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INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

PROGRAM DOCUMENT FOR A

PROPOSED LOAN

IN THE AMOUNT OF US\$400 MILLION

REPUBLIC OF THE PHILIPPINES

FOR THE

PROMOTING COMPETITIVENESS AND ENHANCING RESILIENCE TO NATURAL
DISASTERS SUB-PROGRAM 1 DEVELOPMENT POLICY LOAN

November 18, 2019

Macroeconomics, Trade and Investment Global Practice
East Asia And Pacific Region

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Republic of the Philippines
GOVERNMENT FISCAL YEAR
January 1 – December 31

CURRENCY EQUIVALENTS

(Exchange Rate Effective as of November 14, 2019)

Php50.68 = US\$1.00

ABBREVIATIONS AND ACRONYMS

ACH	Automated Clearing House	DA	Department of Agriculture
AMPLE- CGE	Agricultural Market Model for Policy Evaluation – Computable General Equilibrium	DBCC	Development Budget Coordination Committee
APEC	Asia Pacific Economic Cooperation	DBM	Department of Budget and Management
ARTA	Anti-Red Tape Authority	DBP	Development Bank of the Philippines
ASA	Advisory Services and Analytics	DENR	Department of Environment and Natural Resources
ASEAN	Association of Southeast Asian Nations	DOF	Department of Finance
ATI	Agricultural Training Institute	DOH	Department of Health
BIR	Bureau of Internal Revenue	DOTr	Department of Transportation
BOC	Bureau of Customs	DPL	Development Policy Loan
BOP	Balance of payment	DPWH	Department of Public Works and Highways
BPI	Bureau of Plant Industry	DRF	Disaster Risk Financing
bps	Basis points	DSWD	Department of Social Welfare and Development
BSP	Bangko Sentral ng Pilipinas	DTI	Department of Trade and Industry
BTMS	Budget and Treasury Management System	EAs	Engagement Areas
BTr	Bureau of the Treasury	ECT	Emergency Cash Transfer
CAT-DDO	Catastrophe-Deferred Drawdown Option	EIS	Environmental Impact System
CCAM- DRR	Climate Change Adaptation and Mitigation – Disaster Risk Reduction	EODB	Ease of Doing Business
CIT	Corporate Income Tax	FAO	Food and Agriculture Organization
CITIRA	Corporate Income Tax and Incentives Rationalization Act	FDI	Foreign Direct Investment
COA	Commission on Audit	FIES	Family Income and Expenditure Survey
CPF	Country Partnership Framework	FMI	Financial Market Infrastructure
CPI	Consumer Price Index	FOB	Free on board
CPS	Country Partnership Strategy	FSAP	Financial Sector Assessment Program
CSC	Civil Service Commission	FTE	Fiscal Transparency Evaluation
CTRP	Comprehensive Tax Reform Program	GAA	General Appropriations Act

GDP	Gross Domestic Product	OECD	Organization for Economic Co-operation and Development
GOCC	Government-Owned and Controlled Corporation	PCC	Philippine Competition Commission
GRS	Grievance Redress Service	PDO	Program Development Objective
GSIS	Government Service Insurance System	PDP	Philippine Development Plan
ha	Hectare	PEFA	Public Expenditure and Financial Accountability
IC	Insurance Commission	PFM	Public Financial Management
ICR	Implementation Completion Report	PhilHealth	Philippine Health Insurance Corporation
ICT	Information and communications technology	PhilMec	Philippine Center for Postharvest Development and Mechanization
ID4D	Identification for Development	PhilPaSS	Philippine Payment and Settlement System
IFC	International Finance Corporation	RA	Republic Act
IMF	International Monetary Fund	RCEF	Rice Competitiveness and Enhancement Fund
IRR	Implementing Rules and Regulation	RIA	Regulatory impact assessment
IT-BPO	Information Technology-Business Process Outsourcing	RRP	Reserve repurchase
KYC	Know Your Customer	RSBSA	Registry System for Basic Sectors in Agriculture
LBP	Land Bank of the Philippines	SCD	Systematic Country Diagnostic
LFS	Labor Force Survey	SME	Small and Medium Enterprise
MFD	Maximizing Finance for Development	SOE	State-owned enterprise
MT	Metric tons	SORT	Systematic Operations Risk-Rating Tool
NDRRM	National Disaster Risk Reduction and Management	SSS	Social Security System
NDRRMC	National Disaster Risk Reduction and Management Council	TA	Technical Assistance
NEDA	National Economic Development Authority	TESDA	Technical Education and Skills Development Authority
NFA	National Food Authority	TRAIN	Tax Reform for Acceleration and Inclusion
NGO	Non-governmental organization	U.S.	United States of America
NHTS-PR	National Household Targeting System for Poverty Reduction	VWR25	Vietnamese White Rice 25 percent
NPSA	National Payment Systems Act	WB	World Bank
NRPS	National Retail Payment System	WBG	World Bank Group
OBI	Open Budget Index	WTO	World Trade Organization

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REPUBLIC OF THE PHILIPPINES
PROMOTING COMPETITIVENESS AND ENHANCING RESILIENCE TO NATURAL DISASTERS SUB-PROGRAM 1
DEVELOPMENT POLICY LOAN

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The Philippines Promoting Competitiveness and Enhancing Resilience to Natural Disasters Sub-program 1 Development Policy Loan was prepared by a World Bank team led by Rong Qian, and comprising Lewis Hawke, Kevin Chua, Kevin Cruz, Roberto Galang, Farida Lasida Adji, Pablo Acosta, Sharon Piza, Isaku Endo, Frauke Jungbluth, Eli Weiss, Lesley Cordero, Benedikt Signer, Deanna Villacin, Natasha Beschoner, Jonathan Daniel Marskell, Maya Villaluz, Karen Lazaro, Ray Gomez, Yvette Camba, and Reinaluz Ona. The Team benefited from helpful comments and suggestions from Souleymane Coulibaly (Program Leader and Lead Economist) and Gabriel Demombynes (Program Leader). Fernando Blanco, Cecile Thioro Niang, and Tania Begazo were the peer reviewers. The team benefited from guidance from Mara Warwick (Country Director) and Ndiame Diop (Practice Manager). The team gratefully acknowledges the excellent collaboration of the Government of the Philippines.



SUMMARY OF PROPOSED FINANCING AND PROGRAM

BASIC INFORMATION

Project ID	Programmatic	If programmatic, position in series
P170052	Yes	1st in a series of 3

Proposed Development Objective(s)

The DPL series aim to support Government of the Philippines in: i) promoting competitiveness; ii) enhancing fiscal sustainability; and iii) strengthening financial resilience to natural disasters and climate change.

Organizations

Borrower: REPUBLIC OF THE PHILIPPINES

Implementing Agency: DEPARTMENT OF FINANCE

PROJECT FINANCING DATA (US\$, Millions)

SUMMARY

Total Financing	400.00
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DETAILS

International Bank for Reconstruction and Development (IBRD)	400.00
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INSTITUTIONAL DATA

Change and Disaster Screening

This operation has been screened for short and long-term climate change and disaster risks.

Overall Risk Rating

Substantial



Results

Indicator Name	Baseline (2018) *	Target (2022)
The gap between domestic and international price of rice calculated as domestic price – international price as percent of international price (in percent)	76	Less than 50
Doing Business Indicator “# of days to start a business”	13	Less than 8
Doing Business Indicator “# of procedures to start a business”	31	Less than 20
Use of the foundational ID	0	Bank account opening, civil service pension payments, and other pension payments
Share of electronic payment of transactions among all (retail) payments (in percent)	1 (2013)	More than 25
Budget utilization rate as measured by the ratio of current obligations to total current budget (in percent)	83 (2016)	Not lower than 88
Number of public financial systems integrated with BTMS	0	No less than 3
Number of national government agencies using BTMS for recording, accounting and reporting all their finances	2	No less than 50
Tax revenue as share of GDP (in percent)	14.7	More than 15.2
Share of public assets included in the asset registry for 5 key agencies (in percent)	0	More than 60
Number of agencies using the asset registry	0	More than 5
Share of companies complying with new reinsurance and catastrophe/property insurance reporting requirements and submitting required information using the new template (in percent)	0	More than 75
Number of pre-arranged or improved financial mechanisms for disaster response in place	2	More than 4

*unless otherwise indicated



IBRD PROGRAM DOCUMENT FOR A PROPOSED LOAN TO THE REPUBLIC OF THE PHILIPPINES

1. INTRODUCTION AND COUNTRY CONTEXT

- 1. This proposed Development Policy Loan (DPL) aims to support the government of the Philippines' ambition to boost inclusive growth, accelerate poverty reduction, and strengthen resilience.** The proposed operation, in the amount of US\$400 million, is the first in a series of three operations designed to support critical policy and institutional reforms to achieve the government's development objectives by: (i) promoting competitiveness, (ii) enhancing fiscal sustainability, and (iii) strengthening financial resilience to natural disasters and climate change. The proposed operation responds to a request from the government to support game-changing micro level reforms to expand Philippines' growth potential sustainably. While the Philippines has a robust macroeconomic framework and strong reform program, the government still faces increasing financial need, as global financing conditions are expected to tighten in the medium term. The government is committed to the effective implementation of reforms while maintaining fiscal sustainability with the financial and technical support from the World Bank.
- 2. The Philippine government has established a track record of prudent macroeconomic management and structural reforms which have led to strong economic growth and solid fiscal and external balances.** Since 2010, the Philippines registered its strongest and longest stretch of growth acceleration, becoming one of the best growth performers in the region: growth averaged 6.3 percent in 2010-18, second only to China among large economies in the East Asia and Pacific region. This robust growth reflects the country's continuing efforts to strengthen macroeconomic fundamentals, favorable external conditions, and the cumulative effects of structural reforms. The rapid growth contributed to poverty reduction, with poverty incidence falling from 26.6 percent in 2006 to 21.6 percent in 2015.¹ During the same period, growth also helped decrease inequality as the income of households in the bottom 40 percent of the population increased by 2.9 percent, compared to the average per capita income, which only rose by 1.6 percent.²
- 3. Despite this remarkable progress, more needs to be done to improve the inclusiveness of growth and enhance resilience to natural disasters and climate change.** Income inequality, although declining,³ remains stubbornly high in the Philippines and one of the highest in the region. This is because despite the rapid economic growth, the average real wage has been stagnant since 2000, largely driven by lack of market competition. Cumbersome regulations that are not conducive for creating a vibrant business environment, regulations that favor incumbents in many sectors, restrictions to foreign direct investment (FDI), and limited digital economy and digital government development all limit market competition.⁴ Moreover, continued efforts in revenue mobilization and

¹ According to Philippine Statistics Authority official data.

² World Bank (2018) Growth and Productivity in the Philippines, Winning the future.

³ The GINI coefficient declined from 48.2 percent in 2000 to 44.4 percent in 2015, based on official government data.

⁴ World Bank (2018) Growth and Productivity in the Philippines, Winning the future, World Bank (2018) Fostering Competition in the Philippines: The Challenge of Restrictive Regulations, and Qian Rong and Kevin Thomas Garcia Cruz (2019). Understanding the Philippine Real Wage Stagnation. Manuscript.



expenditure rationalization are crucial as the government continues to boost public investment in physical and human capital.

- 4. Due to its geographical location, the Philippine archipelago is highly at risk to a range of natural disasters, which are expected to worsen with climate change.** The Philippines has been identified as the third most vulnerable country in the world to weather-related extreme events and sea level rise.⁵ Main hazards in the Philippines include typhoons, floods, earthquakes, and volcanic eruptions. Typhoon Yolanda (Haiyan), which was the strongest typhoon ever recorded, hit the Philippines in 2013 and reportedly cost about Php571.1 billion in total damage (US\$12.9 billion) and had a devastating impact on public infrastructure, including roads, hospitals and school buildings.⁶ Climate shocks and disasters affect the poor more as they are less resilient.⁷ Physical and financial preparedness as well as mitigation measures are currently weak in the Philippines, hence the need to take appropriate policy measures while securing the fiscal sustainability of the country.
- 5. The reforms supported by this DPL are fully aligned with the new Systematic Country Diagnostic (SCD) and Country Partnership Framework (CPF).** The new CPF under preparation is structured around three focus areas: (i) investing in Filipinos; (ii) competitiveness and economic opportunity for job creation; and (iii) addressing core vulnerabilities by building peace and resilience. Embedded across the focus areas are the cross-cutting themes of governance and digital transformation, to tackle challenges and position the country to opportunities associated with improved implementation and service delivery. The DPL program is fully aligned with the objectives of the CPF by supporting reforms towards improving business climate, promoting competitiveness, facilitating digitalization of the economy and government service provision, and strengthening financial inclusion, which are long standing reforms needed to boost the quality of job creation. Likewise, the DPL supports reforms to enhance fiscal sustainability while expanding investment in human capital. In addition, the DPL supports the government's efforts to strengthen disaster and climate risk management which is directly aligned with the resilience pillar of the new CPF.
- 6. The reforms supported by the proposed DPL series are considered critical to achieve the government's objectives in the areas of competitiveness, fiscal management, and financial resilience to natural disasters and climate change through a strong emphasis on the implementation.** In particular, pillar 1 supports the government in a) ensuring food security and stable prices by liberalizing the importation of rice; b) simplifying ease of doing business (EODB) by streamlining government procedures; and c) increasing access to economic opportunities through the creation of a foundational ID and better payment systems. Pillar 2 supports the government's effort in enhancing fiscal sustainability by a) improving budget planning and financial management; b) increasing revenue mobilization; and c) reducing fiscal risks from government-owned and controlled corporations (GOCCs). Finally, pillar 3 supports the strengthening of financial resilience to natural disasters and climate change through a) reducing contingent liabilities by creating and managing a

⁵ World Bank (2013). Getting a grip...on climate change in the Philippines: overview (English). Washington DC; World Bank. <http://documents.worldbank.org/curated/en/288101468294989960/Getting-a-grip-on-climate-change-in-the-Philippines-overview>

⁶ World Bank (2017). Philippines: Lessons Learned from Yolanda.

⁷ See e.g. Skoufias, Emmanuel; Kawasoe, Yasuhiro; Strobl, Eric; Acosta, Pablo Ariel (2019). Identifying the Vulnerable to Poverty from Natural Disasters: The Case of Typhoons in the Philippines. Policy Research working paper; no. WPS 8857. Washington, D.C.: World Bank Group.



public asset registry; b) increasing the efficiency of post-disaster financing by expanding the government's risk layering strategy; and c) enhancing regulation for private insurance market against natural disasters. The programmatic series is designed to focus on implementation which has been a challenge in the Philippines, due to capacity constraints and the difficult political environment in which reforms occur.

- 7. The overall risk rating of this DPL operation is substantial.** Substantial risks are derived from political economy and governance challenges, and weak institutional and implementation capacity which, if they materialize, could adversely impact the government's willingness and ability to implement reforms, thereby delaying or preventing the achievement of the Program Development Objectives (PDOs). For instance, when the government introduced cash budgeting for the 2019 national budget, resistance from members of Congress resulted in the re-enactment of the 2018 budget⁸ for the first four months of 2019. Similarly, it took over a year for the government to issue implementing rules and regulations (IRR) for the Ease of Doing Business Act, causing delays in the implementation of the reform. To mitigate these risks, the DPL builds on a strong dialogue with the government's economic team and ongoing technical assistance (TA) to implementing agencies to ensure policy consistency and ownership of the reforms. The new CPF envisions to provide further TA to support the government's implementation of the reforms.

2. MACROECONOMIC POLICY FRAMEWORK

RECENT ECONOMIC DEVELOPMENTS

- 8. The Philippines registered faster economic growth in recent years, but growth decelerated in the first half of 2019.** In the past five years, the economy expanded at an annual rate of 6.4 percent, on average, compared to 5.2 percent in 2008-2013. Although growth in 2018 slowed down to 6.2 percent from 6.7 percent in 2017, the Philippines still outperformed regional peers, only topped by China and Vietnam. Growth moderated in 2018 partly due to the subpar performance of net exports as global growth moderated, international trade weakened, and the cyclical global demand for electronics softened. In addition, higher inflation driven by food supply constraints, high global oil prices, and new excise taxes had a negative impact on private consumption growth, contributing to the growth moderation. Nevertheless, investment growth accelerated in 2018 driven by a surge in public investments⁹ as a result of the government's expansionary fiscal policy to fill the country's infrastructure gap, and a strong recovery in private construction.¹⁰ The Philippines' growth

⁸ Re-enacted budgets are permitted under the Philippines Constitution when the annual budget is not signed into law before the beginning of the financial year to which it applies. In such cases, the previous year's budget is deemed to have been 're-enacted' such that all expenditures authorized for the previous year are applied to the new year, either for part of the year or for the full year when no new budget is approved. The duration of re-enactment is administered by the Department of Budget and Management which provides instructions to agencies on how the re-enacted budget will be implemented.

⁹ The national government public investment program expanded by 41.3 percent, year-on-year, in 2018, substantially greater than the 15.4 percent growth registered in 2017.

¹⁰ Investments in public construction accelerated to 21.2 percent year-on-year in 2018 from 12.7 percent in 2017. Meanwhile, investments in private construction recovered in 2018, growing by 12.9 percent year-on-year in 2018, more than thrice the 3.7 percent growth recorded in 2017.



decelerated further to 5.8 percent year-on-year in the first half of 2019 from 6.3 percent over the same period in the previous year. Economic growth moderation was driven by a contraction in public investment spending due to the delayed passage of the 2019 national government budget and the spending ban on new public work projects before the May mid-term elections.^{11,12} However, the government has accelerated public investment in the second half of 2019 leading to economic growth to reach 6.2 percent in Q3 2019.

- 9. The Central Bank returned to a more accommodative monetary policy stance in the first half of 2019 to support the economy and as inflation moderated, partly reversing the tightening cycle initiated in 2018.** The inflation rates recorded 2.1 percent in average in 2016-2017, within the Bangko Sentral ng Pilipinas' (BSP) inflation target range of 2-4 percent. However, in 2018, inflation breached the target, averaging 5.2 percent, largely due to high food and energy inflation. Local energy prices climbed as global oil prices increased and local electricity prices were adjusted upwards. Excluding the volatile food and energy items, the core inflation also soared, attributed to the pass-through effect of a weaker peso and an underlying price pressure.¹³ The high inflation in 2018 triggered the BSP to respond by raising the key policy rate by a total of 175 basis points (bps).¹⁴ In 2019, as inflation declined steadily,¹⁵ largely driven by lower food prices, rice prices in particular since the implementation of the Rice Liberalization Act, the BSP adopted a more accommodative monetary policy¹⁶ stance in the first half of 2019. The BSP also reduced the overnight reserve repurchase (RRP) by a total of 75 bps to 4.0 percent as of October 2019. In addition, to mitigate domestic liquidity tightness brought about by limited public spending, a total of 200 bps was incrementally deducted from the 18 percent reserve requirement ratio (RRR) faced by universal and commercial banks, bringing it to 16 percent by end-July 2019.¹⁷

- 10. The Philippines' financial system remains stable and resilient.** Philippine banks are well capitalized,

¹¹ The 2019 national government budget was signed into law on April 15, 2019, after a more than four-month long delay due to an impasse between both houses of Congress. The delayed passage resulted in the national government operating under the 2018 budget (reenacted budget) for the first four months of 2019. This resulted in the delayed implementation of new programs and projects under the 2019 budget, as no new programs and projects would receive funding under a reenacted budget.

¹² Fixed investment growth, expanded at its slowest pace since 2011, as public investment was tempered by the reenactment of the 2019 national government budget for the first four months of the year and spending ban for new projects before May election, resulting in infrastructure and other capital outlay disbursements to shrink to 4.3 percent of GDP in the first half of 2019 compared to 5.4 percent in the first half of 2018. In addition, private investment activities also slowed due to uncertainties around the government's ongoing tax-reform program and the external environment.

¹³ The Philippine peso depreciated in nominal terms by 4.3 percent year-on-year in 2018 while the real effective exchange rate depreciated by 2.7 percent year-on-year in 2018. This makes the peso along with the Indonesian rupiah, the weakest currency among regional peers in 2018.

¹⁴ Besides the BSP raising its key policy rate to anchor inflation expectation, the government also implemented trade measures on key commodities to address supply-side drivers of inflation. For instance, an executive order was approved to ease importation of fish, vegetables, meat and other food products to supplement domestic supplies.

¹⁵ Inflation averaged 2.7 percent in the first 10 months of 2019, back within the 2 to 3 percent target.

¹⁶ The BSP's approach to monetary policy is based on inflation targeting based as per its mandate to 'promote price stability conducive to a balanced and sustainable growth of the economy.' The BSP uses monetary policy tools such as the reverse repurchase facility, the reserve requirement ratio, acceptance of term deposits, among other monetary policy instruments. The current inflation target for the Philippines is 2 to 4 percent. For a more detailed discussion on the BSP's approach to monetary policy, please refer to: <http://www.bsp.gov.ph/monetary/targeting.asp>

¹⁷ This is also part of the BSP's broad financial sector reform agenda to promote a more efficient financial system by lowering financial intermediation costs.



with a total capital adequacy ratio of 15.5 percent in June 2019, well above the 10 percent regulatory minimum. The share of non-performing loans remains low at 2.1 percent in June 2019. The banking sector is highly profitable, with a return on equity at 9.8 percent in June 2019 compared to 9.5 percent in June 2018, and a return on asset at 1.2 percent both in June 2018 and June 2019. The share of interest income in total operating income averaged 77.1 percent between March and June 2019 and stood at 77.5 percent in June 2019, an indication that lending continues to be banks' core business rather than other fee-based activities.

11. Widening trade deficits led to low but consistently negative current account balances since 2016.

The current account has been in deficits since 2016, averaging -1.2 percent of GDP between 2016-2018 and reaching -1.0 percent of GDP in the first half of 2019. The current account deficits were driven by expanding trade deficits, which were not offset by net services exports and remittances.¹⁸ Net inflow in financial account financed the deficit which averaged 1.1 percent of GDP between 2016-2018 rising to 2.8 percent of GDP in the first half of 2019.¹⁹ Net FDI inflows averaged 3.0 percent of GDP in the last three years, but slowed in the first half of 2019 as investments were impacted by global trade uncertainties and the government's corporate income tax (CIT) and fiscal incentives reform program. As a result, the balance of payments remained in deficit, averaging -0.4 percent of GDP between 2016-2018. Nevertheless, the balance of payment (BOP) position swung into surplus in the first half of 2019 (2.8 percent of GDP) driven by portfolio inflows and foreign borrowings. At 7.4 months of import coverage in the first half of 2019, the level of international reserves reflects ample external liquidity buffer, despite a decline from 11.7 months of imports coverage in 2013.

12. Fiscal deficits widened as the government adopted an expansionary fiscal policy in 2016 to close the gaps in infrastructure and human capital. With the goal of achieving a more inclusive growth, the government invested heavily in both human and physical capital. This led to increases in the government spending trajectory reaching 17.9 percent of GDP in 2017 and 19.6 of GDP in 2018. As a result, the fiscal deficit expanded from 0.6 percent in 2014 to 3.2 percent in 2018. However, the government experienced a brief pause in fiscal expansion in the first half of 2019, as public expenditures shrunk to 18.0 percent of GDP as a result of the delayed passage of the 2019 national government budget and the spending ban, narrowing fiscal deficit to 0.5 percent of GDP in the first half 2019. Domestic sources are tapped to support the fiscal gap and represented 75 percent of total borrowing in 2018.²⁰ As a result of the government's commitment toward implementing an expansionary fiscal policy and slower pace of nominal GDP growth in the first half of 2019, the government's debt-to-GDP ratio increased to 43.7 percent of GDP in the first half of 2019 from 42.5 percent of GDP in the same period in 2018. Despite the increase, debt metrics remain favorable toward maintaining long-term fiscal sustainability. The country's debt portfolio is composed largely of

¹⁸ Import growth outpaced export growth during this period and merchandise trade has been in deficit since 2013. Capital goods, which used to constitute a quarter of total import bill between 2011-2015, have made up about a third of imports in 2016 onwards. Raw materials and intermediate goods constitute about two-fifths, and consumer goods at about a fifth. The rest of the balance is made of minerals, fuel, lubricants and related materials.

¹⁹ The more dovish stance of the U.S. Federal Reserve since the start of the year contributed to an inflow of capital to emerging markets, including the Philippines where declining inflationary pressure helped improve confidence in the domestic economy.

²⁰ In 2018, net domestic financing, decreased by 19 percent year-on-year in nominal terms to Php591.5 billion from Php731.4 billion in 2017. The huge drop in domestic financing coincided with the sharp increase in net foreign financing, which increased by seven times in 2018 to reach Php191.8 billion, up from Php27.6 billion in 2017. By end-2018, the composition of the debt stock stood at 65:35 in favor of domestic debt.



long-term debt (76.0 percent), while around two-thirds of the country’s total debt is composed of peso-denominated debt.

Table 1. Key Economic Indicators (2014 to 2022)

	2014	2015	2016	2017	2018	2019	2020	2021	2022
	Actual					Projected			
Growth and inflation	(in percent of GDP, unless otherwise indicated)								
Gross domestic product (percent change)	6.1	6.1	6.9	6.7	6.2	5.8	6.1	6.2	6.2
Inflation (period average)	3.6	0.7	1.3	2.9	5.2	2.9	3.0	3.0	3.0
Savings and investment									
Gross domestic savings	16.9	15.3	15.1	15.2	14.4	14.1	14.2	14.5	14.5
Gross domestic investment	20.7	22.0	24.6	25.0	26.9	26.8	28.4	30.0	31.2
Public sector									
National government balance	-0.6	-0.9	-2.4	-2.2	-3.2	-2.0	-2.7	-2.8	-2.8
Primary balance	2.0	1.4	-0.3	-0.3	-1.2	-0.1	-0.7	-0.7	-0.7
Total revenue (government definition)	15.1	15.8	15.2	15.6	16.4	16.6	16.8	17.1	17.3
Tax revenue	13.6	13.6	13.7	14.2	14.7	15.0	15.4	15.5	15.7
Total spending (government definition)	15.7	16.7	17.6	17.9	19.6	18.6	19.5	19.9	20.1
National government debt	45.4	44.7	42.1	42.1	41.9	40.4	39.6	38.4	37.3
Balance of payments									
Total exports (percent change)	12.6	8.5	11.6	19.5	13.4	5.9	8.0	8.3	8.5
Total imports (percent change)	9.9	14.6	20.2	18.1	16.0	6.6	11.5	12.0	12.4
Remittances (percent change of US\$ remittance)	7.5	3.8	4.9	5.3	3.0	3.3	3.3	3.5	3.5
Current account balance	3.8	2.5	-0.4	-0.7	-2.4	-2.0	-2.5	-2.7	-2.7
Foreign direct investment (billions of dollars)	5.7	5.7	8.3	10.3	9.8	10.0	10.5	11.0	11.5
Portfolio investment (billions of dollars)	2.7	5.5	1.5	2.5	0.9	1.0	1.2	1.4	1.5
International reserves									
Gross official reserves ^{1/} (billions of dollars)	79.5	80.6	80.7	81.6	79.2				
Gross official reserves (months of imports) ^{2/}	9.9	10.0	8.8	7.8	7.1				

Sources: Government of the Philippines for historical and World Bank for projections.

1/ Includes gold

2/ Defined as the total of goods and services imports and primary income that can be financed by reserves

13. To ensure fiscal sustainability the government intensified domestic revenue mobilization and adopted more disciplined expenditure management. Financing the infrastructure and human capital investment agenda required efforts to raise additional public revenues. The government instituted tax policy reforms that contributed to revenue increases starting with the passing of the Tax Reform for Acceleration and Inclusion (TRAIN) law, that broadened the tax base, simplified the tax system, introduced new excise taxes and consolidated tax exemptions, resulting in the highest tax ratio in more than two decades in 2018. In addition, non-tax revenue also improved through better monitoring of state-owned enterprises (SOEs). In June 2019, the government further increased tobacco taxes. Ongoing tax reform efforts focus on rationalizing tax incentives, lowering corporate tax rates, further increasing alcohol and tobacco excise taxes, simplifying financial taxes, and unifying property values. To boost the efficiency of public expenditure, the government has launched the Budget and Treasury Management System (BTMS), an integrated financial monitoring system for all agencies which replaced the inefficient and fragmented legacy systems of each agency. In addition, the government is developing suitable instruments to manage the fiscal risk arising from the



destruction of public assets due to natural disasters and climate change.

Table 2. Key Fiscal Indicators (2016 -2020)

	2016	2017	2018	2019	2020
	Actual			Projected	
	<i>(in percent of GDP, unless otherwise indicated)</i>				
Overall Balance	-2.4	-2.2	-3.2	-2.0	-2.7
Primary Balance	-0.3	-0.3	-1.2	-0.1	-0.7
Total Revenues (and grants)	15.2	15.6	16.4	16.6	16.8
Tax Revenues	13.7	14.2	14.7	15.0	15.4
Taxes on net income and profits	6.4	6.5	5.9	5.9	5.8
Taxes on Domestic Goods and Services	4.5	4.8	5.4	5.7	6.2
General Sales, Turnover, or VAT	2.3	2.3	2.6	2.7	2.9
Selected Excises on Goods	1.1	1.3	1.7	1.8	2.0
Selected Taxes on Services	0.4	0.5	0.4	0.4	0.5
Other Taxes	0.6	0.7	0.7	0.8	0.8
Taxes on International Trade and Transactions	2.7	2.9	3.4	3.4	3.4
Non-tax revenue	1.5	1.4	1.7	1.6	1.4
Total Expenditures	17.6	17.9	19.6	18.6	19.5
Current operating expenditures	13.3	13.4	14.0	14.1	14.0
Personal Services	5.0	5.1	5.7	5.8	5.7
Maintenance and other operating expenditures	3.0	2.9	3.0	3.0	3.0
Subsidy	0.7	0.8	0.8	0.7	0.7
Allotment to Local Government Units	2.4	2.5	2.4	2.5	2.5
Interest Payments	2.1	2.0	2.0	1.9	2.0
Tax Expenditures	0.1	0.1	0.1	0.1	0.1
Capital Outlays	4.2	4.5	5.5	4.5	5.5
Infrastructure & other capital outlay	3.4	3.6	4.6	3.6	4.7
Equity	0.1	0.0	0.0	0.0	0.0
Capital transfer to local government units	0.7	0.9	0.9	0.9	0.8
National Government Financing Needs	5.8	4.5	5.4	4.7	5.6
Amortization	3.4	2.3	2.2	2.7	2.9
Domestic	2.2	1.5	1.5	1.8	2.0
External	1.2	0.9	0.6	0.9	0.9

Sources: Bureau of the Treasury, Department of Budget and Management, Philippine Statistics Authority, and World Bank staff calculation.



2.2. MACROECONOMIC OUTLOOK AND DEBT SUSTAINABILITY

- 14. The Philippines' growth outlook is weakened by the difficult external environment and domestic challenges.** The World Bank projects the country's real GDP growth at 5.8 percent in 2019, before edging up to 6.1 percent in 2020 and 6.2 percent in 2021. The forecast takes into account downside risks that have materialized since the beginning of the year, such as the slowdown in public spending, particularly on infrastructure, prevailing market anxiety about the impact of global economic developments on the Philippine economy, including weak global manufacturing activity and trade, as well as heightened uncertainty from escalating trade tensions. Economic growth is expected to recover starting in the second half of 2019 as the government accelerates public investment. Private consumption growth, despite recording a mild slowdown in the second quarter, is expected to accelerate in 2019 compared with 2018. Given the weak external environment, net exports will remain subdued. Nevertheless, economic growth is expected to surpass 6.0 percent in 2020-21 as the impact of this year's public expenditure slowdown dissipates and global growth is expected to slightly improve in the next two years.
- 15. The government's medium-term infrastructure spending agenda is expected to help improve the economy's productivity.** The government has pursued the Build, Build, Build Program – an infrastructure development agenda which aims to increase public infrastructure spending from 5.7 percent of GDP in 2017 to 7.3 percent of GDP in 2022. In line with this, infrastructure outlays increased by 41.3 percent in 2018. The bulk of recent public infrastructure outlays are from small-scale public works projects, and only 11 out of the original 75 priority projects under the program are reportedly under construction. The government has since revised the list of Build, Build, Build projects, dropping at least 29 from the original list due to their infeasibility, while expanding the list of projects to 100 to include smaller projects which were more feasible. Accelerating the implementation of the higher-impact flagship projects while keeping deficits within targets will allow for the maximization of productivity benefits of the infrastructure investment program as well as positive spillover effects to the rest of the economy.
- 16. Continuation of the government's comprehensive tax reform program (CTRP) is expected to support tax revenues increases in the medium-term.** The second package of the government's tax reform program, the Corporate Income Tax and Incentives Rationalization Act (CITIRA) bill, aims to reduce the CIT rate by one percentage point annually from 30 percent to 20 percent, while broadening the corporate tax base through rationalizing fiscal incentives currently administered under some 336 laws, by 13 investment promotion agencies, in 544 economic zones and freeports. The reform seeks to promote investments by moving the CIT rate closer to those of regional peers and encouraging more job creation, innovation, and regional development through a performance-based, targeted, time-bound, and transparent incentives system. The International Monetary Fund (IMF) estimates that revenue losses from the CIT reduction will equal the gains from the incentives streamlining and will thus yield a revenue-neutral reform. The CITIRA bill was passed in its third and final reading at the House of Representatives on September 13, 2019 and is currently undergoing deliberations in the Senate. Other succeeding packages aim to modify the motor vehicle users' charge (Package 1B), reform on property valuation (Package 3), reform to increase excise taxes on tobacco, e-cigarettes, and alcohol (Package 2+), and rationalize passive income and financial intermediaries' taxation (Package 4), which are expected to raise revenue collection. Despite the foreseen difficulties in



passing new tax measures, tax revenue as a share of GDP is still projected to increase through 2021 in line with the country's strong economic growth.

17. The government's financing needs is expected to decrease in 2019 before eventually picking up in the medium term. The delay in the approval of the budget and the pre-election spending ban slowed down public investments in the first half of 2019. As a result, the net financing need is expected to dip from 5.4 percent of GDP in 2018 to 4.7 percent of GDP in 2019, before climbing up in following years, in line with the ramp up in the implementation of the infrastructure investment program (Table 3). Domestic financing will be the main source of financing, as the government follows a financing program in favor of domestic credit. Despite the government favoring domestic credit, the sustained double-digit domestic credit growth in the market suggests that there is no evidence of crowding out of the private sector. Compared to previous years, the share of external source of government financing needs has marginally increased from 20 to now 25 percent. Given the Philippines low overall public debt level, 41.9 percent of GDP in 2018, as well as its recent S&P sovereign credit rating upgrade, the increase in financing needs in the medium term and adjustment in the financing profile is expected to be manageable. This DPL series will provide buffer to government financing needs to face unexpected external and domestic shocks.

18. Prudent debt management policy, coupled with high economic growth, have resulted in low debt sustainability risk for the economy. Under current policies, the overall debt ratio is expected to continue to decline in the medium term. It is most vulnerable to a growth shock, followed by real interest rate and primary balance shocks.²¹ On a cumulative basis, the interest rate-growth differential is the main factor behind the projected fall in public debt as real GDP growth is expected to remain high. Though the country's debt-mix has become more externally funded, about 65:35 with 65 percent from domestic lenders,²² the average residual maturity of external loans increased from 12.1 years in 2017 to 12.3 years in 2018, while the weighted average interest rate on external debt has been on the decline since 2014. The debt composition is anticipated to be stable with a relatively low share of short-term debt and foreign currency-denominated debt, in line with the authorities' debt management policy.

19. External risks have intensified while the threat of capital outflows has abated. The Philippines faces heightened external risks due to the slowdown in global growth and demand, weaker global manufacturing activity, and rising global protectionism.²³ The unresolved trade dispute between the United States of America (U.S.) and China, coupled with a newly emerged trade conflict between Japan and Korea, strains the regional value chain that the Philippines is a part of. This darkens the prospect of the country's export performance, which has already been reeling from the decline in electronics export growth due to the downturn in the electronics production cycle. While the likelihood of intensified capital outflows has subsided, given the more dovish stance of central banks

²¹ Alternative scenarios included historical and constant primary balance scenarios. Under the historical scenario, debt reduction is faster than the baseline, reflecting the country's debt consolidation since 1999 and strong GDP growth. Debt sustainability analysis was also performed in disaster shock scenario which resulted in a larger primary deficit, reflecting added financing needs, and debt levels of about 2.2-2.5 percent of GDP higher than the baseline scenario until 2024.

²² The Development Budget Coordination Committee announced following a 75-25 deficit financing mix in favor of domestic borrowings each year from 2019 to 2022.

²³ Rising global protectionism is a risk to global growth and trade at large, which translates to the risks of weak external demand to the Philippines.



in advanced economies, episodes of abrupt volatility in the financial market remain a possibility, driven by the re-escalation of trade wars and geopolitical disturbances.

Table 3. Government’s Medium-Term Financing Plan (2015-2022)

	2015	2016	2017	2018	2019	2020	2021	2022
	<i>Actual</i>				<i>Projected</i>			
	<i>(in percent of GDP, unless otherwise indicated)</i>							
Financing needs	4.6	5.8	4.5	5.4	4.7	5.6	5.7	5.7
Amortizations	3.7	3.4	2.3	2.2	2.7	2.9	2.9	2.9
Domestic	2.7	2.2	1.5	1.5	1.8	2.0	2.0	2.0
External	0.9	1.2	0.9	0.6	0.9	0.9	0.9	0.9
Primary deficit	-1.4	0.3	0.2	1.2	0.1	0.7	0.7	0.7
Interest payments	2.3	2.1	2.0	2.0	1.9	2.0	2.1	2.1
Financing sources	4.6	3.5	5.7	5.2	5.0	5.9	6.0	6.0
External	1.4	1.0	1.1	1.7	1.6	1.9	2.0	2.0
o/w this operations	0.0	0.0	0.0	0.0	0.0	0.1	0.1	0.1
Domestic	3.2	2.5	4.6	3.4	3.3	4.0	4.0	4.0
Change in cash	0.0	-2.3	1.2	-0.2	0.3	0.3	0.3	0.3

Sources: Government of the Philippines for historical and World Bank for projections

20. A slow recovery in public investments constitutes the main domestic downward risk. While some domestic risks have subsided, including the threat of high inflation, accelerating the roll-out of public investments would be crucial to achieve the baseline growth outlook. The need to judiciously expedite public expenditures, which have fallen short of their desired target in the first half of 2019, is not only important to increase economic growth but also to addresses the country’s physical infrastructure and human capital needs. In particular, several national government agencies continue to face implementation bottlenecks which have prevented line agencies from fully executing their budgets, with issues relating to absorptive capacity, procurement difficulties, and right-of-way.²⁴

21. Identified as one of the most disaster-risk prone countries in the world, the Philippines is subject to substantial losses to public and private assets due to natural disasters. The United Nations Office for Disaster Risk Reduction identified the Philippines as the second country with the highest number of people affected by natural calamities in 2018. The country is prone to typhoons, flooding and extreme weather events, resulting in people displacement and substantial output and asset losses. Estimates show that on a long-term average basis, the Philippines is expected to incur Php177 billion (1.0 percent of GDP) per year in losses to public and private assets due to typhoons and earthquakes. In the next 50 years, it is estimated that the Philippines has a 40 percent chance of experiencing losses exceeding Php1.7 trillion and a 20 percent chance of experiencing losses exceeding Php2.7 trillion. Economic losses may compound as years pass or as the severity of disasters intensify. Hence, an adequate financial risk strategy remains crucial to mitigate contingent fiscal risks.

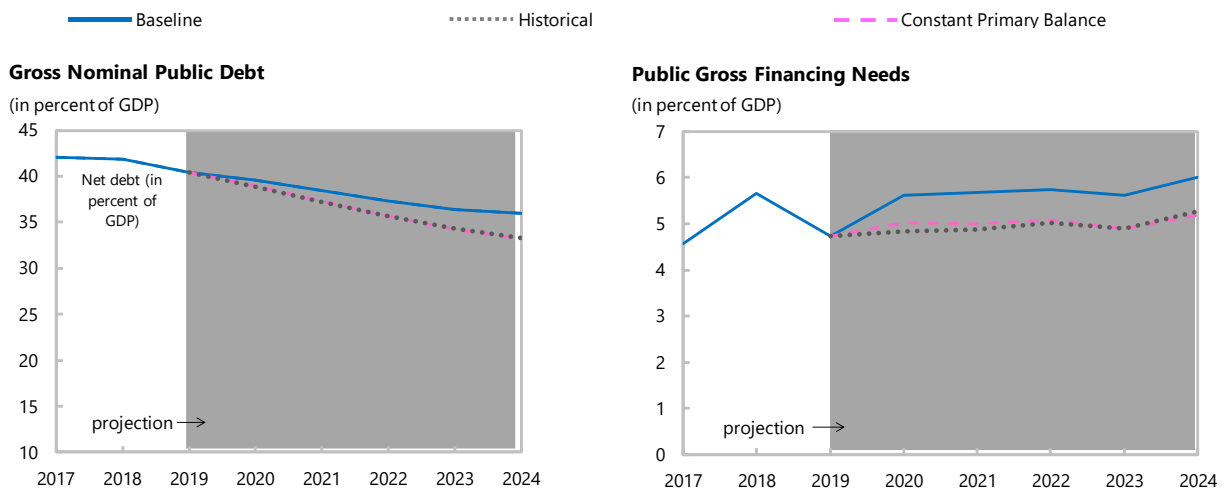
22. Overall, the macroeconomic policy framework is adequate for the purpose of the proposed

²⁴ For example, according to audit reports by the Commission on Audit (COA), the Department of Transportation (DOTr) and the Department of Public Works and Highways (DPWH) disbursed only 20.6 percent and 39.2 percent of their budgets in 2018, respectively.²⁴ Both the DOTr and the DPWH will continue to play an integral role in the government’s infrastructure investment program, and addressing these implementation bottlenecks, which have plagued line agencies for years is crucial in order to ensure that the pace of the public investment program ramps up over the medium-term.



operation. The economy showed increasing resilience to external and domestic shocks which until fifteen years ago negatively impacted the country’s growth path. The central bank is committed to the inflation-targeting objective and responsive to global interest rate movements. Under its helm, the country has accumulated adequate foreign exchange reserves that provide cushion to the impact of global shocks. It has also maintained a flexible exchange rate regime as a first line of defense against external shocks. In terms of fiscal policy, conservative expenditure policy in the past ten years created important fiscal space allowing the current expansion of public investment. The notable improvement in overall macroeconomic stability has been recognized by all three international rating agencies and even resulted in a sovereign credit rating upgrade of BBB+ from S&P. The low level of debt and the ongoing fiscal reforms supported by this DPL will contribute to maintaining a stable fiscal framework. In addition, the continued pursuit of structural reforms such as improving competitiveness of the country will help improve the macroeconomic fundamentals and support more inclusive growth.

Figure 1. National Government Debt-to-GDP Projections under Alternative Scenarios



Source: World Bank estimates

2.3. IMF RELATIONS

23. The Philippines does not have an ongoing program with the IMF. The most recent IMF program expired at end-2000, and all obligations were fully repaid in 2006. Article IV Consultations are conducted on a standard 12-month basis. The last consultations were concluded in July 2018 and the ongoing 2019 consultation is under preparation. Ongoing TA focuses on tax policy and capacity building. The World Bank team maintains a close working relation with the Fund. Exchanges on macro-fiscal issues, public financial management (PFM) reforms, financial sector updates, and monetary policy are conducted on a regular basis. The Bank and the Fund broadly share a similar assessment of the economic conditions of the Philippines. In particular, the Fund noted the strong economic performance of the Philippines due to good macroeconomic management and continued reforms. It, however, noted short term risks such as the less favorable external environment and underscored the need to adjust the policy mix to address the risks. Still, the medium-term economic outlook remains favorable.



3. GOVERNMENT PROGRAM

- 24. The government continues to put strong focus on achieving more inclusive growth through the implementation of key structural reforms that address long-standing policy and institutional challenges.** The government's policy agenda was first presented in the 0+10-point socioeconomic agenda, which promotes continuity on core aspects of recent macroeconomic and development policy that made the Philippines among the most dynamic economies in the region, while ramping up key structural reforms which would accelerate inclusive growth – the type that creates more and better jobs and reduces poverty. The government's policy goals are encapsulated in the long-term vision for the Philippines, known as *AmBisyon Natin 2040*, supported by the current Philippine Development Plan (PDP) 2017 – 2022. The PDP outlines policy priorities for delivering inequality-reducing transformation; increased growth potential; an enabling and supportive economic environment; and foundations for sustainable development.
- 25. The government has crafted a medium-term fiscal program focusing on the implementation of key structural reforms in support of the government's policy agenda.** The government's budgets between 2017-2019 embody its commitment to address the substantial investment gaps in both physical and human capital accumulation. The government has increased the public infrastructure budget since 2016, from 5.1 percent of GDP in 2016 to 6.1 percent of GDP in 2018, with the goal of scaling up to reach 7.3 percent of GDP by 2022. On human capital accumulation, the combined budget for health and education increased from 4.7 percent of GDP in 2016 to 5.8 percent of GDP in 2018. To complement reforms aimed at increasing public expenditure, the government's proposed Budget Modernization Bill aims to revamp the budgeting process, accelerate program delivery, and strengthen government focus and accountability.
- 26. The government initiated the CTRP to finance its inclusive growth agenda and to ensure macro-fiscal sustainability in the long term.** A series of tax reform packages are currently in the government's legislative pipeline with the aim of making the tax system more equitable, efficient, competitive, while generating additional revenue needed to finance the government's development agenda. Each package is intended to focus on a different area of tax policy and attempts to balance tradeoffs between revenue generation, economic efficiency, and fiscal equity. The first package of the government's CTRP, Republic Act (RA) No. 10963, was passed into law on December 19, 2017 and was supported by the Improving Fiscal Management DPL (P167651). A tax amnesty act (RA No. 11213) was also approved on February 14, 2019 and covers estate tax amnesty as well as tax amnesty on delinquencies.²⁵ Moreover, a new tobacco tax bill (RA No. 11346) was approved on July 25, 2019. Additional tax reform packages focusing on areas of corporate income taxes and fiscal incentives, excise taxes on tobacco, e-cigarettes, and alcohol, real property valuation taxes, passive income and financial intermediaries' taxation were filed and are being discussed. Subsequent tax reform packages include motor vehicle users' charge, mining taxation, and general amnesty with lifting of bank secrecy for fraud cases and automatic exchange of information.

²⁵ Estate tax amnesty can be availed within 2 years upon effectivity of the IRR while tax amnesty on delinquencies can be made within 1 year. Congress is asked to pass another separate general tax amnesty bill that includes lifting of bank secrecy for fraud cases, the inclusion of automatic exchange of information, and safeguards to ensure the asset and net worth of declarations are truthful.



27. The government has also embarked into structural reforms targeting distortions and bottlenecks in the real economy. The reform agenda includes measures to simplify regulations, enhance the business environment, promote competition, broaden social and economic inclusion, and strengthen resilience. For example, to simplify business regulations, the government passed the Ease of Doing Business and Efficient Government Service Delivery Act in 2018, amending the Anti-Red Tape Act of 2007 (RA No. 9485) to boost competition and foster competitiveness in the Philippines by simplifying regulations and streamlining procedures. The Rice Liberalization Act (RA No. 11203) tackled decades long constraints toward agriculture sector development by removing the quantitative restrictions on rice imports in favor of a tariff regime which would facilitate greater importation of rice, thereby contributing to poverty reduction through lower rice prices, Filipino’s main food stable, especially among the poor. Furthermore, removing restriction in the rice sector would boost overall agriculture productivity as farmers shift to higher value crops and become more competitive. In addition, the government recently passed the Philippine Identification System (PhilSys) Act and the Universal Healthcare Act, fundamental reforms to improve service delivery, broaden inclusion, and accelerate human capital development in the Philippines.

4. PROPOSED OPERATION

4.1. LINK TO GOVERNMENT PROGRAM AND OPERATION DESCRIPTION

28. This DPL supports the government’s overarching objective of achieving more inclusive growth through promoting competitiveness, enhancing fiscal sustainability, and strengthening financial resilience to natural disasters and climate change with a strong focus on implementation. This operation supports key institutional and policy reforms that are being undertaken by the government as guided by PDP 2017 – 2022 and the 0+10-point socioeconomic agenda. The DPL is structured around three pillars: (i) promoting competitiveness, (ii) enhancing fiscal sustainability, and (iii) strengthening financial resilience to natural disasters and climate change. The operation is the first of the three DPL series to support government reforms through 2021, with second and third operations focusing more on the implementation of the reforms supported in the first operation.

29. The DPL builds on the previous DPL series and the recent stand-alone operation. The previous DPL series supported the overarching objective of helping the Philippines achieve sustained inclusive growth through better fiscal management, improved PFM and accountability, improvements to the investment climate, and better access to and quality of health and education services. The achievements of the four objectives were rated by the Implementation Completion Report (ICR) as substantial, and the overall outcome was rated as satisfactory by the Independent Evaluation Group. The design of this operation was guided by the key lessons from the previous DPL series. First, the importance of a programmatic multi-year format in providing an effective platform to support reforms and institutional development. Second, the close coordination between World Bank teams and government partners which are vital to producing results. Third, the importance of complementary knowledge and TA for the success and results achieved under the DPL series. Moreover, this operation continues to build on the recently completed stand-alone DPL which aimed to support the government to improve fiscal management to promote inclusive growth over the medium-term.

30. Pillar III of this operation is closely aligned with the new Catastrophe Deferred Drawdown Option



(CAT-DDO3) operation under preparation. The two operations are closely coordinated to strengthen complementary aspects of risk financing. Pillar III under this operation strengthens the integration of climate and disaster risk management in the government’s core fiscal planning and public financial management to improve access to enough resources following natural disaster shocks. Meanwhile, CAT-DDO3 will be the bridge between the fiscal resilience and the physical resilience agenda, by strengthening preparedness planning to ensure the effective use of resources following shocks to mitigate disaster impact on the ground.

31. This operation is the first in a new series and is being prepared to align with the new CPF. The government’s financing needs are expected to rise in the medium term due to the expansion of its public expenditure program, which puts increasing focus on addressing investment gaps in both physical and human capital. Given the changing external financing conditions for emerging economies, the government wishes to increase development policy financing in the medium term and requested the World Bank team to prepare a new DPL series under the new CPF. The policy matrix (Annex 1) of this DPL series reflects the World Bank’s continuing engagement with the government and is supported by extensive analytical and advisory work.

32. The program supports the World Bank Group’s (WBG) approach to maximizing finance for development (MFD), containing several reform actions which are expected to crowd in private sector investment. As part of the promoting competitiveness pillar, the EODB reform aims to lower barriers to entry for small and medium enterprises and improve the overall business environment in the Philippines, further crowding in private sector investment and generating greater job creation in the Philippines. Meanwhile, complementary reforms through the introduction of a National ID system through the PhilSys Act and the implementation of a national payment system through the National Payment System Act (NPSA), are expected to boost service delivery, financial inclusion, and facilitate the transition of the Philippine economy into the digital age which would broaden the country’s prospects and further boost investments by the private sector.

4.2. PRIOR ACTIONS, RESULTS AND ANALYTICAL UNDERPINNINGS

Pillar I: Promoting Competitiveness

Objective 1: Promote competition through regulatory reforms to increase agriculture productivity.

Prior Action under DPL I	Trigger for DPL II	Trigger for DPL III
Through the Rice Liberalization Act (RA No. 11203) and the DA-NEDA-DBM Joint Memorandum Circular Number 01-2019, the government has liberalized the rice import market by shifting from a quantitative restriction system to a transparent tariff system.	The government has established clear and transparent eligibility criteria for accessing the Rice Competitiveness Enhancement Fund (RCEF) and has updated the registry system for basic sectors in agriculture (RSBSA) as per Art. 14 of the DA-NEDA-DBM Joint Memorandum Circular Number 01-2019.	



- 33. Philippine rice importation used to be heavily regulated, causing high and volatile rice prices.** Rice is the main staple food of Filipino families, and its production has been one of the most protected in the country through tight quantitative restriction for rice imports. Despite being one of the ten largest rice producers in the world, the Philippines' level of production does not meet its full demand, producing around 93 to 96 percent of its domestic rice requirements, with the rest being imported mainly from Thailand and Vietnam. To promote self-sufficiency, the government has, since 1972, heavily intervened in the rice sector through the National Food Authority (NFA) to procure raw and unprocessed rice from farmers and sell rice to consumers, and through establishing a very strict control over rice imports by importing them itself or imposing quantity restrictions to licensee private importers. This state control has often led to imperfect timing and high costs of rice imports relative to domestic demand needs. As a result, domestic rice prices in the Philippines have consistently been above international export prices from Thailand and Vietnam, with an increasing price differential over time, encouraging rice smuggling and discouraging investment in the domestic formal rice market. Furthermore, distortion in the rice market has been identified as one of the key constraints that prevented sector development as rice producers had little incentives to be efficient in producing rice or to shift to other higher value crops. As a result, the agriculture sector has been stagnant in the last decades with the slowest productivity growth in the region and contributed to slow progress on poverty reduction.
- 34. The DPL series supports the government's bold move to liberalize the importation of rice to lower the price of rice and creates incentives for the sector to become more efficient and competitive.** Given the high impact of rice prices on consumer welfare, rice liberalization has been debated for decades in the legislature. In 2018, the high inflation driven by the rice supply shortage caused by NFA mismanagement of rice imports created a turning point in the reform momentum. The government seized the opportunity and successfully obtained the passage of the Rice Liberalization Act, RA No. 11203, in February 2019 and published the DA-NEDA-DBM Joint Memorandum Circular Number 01-2019 in April 2019. The law eliminates quantitative restrictions on rice importation and liberalizes importation of rice to private importers under a more transparent tariff regime. Since its implementation, both farmgate and retail prices of rice have declined, 22.2 percent and 16.4 percent year-to-year respectively as of October 2019. In addition, the NFA's role in the regulation and licensing of importers has been eliminated and its function has been restricted to the purchasing of the national rice buffer stocks to ensure food security during emergency situations. Moreover, funds generated by the tariff regime will be used for the improvement of local rice productive capacity and efficiency.
- 35. The DPL series supports steps needed during the transition process to mitigate the possible adverse effect on farmers.** Rice prices have declined at all levels, retail, farm-gate and milling, now that importation has been liberalized. So far, farmgate prices have however fallen more than milled rice. In the first two weeks of October 2019, average farmgate price of paddy declined by 22.2 percent from its level in the same period of the previous year. In comparison, the average retail price of milled rice declined by 16.4 percent from a year before. It can also be observed that the decrease in farmgate prices of paddy is larger than the decrease in retail prices of rice. Over time, farmers that cannot produce rice at the market price competitively will need to move to other crops which can be more productive and profitable. The Rice Liberalization Act anticipated this and include provisions to support farmers during the transition process. A key vehicle for this support is the Rice



Competitiveness Enhancing Fund – Php10 billion (approximately US\$200 million) annually over 6 years, plus the tariff revenues collected from rice importation in excess to Php10 billion. Fifty percent of these resources to support producer groups with rice farm equipment; 30 percent for development, propagation, promotion of inbred rice seeds; 10 percent for a credit facility; and 10 percent for rice extension services. It is planned that the annual allocation of the RCEF will focus on increasing the productivity of rice farmers, while the additional resources above Php10 billion will be used for rice farmer financial assistance, titling of agricultural lands, expanded crop insurance on rice and crop diversification program. The RCEF however, was not ready and implementable when the act came into effect and could therefore not soften the impacts of the falling farmgate prices on rice farmers. The Department of Agriculture (DA), in coordination with regional field offices and the agencies²⁶ mandated to operate the fund allocations, are currently working on guidelines covering the eligibility criteria for prospective recipients. A registry system has been set up around four years ago for basic sectors in agriculture, but it needs to be updated and cleaned. The Guidelines for the efficient implementation of the programs under RCEF should also be available. In addition, the NFA will be reorganized to assume its new limited mandate of only maintaining a buffer stock, with the objective of minimizing market distortions.

Expected results: Supported measures are expected to narrow the gap between international and domestic prices,²⁷ increase agriculture productivity and diversification in the medium to long term and contribute to poverty reduction.

Objective 2: Streamline procedures and shorten processing time of government processes to reduce the cost of doing business.

Prior Action under DPL I	Trigger for DPL II	Trigger for DPL III
Through the Ease of Doing Business and Efficient Government Service Delivery Act (RA No. 11032) and the CSC-ARTA-DTI Joint Memorandum Circular No. 2019-001, the government has defined a policy framework to simplify ease of doing business (EODB).	The government has operationalized the Anti-Red Tape Authority, created by RA No. 11032.	The government has reviewed and modified complementary regulations to streamline government processes.

36. Despite its positive economic performance, the Philippines remains a challenging country for private sector development. The Philippines ranked 95th out of 190 countries on EODB according to the Doing Business 2020 report. The business environment is less favorable than in neighboring

²⁶ The Philippine Center for Postharvest Development and Mechanization (PhilMec) for rice farm machineries and equipment, Philippine Rice Research Institute (PhilRice) for the development, promotion, and propagation of inbred rice seeds, the Land Bank of the Philippines (LBP) and Development Bank of the Philippines (DBP) for the credit facility, and PhilMec, PhilRice, Agricultural Training Institute (ATI), and the Technical Education and Skills Development Authority (TESDA) for rice extension services.

²⁷ Calculated as the difference between domestic (wholesale regular mill) and international (Thailand 25% broken free on board (FOB) plus 15% shipping cost) rice prices as percent of international rice prices. Source: Food and Agriculture Organization (FAO).



countries like Malaysia (12), Thailand (21), Vietnam (70), and Indonesia (73). Among the Association of Southeast Asian Nations (ASEAN) countries, the Philippines registered the most significant improvement in both rank (+29) and the EODB score (+5.12) relative to 2019. However, starting a business (topic rank 171) is especially cumbersome, given the time and number of procedures needed. For many industries, multiple operating permits and licenses are required from agencies that need to be renewed on an annual basis. These cumbersome regulations limit competition by providing protection for incumbent firms, particularly in key services for competitiveness such as telecommunication, transportation and logistics.²⁸ With the enactment of RA No. 11032 and its ongoing implementation by the ARTA, all existing business-related regulations shall undergo review to ensure that these will not cause undue burden to the public.

37. The government of the Philippines has made major progress in recent years to overcome the tremendous regulatory burden that restricts trade, competition, and private investments. The enactment of the Ease of Doing Business and Efficient Government Service Delivery Act (RA No. 11032) in May 2018 and approval of the CSC-ARTA-DTI Joint Memorandum Circular No. 2019-001, the IRR in July 2019, support the undertaking of the government in ensuring that regulations do not add undue regulatory burden and cost, which restricts trade, competition and private investments. The law requires shortening of processing time for government transactions to 3, 7, or 20 days depending on complexity as well as the greater use of automation to facilitate the application processes and minimize the face-to-face contact among citizens and government officials. In addition, a government body, the ARTA, was created to implement the reform by enhancing government capacity in permit issuances and the analyses of business regulations through regulatory impact assessment (RIA).

38. The DPL series supports follow-up actions to implement the reforms. Given its recent establishment, there is a need to fully operationalize the ARTA as part of the activities to fully implement the law. This can be undertaken by ensuring a clear organizational structure, proper staffing, regular budget allocation, and defined standard operating procedures to ensure that the ARTA is able to exercise its function of monitoring compliance with the law. Thereafter, the ARTA will focus on exercising oversight functions in the streamlining of processes external to itself by revising and updating the necessary regulations of other government agencies’ procedures to comply with the new processing time requirements of government processes. Many agencies have already started this process.

Expected results: Supported measures are expected to reduce the cost of doing business in the Philippines by expediting the process of opening a business by reducing the number of days to start a business, and by reducing the compliance costs by reducing the number of procedures to start a business.

Objective 3: Increase competitiveness through better access to economic opportunities.

Prior Action under DPL I	Trigger for DPL II	Trigger for DPL III
Through the Philippine Identification System Act (RA No. 11055) and Implementing	The government has piloted the registration for Philippine Identification System (PhilSys)	The government has launched the nationwide registration for PhilSys and put in place mechanisms for

²⁸ Findings from a Product Market Regulation analysis on the Philippines indicate that market entry is difficult due to high administrative burdens while incumbent protection is mandated in many networks sectors.



Rules and Regulations, the government has created the legal and regulatory framework for a foundational ID system that aims to improve service delivery and financial inclusion for citizens and resident aliens.	for a limited and monitored set of sites and target populations.	authentication for digital service delivery.
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39. Well-designed digital identity systems promote competitiveness by streamlining processes and enabling services to shift from face-to-face to online channels. Digitalized identification can enable efficiencies and expansions in service delivery that make doing business easier. Foundational ID systems²⁹ can boost the accessibility, efficiency and integrity of public and private sector services by automating identity authentication (i.e. removing the need for clients to physically provide multiple certified documents), underpinning electronic signatures (i.e. allowing people to sign contracts without the need for a wet signature), and facilitating interoperability and data exchange between information systems (i.e. by providing a unique identifier and acting as a source of truth on identity). As a result, business transaction costs and delivery times will be reduced, business environment will be improved, encouraging more players and thus promoting competition.

40. The Philippines’ current identity ecosystem is inefficient, fragmented, and potentially exclusionary, especially to the poor. Apart from the civil registry, which records births and other vital events, the Philippines does not have a foundational ID system that is universally and easily accessible to all citizens and residents. Instead, it has 30 different, non-interoperable functional ID systems that each provides a narrow set of benefits to users which leads to exclusion. According to the 2017 Global Findex survey, 45 percent of unbanked adult reported a lack of documentation as a barrier to opening a bank account. Moreover, a significant number of adults are still being denied access to government services (15 percent), government financial support (11 percent), and financial services (14 percent) because they lack an appropriate ID. Furthermore, the poorest 40 percent face disproportionate challenges in accessing government services (19 percent) and government financial support (16 percent), which significantly undermines efforts to lift them out of poverty and to provide them economic opportunities.

41. To address these challenges, the government of the Philippines is establishing the PhilSys as a foundational ID system. With technical support from the World Bank, the PhilSys Act (RA No. 11055) was passed in August 2018 and its IRR was adopted in October 2018, supported by the first operation of the DPL series. PhilSys will be implemented by the Philippine Statistics Authority (PSA). The policy objective of PhilSys is to establish a foundational ID system for all citizens and resident aliens of the Philippines to improve the efficiency, transparency, and targeted delivery of public and social services, to enhance administrative governance, and to strengthen financial inclusion. The existing Data Privacy Act also provides important safeguards with respect to the PhilSys’ collection, use, management, and sharing of sensitive personal data, a key issue not only for identity management but also for broader

²⁹ Foundational ID systems are used for many purposes (e.g. a national digital ID) and thus intended to be interoperable and meet the needs of a wide-range of users, as opposed to functional ID systems, which are for specific purposes (e.g. a driving license or passport).



trust in the digital economy and digital government services delivery. The government is also drawing on lessons from other countries to adopt the latest data protection-enhancing technologies and techniques.

42. The new system will support multiple cases where secure authentication of individuals is needed.

Across public and private sectors, the PhilSys is expected to (i) eliminate barrier for people to access services and economic opportunities, especially the poor and vulnerable populations, who currently face challenges in obtaining robust IDs; (ii) enable government services to be delivered digitally/online, reduce the costs and identity-related fraud and risks, and reduce transactions time, which will make offering services to the poor more economically attractive; (iii) improve targeting of social protection by facilitating greater integrity, interoperability, and integration of systems such as keeping *Listahanan*³⁰ up to date; and (iv) strengthen the government’s ability to respond to calamities by making it easier to identify affected populations.

43. The DPL series will support the implementation of this reform agenda.

The government, through the PhilSys Policy and Coordination Council (PSPCC), approved an Implementation Strategy for PhilSys on February 15, 2019. The strategy includes launching a controlled registration and authentication pilot in selected barangays, with pilot use cases beginning in civil service pensions provided by the Government Service Insurance System (GSIS), Social Security System (SSS), and Philippine Health Insurance Corporation (PhilHealth); bank account opening; and social pension (DSWD). This will be followed by nationwide mass registration, leveraging on an ecosystem of partners to reach the scale needed to register at least 105 million people by the end of 2022.

Expected results: Supported measures are expected to improve access to public services and economic opportunities, especially for the poor and vulnerable populations, by using the foundational ID in the case of public pension, social programs, and bank account opening.

Objective 4: Increase access to financial services through improving payment system infrastructures.

Prior Action under DPL I	Trigger for DPL II	Trigger for DPL III
Through the National Payment System Act (NPSA) (RA No. 11127), the government has established the institutional legal framework with the objective of promoting the safety and efficiency of payment systems and provided the Bangko Sentral ng Pilipinas (BSP) with	The government has operationalized the regulatory framework defined in the NPSA through (i) defining the coverage of payment system operators; (ii) defining the oversight framework; and (iii) designating payment systems.	The government has defined procedures to manage potential disruptions to the payment system.

³⁰ The National Household Targeting System for Poverty Reduction (NHTS-PR), is an information management system that employs geographic targeting, household assessment, and validation in order to provide national government agencies, development partners, and other social protection actors with information on who and where the poor are in the Philippines. This information is then used for the identification and selection of potential beneficiaries for various poverty alleviation and social protection programs.



explicit authority and powers to oversee the payment system.		
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- 44. Payment systems serve as a core financial infrastructure of the financial system, but the Philippines’ financial system is not inclusive, thereby hindering competitiveness.** Firms and individuals rely on well-functioning payment systems to make and receive payments. Payments and payment services are, in their own right, an important part of the overall package of financial services. Secure, affordable, and accessible payment systems support smooth financial transactions by discharging financial obligations in a timely manner, better financial management of firms, and expand access to financial services to firms and individuals, boosting firms’ competitiveness. However, the Philippines’ financial system is not inclusive. Indeed, slow progress in financial inclusion has been observed in the Philippines according to Global Findex. In 2017, 34.6 percent of adults had accounts, only slightly up from 31.3 percent and 26.6 percent in 2014 and 2011, respectively. Bank account ownership in the Philippines is lagging behind the rest of ASEAN 5 countries.³¹ Nonetheless, the number of electronic money accounts have significantly increased in 2018 from a year ago. Moreover, non-bank financial institutions, such as the money service businesses, cooperatives and pawnshops also serve as alternative access points aside from banks.
- 45. However, the Government of the Philippines, championed by BSP, has been implementing a series of reforms to promote financial inclusion.** The Philippines passed the NPSA (RA No. 11127), effective since December 2018, supported by the first operation of the DPL series. It grants clear legal authority to BSP for the policy objective of achieving safe, efficient, and reliable payment systems, mandates BSP to coordinate with other domestic and cross-border government agencies and provides for the design and organization of the payment systems in the Philippines. The design of the payment systems includes the designation of payment systems which consists of payment system operators, participants, and automated clearing houses (ACHs – PesoNet and InstaPay – see below).
- 46. The Philippines has been modernizing its payment systems through efforts such as the launching of InstaPay for fast/instant payments for competitiveness and financial inclusion.** The needs of firms and consumers for continuously available payment services have led to the development of fast/instant payment systems. Fast and instant payments would allow consumers and businesses to send and immediately receive payments at any time and provide recipients the ability to use their funds anywhere they choose. Such instant payments eliminate the risk of online merchants not getting paid, as the release of goods and services can be easily synchronized with the payment. For business-to-business payments, instant payments improve cash flow, make it easier to manage funds, reduce late payments, and speed up the payment of invoices. Under the National Retail Payment System (NRPS) framework, supported by the NPSA, two new automated clearing houses have been launched – PesoNet for batch payments and InstaPay for instant payments. InstaPay allows customers of participating institutions to send and receive funds with savings, current, or e-money accounts. Since its launch in April 2018, the number of participating institutions has reached 44 (of which 29 serve as both receiver and sender of payments).

³¹ Indonesia – 49 percent, Malaysia – 85 percent, Singapore – 98 percent and Thailand – 82 percent, and East Asia and the Pacific Region – 71 percent.



47. The DPL series supports the next steps towards effective implementation of the NPSA. The NPSA aims to promote a level playing field for all participating payment service providers, bringing greater efficiency through digital innovation and promoting competition. The government is currently working on operationalizing the regulatory framework for NPSA. The focus is to clarify the scope of BSP’s licensing and supervisory arrangements, and the payment systems oversight as NPSA provides for a broad span of authorities. For example, the regulatory framework aims at (i) defining the coverage of payment system operators required to be register with BSP; (ii) defining the oversight framework for BSP; and (iii) designating payment systems. In addition, the BSP is currently in the process of defining procedures to manage potential disruptions to the payment system. Effective implementation of the regulation and BSP’s oversight of the payment system would address the current obstacles to achieving efficiency in payment systems such as low usage of electronic payments versus cash and checks and manage systemic risks.

Expected outcome and follow up actions: Supported measures are expected to promote financial inclusion by providing a reliable and accessible payment system for greater use of digital payments.

Pillar II: Enhancing fiscal sustainability

Objective 5: Improve national budget planning and management by adopting an annual cash-based budget and an integrated financial management system.

Prior Actions under DPL I	Triggers for DPL II	Triggers for DPL III
Through DBM Circular Letter No. 2019-4, the government has mandated all national government agencies to adopt Budget and Treasury Management System (BTMS) for transactions above Php1 million.	The government has improved budget monitoring and increased transparency by preparing consolidated financial reports on a cash basis.	The government has published medium-term cash-based expenditure plans. The government has integrated the BTMS with other core financial management systems.

48. The Philippine government has maintained a sustained commitment to modernizing its budget to improve budget planning reliability and cash management. The process began in earnest with the PFM reform Roadmap approved in 2012 and continued into the Duterte administration with further budget modernization initiatives. The World Bank’s 2019 Improving Fiscal Management DPL provided an opportunity to recognize the reform program by supporting the Philippine government’s decision to adopt cash budgeting, to prepare the budget on a cash basis, and to establish PFM reform coordination arrangements across central finance and accountability agencies. By embedding management processes to focus on cash needs, to prepare budget estimates on an annual cash basis



and, to monitor and report in-year on a cash basis, the government is gradually changing a long-established culture of obligations management that has persisted for more than 30 years. The initial impact of the change is expected to be a reduction in the deviation between planned and actual expenditure. Agencies are expected to be more conscious of the value of cash management and more focused on timely program implementation. This will lead to demand for better in-year and end-of-year reporting on budget execution and cash management. It will also lead to increased emphasis on medium-term budget planning to complement annual plans and better anticipate future budget needs.

- 49. Tightening of budget control and improvements to cash-based planning and management has met resistance in Congress.** A draft budget modernization law containing provisions for cash-based budgeting and other reform initiatives including fiscal responsibility provisions, increased financial reporting requirements, confirmation of financial responsibilities of central and line agencies, and strengthening of internal audit was submitted to Congress in 2018 but was not passed. In addition, the approval of the 2019 cash-based budget was delayed which caused a substantial drop in public investment growth and negatively impacted economic growth in the first half of 2019. Determined resistance from members of Congress on several grounds, including cash-based appropriations, resulted in the re-enactment of the 2018 budget for the first four months of 2019. Nevertheless, the President vetoed changes proposed by the congressional bicameral committee and signed the cash-based budget into law at the end of April 2019, exemplifying the government's firm commitment to the reform despite the political pressures from the mid-term elections which took place the following month.
- 50. The events associated with the 2019 budget illustrate that the path for such a significant reform is neither simple nor assured.** It has required continuous effort from the government to maintain and extend the reform achievements. The establishment of a legal basis for cash budgeting is a key step in changing institutionalized behaviors and improving the efficiency of budget planning, management and control. Before the 2019 cash-based budget was approved, obligations-based budgeting had been the entrenched mechanism that resulted in long commitment times and unpredictable demands for cash beyond the fiscal year in which resources were approved. This meant difficulty in estimating budget outturns and limited transparency in actual spending from the budget in any specific year.
- 51. The DPL series continues to support the government in improving budget planning, cash management, and monitoring.** The transition to cash-based budgeting and management will require several years of institutional learning and adjustment. The logical follow-on from cash-based budgets is the preparation of financial reports on a cash basis. This will allow the results of budgets to be compared with the approved plans and allow agencies and other stakeholders to learn from those results in preparing future budgets. Annual cash appropriation is the first step that will eventually require a broadening of focus to the medium term in order to yield improvements for major capital investments which have longer implementation timelines as well as other government programs that extend beyond one year. The government has already started preparing the next phase of reforms by developing and circulating a draft medium-term budget manual to agencies for comment. This will form the basis of further development and refinement of medium-term planning and budgeting arrangements.



- 52. The Philippine government's financial management systems are highly fragmented, a major constraint for proper monitoring of budget execution.** Before the establishment of the BTMS, there was no nationwide financial management system. The quality and reliability of systems vary across agencies ranging from highly sophisticated electronic systems to manual encoding. Attempts have been made in recent years to establish a central system, but none have been completely successful. The consequences of this fragmented system have been a lack of consolidated information for monitoring budget execution during fiscal years and slow reporting of annual expenditure outturns. No consolidated financial reports are prepared in the Philippines.
- 53. The government is committed to improve the quality and comprehensiveness of financial reporting by implementing its new financial management system.** The government completed the development of the BTMS in early 2018 when the Department of Budget and Management (DBM) and Bureau of the Treasury (BTr) became the first oversight agencies to use the system. Other agencies such as the Department of Public Works and Highways (DPWH) and the Department of Trade and Industry (DTI) have already started the training and preparation for the adoption of BTMS during 2018. In January 2019 the Secretary of DBM issued a Circular Letter requiring all national government agencies to use BTMS for high-value transactions (Php1 million or more) by July 1, 2019, supported by the first operation of the series. Replacement of the inefficient and fragmented systems with a single system for all agencies will allow faster and more accurate reporting, real time monitoring, and more timely analyses and responses by budget managers to any deviation from expected progress.
- 54. The decision to incorporate high value transactions from all national government agencies in BTMS during 2019 will accelerate the full deployment of BTMS and speed up the capability for preparation of more timely, comprehensive, and consolidated fiscal reports.** As the government moves to cash budgeting, there will be stronger demand for timely in-year and end-year reports on budget execution, particularly in relation to cash availability, commitments and budget utilization. BTMS will make it possible to produce timely and accurate financial reports. The 2019 Improving Fiscal Management DPL supported the adoption of BTMS as the first step towards the government-wide financial management system in the Philippines. This DPL supports the government's decision to mandate rapid deployment to all central government agencies with transactions exceeding Php1 million. Those transactions represented approximately 90 percent of all expenditures in 2018, in terms of value. Details of smaller transactions can be uploaded to BTMS by agencies within a few weeks after the end of each reporting period, allowing for full details of expenditure to be reported much more quickly than at present. When agencies expand their capability to use BTMS over the coming years, all transactions will be captured at source and entered directly into BTMS so reports will be able to be produced in real time, without having to wait for uploads from other systems.
- 55. The DPL series will support the roll out of BTMS and its integration with other government systems for increased systems functionality.** This includes the establishment of a fully integrated financial management system covering all major elements of financial management such as revenue, payroll, procurement, and asset management. This will allow government and managers to obtain comprehensive, real time information on the financial position of national government as a basis for planning and decision-making.

Expected outcomes: Supported measures are expected to improve government budget planning,



budget monitoring, cash management, and budget execution, resulting in more efficient and effective government programs and services.

Objective 6: Increase tax effort and improve management of contingent liabilities from GOCCs.

Prior Action under DPL I	Triggers for DPL II	Trigger for DPL III
Through RA No. 11346, the government has increased excise taxes on tobacco products, effective January 1, 2020.	The government has rationalized corporate tax incentives to reduce inequities and inefficiencies of the tax system.	The government has implemented a system to identify, monitor, and manage contingent liabilities of the Government-Owned and Controlled Corporations (GOCC).

56. Generating additional tax revenue to finance the government’s growing financing needs is crucial in supporting the government’s inclusive growth agenda. To generate additional tax revenues to finance its growing investment needs in human capital, the Philippine government passed RA No. 10351 in 2013, known as the Sin Tax Reform Law, which increased the excise tax rates on tobacco and alcohol products. The revenues from this law were used primarily to finance the government’s Universal Health Care program. In its first year of implementation, excise tax collections on alcohol and tobacco increased from 0.5 percent of GDP in 2012³² to 0.9 percent of GDP in 2013,³³ and further rose to 1.2 percent of GDP in 2017.³⁴ The TRAIN law further updated excise taxes on sin products, but only for excise tax rates on cigarettes packed by hand and machines. Excise taxes on other tobacco and alcohol products were not updated as part of TRAIN.

57. The government increased tobacco taxes to generate additional funding for the recently passed Universal Health Care law. RA No. 11223, known as the Universal Health Care law, seeks to enroll every Filipino in the National Health Insurance Program, providing access to the entire spectrum of health care services, including preventive, promotive, curative, rehabilitative, and palliative care for medical, dental, mental, and emergency health services. In its first year of implementation, the government estimates a funding gap of Php62 billion, which could increase to Php109 billion by its fifth year of implementation. To generate additional revenue to finance Universal Health Care law, the government passed RA No. 11346, effective starting in January 2020, supported by this operation. The law increases excise taxes on cigarettes packed by hand or machine from Php35 per pack in 2019 to Php45 per pack in 2020, increasing gradually to Php60 per pack in 2023, and by 5 percent yearly thereafter. In addition, the government introduced tax on e-cigarettes to reduce the risks in youth addiction to nicotine in the future.³⁵ Estimated additional revenue from tobacco and vapor product reaches Php14.9 billion in 2020, Php22.4 billion in 2021, and Php26.0 billion in 2022. Incremental revenues from the increase in excise tax collections will be used to finance the implementation of the Universal Health Care Law of 2019.³⁶

³² Broken down as follows: Tobacco excise taxes (0.3 percent of GDP) and alcohol excise taxes (0.2 percent of GDP) in 2012.

³³ Broken down as follows: Tobacco excise taxes (0.6 percent of GDP) and alcohol excise taxes (0.3 percent of GDP) in 2013.

³⁴ Broken down as follows: tobacco excise taxes (0.8 percent of GDP) and alcohol excise taxes (0.4 percent of GDP) in 2017.

³⁵ Evidence shows that since e-cigarettes are tobacco products that deliver the highly addictive and toxic substance nicotine, today’s youth who are using e-cigarettes could become tomorrow’s cigarette smokers to continue to feed their nicotine addiction. Source: U.S. Department of Health and Human Services (2016).

³⁶ 64 percent of total tobacco sin tax is earmarked (40 percent to universal health care, 14 percent to support farmers in tobacco-producing provinces, and 10 percent to national level health expenditure to be determined by the Department of Health).



58. The DPL series supports the ongoing comprehensive tax reform program which aims to further enhance the efficiency, equity, and simplicity of the tax system while generating additional revenue. Several other tax reform packages are currently undergoing deliberations in Congress. The second tax reform package aims to reduce the CIT rate while rationalizing fiscal incentives, resulting in a more simplified corporate tax system with less inequities and inefficiencies. Additional increases in tobacco and alcohol taxes are also under discussion. The third tax reform package attempts to harmonize real property valuation to support a more competitive real estate market and improve the efficiency of land use. The fourth package aims to reform passive income and financial intermediaries by simplifying the tax system, while making it fairer and more efficient. These additional tax reform measures are expected to increase revenue collection, while improving the efficiency, equity, and simplicity of the current tax system, helping ensure long-term fiscal sustainability.

59. In addition, the DPL will support the government in improving its ability to identify and estimate contingent liabilities derived from GOCCs. In 2018, the national government paid Php136.7 billion (0.8 percent of GDP) in subsidies to GOCCs and an outstanding national government advances of Php195 billion (11.2 percent of GDP) as of the end of 2017, mainly for debt servicing paid on behalf of GOCCs. Total government guaranteed debt of GOCCs in 2017 was Php490 billion (3.1 percent of GDP). The Department of Finance (DOF) is primarily responsible for the sound and efficient management of the financial resources of the Government, its subdivisions, agencies and instrumentalities, which includes GOCCs, and responsible for the review, approval and management of all public sector debt, with the end view of ensuring that all borrowed funds are efficiently utilized and all such obligations are promptly serviced by the government. While government has been taking efforts to improve the financial viability of GOCCs and has put in place fiscal risk analysis and management, a more systematic framework of managing fiscal risk from GOCCs, in particular national government’s contingent liabilities and GOCCs obligations, need to be pursued to support fiscal risk analysis currently in place.

Expected results: Supported measures are expected to increase revenue collection and more comprehensive information on contingent liabilities from the GOCCs established, including the risk mitigating measures.

Pillar III: Strengthening financial resilience to natural disasters and climate change

Objective 7: Strengthen management of public assets and fiscal risks to natural disasters and climate change.

Prior Action under DPL I	Trigger for DPL II	Trigger for DPL III
Through DBCC resolution No. 2019-4, the government has established a standing body to formulate and recommend public asset management policies.	The government has issued public asset management policies and guidelines.	The government has adopted a web-based National Asset Registry System at the Bureau of the Treasury (BTr).

60. The government is faced with a dual challenge of weak asset management and high disaster and climate risk. The current legislative framework is limited to asset accounting and asset bookkeeping



with limited policies on asset management, asset insurance, and disaster risk management of public assets. The absence of a single lead agency results in limited institutional accountability for asset management and no consolidated comprehensive registry. For example, the Department of Education (DepEd) had unrecorded property amounting to approximately Php3 billion. This affects effective risk management. Improved management of non-financial assets is especially and increasingly important given the government’s focus on building billions worth of new infrastructure under the Build Build Build program against the backdrop of the country’s high disaster and climate risks.

61. The government is implementing a comprehensive reform to improve the management of its public assets. First, the government created a new Asset Registry Division under BTr, supported by Improving Fiscal Management DPL. Moreover, the government strengthened the institutional framework to formulate a public asset management strategy and policies, supported by the first operation of the series. Through this action, the government has issued Development Budget Coordination Committee (DBCC) Resolution No. 2019-4 establishing a Working Group under the DBCC, comprised of the key oversight agencies and the Office of the President, to establish a common policy on the management of national government non-financial assets and set the ground for a permanent body on asset management. Improved public asset information will also provide useful information as the government plans for climate change mitigation measures.

62. The DPL series supports subsequent policy reforms toward better public asset management. Future actions under the series include the issuance of policies and guidelines for asset management.³⁷ Moreover, BTr will continue to develop the national asset registry as the technical support system such as the establishment of a web-based system to facilitate improved access for key agencies. Through these mechanisms, the centralized asset registry will not only be used for direct applications by BTr (e.g. insurance of public assets) but also directly flow into broader applications including asset planning, maintenance, and utilization. Improved asset management and information will be a key input to better preparing for and coping with the fiscal and physical impacts of climate change such as sea level rise and hydro-meteorological disasters. Improved data and policies on public asset also support better planning for post-disaster response and more efficient reconstruction minimizing environmental impacts from delayed or unplanned response.

Expected outcomes: Supported measures are expected to improve public asset management to reduce contingent fiscal risks toward natural disasters and climate change, increase efficiency in the use of public resources, support improved planning and maintenance of public infrastructure, and inform climate change mitigation policies.

Objective 8: Improve private insurance market sustainability for natural disasters and climate change.

Prior Action under DPL I	Trigger for DPL II	Trigger for DPL III
Through Insurance Commission Circulars No. 2018-57 and No. 2017-56, the	The government has issued policies to improve	The government has reviewed minimum tariff rates to support sustainable growth of the

³⁷ As per the mandate of the TWG (established through PA8), this will be a policy for the common management of non-financial assets of the national government, including to protect the rights of the government (ownership), mapping of assets, and open data and information (as appropriate) to enable improved efficiency, effectiveness, and risk reduction in asset management.



government has strengthened regulatory and supervisory capacity of the Insurance Commission to ensure a sustainable insurance and reinsurance market.	catastrophe risk insurance.	catastrophe risk insurance market.
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63. The Philippine insurance market is characterized by below average penetration rates. In the face of natural disasters and climate risks, limited private insurance not only reduces protection of individuals, but also implies substantial contingent liabilities for the government as it may need to absorb losses of private sector assets that could have been insured. Increasing insurance coverage for households and Small and Medium Enterprises (SMEs) is a key area under the government’s Disaster Risk Financing (DRF) strategy. On the supply side, the government is working towards strengthening the performance of the industry especially for catastrophe risk coverage. A key step in the government’s strategy is strengthening the regulatory capacity of the Insurance Commission (IC), to ensure sustainability of the industry as well as to increase market confidence and industry growth. Changes in the market environment (i.e. increasing global reinsurance, new financial products such as parametric insurance and alternative risk transfer, technology, etc.) likewise make it necessary to revamp current institutional and legal constraints as well as mitigate weaknesses in regulatory capacity to help the industry adapt to these changes. Sustainable growth in the insurance market will also require interventions to strengthen demand for risk management. This is under discussion with the IC and the DOF through supporting advisory services and could be added in future operations depending on the political willingness to tackle this.

64. The government is implementing initiatives to improve regulatory capacity of the IC and capacity of the industry to comply with regulation, supported by this DPL through issuance of Circulars 2018-57 and 2017-56. This prior action addresses key policy gaps and regulatory weakness in the industry. Foremost was the mandatory increase in capitalization and net-worth requirements for insurance companies. This has resulted in consolidating the number of market players to just around half the number before the change in law. The circular letter supported by this operation updated the template and requirements for reporting by the market on reinsurance programs in place to improve the availability of reinsurance information from insurance companies and professional reinsurers, to assess compliance with the Insurance Code, and to have a complete picture on the prudential soundness of the insurance companies and professional reinsurers. This will fundamentally increase the supervisory ability of the IC to ensure a sustainable insurance market to meet any large-scale catastrophic losses.

65. The DPL series supports ongoing government initiatives in further strengthening insurance industry regulation. As a next step, the IC and DOF will review the Insurance Code with the specific objective of strengthening regulation related to catastrophic risk coverage which currently has significant weaknesses and gaps. It will address key issues identified through IC Circulars and ultimately help mitigate government contingent liabilities against natural disasters by effectively transferring the risk to the private sector. In addition, IC will review minimum tariff rates to support sustainable growth of the catastrophe risk insurance market.



Expected outcomes: Supported measures are expected to improve market confidence in private insurance coverage resulting to increased private insurance coverage against catastrophe risks, reduce public contingent liabilities, deepen insurance markets, and contribute to crowding-in of additional financing into financial resilience to disasters and climate change.

Objective 9: Minimize the cost and optimize the timing of post-disaster response.

Prior Action under DPL I	Triggers for DPL II	Triggers for DPL III
The government has implemented its risk layering strategy by setting up a combination of financial instruments to efficiently meet funding needs of disasters of different frequencies and severities.	The government has institutionalized the Disaster Risk Financing (DRF) strategy through a recurrent budget allocation.	The government has adopted regulations to link pre-arranged financing directly to pre-arranged funding channels for rapid response.

66. The Philippines is subject to substantial losses to public and private assets due to natural disasters.

On a long-term average basis, the Philippines is expected to incur Php177 billion (1.0 percent of GDP) per year in losses to public and private assets due to typhoons and earthquakes. In the next 50 years, it is estimated that the Philippines has a 40 percent chance of experiencing losses exceeding Php1.7 trillion and a 20 percent chance of experiencing losses exceeding Php2.7 trillion. Risk management of public assets currently suffers from underinsurance and lack of insurance coverage. Therefore, an adequate financial risk strategy will be crucial to mitigate contingent fiscal risks.

67. The government is implementing a comprehensive national Financial Protection Strategy to enhance the government’s fiscal resilience to disasters and climate shocks. The strategy includes a focus on reforms to strengthen the financial resilience at the national, subnational, and individual levels, with DOF moving ahead to gradually build out its menu of risk financing instruments towards a comprehensive risk layering approach that minimizes the cost and optimizes the timing of post disaster response.

68. The government is advancing the implementation of its risk financing strategy through implementing additional financial instruments, supported by the first operation of the series. This transforms the way government funds the cost of responding to increasing disaster losses and climate risks, away from ad-hoc resource mobilization and towards becoming a pro-active risk manager. The risk layering strategy brings together risk retention and risk transfer through: (i) the allocation of budget for the National Disaster Risk Reduction and Management (NDRRM) Fund and public asset indemnity insurance setting forth in the General Appropriations Act (GAA) 2019 to efficiently manage the cost of frequent but less severe events, and (ii) the allocation of funds for a public asset insurance program to reduce government’s contingent liability and ensure sufficient resource for reconstruction of public assets to enable the renewal and expansion of the parametric catastrophe risk insurance



program to provide rapid liquidity for severe events to government agencies and 25 provinces.³⁸ This strategy builds on the principles of MFD by leveraging private markets where most efficient to complement public funds.

69. The DPL series supports complementary reforms that advance the implementation of this strategy to improve financial resilience to natural disasters and climate change. To institutionalize the government’s budget reforms in support of its risk layering strategy, DRF appropriations will be designated as a “Tier 1 budget allocation” for BTr to be included in the core recurrent budget request for DOF. Reforms to the NDRRM Fund will institutionalize DRF principles through a budgetary mechanism, with regular allocations linked to post-disaster disbursement channels. This will improve the efficiency of post-disaster budget execution, a key challenge in disaster response. This effort is complemented by a parallel program, CAT-DDO3, which would strengthen preparedness planning to ensure the effective use of resources following shocks to mitigate disaster impact on the ground.

Expected outcomes: Supported measures are expected to reduce the cost and shorten response time after disasters by having more or improved financial mechanisms for disaster response in place.

70. The DPL program builds on comprehensive analytical underpinnings ranging from technical assistance projects, economic and sector work, and capacity building programs. This includes both Bank and other development partner programs, alongside government assessments. Table 4 outlines each proposed prior action and their analytical underpinnings.

Table 4. DPF Prior Actions and Analytical Underpinnings

Prior Actions	Analytical Underpinnings
Operation Pillar 1: Promoting competitiveness	
Prior action 1: Through the Rice Liberalization Act (RA No. 11203) and the DA-NEDA-DBM Joint Memorandum Circular Number 01-2019, the government has liberalized the rice import market by shifting from a quantitative restriction system to a transparent tariff system.	Philippines Rice Policy Advisory Services and Analytics (ASA) provides a comprehensive analysis on the relaxation of quantitative restrictions on rice importation. Based on the assessment, removing quantitative restrictions on rice and replacing it with a tariff while implementing a complementary policy reform package aimed at improving support to the farm sector and enhancing agricultural productivity should be implemented. The combination of these measures could boost rice production, while substantially reducing poverty.
Prior action 2: Through the Ease of Doing Business and Efficient Government Service Delivery Act (RA No. 11032) and the CSC-ARTA-DTI Joint Memorandum Circular No. 2019-001, the	Game Changers ASA 2016-2020 supports the government’s reform agenda towards improving competition, by providing TA and capacity building support to the Philippine Competition Commission (PCC). In addition, the World Bank produced the <i>Fostering Competition in the Philippines (2018)</i> report, which details the challenges of the restrictive competitive environment in the Philippines. Advisory Services on Ease of Doing Business 2017-2022 provided advisory

³⁸ (ii) is set forth in the Joint Memorandum Circular by DOF and DBM providing guidelines on the implementation, monitoring, and reporting on the use of Php2 billion allocation under the NDRRM Fund for the insurance linked coverage of government facilities against natural calamities.



<p>government has defined a policy framework to simplify ease of doing business (EODB).</p>	<p>services, technical support, and capacity building to DTI and the ARTA on the simplification of procedures to facilitate EODB.</p>
<p>Prior action 3: Through the Identification System Act (RA No. 11055) and Implementing Rules and Regulations, the government has created the legal and regulatory framework for a foundational ID system that aims to improve service delivery and financial inclusion for citizens and resident aliens.</p>	<p>Identification for Development (ID4D) Diagnostic highlighted challenges and constraints of Philippine current identify system. Key policy recommendations included: (i) universal coverage for individuals from birth to death, free from discrimination; (ii) creation of a platform that is interoperable and responsive to the needs of various users; (iii) protection of user privacy and control through system design; (iv) establishment of clear institutional mandates and accountability.</p>
<p>Prior action 4: Through the National Payment System Act (NPSA) (RA No. 11127), the government has established the institutional legal framework with the objective of promoting the safety and efficiency of payment systems and provided the Bangko Sentral ng Pilipinas (BSP) with explicit authority and powers to oversee the payment system.</p>	<p>Financial market infrastructure (FMI) technical note found: i) the payment system and services in the Philippines are not supported by a well-founded legal basis; ii) current oversight powers of the BSP over relevant payment systems, instruments and services are inadequate; and iii) BSP and any other relevant authorities should submit once again a comprehensive Payment Systems Bill to the Congress.</p>
<p>Operation Pillar 2: Enhancing fiscal sustainability</p>	
<p>Prior action 5: Through DBM Circular Letter No. 2019-4, the government has mandated all national government agencies to adopt Budget and Treasury Management System (BTMS) for transactions above Php1 million.</p>	<p>Public Expenditure and Financial Accountability (PEFA) assessment (2016) identified significant weaknesses in the Philippines public financial management arrangements, particularly budget reliability, financial reporting, procurement, asset management, and Congressional oversight of audit reports.</p> <p>Support to Identify and Develop Strategies to Scale up Budget Execution and Provide Front-line Service Delivery 2017 aimed to support development of an action plan for PFM reform, particularly relating to budget execution and strategies to improve efficiency.</p> <p>Reimbursable Advisory Services (RAS) 2018-2019 provided advice on deployment of the BTMS, integration with other crucial public administration systems, establishment of a comptroller general of financial management, and implementation of the upgraded e-procurement system.</p>
<p>Prior action 6: Through RA No. 11346, the government has increased excise taxes on tobacco products, effective January 1, 2020.</p>	<p>Sin Tax Reform in the Philippines ASA. The World Bank supported the government’s initiative to improve revenue collection through the provision of analytical and advisory work in support of the sin tax reform law prior to its passage in 2012. Chief among these were a set of policy notes prepared in 2012/2013 as part of World Bank assistance to the design of the Sin Tax Law, a series of semiannual sin tax monitoring reports, and an ongoing process of policy dialogue on tax and health reform issues.</p>



	Game Changers ASA 2016-2020 supports the Philippine government with TA for its tax reform agenda through the Game Changers program, providing technical support, capacity building, and just-in-time analysis as requested by the DOF.
Operation Pillar 3: Strengthening financial resilience to natural disasters and climate change	
Prior action 7: Through DBCC resolution No. 2019-4, the government has established a standing body to formulate and recommend public asset management policies.	Improving Public Assets and Insurance Data for Disaster Risk Financing and Insurance Solutions (2017) reviewed with respect to data on disaster exposure and losses and found: i) missing data; ii) data spread across multiple entities; iii) low or irregular frequency of data updates; iv) the basis of asset values being stored limiting natural risk financial analysis; and v) lack of information on the physical location of assets. Developing a Public Asset Registry for the Philippines - Inventory and Conceptual Design (2018) found: i) insufficient and weak legislative framework and asset policies on asset management, and asset insurance; ii) unclear institutional accountability and absence of a single entity for asset data management; iii) significant discrepancies in asset data maintained in property records and books of accounts; and iv) no centralized information and communications technology (ICT) systems for asset management.
Prior action 8: Through Insurance Commission Circulars No. 2018-57 and No. 2017-56, the government has strengthened regulatory and supervisory capacity of the Insurance Commission to ensure a sustainable insurance and reinsurance market.	The Financial Sector Assessment Program (FSAP, 2019) assessment found that the Insurance Commission should further strengthen risk-based regulation and supervision methodologies and capacities, that address insurers’ catastrophe risk accumulation and transfer practices, to enhance risk management and financial viability of the local insurance markets. The legal framework should aim at strengthening insurance supervision and increasing the confidence of the population in the ability of local insurers to pay claims, even in the case of severe natural disasters. This is informed by international experience as set out by International Association of Insurance Supervisors in the 2018 Issues Paper on Climate Change Risks to the Insurance Sector. Ongoing World Bank ASA on DRF has supported the development of these actions.
Prior action 9: The government has implemented its risk layering strategy by setting up a combination of financial instruments to efficiently meet funding needs of disasters of different frequencies and severities.	Supporting the Implementation of the Disaster Risk Financing Strategy of the Government of the Philippines (2014-2018) helped the government carry out the institutional and financial analysis to set out a cost-efficient risk layering framework, demonstrating that the most cost-efficient way is to combine various sources of financing. This includes instruments at the national level (budget reforms; contingent financing, sovereign risk transfer); at the subnational level (improving predictability of funds and risk transfer); and individual level (linking risk financing to social safety nets and promoting insurance). World Bank, Financial Protection Against Natural Disasters: An Operational Framework for Disaster Risk Financing and Insurance (2014) summarizes global experience on DRF. Key lessons for efficient risk financing include: i) combining different financial instruments can minimize the cost of mobilizing post-disaster resources; ii) different instruments should be targeted for specific purposes; iii) improving links between funding sources to contingency plans is key for effective response; and iv) data is key for fine-tuning financial instruments.



4.3. LINK TO CPF, OTHER BANK OPERATIONS AND THE WBG STRATEGY

- 71. The proposed DPL is aligned with the priorities of the new CPF under preparation which builds on the four pillars of the Philippines' SCD.** The new CPF under preparation is structured around three focus areas: (i) investing in Filipinos; (ii) competitiveness and economic opportunity for job creation; and (iii) addressing core vulnerabilities by building peace and resilience. Embedded across the focus areas are the cross-cutting themes of governance and digital transformation to tackle challenges and position the country to opportunities associated with implementation and service delivery.
- 72. The DPL is central to achieving the objectives under the new CPF.** The PDO of the proposed DPL is consistent with, and contributes to, the development outcomes of the World Bank's engagement with the Philippine government in the three focus area proposed in the new CPF. In particular, the reforms supported by this operation towards improving the business climate, strengthening financial inclusion, and promoting competitiveness are long-standing reforms needed to create quality jobs in the Philippines, supporting the goal of accelerating poverty reduction, and achieving rapid and sustained inclusive growth. Moreover, the reforms to enhance fiscal sustainability support the new CPF through the governance cross-cutting theme which will provide government the necessary space and institutional strength to support expansion of human and physical capital investment. Finally, government's efforts to strengthen financial resilience to natural disasters and climate change is directly aligned with the resilience pillar under the new CPF, the World Bank's climate change adaptation agenda.
- 73. The DPL builds on a number of ongoing operations and TA to achieve the outcomes of the Country Partnership Strategy (CPS).** The Bank's analytical work and TA are being extensively used in each of the reform areas of the DPL, and to provide inputs into the design and implementation of reforms. The World Bank continues to provide support in rural development both by providing financing and technical assistance in developing agriculture sector development roadmap. Since 2017, the International Finance Corporation (IFC) has provided advisory services support to the DTI and the ARTA on the simplification of procedures to facilitate the design and implementation of EODB. Meanwhile, a detailed ID4D Diagnostic, together with its ID4D initiative, provided analytical support to PhilSys. In support of ongoing PFM reforms, the Bank has provided support through a RAS agreement since 2018 providing advice on implementation of the BTMS, redevelopment of the Philippine Government Electronic Procurement System (PhilGEPS) and linking disparate financial management systems across government with BTMS. To enhance the capacity of the government to manage the impacts of natural disasters, the Philippines had a CAT-DDO DPL in 2011, a second one since 2015, and is preparing a new one in 2019, complemented by multi-sectoral and partly trust-funded ongoing TA. Finally, in the area of tax policy, the Bank provides analytical and advisory services through the Game Changers ASA, which is partly supported by Australia's Department of Foreign Affairs and Trade.

4.4. CONSULTATIONS AND COLLABORATION WITH DEVELOPMENT PARTNERS

- 74. The World Bank Team conducted extensive consultations with the Philippine government in the preparation of this new DPL series.** The Bank team has engaged various government counterparts in



policy dialogue in the preparatory stages of this operation. The government has designated the DOF International Finance Group as the Bank's main counterpart in the policy dialogue and monitoring of the operation. Policy dialogue, monitoring, and evaluation of the program supported by this DPL are shared with DBM, BTr (which is an attached agency of the DOF), National Economic and Development Authority (NEDA), PSA, BSP, ARTA and DA.

75. The government conducted consultations with different stakeholders for the preparation of the DPL series. The government held a formal consultation specific to the DPL series on in April 11, 2019 in Washington DC in which the government, private sector, academe, think tanks, civil society, other governments, foreign investors, and multilateral agencies discussed the country's development priorities and challenges, and exchanged reform experiences with other governments in the areas of promoting competitiveness, enhancing fiscal sustainability, and strengthening financial resilience to natural disasters and climate change. The government also conducts regular consultations with implementation agencies to get updates on the progress of reforms as well as to ensure adequate staffing and resources allocation.

76. The World Bank Team consulted with stakeholders to present the proposed DPL series and hear the stakeholders' views on the DPL's potential benefits and issues. The team met with business groups in Baguio in Luzon and Davao in Mindanao, as well as the academe and non-governmental organizations (NGOs) in Manila and Davao. The representatives from civil society and the private sector agree that the DPL series constitutes a package of reforms that can catalyze the country's development agenda. In addition, civil society representatives highlighted the challenges in implementing the reforms and the convergence that is needed among government agencies.

5. OTHER DESIGN AND APPRAISAL ISSUES

5.1. POVERTY AND SOCIAL IMPACT

77. Government actions supported in this DPL are expected to have positive poverty and social impacts. The analysis carried out on the potential impacts of the reforms supported under this operation suggests a positive impact on poverty and social development indicators. Measures under the promoting competitiveness pillar such as the rice liberalization, establishment of the foundational ID system, and enhancements in the national payment system are expected to improve the welfare of the poor as they are expected to lower the price of rice and improve the accessibility and delivery of public services including the social protection programs. Other reforms under the enhancing fiscal sustainability pillar will improve government spending efficiency and increase revenue collection to finance new investment in physical and human capital, ultimately benefiting the entire population. Actions under the strengthening financial resilience to natural disasters and climate change pillar are also expected to improve welfare of the poor as they are less resilient to natural disasters and will therefore benefit more from faster post-disaster financial response.

78. Rice import liberalization is expected to benefit the poor directly, although some farmers might be negatively affected in the short term. By liberalizing the importation of rice, it is expected that price of rice will decline, benefiting everyone in the country, especially the poor. However, rice is one of the



main agriculture products of farmers. As the price of rice declines, rice producers (palay and farm workers and rice millers) who derive their income from rice sales will be negatively affected. However, mitigation measures are being designed. For instance, the rice liberalization act states that the RCEF will be set up to assist the farmers during the transition period by providing them machinery and equipment, credit assistance, extension services, and seed development programs, to help rice farmers to become more productive and competitive. In the long run, as more farmers move to higher value-added crops, their income will increase, further contributing to poverty reduction.

79. A detailed analysis shows that net rice consumers will gain access to cheaper rice prices and net welfare gain is positive. Rice imports are estimated to increase by 161 percent due to rising demand and reduced domestic production. Around 239,000 hectare (ha) of irrigated rice and another 145,000 ha of rainfed rice farms are projected to be out of production by 2025. Other crops such as oilseed and coconut, fruits and vegetables, sugarcane and pulses are anticipated to be produced in expanding land areas, presumably but not exclusively, from the shifting of farms from less profitable crops like rice to these relatively more profitable commodities as well as from increased demand. Under a medium price assumption, the benefit to consumers far outweighs the loss to producers, by a factor of about 4:1. Retail price will be 20 percent lower than without rice import liberalization, while palay price will be 30 percent lower. The net welfare changes for society represents less than one percent improvement in real income. As a percentage of baseline food expenditure, the lowest decile obtains the largest increment in real income at 5.5 percent. The percentage change declines as per capita income decile rises, dropping to just 0.15 percent for the top decile.

80. Overall, food security will improve, while malnutrition is expected to decrease. Only 4 percent of the overall population are net rice producers with a larger incidence for the lower deciles (i.e. maximum share is 5.7 percent for the second decile, just under the poverty line).³⁹ Because of increased availability and access to more affordable rice, per capita consumption of rice and daily calorie consumption are anticipated to improve, contributing to better food security for the country. Per capita rice consumption is expected to boost by 7.1 percent to 121 kg/year by 2025. These enhanced availability and accessibility to staple food is projected to cut the degree of child malnutrition and chronic hunger in the country by 3.1 and 15.4 percent, respectively, in 2025.

81. The introduction of a robust and inclusive foundational ID system is expected to benefit the poor through better access to public and private services. Evidence from other countries' experience in introducing robust and inclusive ID systems strongly suggests that social returns will be high. These include enabling access to public and private sector services for everyone in the country, specially the poor as they are qualified for social protection programs; reducing transaction costs; and facilitating the protection of vulnerable group and humanitarian responses. In addition, a robust and inclusive ID system will improve financial inclusion. In the Philippines, 14 percent of respondents were denied financial services due to lack of ID. Foundational ID systems can facilitate the opening of access to the financial and banking systems, helping banks and other service providers (e.g., credit agencies, mobile phone providers) fulfil Know Your Customer (KYC) requirements by ensuring that individuals have access to government-recognized IDs and to establish reliable credit histories. Therefore, the new foundational ID system is expected to improve access to financial services of the poor.

³⁹ Note that net rice producers are found even up to the top deciles (though the sub-population share declines with income).



82. Measures related to revenue mobilization are expected to benefit the poor in the long term.

Although higher sin tax on tobacco might lead to short term welfare loss to the poor given their relatively higher consumption of tobacco than richer households, long term welfare gains come from better health and lower medical spending. For instance, after the passage of the 2013 Sin Tax Reform law, smoking prevalence declined from 22.5 percent to 18.7 percent. Such a decline is unarguably expected to contribute to lower health risks from smoking which is the second most important risk factor of disease in the Philippines.⁴⁰ In addition, the additional revenue derived from tobacco taxes will be used to finance universal health care, benefitting the poor the most. This has been the experience with the 2013 Sin Tax Law which increased tobacco excise collections from 0.6 percent of GDP in 2012 to above 1 percent of GDP in 2013-17. As a result, the number of Filipino households whose health insurance premiums were subsidized by the national government almost tripled from 5.2 million primary members in 2012 to 15.2 million in 2017, thereby providing more buffers from negative health shocks, especially to poor and near-poor households. According to the Department of Health (DOH), Php48 billion (0.3 percent of GDP) or 67 percent of incremental revenue for health was allocated for the enrollment and coverage of indigent families and members of the informal economy.⁴¹

83. Measures related to public financial management and financial resilience to natural disasters and climate change are not expected to directly impact poverty or the distribution of incomes. However, indirect effects could occur. For example, a more strategic response to fiscal risks from natural disasters and climate change, and a more efficient public financial management may free up resources for social development spending.

5.2. ENVIRONMENTAL ASPECTS

84. The environmental impact of the reform actions supported by the DPL are estimated to be positive overall. Ongoing World Bank operations and ASA are working with the government to address technical barriers to enable the adoption of risk informed approaches to development, including through the integration of climate change and disaster risk assessments in public investment projects and environmental risk assessments. Improved public asset information supported under this operation will feed into ongoing work to enable more risk informed development planning by the government. Arrangement of dedicated funding for asset rehabilitation will support the provision of sufficient funding for reconstruction to ensure that public investment projects can be carried out more rapidly and to the required level of design as set out in government environmental impact assessment requirements.

85. Reforms are being undertaken by government to address the underlying social, economic, and environmental vulnerabilities to reduce the impact of disasters and climate change. The

⁴⁰ Moreover, the deterring effect of price increases is likely to be more potent for the poor whose limited incomes make them more price elastic. Empirical research in China, Indonesia, the UK, and the US suggest that smoking prevalence changes are more sensitive in among lower-income households. Thus, the positive consequences derived from less or quitting smoking, such as reductions in medical expenses and increases in working years, is also concentrated on the poor.

Source: World Bank (2019), Is Tobacco Taxation Regressive? Evidence on Public Health, Domestic Resource Mobilization, and Equity Improvements.

⁴¹ Department of Health (2018) Sin Tax Law Incremental Revenue for Health Annual Report.



government has taken a comprehensive multi-hazard focus, which includes simultaneous consideration of the various types of geological and/or hydro-meteorological hazards. In managing natural disaster risks, it is essential to determine the existing vulnerability of communities and infrastructure to climate variability and extremes and prevent natural hazards from translating into disasters. The ability of communities to cope with and recover from climate extreme events and other natural hazards is of key importance. To date, the government has initiated the tagging and tracking of climate change expenditures to enable policymakers to take stock of the national climate change response and to assess the institutional readiness for scaling up access to and delivery of climate change finance.

86. The Philippines has a framework to assess the environmental impact of major infrastructure projects, which will apply to reconstruction projects enabled through the public asset insurance pilot supported by this operation. The Department of Environment and Natural Resources (DENR) is responsible for the Environmental Impact System (EIS), which assesses the environmental impacts and risks of major construction projects. The Bank has supported the incorporation of climate risk in the EIS, supported by a guidebook, a revised set of technical guidelines, and a continuing training program for DENR staff at the national and regional offices. A Climate Change Adaptation and Mitigation – Disaster Risk Reduction (CCAM-DRR) Roadmap was approved by the Cabinet Cluster in 2018, with an overall goal of creating ‘Climate- and disaster-resilient communities supporting equitable and sustainable development’. DENR is mandated to oversee the implementation of the said cluster’s Program Convergence Budgeting where indicators and programs, projects and activities are laid out in the National Expenditure Program for 2018 and beyond.

5.3. PFM, DISBURSEMENT AND AUDITING ASPECTS

87. The Philippines has improved public financial management at the national level over the last decade. The 2016 PEFA assessment indicated that 3 of the 7 PFM pillars (transparency, policy-based budgeting, and asset and liability management) are strong and have improved since the 2010 assessment. The financial statements of government agencies are audited annually, latest one available was for 2018. There were no major qualifications on the DOF annual financial statements in the most recent year and most matters raised in previous years’ audit reports were fully or partially addressed. The national government budget is made available to the public online through the DBM website, from the budget proposal stage (the National Expenditure Program), until it is signed by the President of the Philippines and made effective through the GAA.

88. The government continues to make strides in the PFM reform agenda. The previous DPL series supported the formulation and then adoption of a Unified Accounts Code Structure to be used across budgeting, accounting and reporting. A Treasury Single Account has been implemented and BTr is working to expand its coverage. The most recent stand-alone DPL for improving fiscal management and this operation included actions to strengthen budget preparation, cash management and adoption of the BTMS as the basis for a single national government financial information system. In January 2019 the Secretary of DBM issued a circular requiring all national government agencies to use BTMS for high value transactions (Php1 million or more) by July 1, 2019. DBM is also developing links with other financial management systems including fiscal planning and budget preparation, procurement and payroll. In addition, to improve budget predictability and execution, the



government has gradually tightened the validity period for obligations since 2014 until 2019 when an annual cash budget was adopted. The adoption of cash appropriations effectively limited the validity of obligations to the year funds are appropriated.

- 89. Coupled with these are many steps to strengthen procurement which started with the passage of the Government Procurement Reform Act (RA No. 9184) in January 2003.** Several measures were taken under this Act to address systemic procurement corruption including inter alia the mandatory use of public bidding, periodic monitoring and evaluation of the performance of the procurement system through the Agency Procurement Compliance and Performance Indicator system and the mandatory use of electronic procurement and framework contracting. In recent years, the Government Procurement Policy Board (GPPB) developed the policy on organization, staffing and competency requirements for professionalization, standardized all procurement documents and harmonized them with development partners.
- 90. The Philippines posted steady improvements in terms of the overall Open Budget Index (OBI) over the past decade.** From an overall OBI score of 51 in 2006, the Philippines' score improved to 55 in 2010, before reaching a score of 67 in 2017, ranking 19th worldwide. In 2014, the Philippines was one of the pilot countries for the IMF's revised Fiscal Transparency Evaluation (FTE). The Philippines FTE report was published in June 2015. The government is committed to pursuing further public financial management reforms to enhance fiscal transparency through the timely provision of complete and accurate information, which will be facilitated by deployment of the BTMS.
- 91. The adequacy of the foreign reserves control environment in the BSP is based on domestic assessments.** The Philippines does not have an active IMF program to develop safeguard assessments. The BSP is also not subject to international audit. BSP's financial statements are audited by the Commission on Audit (COA) and the World Bank and IMF have been relying on these audited financial statements. The auditor's opinions for BSP audited financial statements related to calendar years 2016 to 2018 are unmodified (unqualified). However, the audit opinions contain an "Emphasis of Matter" paragraph relating to deviation from Philippine Accounting Standards 21 relating to the booking of realized and unrealized gains and losses due to the change in exchange rates. The paragraph reflects the auditor's judgment that the matter is fundamental to users' understanding of the financial statements. The auditor's opinions are not modified in respect to the matter emphasized and remained unmodified.
- 92. The proceeds from the loan will be deposited in USD into a deposit account at the BSP that forms part of the foreign exchange reserves** once the loan becomes effective and the Bank is satisfied with i) the progress achieved by the government in carrying out the program, ii) the adequacy of the government's macroeconomic policy framework, and iii) submission of withdrawal application in required format in US Dollar. Immediately after disbursement of the loan, the government will ensure that the loan amount is promptly accounted for in the government's budget system and transferred to the Philippine peso bank account, and thereby is available to finance budget expenditures. The government will provide a written confirmation to the Bank within 30 days that this accounting and transfer has been completed, including the exchange rate applied to convert the loan proceeds into Philippine Peso, and the name and number of the government's bank account in which the funds have been deposited and that the exact amount was received in the account.



93. Disbursement of the loan will not be linked to any specific purchases and no procurement requirements have to be satisfied. The proceeds of the operation would not be used to finance expenditures excluded under the Loan Agreement. If, after being deposited in a government account, the proceeds of the loan are used for ineligible purposes as defined in the Loan Agreement, the Bank will require the Borrower to refund the amount directly to the Bank. The amount refunded to the Bank will be cancelled from the loan.

5.4. MONITORING, EVALUATION AND ACCOUNTABILITY

94. The DOF is the main liaison with the World Bank on budget support operations, including the proposed operation. However, policy dialogue and monitoring and evaluation of the program supported by this DPL are shared with DBM, as well as the BTr (which is an agency of the DOF), NEDA, PSA, BSP, ARTA, DTI, and DA. The government has designated the DOF International Finance Group as the Bank's main counterparts in the policy dialogue and monitoring of the operation.

95. The key results indicators are prepared taking into consideration the country's statistical system, administrative data collection, and government monitoring system. The World Bank will review implementation progress during supervision to validate M&E findings. Please refer to Annex I for the list of results indicators.

96. Grievance Redress. Communities and individuals who believe that they are adversely affected by specific country policies supported as prior actions or tranche release conditions under a World Bank Development Policy Operation may submit complaints to the responsible country authorities, appropriate local/national grievance redress mechanisms, or the WB's Grievance Redress Service (GRS). The GRS ensures that complaints received are promptly reviewed in order to address pertinent concerns. Affected communities and individuals may submit their complaint to the WB's independent Inspection Panel which determines whether harm occurred, or could occur, as a result of WB non-compliance with its policies and procedures. Complaints may be submitted at any time after concerns have been brought directly to the World Bank's attention, and Bank Management has been given an opportunity to respond. For information on how to submit complaints to the World Bank's corporate GRS, please visit <http://www.worldbank.org/GRS>. For information on how to submit complaints to the World Bank Inspection Panel, please visit www.inspectionpanel.org.

6. SUMMARY OF RISKS AND MITIGATION

97. The overall risk rating of this DPL operation is substantial. Using the Systematic Operations Risk-rating Tool (SORT), two of the nine risks categories are rated substantial (Table 5). These two categories are political economy and governance challenges, and weak institutional and implementation capacity. These are key risks that, if materialized, could adversely impact the government's willingness and ability to implement reforms, and the achievement of the intended positive results. Furthermore, they could also affect the achievement of the PDOs.

98. Political economy and governance risks can weaken or hamper the reforms' momentum. The successful delivery of reforms not only requires policy clarity and commitment, but also consensus



among the government branches on the nature and implementation pace of reforms. Building consensus, however, has been a thorny issue in recent times, manifested in the delayed passage of the 2019 national budget which derailed reform initiatives. Moreover, the unclear timeframe for the passage of the remaining tax reform packages heightens uncertainty among investors. The risk of shifts in political commitment impacting achievement of the PDO are present, given changing alliances in Philippine politics. Nonetheless, a positive news for the administration is that the May mid-term election fared in its favor as the twelve winning senatorial candidates are known to be aligned with the administration.

- 99. Weak institutional and implementation capacity can weigh down the effective implementation of reforms.** Risks related to institutional capacity for implementation and sustainability are substantial. Complex inter-government relations and sometimes overlapping mandates across public agencies often present implementation challenges. The risk of backtracking on reforms remains if pressures from vested interest arise. In addition, bureaucratic implementation capacity maybe compromised through a shortage of managerial staff, lack of incentives to perform, and fragmentation in the bureaucracy.
- 100. The DPL builds on a dialogue with a strong economic team in the Philippines to ensure policy commitment.** This dialogue provides the assurance of policy consistency and ownership of the reform objectives, not only of the oversight agencies, but also of the line agencies which will execute the reform initiatives on the ground. Open communication between the Bank and its counterparts is established to assure ongoing confirmation concerning the specific areas of support under the DPL, and immediate consultation in case of adverse developments. The DPL requires review and sign-off by the president and thus accentuates that the program be fully aligned with core priority reforms of the administration.
- 101. Ongoing TA supports the government in its delivery of reforms.** The past DPLs have highlighted that in addition to strong ownership, a continuous and responsive policy dialogue across agencies and branches of government is critical to supporting the government in the implementation of its priority reforms. In many cases, this has involved just-in-time and strategic support to draw in global experience to advance reform tracks. Numerous TAs and advisory works are ongoing in support of the key pillars of this proposed DPL operations.
- 102. The DPL is selective in supporting substantive inclusive growth actions.** The DPL series select game changing reforms that will take the Philippines to a higher growth path. It focuses on a small number of sectors allowed for easy convergence. It also limits the dependence on actions across various levels of government and agencies. The decision was also made to only include already fully legislative approved actions. Past operations have shown that legislative approval of particular actions can be highly uncertain, and bills and their content can change significantly in the legislative process. The risk of reform reversal remains as a residual risk.



Table 5. Summary Risk Ratings

Risk Categories	Rating
1. Political and Governance	● Substantial
2. Macroeconomic	● Moderate
3. Sector Strategies and Policies	● Moderate
4. Technical Design of Project or Program	● Moderate
5. Institutional Capacity for Implementation and Sustainability	● Substantial
6. Fiduciary	● Moderate
7. Environment and Social	● Moderate
8. Stakeholders	● Moderate
9. Other	● Moderate
Overall	● Substantial



ANNEX 1: POLICY AND RESULTS MATRIX

Prior Actions and (Indicative) Triggers			Results
Prior Actions under DPL 1	(Indicative) Triggers for DPL 2	(Indicative) Triggers for DPL 3	Medium term results indicators
I. Promoting competitiveness			
<p>Prior Action 1: Through the Rice Liberalization Act (RA No. 11203) and the DA-NEDA-DBM Joint Memorandum Circular Number 01-2019, the government has liberalized the rice import market by shifting from a quantitative restriction system to a transparent tariff system.</p>	<p>(Indicative) Trigger 1: The government has established clear and transparent eligibility criteria for accessing the Rice Competitiveness Enhancement Fund (RCEF) and has updated the registry system for basic sectors in agriculture (RSBSA) as per Art. 14 of the DA-NEDA-DBM Joint Memorandum Circular Number 01-2019.</p>		<p>Result: Reduced gap between domestic and international price of rice.</p> <p>Indicator: The gap between domestic and international price of rice calculated as domestic price – international price as percent of international price (in percent) (Baseline 2018: 76; target 2022: less than 50)</p>
<p>Prior Action 2: Through the Ease of Doing Business and Efficient Government Service Delivery Act (RA No. 11032) and the CSC-ARTA-DTI Joint Memorandum Circular No. 2019-001, the government has defined a policy framework to simplify ease of doing business (EODB).</p>	<p>(Indicative) Trigger 2: The government has operationalized the Anti-Red Tape Authority, created by RA No. 11032.</p>	<p>(Indicative) Trigger 1: The government has reviewed and modified complementary regulations to streamline government processes.</p>	<p>Result: Reduced number of days and number of procedures to start a business.</p> <p>Indicator: Doing Business Indicator “# of days to start a business” (Baseline 2018: 13; target 2022: less than 8)</p> <p>Indicator: Doing Business Indicator # of procedures to start a business (Baseline 2018: 31; target 2022: less than 20)</p>
<p>Prior Action 3: Through the Philippine Identification System Act (RA No. 11055) and Implementing Rules and Regulations, the government</p>	<p>(Indicative) Trigger 3: The government has piloted the registration for Philippine Identification System (PhilSys) for a limited and monitored set</p>	<p>(Indicative) Trigger 2: The government has launched the nationwide registration for PhilSys and put in place mechanisms for authentication</p>	<p>Result: Foundational ID widely used.</p> <p>Indicator: Use of the foundational ID (Baseline 2018:0; target 2022: bank account opening, civil service pension</p>



has created the legal and regulatory framework for a foundational ID system that aims to improve service delivery and financial inclusion for citizens and resident aliens.	of sites and target populations.	for digital service delivery.	payments, and other pension payments)
Prior Action 4: Through the National Payment System Act (NPSA) (RA No. 11127), the government has established the institutional legal framework with the objective of promoting the safety and efficiency of payment systems and provided the Bangko Sentral ng Pilipinas (BSP) with explicit authority and powers to oversee the payment system.	(Indicative) Trigger 4: The government has operationalized the regulatory framework defined in the NPSA through (i) defining the coverage of payment system operators; (ii) defining the oversight framework; and (iii) designating payment systems.	(Indicative) Trigger 3: The government has defined procedures to manage potential disruptions to the payment system.	Result: More widespread electronic payments. Indicator: Share of electronic payment transactions among all (retail) payments (in percent) (Baseline as of 2013: 1, target 2022: more than 25)
II. Enhancing fiscal sustainability			
	(Indicative) Trigger 5: The government has improved budget monitoring and increased transparency by preparing consolidated financial reports on a cash basis.	(Indicative) Trigger 4: The government has published medium-term cash-based expenditure plans.	Result: Improved budget execution. Indicator: Budget utilization rate as measured by the ratio of current obligations to total current budget (in percent) (Baseline as of 2016: 83, target 2022: not lower than 88)
Prior Action 5: Through DBM Circular Letter No. 2019-4, the government has mandated all national government agencies to adopt Budget and Treasury		(Indicative) Trigger 5: The government has integrated the BTMS with other core financial management systems.	Result: Improved real time monitoring and planning of government financial position.



<p>Management System (BTMS) for transactions above Php1 million.</p>			<p>Indicator: Number of public financial systems integrated with BTMS (Baseline 2018: 0; target 2022: no less than 3)</p> <p>Result: All government transactions are included in the BTMS and national government agencies use BTMS for recording, accounting and reporting of all their finances.</p> <p>Indicator: Number of national government agencies using BTMS for recording, accounting and reporting all their finances (Baseline 2018: 2; target 2022: no less than 50)</p>
<p>Prior Action 6: Through RA No. 11346, the government has increased excise taxes on tobacco products, effective January 1, 2020.</p>	<p>(Indicative) Trigger 6: The government has rationalized corporate tax incentives to reduce inequities and inefficiencies of the tax system.</p>	<p>(Indicative) Trigger 6: The government has implemented a system to identify, monitor, and manage contingent liabilities of the Government-Owned and Controlled Corporations (GOCC).</p>	<p>Result: Increased tax revenue.</p> <p>Indicator: Tax revenue as share of GDP (in percent) (Baseline 2018: 14.7; target 2022: more than 15.2)</p>
<p>III. Strengthening financial resilience to natural disasters and climate change</p>			
<p>Prior Action 7: Through DBCC resolution No. 2019-4, the government has established a standing body to formulate and recommend public asset management policies.</p>	<p>(Indicative) Trigger 7: The government has issued public asset management policies and guidelines.</p>	<p>(Indicative) Trigger 7: The government has adopted a web-based National Asset Registry System at the Bureau of the Treasury (BTr).</p>	<p>Result: Increased percent of public assets included in the asset registry.</p> <p>Indicator: Share of public assets included in the asset registry for 5 key agencies (in percent) (Baseline 2018: 0; target 2022: more than 60)</p> <p>Indicator: Number of agencies using the</p>



			asset registry (Baseline 2018: 0; target 2022: more than 5)
Prior Action 8: Through Insurance Commission Circulars No. 2018-57 and No. 2017-56, the government has strengthened regulatory and supervisory capacity of the Insurance Commission to ensure a sustainable insurance and reinsurance market.	(Indicative) Trigger 8: The government has issued policies to improve catastrophe risk insurance.	(Indicative) Trigger 8: The government has reviewed minimum tariff rates to support sustainable growth of the catastrophe risk insurance market.	Result: Insurance market sustainability improved. Indicator: Share of companies complying with new reinsurance and catastrophe/property insurance reporting requirements and submitting required information using the new template (in percent) (Baseline 2018: 0; target 2022: more than 75)
Prior Action 9: The government has implemented its risk layering strategy by setting up a combination of financial instruments to efficiently meet funding needs of disasters of different frequencies and severities.	(Indicative) Trigger 9: The government has institutionalized the Disaster Risk Financing (DRF) strategy through a recurrent budget allocation.	(Indicative) Trigger 9: The government has adopted regulations to link pre-arranged financing directly to pre-arranged funding channels for rapid response.	Result: Increased funds pre-arranged for disaster response. Indicator: Number of pre-arranged or improved financial mechanisms for disaster response in place (Baseline 2018: 2; target 2022: more than 4)



ANNEX 2: FUND RELATIONS ANNEX

Philippines—Assessment Letter for the World Bank

October 28, 2019

The Philippine economy continues to expand at a robust pace. Real GDP grew at 6.2 percent in 2018 and is projected to grow at 5.7 percent in 2019. The slowdown mainly reflects government underspending due to a substantial delay in the budget approval by Congress and the 45-day ban on new government projects ahead of the May 2019 mid-term elections, leading to a small output gap. Growth is projected to rebound to 6.2 percent in 2020, led by a normalization of government spending, and supported by the recent monetary easing and continued robust private consumption. After rising markedly in 2018, peaking at 6.7 percent (y/y) in September 2018, inflation has declined recently, recording 0.9 percent (y/y) in September 2019. The decline reflects lower oil prices and measures to stabilize food prices, as well as monetary policy tightening. Inflation is projected at 1.6 percent by end-2019, before increasing to the midpoint of the 2–4 percent target range by end-2020. The current account deficit rose to 2.6 percent of GDP in 2018 due to a larger trade deficit, partly financed by sustained FDI inflows, and is expected to be at slightly lower levels in 2019 and 2020 but still above 2 percent of GDP. Gross international reserves reached US\$86 billion as of end-August 2019, or about 200 percent of the IMF’s reserve adequacy metric. As of September 2019, the peso/US\$ exchange rate had appreciated by 4 percent since October 2018, fully reversing the depreciation in the first three quarters of 2018. Private credit growth has decelerated, to 6.8 percent (y/y) in July 2019 from a high of 15 percent reached in 2018.

While the baseline outlook is positive, the balance of risks is tilted to the downside, including because of risks of weaker-than-expected growth due to global trade tensions and trade-related policy uncertainty, an unexpected tightening of global financial conditions, or weather-related disasters. On the upside, successful implementation of ongoing structural reforms and infrastructure investments could offer the Philippines an opportunity to improve its place in the global production matrix.

The fiscal stance in 2019 is expected to be contractionary, with the government deficit narrowing from 3.3 percent of GDP in 2018 to 2.7 percent, short of the authorities’ target of 3.2 percent. Against the backdrop of underspending in early 2019 and recent weakness in economic activity, the government increased the annual deficit target for 2020–2022 from 3 percent of GDP to 3.2 percent. The revised target implies a moderate, positive fiscal impulse of 0.4 percent in 2020 and a broadly stable public debt-to-GDP ratio just below 40 percent in the medium term. The small fiscal impulse from what is effectively a normalization of government spending is timely and of an appropriate magnitude, given the extent of the recent slowdown and stronger external headwinds. The government should continue to keep public wage increases at prudent levels and raise additional revenue. Implementing the remaining tax reforms, including streamlining tax incentives, increasing excises, and enhancing tax administration, are main priorities in this regard.



The Bangko Sentral ng Pilipinas (BSP) increased the policy rate by 175 bps in 2018 in response to the surge in inflation. With inflation expectations appearing to return to the target band and the real policy rate above the estimated neutral level, the policy rate cuts in May, August, and September this year (by 75 bps cumulatively) are deemed appropriate. With the move to Basle III liquidity requirements, there is also room to continue lowering the reserve requirement ratio (RRR) for commercial banks at a gradual pace (currently 15 percent). The lower RRR would reinforce the role and effectiveness of the policy rate as the primary monetary policy instrument and would also reduce costs of financial intermediation. In this context, the liquidity released by an RRR reduction should be sterilized, thereby leaving the monetary policy stance unchanged. The implementation of the new BSP charter, including the issuance of BSP securities, will further strengthen the operational monetary policy framework.

The financial and corporate sectors weathered well the depreciation of the peso and higher interest rates in 2018. Nonetheless, nonfinancial corporate leverage and balance sheet exposure to exchange rate risks appear to be relatively high by regional standards and warrant vigilance, especially given the risk of credit reacceleration. Greater efforts are needed to improve banking supervision, through the processing of collected accounting data for nonfinancial firms and closer coordination between relevant agencies.

The structural reform momentum has been maintained, with several important reforms adopted in 2018, including rice tariffication, amendments to the BSP Law, Ease of Doing Business (EDB), and national digital ID. Nonetheless, sustained reform efforts are needed. Additional measures could include further lifting restrictions on foreign investment; reducing labor market duality including by increasing flexibility in the labor market; and upgrading the capacity of public administration by leveraging on digital technologies. The AML/CFT framework could be strengthened further by amending the bank secrecy law and making tax evasion a predicate crime.

The Philippines' external position in 2019 was likely in line with medium-term fundamentals and desirable policies (the formal assessment will be made only in the forthcoming 2019 IMF Article IV consultation).

The Philippines is on a standard 12-month Article IV consultation cycle. The 2018 Article IV mission was concluded on July 25, 2018 and discussed by the IMF Executive Board on September 17, 2018.



Table 1. Philippines: Selected Economic Indicators

Population (2018): 106.6 million

Quota: SDR 2,042.9 millions (0.43 percent of total quota)

Main products and exports: electronics, machinery, agriculture products, and business process outsourcing

Key export markets: Hong Kong SAR, Japan, United States, European Union, China, Singapore, and Thailand

	2017	2018	2019 Proj.	2020 Proj.
Output				
Real GDP growth (%)	6.7	6.2	5.7	6.2
Employment				
Unemployment (%)	5.7	5.3	5.2	5.1
Prices				
Inflation (% annual average)	2.9	5.2	2.5	2.3
Inflation (% end period)	2.9	5.1	1.6	3.0
National government finances				
Revenue (% GDP)	15.6	16.3	16.3	16.7
Expenditure (% GDP)	17.9	19.6	19.0	19.8
Fiscal balance (% GDP)	-2.2	-3.3	-2.7	-3.2
On the authorities' presentation (% GDP) 1/	-2.2	-3.2	-2.7	-3.2
General government gross debt (% GDP)	39.9	38.9	39.3	39.3
Money and credit				
Broad money (% change)	11.4	9.0	6.9	8.5
Credit to the private sector (% change)	16.6	15.1	9.0	12.7
3-month PHIREF rate (%) 2/	3.3	6.5
Balance of payments				
Current account (% GDP)	-0.7	-2.6	-2.0	-2.3
FDI (net, % GDP) 3/	-2.2	-1.8	-1.5	-1.4
Reserves (months of imports of goods and services)	8.3	7.3	7.5	6.8
External debt (% GDP)	23.3	24.5	24.2	23.1
Exchange rate				
REER (% change)	-4.5	-2.8

Sources: Philippines authorities, World Development Indicators; and IMF staff projections.

1/ Includes privatization receipts as revenue and excludes the operations of the Central Bank-Board of Liquidators.

2/ Benchmark rate for the peso floating leg of a 3-month interest rate swap. As of December 2018.

3/ In BPM6. A negative value means that the increase in liabilities is greater than the increase in assets.



ANNEX 3: LETTER OF DEVELOPMENT POLICY



Republic of the Philippines
DEPARTMENT OF FINANCE
Roxas Boulevard Corner Pablo Ocampo, Sr. Street
Manila 1004

DEVELOPMENT POLICY LETTER

DAVID R. MALPASS

President
World Bank Group
Washington, D.C.

Dear **President MALPASS**:

The national development objectives of the Government are anchored on the collective long-term vision *Ambisyon Natin 2040*, which envisions a strongly-rooted, comfortable, and secure life for Filipinos by 2040. The Philippine Development Plan (PDP) 2017-2022 is the first plan that is guided by the *Ambisyon Natin 2040*, and is focused on laying a stronger foundation for inclusive growth, a high-trust society, and a globally-competitive economy. Specifically aligned with the thrust to expand economic opportunities, reduce vulnerability of individuals and families and ensuring sound macroeconomic policy, the Government has embarked on several high-impact reform measures that underpin our request for a new development policy loan (DPL) series on Promoting Competitiveness and Enhancing Resilience to Natural Disasters.

This development policy letter outlines our reform program under the new DPL series and expresses our interest in obtaining a USD400 million budget support loan to sustain progress already achieved under the first DPL subprogram (DPL1), and fund Government operations and priority reforms. The program highlights reforms aimed at (i) promoting competitiveness; (ii) enhancing fiscal sustainability; and (iii) enhancing resilience to natural disasters and climate change. It envisions a three-part program supported by three (3) DPL subprograms to be undertaken starting this year until 2022, providing for a strategic timeframe from where the present administration can lay strong foundations which the succeeding policy makers can further build on.

During the period for the DPL1, the Government was able to enact competitiveness reforms, such as the passage of landmark legislations and issuance of their respective implementing rules and regulations: (i) the Republic Act No. 11032 otherwise known as the Ease of Doing Business and Efficient Government Services Delivery Act – a legislation that will cut excessive bureaucratic red tape and address corruption and accountability within the government through streamlined processing of permits and other requirements;(ii) the Republic Act No. 11203 or the Rice Tariffication Law which seeks to provide affordable rice prices for consumers while raising the income of rice farmers; (iii) the Republic Act No. 11055 or the Philippine Identification



System Act that will provide a valid proof of identity as a citizen, as a means of simplifying public and private transactions, promote seamless service delivery, and strengthen financial inclusion; and (iv) the Republic Act No. 11127 or the National Payment Systems Act establishing an institutional framework to promote the safety and efficiency of payments systems. The succeeding subprograms of the present DPL series will further support the implementation of these legislations.

For the second pillar, the Government continues programs aimed at enhancing fiscal sustainability such as mandating national government agencies to adopt the Budget and Treasury Management System (BTMS) for transactions exceeding Php1 million; and increasing excise taxes on tobacco and penalties for illicit trade through enactment of the Package 2+ of the Comprehensive Tax Reform Program. Initiatives that will further enhance and complement these measures are also under way and expected to be delivered within the DPL subprogram 2 period.

Further, to strengthen financial resilience to natural disasters and impacts of climate change, the Government introduces reform actions including the establishment of a standing body that will formulate and recommend public asset management policies; strengthening of the Insurance Commission's supervisory and regulatory capacity to ensure a sustainable insurance and reinsurance market; and implementation of a risk layering strategy by setting up a combination of financial instruments to cost-efficiently meet funding needs during disasters of different frequencies and severities.

The measures presented as part of the DPL series comprise a key subset of the wider measures we are implementing in the context of the *Ambisyon Nasion 2040* and the PDP 2017-2022. The Government remains steadfast in fulfilling its commitment to promote competitiveness, and enhance fiscal sustainability and financial resilience to disasters through the succeeding DPL subprograms and other key avenues. We look forward to the Bank's continued support in this endeavor and in meeting the Government's overall development agenda.

Very truly yours,

CARLOS G. DOMINGUEZ

Secretary of Finance

NOV 13 2019





ANNEX 4: ENVIRONMENT AND POVERTY/SOCIAL ANALYSIS TABLE

Prior Actions	Significant positive or negative environment effects	Significant poverty, social or distributional effects positive or negative
Operation Pillar 1: Promoting competitiveness		
<p>Prior action 1: Through the Rice Liberalization Act (RA No. 11203) and the DA-NEDA-DBM Joint Memorandum Circular Number 01-2019, the government has liberalized the rice import market by shifting from a quantitative restriction system to a transparent tariff system.</p>	No	Yes/Positive
<p>Prior action 2: Through the Ease of Doing Business and Efficient Government Service Delivery Act (RA No.11032) and the CSC-ARTA-DTI Joint Memorandum Circular No. 2019-001, the government has defined a policy framework to simplify ease of doing business (EODB).</p>	No	No
<p>Prior action 3: Through the Identification System Act (RA No.11055) and Implementing Rule and Regulations, the government has created the legal and regulatory framework for a foundational ID system that aims to improve service delivery and financial inclusion for citizens and resident aliens.</p>	No	Yes/Positive
<p>Prior action 4: Through the National Payment System Act (NPSA) (RA No. 11127), the government has established the institutional legal framework with the objective of promoting the safety and efficiency of payment systems and provided the Bangko Sentral ng Pilipinas (BSP) with explicit authority and powers to oversee the payment system.</p>	No	Yes/Positive



Operation Pillar 2: Enhancing fiscal sustainability		
Prior action 5: Through DBM Circular Letter No. 2019-4, the government has mandated all national government agencies to adopt Budget and Treasury Management System (BTMS) for transactions above Php1 million.	No	No
Prior action 6: Through RA No. 11346, the government has increased excise taxes on tobacco products, effective January 1, 2020.	No	Yes/Positive
Operation Pillar 3: Strengthening financial resilience to natural disasters and climate change		
Prior action 7: Through DBCC resolution No. 2019-4, the government has established a standing body to formulate and recommend public asset management policies.	Yes/Positive	No
Prior Action 8: Through Insurance Commission Circulars No. 2018-57 and No. 2017-56, the government has strengthened regulatory and supervisory capacity of the Insurance Commission to ensure a sustainable insurance and reinsurance market.	Yes/Positive	No
Prior action 9: The government has implemented its risk layering strategy by setting up a combination of financial instruments to efficiently meet funding needs of disasters of different frequencies and severities.	Yes/Positive	No



ANNEX 5: Poverty and Social Impact Analysis (PSIA) of the Rice Liberalization Act (RA No. 11203)

Objective of the PSIA: A PSIA of the Rice Liberalization Act (RA No. 11203) is being prepared for the proposed DPL. The objective of the PSIA is to improve the understanding of how the rice policy reforms could directly and indirectly, as well as positively and negatively affect rice consumers and producers, other affected persons, and the society as a whole, with special focus on the poor, both in the short and long term.

Rationale of policy reform: Since 1972, with the establishment of the NFA, then the National Grains Authority, government had intervened heavily in the rice industry. The NFA controlled imports by a system of import licensing and quantitative restrictions, as well as regulation of all aspects of rice marketing, processing, and trade. The Philippines had notified the World Trade Organization (WTO) in 2017 that it is no longer seeking an extension of its special treatment for rice, as it would have required another round of trade concession in other products. However, conformity with WTO will require the amendment of RA No. 8178, the Agricultural Tariffication Act of 1994. Episodes of rising prices which aggravate domestic inflation have turned public sentiment against the status quo in rice policy. In 2018, inflation breached the 4 percent target of the government, largely due to the shortage of NFA stocks. On top of this, NFA persisted as the most heavily indebted GOCC. These considerations strengthened the argument for either its abolition or the revision of its mandate. An emerging consensus was agreed upon by some farmer groups which accepts the policy of tariffication, conditional on the earmarking of tariff collections to rice sector development. Implicit tariffs imposed by quantitative restriction on consumers vary according to how tightly these restrictions were imposed. During the years that allowed minimum imports, implicit tariffs were as high as 120 percent, while in years when restrictions were relaxed, implicit tariffs were in single digits or even negative. In the last two decades, on average, implicit tariffs were at 90 percent.

Enacted reforms: Through the reforms in RA No. 11203, “an Act Liberalizing the Importation, Exportation, and Trading of Rice, Lifting for the Purpose the Quantitative Import Restriction on Rice, and for Other Purposes,” and its accompanying IRR, issued on 5 March 2019, the quantitative import restrictions have been repealed, along with all regulatory functions of the NFA. The NFA was retained but only for the sole function of maintaining buffer stock for emergency purposes. The details on NFA’s streamlining and restructuring are specified in the IRR. As stipulated in the law, tariffs that will be imposed by the Philippine government range from 35 percent for members of the ASEAN; 40 percent for non-ASEAN members for imports below 350,000 metric tons (MT); and 180 percent for non-ASEAN members for imports above 350,000MT. The law allocates at least Php10 billion annually for the Rice Competitiveness Enhancement Fund while rice tariff proceeds in excess of Php10 billion will also be earmarked for support to rice farmers.

Stakeholder analysis: In general, most of the population, who are net rice consumers, will benefit from lower rice prices resulting from cheaper imports. In particular, half of country’s population who live in urban areas will almost definitely be gainers from the reform. The rural population who do not plant rice (e.g. corn, coconut, and sugarcane farmers and fisherfolk) will also reap benefits, including farm workers, even some who work in rice farms. Welfare gains are estimated to be largest for the poorer households, relatively to the baseline, as they allocate greater share of their household budget for rice. At risk from the policy are palay farmers, who are present in every region but are largely concentration in a few regions namely: Region II (Cagayan Valley), Region III (Central Luzon), and Region VI (Central Visayas). There are



also numerous rice farms in Region XII (SOCCSKSARGEN), and in a few other Mindanao regions. Palay farm workers and rice millers, who are usually involved in large industrial operations, are may also be at risk.

Transmission channels: The main effect of the rice liberalization law is the influx of cheap imported milled rice. The effect of the reform is felt primarily through prices: availability of cheap imported rice will bring down the price of milled rice at the retail and wholesale level; in turn this will bring down palay prices. The changes in market incentive will create second-round effects. Consumers may be persuaded to buy more rice as it is cheaper, though due to low elasticity of demand for rice the increase will not be commensurate to the decline in the price (i.e. a 5 percent decline in price will likely stimulate less than 5 percent increase in consumption of rice). Consumers may also make adjustments at the margin from rice substitutes (corn, root crops) back to rice. Initially, specialized rice farmers, traders, and farm workers will absorb the brunt of the income loss from the decline in palay price. The loss will be mitigated over time as they make adjustments to the new set of market incentives. Lastly, the exit of NFA from the rice regulation, and its limited role in the market, will reduce the cost of doing business in the rice industry, and reduce unpredictability owing to discretionary government policy. Its role will now be restricted to maintaining buffer stocks and releasing these during emergency (e.g. natural calamity). On the other hand, it will cease to offer subsidized rice, which in normal periods accounts for about 10 percent of consumption.

Methodology for the quantitative analysis. As the reform is very recent, the assessment will be conducted ex ante. Quantitative analysis aims at the following estimates:

- The short-term impact on the retail price of milled rice, and farmgate price of palay;
- The medium-term impact on the price of milled rice, palay price, together with area harvested of palay and other crops;
- Rice expenditure shares by household group;
- The proportion of households who are net producers of rice, by household group; and
- The shares of rice expenditure in total expenditure of households in various.

To estimate the **short-term impact** of liberalization utilization of the price of rice, the assessment uses a single-commodity, partial equilibrium model of the rice market under the open economy assumption. The model is calibrated to the base data for 2018, based on PSA data for the following:

- Supply and utilization: Production in milled rice, demand (net disposable demand for food), other demand (net withdrawal from stocks, after adjusting for processing, waste, and seed utilization);
- Farmgate price of palay;
- Production of palay; and
- Border price based on Vietnamese White Rice 25 percent.

The price effect of a quantitative restriction is calibrated as a fixed wedge between border price (plus tariff), and the domestic retail price. The change in price in 2019 involves a projected market price with-quantitative restriction; and the projected 2019 prices without- quantitative restriction. Both with-quantitative restriction and without- quantitative restriction scenarios incorporate a shift in demand due to income growth (mediated by income elasticity of demand) and population growth; and supply shifts owing to technological change.

Meanwhile, to estimate the medium-term impact of liberalization on the price of rice, the assessment



uses a general equilibrium model described in Briones (2018), known as Agricultural Market Model for Policy Evaluation – Computable General Equilibrium (AMPLE-CGE) model. AMPLE-CGE is calibrated at a 2016 baseline and is ran to generate annual projections for 2017 to 2021, although only the average for 2019-2021 (the medium-term time horizon) is reported here. The projections are not comparable to the short-term projections owing to the significant differences in model structure.

Estimates of rice expenditure uses Family Income and Expenditure (FIES) data; occupations of household heads are identified by merging FIES with Labor Force Survey (LFS) data for household heads for 2015. Shares of rice expenditure in total expenditure will be disaggregated by decile, poverty status, and by region, on the plausible hypothesis that a given decline in the price of rice will have a larger impact on the household group for which rice accounts for a larger expenditure share.

Similarly, proportion of households who are net rice producers will be disaggregated by decile, by poverty status (poor vs non-poor based on the official poverty line), and by region. Net rice producers are identified as those households whose heads identify their primary occupation as growing of paddy rice; and whose household crop income exceeds household rice expenditure. The hypothesis is that a decline in palay price adversely affects net rice producers. The assessment will try to identify where such households tend to be concentrated (i.e. which income group; whether among the poor; and in which region).

Changes in real incomes disaggregated by household group

The last set of estimates combine the projected short-term changes in price, and converted these to changes in real income, disaggregated by household group.

Results. With quantitative restriction, in 2019 the retail price is expected to drop by about Php2.45 per kg under the low-world price scenario compared to 2018; this corresponds to about Php1.60 per kg drop in palay price. However, with even a medium level world price, the quantitative restriction leads to a higher retail price, as well as a higher palay price. With a high world price, the quantitative restriction leads to an uncomfortably high retail price of nearly Php48 per kg, while palay price soars to Php22 per kg. Without the quantitative restriction, retail and palay prices are much lower; even with the highest world price, retail price still drops to Php38 per kg, while palay price drops to below Php17 per kg. With lower world prices, retail and palay prices drop even lower, all the way down to Php32 pesos retail under the low world price assumption, along with a Php12 peso per kg palay price. Comparing without quantitative restriction (the actual scenario) to with quantitative restriction (the counterfactual scenario), retail price is lower by about 20 percent, regardless of the world price assumed; meanwhile palay price is 28 to 30 percent lower.

Changes in the market price of rice in the short-term

Table 6: Projections for market price of rice, in Php per kg, alternative scenarios for VWR25⁴², 2018-2019

	Milled rice, retail	Palay price
Prices (Php per kg)		

⁴² Vietnamese White Rice 25 percent (VWR25)



2018 Baseline	42.77	18.85
Projections with quantitative restriction		
2019, VWR 25 at USD 332 per ton	40.32	17.25
2019, VWR 25 at USD 358 per ton	43.23	19.15
2019, VWR 25 at USD 398 per ton	47.68	22.06
Projections without quantitative restriction		
2019, VWR 25 at USD 332 per ton	32.42	12.08
2019, VWR 25 at USD 358 per ton	34.70	13.58
2019, VWR 25 at USD 398 per ton	38.20	15.87
Percent change, with quantitative restriction vs without quantitative restriction		
2019, VWR 25 at USD 332 per ton	-19.6	-30.0
2019, VWR 25 at USD 358 per ton	-19.7	-29.1
2019, VWR 25 at USD 398 per ton	-19.9	-28.1

Projections are developed for alternative levels for the average world price, proxied here by Vietnam White Rice 25 percent broken (VWR 25). The levels are: USD332 per ton (the average for the first two months of 2019), which is a low level; the high level at nearly USD400 per ton; and the medium level at USD358 per ton.

Conclusion. The analysis demonstrates that the reform will result in a net gain to society. The benefit to consumers far outweighs the loss to producers, by a factor of about 4:1. The net benefit to society is Php30 billion; while small by national standards (0.64 percent gain in real income), the reform is highly pro-poor, as net benefits tend to be larger as a share in total expenditure for the lower income groups. The explanation is simple: household expenditure on milled rice dwarfs net crop income of net rice producers. Hence a given percentage fall in milled rice expenditure will outweigh the corresponding drop in net rice income; all the more since we expect a percentage drop in palay price correspond to a 1.5 percentage point drop in retail price.