

**Country Assistance Program
for
the Republic of the Philippines**

Government of Japan

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Country Assistance Program for the Philippines

I. Revision of Country Assistance Program for the Philippines

In May 2004, Japan decided to revise the Country Assistance Program for the Philippines at the ODA General Strategy Council (Professor Tsuneaki Yoshida of Tokyo University, Chairman of the Tokyo Task Force). Japan established the first Country Assistance Program for the Philippines in 2000. However, due to the new conditions such as subsequent changes in economic conditions in the Philippines and the announcement of the Medium-Term Philippine Development Plan (MTPDP) by the second Arroyo administration in 2004, Japan decided to revise the Program in order to adjust it to these new conditions. This new Country Assistance Program specifies the direction of Japan's ODA toward the Philippines for the next five years.

II. Significance of Assistance to the Philippines

1. Why Assistance to the Philippines is Important

Assistance to the Philippines is important for various reasons, including: (1) the Philippines lies along vital sea lanes and is thus an important country in geopolitical and regional security terms; (2) Japan and the Philippines share the same values including liberal democracy, human rights, and market economy, and, thus, the Philippines is a key partner in Japan's foreign policy toward Southeast Asia (2006 marked the 50th anniversary since the normalization of diplomatic relations between Japan and the Philippines); (3) Japan and the Philippines have had close economic ties for years (the Japan-Philippines Economic Partnership Agreement (JPEPA) was signed in September 2006).

2. Japan's Assistance Policy and assistance to the Philippines

The principles and goals of Japan's assistance are provided through Japan's Official Development Assistance Charter (ODA Charter) and Japan's Medium-Term Policy on Official Development Assistance (Medium-Term ODA Policy), which emphasize the importance of the perspective of human security and state that Japan pay full attention to the situation regarding the protection of basic human rights in recipient countries. These documents enumerate poverty reduction, sustainable growth, and peace-building as the priority issues of Japan's ODA, and state that ODA should be implemented more efficiently and effectively (through "selection and concentration" and

emphasis on results). The Philippines has difficulties in achieving sustainable growth, and its poverty rate remains as high as 30%. In addition, the Mindanao area has long been plagued by conflicts. Thus, Japan recognizes the importance in assisting the Philippines from the perspective of its overall assistance policy.

III. Analysis and Assessments of the Country Assistance Program for the Philippines in 2000 (hereinafter referred to as “the Program”)

1. Conditions at the Time of Formulation of the Program

Thanks to political stability and undisturbed domestic security under the Ramos administration, as well as the steady growth of foreign investment and exports, the impact of the Asian economic crisis of 1997 on the Philippine economy was comparatively small. Although the succeeding Estrada administration (1999-2000) initially aimed for a balanced budget, it subsequently shifted to a positive fiscal policy which depended on financing from overseas. The following change of governments in 2001 saw the shift to a policy of fiscal austerity.

2. Overview and Results of the Program

(1) Priority Areas

The program focused on the following four priority areas:

- i) Strengthening the economy and overcoming constraints toward sustained economic growth
- ii) Rectification of disparities (Alleviating poverty and redressing regional disparities)
- iii) Environmental protection and disaster prevention
- iv) Human resources development and institution building

(2) Output of Assistance

The output of assistance since the start of the program (FY2001-FY2005) is as follows: approximately 133.1 billion yen in yen loans (E/N-based), 20.8 billion yen in grant aid (E/N-based), and 30.8 billion yen in technical cooperation (based on JICA expenses). The largest allocation of assistance was to the Luzon areas. In terms of category, while economic infrastructure had the largest portion of assistance, environment improvement and poverty elimination had also substantial shares.

(3) Problems Surrounding Yen Loans and General Grant Aid

During the period from FY2003 to FY2005, no new yen loans were provided due to absence of requests owing to the tightened fiscal policies of the Philippine government. In addition, the severe fiscal situation in the Philippines caused delays in the progress of on-going yen loan projects and in the reimbursement of value added tax (VAT) to Japanese contractors. The provision of new general grant aid was also suspended in FY2004 because of the VAT issue, but it was resumed in FY2006 (see below for details).

3. Program Review

(1) Review Concerning Priority Areas

(A) Strengthening the Economy and Overcoming Growth Constraints toward Sustained Economic Growth

(a) Achievements

With the cooperation of other donors, Japan engaged actively in dialogue with the Philippine government through fora such as Consultative Group Meetings concerning the optimal modality of macroeconomic management. With respect to fiscal reform in the Philippines, donors' support for the reform encouraged their implementation and yielded other results.

With respect to the economic infrastructure development, aid was provided for developing roads, ports, airports and railways throughout the country and for formulating plans for power supply development. Other results included the development of environment-related infrastructure.

(b) Challenges

Policy dialogue did not produce adequate results in terms of improving the investment environment and governance.

With respect to the development, operation and management of infrastructure, initially planned results or objectives were not achieved due to the difficulty of grasping the Philippines' difficult fiscal situation and insufficient sense of ownership by the Philippine side.

(B) Rectification of Disparities (Alleviating Poverty and Redressing Regional Disparities)

(a) Achievements

Because the poverty rate in rural areas is high compared with urban areas, aid was provided for building basis for agricultural production, including irrigation facilities. Aid was also provided in such “software” areas as developing and propagating agricultural technology and strengthening farmers’ associations. This aid yielded such results as improved productivity, but the achievement of higher income improvement, as a more fundamental objective, was not entirely fulfilled and challenges still remain. In addition, wide-ranging aid for improving access to basic social services, such as development of health and medical care and water supply facilities and construction of educational facilities, contributed to poverty alleviation.

(b) Challenges

The Philippine government is also grappling with poverty alleviation as a key priority and it is making overall progress in achieving the Millennium Development Goals (MDGs). Nevertheless, the gap between the rich and the poor and regional disparities in income remain conspicuous.

Some elements of Japan’s aid for rural areas, such as providing agricultural technology guidance and strengthening farmers’ associations, will need more time to achieve more tangible results.

(C) Environmental Protection and Disaster Prevention

(a) Achievements

In the area of environmental protection, efforts have been made to strengthen mechanisms for enforcing laws and regulations as well as forest management. Significant achievements were seen in natural disaster prevention in developing comprehensive measures against floods and landslides in both “hard” and “soft” components through concentrating assistance to disaster-prone areas.

(b) Challenges

One issue regarding natural disaster prevention is to improve information dissemination to the communities concerned. As for the environmental protection, there remain many challenges, including waste disposal problem as an especially serious one. Therefore, it is necessary to improve the management capacity of administrative agencies concerned and local governments, through strengthening measures based on laws and regulations.

(D) Human Resources Development and Institution Building

(a) Achievements

Improvement of the environment for basic education was assisted through the measures such as construction of school buildings and classrooms, provision of educational materials and equipment, and training of teachers. Capacity building of central government officials was also conducted through e.g., grant aid for human resources development scholarship. For regional government officials, aid for capacity building for the Autonomous Region in Muslim Mindanao (ARMM) was started in 2004.

(b) Challenges

The shortage of classrooms has not yet been resolved, and large disparities exist in teacher's quality, especially in mathematics and science. The capacity of administrative agencies needs to be further improved.

(2) Review Concerning the Points to Be Taken into Consideration in Aid Implementation

(A) Cooperation with NGOs

Active aid has been provided in community-level development projects through collaboration schemes with NGOs, including grant assistance for grass-roots human security projects. Various types of cooperation with NGOs have been sought so that the benefits would reach the grass-roots levels. In providing direct aid to the poor through such schemes as grant assistance for grass-roots human security projects, cooperation with NGOs with carefully organized assistance is achieving results from the perspective of human security. Collaboration with NGOs has been effective in securing benefits at the grass-roots level in other schemes as well. It is necessary to further study effective ways of cooperation with NGOs.

(B) Consideration for Redressing Regional Disparities

Considering the need to redress regional disparities, many projects have been conducted in rural areas outside of Metro Manila, and thus contributed to mitigating disparities.

(C) Project Implementation Capacity, Debt Repayment Capacity, and Operation and Maintenance Capacity

Since the Philippine government was unable to secure the necessary budget for aid implementation, the progress of some projects, particularly those for yen loans, was hindered, and general grant aid was suspended due to the unreimbursed VAT problem. Consequently, for yen loan projects, both governments conducted a portfolio clean-up exercise in order to reexamine the priority among the ongoing projects, based on a review of the Philippines' fiscal outlook. As a result, some projects were cancelled. Regarding general grant aid, as a result of extensive consultations between the two governments and achieving the payment of 85% of the total amount of unreimbursed VAT as of March 2006, a resumption of general grant aid was announced in April 2006. The issue of unreimbursed VAT also occurred with yen loans, and both governments have continued consultations with a view to a prompt completion.

4. Challenges Encountered and Lessons Learned During Implementation of the Program

(1) Further Strengthening of the Policy Dialogue

In order to deepen mutual understanding among the various players about the direction of Japan's aid and to ensure compatibility between assistance projects of Japan and the development plans of the Philippine government, it is necessary to further strengthen the policy dialogue.

(2) Formulating Assistance Strategies from a Mid-Term Perspective

In order to prevent project delays and the recurrence of the issue of unpaid VAT due to deteriorating fiscal situation, it is important to formulate aid strategies for primary challenges and sectors in line with the MTPDP of the Philippine government and to ensure the implementation based on prioritization of projects from a mid- and long-term perspectives.

(3) Improving Budget Efficiency and Securing an Appropriate Technological Level

While the Philippine government has shown an increased level of awareness of project cost efficiency, Japan also needs to clarify the cost reduction effects by providing explanations of design requirements and cost calculations, among others.

(4) Strengthening Project Appraisals

In order to provide assistance more efficiently and effectively, it is necessary to more strictly conduct project appraisals for identifying and formulating good projects

based on the fiscal situation and administrative capacity of the Philippines. It is also necessary to pay attention to the efforts by the implementing agencies of the Philippines to secure the counterpart budget for the smooth implementation of projects.

(5) Strengthening Monitoring and Evaluation of Projects Following the Implementation
(Securing Sustainability and Self-Sufficient Development)

It is important to strengthen project supervision by project monitoring. Such monitoring should check, among others, if the benefits of the project reach the beneficiaries and if the Philippine side has secured sustainability and self-sufficient development. At the same time, it is also important to secure systems that can appropriately provide feedback of evaluation results to future assistance.

(6) Strengthening Cooperation and Coordination with Various Players

In order to give more effect to the assistance, it is necessary to seek further cooperation and coordination with the following various implementing players.

(A) NGOs

Because Philippine NGOs have a strong interest in Japan's ODA, it is important to seek active linkage and cooperation with such NGOs through dialogue and thereby to enhance the effectiveness of Japan's assistance.

(B) Local Government Units (LGUs)

While the decentralization process is proceeding, implementation capacity of local government units (LGUs) has not been sufficient to address the expansion of scope of their administrative authorities. Therefore, it is necessary to enhance the capacity of LGUs in order to secure the effectiveness of aid.

(C) Other Donors

In order to use the limited financial resources effectively, particularly in securing adequate results of aid in the social development sector, it is necessary to further promote coordination with other donors.

(D) Private Sector

Ensuring the sustained economic growth of the Philippines depends crucially on cooperation with the private sector since what can be achieved through public flow alone is limited under the difficult fiscal situation. It is important to cooperate with companies

that make private investment. Also, it is meaningful to promote dialogue with economic organizations that have influence on investment trends and to grasp needs for economic infrastructure development and other matters.

(7) Emphasizing Policy-Support and Issue-Oriented Assistance

In order to promote “selection and concentration” in our assistance policy and ensure that the aid effect is maintained in the Philippine side, it is necessary to place more importance on policy-support assistance. In addition, it is necessary to provide intensive assistance in certain areas such as sustained economic growth and poverty reduction by utilizing all available schemes and making cross-sector efforts (issue-oriented assistance).

IV. Situation in the Philippines (factors of changes and constraints in the Philippines)

1. Political Situation

The Arroyo administration identified fiscal reform, achieving peace with anti-government forces, and domestic harmony that transcends social classes as the current key policy challenges. In her inaugural address given in July 2004, President Arroyo also mentioned job creation through sustained economic growth and the improvement of basic living conditions.

As the fiscal situation is being improved, the Philippine government is actively promoting infrastructure development. In her State of the Nation Address (SONA) in July 2006, President Arroyo announced a medium-term development plan which aims for more effective development by categorizing regions of the nation into five “Super-Regions,” namely: Northern Luzon and Mindanao as the agribusiness regions, the Luzon Urban Beltway as the center of services and industry, Central Philippines as the center of tourism, and the Cyber Corridor which connects areas providing IT-related services and science technology. In order to realize the plan, she emphasized the need to promote infrastructure development nationwide.

With regard to the peace process with anti-government forces, the government has made progress in achieving peace with some Islamist groups, terrorist bombings have continued in various areas. It is recognized that further efforts are needed in order to achieve stable development and maintain peace in the regions.

In the area of domestic harmony, although suspicions of electoral fraud by President Arroyo in June 2005 led to demands for her resignation and a state of emergency was declared due to a failed coup d’etat by the military in February 2006,

conditions have stabilized at present.

Moreover, in the Philippines, there exist so-called “political killings,” and the Philippine government, regarding the situation as serious, established special investigation teams within the National Police in May 2006 and an investigatory commission which is independent from the police in August. In January 2007, based on reports from the investigatory commission, the Philippine government announced a new counter measure, and in February, the Philippine government accepted Professor Philip Alston, UN Special Rapporteur on extrajudicial, summary or arbitrary executions.

2. Economic Situation

(1) Economic Situation (Insufficient to Get on Growth Track)

Although in recent years, economic growth led by consumption has remained in the 4-5% range, this growth has not spurred job creation commensurate with the population increase (annual 2.3%), and unemployment rate remains at the level of 11-12% annually (measured by the previous standard). In addition, infrastructure investment in the Philippines has stagnated at annual 2% relative to GDP in recent years, which is lower compared to other ASEAN countries such as Thailand and Malaysia.

(2) Characteristics of Economic Structure

One characteristic of demand in the Philippines is the high share of private consumption relative to GDP, which stood at 78.7% in 2004. In contrast, public consumption declined to 6.9% of GDP in 2004, reflecting the austere expenditure management by the government in recent years. On the supply side, the service industries lie at the core of industrial structure.

(3) External Economic Relations

(A) The Manufacturing sector, particularly the production of electronic and electrical equipment, accounts for most of the exports from the Philippines. To achieve an investment- and export-oriented growth, further growth of manufacturing industries is necessary. Therefore, further improvement of the investment environment and supporting industries are essential.

(B) Since 2000, the amount of foreign direct investment (in terms of international balance of payments and equity capital) has followed a downward trend, declining from \$1.82 billion in 2000 to \$630 million in 2003. Although direct investment has

turned upward since 2004, local Japanese Chambers of Commerce and others have pointed out that the lack of infrastructure development has hampered international competitiveness.

- (C) In the international competitiveness ranking, the Philippines has been lowering its position year by year (from 35th in 2000 to 49th in 2006). The efficiency and governance of the Philippine government has been given low ratings.

(4) Fiscal Situation

- (A) Although the government achieved its goals for reducing fiscal deficits in 2005 and 2006, this success was due mainly to expenditure management. Therefore, further revenue collection efforts are necessary through tax increases (through ensuring the implementation of the revised VAT law, etc.) and more efficient tax collection.
- (B) Because the deficits of government-owned and controlled corporations (GOCCs) are at the high level, the Philippine government is promoting reform of the electric power sector and reform of GOCCs.

3. Social Situation (Fight Against Poverty)

(1) Current Situation of Poverty in the Philippines

Although the poverty rate of the Philippines has shown a slight tendency to decline over the past several years (from 33.0% (2000) to 30.0% (2003)) (the population which belongs to the poverty group declined from 25.47 million in 2000 to 23.84 million in 2003), it still remains high. The Gini coefficient (a measure of inequality of income distribution) has been declining slightly (less than 0.47 in 2003), but it is higher than those of other ASEAN countries such as Thailand. In addition, regional disparities within the nation still remain large.

(2) Current Situation of Basic Human Needs in the Philippines

- (A) Compared with other ASEAN countries, the maternal and child health index is poor (The Maternal Mortality Rate was 200 per 100,000 births in 2000, Infant Mortality Rate was 26 per 1,000 births in 2004, and Under-five Mortality Rate was 34 per 1,000 births in 2004). The number of patients with tuberculosis also remains high. Problems remain concerning the supply of safe drinking water in regional districts.
- (B) Although the primary school full enrolment has reached 90%, the completion rate remains less than 70% since the rate of dropouts and repeaters in basic education is high. In addition, due to the effect of population increase and other factors, there is a

shortage of classrooms, educational materials, and teachers. The quality of education is also inadequate.

- (C) In areas which were not mentioned above, there are serious problems such as the lack of the basic infrastructure indispensable for improving income, especially in rural areas.
- (D) In the Philippines, natural disasters hit at as high a frequency as any country in the world, and occur nationwide. The poor are the most frequent victims of such natural disasters.

4. Situation in Mindanao

(1) Mindanao: the Poorest Region in the Philippines

Mindanao is the poorest region in the Philippines. The poverty rate among the Regions in Mindanao in 2003 (Region 9 to 13 and the ARMM) exceeded the national average of 30%. The ARMM, in particular, registered 52.8%, the worst in the country. In 2005, GRDP per capita of all Mindanao Regions went below the Philippines' national average of 14,186 pesos. The 3,433-peso per capita income in the ARMM was the lowest among the 17 Regions of the country and was even less than one-tenth of that of Metro Manila, 35,742 pesos.

Mindanao is facing a number of problems in various sectors as follows:

- (A) In the health sector, mortality rates among infants and pregnant women are high. There is a severe shortage in the supply of medical services.
- (B) In agricultural areas, agricultural productivity is low while people highly depend on agriculture. In areas depending on fishing, the development of fishing ports and fish processing facilities is inadequate.
- (C) There are a number of concerns in the area of basic infrastructure, including shortage of electricity supply, and inadequate and poor water supply, telecommunications, and roads.
- (D) In education, both the rate of completion of primary education and the literacy rate are low. Conspicuously, schools are unevenly located, particularly in the ARMM, and there are areas that have a large concentration of children who cannot commute to school. An overall shortage of classrooms is observed as well.

(2) An Unstable Situation

Long-standing conflicts in Mindanao have hindered both domestic and foreign investment and development assistance, creating an unfavorable cyclical pattern that

further slows down the development of the region. This situation tends to reduce the investment attractiveness not only of Mindanao but also of the Philippines as a whole, and thus hinders the economic development of the nation.

V. Development Challenges of the Philippines and Donors' Responses

1. Development Challenges of the Philippines

- (1) In June 2004, President Arroyo presented the future direction of development of the Philippines in the 10-Point Agenda(*), goals of which included job creation and balancing the budget. In response, the Philippine government announced its MTPDP (2004-2010). This plan focused on the promotion of strong economic growth, poverty reduction through job creation, and achieving peace. The plan points out, in particular, that economic growth in the Philippines is modest compared with neighboring Asian countries and that a higher growth rate (7 to 8% annually) is needed in order to create jobs and reduce poverty.
- (2) The MTPDP also stressed that the resolution of fiscal problems was indispensable to achieving sustained economic growth. The Philippines government then set an objective of achieving reduction of the budget deficit to zero by 2010 (Later, the year of the object was reset from 2010 to 2008 with reflecting the fiscal improvement from 2004 to 2005), and directed effort toward reducing fiscal deficits. As a result, the fiscal situation has improved recently (In 2006, the Philippine government achieved more reduction of deficit going beyond the benchmark).
- (3) In response to the improvement of the fiscal situation, the Philippine government indicated that it would actively promote infrastructure development in order to increase international competitiveness, and presented a policy to increase the infrastructure investment up to 4 to 5% of GDP, through establishing the Comprehensive and Integrated Infrastructure Program. From now on, it is necessary to pay attention to whether such policies can be realized while at the same time maintaining fiscal discipline.

(*) 10-Point Agenda

- (1) The creation of six million jobs in six years via more opportunities given to entrepreneurs, tripling of the amount of loans for lending to small and medium enterprises and the development of one to two million hectares of land for agricultural

business, (2) The construction of new buildings, classrooms, provision of desks and chairs and books for students and scholarships to poor families, (3) The balancing of the budget, (4) The "decentralization" of progress around the nation through the use of transportation networks like the roll-on, roll-off and the digital infrastructure, (5) The provision of electricity and water supply to barangays nationwide, (6) The decongestion of Metro Manila by forming new cores of government and housing centers in Luzon, Visayas and Mindanao, (7) The development of Clark and Subic as the best international service and logistic centers in the region, (8) The automation of the electoral process, (9) A just end to the peace process, and (10) A fair closure to the divisiveness among the Edsa 1, 2 and 3 forces.

2. Activities by Other Donors and NGOs

- (A) Major donors have been watching closely state of play for achieving the balanced budget target set by the Philippine government, and have adopted a prudent stance toward new loans, especially those for the central government. With the recent improvement in the Philippines' fiscal situation, however, donors including the World Bank and the Asia Development Bank are starting the provision of new financing. Donors are also providing assistance to LGUs and NGOs as a direct partner under the decentralization and are seeking an expansion of the role of the private sector.
- (B) Philippine NGOs generally have high levels of capacity, and it is believed that to a significant extent they have established themselves, both in the constitution and in local governance, as a key player in the provision of services, particularly in the social development field.

VI. Direction of Japan's Assistance

Based on the analysis and evaluation of the current Country Assistance Program and the current status of the Philippines, the direction of Japan's assistance has been set as follows:

1. "Selection and Concentration" Based on the Constraints on Assistance for the Philippines

Under the difficult fiscal situations of the Philippines, attention must continue to

be given to the restricting factors such as the debt repayment capacity of the Philippines. Moreover, in view of the fact that Japan's ODA is required to be implemented efficiently and effectively, ODA must be provided under the concept of "selection and concentration."

2. Selection of Priority Development Issues

(A) Although it can be assessed that the individual aid provided under the Program established in FY2000 contributed to socio-economic development of the Philippines to a certain degree, the following challenges can be pointed out:

- (a) Given the difficult economic and fiscal situation of the Philippines, it is important to continue to provide aid for achieving sustained growth aimed at job creation which is a priority issue set forth by the Philippine government, while monitoring the progress of fiscal reform of the Philippines and the accompanying changes in restricting factors on Japan's assistance. Sustained growth is a necessary requirement for achieving poverty reduction.
- (b) Although the poverty rate in the Philippines has been improving, it nevertheless remains high. For further poverty reduction it is necessary to strive for a cross-sectoral approach in regions with high poverty rate to aid multiple sectors in an integrated manner, including enhancement of the capacity of LGUs, aid for agriculture, education, health, and protection of life from natural disasters.
- (c) In Mindanao, which is the poorest area and where unstable situations prevail, further assistance for poverty reduction and peace-building must be provided.

(B) Based on the assessment above, the new Country Assistance Program sets forth three priority development issues, namely, sustained economic growth aimed at the creation of employment opportunities, assistance for empowerment of the poor and improvement of the living conditions of the poor, and assistance for peace and stability in Mindanao.

3. Approach to Priority Development Issues

In light of the challenges encountered and the lessons learned under the existing Program, the guideline to lead assistance to the specific direction is as follows.

(1) Strengthening Policy Dialogue

In order to provide Japan's aid more efficiently and effectively, it is necessary to share recognition on the direction of assistance, and thus it is required to expand

dialogue between the two governments. When engaging in dialogue, Japan should devise ways of providing incentives to encourage the Philippine government to identify, formulate, and manage projects appropriately.

(2) Establishment of Assistance Strategies with a Medium-Term Perspective

In order to formulate and implement projects with a medium-term perspective and to consider aid strategies for primary challenges and sectors, the establishment and use of a rolling plan should be considered.

(3) Assistance for Policy-Making and Administration Capacity Building for the Central Government

In order to give the sustainability of aid and self-sufficient development, it would be desirable for the Philippine side to establish a system to maintain the outcome of aid on their own. Therefore, Japan will strengthen policy-making assistance and aid concerning management and maintenance, institutions, and human resources development for the central government with keeping the perspective of good governance.

(4) Assistance for LGUs and Strengthening Cooperation with LGUs

Amidst the process of decentralization, aid for administrative capacity building will be provided for LGUs so that the outcome of aid adequately reaches the poor in rural areas. For LGUs with high project implementation capacity, assistance through these LGUs should be more positively considered with keeping the perspective of good governance.

(5) Issue-Oriented Assistance

When dealing with comprehensive issues such as aid for sustained growth and poverty reduction, issue-oriented assistance should be strengthened by promoting measures including integrated and cross-sectoral efforts in multiple fields, and utilization of a variety of schemes.

(6) Project Formulation and Implementation Based on the Fiscal Situation and Implementation Capacity of the Philippines

Projects will be formulated and implemented by grasping the content of requested projects as quickly as possible, and by not only scrutinizing the content but also fully taking into account the fiscal situation and implementation capacity of the Philippines.

(7) Assistance through Cooperation with the Private Sector and Promotion of Public-Private Partnerships (PPP)

Because of limitations to what can be achieved by public funds alone, particularly in infrastructure development, it will be examined how to provide aid through cooperation with the private sector and public private partnership (PPP).

(8) Strengthening Cooperation with Civil Organizations and NGOs

This task will be accomplished by not only expanding opportunities for collaboration with NGOs but also actively promoting dialogue at the policy level. Positive consideration will also be given to new methods of cooperation to allow NGOs to conduct their activities in a more active and flexible manner.

(9) Complementation and Coordination between Donors

Establishing sector-based aid strategies in major sectors in coordination with other donors is effective for determining prioritization in project formulation and confirming the financial outlook of the Philippines. In addition, larger aid effect can be expected when complementation between donors is conducted.

(10) Use of Local Human Resources

Local human resources will be actively utilized in cases such as when aid is specially rooted in the local area and when assistance by personnel knowledgeable about security conditions is required.

(11) Strengthening Monitoring and Evaluation Activities

Monitoring and evaluation activities will be strengthened for projects under implementation and those completed.

4. Priority Development Issues and Guideline

The priority development issues will be handled under the following guideline. Refer to the attached document for details.

(1) Sustained Economic Growth Aimed at Creating Employment Opportunities

Aid will be provided to the Philippine government in its efforts to achieve macroeconomic stability (fiscal reform) and to improve policy implementation capacity and governance. Aid will also be provided to help promote foreign direct investment. Furthermore, with a viewpoint of improving infrastructure and services, aid will be

provided for developing the infrastructure that underpins sustained economic development, as well as in the “software” areas such as improving management and maintenance capacity. Such aid will be conducted particularly in those regions that form the core of economic growth, such as the Metro Manila area and Cebu, giving consideration to environment issues.

(2) Empowerment of the Poor and Improvement of the Living Conditions of the Poor

In order to provide assistance that directly reaches the poor from the perspective of human security, aid concerning the improvement of livelihood and expansion of basic social services will be provided, giving emphasis to local viewpoints.

i) Improvement of livelihood (Empowerment of the Poor)

Aid will be provided for the development of facilities and equipment which would contribute to increasing income-earning opportunities for the poor. At the same time, aid will be provided to contribute to the empowerment of the local community and individuals, including local government, citizens’ organizations, and NGOs, as exemplified by the spread of production technology for farmers and fishfolks in rural areas and the strengthening of the capacity of farmers and fishfolks’ organizations.

ii) Expansion of Basic Social Services (Improving the Living Conditions of the Poor)

Aid will be provided for improving access by the poor to basic social services in areas such as health care services, education, and disaster prevention, along with aid for improving the quality of these social services.

(3) Peace and Stability in Mindanao

Assistance for Mindanao will be intensively provided for the purpose of (1) alleviating the most extreme poverty of Mindanao and (2) consolidating for peace in Mindanao. To this end, aid will be given based on the “Support Package for Peace and Stability in Mindanao” with the following areas prioritized: (1) support for policy formulation and implementation (targeted at the ARMM government), (2) improvement of basic human needs, and (3) peace-building.

Priority Development Issues of the Country Assistance Program for the Philippines
(Annex to the Country Assistance Program for the Philippines)

The priority development issues of the Country Assistance Program (Philippines), namely, sustainable economic growth aimed at creating employment opportunities, empowerment of the poor and improvement of the living conditions of the poor, and peace and stability in Mindanao, will be addressed by providing assistance based on the guidelines given below.

I. Sustainable Economic Growth Aimed at Creating Employment Opportunities

1. Basic Approach

As demonstrated through the experience of development in East Asia, economic growth is an essential requirement for achieving sustained poverty reduction. The Medium-Term Philippine Development Plan (MTPDP) sets forth the goal of achieving economic growth of 7 to 8% annually and halving the poverty rate in 2000 (34%) by 2010. These objectives are consistent with Japan's Official Development Assistance (ODA) strategy (as outlined in the ODA Charter and the Medium-Term Policy on ODA), which emphasizes economic growth and poverty reduction.

From this perspective, Japan gives priority in its ODA to assistance in sectors that lead to the achievement of sustained growth led by investment and exports, raising the growth potential of the Philippines. Specifically, Japan will effectively combine support for the development of a foundation for economic growth with cooperation for the improvement of business and investment environment, and cooperate in achieving sustained growth of the Philippines led by investment and exports by providing the assistance described below in a strategic and priority-based manner. Supporting the development of a basis for economic growth, Japan will effectively provide various assistance in "soft" components such as improvement of policy formulation and implementation, management, operation and maintenance abilities, and human resources development, in addition to assistance in "hard" components. Assistance will be provided selectively taking into account the fiscal situation of the Philippines.

In September 2006, the governments of Japan and the Philippines signed the Japan-Philippines Economic Partnership Agreement (JPEPA). When this agreement goes into effect following the approval by the legislative bodies of both countries, it is expected that the economic relationship between Japan and the Philippines will become even stronger and that the business and investment environment in the Philippines will be

improved. It would be more effective if such efforts combined with ODA related to the improvement of the business and investment environment and investment promotion policies are provided.

2. Direction in Each of the Priority Sectors

(1) Improvement of Business and Investment Environment

In order to achieve sustained growth led by investment and exports, it is essential to promote private sector investment through the improvement of business and investment environment. To this end, Japan will cooperate mainly in “soft” components including capacity building in the formulation and implementation of policy in the following sectors.

(A) Macroeconomic Stability (Fiscal Reform)

Achieving economic growth requires a stable macroeconomic environment (public finance, inflation, and currency value). This requires steady improvement of the fiscal outlook.

Fiscal reform will contribute to the improvement of business and investment environment by (1) reducing country risk and promoting new investment by improving debt sustainability, and (2) enabling increases in expenditure for areas including infrastructure investment through higher annual revenues.

In view of the importance of fiscal reform, Japan will provide support in the form of policy advice, such as policy support programs, in the area of policy formulation and also extend cooperation in the area of policy implementation, such as improvement of tax collection capacity.

(B) Investment Promotion Policy

For mid- to long-term development of the Philippines, private sector investment plays an important role. In order to promote private sector investment, it is essential that the Philippines provides investment incentives by specifying business sectors in which the Philippines has comparative advantage (electronics industries, business process outsourcing (BPO), tourism, etc.), and also makes intensified efforts for measures including fostering small and medium enterprises (SMEs) that constitute supporting industries, relaxation of business regulations, and facilitation of trade and investment procedures. It is also important to ensure availability of manpower for the private sector investment and to establish a system which continuously provides such manpower.

In order to promote investment, Japan will cooperate in the areas including: (1) support for formulation and implementation of policy concerning investment promotion;

(2) support for financing, capacity building, and company start-up to SMEs; (3) securing transparency and stability of business regulations; (4) achieving smooth and prompt customs services; (5) human resources development and skills training for producing highly-skilled workforce.

(C) Good Governance

The struggle of the Philippines' public sector to eliminate corruption in administrative and judicial bodies due to weak governance has been a major factor constraining the improvement of the business and investment environment.

Japan will cooperate in this sector from the viewpoint of the improvement of business and investment environment, in coordination with other donors, including the possibility of introducing policy support programs.

The problem of public security is not only a serious matter of concern for those involved in business and investment activities in the Philippines but also a factor which discourages new investment by harming the image of the Philippines inside and outside the country, and thus hinders the improvement of business and investment environment.

Taking the importance of this issue into consideration, Japan will provide cooperation for capacity building of the police and the law enforcement agencies in areas such as maritime safety and airport and seaport security.

(2) Developing a Basis for Economic Growth

In order to achieve sustained growth led by investment and exports, it is necessary to increase incentives for private sector investment by developing a basis for economic growth. To this end, Japan will cooperate in both "soft" and "hard" components in the following sectors:

(A) Development and Improvement of Transportation Networks

Development and improvement of transportation networks contributes significantly to developing the fundamentals for economic growth. From the viewpoint of enhancing the Philippines' international competitiveness, it is especially important to relieve and reduce traffic congestion in Metro Manila and to develop and improve transportation infrastructure networks in areas such as Calabarzon where companies involved in electronics industries (the Philippines's largest exporting industry) are concentrated, and in other industrial centers such as the Subic-Clark-Batangas "Growth Corridor" (including Calabarzon) and Cebu.

From this viewpoint, Japan will provide cooperation, keeping a link with efforts aimed at developing the business and investment environment, in the following areas: (1)

development and improvement of the major transportation networks that support economic growth; (2) strengthening the linkages between these transportation modes; (3) infrastructure planning, operation and maintenance, and financial management; (4) improving management of infrastructure-related government-owned and controlled corporations; and (5) deregulation and private sector participation in the infrastructure field.

(B) Securing a Stable Supply of Electric Power

Electric power supply is a basis of business and economic activities and it is essential to secure the stable supply of electric power for realizing sustainable economic growth.

In the Philippines' electric power sector, the financial difficulty of the National Power Corporation (NPC) is a major factor of the expansion of deficits and debt in the public sector. Meanwhile, reform of the electric power sector, whose principal issues are the sale of NPC's power generation assets to the private sector, privatization of the power transmission sector, and creation of a wholesale electric power market, among others, is not making steady progress. As a result, there was not adequate construction of new power generating facilities and development and restoration of transmission facilities, which increased uncertainty about future electric power supply.

In order to secure a basis for stable supply of electric power at appropriate charges under such circumstances, Japan will conduct the following measures: (1) cooperation concerning the promotion of private sector investment in the power generation sector and the development of power transmission infrastructure; and (2) diversification of energy sources including geothermal and wind power and development of electric power generating facilities that contribute to utilization of the country's own resources, from the viewpoint of enhancing the power generating capacity of the Philippines, giving consideration to environmental protection in these efforts.

(C) Improvement of Urban Environment

In order to realize sustainable economic growth, it is indispensable to improve the environment of cities which are the core of the Philippines' economy. It is also necessary to take appropriate preventive measures in order to avoid the deterioration of urban environment that accompanies economic growth.

From this viewpoint, Japan will provide assistance for the improvement of the urban environment including solid waste management, sanitation measures, and water pollution control, taking into account the fiscal situation of the Philippines.

II. Assistance for empowerment of the poor and improvement of living conditions of the poor

1. Basic Approach

As there remain needs for alleviation of poverty and improvement of basic living conditions, the Philippine government is making efforts for poverty reduction under development goals such as the 10-Point Agenda. In addition, the Philippines is generally making progress in improving indexes concerning the Millennium Development Goals (MDGs), though with different degree of improvement, and is expected to achieve the MDGs by 2015. (It is presently assessed that some of the indexes in the two goals among the eight MDGs, “Achieve universal primary education” and “Improve maternal health,” will be difficult to achieve. In particular, among the 48 indices, “primary completion rate (from the 1st grade to the 5th grade)” and “maternal mortality ratio” are unlikely to achieve.)

Empowerment of the poor and improvement of the living conditions of the poor can be made by assistance that contributes to human security, which means creating an environment which enables people to have active human life. In addition, if peace-building and ensuring public security in the Philippines can be advanced through poverty reduction efforts, that will contribute not only to peace and stability of the Philippines but also to that of Southeast Asia and to Japan’s national interests to secure its peace and prosperity. For this reason, Japan intends to support the self-help efforts of the Philippines toward poverty reduction.

In details, empowerment of the poor and living environment improvement for the poor consist of both the economic factors such as securing employment opportunities and improving the income level of the poor and the factor of improving the access of the poor to basic social services including education, health and medical care, and protection of life against natural disasters. Accordingly, Japan sets forth improving livelihood and expanding basic social services as priority areas.

In the Philippines, there are wide disparities of income between regions. Japan therefore should give consideration to correcting these disparities in its assistance and fully pay attention to regions under severe poverty conditions.

In response to moves toward decentralization including the enactment of the Local Government Code of 1991, while making efforts for fulfillment of local governance capacity, Japan will make efforts to enhance the capacity of local government units (LGUs) as well as to formulate projects based on the local needs, including those initiated by LGUs. Upon project implementation, it is important to secure the appropriate allocation of the Internal Revenue Allotment (IRA) and the appropriate involvement of

the central government when necessary, taking account of the authority and capacity of LGUs. Meanwhile, in order to formulate effective projects, opinions of local residents should be obtained at as early stages as possible so that the poor can directly benefit.

In addition, cooperation and coordination with NGOs, including those of Japan, should be strengthened, securing their independence, and project formulation and implementation should be made responsive to and based on the local circumstances as much as possible, from a cross-sectoral viewpoint.

Furthermore, from the perspective of human security, consideration is given as much as possible to the socially vulnerable people, including women, children, people with disabilities, and indigenous people (IPs).

2. Direction in Each Priority Sector

(1) Improvement of Livelihood

(A) Support for Economic Empowerment of the Poor in Rural Areas

In order to secure new employment opportunities and improve the income of the poor through promotion of agriculture and fishery which are the main industries in rural areas, Japan will prioritize the support such as the development of agriculture and fishery production infrastructure, appropriate operation and maintenance, dissemination of production technology, strengthening the management of farmers and fishfolks' associations, and supporting agrarian reform communities where the poor account for a majority. Support is also given to the development of transportation infrastructure and distribution systems that link rural areas to urban markets. In addition, support is given to the improvement of the income of poor farmers and fishfolks through micro finance, and to the promotion of local industries. Upon the promotion of local industries, it is necessary to strengthen cooperation with LGUs and the private sector in the local area.

In supporting fisheries, the viewpoint of fishery resource management should be taken into consideration.

(B) Supporting Economic Empowerment of the Poor in Urban Areas

Japan will cooperate in providing micro finance to small and medium enterprises (SMEs) and micro-enterprises and in securing employment opportunities. Japan will also provide capacity building of the poor including skill training in order to assist them in getting a higher income. In addition, to address the issue of human trafficking which targets the poor who moved from rural areas, Japan will provide various supports including the protection of victims and extending skill training.

(2) Expansion of Basic Social Services (Improving the Living Conditions of the Poor)

(A) Securing Healthy Life

Japan will prioritize support for maternal and child health aiming at the improvement of maternal mortality and infant mortality ratio, which are especially problematic in the Philippines, among the MDGs. To this end, Japan will make efforts to strengthen local health system and provide support concerning access to safe water and improving sanitary conditions.

Furthermore, Japan will provide support to deal with infectious diseases including tuberculosis, which still remains a major disease. With respect to the emerging infectious diseases such as SARS and avian influenza, Japan will consider the support including emergency aid, while monitoring the trend of occurrence of these diseases.

(B) Securing the Ability to Live Independently

In order to reduce dropout rate and grade repetition rate in primary and secondary education, Japan will provide support for improving the environment that supports school attendance, including community efforts.

To improve the quality of education, Japan will cooperate for enhancing the competency of teachers and the school management capacity and help local communities to support schools.

(C) Securing Access to Basic Social Services

Japan will provide support for improving community roads, electrification, and access to information communications services in rural areas where private investment is not viable.

(D) Protecting Life From Natural Disasters

Japan will support the development, maintenance and management of flood control and sabo (erosion control) infrastructure in high priority sites, as well as strengthening disaster preparedness including evacuation plans etc., taking into account of the fiscal situation of the Philippines. In addition, Japan will provide support for proper forest management (including assistance for coastal areas) such as reforestation which contributes to measures against floods, mudslides, tsunami, and high tides.

Prompt emergency assistance and support for rehabilitation and reconstruction will be provided to regions which have suffered from enormous damages from sudden natural disasters.

III. Peace and Stability in Mindanao

1. Basic Approach

Mindanao is the poorest region of the Philippines. In providing economic assistance to the Philippines, special emphasis should be placed on support to Mindanao in view of freeing the region from extreme poverty. Support to Mindanao has a significant meaning for the consolidation for peace in the region and therefore for the stability and development of the Philippines as a whole. Moreover, building peace and stability in the Mindanao region also contributes to the peace and stability of the Asia-Pacific region, which is important for Japan as well.

The above mentioned two goals of Japan's support to Mindanao - namely, (1) the eradication of extreme poverty and (2) the consolidation for peace - were clearly expressed in the Support Package for Peace and Stability in Mindanao announced by then Prime Minister Koizumi upon President Arroyo's visit to Japan in December 2002.

Reducing poverty and consolidating peace are closely interrelated, and poverty is one of the principal causes of conflicts. Japan's ODA Charter clearly points out that poverty reduction is necessary to eliminate the factors that foster instability, including terrorism.

Based on such recognition, Japan will promote assistance for Mindanao under the Support Package, focusing on three priority areas: (1) support for policy formulation and implementation (targeted at the government of the Autonomous Region in Muslim Mindanao (ARMM)), (2) improvement of basic human needs, and (3) peace-building. (While (1) targets the ARMM government, (2) and (3) cover Mindanao as a whole, including areas outside the ARMM.)

2. Direction in Each Priority Sector

(1) Support for Policy Formulation and Implementation (Targeted at the ARMM Government)

The ARMM has the highest poverty rate in the Philippines, and at the same time covers a wide range of areas consisting of six provinces and one city. Therefore, it is especially important in Mindanao assistance to enhance the administrative capacity of the ARMM government which governs these areas. In addition, ARMM areas will form the core of the "Bangsamoro" homeland, which is planned to come into being as a result of peace negotiations between the Philippine government and the Moro Islamic Liberation Front (MILF), and in this sense too, support to the ARMM is important from the perspective of peace-building.

In order to enhance the administrative capacity of the ARMM government, it is

important that the ARMM has the planning capacity to grasp the needs of residents. For this reason, Japan will continue human resource development through training which is being provided until today. Along with such capacity building, support will also be provided for building an effective and efficient administrative institution.

(2) Improvement of Basic Human Needs

Support for the improvement of basic human needs will be focused on the sectors that are especially problematic, such as health care, education, and water supply. In addition, support will also be provided for rural development and livelihood as well as basic infrastructure which contribute to improving the income of residents.

(A) Health Care

Japan will continue human resource development in the health sector, and support for the enhancement of the local health facilities, focusing on the areas in which ex-participants of training courses are actively working.

(B) Education

Japan will provide support for the improvement of educational environment, including the expansion and renovation of school buildings and the construction of new schools in order to secure an adequate number of classrooms.

(C) Agriculture and Rural Development

Japan will provide support for the increase of farm productivity including the development of agricultural infrastructure and the extension of agricultural technology, particularly in poor areas. Support will also be provided for the development of transportation infrastructure and distribution systems.

(D) Development of Basic Infrastructure

Japan will provide support focusing on the construction and rehabilitation of roads and bridges, strengthening rural electrification, and supplying safe drinking water and basic sanitation facilities.

(3) Peace-Building

(A) In order to foster awareness among residents that contributes to the maintenance of peace, Japan will continue community development and extend cooperation in improving public security.

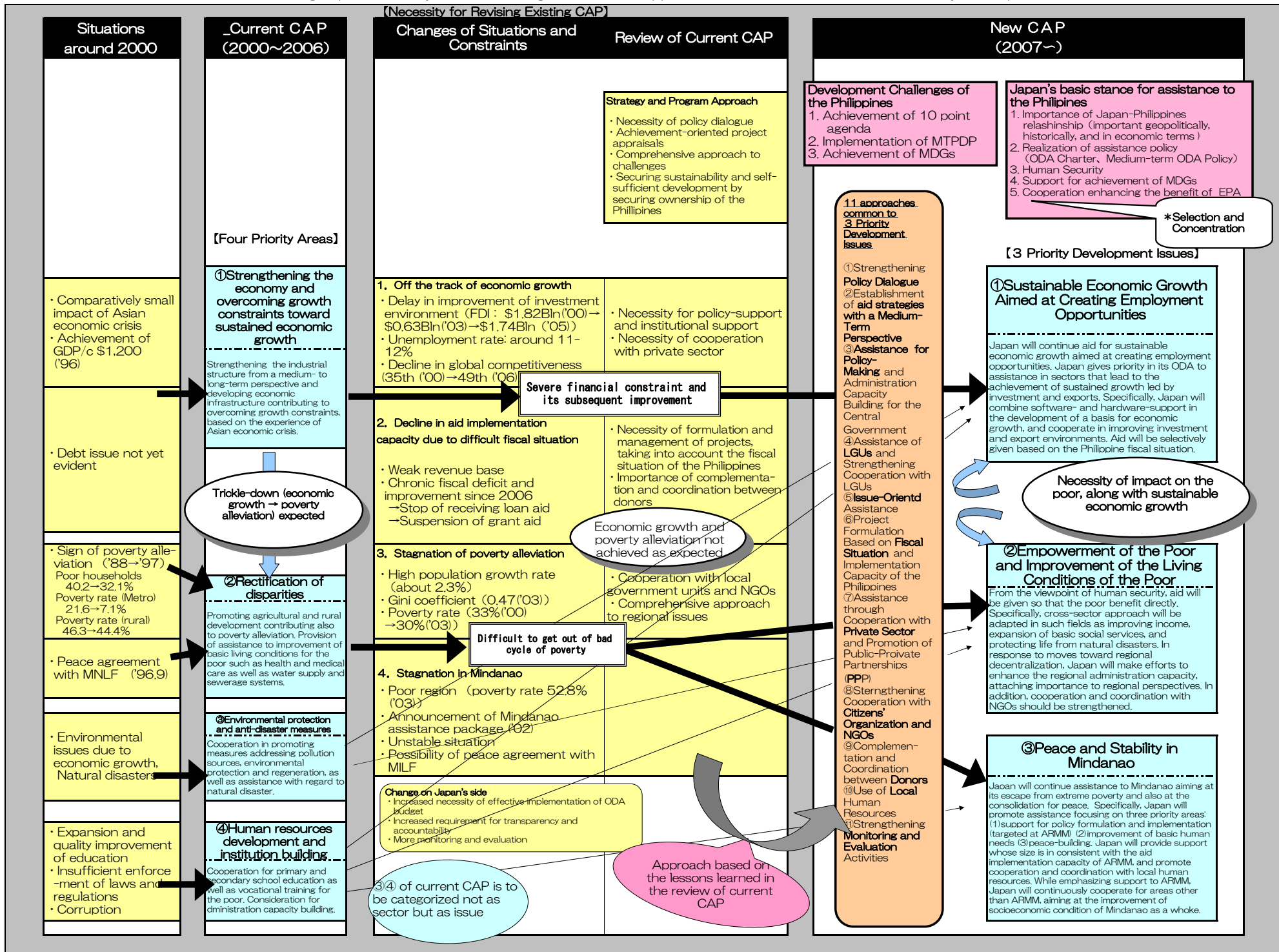
(B) Based on the progress of peace negotiations between the Philippine government and

Note: Japan dispatched a development expert to the International Monitoring Team (IMT) in Mindanao in October 2006, and signed grant contracts for 12 projects of grassroots and human security grant aid in the conflict-affected areas in December 2006.

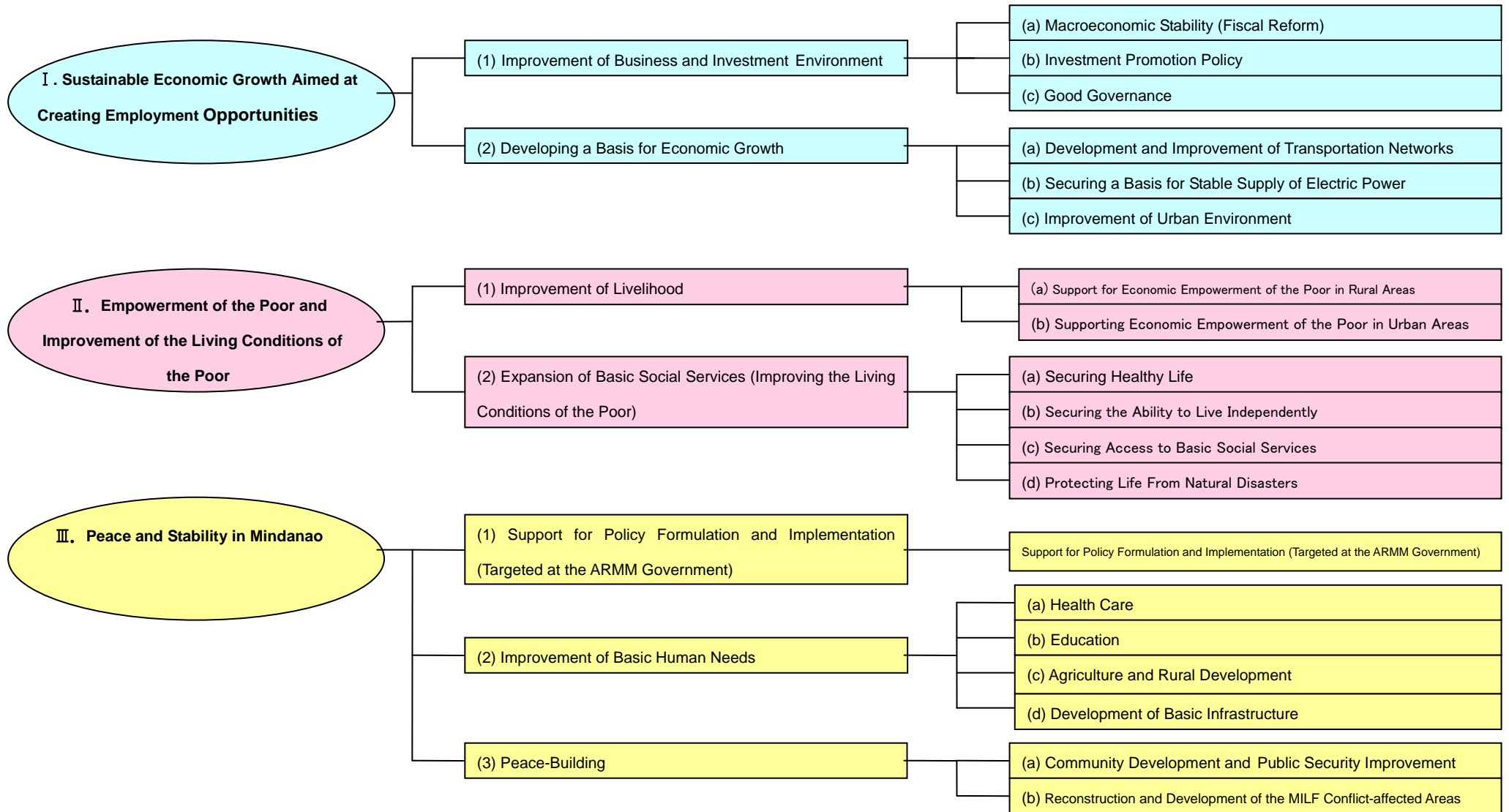
3. Points to Be Taken into Consideration

- (1) In Mindanao assistance, Japan will provide support whose size is consistent with the absorption capacity of the local society, and promote cooperation and coordination with local human resources (e.g., NGOs) in areas where the public security situation is unstable.
- (2) While emphasizing support to the ARMM where provinces with extreme poverty are concentrated, Japan will continuously cooperate for areas other than the ARMM, including the MILF conflict-affected areas, toward improving the socio-economic conditions in Mindanao as a whole.
- (3) In October 2006, Japan established the “Mindanao Task Force” consisting of the Embassy of Japan in the Philippines, the JICA Philippine office, and the JBIC Manila office. This task force, together with the development specialist dispatched to the IMT and in close cooperation with the key players including the Office of the Presidential Adviser on the Peace Process (OPAPP) and the Bangsamoro Development Agency (BDA: an organization established by MILF for socio-economic development), will support the formulation of a development plan for the MILF conflict-affected areas. In addition, taking account of the balanced development between these areas and other areas in Mindanao (including the ARMM areas), the task force has been coordinating assistance among the various schemes so that such assistance is implemented effectively and contributes to peace-building in Mindanao as a whole.

Basic Directions in Revising Japan's Country Assistance Program for the Philippines and Flow Chart of Selection of Priority Development Issues



Japan's Country Assistance Program for the Philippines



(注) ARMM : Autonomous Region in Muslim Mindanao

M I L F : Moro Islamic Liberation Front