File PD-AAD-549
4920272
4920272 (4)
Philippines Rural Roads

p. 2 .2059

MEMORANDUM

September 5, 1974

TO: PPC/DPRE, Arthur M. Handly

FROM: PPC/DPRE/PR, Ronald Bobel

SUBJECT: Philippines FBS - Project Review

Rural Electrification - FY '75 and '76

Several issues should be raised with regard to new rural electrification loan proposals for FY '75 and FY '76.

1. With a recently authorized loan of $18 million for rural electrifation in FY '74, similar proposals for a $22 million loan in FY '75 and a $20 million loan in FY '76 raise questions as to the administrative capacity of the GOP and the cooperatives to carry out such an expanded effort. During intensive review of each of the new loans an assessment should be made of adherence to implementation plans under loans authorized in FY '72 and FY '74, and a careful assessment of Philippine capacity to undertake such a large scale effort.

2. It is noted that a condition of the FY '74 AID loan is the initiation of an evaluation of the countrywide electrification program in terms of the improved social and economic conditions of rural Philippines brought about by electric service. No indication is given regarding the timetable for that evaluation but some results should be forthcoming prior to authorizing an additional $42 million for rural electrification. It will be important to design projects which maximize the social and economic benefits to the rural poor.

3. Inevitable questions arise with regard to the financial aspects of the program. Rate structures should be set which provide a minimum, if any, subsidization so that the electrification program can generate sufficient revenue to pay for its operating costs and amortize its capital investment. The rate mechanism should be flexible enough for rapid adjustment in the face of inflationary conditions. This is particularly important for amortizing foreign debt where a maintenance of value technique is needed.

4. A related financial question concerns the contribution of the GOP to the program. As a self help measure their yearly percentage

contribution should be increasing. In this regard why is it not possible for the GOP contribution to expand sufficiently to preclude AID financing of local currency costs?

5. With regard to technical assistance, it is difficult to justify NRECA services on a grant basis when it is so directly tied to loan financed activities. Surely the cooperatives could amortize such assistance over a multi-year period. Indeed, technical assistance of this nature has usually been financed out of loan funds.

6. It is important that the capital assistance papers be quite explicit as to the proposed tie-in to pump irrigation projects and the nature of the target man to be benefitted. We should take care to assure that our financing acts to redress the balance between powerful and powerless and not solidify it.

Feeder Road Loan Proposal - FY '75

The following issues are among those relevant to the proposed feeder road loan.

1. Of primary importance is the conceptualization and application of the methodology used to select the individual road segments to be constructed. On the benefit side considerable weight should be given to those areas containing large numbers of small farmers who have secure land rights. Without the latter condition the major benefits may accrue to larger landholders whose properties increase in value as a result of the new or improved roads. In the design phase of the AID loan our experience with a similar type program in Brazil might be useful to the USAID and the GOP.

2. With regard to the financial plan, no provision is made for a direct GOP contribution -- only a $5 million contribution from the provincial governments. A contribution of at least $5 million should be required of the GOP to assure their commitment to the program.

3. This program appears appropriate for the fixed cost reimbursement technique as prototype plans will be developed based on unit costing. Thus, if the program is carried out inefficiently the GOP and the provincial governments will pay for it, and not AID. This should be a self-inducement for tighter host country control.

4. The degree of private sector participation in the program should be carefully analyzed. Thus, to what degree will the feasibility studies, design, supervision and construction be carried out by private firms? To the extent government agencies are used their capacity to carry out particular phases of the program should be justified.

5. Consideration should be given to maximizing labor intensive techniques for road construction in order to increase employment in the rural are

Agricultural Research Proposal - FY '75

Preliminary project information indicates that the proposal is consistent with policy goals and should be carried forward to the IRR stage.

The principal issue at this time, and one which must be addressed as the project is developed, is the linkage which exists between Philippine research and extension and the quality of extension delivery. The best research effort can go to waste unless the research information is transferred in understandable form to those - in the public or private sector - responsible for extension advice to the farmer. Furthermore, the extension delivery must be effective if the research information is to be utilized by the farmer. Therefore, part of our programming effort should be directed toward those problems discussed on p. 15 of the FBS... "Overall there are more than 4,000 agricultural extension workers and community development personnel. However, administrative efficiency is not good, and poor logistics support limits their capabilities."

It should be noted that approximately 25% of the loan is to fund technical assistance and training. This further indicates the appropriateness of loan funding for the additional NRECA input under the rural electrification loans and for the T.A. component of the small irrigation systems proposal discussed below.

Small Irrigation Systems Loan - FY '76

The following issues appear relevant to the small irrigation systems loan proposal.

1. The rate structure for water use should be an important consideration of project review. Achieving self-sufficiency would encourage a more rapid expansion of small irrigation systems because it would reduce the amount of budgetary support required. The FBS statement (p. 31) that the program will eventually be on a self-financed basis is disturbing. Such a policy should start in each project area as soon as the improvements are made; otherwise it will be difficult to obtain acceptance of a realistic rate.

2. It would appear that technical assistance could be funded under the loan rather than separately provided as a grant. Note that the agricultural research proposal is to include technical assistance and training under the loan.

3. Adequate agricultural credit and appropriate pricing policies are important ancillary considerations which should be taken into account to assure that production potential is realized from the small systems. With regard to pricing policies, the statement on p. 9 of the FBS that "...the Government is trying to moderate price increases of basic commodities, particularly rice, through a system of subsidies and price controls..." may be a cause of concern if the farmer's profit margin is cut too thin.

While the agricultural credit system has expanded through rural banks, the recent inflation rate of 40% is likely to drive savers away from bank deposits unless the interest rate structure is revised. Although these two issues are not directly project related, adequate policies for each are important for the overall success of any irrigation activity. [illegible]

cc: N. Cohen
B. Odell
P. Boughton
Philippine Desk (Chandler)
E. Griffel

OPTIONAL FORM NO. 10
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GSA FPMR (41 CFR) 101-11.6

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PD-AAD-919
492-T-055

UNITED STATES GOVERNMENT

Memorandum

TO : DISTRIBUTION

DATE: October 25, 1974

FROM : Frank Collins, EA/CCD

19p

SUBJECT: Philippines-Rural Roads (PRP)
Philippines-Rural Electrification III (PRP)
Thailand-Lam Nam Oon (PID)

We have scheduled a meeting of the East Asia Advisory Committee for Capital Assistance for 9:30 a.m., Friday, November 1, 1974, Room 609 RPC, to consider the attached Project Review Proposals (PRP) from the Philippines and the Project Identification Document (PID) from Thailand.

It is recommended that the PRPs and the PID be approved.

Your participation in this meeting is invited.

Attachments:
As stated

DISTRIBUTION:
EA/CCD, Mr. Norman Cohen
EA/CCD, Mr. A. R. Love
EA/CCD, Mr. M. M. Pehl
EA.CCD, Mr. L. W. Bond
EA/PPB, Mr. L. A. Marinelli
EA/SAA, Ms. S. J. Littlefield
EA/PHIL, Mr. D. M. Chandler
EA/TD, Dr. H. Dodge
SER/ENGR(EA), Mr. J. Sloan
GC/EA, Mr. H. Morris
PPC/DPRE, Ms. B. Clary (6)

PROJECT REVIEW PAPER

TO : East Asia Committee on Capital Assistance

FROM: EA/CCD Capital Projects Committee

SUBJ: Philippines Request for Authorization to Proceed with the Intensive Review of a Proposal for Capital Assistance to the Government of the Philippines to assist in financing development of Rural Roads. (Rural Roads - $15.0 million)

Summary:

Borrower: Government of the Republic of the Philippines (GOP).

Implementing Agencies: Department of Local Government and Community Development (DLGCD) and Provincial Governments.

Amount of Loan: $15.0 million

Terms: A.I.D.'s standard terms for Development Loans, i.e., repayment within 40 years including a 10-year grace period, with interest at 2% during the grace period and 3% thereafter.

Project: The project will provide for the reimbursement of up to 75% of costs for Provincial Rural Roads Development. This reimbursement will be through the Special Letter of Credit arrangement.

1. <u>Project Description</u>

This loan financed project is to improve/construct rural roads in those provinces which USAID and the Provincial Development Assistance Project (PDAP) have assisted in acquiring the necessary skills and equipment to construct and maintain their own rural road network. For the purposes of this project rural roads are those roads referred to as: farm to market roads, feeder roads, municipal or provincial roads. Currently with assistance from USAID and PDAP, 14 provinces are qualified to implement the project. This number is expected to expand to 18 provinces in FY 1976 and 22 provinces in FY 1977. As currently planned, the project will construct approximately 750 kilometers of farm to market roads and 2400 linear meters of bridges in the qualifying provinces over a three year period.

The project will be implemented through the Department of Local Government and Community Development (DLGCD). DLGCD is a separate department of the Government of the Philippines and is responsible for the development of local government and community development. The provincial Development Assistance Project is currently under the Development Management Staff in the Office of the President, but is scheduled to be phased into DLGCD, during the next two years. Construction will be initially financed totally by provincial funds. Upon completion of construction, according to standards and cost previously agreed to by USAID/PDAP/DLGCD, DLGCD will reimburse the province for an amount not to exceed 75% of the total estimated and previously agreed upon cost. USAID will reimburse the GOP an equivalent amount of $U.S. by a Special Letter of Credit in a U.S. bank from loan funds for disbursement by the GOP.

II. Selection Criteria

To qualify for financing under this project a province must:

(a) have been in the PDAP program for at least two years, which is considered the minimum period necessary to fully develop the management and engineering capability to properly implement the construction program.

(b) have a provincial development staff capable of conducting feasibility-type/criteria studies for sub-project planning, selection and evaluation.

(c) have a Capital Improvement Program (See Attachment #2).

(d) have a Road Network Program (See Attachment #2).

(e) have a functional Materials Testing Laboratory.

(f) have a Provincial Engineer's Office qualified to handle all aspects of implementation (design, construction, contracting).

(g) have a functional Provincial Equipment Pool with a deadline rate under 25%.

(h) have an Agriculture Section Inventory and Profile (See Attachment #2).

Further, for a particular road segment to qualify for financing under this project it must:

(a) average at least 10 farms of less than 3 hectares within its influence area per kilometer of length. (Note: the exact specification of this criteria must yet be determined).

(b) must not lead to a dead-end or impassable road at both ends.

(c) must lead to or connect to a road network that leads to a poblacion (rural urban center, market place).

(d) satisfy specified economic and technical criteria.

DLGCD, with the concurrence of the USAID Provincial Development staff, will certify that each province and each sub-project meets the criteria listed above before authorizing a province to undertake preparation of final plans and specifications. DLGCD will contract with local A & E firms to provide independent monitoring of the design and construction and provide a certification that work was completed as agreed for purposes of reimbursement.

III. Project Cost

It is estimated that a $15 million loan (U.S. $ = P6.66 or $15 million = P100 million) will be sufficient to reimburse the GOP 75% of total cost for the improvement/construction of 750 kilometers of roads and 2400 linear meters of bridges. Depending upon the design standard it is now estimated that the cost per kilometer of road will range from P50,000 ($7500) to P200,000 ($30,000) and the cost per linear meter of bridges improvement/construction will range from P3,000 ($450) to P15,000 ($2,250). The mix of road to bridges may change as individual provincial plans are completed. Funds will be allocated to the province as shown in Attachment #1. The planned allocation of funds was based upon past performance of the provinces in implementing the 1972 flood rehabilitation project and in consideration of the province's ability to initially finance the project. The total project cost in pesos is estimated at P135 million with P100 million equivalent to be reimbursed by the loan of P35 million to be provided by the province.

The total loan funds will be disbursed over a three year period.

ROADS - KILOMETERS X REIMBURSABLE COSTS (P000's)

Standard	Year - 1 (P x Km)	Year - 2 (P x Km)	Year - 3 (P x KM)
Low	50 x 130 = 6,500	55 x 150 = 8,250	60.5 x 170 = 10,285
Medium	100 x 40 = 4,000	110 x 50 = 5,500	121.5 x 60 = 7,290
High	200 x 37 = 7,400	220 x 51 = 11,220	242 x 55 = 13,310
Totals	17,900	24,970	30,885

BRIDGES - METER X REIMBURSABLE COSTS (P000's)

	Year - 1 (P x LM)	Year - 2 (P x LM)	Year - 3 (P x LM)
Concrete	15 x 350 = 5,250	18 x 400 = 7,200	21.60 x 450 = 9,720
Lumber	3 x 300 = 900	3.5 x 400 = 1,400	4 x 500 = 2,000
	6,150	8,600	11,720

Note: Reimbursable construction costs per kilometer of road for the lowest design standard road is estimated to be approximately P50,000, P100,000 for the medium designed road and P200,000 for the highest designed road. Road costs are increased 10% in the second and third years to allow for escalation. For planning purposes, it is estimated that the total project kilometers of roads will be constructed over the three years as shown on the above table. It is also planned that the construction of 2400 linear meters of bridges will be spread over three years as shown on the above table. Bridge costs were escalated about 20% in the second and third years because of the use of large quantities of steel, cement and lumber.

IV. Current Situation

In general, the Philippines has a dry season and a wet season. The wet season lasts for about six months out of the year and during this season most barrio roads (rural roads) are impassable. This is true even for the province of Bulacan, one of the most developed provinces just north of Manila. During this wet season two thirds of the rice crop is harvested. Adequate farm to market roads are needed to: help the small farmers to move his produce to storage or market facilities during the "sellers market" periods; help extension workers get in the area to help farmers; permit the visits of government workers, social workers and doctors; generally to facilitate the two way movement of goods and services and, thereby, to improve the quality of rural life.

In addition to this proposed project the IBRD is providing $5 million for rural roads to support a major national highway program in Luzon, also financed by the IBRD. The Asian Development Bank also has become interested in rural roads and is considering a road project in Mindanao and smaller projects in Mindoro and other parts of the Philippines. The Government of Australia financed provincial roads in Mindanao. However, these foreign financed road projects are more truck routes rather than rural roads.

The development of the national highway system is essential and understandably a top priority of the national government. It is the upgrading of the national system which will support the development of a rural road linkage to be assisted by the proposed loan. The following major projects are in various stages of implementation throughout the Philippines: the Japanese/Philippines Friendship Highway which is to traverse the full length of the Philippines, the IBRD national highway project in Central Luzon ($69 million), another IBRD project in Mindanao and an ADB project in Mindanao.

V. PDAP Background

In 1968 PDAP was created to replace "Operation Spread". Operation Spread was a very successful joint GOP/USAID program initiated to support agricultural production in two provinces and USAID dealt directly with these provinces in identifying and providing inputs. PDAP was created to work closely with the National Economic Council (NEC) to improve the quality of rural life by accelerating and supporting development in agriculture, infrastructure, tax administration, field management, family planning and nutrition in selected provinces. PDAP's working relationship with NEC was transferred to the Office of the Executive Secretary to the President in December, 197_. It is now planned to phase PDAP into DLGCD where they will continue systems development and pilot installation operations leading to improved local government management systems on a nationwide basis.

PDAP/USAID is continuing to focus on assisting provincial governments through the PDAP projects. This is being accomplished by providing (1) technical assistance in comprehensive planning, fiscal resources development, through vertical and horizontal communication process; (2) providing commodity assistance for the Provincial Development Staff (PDS) operations, equipment pool operations; (3) and funding assistance for the Special Infrastructure Program (SIP) (See Attachment #2).

VI. PDAP Provinces' General Capabilities

The USAID Assistant Director for Provincial Development (AD/PD) has a staff of 16 direct hire and two PASA technical personnel assisting thirty (30) GOP/PDAP technical personnel in attaining the overall objectives of this program. USAID is confident that the qualified PDAP provinces are developed to the point where they can implement this project without additional foreign assistance.

The PDAP project provinces are chosen primarily because of their expressed willingness to accept and utilize technical assistance to improve their management capabilities. In general, they are the more progressive provinces, important agriculturally, and are not the most economically underdeveloped. One of the outputs from successful implementation of this proposed feeder road loan project could be the expansion of the whole PDAP philosophy to many other provinces. This is evidenced by the fact that the number of participating provinces is continually expanding and expected to expand during the next two years. The fourteen provinces selected to initially participate in the proposed rural roads program have demonstrated their abilities to effectively attain PDAP/USAID major objectives of fiscal management and infrastructure development. Eight of the fourteen provinces participated in the Flood Rehabilitation Program in which they gained invaluable experience in road and bridge design, project planning and administration, contract administration, quality control and equipment pool support for force account construction operations. The other six provinces are now participating in the SIP, thereby gaining the same valuable experience.

VII. PDAP Provinces' Engineering Capabilities

The Provincial Engineering Offices (PDO's) were established in

1968, in order to provide the newly responsible local government authority for development and maintenance of local infrastructure with operational capabilities. The PEO's were initially staffed by personnel transferred from the Bureau of Public Highways, the national organization then responsible for maintenance of existing roads, bridges, communal irrigation systems and provincial buildings. Specific USAID inputs have included excess property heavy construction equipment allocations to the PEO's. Perhaps more important than the provision of such physical equipment has been the training programs sponsored by USAID/PDAP to develop skills in all phases of equipment pool management and operations. The following elements were a part of this program: Five Year Capital Improvements Programs, Equipment Pool Development Programs, Development of Equipment Pool Operations Manuals, a Quality Control Development Plans with a Quality Control Operations Manuals, Provincial Road Network Development Plans, Provincial Action Budgets oriented toward development and joint PDAP/Province Work Plans. Success of these programs has led to the creation of a similar program, the Special Intrastructure Program, which involved six other PDAP provinces. These programs have provided a valuable proving grounds for testing and improving the capabilities of the PEO's in provincial program management. The combined staffs of all 14 PEO's include 173 graduate engineers of which 125 are civil engineers and 21 are mechanical engineers (Equipment Pool Supervisors). The remaining 27 are quality control specialists and chemical engineers trained in the management and operation of materials testing and construction quality control facilities.

Ten of the 14 PEO's have fully equipped operational construction materials testing laboratories and the remainder have placed orders for equipment and should be operational before start of this rural road program. Each PEO staff includes at least two qualified quality control laboratory technicians with a combined total of 44 in the 14 provinces. The Quality Control Division of each PEO includes an inspection section to monitor construction methods and practices, a materials quality control laboratory and a survey section for horizontal and vertical controls. The fourteen PEO's have received a ten week equipment pool training program involving training in equipment pool operations and in equipment operations and maintenance. This training is afforded by a team of PDAP/USAID equipment specialist and in accordance with the present schedule will be completed in the remaining provinces by March, 1975.

A combined total of 42 persons from the PDS-PEO staffs have received seminar training on data collection and assimilation for, and preparation of a provincial Road Network Development Plan. With this background of training and operational development programs plus the seminar planned in transport socio-economic analysis, the PDAP provinces will be capable of successfully carrying out this proposed rural road program.

PDAP will directly monitor the Provincial activities under the proposed rural road program with a staff of 30 professional personnel. This staff includes 5 Area Specialists trained in Public Administration and 10 engineers who will assist the provincial activities in road designs cost estimating and construction of projects. Personnel available to assist provinces in specific problem areas include equipment specialists to assist in upgrading the PEO Equipment Pool operations, personnel and administration Specialists, fiscal management specialist and training specialists. A professional economist has been detailed from DLGCD to PDAP to work specifically on the sub-project economic justification methodology.

VIII. Economic Justification

The two traditional economic methodologies applicable to road projects will be used. They are the benefit methodology applicable to penetration roads into new areas (net incremental agricultural output) and the other to road improvement that reduce transport costs (savings in user costs). Social benefits which, however, are unlikely to be quantifiable, may also contribute to the road improvement justification, especially for the health and education sectors will be reviewed and discussed in the benefit/cost analysis when applicable.

Preliminary meetings with PDAP personnel have indicated that they are familiar with these transport economic methodologies and have begun the preparation of several illustrative examples for actual road segments. The purpose of this PDAP exercise is to test the availability of existing information and the requirements for additional information to meet the economic analytical test. PDAP believes that with the work already done on land use, road network inventories and crop yield measurements plus the vehicle operating cost information generated by numerous IBRD and BFW studies, a substantial data base is available. During CAP preparation USAID will be working closely with PDAP to define the extent of available information, its quality and the need for additional data. To facilitate this effort, USAID is endeavoring to recruit an experienced transporation economist to work with PDAP to refine the methodology, review available information, assist in developing the forms and/or instructions to be used, evaluate PDAP analytical capability and determine the the technical training that should be undertaken during project implementation.

IX. Implementation

The Department of Local Government and Community Development (DLGCD) is the government organization responsible for overall implementation of this project. Individual provinces will be responsible for contructing the projects and for continued maintenance. The steps in the project implementation process contemplated at present are as follows:

1. The participating provinces will submit their Provincial Road Network Development Plan to DLGCD for review and approval. Upon approval the province will identify those rural roads that it wishes to construct/improve under this project. This selection will be based upon defined criteria and a feasibility study.

2. When DLGCD and USAID agree on the list of sub-projects to be implemented under this program, the province will allocate the total estimated cost of the approved projects to be implemented during the current fiscal year. The total combined amount of all

provinces allocated over a three year period will not exceed the allocation budget attached to this IRR.

3. The individual provinces will proceed to construct the roads. In most cases the provinces will use force accounts for roads and contractors for bridges. This has generally been the procedure used under the flood rehabilitation program.

4. It shall be the responsibility of DLGCD to contract with a local A & E firm to monitor construction and to certify satisfactory completion. As roads are certified as completed according to the agreed plans and specifications, AID will reimburse the GOP for an amount not to exceed 75% of the previously agreed estimated cost of the road by crediting a Special Letter of Credit (SLC) in the U.S. for U.S. procurement. In actual practice, AID will probably credit the SLC on a quarterly basis, depending upon the speed of project implementation.

X. Problems and Issues

It now appears that a project can readily be developed based upon the positive USAID experience with the PDAP provinces. There is considerable capability in PDAP and chances for successful project implementation are excellent. While there are no major issues and problems that must be resolved before this project can commence the PDAP and USAID are continuing their efforts along several lines:

1. The sub-project economic justification methodology is being refined and training will be provided PEO-PDS's.
2. The design standards currently in use in the Philippines are adopted from those used by the U.S. Bureau of Public Highways. Adoption of these standards to rural roads with an average daily trafic (ADT) below 100 might result

in over designed roads. These standards will be discussed with the GOP and revised, as appropriate.

3. It is the responsibility of DLGCD to contract with local A & E firms to monitor the design and construction of the sub-projects. The degrees and type of monitoring will be specified in the CAP and the method of reporting and assurance of funds to contract for services.

4. Republic Act 917, amended by Presidential Decree-17 and PD-320 now provides for maintenance funds for all provincial roads approved by the Bureau of Public Highways. The procedure requires the province and the national government to share the cost of P3375 per kilometer of road. Assurance will be obtained that the Bureau of Public Highway will readily approve roads proposed under this project and that maintenance funds will be budgeted and provided.

CD:AJT:mm
8/28/74

TENTATIVE ESTIMATE

FIXED COST REIMBURSEMENT FOR COMPLETED PROJECTS

(P million)

PROVINCE	FY 76	FY 77	FY 78	TOTAL
La Union	P 1.0	P 1.0	P 1.5	P 3.0
Pangasinan	2.0	2.0	2.5	6.0
Zambales	1.0	1.5	1.5	4.0
Bataan	1.0	1.5	1.5	4.0
Pampanga	3.5	4.0	4.5	12.0
Bulacan	3.5	4.0	4.5	12.0
Batangas	1.0	1.0	1.5	4.0
Camarines Sur	1.0	2.0	2.0	5.0
Albay	*	*	1.0	1.0
Sorsogon	*	1.0	1.0	2.0
Mindoro Or.	1.0	1.0	1.0	3.0
Aklan	*	*	1.0	1.0
Capiz	*	1.0	1.0	2.0
Antique	*	1.0	1.0	2.0
Iloilo	1.0	1.0	2.0	4.0
Samar	*	*	1.0	1.0
Misamis Or.	2.0	2.5	2.5	7.0
Agusan Norte	*	*	1.0	1.0
Lanao Sur	*	1.0	1.0	2.0
So. Cotabato	2.5	3.0	3.5	9.0
Davao (Norte)	2.5	3.0	3.5	9.0
Palawan	1.0	1.5	1.5	4.0
TOTAL	P 24.0	P 33.5	P 42.5	P 100.0

DEFINITIONS

PDAP - Provincial Development Assistance Project

DLGCD - Department of Local Government and Community Development

NEDA - National Economic Development Authority

P E O - Provincial Engineering Office

ADPD - Assistance Director Provincial Development

G O P - Government of the Philippines

P D S - Provincial Development Staff

Capital Improvement Program - a comprehensive five year listing of major public improvement projects in a proposed priority, time and funding frame.

Provincial Road Network Development Plan - a comprehensive inventory of existing roads of all classes and projections of road requirements for the future, construction schedules, funding, and supporting geological, geographical and socio-economic data.

Agriculture Section Inventory and Profile - a description of the magnitude, nature, and supporting resources of the agricultural sector.

Special Infrastructure Project - a project under an agreed reimbursement to participating provinces for approved infrastructure projects completed according to agreed plans and specifications.

Philippines Rural Roads Issues

1. The objectives of the proposed project loan need to be set forth in detail. As stated in the IRR, they are to build feeder roads, not provincial institutional development or increased agricultural production. There is no basis by which this project might be evaluated, other than so many kilometers of road and linear meters of bridge built.

The project is presented as a general rural development activity, but lacks sufficient information and data about its real impact on the agricultural sector, which should be one of its primary objectives. The IRR is phrased too much in terms of PDAP/Public Administration concerns and not enough in terms of what and how this project will actually help increase agricultural production and improve small farmer income.

2. There should be an interlinkage with irrigation systems and development. The CAP needs to include evidence that agricultural agencies at the national level and their representation in the field are synchronized to these agriculture development plans prepared in the provinces (i.e. National Agricultural Program, not simply provincial agricultural aspirations should be a factor in selection of road sites). There is also a need to assess stated priorities as to what constitutes a major agricultural province.

3. The tentative selection criteria in the IRR do not mention any aspect of the land reform problem. Should not land tenure arrangements be included as a significant selection criterion?

The basis for the tentative allocation of funds in the IRR (Attachment No. 2) is presumed technical-administrative capability-not need. Secondly the PDAP provinces are probably the more economically developed ones in the Philippines. Unless the selection criteria are more precisely stated, there is no basis to show how this loan matches with the AID Congressional mandate for increased social equity.

4. Who is currently building feeder roads? IRR describes Provincial Government role currently as maintenance. Are they building roads or is national government? Will this program be in addition to existing program or will it replace it? It can be questioned if this loan is a substitute for the GOP's own provincial road budget. The size of any current program should be detailed, and how this project can directly benefit the extension of feeder roads development or improve an existing program carefully explained.

5. Why use a catch all term of "rural roads" if we are really talking about barrio roads i.e. non-national, provincial, or municipal roads - and if so should any segments of such "high class roads" be excluded?

The IRR gives a range of costs per kilometer of road and per linear meter of bridges which suggests different types of roads. Types of roads and where they might be located (provincially and topographically) should be specified so a reasonable judgement as to estimated cost can be made.

6. In the early 60's the Philippines had a reasonably successful self help road program wherein rural people provided labor. The lacking element was consistent access to heavy equipment for segments of the work and technical

assistance from Public Works. Since these problems are now "solved" (sic) why not involve people who will use these roads?

7. The IRR states that the DLGCD will have the responsibility to contract with local A & E firms to monitor road construction and certify satisfactory completion. While there are competent A & E firms in the Philippines, there is a need to specify A & E capabilities as it relates to their ability to take on the workload. The relationship of the DLGCD to the A & E firms should also be detailed, i.e., how will DLGCD monitor the monitors?

8. What are the goals, purposes, inputs and outputs? If their are any substantial "development administration" purposes or innovations they might as well be highlighted. Also, estimates of transport cost reduction, agricultural changes, social changes, etc. should be included.

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UNITED STATES GOVERNMENT

Memorandum

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4920272(6)
PD-AAD-549

TO : PPC/EC:Ms. Mary Jane Heyl

DATE: November 18, 1974

FROM : for R M Dangle
Rural Roads Project Committee

SUBJECT: Philippines --- Rural Road - $15 million

18p.

The questions raised in your November 13 memorandum to Mr. John Shannon, PPC/DPRE/PR, are all considered relevant and are answered below. However, first I believe an overview of the subject proposal is necessary, especially in view of your previous long association with the Philippine program.

This new project is a total departure from earlier A.I.D. undertakings in roads development programs both in the Philippines and elsewhere. The three basic major improvements are:

1. The planning, implementation and evaluation is being handled at the Provincial and Municipal level which strikes right at our Congressional mandate to work with the poor majority to enhance their capacity for self-help development in making sure the project is a success. In this case, we are drawing upon the recent success of these provincial staffs in carrying out similar projects under the 1972 Flood Rehabilitation Grant program. And remember, the level of annual average participation in any one province under the project is only approximately $200,000. This is a small amount for the large potential return in institutional development we foresee as an outcome of this self-help effort, not withstanding the physical completion of much needed barrio roads.

2. The PDAP provinces each have organized and built-up a small equipment pool (sufficient for future maintenance needs) using U.S. excess property. Again, this is a departure from past practice which we believe will assure that the equipment pools do not end up as a "disaster case" as some have done in the past. The new element in this case, is a reliance upon the private sector to handle re-conditioning of equipment and the government to be responsible for routine maintenance of equipment. This practice was introduced into the provincial equipment pool programs and to the National Irrigation Administration equipment program (supported by a 1967 AID loan) specifically because of the problems encountered in the old DLF Roads and Bridges Loan. The practice has been highly

successful in both programs and we have plenty of statistical data on deadline rates to support this fact. Furthermore, the project sets a maximum deadline equipment rate that each province must maintain to remain eligible for participation in the subject program.

3. And maybe the most important element of all, a province must participate for several years in a management planning and general development training program before they become eligible to participate in this type of project. The training programs are conducted by PDAP, with USAID assistance, as a continuous operation.

Following the above, here are answers to your questions:

1. How much of resources, if any, available under this loan are going for heavy earth moving equipment?

None. The local currency generated by these loan funds go directly for services and local construction material.

2. What source is funding engineering and management services; will the engineers be local or will they contract for foreigners?

All A&E contracts will be made with Philippine engineering firms who will contract directly with the GOP. Financing will primarily be for the account of the GOP, although some technical services may also be funded out of the loan.

3. Are adequate supply and repair centers, reasonably contiguous, operating, being maintained and tolerably administered?

Yes. The modus operandi for equipment maintenance is one of the innovations which should make this project potentially one of the most successful AID financed road endeavors. Reconditioning of U.S. excess property equipment is carried out by contract with the private sector. Routine maintenance is accomplished at each provincial equipment pool headquarters. This system of going to the private sector for heavy maintenance eliminates the need for the local government agencies to maintain a large spare parts inventory.

Furthermore, provinces failing to properly maintain their equipment are dropped from the project eligibility list.

4. What is our, or the U.S. Bureau of Public Roads' objective opinion of the capacity of the Philippine Bureau of Public Roads or its equivalent to oversee, maintain, operate and administer this project?

Neither the U.S. Bureau of Public Roads nor the Philippines Department of Highways are directly involved with this project. The project planning, implementation, and evaluation will be accomplished by the provincial governments' engineering office. Based upon the PDAP provinces' recent performance of administering a similar type project under the 1972 Rehabilitation Grant program and a PL-480 Special Infrastructure Project, USAID is confident that this subject project will be extremely successful.

5. Have we ensured that no segment of the rural road program is purely political; i.e., a private road to the Governor's estate (as was the case in Mindanao)?

Yes. Very stringent selection criteria have been developed to assure that selected road segments will serve the small farmer in primarily rice and corn agricultural areas.

6. What about the capacity of the local, provincial, county, what have you, authorities to carry out their part in their segment of the project?

The size of the program is based upon the proven capabilities of each provincial government to implement their portion of the project within the specified three years time period.

7. Has anyone looked at the old GAO report or early AID inputs into the road program in the Philippines so that we are ready to indicate how we are prepared to prevent a repetition of the deficiencies reported therein?

Members of the Project Committee and the old Asia Capital Development Office who helped develop this project are familiar with the old DLF Road and Bridges Project and its problems. This project is designed to prevent repetition of deficiencies reported in past Philippine, as well as other AID financed, road projects.

The Mission believes this project will be successful for the reasons stated in the introductory overview and that past reported deficiencies should not re-occur.

8. How does this fit into a transportation sector analysis of the Philippines, if any? I have taken note of the allegation that the Philippines' four-year plan contains a transportation section of which this is part. But, I wonder if any AID person has formed an independent judgment on the quality of the transportation sector. How it fits into the national plan and how this project fits into the transportation plan.

The IBRD, in their transportation sector and agricultural sector surveys, identify the lack of adequate low cost farm-to-market roads as a constraint to adequate development of the rural area. The IBRD identifies that AID technical assistance to the provincial program in planning, design, construction and maintenance has been able to generate in effect a substantial volume of highly productive infrastructure investment in the form of relatively simple, low standard and low cost farm-to-market roads with consequent impact on local economic activity, employment and income. This project is designed to bring this program to an increasing number of provinces.

9. What is the proportion of local currency to foreign exchange requirements?

This is a 100% local currency project.

Tab 2

Beneficiaries

One of the major problems in attempting to evaluate the potential beneficiaries of any program in the rural areas of the Philippines is the comparitive lack of statistical information on these areas. This is particularly true as it applies to the distribution of income and wealth and patterns of lesser use in agriculature and the rural areas generally. Our concern in this regard is supported by the extensive International Labor Organization report "Sharing in Development, A Program of Employment, Equity and Growth for the Philippines" and by the recent IBRD economic team in its efforts to provide analysis in this area.

A general breakdown of the distribution of the "rural poor" (in this case the lower 40 percent income bracket) was completed by the recent IBRD economic team. The tabular summary of this analysis is shown on the following page by Region. A location map showing the provincial composition of each region is also included.

The bottom 40 percent of Filipino families receive approximately 12 percent of the national income and include 15 million people. 12 million of these people reside in rural areas with the majority living in farm households. In comparison, the top five percent of the population received 25 percent of the income.

As indicated in the tables, income levels and related incidence of poverty vary considerably throughout the Philippines. Ilocos, Cagayan Valley, Bicol and the Eastern Visayas are high in the incidence of poverty. Southern Tagalog, Eastern Visayas and Southwest Mindanao start out in terms of absolute numbers. The Central Luzon area, while high in medium income, nevertheless has a high incidence of rural poor (28.0% in the lower 40%) and accounts for 12.5% of the rural families in this income bracket.

In selecting the provinces to be included in the proposed program, the GOP and USAID have had to balance the factors of distribution and incidence of poverty against other key project criteria, e.g. (a) provincial government competence and available equipment pools; (b) association with agricultural land - particularly rice and corn farmers; (c) the related nationwide focus of the agrarian reform program which this project partially supports; and (d) other supporting government programs which enhance the prospect, that the roads constructed will in fact support an integrated GOP effort rather than an isolated activity.

The rural road project proposed herein will be implemented in eight of the ten regions of the Philippines in which reside approximately 85 percent of the 40 percent target population. Approximately 25 percent of the 12 million rural poor included in the bottom 40 percent are located in the twenty-two provinces included in the proposed program.

Regional Population Distribution, Family Income and Distribution of the Bottom 40 Percent in 1971

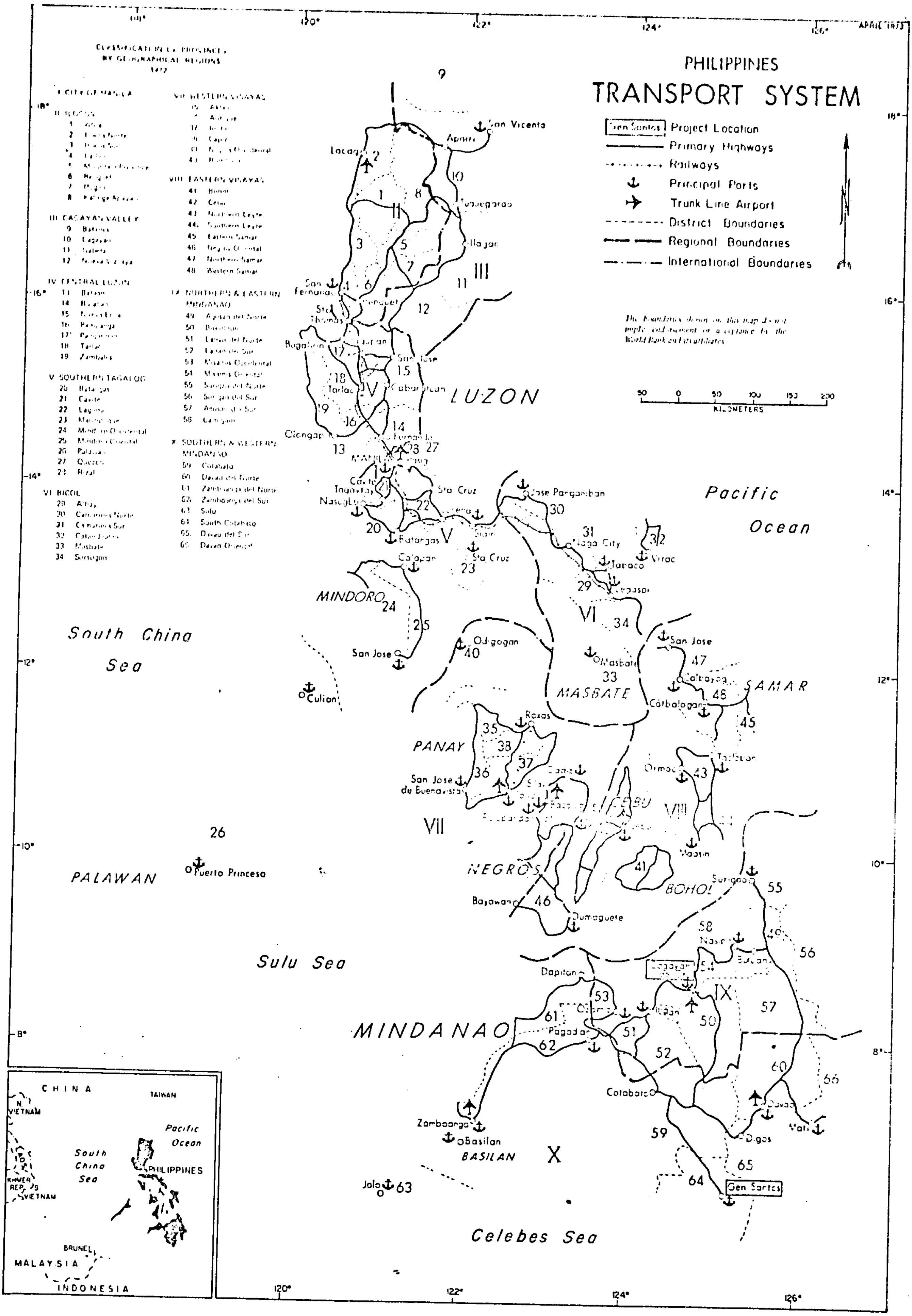
Region	1971 Population (mid-year) (million) A	%	Family Income (Pesos) Mean B	Median C	C/B (%)	Distribution of Bottom 40% of Families: No. of People (Millions) D	%	D/A (%)
Philippines - Total	37.92	100.0	3736	2454	65.7	15.17	100.0	40.0
Northern Luzon	3.39	8.9	2890	1741	60.2	1.87	12.4	55.2
Ilocos	1.87	4.9	3299	1813	55.0	0.98	6.5	52.4
Cagayan Valley	1.52	4.0	2390	1652	69.1	0.89	5.9	58.6
Central Luzon	6.68	17.6	4895	3556	72.7	1.61	10.6	24.1
City of Manila	1.40	3.7	7785	5202	66.8	0.10	0.6	7.1
Central Luzon	5.28	13.9	4127	3119	75.6	1.51	10.0	28.6
Southern Luzon	10.16	26.8	3868	2634	68.1	3.81	25.0	37.5
Southern Tagalog/a	7.12	18.8	4332	2960	68.3	2.25	14.7	31.6
Bicol	3.04	8.0	2784	1874	67.3	1.56	10.3	51.3
Visayas	9.38	24.8	2818	1930	68.5	4.68	30.9	49.9
Western Visayas	3.86	10.2	3206	2332	72.7	1.50	9.9	38.9
Eastern Visayas	5.52	14.6	2548	1651	64.8	3.18	21.0	57.6
Mindanao	8.31	21.[illegible]	3382	2411	71.3	3.20	21.1	38.5
NE Mindanao	3.14	8.3	3062	2186	71.4	1.36	9.0	43.3
SW Mindanao	5.17	13.6	3577	2549	71.3	1.84	12.1	35.6

Source: (a) Population - by interpolating 1970 Census data.

(b) Mijares, Tito A. and I. C. Belarmino, "Some Notes on the Sources of Income Disparities among Philippines Families," Journal of Philippine Statistics, Vol. 24, No. 4, 4th quarter 1973, P xv-xxii.

(c) Distribution of bottom 40 percent of families based on mission calculations using the 1971 household income-expenditure survey data.

/a Includes part of the Greater Manila Area.



PHILIPPINES
TRANSPORT SYSTEM
Gen Santos Project Location
Primary Highways
Railways
Principal Ports
Trunk Line Airport
District Boundaries
Regional Boundaries
International Boundaries
KILOMETERS
LUZON
MINDORO
MASBATE
SAMAR
PANAY
NEGROS
CEBU
BOHOL
PALAWAN
MINDANAO
BASILAN
South China Sea
Pacific Ocean
Sulu Sea
Celebes Sea
Lacag
San Vicente
Aparri
Tuguegarao
Ilagan
San Fernando
Sta. Thomas
Bugallon
San Jose
Cabanatuan
Tarlac
Olongapo
Manila
Sta Cruz
Nasugbu
Batangas
Calapan
Jose Panganiban
Naga City
Tabaco
Virac
Legaspi
Odiongan
San Jose
Masbate
Culion
Catbalogan
Calbayog
Roxas
Tacloban
Ormoc
San Jose de Buenavista
Maasin
Surigao
Bayawan
Dumaguete
Nasipit
Dapitan
Pagadian
Cotabato
Zamboanga
Basilan
Jolo
Davao
Digos
Mati
Gen Santos
Puerto Princesa
CHINA
TAIWAN
N. VIETNAM
KHMER REP.
S. VIETNAM
PHILIPPINES
MALAYSIA
BRUNEI
INDONESIA

Mitigating factors have precluded implementing the project in certain areas. The Cagayan Valley and Southwestern Mindanao have been excluded for reasons of peace and order. Combined, these two areas include approximately 14 percent of the bottom 40 percent. To assure that benefits of road development reach rural poor farmers and not large landowners, the project will not be implemented in the large sugar plantation areas. This will exclude another approximately 6 percent of the rural poor, most of whom are landless agriculture laborers and not farmers (tenant or owner).

The criteria for road selection include a requirement that any road to be developed must have an average of ten farms of three hectares or less within its influence area per kilometer. This will encompass many of those who are included in the bottom 40 percent of the income scale.

As discussed throughout this paper, a key objective of this project is the institutional development objective of developing local government capability to implement programs on a sustained basis over the long-term period required to eventually reach the rural poor at large. Vompletion of the proposed programs in the selected provinces will provide the base for expanded activity in each of these provinces - by the provincial governments themselves and with a substantially improved opportunity for the rural population themselves to influence project selection. In the long term, such afccus on the institutional base required is the only meaningful strategy for eventually reaching the target beneficiaries. In the same context - experience in the target provinces will provide a base from which these programs can be expanded to new provinces - thereby extending benefits to those areas currently excluded from this project.

Tab 3

Government Contribution to Rural Roads Program

As noted in Section I, the government has programmed 20,000 km of rural roads in the current four-year plan. To sustain such a program there will need to be a substantial transfer of resources from the central government to the provinces both for construction and maintenance.

The GDP has already taken a major step in this direction with the passage of Presidential Decree No. 17, amending the Philippines Highway Act of 1953.

This decree provides for, among other things, increasing the availability of maintenance funds by allocating 82% of the Highway Maintenance Fund (HSF) to national and provincial roads.

Under this revised act, the provincial governments, cities and municipalities will receive a direct annual maintenance contribution kilometer of roads and on a continuous basis. This action is probably more important in the long run than central government transfers for new construction. Without such assistance, the provincial road network would likely pose a rapidly expanding budget drain on the local areas and presage a return to the progressive deterioration of the provincial roads.

In the proposed project the central government will be contributing an estimated \$504,000 per year for maintenance of the roads constructed. This equates to \$10.1 million over the estimated 20 year life of these roads.

In addition to the maintenance contribution, the proposed loan is the first time the GOP has borrowed externally for, and directly transferred to the provincial governments a substantial block of resources for rural roads. Most notably in this case, this transfer of funds is for projects implemented by the provincial governments.

Since these funds will be transferred to the provinces on a grant basis, the central government will be shouldering 75 percent of the cost of the roads and correspondingly the foreign exchange risks and debt service obligations. The grant transfer (rather than a loan to the provinces approach practiced in other countries) makes sense in the Philippine context. The provinces will not be able to soon assume major debt service payments to the central government.

Increased taxes and other revenue resulting from road improvements will accrue to the provincial coffers and facilitate an expanded joint central government/provincial funded basis in the future. Provinces with greater financing capabilities will probably have to shoulder a larger percentage of costs in future programs, thereby providing a skewing of central government contributions to the lower income provinces.

In addition to the above aspects, the central government is expected to make a direct budgetary contribution of ₱7.0 million to the project to finance consulting engineering services.

Tab 4

4. Relationship to Agrarian Reform

There are approximately one million rice and corn tenant farmers in the Philippines tilling 1.8 million hectares of land. This is in addition to approximately 600,000 owner-tillers who are farming less than 2 hectares each.

In October 1972, the Government of the Philippines initiated an Agrarian Reform program which would transform the nation's rice and corn tenants into amortizing owners. These tenant farmers till an average of about 1.8 hectares. After making their share payments, they are left with little more grain than is required to feed their families until the next harvest.

The Philippine Agrarian Reform program is designed to do more than transform tenants into owners of the land they till. It seeks to provide these farmers with a support system to move them beyond subsistence. It is therefore a development program for small farmers rather than simply a land transfer program. The support system being developed is to provide farmers with production credit, extension services and access to inputs and markets.

The GOP land distribution program has been carried out in stages, beginning with estates esceeding 100 hectares. The program was then expanded to cover estates in the 50-100 hectares category and the 24 to 50 hectare category.

Progress was exceptional in the first year of the program with almost 15 percent of rice and corn tenants reported to have been made program beneficiaries. Progress in the second year was less impressive with less than an additional three percent of the tenants benefitting. The Government attributes the slow-down mainly to the emergence of resistance on the part of middle class landlords who are now subject to the reform effort as smaller hectarages have been brought under the program. Though this may be a major reason, it is also probable that the program tried to move too rapidly in the first and second years. Efforts have been delayed while bureaucratic and paper work bottlenecks of the first year have had to be unblocked. Significant progress has been made in developing more effective bureaucratic procedures and foreign observers feel that the delays will have been overcome by year's end.

More importantly perhaps, President Marcos is expected to reaffirm the will of the government to carry out this program. It is anticipated he will: (a) authorize the program to proceed from the 24-7 hectare level; (b) authorize the publication of program implementing regulations which have been designed to effectively deal with problems which slowed the program in the second year, and (c) will seek to overcome landlord opposition to the program by authorizing more liberal landlord compensation terms.

As stated above, the GOP intended the program to not be simply a land transfer program but that it be a program of small farmer development. Progress in developing a small farmer support system tailored to the needs of program beneficiaries has been very good. Non-collateral, small farmer loans have increased tenfold since the program's initiation and now exceed one-half billion Pesos. Credit is currently limited only by the capabilities of lending institutions to handle loans and not a shortage of funds. The government has developed a four-year Rural Bank Development Program which would, among other things, increase the number of rural banks by 50% (to a total of 1,000 institutions) and upgrade existing bank management capabilities to enable them to manage larger portfolios. The program seeks to make the rural banking system capable of meeting virtually all credit needs of the nation's small farmers within five years.

Progress in the farmer organization, the Samahang Nayon Program, which will form the base for an effective small farmer cooperative system, has also been exceptional. Almost 500,000 prospective land reform beneficiaries have been organized into barrio associations and have had over one year of training in such subjects as agricultural production, use of credit, cooperative principals, etc. These farmers will graduate from this comprehensive 64 week course by the end of December 1974, and will be encouraged to form themselves into multi-municipality marketing cooperatives. The government has, in the meantime, recruited and trained a cadre of professional cooperative managers to operate the prospective marketing cooperatives.

The farmer associations, although not yeat eligible to form themselves into cooperative, have assisted the banking community in loan distribution and collection, and assisted in the distribution of the farm inputs and assembling of produce for marketing.

As part of this program, the government has increased the number of agricultural extension agents to over four thousand. All have agricultural degrees and most have now been trained in the production of high yielding rice or corn varieties.

In addition to these services, the government has begun developing plans to see that program beneficiaries have access to irrigation and roads. All projections of costs of the agrarian reform program have included estimates of the cost of such new infrastructure and have identified this as an area where foreign assistance would be sought. The rural roads project presented here is being incorporated as an integral part of the overall Agrarian Reform Project.

In each participating province of this project, the Provincial Development Staff (PDS) will have primary responsibility for the preparation of an Annual Implementation Plan (AIP). In their capacity as the provincial planning staff, they are responsible for coordinating all local programs with the national activities in their particular provinces.

Agrarian Reform is a high priority program of the GOP that has some common goals with the rural roads program. The PBS, as a matter of course, closely coordinates provincial programs with the needs of the Agrarian Reform effort in their province. This local planning element permits the maximum utilization of rural inputs to serve the needs of the small farmers benefitting from the Agrarian Reform program.

Rural roads are one key to the success of this government initiative. Banks do not provide loans to farmers whom they can not supervise. Extension workers cannot spare the time required to visit isolated barrios. Where roads do not exist, fertilizer must be brought to the farm on inefficient draft-animal sleds and production surpluses brought to the market the same way. Thus, the economic margins of the farmer are squeezed between both increased input costs and increased marketing costs.

While the proposed loan will support the Agrarian Reform program, it will benefit all small farmers whether tenant or owner. The isolated farmer is more susceptible to risks than those with roads. Where roads exist, farmers have the option of machine tilling, threshing and drying. Without such access, planting may be delayed and crops harvested in rainy weather may deteriote before they can be processed.

Finally, the isolated farmer has little incentive to produce crops or animals beyond what his family can consume. His isolation gives him no access to marketing information and thus, he proceeds to the market ignorant of prices and is forced to either take what is offered or face the alternative of carrying his commodity back over the roadless fields to his farm.

In short, the small farmer beneficiary who has access to roads holds one of the crucial keys needed to develop his enterprise into something more than subsistence activity. The beneficiary without such access must continue to face the prospect of a hand-to-mouth existence.

Tab 5

5. Philippine Economic Situation and Debt Service Capacity

Recent Economic Developments

In the past two years there has been a sharp increase in the level of economic activity in the Philippines. The growth in real GNP, which had been about 5-6 percent a year for more than a decade, doubled to 10 percent in 1973, and is estimated to be about 7 percent this year. The strong recovery in 1973 was led by the international commodity boom and resultant increased export incomes in the Philippines by a strong recovery in agricultural and industrial production for the domestic market, and by an expansion in public and private investment. Underemployment and unemployment remain quite high, however, and in common with most other countries, the rate of inflation increased appreciably in the past 18 months.

The agricultural sector grew by 7 percent in 1973. Rice production in crop year 1973-74 increased by 23 percent over the level of the previous year when flood severely affected output. This increase has been mainly due to favorable weather conditions, increased use of fertilizers, more supervised credit and increased investments in supporting rural services. The Government has moved ahead with its program of agrarian reform for the nation's one million rice and corn farm tenants. By mid-1974, 176,000 land transfer certificates had been issued, mainly to tenants on the larger holdings. The Government now hopes to issue certificates to all tenants on farms above 24 hectares. There is a strong prima facie case for pressing ahead with the program in the 7-24 hectare farm size range. Implementation below the 7 hectare level will be extremely difficult and benefits less obvious, in view of the numerous owners and tenants and small parcels of land held.

The industrial sector grew by about 12 percent in 1973. Non-traditional industrial exports, which have been increasing since 1970, are estimated to have doubled in 1973 to about $200 million. However, industrial exports have been affected by the recent slowdown in the economics of key trading eartners, and earnings are expected to level off this year.

The growth in production was also assisted by increased public development outlays in 1973 made possible by a significant improvement in the financial position of the Government. The ratio of public investment to GNP is currently about 3 percent compared with 1.8 percent in FY '72. The Government has implemented a series of long needed tax reform and improvements in tax administration. As a result, the ratio of National and Local Government tax revenues to GNP has increased from an average of 9 percent in recent years to an estimated 12.4 percent in FY'74.

High prices for the Philippines' chief exports, including coconut products, sugar, copper and wood products, were largely responsible for an increase in merchandise receipts of almost 70 percent in 1973. International reserves rose by about $600 million during the year and stood at $876 million, equivalent to about five months of imports, at the end of the year. However, since mid-1974, a large trade deficit has appreared, largely because the growth in export prices has moderated but import prices have continued to rise rapidly. Because of the very rapid growth in export income in the past two years, and continued good debt management policies of the Government, the burden of medium and long-term debt has declined dramatically. The ratio of debt service payments to export receipts has come down to an estimated 15 percent this year, compared with a high of 27 percent in 1971.

In the latter part of 1973 inflation emerged as a major problem. Since mid-1973 consumer prices have been rising at an annual rate of more than 40 percent. This has been caused by the large increase in liquidity since the export boom began in 1973, and by a number of cost-push factors, including the higher rate of world inflation, domestic food shortages and the increased cost of petroleum. Monetary and fiscal policies have aimed at absorbing the excessive liquidity expansion, and in recent months the rate of inflation has been moderating.

The Energy Crisis

Imported petroleum provides some 97 percent of the Philippines' total energy requirements. In 1973 the equivalent of 71 million barrels of petroleum crude and petroleum products were imported at a cost of about $230 million c.i.f. When the energy crisis developed late last year, the Government moved quickly with conservation measures to reduce non-essential consumption. In 1974 imports of petroleum and products are likely to be about 71 million barrels at a cost of about $780 million c.i.f.

The Government has decided to accelerate the development of local energy sources, especially hydropower and geothermal energy. Supplemented with nuclear energy in the 1980's, total demand for energy is expected to grow at about 10 percent a year, and even with more rapid development of natural power sources, petroleum would still account for more than 90 percent of total energy needs by 1980.

Growth Prospects

The abrupt deterioration in the external terms of trade since the middle of 1974, and the recession in the economics of key trading partners threatens some of the Philippine' recent economic gains. The labor force continues to grow at 3 percent a year, and although employment has expanded appreciably in the past 18 months, there is still widespread unemployment and underemployment.

Priority is being given to expanding food production for the domestic market, to expanding export production and to accelerating development of local energy resources. In the case of export production, the Government recognizes that the increased cost of petroleum and other imports cannot be financed indefinitely by borrowing abroad. It is actively encouraging both local and foreign investors to expand the productive capacity of export industries and to undertake major new import-replacing investments. The Government is seeking increased support from the international financial community to help carry out its development program and to ease adjustment to higher petroleum and other import prices. Because of the substantial improvement in the external debt burden and international reserve position in the past 18 months, the Philippines now has the capacity to borrow externally larger amounts of capital in support of its development program.

Maintaining a GNP growth rate of about 7 percent a year in real terms during the next few years will depend heavily on the buoyancy of the domestic market. The prospects are for continued expansion in agriculture, with a 4-5 percent increase in production in the year ahead. Continued expansion in public and private investment demand should help sustain industrial output expansion. Increased investments will be needed in a wide range of consumer and intermediate goods industries.

The increased size of the domestic market and growing export demand would seem to justify a wider range of investments during the latter part of the decade in large-scale, capital-intensive industrial projects, particularly in meneral-based processing industries where long-term comparative advantage may be strong. A number of big projects are proposed in mining, wood processing, fertilizer, steel and shipbuilding, which are likely to push up the private investment rate from recent levels of about 16 percent of GNP to perhaps 22 percent by the latter part of the decade. A substantial amount of the funds needed for these projects would have to come from external sources. But since the individual cost of many of them will exceed $100 million, Consultative Group members can play an important role in helping the Government to obtain suitable co-financing arrangements, both with bilateral partners and with the private sector.

The public infrastructure program that was approved last year, which called foroutlays of about P12 billion at current prices in FY '74-77, has become outdated because of the subsequent rapid inflation and by changes in investment priorities as arresult of the energy crisis. A new program is being finalized, with more emphasis on developing nuclear and indigenous power resources and on irrigation, feeder roads and other projects to support increased food and export production. Public investment is likely to increase by about 15 percent a year in real terms so the ratio of public investment to GNP would rise from the present level of 3 percent to about 4 percent by 1977.

The domestic savings rate should rise from an estimated 19 percent of GNP at present to perhaps 20.5 percent by 1977. Foreign savings (i.e., the current account deficit in the balance of payments) would rise from an estimated 2.5 percent of GNP this year to about 4 percent in 1977. This foreign savings gap would decline in the latter part of the decade as the proposed investments in new export and import-replacing capacity begin to bring results.

Balance of Payments

Merchandise export receipts are projected to increase by a total of about 30 percent in the next two years. Import payments are projected to increase by a total of almost 40 percent in the same period, including a 30 percent increase in prices. Under these assumptions, the trade deficit would rise from an estimated $680 million this year to about $1,250 million in 1976.

Although exports are projected to grow more rapidly than imports in real terms over the next two years, this gain is more than offset by a cumulative decline in the external terms of trade of about 23 percent during 1975 and 1976. This would bring the terms of trade back to the level that prevailed in 1972, thus wiping out the gains made in the recent export price boom.

External Finance

If the projections of exports, imports and external terms of trade were to be realized, the Philippines would require a total foreign capital inflow of about $2,340 million during 1975 and 1976 to cover the current account deficit and medium and long-term loan repayments.

Direct investment would provide about $190 million of this. Greater use of short-term trade finance is expected because of the increased oil import bill and generally higher levels of imports. A net inflow of about $480 million would be in line with the increase in the value of trade being financed. About $1,080 million could be expected from supplier's credits and other medium and long-term loans to the private and public sector, including about $280 million from project loans extended by Consultative Group members. The balance of the required capital inflow of about $180 million in 1975 and $410 million in 1976 would have to come from other borrowings. The Central Bank could finance the entire deficit by short and medium-term borrowing while maintaining or even increasing the level of international reserves. Net reserves, however, would be negligible by 1976.

The recent important gains in reducing the external debt burden and improving the external reserve position should not be lost now by excessive recourse to short and medium-term borrowing by the banking system. In these circumstances, foreign donors should consider extending quick-disbursing commodity loans with long maturities. Some assistance may also be forthcoming from the IMF.

With a combination of quick-disbursing commodity aid from Consultative Group members and assistance from the IMF, foreign exchange availabilities would be sufficient for import requirements in 1975, while at the same time maintaining a reasonable external debt profile. The much larger shortfall in foreign exchange availabilities projected for 1976 would have to be met with an appropriate combination of long and medium-term loan funds to prevent an undue increase in the debt burden in later years. Quick disbursing commodity aid on suitably long-term would again be needed. However, there is considerable scope for additional medium and long-term loans from donors to finance capital goods imports which are projected to reach $1.2 billion in 1976. In the months ahead, the Government and aid donors alike should explore this possibility. If these efforts are unsuccessful, the Government would have to reassess its growth strategy for 1976.

If the projected inflows on the capital account are forthcoming, and if the presently identified shortfalls in foreign exchange availabilities are met with an appropriate combination of medium and long-term loan capital as suggested, mamangement of the external debt and debt servicing should not present serious problems.

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MEMORANDUM

TO: PPC/DPR, Mr. Arthur M. Handly

FROM: Acting DAA/EA, Norman L. Sweet

SUBJECT: Notification of Clearances and Request for DLSC Consideration

Please be advised that the attached loan proposal has been cleared by the A/DAA/EA as well as the other offices noted, and it is requested that it be distributed to the Development Loan Committee by November 20 and be considered at a meeting of the Development Loan Staff Committee by November 25.

LOAN NAME: Philippines - Rural Roads Loan

AMOUNT: $15.0 million

Members of the Regional Review Committee:

1. A/DAA/EA, Norman L. Sweet
2. EA/CCD, Norman Cohen
3. EA/EAA, S. J. Littlefield
4. GC/EA, Herbert E. Morris
5. EA/PPB, Lawrence A. Marinelli

The following offices of A.I.D. received the Loan Paper and the noted representatives attended the Regional Loan Review on November 13, 1974:

SER/ENGR/EA: Clarence Groceman
PPC/DPRE: J. Shannon
GC/EA: Stephen Tisa
EA/DP: Walter Sherwin

Indicated below are the only unresolved issues they raised: None

Issues, if any, which may be raised by outside agencies. None

Attachment
Loan Proposal

EA/CCD:LBond:is (11/18/74)

Clearances: EA/CCD:FCollins, Jr.__________
EA/CCD:NCohen__________
EA/Loan Div. ALove__________

November 18, 1974

MEMORANDUM

TO: Acting DAA/EA, Mr. Norman Sweet

FROM: EA/CCD, Frank Collins, Jr.

SUBJECT: Philippines Rural Road Loan Project

PROBLEM

The Philippine Rural Roads Loan CAP for $15.0 million was reviewed at the East Asia Project Advisory Committee (EAPAC) Meeting on November 13. At the meeting, a number of issues were raised by you and various participants. These questions have now been reviewed by the Project Committee. Where required, changes have been made to the Capital Assistance Paper to address the issues raised.

Based on the revisions to the paper and other comments noted in this memorandum, the Project Committee recommends you concur in submission of the Project Paper to PPC for a DLSC review and subsequent authorization by the Deputy Administrator.

DISCUSSION

1. PPC questions posed by M. J. Heyl Memorandum of November 13.

A number of questions relating to the proposed project were set forth in Mary Jane's memorandum. These were discussed at the EAPAC and written comments have been prepared to these questions (see Tab 1 for questions and response).

2. Philippine Economic Position, Justification of AID Assistahce and Concessionary Terms.

It was noted at the review that the GOP has Foreign Exchange reserves of $1.2 billion. The question was posed as to whether there was continued justification for AID assistance and concessional lending terms in view of this position.

The determination to provide AID Development Loan assistance to the GOP at a $35 million level was made on the basis of the FY 1975 FBS review chaired by the old Asia Bureau. This decision was subsequently confirmed in the Agency's submission to OMB and the project is identified in the FY 75 Congressional Presentation.

We have reviewed the most current economic report on the Philippines (IBRD Nov. 7). As noted in the report, the international reserves as of June were approximately 1.3 billion (net reserves of $385 million). This reserve position reflects the recent, but short term, boom in export prices of Philippine commodities which contributed to an increase in reserves of $600 million in 1973. Since mid-1974 a large trade deficit has appeared reflecting a decline in external terms of trade. The IBRD estimates a decline of 23% in the terms of trade over the balance of 75 and through 1976. Gross reserves have dropped by $100 million since June. Additional trade deficits are estimated at $600 million in 1975 and $1,250 in 1976. Net reserves may therefore be negligible by the end of 1976.

Given the above shift in the Philippine economic picture, the Project Committee sees no basis for reversing the earlier decision to proceed with $35 million of DL to the Philippines this year, including the proposed Rural Roads project.

The economic section of the loan paper has been revised to include an updated summary of the economic situation as extracted from the IBRD report. (Tab 2).

With respect to the question of concessional terms of assistance, we feel the deterioration in the Philippine economic picture would argue in any event for continued concessional terms of assistance to the GOP. Beyond this consideration however, the Agency still has a policy of maintaining loan terms at the concessional level. While this policy is under review, current practice does not provide for intermediate terms. The Agency has traditionally handled the question of an improved Balance of Payments picture by dropping the level of assistance rather than hardening the terms.

3. Selection of AID vs. Other Donors

The question was posed at the review whether AID is the appropriate lender for this project, rather than other donors.

The GOP has approached AID for assistance in this project for a number of reasons.

(a) AID has direct experience with rural road projects and a close working relationship with the provincial governments.

(b) The GOP has, as noted in the CAP, encouraged the other donors (IBRD, ADB, Japanese, etc.) to assist in major highway and related transportation projects. The GOP prefers to utilize the funds of the other donors in those areas where AID's new priorities preclude participation.

(c) The proposed project does fall within AID's priorities.

4. Institutional Development Aspects

A question was posed as to whether the project was not in fact simply a capital transfer with little institutional development included.

The major thrust of the proposed project is in fact institutional development. The $15.0 million loan will be spread over 22 provinces.with the average contribution per province being $680,000. Since the program will be administered by the Provincial governments, we expect the project to result in an improved local institutional base capable of selecting, designing, constructing, maintaining and evaluating rural roads programs. Included in this program will be introduction to the Provincial Governments (for the first time) of detailed economic analysis of road projects. This will help avoid the traditional choice of projects by ad hoc methods and overriding political factors as a major consideration.

It should be noted that the 750 km undertaken under this loan is only a small portion of the planned 20,000 km or rural roads investments contained in the current four year plan. The institutional development aspects of this project, therefore, are critical in the process of assisting the GOP to meet this longer term need by increasing substantially the capacity at the provincial level.

5. Beneficiaries

The question was posed as to whether rural roads projects in general, and this project in particular, meet AID's new mandate to reach the poorest majority.

The PPC representative indicated, and subsequent discussions with PPC have confirmed, that rural road projects are considered to be responsive to AID's new directives (each project must of course justify this conclusion in the country context).

As we indicated at the review, the proposed loan concentrates its activities in provinces where a large portion of the "poor majority" of the Filipinos reside. The proposed project will directly reach a percentage of these people with the specific roads constructed under this loan. How many will be directly affected we do not know. However, this will be evaluated and the data fed back into the provincial planning mechanism. Most importantly - the institutional development achieved at the provincial levels will provide the basis for a sustained GOP program to eventually provide adequate transport facilities to the population throughout these provinces.

We have added a new section of the CAP with a break out of the location of the lower 40% income bracket in the Philippines. We feel the rural roads are satisfactorily distributed through the low income areas, particularly given our other constraints e.g. inability to operate in the Muslim areas of S.W. Mindinao due to the fighting, in the Cagayan Valley (due to NPA activities) and our in house decision to exclude portions of the sugar bloc areas. (See Tab 3).

6. Central Government Contribution to the Project

In response to PPC's request, the paper has been revised to more clearly set forth the role of the Central Government in contributing to the financial requirements of this and future rural roads programs. (See Tab 4).

7. Economic Return

At the meeting, the question of the minimum economic return was raised. The 15% floor internal rate of return for qualifying projects was set by the Philippine Government. Since this rate is a "floor" rate, actual returns will vary above this base. We feel the 15% base rate is appropriate particularly for these rural roads type projects. Moreover, we did suggest to the GOP that consideration be given to lowering the rate ofor the penetration road sub-project where social and economic benefits are much harder to estimate, where the costs per km of road are much lower, and where the direct impact on the poor farmer will be the greatest. We still believe this to be desirable. Primary emphasis on the economic return as a selection factor will, we fear, skew sub-project selection toward projects with road used benefits rather than penetration road benefits. Such a skewing will increase the overall economic return of the road program, but to the detriment of projects providing direct economic and social benefits to the poor farmers in the inaccessible areas.

8. Project and Program Priorities

With respect to the question of "why this project", and how does it relate to sector strategy, GOP priorities, AID priorities, etc., we have expanded the initial section of the loan paper to more fully address this question.

Selection of the rural roads program was based on a review of the IBRD Ag Sector Survey (1973), the IBRD Transportation Sector Analysis (1973 Economic Report) and a joint IBRD/UNDP study on the transport sector.

The proposed rural roads project addresses a gap in the priority requirements for assistance to the combined agricultural/transportation sectors. This project, as do most of the USAID/Philippine program activities, focuses on the rural or "downstream" end where the other donors are not yet fully active. Related priority projects in the Agricultural Sector are being addressed by AID, including: (1) Agriculture Research, a $5.0 million project which is nearing the PRP stage; (2) Irrigation, a $3.0 million small scale irrigation pilot project which is at the PID stage and working to be completed in FY 75; (3) Integrated Area Development Program, under development in the Bicol (one of the lowest income areas in the Philippines) and directed toward developing a coordinated input of all agriculture sector requirements in a concentrated geographical area; and (4) Supporting Grant Projects in Agrarian Reform and Small Farmer Income and Production which are also under implementation.

In summary, we think this project does reflect consideration of supporting agriculture and transport sector analysis, meets both GOP and AID priorities and complements other donor programs and other AID programs.

9. Exploitation of the Farmer

You expressed concern about the prospects that improved rural roads and resulting increased access to the rural areas would open the rural farmer to potential exploitation.

We feel the most important factor affecting exploitation or non exploitation of the farmer is the central government's attitude toward assisting the rural poor. All evidence indicates that the Philippine government views support by the rural population as a key factor affecting the political stability of the country. Correspondingly the government is both (1) attempting to improve the honesty and efficiency of its administration in the rural areas and (2) Marshalling a coordinated package of assistance programs specifically focused on assistance to the rural population.

Once the roads are completed they will be available to all elements of the population. Some local incidences of exploitation will undoubtedly occur. Given the favorable central government attitudes however, we feel confident that the benefits to the rural population will far outweigh any incidences of mususe due to improved rural access.

10. Agrarian Reform

Because of the interest in the current status of the agrarian reform program, we have included an expanded discussion of this aspect in the CAP text (See Tab 5).

The Project Committee believes that the proposed rural roads program and the other aspects of the GOP agrarian reform effort are being reasonably well coordinated.

11. Loan Authorization

The loan authorization has been expanded per GC's suggestion to include major covenants and conditions precedent.

Recommendation

That you sign the attached memorandum to PPC requesting a DLSC meeting to consider this project.

EA/CCD:ARLove:mk

Clearances:
ASIA/EA:SJLittlefield (draft)
ASIA/EA:DChandler (subs)
USAID/Manila/ALCD:RDangler (draft)
GC/EA:HMorris ______________
EA/CCD:NCohen (draft)
EA/CCD:LBond (draft)

Attachments:
1. Tab 1
2. Tab 2
3. Tab 3
4. Tab 4
5. Tab 5
6. Memorandum to PPC/DPR, Mr. Arthur M. Handly

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265
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A. I. D. Loan No. 492-T-035

PD-AAV-549

4920272

29p.

LOAN AGREEMENT

(PHILIPPINES: Rural Roads Project)

Between the

REPUBLIC OF THE PHILIPPINES

and the

UNITED STATES OF AMERICA

Date: March 24, 1975

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LOAN AGREEMENT

LOAN AGREEMENT, dated the 24th day of March, 1975 between the GOVERNMENT OF THE REPUBLIC OF THE PHILIPPINES (hereinafter called the "Borrower"), acting through the NATIONAL ECONOMIC AND DEVELOPMENT AUTHORITY, and the UNITED STATES OF AMERICA, acting through the AGENCY FOR INTERNATIONAL DEVELOPMENT (hereinafter called "A.I.D.").

ARTICLE I

The Loan

SECTION 1.01. The Loan. A.I.D. hereby agrees to lend to the Borrower, pursuant to the Foreign Assistance Act of 1961, as amended, an amount not to exceed Fifteen Million United States Dollars ($15,000,000), ("Loan") to be used exclusively to reimburse the Borrower for up to 75% of the reasonable local currency costs of Part B of the Project as defined in Section 1.02 hereof using the reimbursement procedures specified in Article V. The aggregate amount of disbursement under the Loan is hereinafter referred to as "Principal".

SECTION 1.02. Project. The Project shall consist of (a) the development of the institutional capability of Participating Provinces by providing these entities the responsibility for identifying, planning, implementing and evaluating subprojects using Borrower resources and the institutional capability of the Department of Local Government and Community Development (DLGCD) by providing DLGCD the opportunity to coordinate and implement the Project on behalf of the Borrower; and (b) the construction and/or improvement of feeder and penetration roads and of bridges in rural areas.

ARTICLE II

Borrower Repayment Terms and Interest

SECTION 2.01. Interest. The Borrower shall pay to A.I.D. interest, which shall accrue at the rate of two percent (2%) per annum for ten years following the date of the first disbursement hereunder and at the rate of three percent (3%) per annum thereafter, on the outstanding balance of Principal and on any due and unpaid interest. Interest on the outstanding balance shall accrue from the date of each respective disbursement (as such date is defined in Section 5.04) and shall be computed on the basis of a 365-day year. Interest shall be payable semi-annually. The first payment of interest shall be due and payable no later than six (6) months after the first disbursement hereunder, on a date to be specified by A.I.D.

SECTION 2.02. Principal. The Borrower shall repay the Principal to A.I.D. within forty (40) years from the date of the first disbursement hereunder in sixty-one (61) approximately equal semiannual installments. The first installment of Principal shall be payable nine and one-half (9-1/2) years after the date on which the first interest payment is due in accordance with Section 2.01. Upon completion of disbursements, A.I.D. will furnish the Borrower with an amortization schedule in accordance with this Section.

SECTION 2.03. pplication, Currency and Place of Payment. All payments of interest and Principal hereunder shall be made in United States dollars and shall be applied first to the payment of any interest due and unpaid and then to the repayment of Principal. Except as A.I.D. may otherwise specify in writing, all such payments shall be made to the Controller, United States Agency for International Development, Washington, D.C., U.S.A. and shall be deemed made when received by the Office of the Controller.

SECTION 2.04. Prepayment. Upon payment of all interest and refunds then due, the Borrower may prepay, without penalty, all or any part of the Principal. Any such prepayment shall be applied to the installments of Principal in the inverse order of their maturity.

SECTION 2.05. Renegotiation of the Terms of the Loan. The Borrower agrees to negotiate with A.I.D., at such time or times as A.I.D. may request, an acceleration of the repayment of the Loan in the event that there is any significant improvement in the internal and external economic and financial position and prospects of the country of the Borrower.

ARTICLE III

Conditions Precedent

SECTION 3.01. Conditions Precedent to Commencement of the First Subproject. Prior to the commencement of the first subproject under this Project, the Borrower shall, except as A.I.D. shall otherwise agree in writing, furnish to A.I.D. in form and substance satisfactory to A.I.D.:

(a) An opinion of the Secretary of Justice of the Borrower, or of other counsel acceptable to A.I.D., that this Loan Agreement has been duly authorized and/or ratified by, and executed on behalf of, the Borrower and that it constitutes a valid and legally binding obligation of the Borrower in accordance with all of its terms.

(b) A statement of the names of the persons holding or acting in the office of the Borrower specified in Section 9.1 (b), together with evidence of their authority and a specimen signature of each such person certified as to its authenticity by either the person rendering the legal opinion pursuant to Section 3.01 (a) or the person executing this Loan Agreement.

(c) Written assurance by the Borrower that sufficient funds will be made available to DLGCD for the purpose of promptly reimbursing a Participating Province in accordance with the terms of this Loan Agreement.

(d) A copy of an executed contract or contracts, financed by DLGCD, with a firm or firms satisfactory to A.I.D. to perform engineering services for the Project including review and monitoring of subproject planning and implementation by Participating Provinces and certification of completion of subprojects in accordance with agreed plans and specifications.

(e) A standard form Project Implementation Agreement the terms of which shall include the requirements set forth in Article IV, Sections 4.01, 4.02, 4.03 and 4.04 of this Loan Agreement. The standard form Project Implementation Agreement shall not thereafter be materially amended or modified without the prior written concurrence of A.I.D.

(f) A three-year implementation plan for the Project prepared by DLGCD, including a projection of funds available to finance the contract or contracts with a firm or firms to provide engineering services as described in subsection (d) above.

(g) Written assurances from the Borrower that all roads and bridges improved or constructed under this Project will be classified as

Provincial Roads and therefore eligible for annual maintenance funds as specified in Presidential Decrees 17 and 320 and that such funds will be provided in accordance with such Presidential Decrees.

SECTION 3.02. Terminal Date for Meeting Conditions Precedent. Except as A.I.D. may otherwise agree in writing, if the conditions specified in Section 3.01 are not met within 120 days, from the date of this Agreement, A.I.D., at its option, may terminate this Agreement by giving written notice to the Borrower.

SECTION 3.03. Notification of Meeting Conditions Precedent. A.I.D. shall notify the Borrower upon determination by A.I.D. that the conditions precedent specified in Section 3.01 have been met.

ARTICLE IV

Subproject Implementation and Financing

SECTION 4.01. Execution of Implementation Agreements, Subproject Identification, Planning and Acceptance for Financing. The standard form project implementation agreement shall be executed by the Province and DLGCD, and be in full force and effect, prior to the commencement of the first subproject in the Province. Prior to the commencement of each subproject, the Borrower shall, except as A.I.D. otherwise agrees in writing, assure the following:

(a) The subproject has been identified by the Participating Province in accordance with eligibility criteria set forth in Implementation Letters.

(b) Technical soundness appraisals were performed, and plans, specifications, cost estimates and, where appropriate, economic analyses and feasibility studies were developed, by the Participating Province, in accordance with procedures set forth in Implementation Letters.

(c) The analyses, plans, specifications, cost estimates and feasibility studies prepared under subsection (b) were submitted, promptly upon preparation, to DLGCD and A. I. D. for review and approval. Approval by A. I. D. may, at its option, be based solely upon the recommendation of DLGCD and concurrence of the engineering firm mentioned in Section 3. 01 (d). (Plans and specifications approved by A. I. D. shall hereinafter be referred to as the "agreed plans and specifications".)

(d) The agreed amount (the amount of the loan proceeds that will be available for reimbursement upon completion of the subproject in accordance with agreed plans and specifications) has been established by DLGCD and A. I. D. The agreed amount shall not exceed seventy-five percent (75%) of the estimated cost of the subproject. Items that may be included in the estimated cost of a subproject ("Eligible Items"), on which the agreed amount will be based, will be described in Implementation Letters. Such estimated cost shall not include, however, taxes imposed specifically and explicitly on Eligible Items.

(e) Except as A.I.D. may otherwise agree in writing, the Borrower shall assure that all contracts, irrespective of amount, and all firms selected to perform such contracts, are, prior to execution, submitted to A.I.D. for written approval, if such contracts are for goods or services for a subproject and the agreed amount for such subproject is the peso equivalent of in excess of $100,000 or such subproject is one of a group of subprojects which are so interrelated that, upon completion, such subprojects result in a specific, self contained undertaking and the aggregate agreed amount for such group of subprojects is the peso equivalent of in excess of $100,000.

SECTION 4.02. Subproject Implementation. The Borrower shall assure that the Participating Province shall finance and execute the subproject in accordance with agreed plans and specifications, and the terms of this Loan Agreement.

SECTION 4.03. Procurement.

(a) Unless the prior written approval of A.I.D. to the contrary is obtained, all goods and services procured for the Project shall have their source and origin in the Republic of the Philippines, as further defined in Implementation Letters. Goods and services procured from a source other than the Republic of the Philippines, upon receipt of the approval of A. I. D., shall have their source and origin in countries included in A. I. D. Geographic Code 941.

(b) Except as A. I. D. may otherwise agree in writing, no subproject commenced prior to the date of this Loan Agreement shall be eligible for reimbursement by A. I. D.

(c) No more than reasonable prices will be used in determining estimated subproject costs for any goods or services financed on a fixed amount reimbursable basis, in whole or in part, under the Loan. Such items shall be procured on a fair and, except for professional contract services, on a cost competitive basis wherever practicable.

SECTION 4.04. Reimbursement by Borrower through DLGCD. The Borrower through DLGCD shall promptly reimburse a Participating Province the agreed amount, on a grant basis, upon determining, with the concurrence of the engineering firm, that the subproject has been completed in accordance with agreed plans and specifications and the terms of this Loan Agreement and of the Project implementation agree-ment.

SECTION 4.05. Reimbursement by A. I. D.

(a) Except as A. I. D. may otherwise agree in writing, prior to A. I. D. issuing Special Letter(s) of Credit (defined in Section 5.01) for reimbursement of the agreed amount for each completed subproject, the completed subproject must be accepted by A.I.D. Prior to acceptance of a completed subproject by A.I.D., the Borrower shall furnish A.I.D. the following in form and substance satisfactory to A.I.D.:

(i) Certification by the Participating Province, approved by the engineering firm, that the subproject for which reimbursement is requested has been completed in accordance with agreed plans and specifications;

(ii) Certification by DLGCD that it has reimbursed the Participating Province, on a grant basis, for the agreed amount with respect to the completed subproject;

(iii) Certification by DLGCD that all goods and services for the subproject had their source and origin in the Republic of the Philippines, or that approval of A.I.D. was obtained, pursuant to Section 4.03, prior to the procurement of goods or services for the subproject from another source and that the conditions attached to such approval have been satisfied;

(iv) Such other documents as may be described in Implementation Letters issued pursuant to Section 9.02 of this Loan Agreement.

(b) Prior to acceptance by A.I.D. of a completed subproject for reimbursement, A.I.D. may, at its option, inspect the subproject within 30 days of DLGCD's final acceptance to determine whether such subproject has been completed in accordance with agreed plans and specifications, the project implementation agreement and this Loan Agreement.

ARTICLE V

Disbursements

SECTION 5.01. Reimbursement for Local Currency Costs.

(a) After acceptance by A.I.D. of each completed subproject in accordance with Section 4.05 of this Loan Agreement, the Borrower may obtain reimbursement by A.I.D. for such subproject by submitting requests to A.I.D. for the issuance of Irrevocable Special Letters of Credit ("SLC"), by one or more banks in the United States designated by the Borrower and satisfactory to A.I.D., to the Borrower or any designee of the Borrower pursuant to such documentation requirements as A.I.D. may prescribe in the SLCs and Implementation Letters. Such documentation shall include, among other things, evidence of Philippine general commodity imports from the United States of equal value to the dollars requested for disbursement excluding freight charges on all but U.S.-flag vessels. Banking charges incurred pursuant to this Section in connection with commitment documents and disbursements shall be for the account of the Borrower and if requested, may be financed hereunder.

(b) The rate of exchange that shall be used in determining the amount of dollars to be made available shall be the selling rate for U.S. dollars set by the Central Bank of the Philippines on the date of acknowledgement of receipt by USAID/Manila of an application for reimbursement, by the Borrower. Taxes, fees, commissions, and similar charges, if any, are not included in determining the appropriate exchange rate.

SECTION 5.02. Other Forms of Disbursement. Disbursements may also be made through such other means as the Borrower and A.I.D. may agree to in writing.

SECTION 5.03. Terminal Date for Requests for Reimbursement and for Disbursements. Except as A.I.D. may otherwise agree in writing, no reimbursement as defined in this Article, shall be made in response to requests for reimbursement received by A.I.D. after forty (40) months from the date of execution of this Loan Agreement. A SLC, however, will remain available for drawdown for up to three years following the last upward adjustment in its face amount. After that time A.I.D may at its option terminate it and apply any realized funds to a reduction in the outstanding Principal.

SECTION 5.04. Date of Disbursement. Disbursements by A.I.D. shall be deemed to occur on the date on which A.I.D. opens or amends the SLC referred to in Section 5.01.

ARTICLE VI

Particular Covenants and Warranties

SECTION 6.01. Implementing Agency. Except as A.I.D. may otherwise agree in writing, the Project shall be implemented on behalf of the Borrower by DLGCD.

SECTION 6.02. Project Implementation Agreement. The Borrower through DLGCD shall assure that each subproject shall be implemented by each Participating Province in accordance with the project implementation agreement executed by DLGCD and such Participating Province pursuant to Section 3.01 (e) of this Loan Agreement and that all other terms and conditions of such project implementation agreement are observed by the parties thereto.

SECTION 6.03. Project Evaluation Procedures. The Borrower through DLGCD shall assure that the Project Evaluation Procedures described in Implementation Letters are effected.

ARTICLE VII

General Covenants and Warranties

SECTION 7.01. Execution of the Project.

(a) The Borrower shall carry out the Project, and cause all subprojects to be carried out, with due diligence and efficiency and in conformity with sound engineering, construction, financial, administrative and management practices.

(b) The Borrower shall cause the Project, including all subprojects, to be carried out in conformity with all plans, specifications, contracts, schedules and other arrangements, and with all modifications therein, approved by A. I. D. pursuant to this Agreement.

SECTION 7.02. Funds and Other Resources to be Provided by Borrower. The Borrower shall provide, or cause to be provided by Participating Provinces, promptly as needed all funds, in addition to the Loan, and all other resources required for the punctual and effective carrying out, maintenance and repair of the Project and each subproject.

SECTION 7.03. Operation and Maintenance. The Borrower shall assure that each subproject comprising the Project is adequately maintained, repaired and operated in accordance with sound engineering, construction, financial, administrative and management practices and in such manner as to insure the continuing and successful achievement of the purposes of the Project and each subproject.

SECTION 7.04. Management. The Borrower shall provide for the Project, and cause each Participating Province to provide with respect to each subproject, qualified and experienced management and training for such staff as may be appropriate for the maintenance and operation of the Project and subprojects.

SECTION 7.05. Utilization of Eligible Items. Except as A.I.D. may otherwise agree in writing, all Eligible Items shall be used exclusively in carrying out the Project. This restriction shall apply only until such time as such goods can no longer be usefully employed for the Project, provided that no goods financed hereunder shall be exported from the Republic of the Philippines without the prior written approval of A.I.D., and provided further that no Eligible Items shall at any time be used to promote or assist any project or activity associated with or financed by any country not included in Code 935 of the A.I.D. Geographic Code Book as in effect at the time of such projected use except with the prior written consent of A.I.D.

SECTION 7.06. Information and Marking. The Borrower shall give publicity to the Loan provided for herein and the Project as a program of United States aid, and shall cause subproject sites financed under the Loan to be identified as prescribed in Implementation Letters.

SECTION 7.07. Notice of Material Developments. The Borrower represents and warrants that all facts and circumstances that it has disclosed or course to be disclosed to A.I.D. in the cause of obtaining the Loan are accurate and complete, and that it has disclosed to A.I.D., accurately and completely, all facts and circumstances which may materially affect the Project or the discharge of its obligations under this Loan Agreement, and shall inform A.I.D. of any conditions which may constitute a default hereunder or which interfere, or which it is reasonable to believe may interfere, with the Project or any subproject or with the discharge of any of its obligations hereunder.

SECTION 7.08. Inspections. Irrespective of whether A.I.D. exercises its right to inspect a completed subproject prior to acceptance under Section 4.05 (b) of this Agreement, the authorized representatives of A.I.D. shall have the right at all reasonable times, whether prior to completion of the Project or any subproject or subsequent thereto, to inspect the Project, the subprojects, the books and records referred to in Section 7.11 and any other documents, correspondence, memoranda, or records relating to the Loan provided for herein or to the Project or any subproject. The Borrower shall cooperate with A.I.D. to facilitate such inspections and shall afford a reasonable opportunity for authorized representatives of A.I.D. to visit any part of the Republic of the Philippines for any purpose related to the oan provided for herein.

SECTION 7.09. Taxes. The Borrower covenants and agrees that this Loan Agreement shall be free from, and the Principal and interest shall be paid to A.I.D. without deduction for and free from, any taxation or fees imposed under any laws or decrees in effect within the Republic of the Philippines, or that any such taxes or fees so imposed or payable shall be reimbursed by the Borrower.

SECTION 7.10. Commissions, Fees and Other Payments.

(a) The Borrower warrants and covenants that in connection with obtaining the Loan provided for herein, or taking any action under or with respect to this Loan Agreement, it has not paid, and will not pay or agree to pay, nor to the best of its knowledge has there been paid or will there be paid or agreed to be paid by any other person or entity, commissions, fees or other payments of any kind, except as regular compensation to the Borrower's or Participating Provinces' full-time officers and employees or as compensation for bona fide professional, technical or other comparable services. The Borrower shall promptly inform A.I.D. of any payment or agreement to pay for such bona fide professional, technical or comparable services to which it is a party or of which it has knowledge (indicating whether such payment has been made or is to be made on a contingent basis), and if the amount of any such payment is deemed unreasonable by A.I.D., the party concerned shall cause a reduction satisfactory to A.I.D. to be made therein.

(b) The Borrower warrants and covenants that no payments have been or will be received by the Borrower or any Participating Province, or any official of the Borrower or Participating Provinces, in connection with the procurement of goods and services for subprojects, except fees, taxes or similar payments legally established in the country of the Borrower.

SECTION 7.11. Maintenance and Audit of Records. The Borrower shall maintain, or cause the Participating Provinces to maintain books and records relating to the Project, the subprojects and to this Loan Agreement as A.I.D. shall subsequently set forth in Implementation Letters. Such records shall be maintained for a period of five (5) years after the date of last disbursement by A.I.D.; or until all sums due A.I.D. under the Loan Agreement have been paid, whichever shall first occur.

SECTION 7.12. Reports. The Borrower shall furnish A.I.D. such information and reports relating to the Project, the subprojects, Eligible Items, and the Loan provided for herein as A.I.D. may reasonably request.

SECTION 7.13. Continuing Consultation. The Borrower, Participating Provinces and A.I.D. shall cooperate fully to assure that the purpose of the Loan will be accomplished. To this end, the Borrower, Participating Provinces and A.I.D. shall from time to time, at the request of any party, exchange views through their representatives with regard to the progress of the Project and subprojects, the performance by the Borrower of its obligations under this Agreement, the performance by the Participating Provinces under project implementation agreements, the performance of the consultants, contractors, and suppliers engaged on the Project, and other matters relating to the Project.

ARTICLE VIII

Cancellation and Suspension

SECTION 8.01. Cancellation by the Borrower. The Borrower may, with the prior written consent of A.I.D., by written notice to A.I.D., cancel any part of the Loan which, prior to the giving of such notice, A.I.D. has not disbursed or committed itself to disburse.

SECTION 8.02. Events of Default; Acceleration. If any one or more of the following events ("Events of Default") shall occur:

(a) The Borrower shall fail to pay in full any interest payment or installment of Principal required under this Agreement when the same shall become payable by it;

(b) The Borrower shall fail to comply with any other provision contained herein;

(c) Any representation or warranty made by or on behalf of the Borrower with respect to obtaining the Loan provided for herein or made or required to be made hereunder is incorrect in any material respect;

(d) A material default shall have occurred after the date hereof, and not been remedied after notice, under any other loan agreement or any other agreement between the Borrower or any of its agencies and A.I.D. or any of its predecessor agencies;

then A.I.D., at its option, may give to the Borrower notice that all or any part of the unrepaid Principal under the Loan provided for herein will be due and payable sixty (60) days thereafter, and unless the Event of Default is remedied within such sixty (60) days, such Principal and all interest accrued thereon shall become immediately due and payable.

SECTION 8.03. Suspension of Disbursements. In the event that at any time:

(a) An Event of Default has occurred and has not been remedied as provided above; or

(b) An event occurs that A.I.D. determines to be an extraordinary situation which makes it improbable that the purposes of the Loan provided for herein will be attained or that the Borrower will be able to or will perform its obligations hereunder; or

(c) Any disbursement would be in violation of the legislation governing A.I.D.;

then A.I.D., at its option, after notice to the Borrower, may (i) decline to issue further commitment documents, (ii) suspend or cancel outstanding commitment documents to the extent that they have not been utilized, giving notice to the Borrower thereof, and (iii) decline to make other disbursements.

SECTION 8.04. Cancellation by A.I.D. Following any suspension of disbursements pursuant to Section 8.03, if the cause or causes for such suspension of disbursements shall not have been eliminated or corrected within sixty (60) days from the date of such suspension, A.I.D. may at its option, at any time or times thereafter, cancel all or any part of the Loan that is not then disbursed.

SECTION 8.05. Continued Effectiveness of Agreement. Notwithstanding any cancellation, suspension of disbursement, or acceleration of repayment, the provisions of this Agreement shall continue in full force and effect until the payment in full of all Principal and any accrued interest hereunder.

SECTION 8.06. Refunds.

(a) In the case of any disbursement not supported by valid documentation in accordance with the terms of this Agreement, or of any disbursement not made or used in accordance with the terms of this Agreement, A.I.D., notwithstanding the availability or exercise of any of the other remedies provided for under this Agreement, may require the Borrower to refund such amount in United States dollars to A.I.D. within thirty days after receipt of a request therefor. Such amount shall be made available first for the cost of goods and services procured for the Project hereunder to the extent justified; the remainder, if any, shall be applied to the installments of Principal in the inverse order of their maturity and the amount of the Loan shall be reduced by the amount of such remainder. Notwithstanding any other provision in this Agreement, A.I.D.'s right to require a refund with respect to any disbursement under the Loan shall continue for five years following the date of such disbursement:

(b) In the event that A.I.D. receives a refund from any contractor, supplier, or banking institution, or from any other third party connected with the Loan, with respect to goods or services financed under the Loan and such refund relates to an unreasonable price for goods or services or to goods that did not conform to specifications, or to services that were inadequate, A.I.D. shall first make such refund available for the cost of goods and services procured for the Project hereunder, to the extent justified, the remainder to be applied to the installments of Principal in the inverse order of their maturity and the amount of the Loan shall be reduced by the amount of such remainder.

SECTION 8.07. Non-waiver of Remedies. No delay in exercising or omission to exercise any right, power or remedy accruing to A.I.D. under this Loan Agreement shall be construed as a waiver of any such right, power or remedy.

SECTION 8.08. Expenses of Collection. All reasonable costs incurred by A.I.D. (other than salaries of its staff) after an Event of Default has occurred, in connection with the collection of amounts due under this Loan Agreement or of any refund may be charged to the Borrower and reimbursed as A.I.D. shall specify.

ARTICLE IX

Miscellaneous

SECTION 9.01. Designation of Representatives.

(a) All actions required or permitted to be performed or taken under this Loan Agreement by the Borrower or A.I.D. may be performed by their respective duly authorized representatives.

(b) The Borrower hereby designates the Director-General, National Economic and Development Authority as its representative with authority to designate in writing other representatives in their dealings with A.I.D. The representative(s) designated in or pursuant to the preceding sentence, unless A.I.D. is given notice otherwise, shall have authority to agree, on behalf of the Borrower, to any modification of this Loan Agreement. Until receipt by A.I.D. of written notice of revocation of the authority of any such representative, A.I.D. may accept the signature of such representative on any instrument as conclusive evidence that any action effected by such instrument is authorized by the party on whose behalf such representative purports to act.

SECTION 9.02. Implementation Letters. A.I.D. shall from time to time issue Implementation Letters that will prescribe the procedures applicable hereunder in connection with the implementation of this Loan Agreement.

SECTION 9.03. Communications. Any communication or document given, made or sent by the Borrower or A.I.D. pursuant to this Loan Agreement shall be in writing or by telegram, cable or radiogram and shall be deemed to have been duly given, made or sent to the party to which it is addressed when it shall be delivered to such party by hand or by mail, telegram, cable or radiogram at the following address:

To the Borrower:

Mail Address:	National Economic and Development Authority P. O. Box 1116 Manila, Philippines
Cable Address:	NEDAPHIL

To A.I.D.:

Mail Address:	United States Agency for International Development c/o American Embassy Manila, Philippines
Cable Address:	USAID/AMEMB MANILA

Other addresses may be substituted for the above upon giving of notice as provided herein.

All communications and documents submitted to A.I.D. hereunder shall be in English, and all technical and engineering specifications therein shall be in English except as A.I.D. may otherwise agree in writing.

SECTION 9.04. Termination Upon Full Payment. Upon payment in full of the Principal and any accrued interest, this Agreement and all obligations of the Borrower and A.I.D. under this Loan Agreement shall terminate.

IN WITNESS WHEREOF, Borrower and the United States of America, each acting through its respective duly authorized representative, have caused this Agreement to be signed in their names and delivered as of the day and year first above written.

REPUBLIC OF THE PHILIPPINES	UNITED STATES OF AMERICA
By: Ferdinand E. Marcos	By: William H. Sullivan
Title: President, Republic of the Philippines	Title: Ambassador to the Republic of the Philippines
By: Jose A. Roño	By: Thomas C. Niblock
Title: Secretary, Department of Local Government and Community Development	Title: Director, USAID/Philippines

492-272

5 FEB 1979

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2p.

The Honorable
Jose A. Roño
Minister of Local Government
and Community Development
Quezon City Hall, Quezon City

Subject: AID Loan No. 492-T-035
Rural Roads Project
Project Implementation Letter No. 12

Dear Minister Roño:

This is to confirm USAID's receipt and acceptance of MLGCD's request for reimbursement, transmitted through NEDA in a letter dated Nov. 10, 1978, under the provision of Loan No. 492-T-035 and subsequent Implementation Letters No. 3 and 4.

Check No. 11,748,489 dated 8 December 1978 has been prepared in the amount of ₱3,614,000 payable to the Treasury of the Philippines for the account of MLGCD. Twelve USAID loan reimbursements have thus far been made bringing the total amount reimbursed to ₱78,676,277.80.

Sincerely yours,

Peter M. Cody
Director

cc: NEDA

bcc: OC
PO
CD
MLGCD/RRP

Clearance: OC ______
CD ______
PO ______
OFD ______

RRPlampohler:cbc
31 January 1979

UNITED STATES GOVERNMENT

Memorandum

4920272

TO : Distribution

DATE: March 23, 1979

FROM : J. R. Nussbaum, ASIA/PD/EA

SUBJECT: Philippines - AID Loan No. 492-T-035 (492-0272)
Rural Roads Project - Implementation Letter No. 15

Attached for your information and files is a copy of subject document.

Attachment: a/s

Distribution:

FM/LD:SHudec
FM/GFD:JO'Neill
GC/ASIA:HMorris
ASIA/PT:RNachtrieb
ASIA/TR:TMArndt
ASIA/DP:RHalligan
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DS/DIU/DI