

## The Philippine Water Revolving Fund Support Program

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# UPDATED WORKPLAN

## PHASE 1-YEAR 1

April – December 2007



This project is implemented by Development Alternatives, Inc. with in association with:  
The Community Group International LLC  
Consultants for Engineering Science and Technology, Inc.  
Resource Mobilization Advisors

## **PREFACE**

The United States Agency for International Development (USAID) Philippine Mission has contracted Development Alternatives Inc. (DAI) to implement the Philippine Water Revolving Fund Support Program (PWRF) under contract number EPP-I-00-04-00023. The effective date of the contract is October 1, 2006. Phase 1 will run from said date to September 30, 2007. Phase 2 is contingent on USAID's exercise of the option to continue the program from October 1, 2007 to September 30, 2011. DAI will implement the project with the participation of TCG International, LLC, Resource Mobilization Advisors and Consultants for Engineering Science and Technology, Inc.

In compliance with the provision of the contract, the team submitted in November the First Year Annual Work Plan, covering a 15-month period. The team conducted a review of the work plan in March 2007. Current conditions and new development merited an adjustment of the work plan as presented herein. The revised work plan covers the period April 1 to December 31, 2007. The accompanying gantt chart shows the revised schedule of activities.

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April 20, 2007

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## 1. Introduction

This updated first year Work Plan covers the period from April 1 to December 31, 2007. The First Year work plan activities focuses on achieving the following objectives under Phase I of the Program:

- Set up the appropriate institutional arrangements for the PWRF, including supporting efforts to secure the loan from the Japan Bank for International Cooperation (JBIC) and its operating and policy guidelines; and United States Agency for International Development's Development Credit Authority (USAID-DCA) guarantee agreement;
- Strengthen selected water and finance sector institutions vital to PWRF Program's success; and
- Assist local government units (LGUs) and water districts (WDs) to develop a pipeline of viable projects in anticipation of an operational PWRF within 2007.

The adjustments in the priority activities and schedule are based on the following developments:

- The Department of Finance (DOF) concurrence of the scope of work for the rationalization of credit programs was not obtained until April 4, 2007. The new undersecretary in charge of the implementation of EO 279 has yet to be brought on board the EO's Oversight Committee. This has delayed our analysis and preparation of rationalization guidelines.
- The LWUA Employees Association successfully secured a writ of injunction for EO 279. As such the implementation of EO 279 is held in abeyance. Although the team is now proceeding with the preparation of rationalization guidelines, their issuance may have to be withheld until the resolution of the case.
- JBIC has yet to formally confirm the inclusion of the Environment Development Program Loan, which includes PWRF funding, under the current 27<sup>th</sup> Yen Loan Program. The 27<sup>th</sup> YLP was previously expected to be signed in March this year. Postponement of EDP/PWRF to the 28<sup>th</sup> YLP will delay the implementation of the Fund by at least a year.
- With the uncertainty of JBIC funding, USAID advised the team to hold off any major efforts on work plan activities that are premised on fund availability, e.g., project development. However, in April, seeing the interest of some commercial banks in water sector lending, the team and USAID agreed to explore interim financing for PWRF, e.g. second-generation funds of DBP. Hence the team has resumed its project development work.

- The change in the Development Bank of the Philippines (DBP) point person and coordinating team for the PWRF necessitated a new round of briefings and opened discussions on the financial structure. Comments and suggestions that would require fundamental change in the scope and structure surfaced. It became apparent that management buy-in is tenuous, given the following concerns: field personnel's resistance to the paradigm shift, skepticism on the viability of the structure and the perceived inequity in the risk reward ratio between DBP and PFIs. At any rate, DBP agreed to adopt the PWRF structure subject to the following:
  - the pricing of the loan components of DBP and PFI should be commensurate to the risks taken; and
  - the structure will be continually reviewed and adjusted or changed depending on changes in the market.
- The ICC approval of the PWRF is still pending. The most recent schedule given for presentation to the ICC Technical Board is on April 20, 2007. ICC Cabinet Committee presentation will likely be in May 2007. The ICC approval is a pre-requisite of the JBIC loan application processing.

The revised work plan per component is shown in the next sections. The discussion will be prefaced by the expected outputs as outlined in the contract, the accomplishments to date and the attenuating conditions that necessitated the adjustment.

## 2. Component 1: PWRF Set-up and Institutional Development

### OBJECTIVE

Establish and operationalize the PWRF lending program and put in place the DCA co-guarantee agreement with LGUGC.

### COMPONENT 1 DELIVERABLES and SUMMARY of ACCOMPLISHMENTS

Deliverables	Accomplishments
<ul style="list-style-type: none"> <li>▪ Updated financial model for the PWRF</li> </ul>	Completed and submitted to DBP
<ul style="list-style-type: none"> <li>▪ Information memorandum for ICC</li> </ul>	Completed; continually assisting DBP respond to issues raised by the ICC evaluation team; Technical Board presentation scheduled on April 12, 2007
<ul style="list-style-type: none"> <li>▪ Working Paper for the MDFO Secretariat for the stand-by credit line arrangement</li> </ul>	Under preparation
<ul style="list-style-type: none"> <li>▪ Credit framework arrangement sections of the Operating Policy Guidelines of the JBIC loan to the Development Bank of the Philippines</li> </ul>	The team has prepared a working draft of the OPG, which is currently being reviewed by DBP. The OPG is a work in progress and will be worked on through loan signing.
<ul style="list-style-type: none"> <li>▪ MOA between DBP and PFIs and inter-creditor agreement</li> </ul>	
<ul style="list-style-type: none"> <li>▪ Business plan and marketing strategy of the PWRF</li> </ul>	
<ul style="list-style-type: none"> <li>▪ Finalized standard loan agreement, guarantee agreement, and MDFO loan agreement</li> </ul>	Draft has been prepared under the FORWARD project; requires validation by PFIs and borrowers
<ul style="list-style-type: none"> <li>▪ Guidelines for the Standby Credit Line of DBP</li> </ul>	
<ul style="list-style-type: none"> <li>▪ Credit screening guidelines for water districts</li> </ul>	
<ul style="list-style-type: none"> <li>▪ Training workshops on familiarization with the water sector and utility operation indicators, credit screening of water utilities</li> </ul>	
<ul style="list-style-type: none"> <li>▪ Study tour for 8-10 participants to view US or Indian experience with pooled financing mechanisms</li> </ul>	

## PLANNED ACTIVITIES

### 1.1 Assist Implementing Entities to Establish and Operationalize the PWRF.

**Facilitating approval of PWRF.** Our team will continue to provide assistance to DBP respond to issues raised in the ICC evaluation and provide them with other necessary information. We will also continue to hold discussions with DBP officials and staff to promote buy in and understanding of the PWRF.

In addition, we will as may be requested assist PFIs, LGUGC, and MDFO secure their respective Boards' final approval and commitment of resources to the PWRF.

**Facilitating Approval of the JBIC Loan for PWRF.** As of this writing, JBIC has not committed to the EDP/PWRF loan yet. There are positive indications however from the JBIC Philippine Representative Office that the loan may still be included in the 27<sup>th</sup> Yen Loan Program that is scheduled for signing this year. Our team has given a work in progress draft of the PWRF Operating Policy Guidelines to DBP in preparation for the PWRF loan appraisal. The OPG is an accompanying document of the loan agreement. We will continue to improve the OPG in consultation with DBP, and provide other assistance required in the processing of the loan.

**Facilitating Interim Financing for PWRF.** In view of the delay in the JBIC financing, our team will look into interim financing schemes to test the PWRF financing structure. We team will work out the following with concerned partners:

- Use of second generation funds of DBP to advance the financing, with the option for take out using the new JBIC loan once it is in place.
- Use of PFI financing for 100% of the loan, with a stand-by credit line provided by DBP for water district projects and MDFO for LGU projects. Current market rates are competitive with ODA re-lending rates; however lending terms are still between 7 to 10 years only.

**Preparation of implementation guidelines.** Our team will assist the DBP to:

- Prepare the operating guidelines of PWRF,
- Review and refine the loan application process and repayment arrangements;

<b>Box 1. Indicative PWRF Business Plan Outline</b>	
A. Background	<ul style="list-style-type: none"> <li>▪ Business Concept</li> <li>▪ Situationer</li> <li>▪ Key Success Factors</li> </ul>
B. Vision/ Mission Statement	
C. Market Analysis	<ul style="list-style-type: none"> <li>▪ Overall Market</li> <li>▪ Changes in the Market</li> <li>▪ Target Market</li> <li>▪ Customer Characteristics</li> <li>▪ Customer Need</li> <li>▪ Customer Borrowing Decisions</li> </ul>
D. Competitive Analysis	<ul style="list-style-type: none"> <li>▪ Sector Overview</li> <li>▪ Analysis of Competition</li> <li>▪ Opportunities</li> <li>▪ Threats and Risks</li> </ul>
E. Strategy	<ul style="list-style-type: none"> <li>▪ Key Competitive Capabilities</li> <li>▪ Key Competitive Weaknesses</li> <li>▪ Strategy</li> <li>▪ Implementing Methodology</li> </ul>
F. PWRF Loan Product – Description of product	
G. Marketing the PWRF – marketing strategy and tactics	

- Facilitate discussions with PFIs on how they can participate in the PWRF (e.g., through a credit line); and
- Facilitate discussions with MDFO on the re-financing arrangements, and the drafting of operating guidelines for the MDFO standby loan facility for the PWRF.

**Preparation of the business plan.** We will help DBP to prepare the business plan and the marketing strategy for PWRF. The business plan will provide the PWRF administration team in DBP with a roadmap on how to develop the market for this product with both the water utility borrowers and the PFI lenders. The business plan will also look into the vital elements for PWRF's transition to pooled financing. The assistance will cover the following:

- Strengthening DBP's Water and Sanitation Lending Strategy
  - Assist DBP in coming up with a water sector strategy that will articulate the bank's lending strategy towards the sector.
  - Assist DBP in identifying the market for water and sanitation loans
- Enhancing the Capacity of DBP's Water Lending Unit
  - Evaluate DBP's capacity and address organizational constraints in increasing exposure towards the water and sanitation Sector.
  - Assist DBP identify the skills and human resources requirement in order to effectively promote PWRF.
  - Provide other inputs on how to effectively promote the water and sanitation sector to other Private Financial Institutions under the PWRF Public-Private Partnership framework.
  - Assist DBP come up with a medium term business plan for the water lending department that will identify opportunities and risks in the water and sanitation sector.
- Marketing PWRF
  - Assist DBP in conceptualizing the marketing plan for PWRF including coming up with standard marketing kits and presentations to PFI's, DBP Branch Heads, LGU leaders and other stakeholders.

## **1.2 Provide Institutional Support to PWRF**

**Capacity building for key implementers.** We will conduct a needs assessment and prepare a capacity building plan for key implementers: DBP, LGUGC, MDFO and PFIs. The topics will cover, among others, the following elements:

- Credit screening of water utilities
- Familiarization with water utility management and best practices
- Appraisal of water supply and sanitation projects
- Familiarization with the policy, institutional and regulatory regime for water utilities

The credit screening guidelines that will be prepared primarily for LGUGC will be based on international credit rating methodology, criteria and indicators. Moreover, subject to availability of resources, we may also provide technical assistance to LGUGC in developing their guarantee pricing policy for water projects.

### **1.3 Conduct Study Tours to Improve Executing Agencies' Understanding of Revolving Fund Operations**

**Study tour.** We plan to organize a study tour either in India or in USA around July or August 2007. We believe that the experience, at this point in time, is most relevant to helping GRP leaders understand how a revolving fund can be organized, established and capitalized. Participants will visit either a State Revolving Fund in the US or the Tamil Nadu and Bangalore Urban Development Funds in India. Objectives include:

- Discuss and understand the legal and operating/organization structure put in place by both States to finance local infrastructure;
- Understand the importance of establishing the appropriate policy framework to support revolving fund operations;
- Understand the role and importance of credit ratings to mobilizing private capital; and
- Understand the role and options for structuring credit enhancements to attract private capital.

Through this study tour, we expect participating policy makers to gain insights that will facilitate the transition of the PWRF from access loans to securities to raise domestic capital.

## 3. Component 2: Water Supply and Sanitation Project Preparation

### OBJECTIVE

Assist water districts and LGUs to improve or update pre-investment studies and implement immediate measures to improve project creditworthiness.

### COMPONENT 2 DELIVERABLES

- Prioritization criteria developed and approved by the PWRF Steering Committee and DBP
- At least 7 and up to 10 projects are ready for PWRF funding
- Credit ratings completed for at least two projects
- Plan developed for establishing a Project Development Facility
- Establish procurement mechanism for providing technical assistance needs to utilities

None of the Component 2 deliverables have been completed yet. Initiating activities are in progress.

### PLANNED ACTIVITIES

#### 2.1 Assist Utilities to Finalize Projects for PWRF Funding

**Prepare prioritization criteria.** Our team has prepared an initial draft of the prioritization criteria. The prioritization criteria will be incorporated in the operating guidelines of DBP.

**Conduct rapid screening/appraisal of projects.** Our team validated readiness of the projects identified in the JBIC SAPROF demand analysis (see Table 1), and of the 13 identified with feasibility studies, only four projects from Zamboanga City, San Fernando City, Metro Davao Water Districts, and Allacapan Municipality have current and complete-enough pre-investment studies.

#### **Assist targeted utilities to improve projects.**

The rest of the target projects require more in depth technical assistance in terms of updating and refining cost estimates, financial analysis, tariff levels and other aspects to bring these project pre-investment studies to a level acceptable to lenders.

**Table 1. List of Potential Project for PWRF Funding**  
(Identified by the JBIC SAPROF's Demand Analysis)

No.	Water Service Providers	Investment Program	Project Profile				Status of Project Preparation (as of end-March 2007)
			Project Component	Description	Project Cost (Million Peso)	Implementation Period	
<b>W D s</b>							
19	Baliwag	2006-2011: P150M	Pipeline expansion program, Parallel pipeline expansion		150	2008	Bulk water supply for a cluster of WDs in Bulacan is being proposed
			Well drilling, ground reservoir, water tank			2008	
		2012-2016:	Rehabilitation, lot purchase for new pumping station			2008	
35	Silang	2006-2011: P166.5M	Source Development and Expansion-Component 1	Additional 4,320 cum/day	166.5	2006	Master Plan/Program of Works submitted to DBP. Project endorsed to credit committee.
			Source Development and Expansion-Component 1	Additional 6,740 cum/day		2007	
		2012-2016:	Source Development and Expansion-Component 1	Additional 5,990 cum/day		2008	
38	San Pablo	2006-2011: P133M	Source Development	Development of Lumbo Spring, Balumbong Spring, and Calibato Lake	132.2		As per meeting of 5 February 2007, WD is inclined to use its own funds for new projects
			Network System Modification	Installation of new transmission lines and isolation valves			
		2012-2016:	Network Expansion/Extension Program	Installation of 100mm diameter to 200mm diameter pipes			
49	Davao City	2006-2010: P4275 M	Tamugan Surface Water Development Project	Development of 200,000 m3/day surface water source	3000		FS updating to be bid out 2nd qtr of 2007
			Bunawan-Lasang Water Supply System Phase II	Development of groundwater sources, pipe laying		275	2007

No.	Water Service Providers	Investment Program	Project Profile				
			Project Component	Description	Project Cost (Million Peso)	Implementation Period	Status of Project Preparation (as of end-March 2007)
			Indangan Water Supply System			2007	preparing P600M+ project for NRW reduction/pipeline replacement Project deferred
57	San Fernando City	2006-2011: P100M 2012-2016: P240M	Water Supply Improvement and Expansion Project		100	2006	F/S to be finalized April 2007. DBP advised (April 2) PWRF Team that project will not be funded under the PWRF
58	Tagum City	2006-2011: P360M	Surface water dev't & rehab of pipes	P70M for rehab of pipes for add'l supply of 21,500 cu.m./day surface water (P290M)	360	2006	FS still to be prepared. PWRF project development TA for water treatment being considered, in conjunction with a TA from the Davao WD.
59	Cabanatuan	2006-2011: P567M 2012-2016:	Modular Water Treatment Plant; Reservoir; Expansion		100	2007-2009	FS still to be prepared. Project development TA for water treatment being considered.
62	Legaspi City	2006-2011: P219M 2012-2016:	Bulk Water Supply		200	2009	P50 million bulk water supply project for bidding
64	Tagaytay City	2006-2011: P901.6M 2012-2016:	NRW Reduction	Replacement of old pipes	50	2007-2008	Conceptual Stage
65	Puerto Princesa City	2006-2011: P250 M 2012-2016:	Bulk Water Development	Bulk supply of 25,000 cum/day	250	2007	Per the WD, technical study was finalized by LWUA. Financial-

No.	Water Service Providers	Investment Program	Project Profile				
			Project Component	Description	Project Cost (Million Peso)	Implementation Period	Status of Project Preparation (as of end-March 2007)
							economic study still needs to be prepared. PWRF TA may be extended for the fin-eco study.
72	Zamboanga City	2006-2011: P 195 M 2012-2016:	Pipeline Replacement/ Upgrading and Water Development/ Secondary Line Project		195	2006-2007	Approved by DBP
73	Metro Quezon	2006-2011: P64M	Replacement of water system (Tayabas); distribution program		64	2006	Feasibility Study completed. Loan for reimbursement of project expenditures
76	Cagayan de Oro City	2006-2011: P 394M (one project ongoing)	Bulk Water Supply Improvement Project	Additional 50,000 m3/day supply	200	2009-2010	
78	Metro Cebu	2006-2011: P2,459M 2012-2016:	Carmen Bulk Water Supply (Acceptance)	Installation of new distribution lines, reservoirs, and booster pumps	682	2009	Proposed distribution system expansion project (P682+ million) may be re-designed if new water resources are developed instead of Carmen surface water source (Ayala BOT)
94	Metro Iloilo		Rehabilitation of Distribution Lines		250	2007	
				<b>Sub-Total</b>	<b>6174.7</b>		

## **2.2 Assist Potential Borrowers Implement Measures to Improve Project Viability and Credit Worthiness**

**Conduct Rapid Needs Assessment of Targeted Utilities.** Objective of the rapid needs assessment will be to identify those operational, financial and management improvements the utilities can undertake to enhance the viability of the projects. As part of this assessment, we will support the credit screening of at least two utilities with projects for PWRF funding. We will use the credit screening to highlight those areas where the utilities can improve operations, and also, as described in Activity 3.2, to compare the credit screening with the creditworthiness classification system currently employed by LWUA

**Assist Targeted Utilities to Undertake Immediate Reforms.** Our team will assist borrowers to identify and implement reforms they can immediately improve the creditworthiness and viability of proposed projects. For instance, our team will help utilities analyze and map out approaches to revise tariff rates to reflect full cost of operations, improve billings and collections, and recommend other changes to improve overall utility operations and financial performance.

## **2.3 Establishment of a Project Development Facility**

Many utilities have highlighted the lack of access to funds for project development as a key constraint to preparing projects for system expansions and upgrades. The team will analyze options and make recommendations for institutionalizing a project development facility that provides loans to utilities for project feasibility and design studies. The team will prepare analysis of existing project development facilities that are being funded through various donor loan programs, and identify the weaknesses and strengths of these facilities. From this analysis, and in discussions with GRP officials, team will identify options for establishing a stand-alone PDF, and options for how it could be capitalized and administered.

## **2.4 Purchase Order Mechanism Developed for Procuring Services**

Our team will prepare a procurement mechanism for delivering short-term assistance to utilities. In addition, the team will develop templates and an evaluation system that water utilities can use to contract out specific technical services. Through the PWRF mechanism, we will be able to quickly deliver technical assistance. The templates and evaluation system will enable utilities to put in place their own mechanism to quickly avail of technical expertise in a transparent and cost-effective manner.

## 4. Component 3: Water and Finance Sector Strengthening

### OBJECTIVE

Help implement strategic reforms that facilitate achieving the targets under Components 1 and 2.

### COMPONENT 3 DELIVERABLES

- Draft EO 279 implementing guidelines to rationalize credit programs and draft ICC resolution adopting guidelines
- Recommendations on segmentation of the market based on credit classification criteria consistent with international standards.
- Recommendations on short-term credit program to assist non-creditworthy utilities to reform and restructure operations to improve creditworthiness
- Action plan for instituting credit ratings for all water districts and LGU water projects
- Position Paper for Central Bank on eligibility of water projects for Agri-Agra Law compliance
- Long-term Business planning framework for water districts
- Small grants program design

None of the Component 2 deliverables have been completed yet. Initiating activities are in progress.

### PLANNED ACTIVITIES

#### 3.1. Support the Rationalization of Credit Programs for Water Supply

Executive Order 279 enunciates the long-term goal of the government to shift water sector financing to market-based lending and to realign the role of the Local Water Utilities Administration towards financing of less than creditworthy utilities and provision of technical assistance to utilities. Under this policy:

- All creditworthy utilities will shift immediately to market-based lending provided by GFIs and PFIs. The policy suggests that non-creditworthy utilities will be allowed access to concessional financing.
- Through LWUA, the GRP will establish and implement a technical assistance support program that assists non-creditworthy utilities to undertake reforms and achieve creditworthy status, thus facilitating the shift to market-based lending.

While policy statements are clear, the policy lacks detailed implementing rules, regulations and operational guidelines to implement this policy. As such, GFIs have continued to provide multiple loan products that offer differing rates and terms

depending upon the source of funds. It is in this environment that we have designed the PWRF. However, successful implementation of the PWRF requires that the GRP eliminate lending by GFIs to creditworthy water utilities at less than market rates.

DOF has committed to lead the preparation and issuance of operating guidelines to implement the rationalization of credit programs. Our team is positioned to provide technical assistance to DOF and to the Oversight Committee on the matter. We have prepared the scope of work and identified a credit policy specialist to lead the work. We got DOF's imprimatur for this undertaking only in the first week of April. The hold back is largely due to the change of the DOF undersecretary charged with the oversight of EO 279 policy implementation.

Our team facilitated the orientation of the new undersecretary and his staff on water policy reforms. We arranged a meeting between the DOF team and one of the principal authors of the study, *Reforms in the Financing Policies in the Water Sector, Graduation Policies in the Water District and Approaches to Various Regulatory Issues* (Stone and Webster, 2003), the recommendations of which became the basis of EO 279 policy guidelines.

The rationalization study is scheduled to be undertaken between April and June 2007. The study will cover the following:

- Review the World Bank study on rationalizing credit lines, and based on this review, undertake further analyses of the current credit lines available for water sector lending. This review will analyze terms, tenors, collateral requirements, equity contributions, etc. and compare these credit facilities with what is currently available in the private financial market. Based on this review, recommendations will be made on the rationalization strategy.
- Based thereon, the team will recommend further an implementation plan for rationalizing the credit lines to comply with EO 279 policies.
- Host a workshop with DOF, NEDA and GFIs on the study, recommendations and draft action plan for rationalizing the credit lines.
- Host a similar workshop with the different donors currently involved in the water sector (i.e. World Bank, JBIC, GTZ, ADB, KfW and others) to review the results of the analysis, recommendations and draft action plan.
- Based on the feedback from these workshops, finalize the recommendations and action plan and prepare a draft policy paper on rationalizing the credit lines for ICC review and adoption by the NEDA Board.

### **3.2 Support EO 279 Oversight Committee Implementation of Financing Policies**

Related to the rationalization of the credit lines, full implementation of policies outlined in EO 279 also requires a clear definition of how the market will be segmented between creditworthy and non-creditworthy utilities. The EO 279 policy limits LWUA's financing role to the less than creditworthy utilities. LWUA has previously focused its lending to creditworthy utilities, and as such will need to review its lending guidelines with the shift

in clientele. Moreover, since EO 279 cannot supersede the LWUA mandate as provided for by a special law, it maintains the right to be the senior lender to water utilities. LWUA has to issue a waiver before water districts can take on other loans that would have equal repayment rights with the existing LWUA loan.

Our team will assist EO 279 OC analyze how the market of water utilities will be segmented between creditworthy and non-creditworthy utilities. LWUA has categorized water districts as creditworthy, semi-creditworthy, pre-creditworthy and non-creditworthy. This scheme provides the immediate starting point for segmenting the market and linking this segmentation to the rationalization of credit lines. During the first year, we will:

- Review and analyze the current creditworthiness criteria and benchmarks being applied by the EO 279 OC, and make recommendations for aligning these criteria with internationally accepted credit rating standards and processes.
- Using the credit screening guidelines developed under Component 1, we will test the screening guidelines on at two water districts that are preparing projects for PWRF funding.
- Host a workshop with the EO 279 OC and other stakeholders to review and agree upon an action plan for adopting a revised credit classification process more in line with international standards.
- Collaborate and support Eco-Asia, in helping LWUA design an alternative, short-term financing program for assisting non-creditworthy utilities to undertake reforms needed to achieve creditworthy status. Providing short-term financing for operational reforms will help avoid the moral hazard of making available long-term capital loans to non-creditworthy utilities.

In the original work plan we had included a task on the preparation of a roadmap to institutionalize credit rating of water districts and LGUs. We had planned to do a review of international experience in developing the credit rating market, holding consultations among key stakeholders to draw support for a national policy to mandate credit rating, and finally prepare a policy paper for mandatory credit rating.

Based on further review of this approach and comments from our international finance specialist, the team realized that mandatory credit rating will be a heavy handed move on the part of the government. The establishment of credit rating agencies cannot viably be done through regulation; rather it should be driven by market demand. Rating agencies are unlikely to set up shop unless they see a significant deal flow. Moreover, mandating a rating as a condition of debt financing may establish a barrier to finance as the costs of a rating will be relatively high because establishing a rating system would be spread over a limited number of issues.

Furthermore, we were advised that with the current financial structure of the PWRF, credit rating is not yet critical. With the direct lending arrangement of DBP and PFIs, these lenders are expected to do in depth project appraisal and evaluation of borrower's creditworthiness since their funds are on the line. Moreover, in the case of PFIs, LGUGC's guarantee will be a more powerful market maker than an independent credit rating.

Hence, credit rating will have little value added. Credit rating will be critical once the financing modality shifts to bond issuance, or when a secondary trading market for securities is established. At this point the credit rating even without an explicit regulation will develop by necessity.

### **3.3 Prepare PWRF Transition to Greater Private Sector Participation**

One of DBP's pre-condition in the implementation of the PWRF is to ensure dynamism and responsiveness to the evolving market situation of PFIs and borrowers. The team will continually work with DBP review and modify the PWRF structure to ensure its relevance and effectiveness.

In the same vein, the team will respond to the suggestion of the new undersecretary of DOF to continue the development of a pooled bond financing scheme, subject to his commitment to work on enablers, e.g., reserve fund to collateralize bond or other similar credit enhancements. In the original work plan this task was put in the option years. The work can be advanced if DOF is indeed keen on pursuing the analysis and design at this time. We will conduct discussions with the DOF official and his staff to prepare the scope of work of this task.

### **3.4 Facilitate Agri-Agra Eligibility of Water Sector Lending**

Presidential Decree 717 requires mandatory allocation of funds for agrarian reform and agricultural credit. All banking institutions should set aside 25% of their loan funds for the aforementioned sectors. This list was later expanded to include: educational institutions, cooperatives, hospitals, socialized and low cost housing and local government unit loans without national government guarantees. Sanctions are imposed on banks that fail to comply. Many banks find it difficult to comply with this requirement. In the first quarter of 2006, universal and commercial banks lent only 7.4% of their total loan funds for agri-agra and other eligible projects.

As an incentive for PFIs to lend to water supply and sanitation projects, our team will assist DOF in preparing the request to Central Bank (CB) to include water supply and sanitation projects in the list of eligible projects. CB requires the submission of a position paper that will provide the analysis and the justification for the request. Our team will draft the position paper and we will backstop DOF in the presentation of the position paper to the Monetary Board.

### **3.5 Prepare Business Planning Framework for Utilities**

In preparation for the capacity building technical assistance to utilities on long term planning and investment programming, our team will prepare a business plan framework. The framework will help the utilities formulate their vision, mission, objectives, strategies and programs for a given period. The framework will be harmonized with the sector policy as stated under the Medium Term Philippine Development Plan and with the regulatory framework. Moreover the team will prepare the training design for business plan preparation and the system for the selection of participants.

### **3.6 Design Small Grants Program**

We will prepare the design of a small grants program that is linked to the PWRF. Grants could be used to:

- Leverage capital for expanding safe water supply to poor neighborhoods on a full cost recovery basis, especially in areas served by those utilities receiving support from the PWRF; and
- Fund training programs for utility managers on creative approaches on providing poor neighborhoods with safe water and basic sanitation.

## 5. Component 4: General PWRF Program Support

### OBJECTIVE

Provide technical secretariat support to the PWRF Steering Committee and Technical Working Group; and support USAID in reporting, advocacy and collaboration with JBIC on the PWRF.

### COMPONENT 4 DELIVERABLES

Deliverables	Accomplishments
<ul style="list-style-type: none"> <li>▪ At least one meeting per quarter for the Steering Committee and the Technical Working Group</li> </ul>	Steering Committee meetings held last November 2006 and March 2007
<ul style="list-style-type: none"> <li>▪ Meetings and consultations as scheduled as necessary with the Implementation Committee</li> </ul>	Various meetings and consultations with key stakeholders
<ul style="list-style-type: none"> <li>▪ Technical papers, presentations, inputs to USAID reports and communication materials on the PWRF, as may be required by USAID</li> </ul>	Submitted on demand
<ul style="list-style-type: none"> <li>▪ Set up PWRF Website</li> </ul>	

### PLANNED ACTIVITIES

#### 1. Provide technical secretariat support to the PWRF Steering Committee and Technical Working Group

In both phases, our team will continue to provide technical secretariat support to the PWRF Steering Committee and its Technical Working Group, and to the proposed Implementation Committee. We will facilitate policy decisions by preparing thorough analyses of issues for resolution.

#### 2. Provide Support to USAID's Reporting, Advocacy and Collaboration with JBIC on the PWRF

We also will support USAID's collaboration with JBIC on the PWRF by hosting meetings, carrying out any required analyses, and producing reports and other communications materials. We will respond to any request of USAID to provide inputs to its reporting and advocacy needs for the PWRF program. We can also provide technical and logistic support to any workshop or forum that USAID and JBIC may organize to promote their collaboration. Our team can also serve as a resource group for similar initiatives of USAID and JBIC in other target countries, e.g., Indonesia.

### **3. Knowledge/Information Dissemination and Management**

The team will design a PWRF website that can serve as a portal for reports and other information related to the PWRF, and also provide access for stakeholders to other information related to water sector finance, revolving funds and water utility operations. While the PWRF website will initially be managed by the team, we anticipate moving the website management and maintenance to the PWRF unit to be established within DBP.

The overall work plan and schedule of activities is shown in Figure 1.

**Figure 1: PWRF Phase 1/Year 1 Annual Project Work Plan**

MAJOR TASKS	Phase 1: Year 1										Status	Respon- sibility (L=Lead)	Expected Outputs	
	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec					
<b>Component 1: PWRF Set-up and Institutional Development</b>														
Assist DBP secure ICC approval of the PWRF and the JBIC loan		■											<i>Porciuncula</i>	Information memorandum for ICC
Update/Construct PWRF Financial Model											<b>Done</b>		<i>Sr. Finance Specialist/ Pantillano + Porciuncula</i>	Financial Model for PWRF
Recommend to the MDFO Policy Governing Board the funding commitment and mechanism for provisioning for the stand-by credit line		■											<i>Pantillano</i>	Working paper for the MDFO Secretariat
Facilitate MDFO preparation of guidelines for the Standby Credit Line		■											<i>Pantillano</i>	Draft of Standby Credit Guidelines
Operating and Policy Guidelines (OPG) for the PWRF component of the EDP		■											<i>Pantillano (L)+ Porciuncula+ STTA: Johnson</i>	Draft credit framework agreement sections of the OPG
Facilitate interim financing for PWRF														
Draft DBP's inter-creditor agreements with participating PFIs			■										<i>Pantillano (L) + STTA: Gonzales and Johnson</i>	Draft MOA between DBP and PFIs and inter-creditor agreement
Conduct Consultations with specific credit committees													<i>Pantillano (L), + STTA Johnson</i>	Roundtable Discussions
Facilitate Signing of MOU between DBP and PFIs					■								<i>Porciuncula (L)+, Pantillano</i>	Signed MOU between DBP and PFIs

MAJOR TASKS	Phase 1: Year 1										Status	Responsibility (L=Lead)	Expected Outputs
	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec				
Provide inputs to DCA and the Mission in preparing the co-guarantee agreement with LGUGC												<i>Porciuncula (L)+ Team</i>	Inputs to the DCA and LGUGC Co-guarantee Agreement
Facilitate Signing of Guarantee Agreement												<i>Porciuncula (L)+ Pantillano</i>	Signed Guarantee Agreement
Prepare PWRF Operating Guidelines, including intake protocols, project appraisal, credit review, monitoring system, application process flow												<i>Pantillano (L)+ STTA (Johnson, Gonzales)</i>	Draft Operating Guidelines and Manual of Operations
Facilitate DBP's preparation of the PWRF Business Plan (including marketing strategy)												<i>Pantillano (L)+ STTA: TBD</i>	Business plan and marketing strategy for the PWRF
Prepare PWRF Marketing Materials												<i>Pantillano (L)+ TBD</i>	Marketing Information Materials
Assist in the implementation of the marketing plan												<i>Pantillano (L)+ Team</i>	Inputs to the implementation of the marketing plan
Assist LGUGC develop credit screening guidelines/manual for water districts												<i>Pantillano (L)+ TCGI STTA</i>	Draft credit screening manual for water districts
Conduct training needs assessment for DBP , LGUGC and PFI staff												<i>Pantillano</i>	Needs Assessment Report
Prepare training design, plan and program												<i>Pantillano</i>	Training Manual
Train DBP and PFI staff on the PWRF and appraisal of water and sanitation projects												<i>Pantillano (L)+ Team +STTA: deVera, Giantris</i>	Training seminars for PFI staff
Continue to provide institutional support to key implementers: updating of guidelines, training, and other technical assistance												<i>Pantillano (L)+ Team +STTA: Johnson, deVera, TCGI, Gonzales</i>	TBD
<b>1.3 Conduct study tours to India and potentially to the U.S. to</b>												<i>TCGI(L)+ Porciuncula and</i>	Briefing papers and program

MAJOR TASKS	Phase 1: Year 1										Status	Responsibility (L=Lead)	Expected Outputs
	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec				
<i>improve executing agencies' understanding of operation of revolving funds</i>												Team	Study tour in the US or India (e.g. Tamil Nadu Pooled Financing)
<b>Component 2: Water and Sanitation Project Preparation</b>													
<b>2.1 Assist utilities finalize projects for PWRF funding</b>													
Establish criteria with DBP for prioritizing PWRF investments	■											Sr. PS/Asuncion(L) and Pantillano	Criteria developed and approved by DBP
Conduct rapid screening/appraisal of project feasibility/preparation documents												Asuncion (L)/Pantillano	Rapid assessment of FSS
Assist targeted utilities to improve pre-investment analysis, technical design, demand forecasting and financial analysis to meet PWRF due diligence requirements												Asuncion(L)+ Pantillano and STTA: TBD	Seven (7) to ten (10) projects ready for PWRF funding
<b>2.2 Assist potential borrowers implement measures to improve project viability and creditworthiness</b>													
Conduct rapid needs assessment of immediate operation and management improvements to enhance viability of projects												Asuncion (L)+ STTA	Needs assessment of immediate management reforms
Assist targeted utilities implement measures to improve technical operations and financial management, e.g., cost efficiency measures, tariff setting, billing and collection, performance monitoring												Asuncion (L)+ STTA	Policy, management reforms at water utility level
<b>2.3 Prepare concept paper and feasibility assessment a Project Development Facility</b>												Porciuncula(L)+ Asuncion, McCluskey	Plan for establishing a Project Development Facility
<b>2.4 Develop a purchase order mechanism for procuring</b>						■						Asuncion	Procurement mechanism for

MAJOR TASKS	Phase 1: Year 1										Status	Responsibility (L=Lead)	Expected Outputs
	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec				
<i>services to meet the technical assistance needs of utilities</i>													providing technical assistance needs of utilities
<b>Component 3: Water and Finance Sector Strengthening</b>													
<b>3.1 Support the rationalization of credit programs for water supply and sanitation</b>													
Review existing materials on credit program rationalization and prepare TOR for the water sector												<i>Sr. PIDS</i>	TOR for credit program rationalization
Prepare Analysis Paper of current credit lines and recommendations and action plan for implementing recommendations												<i>STTA: Credit Policy Specialist (CPS)</i>	Analysis Paper of Credit Program Rationalization
Host workshop with DOF, NEDA and GFIs on study and recommendations												<i>Sr. PIDS(L)+ STTA: Credit Policy Specialist (CPS)</i>	Workshop with GOP oversight agencies and GFIs
Host workshop with donors on study/recommendations												<i>Sr. PIDS (L)+ STTA: Credit Policy Specialist (CPS)</i>	Workshop with donors
Finalize analysis paper and recommendations and prepare DOF's memorandum to ICC for review and adoption through a NEDA board resolution.				■								<i>Sr. PIDS (L)+ STTA: Credit Policy Specialist (CPS)</i>	Draft memorandum for the ICC NEDA Board
Prepare IRRs for adopted policy rationalizing credit lines				■								<i>Sr. PIDS (L)+ STTA: Credit Policy Specialist (CPS)</i>	Draft EO 279 implementing guidelines to rationalize credit programs; draft ICC Resolution adopting guidelines
<b>3.2 Support implementation of EO 279</b>													
Review and analyze the current creditworthiness criteria and benchmarks being applied by the EO 279 OC and make recommendations for aligning				■								<i>Sr. PIDS, TCGI STTA</i>	Revised creditworthiness criteria adopted by EO 279 OC

MAJOR TASKS	Phase 1: Year 1										Status	Responsibility (L=Lead)	Expected Outputs
	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec				
criteria with internationally accepted credit rating standards and process.													
Host workshop with EO 279 OC to review and agree on action plan for adopting a revised credit classification process												Sr. PIDS	Workshop with EO 279 OC
Provide continued support to EO OC for implementation of Action Plan												Sr. PIDS	LWUA financing policies consistent with rationalization guidelines
Test the use of credit screening guidelines on two water utilities applying for PWRF loans												TCGI	Credit screening of 2 water utilities applying for PWRF loan
<b>3.3 Prepare PWRF Transition to Greater Private Sector Participation</b>													
Continually review and introduce enhancements to the PWRF structure												Pantillano (L) + Team	Enhanced PWRF structure
Conduct analysis and plan to transition PWRF to pooled bond financing												Pantillano (L) + Team, Johnson	Analysis and recommendations on the shift to pooled bond financing
<b>3.4 Facilitate provision of incentives to PFIs for lending to the sector</b>													
Develop analytic study with recommendations on including water/sanitation projects for agri-agra eligibility												Sr. PIDS(L)+STTA: Sol Castro	Position paper for Central Bank
Support DOF's review and presentation to BSP												Sr. PIDS	
<b>3.5 Prepare business plan framework for utilities</b>												Sr. PIDS (L) + ST TA; deVera (4 weeks)	Business plan framework for water utilities

MAJOR TASKS	Phase 1: Year 1									Status	Responsibility (L=Lead)	Expected Outputs
	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec			
<i>3.6 Design PWRF small grants program</i>											<i>Porciuncula (L)+ Administrative Specialist/ Mendoza</i>	Small Grants Plan
<b>Component 4: General PWRF Program Support</b>												
<i>4.1 Provide technical secretariat support to the PWRF Steering Committee, the Technical Working Group, and the Working Group that will be convened as a result of the MOU for Implementation</i>											<i>Porciuncula (L)+ Team</i>	Technical secretariat support to PWRF Committees
<i>4.2 Provide overall support to USAID's reporting, advocacy, and collaboration with JBIC on the PWRF</i>											<i>Porciuncula(L)+ Team</i>	Overall program support to USAID and to the USAID/JBIC collaboration
<i>4.3 Prepare PWRF website</i>											<i>Mendoza (L)+ Team</i>	PWRF website