Program Information Document (PID)

Concept Stage | Date Prepared/Updated: 10-Dec-2020| Report No: PIDC30638

BASIC INFORMATION

A. Basic Project Data

Country	Project ID	Project Name	Parent Project ID (if any)
Philippines	P175008	Philippines First Financial Sector Reform Development Policy Financing (P175008)	
Region	**Estimated Board Date**	**Practice Area (Lead)**	**Financing Instrument**
EAST ASIA AND PACIFIC	Jul 14, 2021	Finance, Competitiveness and Innovation	Development Policy Financing
Borrower(s)	**Implementing Agency**		
Republic of the Philippines	Department of Finance		

Proposed Development Objective(s)

The program development objective of this programmatic operation is to support financial sector reforms that will support the Government of the Philippines in achieving a resilient, inclusive and sustainable financial sector.

Financing (in US$, Millions)

SUMMARY

Total Financing	200.00

DETAILS

Total World Bank Group Financing	200.00
World Bank Lending	200.00

Decision

The review did authorize the preparation to continue

B. Introduction and Context

Country Context

1. **The proposed Development Policy Loan (DPL) supports the Government of the Philippines in achieving a resilient, inclusive, and sustainable financial sector to enable a more inclusive green recovery from the Coronavirus Disease 2019 (COVID-19) pandemic.** The proposed operation is the first in a programmatic series of two IBRD operations that aims to support the Government of the Philippines in: i) strengthening financial sector stability and resilience, ii)

expanding financial inclusion for individuals and firms, and iii) catalyzing disaster risk and sustainable finance.

2. **Prior to the pandemic, sound macroeconomic fundamentals and a commitment to transformational structural reforms were accelerating inclusive growth in the Philippines.** The economy grew by an average of 6.3 percent per year in 2010-2019, as a result of strong macroeconomic fundamentals, a supportive policy environment, favorable external conditions, and the cumulative effects of structural reforms. In recent years, the government strengthened its commitment to structural reforms, focusing on areas of competition and competitiveness, and accelerating its investment in human and physical capital, while remaining committed to prudent fiscal management. This contributed to an acceleration in the pace of poverty reduction, with the poverty incidence falling from 26.6 percent in 2006 to 16.6 percent in 2018, with the decline in poverty accelerating between 2015 to 2018.[1]

3. **However, the hard-won gains in poverty reduction are being unraveled by the unprecedented health and economic crisis posed by the COVID-19 pandemic.** The COVID-19 outbreak in March, forced the economy to a near halt as the government took swift and strong measures in an effort to flatten the infection curve. This caused severe disruptions in domestic economic activity, which combined with a similarly choked global economy led to the sharpest GDP contraction in over three decades.

4. **To mitigate the impact of the pandemic, the BSP has accelerated its accommodative policy stance and has taken extraordinary measures to support the government's COVID-19 response.** After peaking at 5.2 percent in 2018, headline inflation decelerated to 2.5 percent in 2019 and the first eight months of 2020, within BSP target range giving space for accommodative monetary policy. To mitigate the impact of the COVID-19 outbreak, the BSP reduced the key policy rate by a cumulative 175 basis points (bps) to 2.25 percent, and the reserve requirement by 200 bps to 12.0 percent as of October 2020. The BSP has also adopted other regulatory measures to facilitate online transactions and the monetary authorities have taken preemptive actions to minimize the economic fallout of the COVID-19 pandemic.[2]

5. **The financial system, while smaller than Asian peers, has broadly withstood the impact of COVID-19.** In terms of financial depth, access and efficiency, Philippines's financial development is above average among emerging markets but on the lower side among emerging Asian economies . The bank capital adequacy ratio (CAR) has been stable at about 15 percent, during the past decade, though lower than other Asian emerging markets[3]. The banking sector nonperforming loans ratio (NPLs) at 2.8 percent at end August 2020, though higher compared to 2.0 percent prior to the onset of COVID-19, are much below the level following the Asian Financial Crisis (AFC) of 1997-98. The key risks to financial stability arise from significant interlinkages between banks and non-financial corporates through mixed conglomerate ownership structures and large lending exposures.

Relationship to CPF

6. **The reforms supported by this DPL series are fully aligned with the Country Partnership Framework (CPF).** The 2019-2023 CPF focuses on three development objectives: (i) job creation; (ii) improving human capital; and (iii) building resilience to conflict and natural disasters, which remain relevant in the current context. The cross-cutting themes

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[1] After remaining stubbornly high between 2006 to 2012, the poverty incidence fell from 23.3 percent in 2015 to 16.6 percent in 2018, according to national poverty line reported by the Philippine Statistics Authority.

[2] The BSP (i) relaxed know-your-customer (KYC) requirements to facilitate the delivery of social protection programs; (ii) digitized some operations and waived types of penalties and fees for foreign exchange transactions; (iii) suspended charges on electronic payment and financial services fees for six months; (iv) provided relief measures to micro, small, and medium enterprises by temporary reducing the credit risks assigned to their loans; and assigning a 0 percent risk weight for their guaranteed loans, among others.

[3] CAR stood at 22.5 percent in Indonesia, 18.4 percent in Thailand, and 17.7 percent in Malaysia. Source: IMF Financial Soundness Indicator; latest available data.

include governance and digital transformation. Financial sector reforms contribute to these objectives across pillars, by improving access to finance by individuals and firms, bridging the gaps in human capital development with accessible and affordable financial services (e.g. digital payments, insurance) and strengthening resilience with disaster risk finance and climate change and green finance.

C. Proposed Development Objective(s)

The program development objective of this programmatic operation is to support financial sector reforms that will support the Government of the Philippines in achieving a resilient, inclusive and sustainable financial sector.

This programmatic DPL series is structured around the following three pillars and set of objectives:

(i) **Pillar A supports reforms aimed at strengthening financial sector stability and resilience**, with the objective of supporting the authorities in addressing legal, regulatory and supervisory gaps in financial sector and increasing the availability of long term finance.

(ii) **Pillar B supports reforms aimed at expanding financial inclusion for individuals and firms**, with the objective of supporting the authorities in accelerating reforms aimed at promoting innovative financial services, building consumer trust in the financial sector, and improving micro, small and medium enterprises access to finance.

(iii) **Pillar C supports reforms aimed at catalyzing disaster risk and sustainable finance**, with the objective of supporting the authorities in implementing reforms aimed at enhancing public-private partnership based financial instruments for disaster risk financing and greening the financial sector to support sustainable economic recovery from COVID-19 pandemic.

Key Results

7. **The expected outcomes of policy actions supported under the program includes** strengthening financial sector stability and resilience, expanding financial inclusion for individuals and firms and catalyzing disaster risk and sustainable finance.

D. Concept Description

8. **This proposed operation supports reforms aimed at strengthening the resilience of the financial sector to withstand the risks arising from the COVID-19 crisis, while accelerating medium-term financial sector structural reforms to support sustainable economic recovery**. Importantly, the operation supports transformational reforms aimed at promoting innovative financial services by harnessing digital technologies, improving micro, small and medium enterprise access to finance by de-risking private commercial bank financing, and catalyzing sustainable finance by greening the financial sector. To achieve these objectives, the programmatic DPL series is structured around three reform pillars. The program of reforms proposed across the three pillars strongly complement each other to achieve the program development objective.

9. **This proposed program builds on strong analytical and advisory work on financial sector development and Government of the Philippines commitment.** The proposed reforms are informed by strong analytical and advisory work undertaken by the authorities, World Bank and other development partners, including the joint IMF-World Bank

Financial Sector Assessment Program (FSAP) Update 2020.

E. Poverty and Social Impacts, and Environmental, Forests, and Other Natural Resource Aspects

Poverty and Social Impacts

10. **The proposed DPL's prior actions associated with the reforms actions pose no adverse poverty and social impacts.** Rather, the direct and indirect impacts of the actions are likely to be positive. While poverty levels in the Philippines have declined over the years, they remain high and the government's socioeconomic policy agenda – which focuses on infrastructure, education, and health – seeks to address these challenges. The proposed operation will enable the financial sector to play an effective role in reducing inequalities, supporting green and inclusive economic recovery from the pandemic. This will be achieved through strengthening the resilience of the financial sector to withstand the effects of COVID-19, expanding financial inclusion for individuals and MSMEs, increasing access to catastrophe risk insurance and greening the financial sector.

Environmental, Forests, and Other Natural Resource Aspects

11. The DPF supports reforms towards a stable, inclusive and sustainable financial sector that can have an overall positive impact to the natural environment and contributes to the resilience of businesses and consumers.

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APPROVAL

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