3	0	0	0	0
Number of water district Loans	0	0	0	0	0	0	1	1	3
Value of LGU Loans (PhP millions)	256.28	0	117.00	0	514.32	0	0	0	0
Value of LGU Loans (US$ thousands)	$5,700	0	$2,297	0	$9,210	0	0	0	0
Value of water district Loans (PhP millions)	0	0	0	0	0	0	39.29	160.65	289.85
Value of WD Loans (US$ thousands)	0	0	0	0	0	0	$770	$3,565	$6,979

The loan guarantees extended by LGUGC and backed by the U.S. government under the DCA agreement were instrumental in mobilizing private financing for LGUs and water districts. LGUGC's ability to mobilize such financing was supported by its marketing and education efforts, its cooperative working relationship with PFIs and other stakeholders, and its sound operations abetted by direct technical assistance and the monitoring and evaluation activities of USAID. Absent the LGUGC guarantee, it is unlikely that PFIs would have entered the LGU or water district lending markets, and absent the DCA guarantee, it is unlikely that the amount of financing mobilized would have reached the levels it did.

Findings And Conclusions For Question 4

Question 4: To what extent, if any, did the DCA guarantee influence changes in characteristics of LGUGC's guarantee portfolio?

Conclusion: The DCA guarantee increased the leverage of LGUGC thereby providing it the opportunity to enlarge its loan portfolio. There is some evidence that the DCA guarantee did lead over time to improved tenors for all water district guaranteed loans. There was also anecdotal evidence that interest rates under guaranteed loans may have been lower than PFIs would have applied to other loans with a similar high risk profile in the absence of any guarantee, but the assertion could not be verified. Otherwise, there was little notable influence of the DCA guarantee on the characteristics of loans in LGUGC's guarantee portfolio. The interest rate and collateral of LGUGC guaranteed loans showed no market improvement over the course of the DCA agreement. LGUGC guaranteed loans made outside the DCA guarantee were, for the most part, similar to those carrying the DCA guarantee.

Findings: The DCA guarantee reduced LGUGC's risk exposure in the event of default. This in turn reduced the cost of estimated loan defaults freeing capital and permitting LGUGC the opportunity to increase the number and/or value of the loans guaranteed, however, by precisely how much cannot be determined on the basis of available information. From the perspective of

USAID, it obligated approximately US$1 million to the DCA, exclusive of technical assistance, resulting in US$28.5 million in guaranteed loans for a rough leverage ratio of over 28 to 1.

There is no significant difference in the average tenor for LGU loans guaranteed by LGUGC that were covered by the DCA guarantee and those that were not. The average loan tenor for DCA guaranteed loans to water districts was only moderately higher than other LGUGC guaranteed loans to water districts. Table 5 shows the average loan tenor for those LGUGC guaranteed loans to LGUs and water districts without DCA guarantee coverage and those with DCA guarantee coverage.

TABLE 5. AVERAGE LOAN TENOR OF LGUGC GUARANTEED LOANS TO LGUS AND WATER DISTRICTS WITHOUT DCA COVERAGE VS. DCA GUARANTEED LOANS

BORROWER	NUMBER OF LOANS – NON-DCA	NUMBER OF LOANS – DCA	AVERAGE TENOR – NON-DCA	AVERAGE TENOR – DCA
LGU	8	6	6.6	7.0
Water District	3	5	8.3	9.4
Total	11	11	7.4	8.1

The data does suggest that the tenors for guaranteed water district loans overall did improve. Of the eight total water district loan guarantees, the last six carried 10 year tenors. The first DCA guaranteed water district loan was for the same 7 year tenor as the DCA guaranteed loans to LGUs, and the first guaranteed loan without DCA coverage had a 5 year tenor. The next four water district guaranteed loans were all under DCA guarantee coverage and each carried the maximum 10 year term. Finally the last two water district guaranteed loans, which were not DCA guaranteed, also were for 10 years. While the tenor of the loans could be a function of the nature of the projects, the type of loan instrument, or competitive influences, the pattern and trend still suggests that PFI experience with the guaranteed loans to LGUs and the first water districts was likely a contributing factor in the swift expansion of PFI water district loan tenors to ten years.

Interest rate spreads remained more or less constant for DCA guaranteed loans, ranging from 2.5%-3.25% over the base rate on loans to both LGUs and water districts. Spreads among non-DCA guaranteed loans exhibited a larger range from a low of 1.5% to a high of 3.75%. This data alone does not indicate a difference in interest rates for LGUGC guaranteed loans. There is some anecdotal evidence that the spreads and, therefore, the interest rates charged were lower than they would have been in the absence of the LGUGC and DCA guarantees. The Philippine National Bank (PNB), for example, indicated that it normally charges a 5%-6% spread over base rate on loans with risk characteristics similar to water district loans, which is 1.7-2 times higher than the 3.0% spread it charged to the Metro Iloilo Water District. However, this information could not be confirmed.

A review of the collateral used to secure all LGUGC guaranteed loans to LGUs and water districts (including those that were covered by the DCA guarantee and those that were not) reveals no meaningful trends. For the most part the collateral was similar within the respective sectors and

there is no evidence that the DCA guarantee led to improved collateral terms. The collateral for LGUGC guaranteed loans with and without DCA guarantee coverage is set forth in Annex B.

OUTCOME FINDINGS AND CONCLUSIONS

The evaluation analyzed whether LGUGC's experience with the DCA guarantee improved access to private credit within the target sectors but outside of the coverage of the DCA guarantee, and other LGUGC behavioral changes.

The outcome evaluation questions were as follows:

Question 5: To what degree have desired outcomes contemplated in Action Package, Legal Agreement, and other relevant documents with respect to guaranteed loans outside the protection of the DCA guarantee been achieved so far?

Question 6: What factors at the LGUGC level can be associated with achievement of desired outcomes (*e.g.,* TA; LGUGC staff training; revised LGUGC strategy, procedures and structure; new management, etc.)?

Question 7: Has LGUGC made loan guarantees to the target sectors outside of DCA coverage? If so, how have such LGUGC guaranteed loans to the target sectors performed relative to DCA guaranteed loans to the target sectors?

Question 8: Has LGUGC moved into any new sectors and types of borrowers outside the DCA guarantee? If so, has the DCA guarantee, as a demonstration model, played any role in LGUGC's decisions? How have LGUGC's guaranteed loans in all sectors outside of the DCA guarantee performed relative to its DCA guaranteed loans in the target sectors?

Findings And Conclusions For Question 5

Question 5: To what degree have desired outcomes contemplated in Action Package, Legal Agreement, and other relevant documents with respect to guaranteed loans outside the protection of the DCA guarantee been achieved so far?

Conclusion: The desired outcomes anticipated under the relevant documents, including encouragement of private capital flows to creditworthy local infrastructure projects, acceleration of LGUGC's ability to gain the confidence of the local credit markets, and expansion of the scope of its efforts, have been satisfactorily achieved. LGUGC has successfully gained the confidence and respect of the private finance community, expanded its efforts, and guaranteed loans to the target sector outside of DCA coverage amounting to PhP2,089.30 million (US$42,120,590). When LGUGC's entire portfolio of loan guarantees to the target sectors is considered, approximately PhP3.5 billion (or $70.6 million) in private financing for the target sectors has been mobilized. External influences, however, curtailed the total scale of lending achieved. Although the scale of mobilization is relatively modest, the important point is the introduction of private financing to the sectors.

Findings: LGUGC, by capitalizing on the credibility conferred on it by the DCA, has guaranteed loans to the target sectors totaling PhP3.5 billion (or $70.6 million), essentially opening the door for private financing of LGUs and water districts. Of that total, PhP2,089.30 million (US$42,120,590) is attributable to guarantees outside of DCA coverage (see the Findings for Question 7). According to the DCA Guarantee Agreement as ultimately amended, the purpose of the guarantee is as follows: *"The USAID guarantee, together with such technical assistance and training as the Parties may mutually agree upon, is intended to strengthen LGUGC's ability to mobilize private capital lending for local government infrastructure services and facilities and for Water Districts in the Philippines."* The Action Packages indicate the DCA guarantee was designed to enhance the confidence of the local credit markets in LGUGC and allow it to expand the reach of its endeavors.[31] When the Guarantee Agreement was amended in January 2006 to include water districts, the Action Package considered it an expansion of an innovative mechanism that would enable introduction of private sector financing to a sector previously unserved.

As previously mentioned, before the establishment of LGUGC in 1998, very few private banks lent to LGUs or had much experience with municipal finance. Prior to the DCA Guarantee Agreement, LGUGC had guaranteed two small bond floats. After the DCA agreement, LGUGC guaranteed six LGU bond issues under the DCA guarantee, and six additional LGU bond issues and two LGU term loans that were not covered by the DCA guarantee. According to a study by the Asian Development Bank,[32] as of March 2008, 84.7% of the aggregate outstanding debt of LGUs was held by the two GFIs (Land Bank and Development Bank), and the Municipal Development Fund Office.[33] PNB and the Philippines Veterans Bank, the two private banks authorized to hold LGU IRA deposits, were responsible for 13.8% of loans to LGUs.[34] Other private banks holding bonds from LGUs guaranteed by LGUGC were 1.4% of the overall outstanding LGU debt market. This is vivid illustration of the existing duopoly in LGU lending, and the importance of the depository relationship in the competition for LGU loans. While LGUGC's share of the overall LGU debt market was always small, the important fact is the act of entry—that non-depository private banks are represented in the market at all. LGUGC encouraged and facilitated lending to LGUs by private banking sources, and those non-LGU depository banks interviewed indicated that they would not have entered the market without the LGUGC guarantee.

Likewise, water district financing was virgin territory for PFIs. Virtually all financing for water districts was by the LWUA. Private banks had no experience in lending to water districts, were

---

[31] The original Action Package cited the DCA agreement as supporting the then effective Strategic Objective (SO) 2, "*Improved National Systems for Trade and Investment*" and most relevantly Intermediate Result (IR) 1, "*Fiscal Resource Mobilization and Allocation Improved,*" and IR 3, "*Financial Markets Improved.*" The Action Package for the amendment adding WDs to the borrower cohort described the amendment as supporting the then current Mission SO 2, "*Performance of Selected Government Institutions Improved,*" and specifically IR 3, "*Innovations in Trade and Investment Programs Promoted.*"

[32] ADB Sector Study Report. October 2008. Philippines: Sources of Local Government Unit Financing.

[33] The Municipal Development Fund Office, a part of the Philippines Department of Finance, manages the Municipal Development Fund through which it channels ODA primarily to lower income LGUs.

[34] PNB is a former GFI that completed privatization in 2007, and the Philippines Veterans Bank is a private bank whose directors are appointed by the President. Although private banks, PNB was granted the ability to retain LGU deposits by special authority of the Monetary Board, and the Philippines Veterans Bank may accept LGU deposits by law.

concerned about the ability of water districts to repay loans and the value of their collateral (since there was no IRA to intercept), and were uncertain how to evaluate the credit risk. LGUGC vigorously marketed financing of water district projects, providing instruction to both water districts and PFIs. USAID supported LGUGC by partnering with ODA from Japan, which led to the first private investment in a water district, Metro Iloilo WD. Thereafter, LGUGC guaranteed four more water district loans covered by the DCA guarantee, and an additional three water district loans without DCA coverage. An additional two LGUGC guaranteed loans involve water district participation but are to bulk water suppliers and therefore beyond the target sectors. All GFIs and PFIs interviewed acknowledged that LGUGC, with the imprimatur of USAID support, initiated private financing of water districts.

Findings And Conclusions For Question 6

Question 6: What factors at the LGUGC level can be associated with achievement of desired outcomes (*e.g.,* TA; LGUGC staff training; revised LGUGC strategy, procedures and structure; new management, etc.)?

Conclusion: The relationship started with USAID by the DCA allowed LGUGC to benefit from multiple other forms of assistance, which led to the development of expertise, procedures and management. As a result, much of the achievement of desired outcomes can be attributed indirectly to the DCA through technical assistance; monitoring and evaluation by the USAID/Philippines and EGAT/DC; and the strategy revisions adopted by LGUGC.

Findings: Technical assistance has been essential to LGUGC's growth and operations. Required by the USAID guarantee agreement to meet certain conditions, the direct technical assistance was critical in the development of (i) LGUGC's credit screening process; (ii) an LGU database containing data on 506 LGUs, which is employed in the LGU credit screening process; (iii) the credit rating system for LGUs; (iv) guarantee fee pricing; and (v) a water district credit rating system. To date 40 LGUs and 11 water districts have received a credit rating. As a result of the screening and rating systems established, LGUGC has been described as the "leading repository of expertise in rating LGU creditworthiness in the Philippines."[35]

In addition to direct technical assistance, LGUGC benefitted from a close and collaborative relationship with USAID/Philippines through monitoring of the DCA. Mission staff and EGAT/DC personnel worked closely with LGUGC on issues such as internal controls; organizational structure; procurement; review and assessment of financial statements; review of provisioning requirements; financial risk management and reporting; computing interest caps; re-pricing methodology disclosure; and ensuring the accuracy of outstanding loans, internal payment projections, and foreign exchange rates. Further, it allowed exposure of potential problems at an early stage. This technical support was vital in strengthening LGUGC's policies and procedures in managing guarantees.

---

[35] Special Assistance for Project Formation (SAPROF) for the Philippine Water Revolving Fund in the Republic of the Philippines, SAPROF Team for JBIC (December 2006).

LGUGC also revised its strategy over time in response to changed circumstances and lessons learned. When competition from GFIs for LGU financing increased and utilization under the DCA slowed, LGUGC and USAID turned their attention to water/sanitation finance. The partnership between the U.S. and Japan to assist selected countries achieve their MDG targets for water supply and sanitation had led to an on-going collaboration involving consultation at the highest levels of the respective governments, strengthening their cooperation and enhancing the coordination of development aid. In the Philippines, one of the countries chosen for such assistance, the existence of LGUGC constituted a ready-made vehicle for USAID contribution (via the DCA) to the joint effort of the countries to bring private capital into the water and sanitation sector.

In 2004 USAID, the Japan Bank for International Cooperation (JBIC) and the Development Bank signed two Memoranda of Understanding on water and sanitation. The first Memorandum was for the implementation of a Municipal Water Loan Financing Initiative, a pilot program to encourage private sector investment in water infrastructure through LGUGC and the DCA guarantee in combination with an ODA loan from Japan. This Initiative ultimately led to an LGUGC guaranteed loan to the Metro Iloilo WD. The second Memorandum was for a feasibility study to create the Philippine Water Revolving Fund. The following year a third Memorandum was signed by USAID, Japan International Cooperation Agency (JICA),[36] the Department of Finance, the National Economic Development Authority, and the Bankers Association to form a steering committee to produce a design and implementation framework for the PWRF. The work of the U.S./Japan partnership was well timed with respect to both DCA guarantee utilization and the advancement of Philippine government policies embodied in EO 279 to promote increased private financing for creditworthy water service providers. In light of the increased priority of water sector finance in the policies of all three governments, LGUGC with the support of USAID/Philippines, requested the DCA Guarantee Agreement be expanded to include revenue generating water infrastructure projects of water districts, and the agreement was so amended effective January 2006.

Other LGUGC strategic adjustments in the last few years have included exploration of ways to increase LGUGC's share of the LGU debt market through the Bankers Association of the Philippines member banks' network, expansion of its Relationship Management Department, restructuring for more aggressive marketing, and review and reassessment of policies in response to the guarantee of water sector loans. It is also currently assessing the viability of establishing a credit rating system and a guarantee mechanism for energy cooperatives.

---

[36] Until October 1, 2008, JICA primarily focused on technical assistance to developing countries. Effective October 1, 2008, the overseas economic operations (the concessional loan activities) of JBIC, and part of the grant operations of Japan's Ministry of Foreign Affairs, were merged into JICA, bringing all three components of ODA, (*i.e.*, TA, grants, and concessional loans) within the purview of JICA.

Findings And Conclusions For Question 7

Question 7: Has LGUGC made loan guarantees to the target sectors outside of DCA coverage? If so, how have such LGUGC guaranteed loans to the target sectors performed relative to DCA guaranteed loans to the target sectors?

Conclusion: LGUGC has guaranteed loans to the target sectors without DCA coverage. Of the 22 target sector loans guaranteed by LGUGC, at least half by both number (11) and value (US$42,120,590) are non-DCA guaranteed loans. There have been no defaults on LGUGC loan guarantees to the target sectors made outside of DCA coverage, and they have performed on a par with loans covered by the DCA, indicating the credit evaluation procedure employed by LGUGC is appropriate and reliable.

Findings: LGUGC has guaranteed loans to the target sectors without DCA coverage, and PFI confidence in LGUGC, inspired by the DCA commitment was certainly a factor in encouraging their participation in the financing of the sectors. The financial and managerial discipline imposed by the DCA, together with the skills fostered and analytical tools developed by direct technical assistance, helped LGUGC to extend its guarantees to the target sectors outside of the DCA.

Since inception of the DCA guarantee to June 30, 2009, the total value of the loans and bonds to the target sectors that have been guaranteed by LGUGC outside of DCA coverage is PhP2,089.30 million (US$42,120,590), including eight bond issues and loans to LGUs (six bond issues and two term loans) and three term loans to water districts. As mentioned earlier, two small bond issues were made before the DCA Guarantee Agreement was entered into and consequently are not included.

Table 6 below represents a summary of each of the LGU bonds and loans guaranteed by LGUGC without DCA guarantee coverage, which total PhP1,728.05 million (US$34,265,094). By June 30, 2009, the first five bond issues listed in Table 6 were fully redeemed leaving one bond issue and two term loans in place.

TABLE 6. LGUGC GUARANTEED BONDS/LOANS TO LGUS OUTSIDE DCA COVERAGE

BORROWER	YEAR	TYPE	PURPOSE OF LOAN	LOAN AMOUNT (PHP MILLIONS)	LOAN AMOUNT (US$)	LOAN TENOR (YEARS)	INTEREST RATE
City of Caloocan	2000	Bonds	Public Market, Comm'l Area w/ Toll Parking; Gen. Hospital	620.00	$12,550,607	7	182-day T-bill +3%
City of Tagaytay	2001	Bonds	Convention Center w/ Lodging Facility	220.00	$4,588,113	7	182-day T-bill +2.5%
City of Iloilo	2001	Bonds	Employee Housing	130.00	$2,605,210	3	182-day T-bill +2.5%
Province of Leyte	2003	Bonds	Academic Center	205.00	$3,749,428	7	6-month MART1 +3.75%
Municipality of San Juan	2003	Bonds	Multi-purpose Gym, Comm'l Bldg. & Toll Parking	390.00	$7,317,073	7	6-month MART1 +3%
Municipality of Baliwag	2006	Bonds	Integrated Solid Waste Management - MRF	50.00	$942,509	7	6-month MART1 +3%
Agoo Public Market	2008	Term Loan	Construction of a public market	93.50	$2,066,732	10	3-month PDST-F +3%
Imus Cadastral Project	2008	Term Loan	Cadastral survey	19.55	$445,422	5	3-month PDST-F +3%
	TOTAL			1,728.05	$34,265,094		

Table 7 summarizes each of the three water district loans guaranteed by LGUGC that were not placed under DCA coverage, amounting to PhP361.25 million (US$7,855,496). In addition to the three LGUGC guaranteed water district loans outside of the DCA that are listed below and the five water district loans subject to the DCA previously identified, there were six water financing transactions lost or suspended through LWUA's interference. Given the ongoing interest in water district lending expressed by the PFI's, together with loss of the water sector transactions for guarantee, it is probable that, without the market distortions created by LWUA, the number and value of water district loans at the time of evaluation would have been appreciably higher.

TABLE 7. LGUGC GUARANTEED LOANS TO WATER DISTRICTS OUTSIDE DCA COVERAGE

BORROWER	YEAR	TYPE	PURPOSE OF LOAN	LOAN AMOUNT (PHP MILLIONS)	LOAN AMOUNT (US$)	LOAN TENOR (YEARS)	INTEREST RATE
Calamba WD	2007	Term Loan	Repair & rehabilitation of existing water lines &distribution system	34.00	$735,322	5	3-month PDST-F +3%
Cabanatuan City WD	2008	Term Loan	Rehabilitation & expansion of water system	212.50	$4,786,263	10	3-month PDST-F +1.5%
Mabalacat WD	2008	Term Loan	Design & construction of ground reservoir & upgrading of the existing water supply system	114.75	$2,333,911	10	3-month PDST-F +2.5%
TOTAL				361.25	$7,855,496		

When LGUGC's non-DCA loan guarantees to the target sectors are combined with its DCA loan guarantees, the total portfolio value of target sector guaranteed loans amounts to approximately PhP3.5 billion (or $70.6 million). LGUGC loan guarantees outside of DCA coverage represent 60% of the value of that full target sector loan guarantee portfolio. The percentage breakdown of the value of LGUGC guaranteed loans to the target sectors, both with and without DCA guarantee coverage, is shown in Figure 4. Figure 5 represents the percentage breakdown on the basis of the total number of loan guarantees LGUGC has made to the target sectors.

According to LGUGC, all loans to the target sectors outside the DCA have honored their loan commitments and there have been no defaults. Although the performance of individual loans may vary, the credit evaluation standards and monitoring processes applied to DCA guaranteed loans are the same as those applied to non-DCA guaranteed loans, and the performance of loans outside of DCA coverage has been equivalent to those covered by the DCA. This suggests the credit assessment procedure is sound.

FIGURE 4. LGUGC GUARANTEED LOANS WITHIN TARGET SECTORS BY VALUE

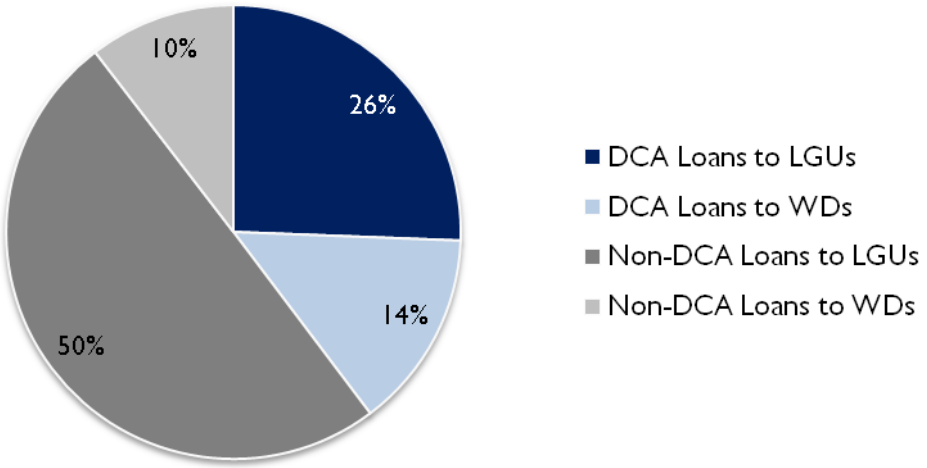
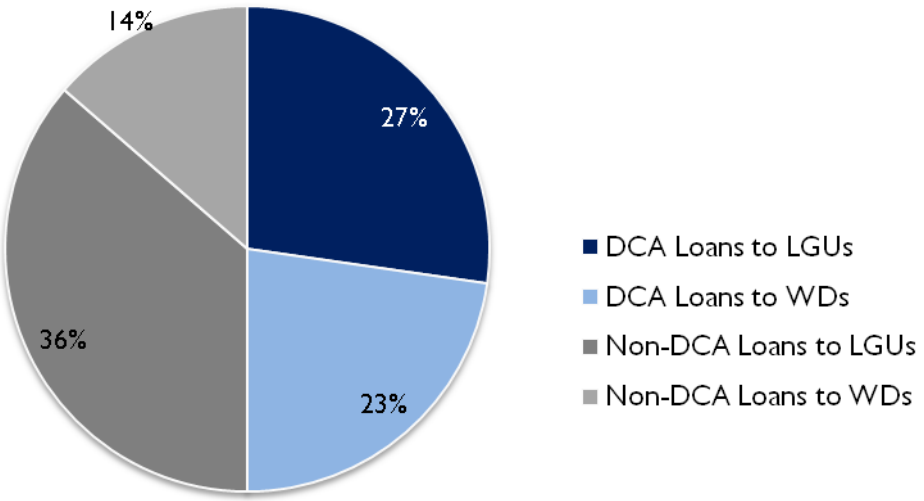


FIGURE 5. LGUGC GUARANTEED LOANS WITHIN TARGET SECTORS BY NUMBER OF LOANS



Findings And Conclusions For Question 8

Questions 8: Has LGUGC moved into any new sectors and types of borrowers outside the DCA guarantee? If so, has the DCA guarantee, as a demonstration model, played any role in LGUGC's decisions? How have LGUGC's guaranteed loans in all sectors outside those targeted by the DCA guarantee performed relative to its DCA guaranteed loans in the target sectors?

Conclusion: LGUGC has cautiously moved beyond the DCA target sectors to a limited degree, and is considering expansion into other sectors, including the energy sector, specifically electric

cooperatives. It has also extended its services to include program management of guarantee funds of other donors and IFIs, which reflects the confidence of the Philippine government and the development community in LGUGC's qualifications. From interviews with the LGUGC's management and staff and from observations, it is reasonable to conclude that the DCA as a demonstration model was a significant factor in LGUGC's decision to proceed into new areas. It is too early to compare the performance of loan guarantees outside the target sectors to those within but there have been no defaults yet.

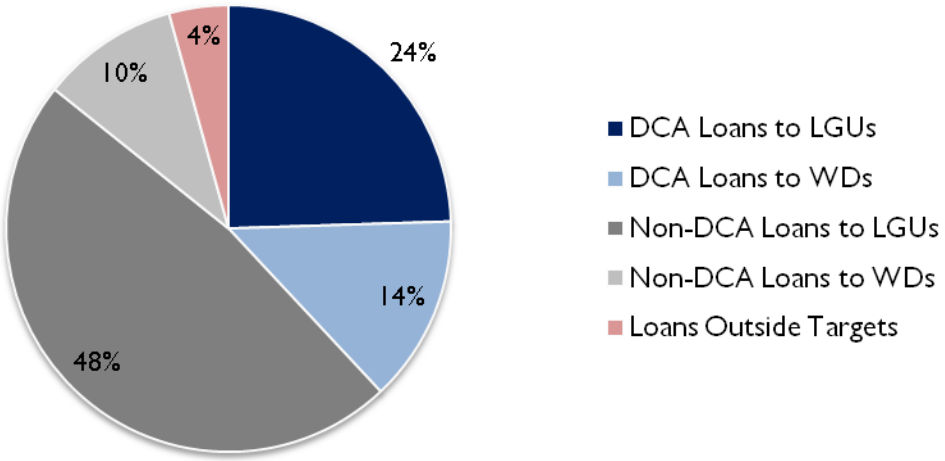
Findings: LGUGC has begun to carefully move into new sectors and to pursue new types of borrowers. In September 2008, LGUGC guaranteed a small PhP7.82 million (US$168,974) loan to Gerphil Renewable Energy, Inc. for construction of a mini-hydroelectric plant. It has also begun to guarantee loans to bulk water suppliers. LGUGC has guaranteed loans to bulk water suppliers of the Legazpi City Water District and the Norzagaray Water District. Although the loans involve the water districts and they are parties to the transaction, the loans are made to the bulk water suppliers and LGUGC guarantees the water districts' monthly obligations to them. These three guaranteed loans total PhP156.57 (US$3,424,407). Table 8 presents a summary of the foregoing guarantees.

TABLE 8. LGUGC GUARANTEED LOANS TO NEW SECTORS AND BORROWERS

BORROWER	YEAR	PURPOSE OF LOAN	LOAN AMOUNT (PHP MILLIONS)	LOAN AMOUNT (US$)	LOAN TENOR (YEARS)	INTEREST RATE
Bulk Water Supplier to Legazpi City Water District	2007	Bulk water supply	89.25	$1,992,348	7	9% Fixed
Gerphil Renewable Energy, Inc.	2008	Construction of mini-hydro electric plant	7.82	$168,974	10	10.5769% Fixed
Bulk Water Supplier to Norzagaray Water District	2009	Bulk water supply	59.5	$1,263,085	7	9% Fixed
TOTAL			156.57	$3,424,407		

Figure 6 reflects the relative value of all loans guaranteed by LGUGC including those outside the target sectors.

FIGURE 6. ALL LGUGC LOANS BY CATEGORY



Given the competencies LGUGC established as a result of the DCA and the experience of PFIs in lending to the target sectors with LGUGC guarantees, it is reasonable to conclude that the DCA guarantee as a demonstration model was a significant factor in LGUGC's decision to cautiously and deliberately expand beyond the target sectors.

LGUGC has also expanded its services to include guarantee program management. It was selected by the Philippines Department of Energy to serve as the Guarantee Program Manager for several projects supported by the World Bank, the United Nations Development Programme (UNDP), and the Global Environment Facility (GEF). Specifically the project guarantee funds for which LGUGC serves as program manager are: (i) the Electric Cooperative System Loss Reduction Project—Partial Credit Guarantee Fund; (ii) the Rural Power Project for Photovoltaic Systems—Loan Guarantee Fund; and (iii) the Capacity Building to Remove Barriers to Renewable Energy Development—Loan Guarantee Fund Program. LGUGC was chosen as program manager for the funds on the basis of its technical and financial qualifications. The selection affirms the capabilities and skills developed through implementation of the DCA guarantee and the accompanying technical assistance, as well as the reputation LGUGC has achieved among government counterparts and other donors and IFIs.

There have been no defaults under the loan guarantees to new sectors and borrowers. However, since there are only three such relatively new guarantees, their performance relative to the performance of the loans to the target sectors under the DCA guarantee cannot be assessed. The fact that LGUGC has another bulk water supplier loan among its proposed guarantees is some evidence to suggest that the loans are performing.

IMPACT FINDINGS AND CONCLUSIONS

On the impact level, the evaluation considered what, if any market change occurred by virtue of the DCA guarantee, and any demonstration effect it may have had.

Question 9: Have any PFIs initiated or increased lending to the sectors targeted by the DCA guarantee without benefit of a guarantee, or are any contemplating lending to the target sectors absent a guarantee? If so, what role did the DCA guarantee play as a demonstration model?

Question 10: Did loan access and/or terms improve for borrowers within the targeted sectors? If so, how and why? What role did the DCA guarantee play as a demonstration model?

Findings And Conclusions For Questions 9 And 10

Conclusion: To date impact of the DCA guarantee has been modest. One PFI recently lent to a water district without a guarantee. Although partially as a result of a familiar relationship, the PFI reported it would not have made the loan had it not been for its experience with the DCA and LGUGC guarantees. The same bank is contemplating lending to LGUs without a guarantee. USAID'S history with the DCA guarantee and the LGUGC led to approval of a second DCA guarantee with LGUGC as part of the Philippine Water Revolving Fund. The interest of private commercial banks in participating in the PWRF is likely due at least in part to their knowledge of and experience with LGUGC and its implementation of the original DCA. Access to private financing by target sector borrowers has improved to a limited degree with approximately PhP3.5 billion (US$70.6 million) going to such borrowers under LGUGC guaranteed loans during the period covered by the DCA. The DCA unquestionably played a significant role in the improvement of target sector access to private investment, most importantly by strengthening the credibility and capacity of the LGUGC.

Perhaps what is most important in terms of market impact is the fact that the overarching goal of the DCA guarantee was served: to introduce private investment to sectors where essentially none existed before—water infrastructure services and facilities of LGUs and water districts. The DCA guarantee was certainly a contributing factor, together with policies of the Philippine Government, the development of the PWRF, and the influence of assistance programs of other donors and IFIs, in initiating the process of private sector financing to the target sectors. Its long term impact as a demonstration model, therefore, could be significant.

Findings: It needs to be reiterated here that, being a partial re-guarantee of a partial LGUGC guarantee, the DCA guarantee involved is unique, not as a DCA transaction, but within the agreed Evaluation Framework to be employed. This is the case particularly when the financial partner's function is to open markets to private investment where neither borrower nor lender has had prior exposure. The impact of the DCA to date has been at best modest, but its long term impact as a demonstration model could be significant, particularly if the expressed policies of the Philippine government for rationalization and segmentation of funding for the target sectors are enforced.

To date one PFI, a bank long active in LGUGC, has lent to a water district without an LGUGC guarantee. The bank recently made a PhP100 million loan (US$2,100,000) to a water district with whom it was familiar. According to the bank's representative, however, the bank would not have made this loan without its experience with LGUGC and the DCA. With other water district borrowers, the bank would probably require the guarantee. But the representative also stated the bank is looking to lend to LGUs without a guarantee.

The injection of private finance into LGU and water district lending through loan guarantees improved loan access for borrowers in the target sectors. LGUGC has guaranteed roughly PhP3.5 billion (US$70.6 million) in PFI loans, which loans would not have been made without the LGUGC guarantees and the backing of the DCA. However, guarantees or other risk mitigation measures will continue to be necessary for PFI participation in the target sectors, particularly capital financing for water district infrastructure, since experience with lending to the target sectors is still limited.

As previously noted, there has been a trend toward longer tenors under LGUGC guaranteed loans. This trend is expected to be encouraged under the public-private co-financing arrangement of the Philippine Water Revolving Fund.

USAID's experience and history with the LGUGC and DCA guarantees, including their use in the Municipal Water Loan Financing Initiative, led to the approval of a second Philippines DCA guarantee (Guarantee Number 492-DCA-08-003) in 2008 as part of the Philippine Water Revolving Fund. Under the second DCA guarantee, LGUGC may guarantee up to US$37,500,000 in loans for water projects to creditworthy LGUs and water districts. The maximum re-guarantee percentage under the second DCA guarantee is 40% of LGUGC's 85% loan guarantee portfolio, with a Guarantee Ceiling of US$12,750,000.

The PWRF is capitalized by a JICA concessionary loan to the Development Bank that will leverage private funds to finance creditworthy water supply and sanitation projects. The Development Bank, using the concessionary loan funds of JICA, will make long term loans (with 15 to 20 year tenors) to water service providers combined with private sector commercial loan funds partially guaranteed by LGUGC and supported by the new DCA guarantee (with approximately 10 year tenors). While the initial maturities of the PFI loans will be 10 years, they will be amortized over 15 to 20 years, which reduces the debt service burden on the borrowers. At the end of 10 years PFIs have the option to extend the loans. The Municipal Development Fund Office will provide a standby line of credit for use should the private banks decline to extend their loans. The PWRF is, therefore, structured to allow funding to be affordable to water service providers while preserving the market terms of the private loans. It also attempts to address the problem of lack of correspondence between the limited loan tenors offered by PFIs and the longer tenors required by larger water infrastructure projects. No loans have been made under the PWRF yet.

The willingness of PFIs to participate in the PWRF with the second DCA guarantee can possibly be attributed to a number of factors (*e.g.*, the structure of the PWRF, the participation of the

Development Bank and the Municipal Development Fund Office), but the demonstration effect from the instant DCA agreement is almost certainly one of them.

Based on the foregoing, the impact of the DCA guarantee as a demonstration model so far has been modest. However the overall goal of the DCA guarantee is to bring needed PFI investment to bear in financing the water supply and sanitation sector. USAID support for LGUGC through the DCA guarantee was a key factor (along with a number of elements, including Philippine Government policies and priorities, the evolution of the PWRF, and the effect of other donor activities) in introducing private investment into the target sectors where there had been little or no private lending activity. As stated in the Concept Paper for DCA Evaluation "…*the 'demonstration effect'…refers to the longer term goals that occur well after a guarantee has expired*." The introduction of private investment to the sectors and the process the DCA guarantee helped to start is an impact, which in the long term could be significant. Progress has been slow due to exogenous influences, most recently the actions of the LWUA. But a beginning was made. The process is continuing with the PWRF and the credit enhancement provided by LGUGC under the second DCA guarantee. A number of donor projects are now under development to improve financing of either urban infrastructure generally or the water sector specifically, including the World Bank's project aimed at assisting less-than-creditworthy water service providers to complement the PWRF.

VIII. SUMMARY OF CONCLUSIONS

OUTPUT CONCLUSIONS

The DCA guarantee and the LGUGC shared the aim of mobilizing private financial resources for infrastructure projects, initially to local governments through creation of a municipal bond market. Over the course of the DCA guarantee, the objective evolved. When the municipal bond market evaporated as a result of external factors, the DCA Guarantee Agreement was expanded to include water districts as well as local governments. However, the DCA guarantee and LGUGC remained aligned throughout and the DCA served to strengthen the ability of LGUGC to accomplish their mutual objective by critically enhancing the credibility of LGUGC. To the private financial community, the DCA guarantee evidenced the commitment of USAID to LGUGC and assured scrupulous monitoring, which elevated the confidence of private banks in LGUGC's guarantee program.

Prior to the LGUGC private financing to the target sectors was virtually zero. While government policies and other donor and IFI programs encouraged PFI investment, the LGUGC guarantee program, supported by the DCA guarantee, provided the necessary risk mitigation and level of comfort to permit private capital actually to begin to flow to the target sectors, albeit in a modest volume. LGUGC guaranteed 22 loans to LGUs and water districts, of which 11 were placed under the DCA guarantee, allowing borrowers in the sectors access to private financing essentially for the first time.

No significant differences were detected in interest rates or collateral between the loans placed under the DCA guarantee and those that were not. There is evidence the DCA may have played some part in an increase in tenors of LGUGC guaranteed loans to water districts (both with and without DCA coverage) to the DCA maximum tenor of 10 years. Other factors that may have contributed to the increase in tenors of guaranteed water district loans include the character of the project, the type of financing instrument, and GFI competition.

Despite active marketing by LGUGC of its loan guarantee program, lack of experience with municipal bonds by both PFIs and LGUs translated into slow initial utilization of the DCA guarantee, until water districts became eligible for the guarantee. LGUGC marketing and education efforts then shifted to aggressively target the water district market, and DCA utilization swiftly climbed to its present rate of 86.3 % until private financing of the market was interrupted by the actions of the LWUA.

OUTCOME CONCLUSIONS

According to the DCA Guarantee Agreement and Action Packages, the desired outcomes for guaranteed loans were increased local credit market confidence in LGUGC, encouragement of private capital flows to the target sectors, and expansion of its operations. The local financial community had to have confidence in LGUGC for the desired outcomes to be realized. As

previously discussed, the DCA guarantee did provide LGUGC increased credibility. Additionally, the procedures, processes, management systems, and analytical methods and tools employed by LGUGC in its operations are to a significant extent a product of the monitoring and evaluation of the DCA guarantee performed by USAID/Philippines and EGAT/DC, as well as the related technical assistance and training provided through USAID.

Benefiting from the credibility provided by the DCA and accompanying scrutiny by USAID, LGUGC guaranteed 11 loans to LGUs and water districts outside of the DCA. Those target sector loan guarantees made without DCA protection represent approximately 60% by value of LGUGC's entire target sector loan guarantee portfolio. Since private financing effectively played no role in the target sectors before the LGUGC, its loan guarantees made outside of DCA guarantee coverage did modestly increase access to credit for target sector borrowers. LGUGC's experience with the DCA guarantee, including increased credibility and improved operational capabilities, make it reasonable to conclude the DCA was instrumental in its promotion of target sector private investment through loan guarantees outside of the DCA guarantee.

Strategic adjustments also aided LGUGC in its efforts to fulfill the outcomes anticipated by the Action Packages. As the municipal bond market waned, the DCA agreement was strategically modified to include water districts. The DCA guarantee and LGUGC proved important to both the U.S. and Japan by opening opportunities for partnering around water and sanitation finance in the Philippines, and led to amendment of the DCA agreement to make infrastructure projects of water districts eligible for the guarantee. The existence the DCA, in combination with LGUGC, offered the partnership a convenient, available and effective instrument for the attraction of private investment to the target sectors. As part of the joint U.S./Japan Municipal Water Loan Financing Initiative, LGUGC and the DCA helped provide the first private financing for a water district, which foreshadowed the creation of the Philippine Water Revolving Fund, and a second DCA agreement with LGUGC to support the PWRF. With vigorous marketing, LGUGC ultimately made a total of eight water district loan guarantees after the DCA agreement was modified in 2006 to include them, three of which were outside of DCA coverage.

LGUGC has begun to guarantee loans in new sectors and to new borrowers on a small scale. It has guaranteed loans to the bulk water suppliers of two water districts, and to a renewable energy company for construction of a mini-hydropower facility. It is also exploring expansion into other markets. Further, LGUGC is offering additional services and now acts as program manager for three guarantee funds of other donors and IFIs. It can be concluded that the DCA guarantee as a demonstration model, influenced the actions of LGUGC in venturing into new areas, since many of the same LGUGC capabilities cultivated under the DCA guarantee can be applied to the new sectors and services.

LGUGC applies the same credit standards and monitoring procedures, developed with USAID assistance, to all guaranteed loans. To date LGUGC guaranteed loans (both DCA and non-DCA guaranteed) to the target sectors have been equivalent in performance and there have been no defaults or claims, indicating the soundness of the assessments. However, as to guaranteed loans

beyond the target sectors, it is too early to appraise their performance relative to the DCA guaranteed loans.

When considered collectively, the foregoing supports the conclusion that LGUGC did expand the scope of its efforts and that the desired outcomes have been satisfactorily achieved with respect to LGUGC guaranteed loans outside of the DCA.

IMPACT CONCLUSIONS

The DCA guarantee is a partial re-guarantee of a partial guarantee, and as such any attribution is very difficult and primarily subjective. The impact of the DCA so far has been modest. Currently, one loan has been made by a PFI to a water district without any guarantee. The lending bank indicated its experience with the DCA and LGUGC guarantees was crucial to the grant of the loan, but the borrower was a known quantity to the lender, and future loans to water districts would likely still require some form of credit enhancement. However, the lender is considering making loans without a guarantee to LGUs.

Target sector borrowers have accessed approximately US$70 million in private financing guaranteed by LGUGC (under both DCA and non-DCA guaranteed loans). That amount stands to be multiplied by the newly created Philippine Water Revolving Fund. Building on the subject DCA, USAID's relationship with LGUGC, and experience with both in the earlier pilot project under the Municipal Water Loan Financing Initiative, the PWRF uses a new DCA guarantee to backstop LGUGC guarantees of private commercial capital. The private resources attracted by the guarantees unite under the PWRF with concessional ODA from Japan to fund water and sanitation projects at a blended rate. The decision of PFIs to participate in the PWRF is very likely a product of the demonstration effect of the DCA. Other reasons contributing to the decision include involvement of the Development Bank and the Mutual Development Fund Office, and the design of the PWRF.

Many measures have helped promote progress in achieving the mobilization of private investment to fund LGU and water district infrastructure, including Philippine government laws, regulations and policies; the development of the PWRF; and projects of other donors and IFIs. But with the DCA guarantee, the movement of private capital to these sectors, where private financing was basically unknown, could actually be seen. A demonstration effect by definition involves experience over a long term. The long-term impact of the DCA guarantee may be the process it began and that impact could be significant.

BIBLIOGRAPHY

ADB Report and Recommendation of the President to the Board of Directors. 2007. "Republic of the Philippines: Local Government Financing and Budget Reform Program Cluster (Subprogram 1)."

Asian Development Bank Sector Study Report. October 2008. "Philippines: Sources of Local Government Unit Financing."

Asian Development Bank Technical Assistance Consultant's Report. March 2009. "Philippines: Preparing the Philippine Basic Urban Services."

Asian Development Bank Technical Assistance Report. September 2008. "Republic of the Philippines: Preparing the Water District Development Sector Project."

Bureau of Local Government Finance (Philippines). June 2008. Moving Toward A Positive and Sustainable LGU Financial Performance: Statement of Income and Expenditures CY 2005-2007).

Economist Intelligence Unit. 2008. "Country Profile: Philippines." Economist Intelligence Unit, London, U.K.

Economist Intelligence Unit. June 2009. "Country Report: Philippines". Economist Intelligence Unit, London, UK.

Florento, Hector. September 2004. "Analysis of Constraints to Mobilizing Sector Financing for Water Supply and Sanitation Projects in the Philippines." Development Alternatives, Inc.

Freire, M and J. Peterson (eds.). 2004. "The Philippines, Subnational Capital Markets in Developing Countries: From Theory to Practice". Chapter 26.

Japanese Bank for International Cooperation. December 2006. "Special Assistance for Project Formation (SAPROF) for the Philippine Water Revolving Fund in the Republic of the Philippines: Final Report".

Kehew, Robert; Matsukawa, Tomoko; and Petersen, John. February 2005. World Bank Discussion Paper, "Local Financing for Sub-Sovereign Infrastructure in Developing Countries: Case Studies of Innovative Domestic Credit Enhancement Entities and Techniques."

Murata, Osama. March 19, 2006. Presentation to the Fourth World Water Forum, Mexico City. "Mobilizing Private Funds to the Water Sector."

Pellegrini, Anthony and Soriano, Cecilia. August 2002. "A Study to Revisit the LGU Financing Framework and Its Implementation". Final Report for the Philippines Department of Finance.

Philippine Water Revolving Fund Support Program. 2008. "Water Supply Project Appraisal Guidebook."

Bureau of Local Government Finance (Philippines). June 2008. Moving Towards A Positive and Sustainable LGU Financial Performance: Statement of Income and Expenditures CY 2005-2007.

Saldana, Cesara. February 1997. "Study for the Design of a Viable Private LGU Debt Guarantee Institution."

Soriano, Cecelia. July 2008. "Policy Issue Paper on Credit, Financing and Investments in the Water Supply Sector."

ANNEX A – CONTACT LIST

Name	Title	Organization
Leonilo G. Coronel	Executive Director	Bankers Association of the Philippines
Christopher "Rey" C. Ancheta	Operations Officer	The World Bank in the Philippines
Mary Joy Jochico	US-AEP Program Manager Office of Energy and Environment	USAID/Philippines
Maria Cynthia Nona M. Razo	Financial Analyst Financial Management Services Division	USAID/Philippines
Manny Miciano		USAID/Philippines
Bing Almeda		USAID/Philippines
Alberto E. Bienvenida	Senior VP/Head of Merchant Banking Division	Allied Bank
Lydia N. Orial	President/CEO	LGUGC
Thelma C. Sansales	Head/Senior Manager Operations Department	LGUGC
Aileen B. Castro	Head, Relationship Management Department	LGUGC
Ernestina Carbajal	City Administrator	Pasay City
Liduvino S. Geron	First Vice President Program Management Group	Land Bank of the Philippines
Ignacio C. Serrano	Senior Assistant Vice President	Development Bank of the Philippines
Rosemarie N. Sumway	Senior Manager Fund Sourcing	Development Bank of the Philippines
Justino A. Bote		Development Bank of the Philippines
Aurelio R. Montinola III	President	Bank of the Philippine Islands
Alberto E. Pascual	Senior Vice President	Bank of the Philippine Islands
Georgia A. Gamboa	Vice President	Bank of the Philippine Islands
Nanette A. Biason	Senior Manager	Bank of the Philippine Islands

Jin Wakabayashi	Representative Chief, Poverty Reduction Coordination Section	JICA
Flerida C. Chan	Senior Program Officer Poverty Reduction Section	JICA
Alma D. Porciuncula	Chief of Party	PWRF/DAI
Daniel I. Landingin	Acting Administrator	Local Water Utilities Administration
Cecilia Soriano	Consultant	
Alfonso C. Transeco	Senior Vice President Government Banking Division	Philippine National Bank
Josefino R. Gamboa	Senior Vice President Government Banking Division	Philippine National Bank
Armando A. Inabangan, Jr.	Senior Assistant Vice President, Government Banking Division	Philippine National Bank
Justino P. Fabian	Chairman of the Board	City of San Fernando Water District
Jorge P. Gumba	General Manager	City of San Fernando Water District
Paul Robert Flegler	Investment Specialist	Asian Development Bank
Jesus Tirona	Former President of LGUGC	Banco De Oro
Clyde Silao Esguerra	Development Management Officer III	Municipal Development Fund Office
Jeremias N. Paul, Jr.	Undersecretary	Department of Finance
Jose Arnold M. Tan, Jr.	Deputy Executive Director	Bureau of Local Government Finance
Ami Mary Magdalene B. Salva	OIC-Chief, PLANS Division	Bureau of Local Government Finance
Dave Penano	Municipal Administrator	Municipality of Carmona
Valentino S. Bagatsing	Investment Officer	International Finance Corporation

ANNEX B – COLLATERAL FOR LGUGC GUARANTEED LOANS TO LGUS AND WATER DISTRICTS DCA GUARANTEED LOANS AND NON-DCA GUARANTEED LOANS

Account	Collateral / Security
Non-DCA Guaranteed Loans	
Leyte Liberation Bonds - Series A	1. Proceeds from the revenues of the Project 2. Project improvement and facilities funded by the sale of the Bonds 3. Assignment of the deposit account as contemplated on the Deed of Assignment of Deposit of Internal Revenue Allotment
Baliwag Star Bonds	1. Proceeds from the revenues of the Project 2. Project lot covered by TCT No. 13875 3. Improvement and facilities funded by the sale of the Bonds 4. Assignment of the deposit account as contemplated on the Deed of Assignment attached as Annex "B" of the Trust indenture
Calamba Water District	1. Assignment of Reserve Fund 2. Assignment of Water Billings 3. Deed of Undertaking on the Assignment of Usufruct Rights on the Project Assets in favor of LGUGC 4. Insurance Coverage of Insurable Assets endorsed in favor of LGUGC and Lender 5. Real Estate Mortgage and Chattel Mortgage on properties offered as collaterals in favor of LGUGC and Lender
Agoo Public Market	1. Deed of Assignment of 20% of Internal Revenue Allotment (IRA) 2. Assignment of Project Revenue Fund Account which is subject to hold-out in an aggregate amount of P1.2 million 3. Unregistered joint mortgage on a parcel of land together with the buildings and all improvements, machineries and equipment now existing and which may hereafter be constructed, erected or placed thereon in favor of BPI & Allied Bank 4. Assignment of Usufruct Rights
Legazpi City Water District	1. Assignment of Reserve Fund 2. Assignment of Water Billings 3. Deed of Undertaking on the Assignment of Usufruct Rights on the Project Assets in favor of LGUGC 4. Insurance Coverage of Insurable Assets endorsed in favor of LGUGC and Lender 5. Real Estate Mortgage and Chattel Mortgage on properties offered as collaterals in favor of LGUGC and Lender
Cabanatuan City Water District	1. Hold-out on Reserve Fund equivalent to 3 monthly loan amortizations plus 1 annual guarantee fee 2. Assignment of Water Billings
Mabalacat Water District	1. Assignment of Reserve Fund 2. Assignment of Water Billings
Norzagaray Water District	1. Assignment of Reserve Fund 2. Assignment of Water Billings

DCA Guaranteed Loans	
Carmona Bonds	1. Proceeds from the revenues of the Project 2. Project improvement and facilities funded by the sale of the Bonds 3. Assignment of the deposit account as contemplated on the Deed of Assignment of Deposit of Internal Revenue Allotment
Pasay Kaunlaran Bonds	1. Proceeds from the revenues of the Project 2. Project improvement and facilities funded by the sale of the Bonds 3. Assignment of the deposit account as contemplated on the Deed of Assignment of Deposit of Internal Revenue Allotment
Imus Bonds - Series A	1. Proceeds from the revenues of the Project 2. Project improvement and facilities funded by the sale of the Bonds 3. Assignment of the deposit account as contemplated on the Deed of Assignment of Deposit of Internal Revenue Allotment
Metro Iloilo Water District	1. Assignment of Reserve Fund with Hold-out in an amount equivalent to 1 monthly amortization plus the amount of annual guarantee fee in favor of PNB
Silang Water District	1. Assignment of Reserve Fund with hold-out in an amount equivalent to 1 month amortization plus 1 annual guarantee fee 2. Assignment of Water Billings 3. Deed of Undertaking on the Assignment of Usufruct Rights on the Project Assets in favor of the Guarantor 4. Insurance Coverage of Insurable Assets endorsed in favor of the Guarantor 5. Real Estate Mortgage and Chattel Mortgage on properties offered as collaterals in favor of the Guarantor
Laguna Water District	1. Hold-out on Reserve Fund equivalent to 3 monthly loan amortizations on the outstanding balance 2. Assignment of Water Billings
City of San Fernando Water District	1. Hold-out on Reserve Fund equivalent to 3 monthly loan amortizations on the outstanding balance 2. Assignment of Water Billings
Indang Water District	1. Hold-out on Reserve Fund equivalent to 3 monthly loan amortizations plus 1 annual guarantee fee 2. Assignment of Water Billings

ANNEX C – PHILIPPINES DCA EVALUATION FRAMEWORK

EVALUATION QUESTIONS	DATA SOURCES (1) pre-field activities (2) field activities	DATA COLLECTION METHODS (1) pre-field activities (2) field activities	HOW DCA WILL USE THE EVALUATION FINDINGS, CONCLUSIONS AND RECOMMENDATIONS AND OTHER COMMENTS
OUTPUT LEVEL (Loans Disbursed, Additionality…):			
1a. How did the DCA guarantee fit into LGUGC's ongoing strategy? What market potential did the DCA guarantee help open for LGUGC? 1b. How did LGUGC implement the DCA loan guarantee program, and did implementation of its loan guarantee program change over the course of the DCA guarantee (e.g., marketing campaigns, changed terms, training, revised staff structure and responsibilities, improved communications within LGUGC, etc.)? And why?	(1) CMS data (1) DCA documents: Risk assessments, Action Packages, Legal Agreements, CRB minutes, biennial reviews, (1) or (2) Mission documents (2) Mission/ contractor/ staff (2) LGUGC officers and staff (2) BPA officers and staff (2) PDB officers and staff	(1) Review of data and documents in Washington/DCA; interviews with DCA staff (1) & (2) Review of documents in USAID missions (1) & (2) Interviews of cognizant USAID / contractor staff (2) Review of LGUGC data in the field (2) Guided interviews with LGUGC, BPA and PDB officers and staff	DCA use: Purposes 2 & 4 above and to enhance discussions with potential guarantee partners; to enhance the training that DCA provides to guarantee partners, missions, et al. Other Comments: Questions in 1a and 1b are primarily *descriptive* for LGUGC.

EVALUATION QUESTIONS	DATA SOURCES (1) pre-field activities (2) field activities	DATA COLLECTION METHODS (1) pre-field activities (2) field activities	HOW DCA WILL USE THE EVALUATION FINDINGS, CONCLUSIONS AND RECOMMENDATIONS AND OTHER COMMENTS
2a. Did LGUGC's use of the DCA guarantee improve access to credit for the target sectors? If so, how much local private capital was mobilized ("leveraging")? 2b. To what extent, if any, did the DCA guarantee influence changes in characteristics of LGUGC's loan guarantee portfolio?	(1) CMS (1) DCA biennial reviews (1) DCA portfolio managers (2) LGUGC officers/staff (2) LGUGC electronic files (as available) or samples of files (1) or (2) LGUGC annual reports (1) or (2) Industry/Central bank studies (2)Mission technical officers, CTOs and TA providers	(1) Analysis of CMS data (1) Documents review (1) Interviews of cognizant DCA staff (2) Guided Interviews of LGUGC officers/staff (2) Analysis of LGUGC electronic files on guaranteed loans within the targeted sectors covered by DCA guarantee (or samples thereof) (2) Analysis of LGUGC electronic files on borrowers covered by DCA guarantee (or samples thereof)	DCA use: To report on loans to stakeholders and Purposes 3 &4 above. Other Comments: Question 2a is primarily *descriptive* for LGUGC, addressing whether the DCA guarantee improved credit access for the target sectors. Question 2b is *explanatory*, *i.e.*, the extent to which the DCA guarantees influenced change. What we learn can affect what DCA does when talking to potential and actual guarantee partners, *e.g.*, asking them what they would change with a guarantee; encouraging guarantee partners to do x, y, or z; and so on in discussions; DCA TA and training to guarantee partners; and DCA encouragement of missions to provide TA and training aimed at increasing positive policies and behavior of guarantee partners.

EVALUATION QUESTIONS	DATA SOURCES (1) pre-field activities (2) field activities	DATA COLLECTION METHODS (1) pre-field activities (2) field activities	HOW DCA WILL USE THE EVALUATION FINDINGS, CONCLUSIONS AND RECOMMENDATIONS AND OTHER COMMENTS
OUTCOME LEVEL (LGUGC Behavior Change):			
3a. To what degree have desired outcomes contemplated in Action Package, Legal Agreement, and/or other relevant documents outside the protection of the DCA guarantee been achieved so far? What is the potential for sustainability of those outcomes? 3b. What factors at the LGUGC level can be associated with achievement of desired outcomes (*e.g.,* TA; LGUGC staff training; revised LGUGC strategy, procedures and structure; new management, etc.)? 3c. How have LGUGC's guaranteed loans to the target sectors outside of DCA coverage (if any) performed relative to DCA guaranteed loans to the target sectors?	(1) CMS data review (1) DCA documents: Risk assessments, Action Packages, Legal Agreements, CRB minutes, biennial reviews (1) or (2) Mission documents (2) LGUGC electronic files (as available) or samples of files (2) LGUGC annual reports (2) Mission/ contractor/staff (2) LGUGC officers/staff	(1) Analysis of CMS data (1) Documents review (2) Interviews of cognizant Mission/contractor staff and other stakeholders (2) Guided Interviews of LGUGC officers/staff (2) Analysis of LGUGC electronic files on borrowers covered by DCA guarantee (or samples thereof) and on borrowers in targeted sectors under loans outside of DCA coverage, if any (or samples thereof)	DCA use: Purposes 2, 3 & 4 above; to identify ways to achieve desired outcomes when dealing with potential guarantee recipients; to enhance the training that DCA provides to guarantee partners, missions, *et al.* Other comments: Question 3a is both *descriptive* and *comparative* (actual outcomes achieved to date through DCA guarantees vs. intended outcomes). Question 3b is *explanatory* in nature (to identify factors associated with why desired outcomes were achieved or not). Question 3c is *comparative* comparing performance of guaranteed loans to target sectors within and without DCA coverage.

EVALUATION QUESTIONS	DATA SOURCES (1) pre-field activities (2) field activities	DATA COLLECTION METHODS (1) pre-field activities (2) field activities	HOW DCA WILL USE THE EVALUATION FINDINGS, CONCLUSIONS AND RECOMMENDATIONS AND OTHER COMMENTS
4a. Has LGUGC moved into any new sectors and types of borrowers outside the DCA guarantee? 4b. If so, has the DCA guarantee, as a demonstration model, played any role in LGUGC's decisions? 4c. How have LGUGC's guaranteed loans in all sectors outside of the DCA guarantee performed relative to its DCA guaranteed loans in the target sectors?	(2) Mission documents (2) Mission technical officers, CTOs and TA providers (2) LGUGC officers/staff (2) LGUGC electronic files (as available) or samples of files	(2) Documents review (2) Interviews of Mission technical officers, CTOs and TA providers (2) Guided Interviews of LGUGC officers/staff (2) Analysis of LGUGC electronic files (as available) or samples of files	DCA use: Purposes 1 & 3. Other comments: Question 4a is *descriptive*; question 4b is *explanatory*; and question 4c is *comparative*.
IMPACT LEVEL (Market Demonstration Effect):			
5a. Have other private financial institutions (PFIs) initiated or increased lending to the sectors targeted by the DCA guarantee without benefit of a guarantee, or are any contemplating lending to the target sectors absent a guarantee?	(1) and (2) Sector/banking reports (if available) (2) LGUGC officers/staff (2) Associations of banks/ municipalities/water districts in the country/sector (2) Selected PFIs	(1) and (2) Documents review (2) Interviews of knowledgeable representatives of USAID Mission/TA contractor(s)/other donors/other	DCA use: Purposes 1 & 2. Other comments: Questions 5a and 5b will be answered qualitatively, for the most part, citing available sectoral data as appropriate.

EVALUATION QUESTIONS	DATA SOURCES (1) pre-field activities (2) field activities	DATA COLLECTION METHODS (1) pre-field activities (2) field activities	HOW DCA WILL USE THE EVALUATION FINDINGS, CONCLUSIONS AND RECOMMENDATIONS AND OTHER COMMENTS
5b. If so, what role did the DCA guarantee play as a demonstration model?	(2) USAID TA providers (2) Other key stakeholders	stakeholders (2) Guided interviews of LGUGC officers/staff (2) Guided interviews of the staff of selected PFIs	
6a. Did loan access and/or terms improve for borrowers within the targeted sectors? 6b. If so, how and why? 6c. What role did the DCA guarantee play as a demonstration model?	Same as for Question 5.	Same as for Question 5.	Same as for Question 5.

EVALUATION QUESTIONS	DATA SOURCES (1) pre-field activities (2) field activities	DATA COLLECTION METHODS (1) pre-field activities (2) field activities	HOW DCA WILL USE THE EVALUATION FINDINGS, CONCLUSIONS AND RECOMMENDATIONS AND OTHER COMMENTS
QUESTIONS THAT APPLY TO ALL THREE LEVELS—OUTPUT, OUTCOME AND IMPACT:			
7a. What are the exogenous factors (*e.g.*, financial sector reform, government intervention, lender industry competition, financial shocks, other donor behavior, others?) that have affected the financial sector? How have they done so? 7b. Have the exogenous factors affected the performance of the DCA guarantee (*i.e.*, at output, outcome and impact levels)? If so, how?	(1) Review of World Bank, and other donor or research documents/web sites (2) Cognizant USAID/TA contractor staff /other donor representatives (2) LGUGC officers/staff (2) Key stakeholders (e.g., central banks, banking associations, etc.)	(1) Documents review (2) Interviews of cognizant USAID/contractor staff (2) Guided interviews of LGUGC officers/staff (2) Other donor/key stakeholder interviews	DCA use: To set in context the Evaluation findings for Questions 1 – 6.