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REPORT AND RECOMMENDATION

OF THE

PRESIDENT

TO THE

EXECUTIVE DIRECTORS

ON A

PROPOSED LOAN

TO

THE REPUBLIC OF THE PHILIPPINES

FOR

A SECOND INDUSTRIAL INVESTMENT CREDIT PROJECT

THROUGH

THE DEVELOPMENT BANK OF THE PHILIPPINES

December 3, 1975

Public Disclosure Authorized

CURRENCY EQUIVALENTS

US$1	=	₱ 7.5
₱ 1	=	US$0.1333
₱ 1 million	=	US$133,000
₱ 1 billion	=	US$133 million

FISCAL YEAR

July 1 - June 30

REPORT AND RECOMMENDATION OF THE PRESIDENT TO THE EXECUTIVE DIRECTORS ON A PROPOSED LOAN TO THE REPUBLIC OF THE PHILIPPINES FOR A SECOND INDUSTRIAL INVESTMENT CREDIT PROJECT THROUGH THE DEVELOPMENT BANK OF THE PHILIPPINES

I submit the following report and recommendation on a proposed loan to the Republic of the Philippines for an equivalent of US$75 million. The loan would have a term of 18 years including 4 years of grace and an interest rate of 8.5 percent per annum. The proceeds of the loan would be relent to the Development Bank of the Philippines (DBP) on the same terms as those of the Bank loan for onlending to specific productive enterprises.

PART I - THE ECONOMY

2. The most recent Economic Report - "Current Economic Position and Prospects of the Philippines" (No. 568-PH of November 7, 1974) was circulated to the Executive Directors on November 11, 1974. A basic economic mission visited the Philippines in April/May 1975 and is now preparing its report. The discussion below includes the findings of the mission. Annex I of this report contains country data.

Recent Developments

3. During the 1960's the economy grew in real terms at the rate of 5-6 percent per annum. However, the rate of growth was less than the level that might have been achieved if the considerable natural and human resources of the Philippines had been exploited more effectively. Moreover, the benefits of growth were not distributed widely and unemployment rose. Low levels of taxation resulted in inadequate public investment in necessary infrastructure and social services. Relatively weak export performance, combined with a failure to reduce the import dependence of domestic industry, resulted in a steady deterioration in the balance of payments position.

4. During 1970-72, the authorities adopted policies of monetary and fiscal restraint in order to lay a firm basis for future growth. With assistance from the Consultative Group, they succeeded in improving substantially the maturity structure of the external public debt. Real GNP during that period increased at about 5 percent a year. In 1972, following severe floods, the President began a series of social and economic reforms in the country including an agrarian reform program, tax reforms, and an administrative reorganization. These programs are beginning to show results.

5. In 1973, there was a sharp increase in the level of economic activity in the Philippines. This upsurge was led by the international commodity boom, which resulted in higher export incomes in the Philippines, a strong recovery in agricultural and industrial production for the domestic market and an expansion in public and private investment. The growth in real GNP doubled to 10 percent.

6. Like most countries, the Philippines was profoundly affected by the tumultuous events in the world economy that began with the jump in the prices for food and petroleum in late 1973. With international trade the equivalent of almost half of its GNP, the Philippines proved quite vulnerable to the impact of world inflation, the increase in oil prices and the prolonged recession in the industrialized countries. This sequence of events has temporarily frustrated the Government's attempt to accelerate the rate of development, and in 1974 GNP increased by only about 6 percent in real terms. While adverse effects of the recession were cushioned somewhat in 1974 by a modest improvement in the external terms of trade, the Philippines has been even more seriously affected in 1975 by the continued rise in import prices and reduced demand for Philippine exports. The real growth of GNP in 1975 is not expected to exceed the level of the previous year. Improvement in the growth performance in 1976 can be expected only if recovery takes place in the economies of the Philippines' main trading partners.

7. Agricultural production has grown at an average rate of 3.2 percent per year during the 1970s, a period which has been affected by unusually adverse weather conditions. Rice production increased by 25 percent in 1973-74, but due to serious damage by typhoons, it grew by only 1 percent in 1974-75, and the Government had to import 200,000 tons in the first half of 1975 to ensure adequate stocks. However, initial indications are that the outlook for rice production in 1975-76 is bright. The Government is giving the highest priority to increasing agricultural production and has initiated a number of programs designed to expand the use of fertilizer, irrigation and supervised credit. It has also intensified efforts to expand social services needed in rural areas, including rural electrification, health and family planning services as well as small-scale road and irrigation projects.

8. Although progress has been slower than initially planned, the Government has moved ahead with its agrarian reform program for the nation's one million tenant farmers who grow rice and corn. By mid-1975, land transfer certificates had been issued to nearly 200,000 tenants and progress had been made on land valuations and the transfer of titles. The Government has raised the cash portion of the compensation package to landlords to reduce their resistance to land reform, but strong administrative efforts will be necessary to ensure continued progress in the implementation of the Program.

9. Industrial production, which grew by 12 percent in 1973 was adversely affected in 1974 by the world-wide economic slowdown and grew by only 3.6 percent in 1975. This sector, which is discussed more fully in Part III of this report, has good growth prospects.

10. The Government has made significant progress in increasing public investment. The ratio of public investment to GNP is currently about 3 percent compared with 1.[illegible] percent in FY72. The Government has also implemented a series of long needed tax reforms and improvements in tax administration. These reforms aided by the increased economic activity, the boom in export incomes, and domestic inflation, resulted in a 36 percent increase in national government tax revenues in FY73, and an estimated 47 percent in

FY74. As a result, the ratio of national government tax revenues to GNP has increased from an average of 9 percent in recent years to an estimated 12.3 percent in FY74. However, because of lower growth of foreign trade and domestic incomes the ratio fell to about 11.5 percent in FY75.

11. In the latter part of 1973, inflation emerged as a major problem in the Philippines and in 1974 consumer prices rose by almost 40 percent. The rise was caused by the large increase in liquidity that came with the export boom in 1973-74, and by a number of cost-push factors, including the higher rate of world inflation. To deal with this problem, the Government adopted contractionary monetary and fiscal policies, and attempted to reduce the impact of inflation on consumers by subsidizing such essential goods as wheat, imported rice, and cooking oil. As a consequence of the Government's measures, the annual rate of inflation decreased to less than 20 percent at the end of 1974 and less than 10 percent as of mid-1975.

12. The rapid inflation in 1974 exacerbated the decline in real wages which had begun in 1970. Overall, there was a decline of about 20 percent in real wages during 1974. In order to offset the deterioration of real wages in urban areas, the Government increased the salaries of Government employees and directed private firms to grant emergency cost of living adjustments to employees earning less than ₱ 600 per month. Nevertheless real urban wage incomes declined and reduced the demand for manufactured products, which contributed to the poor performance of the manufacturing sector in 1974. The depression in the urban areas was partly offset by the improvement in rural incomes that stemmed from continued high prices for agricultural commodities.

13. On the external side, the Philippine balance of payments benefitted considerably from the international commodity price boom during 1973. High prices for the country's chief exports, including coconut products, sugar, copper and wood products resulted in a 70 percent boost in export earnings and a balance of payments surplus of about $670 million. Since mid-1974 the external trade position has deteriorated due to the sharp increase in the price of oil and other imports and less favorable prices for Philippine exports. In 1974, imports nearly doubled while exports rose by only about 50 percent and as a result the balance of payments surplus fell to about $100 million. However, international reserves at the end of 1974 remained comfortably high amounting to about $1.2 billion, equivalent to roughly four months imports.

14. Due to the prevailing recession in the economies of the Philippines' main trading partners, there will probably be a 20 percent deterioration in the terms of trade during 1975 resulting in a decrease in export earnings of about 10 percent. As the import volume is estimated to rise only marginally, partly as a result of the domestic recession, the value of imports will probably rise by not more than 15 percent. The net result of these projected trends is probably that the Philippines may have an overall balance of payments deficit of about $350 million in 1975 and $220 million in 1976. These deficits can be managed without serious pressure on reserves through

utilization of the IMF oil facility (and possibly in 1976 of the extended facility of the IMF) and by short-term foreign borrowing by the Central Bank.

15. The overall level of debt of the Philippines is expected to remain within reasonable limits, as the ratio of debt service payments to exports would average about 16 percent during the rest of this decade. At present, the Bank/IDA share in total debt outstanding is about 8 percent and its share in debt-service is about 5 percent. These shares are expected to increase slowly in the years ahead.

16. Foreign assistance is expected to continue to be of major importance in helping to finance the larger investment expenditures which will be necessary for the country's development. In order to ensure that disbursement of external assistance reaches levels commensurate with the level of development expenditures which will be required during the latter part of the decade, total commitments will need to be maintained in real terms at least at the level of about $500 million which was achieved in 1974. The Consultative Group for the Philippines at its meeting in Paris on October 1, 1975, agreed that it would be reasonable for the Philippine Government to seek aid commitments of about $600 million during 1976.

Growth Prospects

17. Despite the slowdown in the growth of the economy which is primarily a result of worldwide economic conditions, the Government remains committed to regaining the growth momentum which began in 1973 to provide for a continued increase in incomes and employment. High priority must be accorded to expanding employment opportunities - in the short-term as well as the long-term - because unemployment and underemployment are still high and the labor force continues to grow at 3 percent a year.

18. Priority must also be given to expanding food production for the domestic market, to expanding industrial export production and to accelerating development of local energy resources. The difficulties experienced during the last two years in importing sufficient quantities of food at reasonable prices, especially cereals, have increased the Government's resolve to achieve self-sufficiency in rice and corn as soon as possible. The Government rightly recognizes that the increased cost of petroleum and other imports cannot be financed indefinitely by borrowing abroad and it is actively encouraging both local and foreign investors to expand the productive capacity of export industries and to undertake major new import-replacing investments. Because it will take time for these investments to have an impact on the balance of payments, the Government is seeking increased support from the international financial community to help carry out its development program and to ease the adjustment to higher petroleum and other import prices. Because of the substantial easing of the external debt burden which has taken place in the last several years, the Philippines now has the capacity to borrow externally larger amounts of capital in support of its development program.

19. Given the likely availability of resources and the expected growth in various sectors, it is reasonable for the Government to plan for a longer

term growth in GNP of about 7 percent a year in real terms. To achieve this objective increased investments will be needed in a wide range of industries. Public investments also need to be increased. A new public infrastructure program is being prepared, and the Government is putting emphasis on developing nuclear and indigenous power sources and on irrigation, feeder roads and other projects to support increased food production. The Government has made considerable progress in recent years in building up the capacity of public sector agencies to prepare and execute projects. However, there will be a need for continued efforts to strengthen this aspect of administration. The ratio of public investment to GNP will need to rise from the present level of 3 percent to about 5 percent by 1980. To support the level of investment, the Government will need to intensify its tax efforts so that the ratio of national taxes rises from its present level of 11-12 percent to 14 percent by 1980.

PART II - BANK GROUP OPERATIONS IN THE PHILIPPINES

20. The Philippines has received 31 Bank loans and three IDA credits totalling $722.2 million, net of cancellations. About 40% of the Bank/IDA lending, $293 million, has been for infrastructure projects in power, transportation, and water supply whilst $38 million has been for population and education. Of the remainder about $216 million has been for agriculture and about $175 million for industry in four loans for the Private Development Corporation of the Philippines, one loan for the Development Bank of the Philippines and one for small and medium industries. There has been a marked improvement in the way Bank financed projects in the Philippines have been executed in the last three years compared with experience in the 1960s when shortages of peso counterpart funds combined with poor administration to cause serious problems. All these projects are now going reasonably well. Annex II contains a summary statement of Bank loans, IDA credits and IFC investments as of October 31, 1975 and notes on the execution of on-going projects.

21. The Bank's lending program has been designed to continue to support the increased Philippine development effort with its particular emphasis on agriculture and infrastructure. Shortages of domestic revenues led to low investment for these purposes in the past. The last three years have seen major changes which have helped to overcome these constraints and both the ambitious Philippine development program and the Bank's lending program have been designed to make good past neglect and to meet future needs. Commitments in FY74 amounted to $165.1 million, and in FY75 $208 million compared to an average of about $30 million a year in the preceding five years.

22. One loan of $42 million for the Magat Irrigation project has already been approved by the Executive Directors in FY76. In addition to the proposed project, other projects which may be ready for Board consideration in FY76 include livestock, fisheries, grain storage, education, urban development and irrigation.

23. IFC has made commitments in the Philippines totalling $76.2 million for investments in 13 companies in the fields of development banking, power, telecommunications, ceramic tiles, paper, petroleum products, nickel mining and refining, chemicals and synthetic fibers. Of these investments, as of October 31, 1975, $18.2 million have been sold, $0.4 million cancelled and $3.4 million repaid, leaving a net portfolio of $54.2 million. On the same date $2.1 million was undisbursed. Preliminary proposals have been received for an aluminum smelter and other projects in the pulp and paper, dinnerware, metal alloys and shipbuilding fields.

PART III - THE INDUSTRIAL SECTOR AND INDUSTRIAL FINANCE

The Industrial Sector

24. Industry (defined as manufacturing, mining and construction) is the third largest sector in the Philippine economy (after agriculture and services). In 1974, it accounted for almost 30 percent of net domestic product, absorbing over one-third of total fixed investment and providing employment for 15 percent of the total labor force. Manufacturing is by far the largest component of the industrial sector, and in 1974 accounted for 20 percent of net domestic product and for 10 percent of the labor force. Manufacturing enterprises are predominantly privately owned, and generally concentrated in large scale, vertically integrated, capital intensive units. Food and beverages are the largest manufacturing group, followed by chemicals and petrochemicals, and textiles. Geographically, over 65 percent of manufacturing enterprises are concentrated in the Greater Manila and southern Luzon area, although industrialization has been increasing in northern Mindanao and the Western Visayas.

25. Historically, Philippine industrial production was geared primarily to meeting the needs of the domestic market and there has been a heavy reliance on protection policies applied through the tariff system and some degree of import control. In the late 1960s, the Government became aware of the problem implicit in this approach and through the Investments Incentives Act of 1967 and the Export Incentives Act of 1970 has sought to diversify the traditional industrial base and to expand exports and industrial employment. Both Acts are administered by the Board of Investments (BOI) in the Department of Industry (DOI). Under these Acts incentives are provided to enterprises which are undertaking productive investments in those industries which are set out in BOI's annually revised investment and export promotion plans. However, there is growing doubt as to whether these policies have been fully successful in overcoming the effects of the earlier protectionist policies, and the National Economic and Development Authority (NEDA) and DOI are currently studying this matter. For the future the Government's industrial stategy is designed: to expand investments in a few large-scale projects such as wood processing, fertilizer, and copper smelters which will contribute to a major expansion of exports or a reduction in imports; to encourage projects to strengthen and diversify non-traditional exports and allow for greater integration in existing industries; and to emphasize the promotion of small and medium industries

to boost employment generation, encourage regional dispersal of industry and bring production closer to raw materials and markets.

26. The growth rate of the industrial sector fell to 3.5 percent in 1974 compared to 12 percent during the previous year. This decline is primarily a result of depressed demand for Philippine exports on the part of the country's main trading partners and the concomitant slowdown in the rate of economic growth in the Philippines. Nonetheless, the longer-term prospects for industrial growth are very favorable, because of the existence of the natural and human resource endowments of the Philippines and a very active private sector. In recognition of these prospects, applications for planned investments in 1974 were more than twice the level of the previous year.

27. The Four Year Development Plan for FY75-78 estimates that total industrial investment in the period will be about $3.3 billion. The estimates for the period 1976-80 are about $7.4 billion, or about triple the level of investment in the period 1972-75. Investment in manufacturing is expected to account for about 90 percent of this. These levels of investment will require a large and sustained increase in domestic resource mobilization, as well as a steady inflow of foreign capital on reasonable terms.

Industrial Finance

28. The Philippines has a well-developed financial system, but there are insufficient long-term funds available to finance industrial investment. DBP and the Private Development Corporation of the Philippines (PDCP) are the main sources of such finance, and they provide about 95 percent of the long-term finance available to the private sector in the Philippines. Working capital needs are financed mainly by commercial banks, which in 1974 provided $3.6 billion in domestic credit, 30 percent of which went to the manufacturing sector. The remaining gaps in financing are covered by internally generated funds and by equity financing through the capital market. The two long-term financing institutions, DBP and PDCP, accounted for less than 8.5 percent of the Philippines total net financial assets which stood at $12.6 billion at the end of 1974. This low proportion reflects the predominance in the Philippines of institutions and markets dealing in short-term funds. In order to help strengthen the financial sector, the Government has requested the assistance of the Bank, IFC and the IMF to undertake a series of studies of the capital market and the commercial banking system. The proposed loan is expected to help increase the availability of long-term capital in the Philippines by providing financial and institutional support to DBP in its efforts to expand its long term lending to high priority industrial projects.

29. The proceeds of the first loan through DBP (Loan No. 998-PH) have been used to finance a wide variety of sub-projects in textiles, chemicals, energy, edible oil processing, wood processing, milling, mining, machine tool manufacturing and other manufacturing. These sub-projects have estimated economic rates of return ranging from 11% to 80%. The internal financial rates of return for these sub-projects varied from 14% to 50%. DBP expects to approve projects utilizing the entire $48 million available under the first loan by the end of November.

PART IV - THE PROJECT

30. The proposed loan is the eighth in a series of Bank Group loans for financing industrial investment in the Philippines. The most recent of these was a $30.0 million Bank loan for the development of small and medium industry which was approved in May 1975 (Loan 1120-PH). The proposed project was appraised in May 1975 and negotiations were held in October 1975. The leader of the Philippine negotiating team was J.V. de O'Campo, Acting Chairman, DBP. The Appraisal Report (No 872a-PH) on the project is being distributed separately to the Executive Directors. Annex III provides a loan and project summary.

31. The proposed loan of $75 million would help finance the foreign exchange costs of capital goods imports for medium and relatively large industrial sub-projects. Eligible enterprises would include those engaged in manufacturing, agro-industries, mining, ocean shipping and tourism. The proceeds of the loan would be directed mainly towards investments which would: further diversify the non-traditional export base; encourage greater domestic value-added through domestic processing of traditional exports; and encourage intermediate and capital goods production.

32. In addition to increasing the availability of medium and long-term resources for medium and large scale enterprises in the Philippines, the proposed loan would continue the process, begun under the first industrial investment credit loan, of assisting DBP to make institutional improvements. These would include improvements in the caliber of DBP's industrial projects department staff, and its project appraisal and follow-up procedures; a strengthening of DBP's long-term resource base; and an improvement in DBP's financial performance. The project would also provide for material improvements in the quality of DBP's audits which are carried out by the Commission on Audit (COA) and the Central Bank (CB).

33. At the request of the Government, the proposed loan would, as in the case of previous loans for DBP, be made to the Government which would relend the proceeds of the Bank loan to DBP on the same terms as those of the Bank loan. Within DBP the proposed loan would be handled by Industrial Projects Department I (IPD I) as was the case with the first loan. Both the Bank loan and the subsidiary loan from the Government to DBP would be for 18 years including a grace period of 4 years at an interest rate of 8.5 percent per annum. In accordance with Philippine law, the relending rate charged by DBP to sub-borrowers would be 12 percent per annum for loans secured by land and 14 percent for loans which are not so secured (See Section 4.08 of the Loan Agreement). Sub-loans would be committed over the next two years and disbursed over four years. They would be for a maximum term of 15 years, including an appropriate grace period. Sub-borrowers would assume the foreign exchange risk on the currencies of the countries from which goods and services are procured. The Government would bear any residual exchange risk between the currency of procurement and the currency of obligation, for which Government would charge DBP a fee of 0.75 percent per year on amounts outstanding

on the Bank loan (see Schedule 3 of Loan Agreement). A ceiling of $5 million would be set for any sub-loan made by DBP for an individual investment project under the proposed loan (See Section 3.04 of the Loan Agreement). As under the first industrial loan to DBP, sub-loans of less than $1 million would be made without the Bank's prior approval. The aggregate limit of such sub-loans would be $30 million (see Section 2.02(b) of the Loan Agreement). Based on experience with the average size of industrial sub-loans under the first loan, it is estimated that with this free limit, about 70 percent by number or 85 percent of the amount of DBP's sub-loans would require the prior approval of the Bank staff. This would enable Bank staff to closely monitor the progress of the project.

34. DBP, established in 1958 as a wholly Government-owned development Bank, operates in all the important sectors of the economy. The bulk of DBP financing, including guarantees and equity investments, has gone to industry which accounts for about $2 billion or 70 percent of total commitments. The balance of about $800 million is accounted for by agriculture, real estate and other sectors, including lending to municipalities and private development banks. DBP's financing in the past two years accounted for about 13 percent of total fixed investment in the Philippines, and its industrial financing for 26 percent of total investment in the industrial sector. In addition to its financing, DBP has also helped to promote investment in low-cost housing and has assisted in the establishment of provincial private development banks and the Greater Manila Terminal Food Market. Because of the size of its financing and the wide variety of its activities, DBP has played and is expected to continue to play a central role in the economic development of the Philippines.

35. DBP's present management has continued its efforts to strengthen the institution and to raise the standards of its operations. While there has been some necessary movement of experienced staff, particularly from IPD I, to bolster weaker departments, the overall quality of DBP's management has generally improved. DBP has expanded its professional staff by 30 percent since December 1973, and reduced its services staff by 1.5 percent over the same period. IPD I had a total staff of 62 as of April 30, 1975. Since then it has employed 21 additional staff and expects to complete recruitment by the end of 1975 to fill the authorized positions still vacant. IPD I is recruiting mainly recent graduates, and DBP is developing suitable training programs both internally and with the Development Academy of the Philippines (DAP) to enable new staff to become fully operational as soon as possible. In the past year, DBP staff have also made training visits to other DFCs to study their operating systems and adapt them for DBP's use. During negotiations, improved procedures for loan appraisal and supervision were informally agreed upon and the impact of these on IPD I's operations will be closely monitored by the Bank.

36. DBP's lending operations have increased particularly rapidly in the last year and reached an unprecedented level of $324 million in FY75, compared to $39 million in FY74 and $31 million in FY73. In addition to a major and unusual increase in hotel lending operations, DBP's lending increased

in other sectors, especially industry. This increase offset a deliberate reduction in DBP's guarantee operations which declined from $373 million in FY74 to $123 million in FY75. Equity investments, mainly in government enterprises, were approved for amounts totalling $28 million in FY75, a much higher level than in the previous two years.

37. DBP's financial position is reasonably sound. As of June 30, 1975, DBP's total assets stood at $1.0 billion and its contingent liabilities (outstanding guarantees) totalled $467 million. Its liquidity position is secure (current ratio 1.3 as is its present long-term capital structure (long-term debt-equity ratio 3.8:1). In order to increase DBP's long-term domestic resources, Government is paying in an additional $100 million (₱ 750 million) in the next two years to increase DBP's equity. In addition, the Government will convert ₱ 400 million in short-term Treasury deposits in DBP into a loan with a five year maturity (see Section 4.11(c) of the Loan Agreement). The Government has also agreed to make by 1980 satisfactory arrangements to support DBP's large hotel financing program (see Section 4.11(a) of the Loan Agreement). To ensure the continued strength of DBP's capital structure, DBP has agreed for the first time to limit total borrowings and outstanding contingent liabilities to no more than 10 times its equity base (see Section 4.05 of the Loan Agreement). This limit is considered satisfactory. DBP has also agreed to set up a special foreign exchange loss reserve account, and to adopt a reserves policy statement satisfactory to the Bank (see Sections 3.01(b) and 4.07 of the Loan Agreement). DBP's net income for FY75 was $10 million, a decline on an annual basis of 21 percent. This is in contrast to the rising trend of FY73 and FY74. The decline in income reflected mainly a decline in collections, as a result of the effects of the economic downturn in FY75 on many of DBP's clients, and rapidly rising expenses. DBP has agreed to take the actions outlined in para. 38 in order to improve its financial performance (see Sections 4.08, 4.09 and 4.10 of the Loan Agreement).

38. DBP's arrears situation, which has improved substantially over the past year, continues to need substantial improvement. As of June 30, 1975, total arrears on the total loan portfolio including interest, amounted to nearly $75 million or 15.5 percent of the portfolio, compared to 23.5 percent a year ago; and the number of accounts in arrears amounted to 60 percent of the total, compared to 57 percent a year earlier. Defaults on guarantees have required DBP to advance an average of about $53 million annually over the past four years. These advances, which are immediately due and payable, amounted to $73 million equivalent as of March 31, 1975, or 15.6 percent of the outstanding guarantee portfolio. To reduce arrearages on its loan and guarantee accounts, DBP launched a major collection effort, beginning in January 1974, but this was retarded by the economic downturn in FY75. To alleviate the arrears problem, DBP has agreed to: reschedule all accounts in need of such action by March 31, 1976; further improve its system of recording and reporting arrears; establish prompt reminder procedures for overdue accounts and increase its penalty charges (see Sections 4.08, 4.09 and 4.10 of the Loan Agreement).

39. DBP's accounts are audited by Government auditors, whose reports, although thorough in many respects, do not cover certain essential aspects of DBP's financial condition, namely, the quality of the portfolio and the

adequacy of provisions made for doubtful accounts. Both DBP and the Government concur with the views of the Bank staff on the need for improving the coverage of the audit. Agreement was reached during negotiations on the form, coverage and timetable for submission of the improved audits. It was also agreed that in the event audit reports for FY76 and beyond were found to be unsatisfactory, the government would take all such steps, including the appointment of outside independent auditors, as necessary to enable the Bank to make firm judgements about DBP's financial condition (See Section 4.03 of the Loan Agreement).

40. DBP expects to commit loans and guarantees totalling $580 million during the two-year period from July 1, 1975. Projected commitment levels have risen considerably compared to forecasts of 18 months ago, mainly because capital goods prices have increased at a much more rapid rate than anticipated. The proposed loan of $75 million would cover just over 50 percent of DBP's total direct foreign exchange commitment requirements over the next two-year period. DBP would finance the balance through a proposed loan of $25 million from the Asian Development Bank (ADB), and also hopes to obtain additional commercial borrowings. DBP's local currency requirements are expected to be provided by the Government and to some extent through DBP's internal cash generation and resource mobilization efforts. With the institutional improvements described in this report, DBP can be expected to carry out the projected level of operations effectively and to continue to improve steadily its financial position and performance.

PART V - LEGAL INSTRUMENTS AND AUTHORITY

41. The draft Loan Agreement between the Republic of the Philippines and the Bank, the Report of the Committee provided for in Article III, Section 4 (iii) of the Articles of Agreement of the Bank and the text of a draft resolution approving the proposed loan are being distributed separately to the Executive Directors. The loan would not become effective until a Subsidiary Loan Agreement was concluded between the Government and DBP.

42. I am satisfied that the proposed loan would comply with the Articles of Agreement of the Bank.

PART VI - RECOMMENDATION

43. I recommend that the Executive Directors approve the proposed loan.

Robert S. McNamara
President

Attachments
December 3, 1975

COUNTRY DATA - PHILIPPINES

AREA	POPULATION	DENSITY
300,000 km2	39.04 million (mid-1972)	.. Per km2 of arable land

SOCIAL INDICATORS

	Philippines 1960	Philippines 1970	Reference Countries: Thailand 1970	Turkey 1970	Korea* 1970
GNP PER CAPITA US$ (ATLAS BASIS) /1	160 /a	220 /a	220 /b	370 /b	310 /b
DEMOGRAPHIC					
Crude birth rate (per thousand)	..	45 /c	43 /c	38 /c,d	28
Crude death rate (per thousand)	..	12 /c	10 /c	13 /c,d	8
Infant mortality rate (per thousand live births)	..	80	80-90	145 /e	..
Life expectancy at birth (years)	51 /f	58	59	55 /g	65
Gross reproduction rate /2	..	3.3	3.2	2.6 /d,g	2.5
Population growth rate /3	3.0	3.0 /h	3.1 /h	2.5 /h	2.2 /h
Population growth rate - urban	2 /i,j	4 /j	5 /k	4.5 /l	6 /m
Age structure (percent)					
0-14	46	43 /b	45	42	40 /b
15-64	51	54 /b	52	54	57 /b
65 and over	3	3 /b	3	4	3 /b
Age dependency ratio /4	1.7	0.9 /b	0.9	0.8	0.8 /b
Economic dependency ratio /4	1.7	1.5	1.1	1.1	1.4
Urban population as percent of total	30 /j	32 /j	25 /k	39 /b,l	41 /m
Family planning: No. of acceptors cumulative (thous.)	..	409	490	484 /p,q	..
No. of users (% of married women)	..	8	10	8.2 /e	..
EMPLOYMENT					
Total labor force (thousands)	9,100	12,300	16,500	14,500 /r	10,500 /b
Percentage employed in agriculture	61	51	81	67	48 /b
Percentage unemployed	7	7 /ab	..	4	5 /b
INCOME DISTRIBUTION					
Percent of national income received by highest 5%	29 /s,t	25 /o,t	17 /t,u	32 /e,t,v	15 /o,t
Percent of national income received by highest 20%	56 /s,t	54 /o,t	46 /t,u	60 /e,t,v	37 /o,t
Percent of national income received by lowest 20%	5 /s,t	4 /o,t	7 /t,u	3 /e,t,v	10 /o,t
Percent of national income received by lowest 40%	13 /s,t	12 /o,t	17 /t,u	10 /e,t,v	24 /o,t
DISTRIBUTION OF LAND OWNERSHIP					
% owned by top 10% of owners	..	..	..	53	28
% owned by smallest 10% of owners	..	..	..	0.9	2
HEALTH AND NUTRITION					
Population per physician	..	9,100 /w	7,970	2,220	2,210 /y
Population per nursing person	..	5,390 /w	6,650	1,880 /x	1,760 /y
Population per hospital bed	1,180 /aa	850 /ab,ac	850	490	1,920
Per capita calorie supply as % of requirements /5	83	85	105	110	103 /ab
Per capita protein supply, total (grams per day) /6	44	45	52	78	65 /ab
Of which, animal and pulse	19 /ad	22 /ab	17 /ac	22 /ae	19 /ab
Death rate 1-4 years /7	9 /aa	7 /ab	..	15 /af	..
EDUCATION					
Adjusted /8 primary school enrollment ratio	91	112 /ag,ah	80 /e	111 /ag	104
Adjusted /8 secondary school enrollment ratio	26	45 /ah	13 /e	28	41
Years of schooling provided, first and second level	10	10	12	13	12
Vocational enrollment as % of sec. school enrollment	14	10 /ah,ai	12 /ab,aj	14	15 /o
Adult literacy rate %	..	72 /r	70 /o,r	55	91 /ak,al
HOUSING					
Average No. of persons per room (urban)	..	..	..	1.9	2.7
Percent of occupied units without piped water	80 /am	66 /am	..	64 /am	80 /an
Access to electricity (as % of total population)	17 /ao	23 /ah	17	41	50
Percent of rural population connected to electricity	..	6 /ah	13	18	30
CONSUMPTION					
Radio receivers per 1000 population	22	46 /b	83 /b	107 /b	128 /o
Passenger cars per 1000 population	3	8 /b	7 /o	4	2 /b
Electric power consumption (kwh p.c.)	101	255 /b	169 /b	304 /b	392 /b
Newsprint consumption p.c. kg per year	1.3 /z	1.7 /b	1.5 /b	2.2 /b	3.7 /b

Notes: Figures refer either to the latest periods or to the latest years. Latest periods refer in principle to the years 1956-60 or 1966-70; the latest years in principle to 1960 and 1970.

/1 The Per Capita GNP estimate is at market prices for years other than 1960, calculated by the same conversion technique as the 1972 World Bank Atlas.

/2 Average number of daughters per woman of reproductive age.

/3 Population growth rates are for the decades ending in 1960 and 1970.

/4 Ratio of population under 15 and 65 and over to population of ages 15-64 for age dependency ratio and to labor force of ages 15-64 for economic dependency ratio.

/5 FAO reference standards represent physiological requirements for normal activity and health, taking account of environmental temperature, body weights, and distribution by age and sex of national populations.

/6 Protein standards (requirements) for all countries as established by USDA Economic Research Service provide for a minimum allowance of 60 grams of total protein per day, and 20 grams of animal and pulse protein, of which 10 grams should be animal protein. These standards are somewhat lower than those of 75 grams of total protein and 23 grams of animal protein as an average for the world, proposed by FAO in the Third World Food Survey.

/7 Some studies have suggested that crude death rates of children ages 1 through 4 may be used as a first approximation index of malnutrition.

/8 Percentage enrolled of corresponding population of school age as defined for each country.

/a Computed by applying to the 1970 figure the growth rate of GNP/capita in real terms from 1960 to 1970; /b 1972; /c 1965-70 UN estimate; /d Derived from sample survey estimates (240,000 persons) excluding 17 Eastern provinces; /e 1968; /f 1946-49; /g 1965-67; /h 1960-72; /i 1956-60; /j For definition of urban see UN Demographic Yearbook 1971, p. 156; /k Over 10,000 population; /l Administrative centers of provinces and districts ("Vilayet" and "Kaza" centers); /m Seoul city and municipalities of 5,000 or more inhabitants; /n Estimate; /o 1971; /p 1964-June 1974; /q 86 percent being IUDs; /r 15 years and over; /s 1961; /t Households; /u Urban only; /v Disposable income; /w Personnel in government services only; /x Including assistant nurses and midwives; /y Number on the register, not all working in the country; /z Imports only; /aa 1962; /ab 1969; /ac Including rural hospitals; /ad 1960-62; /ae 1964-66; /af 1966-67; /ag Including overage students; /ah 1967; /ai Public education only; /aj Data on vocational education refer to public schools and include technical education at post-secondary level; /ak 10 years and over; /al Definition not available; /am Water piped inside or outside; /an Water piped inside; /ao Percentage of dwellings.

* Korea has been selected on the basis of its similar population, location and income level and like the Philippines, it is expected to grow rapidly in the coming years.

ECONOMIC INDICATORS 1/

GROSS NATIONAL PRODUCT IN 1974

	US$ Mln.	%
GNP at Market Prices	14,550	100.0
Gross Domestic Investment	3,630	24.9
Gross National Saving	3,420	23.5
Current Account Balance	-210	-1.5
Exports of Goods, NFS	3,357	23.1
Imports of Goods, NFS	3,782	27.2

ANNUAL RATE OF GROWTH (%, constant prices)

	1960-65	1965-70	1971	1972	1973	1974
GNP at Market Prices	5.5	5.7	6.5	4.3	10.0	5.8
Gross Domestic Investment	12.6	1.6	5.9	-3.5	9.4	23.4
Gross National Saving	15.0	3.6	13.2	-8.2	49.1	-11.6
Current Account Balance	.	.	.	.	.	.
Exports of Goods, NFS	11.0	4.5	5.0	1.5	18.7	-24.1
Imports of Goods, NFS	7.3	7.2	5.4	2.7	13.1	20.4

OUTPUT, LABOR FORCE AND PRODUCTIVITY IN 1974 1/

	Value Added		Labor Force 2/		V. A. Per Worker	
	US$ Mln.	%	Mln.	%	US $	%
Agriculture	4,187	36.0	7.6	53.9	551	67.0
Industry	3,850	33.1	2.4	17.0	1,604	194.9
Services	3,581	30.8	3.8	27.0	942	114.5
Unallocated	.	.	0.3	2.1	.	.
Total/Average	11,618	100.0	14.1	100.0	823	100.0

GOVERNMENT FINANCE

	General Government			Central Government		
	(Mln.)	% of GDP		(Pesos Mln.)	% of GDP	
	197	197	196 -7	FY74	FY74	FY71-73
Current Receipts	..	..	..	10,370	12.2	9.0
Current Expenditure	..	..	..	7,915	9.3	8.0
Current Surplus	..	..	..	2,455	2.9	1.0
Capital Expenditures	..	..	..	2,646	3.1	1.4
External Assistance (net)	..	..	..	186	0.2	0.4

MONEY, CREDIT and PRICES

	1965	1969	1970	1971	1972	1973	1974
		(Million pesos outstanding end period)					
Money and Quasi Money	5,136	8,959	10,140	11,720	13,243	16,837	19,766
Bank credit to Public Sector 3/	980	3,565	3,479	3,907	4,817	6,820	7,627
Bank Credit to Private Sector	8,223	13,139	15,396	18,010	21,531	26,906	34,326
		(Percentages or Index Numbers)					
Money and Quasi Money as % of GDP	21.1	27.0	25.0	23.2	23.5	23.5	19.9
General Price Index (1963 = 100)	100.0	111.4	137.7	159.3	175.3	218.4	337.5
Annual percentage changes in:							
General Price Index	2.2	1.3	23.6	15.7	10.0	24.6	54.5
Bank credit to Public Sector	..	27.9	-2.4	12.3	22.3	41.6	11.8
Bank credit to Private Sector	..	9.0	17.2	17.0	27.0	25.0	27.6

NOTE: All conversions to dollars in this table are at the average exchange rate prevailing during the period covered.

1/ All current factor cost.

2/ Total labor force; unemployed are allocated to sector of their normal occupation. "Unallocated" consists mainly of unemployed workers seeking their first job.

3/ Covers credits from all important fiancial institutions.

.. not available

. not applicable

TRADE PAYMENTS AND CAPITAL FLOWS

BALANCE OF PAYMENTS

	1971	1972	1973	1974
		(Million US$)		
Exports of Goods, NFS		1,432	2,443	3,357
Imports of Goods, NFS		1,484	2,008	3,782
Resource Gap (deficit = -)		-52	+435	-425
Interest Payments (net)		-92	-53	-55
Workers' Remittances				
Other Factor Payments (net)		-33	-60	
Net Transfers		188	234	271
Balance on Current Account		+11	556	-210
Direct Foreign Investment		-22	77	59
Net MLT Borrowing				
Disbursements		390	377	402
Amortization		250	335	339
Subtotal		140	42	63
Capital Grants				
Other Capital (net) 1/		15	-43	373
Other items n.e.i 2/		-106	-38	4
Increase in Reserves (+) 3/		+38	+594	289
Gross Reserves (end year) 4/		735	1,416	1,978
Net Reserves (end year) 4/		80	753	934
Inter.Reserves (end year) 5/		282	676	1.165
Fuel and Related Materials				
Imports of Goods, NFS		1,514	2,008	3,782
of which: Petroleum		147	184	653

MERCHANDISE EXPORTS (AVERAGE 1972-74)

	US $ Mln	%
Coconut Products	403	21.2
Sugar Products	426	22.4
Forest Products	337	17.7
Mineral Products	393	20.7
Fruits and other agricultural Products	117	6.2
Other manufactures	224	11.8
Total	1,900	100.0

EXTERNAL DEBT, DECEMBER 31, 1974 6/

	US $ Mln
Public Debt, incl. guaranteed	1,113
Non-Guaranteed Private Debt	985
Total outstanding & Disbursed	2,098

DEBT SERVICE RATIO for 1974 7/

	%
Public Debt, incl. guaranteed	6.6
Non-Guaranteed Private Debt	8.9
Total outstanding & Disbursed	15.5

IBRD/IDA LENDING, October 31,1975 (Million US $):

	IBRD	IDA
Outstanding & Disbursed	247.5	6.5
Undisbursed	380.1	15.7
Outstanding incl. Undisbursed	627.6	22.2

RATE OF EXCHANGE

	1965-69	1970-71
US$ 1.00 = Ps.	3.92	6.43
Ps. 1.00 = US$	0.26	0.16

April 1972-July 1975		Since July 1975	
US$ 1.00 = Ps.	6.78	US$ 1.00 =	Ps. 7.5
Ps. 1.00 - US$	0.15	Ps. 1.00 =	US$ 0.133

1/ Includes SDRs, short-term private loans, Central Bank liabilities and use of IMF credit.
2/ Errors and omissions
3/ Includes net commercial bank holdings plus foreign exchange holdings of Central Bank and monetary gold. This entry is equivalent to the change in international reserves.
4/ Includes Central Bank and commercial bank reserves.
5/ Gross reserves of Central Bank plus net reserves of commercial banks.
6/ Excludes short-term debt and IMF standby credit and is on a disbursement basis.
7/ Ratio of Debt-Service to Exports of Goods and Non-factor Services.

PHILIPPINES

A. Statement of Bank Loans and IDA Credits to the Philippines as of October 31, 1975

Loan or Credit Number	Year	Borrower	Purpose		(US$ millions) Amount less Cancellations Bank	IDA	Undisbursed
13 loans and credits fully disbursed					197.0		
637-PH	1969	Republic of the Philippines	Irrigation		34.0		1.0
720-PH	1971	"	Rice Processing and storage		14.3		11.4
731-PH	1971	"	First Highway		8.0		1.7
809-PH	1972	National Power Corporation	Power		22.0		17.5
823-PH	1972	Republic of the Philippines	Livestock		7.5		2.8
349-PH	1973	"	Education II			12.7	9.0
891-PH	1973	"	Fisheries		11.6		8.6
939-PH	1973	"	Ports		6.1		5.8
950-PH	1973	"	Highway II		68.0		45.4
472-PH	1974	"	Aurora-Penaranda Irrigation			9.5	6.7
984-PH	1974	"	"		9.5		9.4
998-PH	1974	"	DFC - DBP I		50.0		29.1
1010-PH	1974	"	Third Rural Credit		22.0		7.3
1034-PH	1974	National Power Corporation	Power		61.0		54.1
1035-PH	1974	Republic of the Philippines	Population		25.0		24.9
1048-PH	1974	"	Shipping		20.0		20.0
1052-PH	1974	Philippine National Bank	DFC		30.0		28.5
1080-PH	1975	Republic of the Philippines	Tarlac Irrigation		17.0		16.9
1102-PH	1975	"	Rural Development		25.0		24.9
1120-PH	1975	"	Small and Medium Industries		30.0		28.8
1154-PH	1976	"	Magat Irrigation		42.0		42.0
					700.0	22.2	395.8
Of which has been repaid (Bank and 3rd Parties)					72.4	-	
Total now outstanding					627.6	22.2	
Amount sold				13.3			
of which has been repaid (3rd Parties)				12.1	1.2	-	
Total now held by Bank and IDA (prior to exchange rate adjustments)					626.4	22.2	
Total undisbursed					380.1	15.7	395.8

B. Statement of IFC Investments in the Philippines as of October 31, 1975

Fiscal Year	Company	(Amount US$ million) Loan	Equity	Total
1963 & 1973	Private Development Corporation of the Philippines	15.0	4.4	19.4
1967	Manila Electric Company	8.0	-	8.0
1967	Meralco Securities Corporation	-	4.0	4.0
1970	Philippine Long Distance Telephone Company	4.5	-	4.5
1970 & 1972	Mariwasa Manufacturing Inc.	0.8	0.4	1.2
1970	Paper Industries Corporation of the Philippines	-	2.2	2.2
1971	Philippine Petroleum Corporation	6.2	1.8	8.0
1972	Marinduque Mining and Industrial Corporation	15.0	-	15.0
1973	Victorias Chemical Corporation	1.9	0.3	2.2
1974	Filipinas Synthetic Fiber Corporation	1.5	-	1.5
1974	Maria Christina Chemicals	1.5	.5	2.0
1974	Republic Flour Mills Corporation	1.2	-	1.2
1975	Philippine Polyamide Industrial Corporation	7.0	-	7.0
	Total	62.6	13.6	76.2
	Less sold, acquired by others, repaid or cancelled	14.9	7.1	22.0
	Now held	47.7	6.5	54.2
	Undisbursed	2.1	-	2.1

C. Projects in Execution [1/]

Ln. No. 637-PH — Upper Pampanga River Irrigation; US$34.0 million Loan of August 18, 1969; Date of Effectiveness: October 15, 1969; Closing Date: June 30, 1976

This is the first major irrigation project in the Philippines and will supply water year-round to nearly all its 84,000 ha command area. The project's on-farm development scheme is setting a pattern for future irrigation development in the country. Despite some delays caused by the 1972 floods, the dam was commissioned on September 7, 1974 ahead of schedule. All work is expected to be completed in 1975 and the loan entirely disbursed by June 30, 1976, the Closing Date. Project costs have increased 40% over appraisal estimates, largely as a result of rapid inflation, the effects of successive devaluations of the peso, and design changes in the dam (which accounted for nearly half the increase in costs). The increase in costs is being financed by the Government. However, as a result of the close coordination established between irrigation and agricultural supporting services, the project is expected to reach full development in 7 years after completion of construction, instead of 13 years which was the appraisal estimate. Also, nearly 7,000 ha have been added to the project, mostly by including lands which were formerly under a private irrigation system. Finally, there has been a considerable increase in the projected world market price of rice. As a result, the rate of return estimate is now more favorable than at appraisal.

Ln. No. 720-PH — Rice Processing and Storage; US$14.3 million Loan of February 4, 1971; Date of Effectiveness: May 10, 1971; Closing Date: June 30, 1977

This project provides long-term credit through the Development Bank of the Philippines to finance a program for the development and modernization of the rice and corn processing industry. Originally the project was restricted to rice and to the private sector, and the emphasis was on the construction of new integrated rice mills with large capacities. Due in part to poor harvests and in part to large cost increases for rice mills, the demand for sub-loans for new integrated rice mills turned out to be small, and, as expalined in the President's Memorandum dated June 8, 1972 (R72-40), the loan agreement was amended to shift the project emphasis to rehabilitation of existing rice milling facilities. In spite of this the project made little progress. The loan agreement was amended again in

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1/ These notes are designed to inform the Executive Directors regarding the progress of projects in execution, and in particular to report any problems which are being encountered, and the action being taken to remedy them. They should be read in this sense, and with the understanding that they do not purport to present a balanced evaluation of strengths and weaknesses in project execution.

April, 1974 basically (i) to expand the scope of the project to include corn in addition to rice, (ii) to enable local governments and the National Grains Authority to borrow funds under the project, and (iii) to streamline procurement procedures (President's memorandum SecM74-244 of April 15, 1974). As a result of these amendments, the project is now progressing satisfactorily and the loan is expected to be fully disbursed long before the revised Closing Date, June 30, 1977.

Ln. No. 731-PH — Highway; US$8.0 million Loan of April 14, 1971; Date of Effectiveness: July 23, 1971; Closing Date: June 30, 1976

The project is financing the construction and improvement of the Cotabato - Digos road in Mindanao (160 km.). Construction is only 55% complete based on the original scope of works, the delay being mainly due to civil disturbances and army activity on part of the road representing about 20% of the total roadworks. As there is little chance of the contractor being able to enter this area, the Bank has agreed to a Government proposal to delete this stretch of the road from the contract and eventually execute the work by force account; the undisbursed amount of the loan fund will be applied to the balance of works which can be completed by contract. The total cost of the reduced project is estimated to be about US$16.4 million compared to appraisal estimate of US$15.8 million. The increase in cost is due to a rise in construction costs which has been substantial since oil price increases in late 1973. The roadworks are expected to be completed by the end of December 1975. The other components of the project including UNDP financed feasibility studies were completed in 1973. The closing date has been extended from May 15, 1975 to June 30, 1976. Technical assistance to the Department of Public Highways is continuing with Bank financing under the Second Highway Project.

Ln. No. 809-PH and Cr. No. 296-PH — Fifth Power; US$22.0 million and US$10.0 million Loan and Credit of April 3, 1972; Date of Effectiveness: July 1, 1972; Closing Date: June 30, 1978

The project is helping the National Power Corporation (NPC) to finance the construction of a second thermal unit of 150-MW at Bataan and transmission facilities in Luzon. After initial delays, the project is proceeding satisfactorily, and the unit is expected to be commissioned during the second quarter of 1976. Construction work is continuing on 230 kV transmission lines. NPC's financial situation has been improved by the imposition in July 1973 of a surcharge to cover increased fuel costs. Further tariff increases were approved, effective July 1, 1974 and again in July 1, 1975, although this last increase still has not received Presidential approval.

Ln. No. 823-PH — Livestock; US$7.5 million Loan of May 25, 1972; Date of Effectiveness: November 9, 1972; Closing Date: December 31, 1978

The project is assisting Government in carrying out its livestock development program through credit supervised by the Development Bank of the

Philippines. The start of DBP lending operations was delayed by about six months because of late appointment of technical staff. Although sub-loan commitments were slow as a result of this, they are now improving, and all funds are expected to be fully committed by December, 1975. The project has expanded the agricultural credit capability of DBP into a new and important field thus meeting a previously unsatisfied demand for small to medium scale livestock development finance.

Cr. No. 471-PH — Aurora-Penaranda Irrigation; US$9.5 million Credit of May 14, 1974; Date of Effectiveness: August 22, 1974; Closing Date: June 30, 1979

Ln. No. 984-PH — Aurora-Penaranda Irrigation; US$9.5 million Loan of May 14, 1974; Date of Effectiveness: August 22, 1974; Closing Date: June 30, 1979

This is the second irrigation development and rehabilitation project in the Philippines to be financed by the Bank. The project will divert water from the Aurora basin into the Pantabangan Reservoir of the first project, to provide year-round irrigation for 25,300 ha of rice land in Central Luzon. The project also includes an Irrigation Development Study for Central Luzon to inventory water, land, and other resources and identify priority irrigation projects. Although there has been some delay in constructing the two diversion dams because of the need for more extensive foundations and abutment area grouting than originally expected, most difficulties have been overcome and the work is progressing satisfactorily. Diversion of 75% of Aurora water into Pantabangan Reservoir was achieved in September, 1975, one year ahead of the appraisal schedule. In the service area, lack of competition and high bids have delayed awarding of contracts. Urgent work is being done by Government force account, although the Credit Agreement sets a force account limit of about 20% on civil works in the service area. Project costs have increased about 54% over appraisal estimates, largely as a result of rapid inflation. There would be added benefits from early diversion, however, resulting in additional water for irrigation sooner than planned, and the rate of return is expected to fall from 17% at appraisal to 14%.

Ln. No. 998-PH — Industrial Investment and Smallholder Tree-farmers: US$50.0 million Loan of June 12, 1974; Date of Effectiveness: September 9, 1974; Closing Date: December 31, 1981

The proceeds of the loan are being relent to the Development Bank of the Philippines (DBP). The industrial portion of the loan (US$48 million) is being used by DBP to make sub-loans to finance direct imports for medium and relatively large industrial projects. DBP is using the balance (US$2 million) to finance about 1,300 smallholders in a pilot tree-farming project. The loan became effective on September 9, 1974. As of September 30, 1975 commitments for sub-loans totalling $35 million had been made.

Ln. No. 1010-PH — Third Rural Credit; US$22.0 million Loan of June 17, 1974; Date of Effectiveness: August 27, 1974; Closing Date: December 31, 1977

The Central Bank relends the proceeds of the Loan (except for a small amount for an evaluation study) to participating banks. These on-lend the funds to farmers and rural entrepreneurs to finance investment in farm mechanisation, on-farm transportation, farm support facilities and equipment, coastal and inland fisheries, small-scale livestock development and cottage-scale agro-industry. The project also provides for a review by local experts of the first, second and third rural credit projects. The loan became effective on August 27, 1974. Collection of arrears by a sizeable number of participating banks from beneficiaries under the first and second projects is not satisfactory. This is being watched closely by Bank staff and appropriate steps are being taken to improve such collections.

Ln. No. 1034-PH — Sixth Power; US$61.0 million Loan of July 31, 1974; Date of Effectiveness: November 15, 1974; Closing Date: December 31, 1978

The project is helping the National Power Corporation (NPC) to finance a 100 MW hydro plant at Pantabangan and transmission lines for the further expansion of the Luzon grid and feasibility studies by consultants for a future power project. Major equipment for the plant has been contracted and project commissioning is expected by the end of 1976. The transmission system expansion is also proceeding satisfactorily. NPC raised its tariffs on July 1, 1974 to meet the covenanted rate of return of 8 percent. But due to inflation NPC was not able to achieve this. NPC therefore increased tariffs on July 1, 1975, but this increase still has not received Presidential approval.

Cr. No. 349-PH — Second Education; US$12.7 million Credit of January 5, 1973; Date of Effectiveness: April 11, 1973; Closing Date: December 31, 1978

The project is assisting Government to improve such areas as education planning, management and curriculum development, science teacher training, and training of technicians, skilled craftsmen and farmers. The project is currently a few months behind schedule, but the delay is being reduced through action by the project unit on civil works, designs and equipment procurement. The project is expected to be completed on schedule. Current problems include unexpected cost overruns (42% higher than the original estimate), difficulty in introducing reforms in admissions, and quality standards of project agricultural colleges. The government has agreed to finance overruns and is considering steps to solve the other problems. Disbursements are well underway and are expected to remain ahead of, or on, schedule until project completion.

Ln. No. 891-PH — Fisheries; US$11.6 million Loan of May 21, 1973; Date of Effectiveness: December 5, 1973; Closing Date: June 30, 1979

This project is designed to provide long term credit to the private sector through the Development Bank of the Philippines for marine and inland fisheries development. The loan became effective on December 5, 1973. The demand for loans is adequate, and the organization to implement them has been properly established. The project is progressing satisfactorily, and all funds are expected to be fully committed by June, 1976.

Ln. No. 939-PH — Second Ports; US$6.1 million Loan of October 24, 1973 Date of Effectiveness: December 19, 1973; : Closing Date: December 31, 1977

This project provides for the rehabilitation and expansion of the ports of General Santos and Cagayan de Oro in the island of Mindanao. The Contract for General Santos was awarded in May 1975 and work has started. For Cagayan de Oro, a bid has been selected and award of contract is awaiting Government approval.

Ln. No. 950-PH — Second Highway; US$68.0 million Loan of December 12, 1973; Date of Effectiveness: December 27, 1973; Closing Date: December 31, 1977

The project is helping the Government to implement its program of construction, improvement and rehabilitation of highways and feeder roads, by financing the construction, improvement and rehabilitation of 1400 kms. of roads in Luzon. Work has begun on all fourteen contracts, ten of which were awarded to local contractors. In line with world-wide inflation, costs have increased sharply, but price adjustments are being awarded to contractors by the Government to offset the sharp rises in costs of basic materials, fuels and labor. The UNDP financed Road Feasibility Studies (Phase II), for which the Bank is executing Agency, have been completed and a possible Third Highway project has already been indentified and pre-appraised. Execution of other minor project items is proceeding generally on schedule.

Ln. No. 1035-PH — Population; US$25.0 million Loan of July 31, 1974; Date of Effectiveness: November 13, 1974; Closing Date: December 31, 1979

The project is assisting the Government in expanding rural health infrastructure, staff training facilities, and research and communications capacity. This will help the Philippines achieve their long-term goal of fertility reduction. It is progressing satisfactorily.

Ln. No. 1048-PH — Inter-Island Shipping; US$20 million Loan of October 29, 1974; Date of Effectiveness: January 15, 1975; Closing Date: June 30, 1979

The Government is relending the proceeds of the loan to the Development Bank of the Philippines for onlending to beneficiaries for the

acquisition of new and used ships and for major repairs and conversions. The loan became effective on January 15, 1975. It is progressing satisfactorily.

Ln. No. 1052-PH — Private Development Corporation of the Philippines; US$30 million Loan of November 12, 1974; Date of Effectiveness: February 7, 1975; Closing Date: June 30, 1979

The project assists in the financing of industrial sub-projects in the Philippines, the bulk of which are expected to go to export-oriented manufacturing projects. The loan became effective on February 7, 1975. It is progressing satisfactorily.

Ln. No. 1080-PH — Tarlac Irrigation; US$17.0 million Loan of January 27, 1975; Date of Effectiveness: April 27, 1975; Closing Date: December 31, 1980

The project will assist the Government to improve and expand 34,000 hectares of land in Central Luzon for wet season irrigation for rice growing. It will also provide for a groundwater pilot scheme, a water management training program and a national irrigation systems improvement study. The loan became effective on April 27, 1975. It is proceeding satisfactorily.

Ln. No. 1102-PH — Rural Development; US$25.0 million Loan of April 16, 1975; Date of Effectiveness: July 28, 1975; Closing Date: June 30, 1981

The project will assist the Government to carry out a rural development project on the island of Mindoro, which will include infrastructure and irrigation improvements, and ecological and health improvement measures. The Loan became effective on July 28, 1975. It is progressing satisfactorily.

Ln. No. 1120-PH — Small and Medium Industries Development; US$30.0 million Loan of June 5, 1975; Date of Effectiveness: August 20, 1975; Closing Date: August 31, 1979

The Government is relending $15 million of the loan proceeds to the Development Bank of the Philippines (DBP) and $12 million to the Industrial Guarantee Loan Fund (IGLF) to finance a wide range of small and medium industries sub-projects; $2.3 million to the National Electrification Administration (NEA) to finance the establishment of 24 industrial producer cooperatives; $0.7 million to the Department of Industry (DOI) to establish 7 Regional Technical Assistance Centers to provide technical assistance to small industries. The loan became effective on August 20, 1975. It is progressing satisfactorily.

Ln. No. 1154-PH Magat Multipurpose Project; US$42.0 million Loan of August 7, 1975; Date of Effectiveness: November 4, 1975; Closing Date: June 30, 1982

The project will assist the Government to improve and expand 35,000 ha. of land in the Cagayan Valley, Northern Luzon, for wet and dry season irrigation for rice growing. It will provide for the construction or upgrading of about 830 kms of project roads, construction of an airstrip, access roads and a bridge across the Magat River near the Magat River Irrigation System diversion dam. The project will also provide for detailed engineering studies and economic evaluation of the proposed Magat Dam and reservoir, a water management training program and technical assistance to the National Irrigation Administration, the implementing agency, in systems operation and construction management. Consultants have been selected and have begun work on the engineering and economic evaluation studies. The Loan became effective on November 4, 1975.

ANNEX III

PHILIPPINES

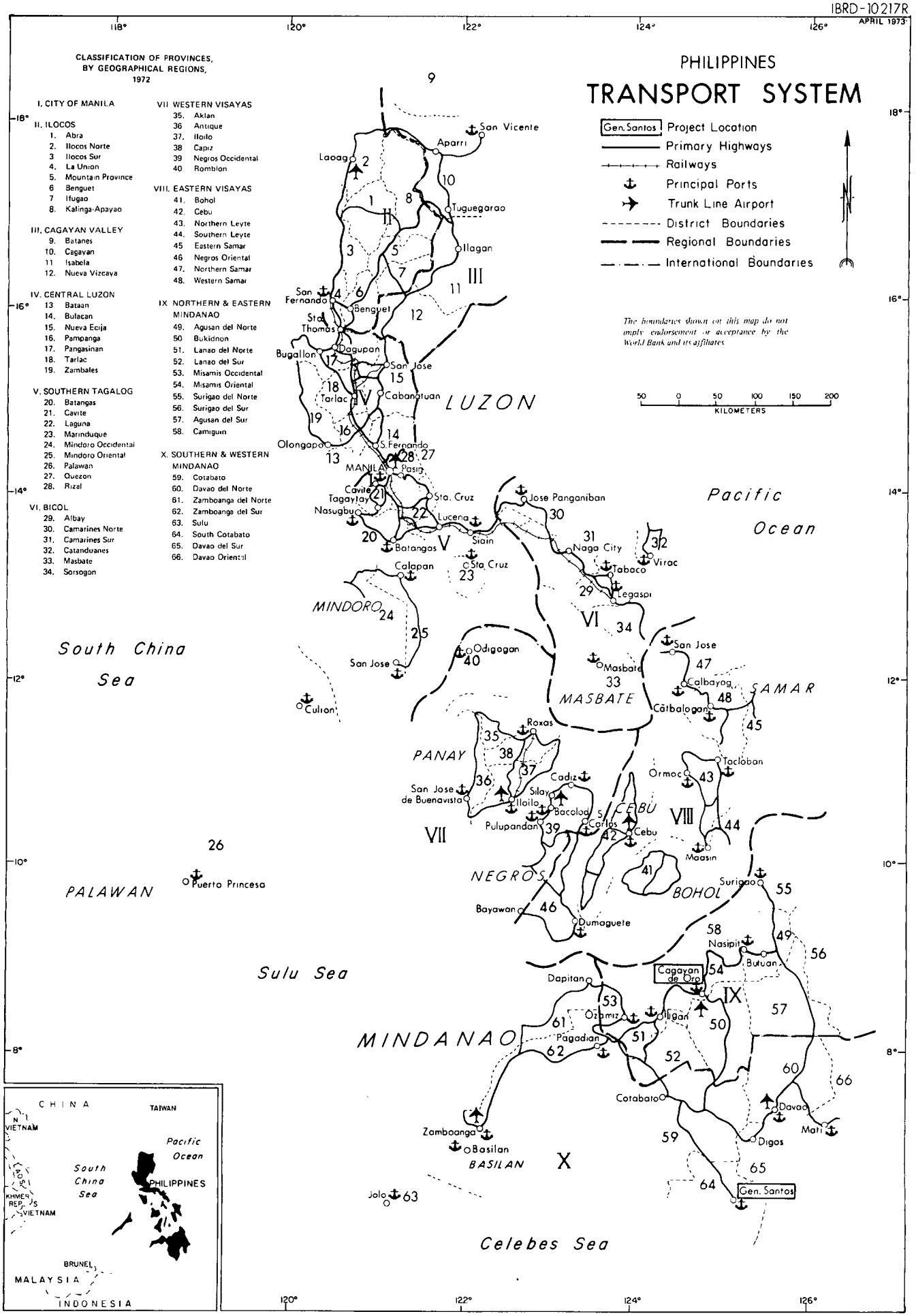
SECOND INDUSTRIAL INVESTMENT CREDIT PROJECT

LOAN AND PROJECT SUMMARY

Borrower:	The Republic of the Philippines
Beneficiary:	Development Bank of the Philippines (DBP)
Amount:	US$75 Million equivalent
Terms:	The loan would be for a term of 18 years including a grace period of 4 years and at an interest rate of 8.5 percent per annum.
Relending Terms:	The Government would relend the proceeds of the loan to DBP on the same terms as those for the Bank loan. DBP would onlend to ultimate borrowers at an interest rate of 12% per annum on loans secured by land, and at 14% per annum on loans not so secured, for a maximum period of 15 years including an appropriate grace period.
Project Description:	The loan would be used by DBP to make sub-loans for financing capital goods imports requirements for manufacturing, agro-industries, mining, ocean shipping and tourism.
Estimated Disbursements:	The loan would be committed over 2 years and disbursed over 4 years.
Appraisal Report:	Appraisal Report No. 872a-PH dated November 5, 1975.

IBRD-10217R
APRIL 1973

PHILIPPINES
TRANSPORT SYSTEM



CLASSIFICATION OF PROVINCES, BY GEOGRAPHICAL REGIONS, 1972

I. CITY OF MANILA

II. ILOCOS
1. Abra
2. Ilocos Norte
3. Ilocos Sur
4. La Union
5. Mountain Province
6. Benguet
7. Ifugao
8. Kalinga-Apayao

III. CAGAYAN VALLEY
9. Batanes
10. Cagayan
11. Isabela
12. Nueva Vizcaya

IV. CENTRAL LUZON
13. Bataan
14. Bulacan
15. Nueva Ecija
16. Pampanga
17. Pangasinan
18. Tarlac
19. Zambales

V. SOUTHERN TAGALOG
20. Batangas
21. Cavite
22. Laguna
23. Marinduque
24. Mindoro Occidental
25. Mindoro Oriental
26. Palawan
27. Quezon
28. Rizal

VI. BICOL
29. Albay
30. Camarines Norte
31. Camarines Sur
32. Catanduanes
33. Masbate
34. Sorsogon

VII WESTERN VISAYAS
35. Aklan
36. Antique
37. Iloilo
38. Capiz
39. Negros Occidental
40. Romblon

VIII. EASTERN VISAYAS
41. Bohol
42. Cebu
43. Northern Leyte
44. Southern Leyte
45. Eastern Samar
46. Negros Oriental
47. Northern Samar
48. Western Samar

IX NORTHERN & EASTERN MINDANAO
49. Agusan del Norte
50. Bukidnon
51. Lanao del Norte
52. Lanao del Sur
53. Misamis Occidental
54. Misamis Oriental
55. Surigao del Norte
56. Surigao del Sur
57. Agusan del Sur
58. Camiguin

X. SOUTHERN & WESTERN MINDANAO
59. Cotabato
60. Davao del Norte
61. Zamboanga del Norte
62. Zamboanga del Sur
63. Sulu
64. South Cotabato
65. Davao del Sur
66. Davao Oriental