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# DCA LOAN GUARANTEE PHILIPPINES IMPACT BRIEF



## BACKGROUND

Access to basic services dramatically affects the living conditions, health, and economic wellbeing of the

Philippine people. However, infrastructure in the Philippines to support basic services is lacking, leaving many of the country's poor without access. Funds required for infrastructure improvements and expansion far outstrip current financing sources including external donor resources. Promotion of private financing of local public infrastructure is one approach USAID/Philippines

has taken to span the breach between those that have access to essential services and those that do not. In the Philippines much of the responsibility for local infrastructure rests with local government units (LGUs). Although local governments have the authority to borrow private capital, they have almost exclusively borrowed from government financial institutions (GFIs). Private financial institutions have been reluctant to lend to LGUs due to a lack of information, skepticism about the creditworthiness of local governments, and a tradition of conservative lending practices.

The Local Government Unit Guarantee Corporation (LGUGC) was formed in 1998 to provide credit enhancement to attract private financing for local public infrastructure projects. LGUGC was initially owned by the Bankers Association of the Philippines (a trade organization of commercial banks), and Development Bank of the Philippines (a GFI), with Asian Development Bank added as an equity owner in 2005. Soon after its formation, in 1999, USAID

entered into a DCA Guarantee Agreement with LGUGC to re-guarantee 30 percent of the principal and interest LGUGC is obligated to pay in the event of default of a loan qualifying for coverage under the agreement up to an identified ceiling. The DCA guarantee was initially focused on the municipal bond market and infrastructure projects of LGUs, but over time evolved to focus on water infrastructure projects and included independent water districts, in addition to local governments, as eligible borrowers.

## EVALUATION OBJECTIVES

USAID's Economic Growth, Agriculture and Trade Bureau's Office of Development Credit (EGAT/DC) commissioned SEGURA/IP3 Partners LLC to conduct this evaluation of the DCA agreement with LGUGC in the Philippines. The evaluation was guided by an Evaluation Framework – developed by SEGURA/IP3 in conjunction with USAID and adapted to the Philippines context – designed to assess results at three levels: output, outcome, and impact. It also examined the effect of exogenous influences. The evaluation assesses the performance of the DCA guarantee with respect to the mobilization of private commercial lending to (initially) LGUs and (later) water districts.

## EVALUATION METHODOLOGY

A two-person team conducted the evaluation using a combination of quantitative and qualitative methods. Field work took place in Manila and outlying areas during July 8-17, 2009. Primary sources of information were interviews with key informants representing a variety of DCA stakeholders; documents pertaining to the DCA guarantee; and secondary information from the USAID Credit Management System, LGUGC, government and private financial institutions, target sector borrowers, and additional research.

### ABOUT DCA

USAID's Development Credit Authority (DCA) was created in 1999 to mobilize local private capital through the establishment of real risk sharing relationships with private financial institutions in USAID countries. The tool is available to all USAID overseas missions and can be used as a vehicle for providing much needed credit to an array of enterprises and underserved sectors. The evaluation in the Philippines is part of a set of evaluations EGAT/DC is undertaking in different countries, to test a series of developmental hypotheses related to the DCA guarantees.

### PHILIPPINES DCA LOAN GUARANTEE

Starting Date	Ending Date	Number of Loans	Aggregate Amount of Loans	Utilization Rate	Average Loan Size
1999	2014	11	US\$28,521,273	86.3%	US\$2,592,843



## KEY FINDINGS AND CONCLUSIONS

### OUTPUT

**Conclusions** The purpose of the DCA guarantee as finally amended – to strengthen LGUGC’s ability to mobilize private capital for creditworthy water infrastructure projects of local governments and water districts – complemented LGUGC’s strategy to facilitate private financing through loan guarantees for local infrastructure projects. The formal commitment of USAID in the form of the DCA guarantee assured rigorous oversight and was critical in establishing the credibility of LGUGC among private financial institutions and other stakeholders. The DCA guarantee was used by LGUGC to improve access to private sources of credit for local governments and water districts where little or none had previously existed, although the volume of lending was less than anticipated due to adverse external influences. There is evidence the DCA guarantee may have played a part in increasing tenors of LGUGC guaranteed loans to water districts (both with and without DCA coverage).

**Findings** in support of these conclusions include:

- LGUGC made 11 DCA guaranteed loans to LGUs and water districts totaling approximately US\$28.5 million, including six LGU bond issues and five water district loans.
- Interviews confirm that the DCA guarantee significantly enhanced the confidence of private financial institutions in LGUGC, thereby encouraging lending to the target sectors.
- There were no significant differences in interest rates or the collateral required between DCA guaranteed loans and other LGUGC guaranteed loans. However, the pattern and trend of tenors of all LGUGC guaranteed loans to water districts suggest experience of private financial institutions with lending under the DCA and LGUGC guarantees played a part in the improvement of the tenors of such loans to the 10 year DCA permitted maximum.

### OUTCOME

**Conclusions** A number of factors contributed to LGUGC’s achievement of desired DCA outcomes (i.e., encouragement of private capital flows to the target sectors, increased local credit market confidence in LGUGC, and expansion of the scope of its operations). Most important among the factors were the revised strategy of USAID and LGUGC to include water districts under the DCA guarantee, as well as USAID direct technical assistance and DCA monitoring support, which served to strengthen the LGUGC. LGUGC was incorporated into collaboration between USAID and the Government of Japan to facilitate private investment in water and sanitation. The DCA guarantee led LGUGC to guarantee loans to the target sectors without the DCA re-guarantee. Since private financing effectively played no role in the target sectors before the LGUGC, its loan guarantees made outside the DCA guarantee increased access to credit for target sector borrowers. LGUGC has also begun to cautiously expand its guarantee activities outside of the target sectors, and has broadened its services by becoming program manager of three other guarantee funds for other organizations.

**Findings** in support of these conclusions include

- Interviews with private financial institutions repeatedly affirmed the importance of LGUGC and its perceived backing by USAID as critical to their decision to enter the new areas of LGU and water district financing.
- Interviews with LGUGC management and staff indicated that experience with the DCA guarantee of bonds/loans to LGUs prepared it for implementation of the decision to expand

### EVALUATION QUESTIONS

**Output**—Did LGUGC’s use of the DCA guarantee conform to guarantee objectives as described in the Guarantee Agreement (i.e., “to strengthen the LGUGC’s ability mobilize private capital lending for local government infrastructure services and facilities and for water districts in the Philippines”)?

**Outcome**— Did the DCA guarantee influence behavioral changes at the LGUGC-level, and did LGUGC’s experience with the DCA guarantee improve access to credit for entities in the target sectors outside of the DCA guarantee coverage?

**Impact**— Did the guarantee have a demonstration effect that improved access to credit for entities in the target sectors by increased lending from the private banking sector without use of the guarantee?

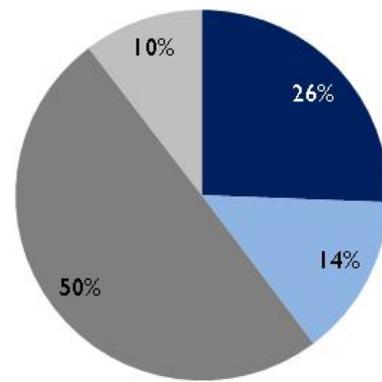
- the DCA guarantee to the water district market.
- LGUGC has guaranteed 11 loans to the target sector (eight bond issues/loans to LGUs and three loans to water districts) without the protection of the DCA guarantee, totaling over US\$42.1 million and representing 60 percent of its entire target sector loan guarantee portfolio.
  - LGUGC has extended its guarantees beyond the target sectors by guaranteeing one loan to a renewable energy company for a mini-hydroelectric plant, and two loans to bulk water suppliers of water districts. LGUGC currently serves as program manager for three energy sector guarantee programs of other donors/international financial institutions.

## IMPACT

**Conclusions** Being a partial re-guarantee of a guarantee makes assessment of the impact of the Philippines DCA guarantee difficult to quantify, and primarily subjective. The impact of the DCA guarantee has been modest to date. However, the DCA guarantee was a key factor, in combination with a number of elements, in initiating private lending to the target sectors. The true impact may be what was begun—the process of introducing private investment in the target sectors. The process continues with the creation of the new Philippines Water Revolving Fund (PWRF), a joint U.S./Japan initiative to coordinate and combine concessionary donor funds with commercial private financing for water infrastructure projects. The PWRF, launched in October 2008, utilizes LGUGC, a new DCA guarantee and concessionary loans from Japan International Cooperation Agency (JICA) to attract longer-term private investment and build on the progress made under the first DCA guarantee. Experience gained with this DCA guarantee and the existence of LGUGC, as strengthened by the monitoring and technical assistance that accompanied the DCA guarantee, were important factors in the formation of the PWRF and the commitment to participate of private financial institutions. Furthermore, the World Bank is planning a program to complement the PWRF.

This publication was produced for review by the United States Agency for International Development. It was prepared by SEGURA/IP3 Partners LLC under SEGIR Global Business, Trade and Investment II – IQC Indefinite Quantity Contract, Number EEM-I-00-07-00001-00 Task Order # 04, Development Credit Authority Evaluation

## LGUGC GUARANTEED TARGET SECTOR LOANS BY VALUE



■ DCA Loans to LGUs    ■ DCA Loans to WDs  
 ■ Non-DCA Loans to LGUs    ■ Non-DCA Loans to WDs

In the long term, the impact of the DCA guarantee as a demonstration model could be significant.

**Findings** in support of these conclusions include:

- Prior to the LGUGC, there was virtually no access to private sector financing in the target sectors.
- One private financial institution has made a loan to a water district without a guarantee, which it would not have made without its experience with LGUGC, and is considering lending to LGUs without a guarantee.
- Target sector borrowers have accessed about US\$70.6 million in private financing guaranteed by LGUGC (both DCA and non-DCA guaranteed loans).
- LGUGC participated in a pilot project, which presaged the PWRF.
- Based on experience with the subject DCA guarantee, a new guarantee with LGUGC was approved by USAID to serve as an integral part of the PWRF.
- Several donor/international financial institution projects under development are directed toward either urban infrastructure generally or the water sector specifically, including a World Bank project aimed at assisting less-than-creditworthy water districts to complement the PWRF.

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