



Mobilizing Private Sector Funds to the Water Supply Sector Through the Philippine Water Revolving Fund (PWRF)

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Presented to the Technical Workshop on Project Preparation
for Transformational Climate Resilience Water Concepts in Asia

Date: October 15-16, 2018

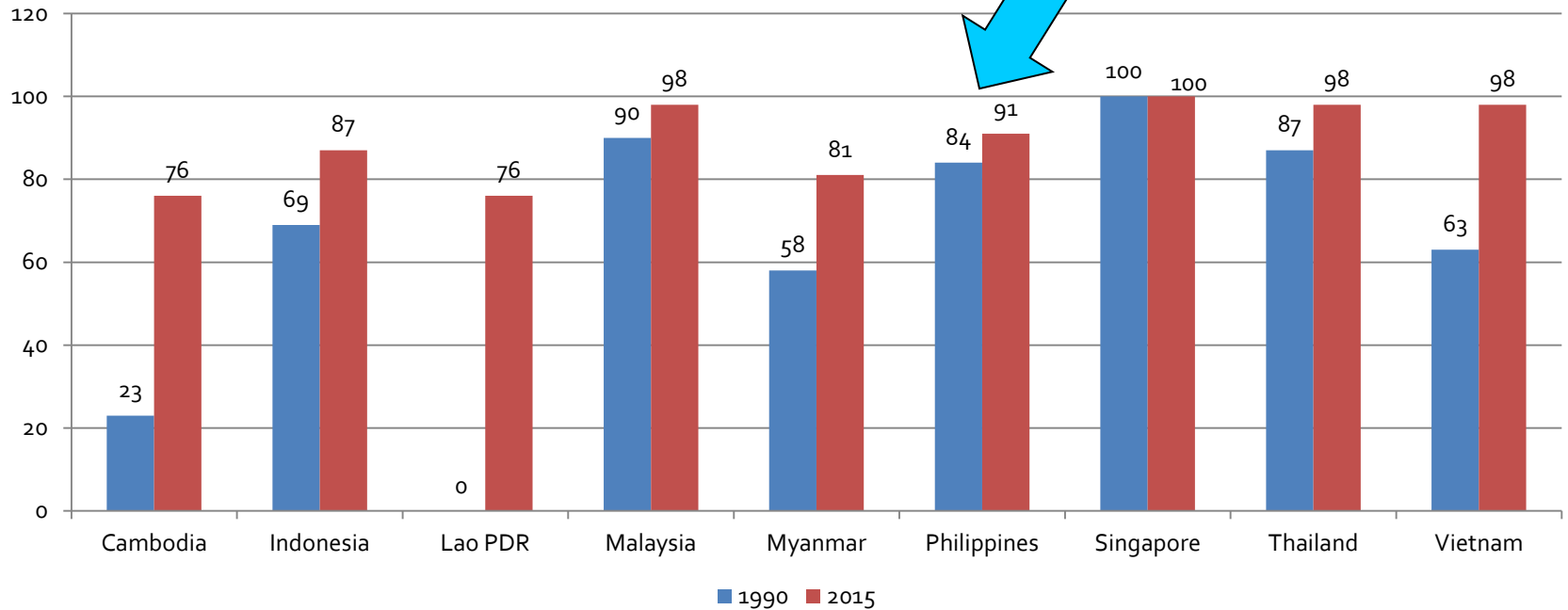
Venue: Asian Development Bank

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 - A. Drivers for PWRF Development
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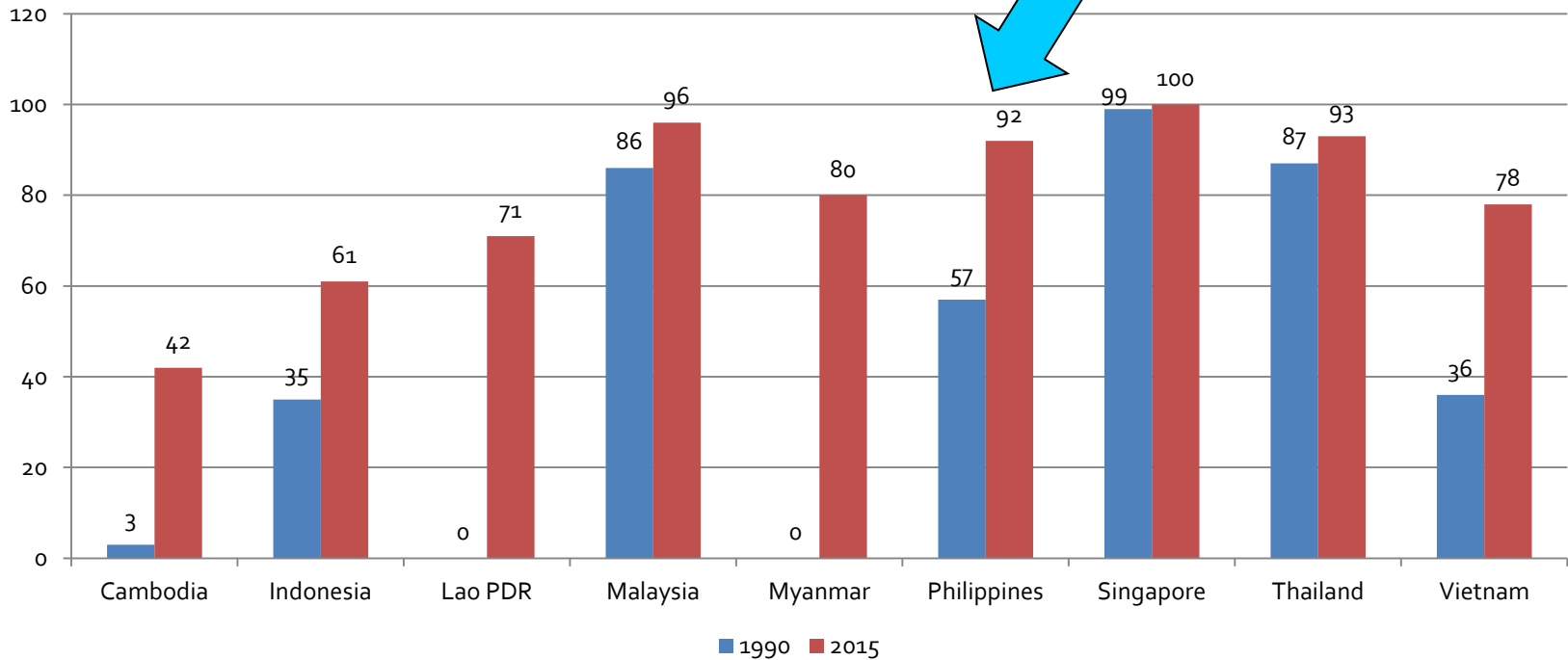
I. Overview of Water Supply & Sanitation Sector in the Philippines

ASEAN Population with Access to Safe Drinking Water (%)



- Philippines increased its access to safe drinking water, from 84% in 1990 to 91% in 2015
- However, compared to countries similar to size and population, the Philippines is still behind Thailand and Vietnam, both at 98% and a little ahead of Indonesia (87%) in terms of water access

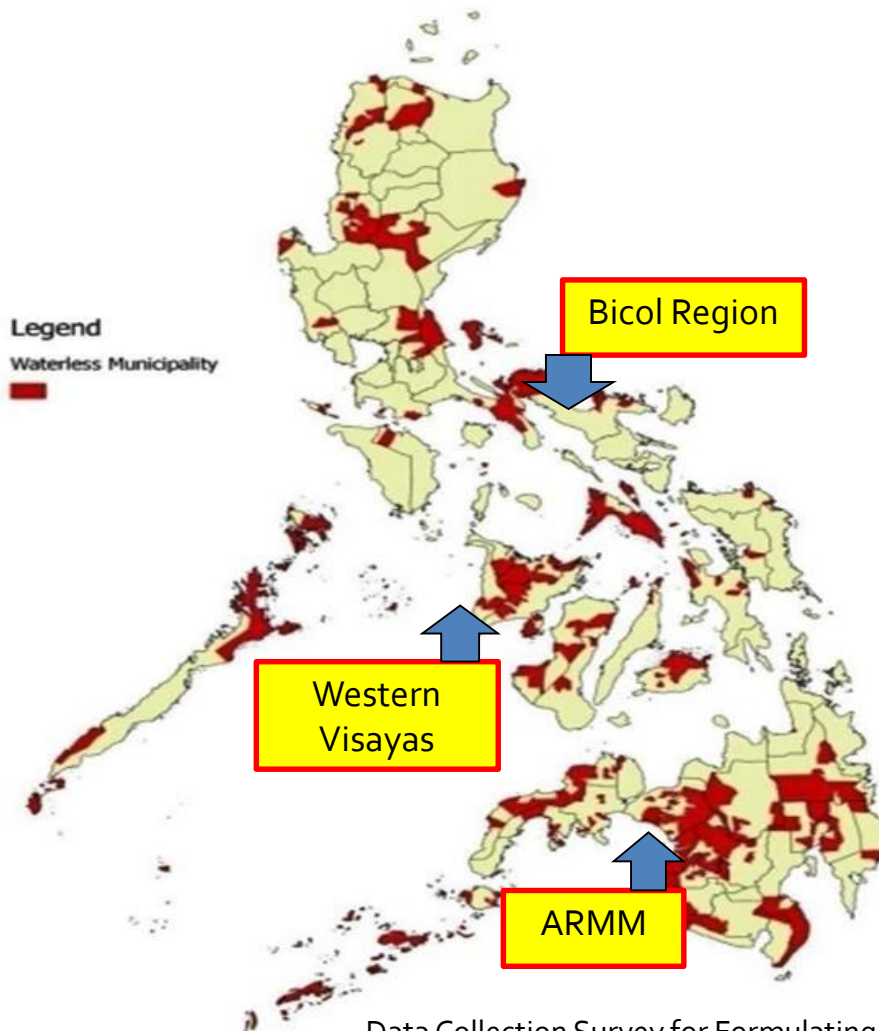
ASEAN Population with Access to Sanitation Facilities (%)



- Philippines' MDG target for access to sanitation was at 83.8% by 2015 and has already been achieved at 92%
- As per MDG definition, "access to improved sanitation" is defined as "proportion of people using basic sanitation or toilets"

Source: UN-WHO Joint Monitoring Programme (JMP) Report 2015

Map of Waterless Municipalities in Philippines



- 332 municipalities remain waterless (around 22% of total)
- “Waterless municipalities” are defined as municipalities with less than 50% water supply service coverage
- ARMM has the highest number of waterless municipalities at 87; followed by Western Visayas (40) & Bicol Region (25)

Number of Water Service Providers (WSPs) in the Philippines

Management Type	Total No. of WSPs	Per Cent Distribution
Water Districts	569	2%
LGU-Run Utilities	4,108	17%
BWSA/RWSA/Cooperative/ Unnamed Water Service Providers	15,938	66%
Others	3,533	15%
TOTAL	24,148	100%

Legend: BWSA/RWSA – Barangay/Rural Water & Sanitation Associations

Source: National Water Resources Board (NWRB), Listahang Tubig, Infographics (October 2014 to May 2015)

- Low awareness on importance of environment in general; water & sanitation in particular & linkage with other sectors
- Fragmented institutional set-up; weak coordination & institutional capacities
- Weak governance, lack of enforcement (manpower constraint; limited knowledge of laws/policies; fund limitation)



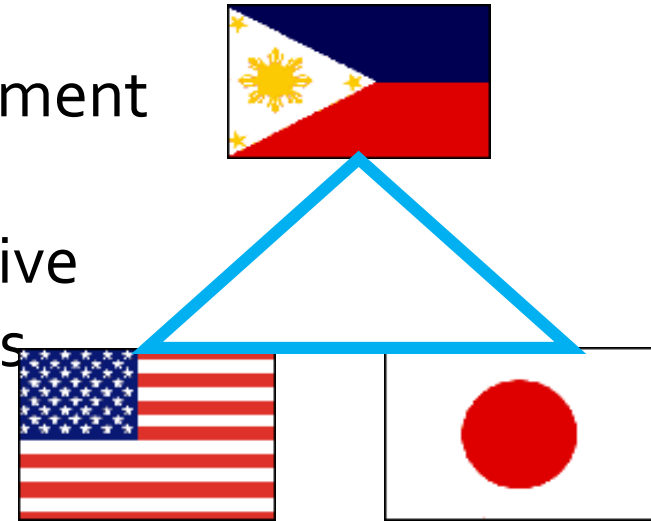
- Financial issues (preference of local government units (LGUs) to invest in vote getting type of projects; preference for grant assistance; inability to meet loan requirements)
- Poor reporting & monitoring of data
- Lack of updated data on environmental/water resources



II. Development of the Philippine Water Revolving Fund (PWRF)

A. Drivers for PWRF Development

- World Summit for Sustainable Development held September 2002 where US-Japan launched Clean Water for People Initiative to accelerate efforts to achieve the UN's Millennium Development Goal (MDG) targets for water supply & sanitation (WSS) sector



- Executive Order 279 (2004): Support Government Financing Policy to institute financing reforms for WSS sector; shift financing of creditworthy utilities to market & cost-based lending (e.g., banks) ; promote private sector participation

➤ Republic Act 9275 (2004): Support for implementation of Clean Water Act (CWA) or Comprehensive Water Quality Management

➤ Huge funding gap for WSS sector

➤ Priority placed by the administration on water supply & sanitation (WSS) sector & encouraging private sector participation



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- **Leverage** official development assistance (ODA) funds with funding from private financing institutions (PFIs)
- Develop an **innovative financing mechanism acceptable to PFIs** but at the same time **affordable** through **blending of funds** to water supply & sanitation (WSS) service providers
- Develop financing mechanism **with revolving capacity**

C. Design Considerations

Market Situation...

- PFIs are not active or have no experience in lending to water supply projects of water districts & local government units (WDs/LGUs)
- PFI lending rates are floating/variable & higher compared to government financial institutions (GFIs) & clients prefer fixed rate
- PFI tenor ranged from 5-7 years only but requirements of water supply projects is minimum of 15 years
- Water service providers' (WSPs such as WDs/LGUs) funding is mainly sourced from government (LWUA, GFIs), donor funds & revenues from customers
- Operationally, WDs rely on revenues only while LGU-run water utilities are not ring-fenced & rely on internal revenue allotment (IRA)

C. Design Considerations

Government Policy...

- Financing (EO 279) and environmental reforms (RA 9275, CWA) are in place
- No government grant available nor can government borrow money to capitalize a reserve fund
- Government not keen on creating new institution

Consultations among relevant stakeholders...

- Consultations undertaken among Government of the Philippines (*through Department of Finance [DOF], government financial institutions [GFIs, LandBank & DBP], National Economic & Development Authority [NEDA]*) PFIs, USAID and JICA
- USAID and JICA commissioned studies (demand & feasibility) to establish viability of a full-scale revolving fund that will mobilize private sector funds



Testing the waters...

- Signing of **Memorandum of Understanding (MOU)** among USAID, JICA, DBP, LGUGC to pilot test the **Municipal Water Loan Finance Initiative (MWLFI)**
- Road shows conducted in areas with potential water supply projects
- **Challenges** encountered include:
 - MWLFI offered a higher blended interest rate
 - Resistance from WSPs in having to deal with more parties (DBP & PFI)
 - Resistance from DBP branch heads to the participation of private banks
 - Lack of interest of some WSPs to avail of MWLFI package
 - Some pipeline projects were purely for refinancing but MWLFI intention is to include new investments



C. Design Considerations

Testing the waters...

- Candidate WSP, ***Metro Iloilo Water District (MIWD)*** was identified; due diligence activities initiated; & high level negotiations held; transaction took over a year to complete
- Under the MWLFI MOU, idea was to finance MIWD account through an ongoing ***JICA-assisted two-step loan to DBP – Environmental Infrastructure Support Credit Project Phase II*** (EISCP II, Loan Agreement No. PH-P199) but did not materialize...
- Instead, DBP use its own funds with intention to refinance cost from forthcoming JICA loan as the above two-step loan expired in March 2006 when negotiations with MIWD were concluded



C. Design Considerations

Testing the waters...

- Final configuration of MWLFI loan to MIWD:

Total Loan Amount = PhP 788 Million (15% rehabilitation; 85% refinancing)

DBP Share = PhP 591 Million (75%)

PFI Share (Phil. National Bank [PNB]) = PhP 197 Million (25%)

Blended interest rate = 10.5%

Guarantee fee paid by PFI = 1.16%

Tenor of DBP loan = 18 years (inclusive of 2-year grace period)

Tenor of PFI loan = 7 years (inclusive of 2-year grace period)



Testing the waters...

- Lessons from the pilot implementation...
 - In an environment of competing lending institutions, PWRP will not succeed if it will offer higher interest rates that are more aligned to the market rather than cost-based
 - Hard sell for all parties & it ran the risk of not proceeding
 - Deal was substantially watered down with LWUA limiting refinancing of existing loans of WDs to 49% & charging a pre-termination fee of 3%; limits leveraging of concessional funds
 - MIWD had to deal with many parties as there were no common set of guidelines and procedures among lenders



Testing the waters...

- Lessons from the pilot implementation...
 - Poor incentive to most stakeholders – same amount of work for DBP using usual two-step loan but giving up 25% of the deal to PFIs
 - Reluctance of borrower to borrow on less than favorable terms that those offered to less creditworthy customers who by virtue of their lack of creditworthiness are entitled to access traditional concessional facilities; moral hazard issue
 - Strong oversight role of DOF & NEDA needed on financing policy between GFIs & non-bank lending institution (e.g. LWUA) that is consistent with what national policy aims to achieve



C. Design Considerations

Timeline

2002	2003	2004-2005
<ul style="list-style-type: none"> ❖ World Summit for Sustainable Development ❖ Clean Water for People's Initiative ❖ Policy reforms in Philippines on financing & comprehensive water quality management 	<ul style="list-style-type: none"> ❖ Consultations initiated among Philippine (Department of Finance [DOF], LandBank, Development Bank of the Philippines [DBP]); USAID, LGUGC & JICA; continued until the Loan Agreement between DBP & JICA was signed in 2008 	<ul style="list-style-type: none"> ❖ Analysis of Constraints to Mobilizing Private Sector Financing for Water Supply & Sanitation Projects commissioned by USAID ❖ MOU for Municipal Water Loan Finance Initiative (MWLFI) signed to pilot test a PWRP account ❖ Road shows conducted to identify possible MWLFI borrowers ❖ JICA Participation in World Economic Forum Financing for Development to present PWRP concept

C. Design Considerations

Timeline

2006

- ❖ The PWRF Revolving Fund Design & Implementation Framework commissioned by USAID
- ❖ Special Assistance for Project Formulation for PWRF commissioned by JICA to verify feasibility & establish demand for the facility
- ❖ Pilot testing of MWLFI account through Metro Iloilo Water District (MIWD)

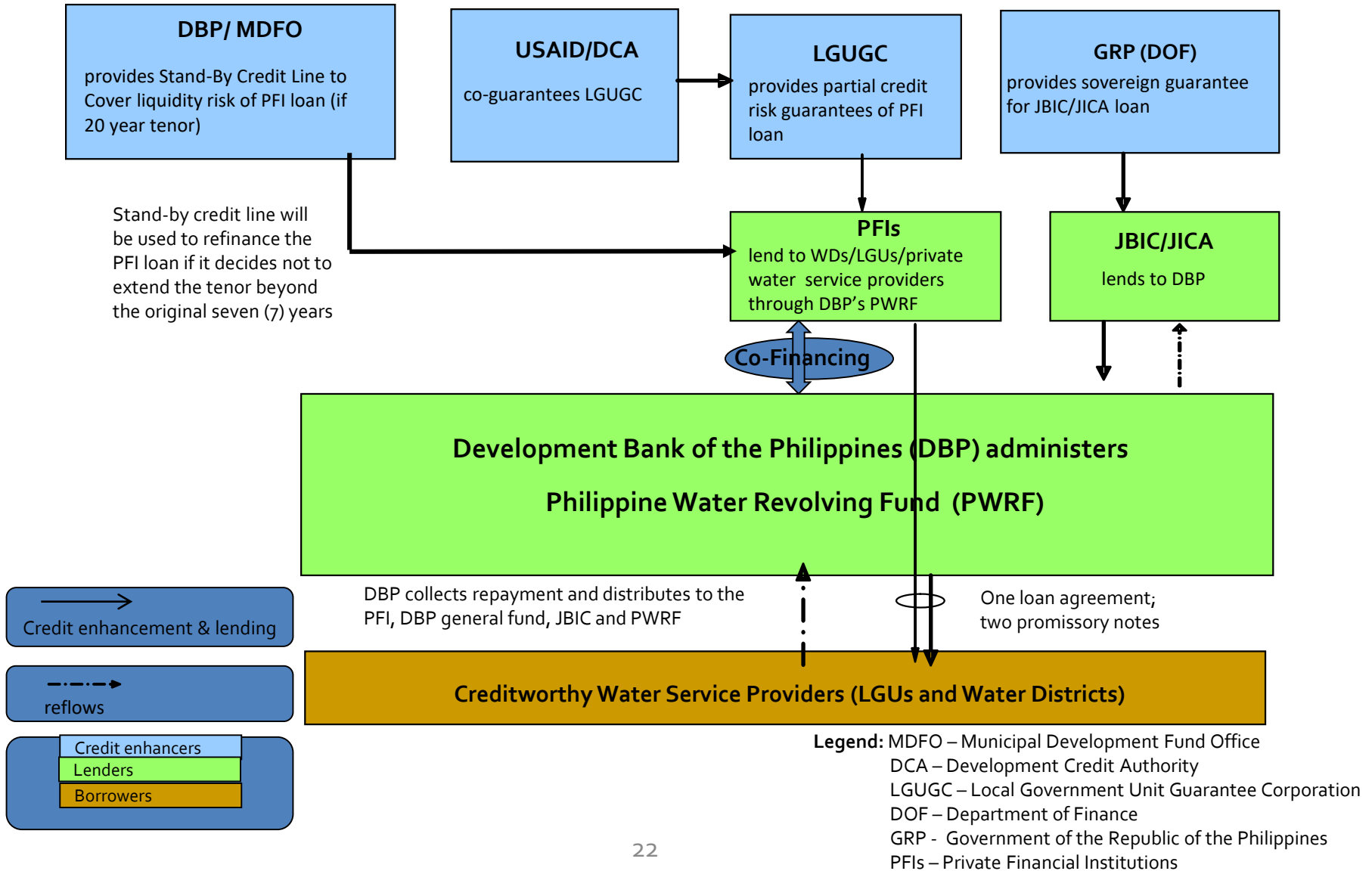
2007

- ❖ Continued consultations among PWRF stakeholders conducted among USAID, JICA, DBP, LGUGC, DOF, NEDA

2008-2017

- ❖ Appraisal of Environmental Development Project (EDP) where PWRF was integrated
- ❖ Signing of Loan Agreement in Sept. 2008 between DBP & JICA for EDP where PWRF scheme was integrated
- ❖ To address & resolve implementation issues: (a) regular PWRF Steering Committee (SC) meetings; and (b) Project Implementation Review (PIR) meetings were organized by USAID & JICA, respectively

D. PWRF Financing Structure



Key Features of PWRF

- Blended ODA & private financing to lower rates & introduce PFIs to WSS sector
- Liquidity cover to PFIs to address mismatch in tenor
- Credit risk enhancement provided by a local guarantee agency (*LGU Guarantee Corporation*), backed by a Development Credit Authority (DCA) co-guarantee through USAID
- Revolving feature; ring-fenced revolving account from the principal repayments of sub-borrowers to ensure sustainability

Complementary & catalytic role of USAID and JICA collaboration



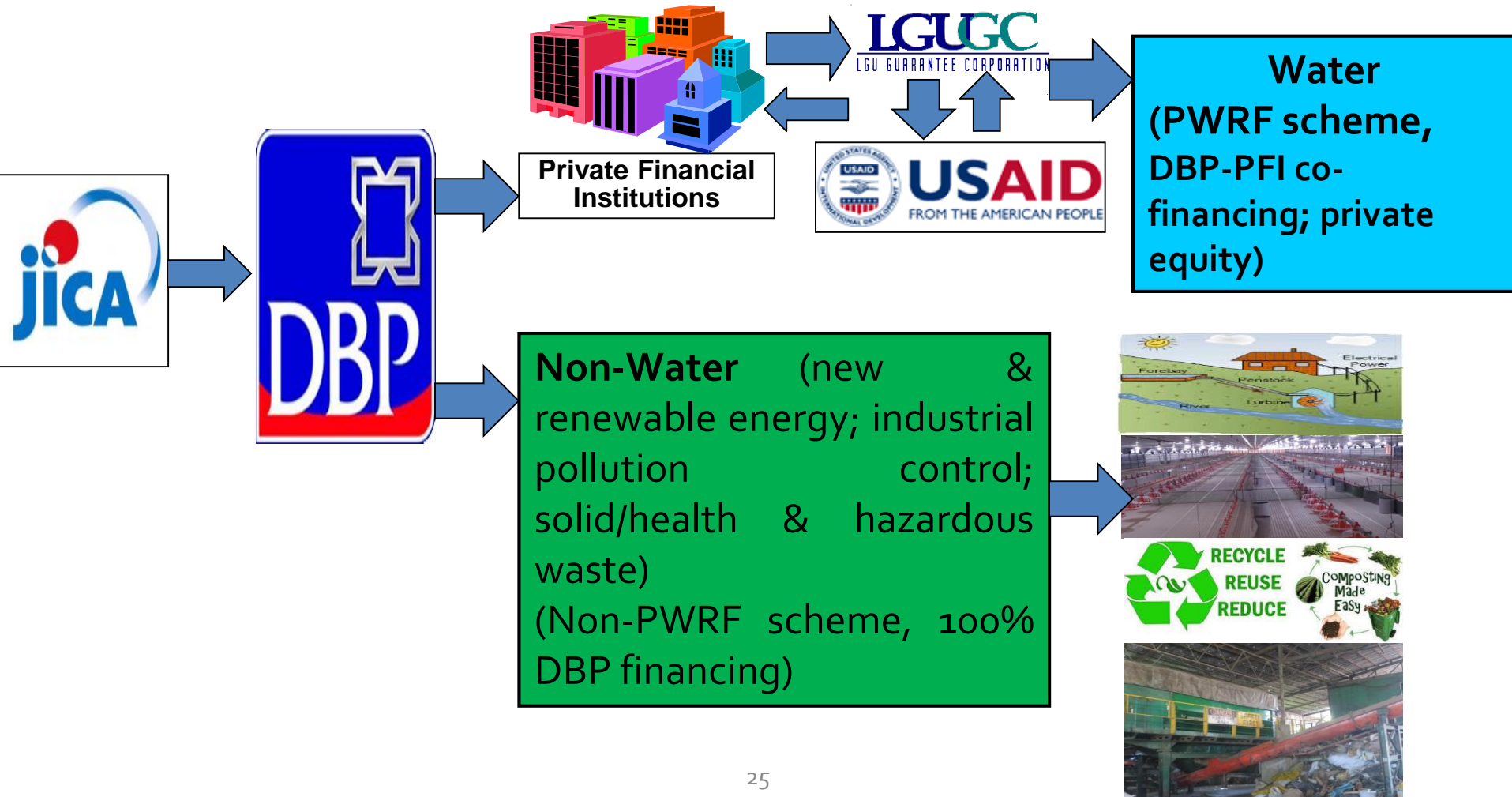
- Institutional support, coordination with PFIs and other stakeholders
- Assistance in project development
- Assistance in policy reform
- Utility reform (ring-fencing, improvements in business planning of water service providers, performance contracting)
- Training and capacity enhancement for PFIs (project appraisal), service providers such as water districts (WDs), local government units (LGUs), private sector utility providers



- Provision of ODA funds to DBP for re-lending to water supply & sanitation service providers through a two-step loan called Environmental Development Project (EDP, Loan Agreement No. PH-P243)
- Long tenor and grace period which enabled liquidity cover to PFI loans
- Championed and introduced an innovative co-financing facility between DBP and PFIs
- Technical assistance

Key Features of PWRF

Integration of PWRF in JICA's Two-Step Loan called Environmental Development Project (EDP)



Terms & conditions of EDP-PWRF facility with DBP



- ***Tenor:*** 20 years inclusive of maximum 3 year grace period
- ***Financing mix:*** initially 75% JICA/DBP funds and 25% PFI funds
- ***Interest rate:*** Fixed, benchmarked against a reference rate + interest spread (1-3%) depending on credit risk of borrower
- ***Equity requirement:*** Minimum of 10% based on total project cost; may be waived on a case-to-case basis
- ***Take-out feature:*** offered to borrowers who cannot afford the PFIs' short tenor (minimum term of 7 years); DBP & PFIs have option to be taken out; extend the loan or receive a balloon payment

Credit risk guarantee for PFI portion of loan



- LGUGC can provide credit risk guarantee to PFIs of up to 85% of PFI loan exposure; PFIs are charged a 1% guarantee fee
- USAID-DCA will issue a co-guarantee to LGUGC guarantee of PFI loan covering up to 50% of LGUGC's exposure



Private Sector Participation Guidelines

- PWRF recognizes the dynamic nature of the financial markets and the revolving requirements of water service providers in general
- Private sector participation was defined as both private equity and debts or a combination of both

Private Sector Participation Guidelines

❖ *Via debt to water service providers (WSPs)*

➤ *DBP-PFI co-financing*

➤ *PWRF re-lending to a PFI* – PFI uses its own fund (at least 25%) & takes on risk of its borrower; borrows rest from PWRF facility; DBP imposes a cap on interest spread that PFI can impose on DBP-funded portion

➤ *Full PFI financing with stand-by loan agreement* – PFI provide 100% of project loan financing but if its loan term cannot match payback period of project; PFI secures a stand-by loan from DBP to refinance its loan to WSP

❖ *Via equity to private WSPs*

➤ *Direct equity in a private corporation/service provider or a joint venture* – DBP loan exposure shall be up to 75% of total project cost or PhP 250 Million, whichever is lower; private investor share is minimum of 25%



E. PWRF Financing Milestones under Environmental Development Project

A. Environmental Development Project (EDP) Profile

Loan Agreement Signing	September 30 ,2008		
Loan Expiry Date	January 7, 2017 (with 1-year extension)		
Implementing Agency	Development Bank of the Philippines (DBP)		
Loan Amount & Interest Rate	Total	JPY 24, 846 Million	
	Water	JPY 7,600 Million a/	1.40%
	Non-Water Consulting Services	JPY 17,000 Million b/	0.65%
		JPY 246 Million	0.01%
Disbursement Performance	99.72%		

a/ Water category adopted PWRF financing mechanism.

b/ Non-water category (include new & renewable energy [NRE]; industrial pollution control [IPC]; solid/health care/hazardous waste management [SHCHWM]) adopted usual two-step loan financing mode of JICA.



E. PWRP Financing Milestones under Environmental Development Project

B. PWRP Financing Mechanism Milestones

Initial loan allocation	JPY 1.5 Billion (6% of total loan allocation)
Final amount disbursed	JPY 7.6 Billion (31% of total loan allocation)
Number of sub-projects or accounts generated	17 (23% of total accounts)
On-lending interest rate	Ranged from a low 6% to a high of 9.5%
Participating private financing institutions (PFIs)	Bank of the Philippine Islands (BPI) Security Bank Corporation (SBC)
NEDA Good Practice Award of 2017	<ul style="list-style-type: none">▪ Mainstreamed environmental, social, climate change considerations in project evaluation & monitoring; DBP's Environmental Performance Monitoring (EPM) system adopted in all DBP-funded projects

NEDA - National Economic Development Authority

PWRF SUB-PROJECT PROPONENT: Puerto Princesa Water District



3,000 cubic meter reservoir



25 MLD Treatment Plant



Infiltration Gallery



Impounding Facility

Description: Rehabilitation of existing facilities and expansion of service coverage
Total Project Cost: PhP 536.28 Million
DBP Loan: PhP 361.99 Million (68%)
PFI Share: PhP 120.66 Million (22%)
Equity Share: PhP 53.63 Million (10%)
PFI Partner: Bank of the Philippine Islands (BPI)



PWRF SUB-PROJECT PROPONENT: Boracay Island Water Company



Settling tank



Submarine pipeline



Treatment Plant



Reservoir

Description: Rehabilitation and expansion of water supply and sewerage systems

Total Project Cost: PhP 1,631.1 Million

DBP Loan: PhP 750 Million (46%)

PFI Share: PhP 250 Million (15%)

Equity Share: PhP 631.1 Million (39%)

PFI Partner: Security Bank





PWRF SUB-PROJECT PROPONENT: Laguna AAA Water Corporation



Matang Tubig Spring Source Facility



Settling Tank

Description: Source development;
expansion & rehabilitation of pipeline
Total Project Cost: PhP 2,149 Million
DBP Loan: PhP 1,333 Million (62%)
Equity: PhP 816 Million (38%)



PWRF SUB-PROJECT PROPONENT: Cebu Manila Water Development Corporation



Surface water source facility

Description: Construction of 35 MLD bulk water supply system

Total Project Cost: PhP 1,225.2 Million

DBP Loan: PhP 751.6 Million (61%)

Equity: PhP 473.6 Million (39%)



Water treatment facility

DBP Entry:

Institutionalizing Environmental,
Social and Climate Change
Considerations in Project
Evaluation and Monitoring in DBP's
Credit Process



Php 3.3 Billion

JPY 7.6 Billion

Operation Indicator	Achieved
Water production (m3/yr)	85,193,485
Pipe network (km)	1,827

Effect Indicator	Achieved
Service connection (no.)	216,872
Reduction in NRW (%)	14.37
Water conserved (m3/yr)	11,656,274



Source: DBP

Note: Pictures of EDP sub-projects & awarding of NEDA good practice award are courtesy of DBP

F. Challenges, Solutions And Some Conclusions

CHALLENGES

➤ ON POLICY AND INSTITUTIONAL BOTTLENECKS

- ❖ Continuing institutional & regulatory fragmentation of the sector; no consolidated or updated data on WSS sector
- ❖ Resistance to paradigm shift/weak enforcement of new financing policy
- ❖ Difficulty of water districts (WDs) to secure waiver which entails that WDs secure prior written consent from LWUA if they borrow from other sources
- ❖ Competition between DBP & LWUA; between DBP & PFIs
- ❖ Need to build robust pipeline of bankable WSS projects and continuing information, education & communication (IEC) on market-based financing particularly WDs/LGUs

F. Challenges, Solutions And Some Conclusions

CHALLENGES

➤ ON MARKET CONDITIONS

- ❖ Market liquidity & low interest rate regime
- ❖ More effort needed to build DBP and PFI partnership to address not only the investment requirements but also developmental impacts of WSS sector
- ❖ PFI willingness to finance WSS projects on their own; matching DBP terms & conditions in some cases
- ❖ Little interest of some PFIs to co-finance small projects (e.g < PhP 200 Million)
- ❖ Need to develop other credit enhancements: credit risk & liquidity mechanisms (e.g., guarantee scheme, ring-fencing & revolving feature of funds) to attract more private sector involvement

F. Challenges, Solutions And Some Conclusions

SOLUTIONS

- ❖ Donor meetings organized to drum up support on policy reforms on WSS sector and PWRP facility
- ❖ Positive engagement and dialogues with LWUA undertaken by DBP, JICA, USAID & LGUGC to address waiver issue
- ❖ DBP adjustments of its terms and conditions (reduction in interest rate/spreads; longer tenor); through consulting component of EDP, more intensive marketing/roadshows of PWRP facility conducted
- ❖ USAID support & JICA assistance in project development for selected water service providers that are potential PWRP borrowers
- ❖ Regular coordination meetings conducted between and among JICA, USAID and DBP

F. Challenges, Solutions And Some Conclusions

SOME CONCLUSIONS

- ❖ *Modest contribution of PWRP facility in leveraging public resources with private sector funds; experience was challenging but it can be done!*
- ❖ Need for a ***champion*** to push innovative financing schemes
- ❖ PWRP served ***as a stimulus to encourage private sector lending***; but continuing this innovative financing scheme depends on efficient enforcement of policy reforms & market conditions
- ❖ ***Government commitment*** to policy implementation & emphasis on ***development initiatives & objectives is critical***
- ❖ ***Blended ODA & private sector financing*** can result to lower rates that can ***benefit end-users***

SOME CONCLUSIONS

- ❖ ***Credit risk and liquidity enhancements*** can provide incentives to encourage private sector participation
- ❖ Through efforts of all stakeholders, growing interest of water service providers on accessing PFI funds (traditionally financed by GFIs) has been noted to a certain extent
- ❖ Fostered ***awareness among PFIs*** of lending opportunities in WSS sector ***but*** as they gained experience, also gave them option to finance projects on their own without co-financing with DBP

F. Challenges, Solutions And Some Conclusions

SOME CONCLUSIONS

- ❖ Developing ***workable public-private partnership (PPP) models*** not only in financing but also in operations & maintenance (O & M) in WSS facilities is possible
- ❖ ***Complementation of donor activities*** (e.g. USAID and JICA) which provided opportunities for innovative project concepts and out-of-the-box solutions on assistance package takes time given comparative advantage of each

F. Challenges, Solutions And Some Conclusions

“Don’t limit your challenges. Challenge your limits.”

“Sometimes overcoming a challenge is as simple as changing the way you think about it.”

Anonymous

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Thank you for your attention...