Guarantees and Onlending to Sub-National and Parastatal Borrowers: The Case of the Philippines

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Outline of Presentation

- Institutional Arrangements
- Policy Considerations
- Risk Management
- Areas for Improvement
- Current Policy Thrusts and Objectives
- Concluding Remarks

Institutional Arrangements

- Various Ways of Raising Debt
  - Depends on credit standing
  - Bank financing including from Government Financial Institutions (GFIs)
  - Capital Markets
  - Official Development Assistance (usually through onlending schemes)
  - Creditors usually ask for a sovereign guarantee

Institutional Arrangements

- **Institutionalized Approval Process**
  - ✓ President of the Philippines
  - ✓ Monetary Board of the Bangko Sentral
  - ✓ National Economic and Development Authority (NEDA) Board
  - ✓ Department of Finance (DOF)
  - ✓ Department of Justice (DOJ)
  - ✓ Governing Boards/Bodies

Institutional Arrangements

- **Legal Bases is a Must**
  - ✓ **Foreign Borrowings Act**
  - ✓ **General Appropriations Act**
  - ✓ **Respective Charters of the Government Owned or Controlled Corporations (GOCCs) and GFIs – at least 51% ownership**
  - ✓ **National Government (NG) legally prohibited from guaranteeing borrowings of Local Government Units (LGUs)**

Institutional Arrangements

- NG Guarantee depends on Charter
  - Subject to Contract (Not automatic)
  - Automatic
  - Solidary (NG as primary obligor)
  - Subsidiary
  - Subject to Excussion
  - Finance Secretary sign off on guarantee.
  - In practice, NG advances funds to prevent a guarantee call and avoid cross default.

Policy Considerations

- Approval process incorporates various checks and balances to prevent abuse of authority.
- Seeks to avoid repeat of historical experience.
- Borrowings for productive activities and must be consistent with NG priorities, plans and programs.
- Extension of guarantees must be legally, socially and economically justified.

Policy Considerations

- Impact on NG Fiscal Position and the Consolidated Public Sector Financial Position.
- Policy bias for private sector as engine of economic growth and privatization.
- Adoption of hard budget constraints for GOCCs/GFIs.
- Current arrangement needs improvement.

Risk Management

- Interagency approval process focuses on entry conditions .
- Conditions attached such as payment of guarantee fees , establishment of sinking fund, legal and prudential ceilings etc.
- Focused on 14 monitored non-financial government corporations (MNFGCs) and GFIs.
- Emphasis on explicit guarantees.

Risk Management

- Privatization e.g. power sector.
- Creation of Debt and Risk Management Office (July 2010).
- Increasing attention to contingent liabilities, including performance undertakings on PPP's and their estimation.
- Is work in progress. Needs further improvement.

Areas for Improvement

- Debt and Risk Management functions of the DOF, including capacity building measures.
- Oversight of government corporate sector beyond the 14 MNFGCs and GFIs.
- Better estimation and management of fiscal risks arising from contingent liabilities e.g. inclusion in budgetary process.
- Higher standards transparency and disclosure e.g. fiscal risk document.

Current Policy Thrusts and Objectives

- **Proactive debt and risk management under a centralized system in the DOF.**
  - ✓ **Pursue local currency borrowing and other innovative financing structures that will reduce forex and other risks.**
  - ✓ **Proactive engagement with investors and rating agencies.**
  - ✓ **Diversify currency, market and investor base.**

Current Policy Thrusts and Objectives

- **Enhanced oversight of the government corporate sector under a centralized oversight body.**
  - ✓ **Quality at entry for Board Directors.**
  - ✓ **Strengthened board governance, including the Audit and Risk Management Committee functions.**
  - ✓ **Adoption of higher standards of transparency and disclosure.**
  - ✓ **Adoption of performance contracts.**

Current Policy Thrusts and Objectives

- **Better management of fiscal risks resulting from guarantees and onlending activities.**
  - ✓ Stricter implementation of hard budget constraints.
  - ✓ Closer scrutiny of requests for borrowing and NG advances .
  - ✓ Better financial and operational performance through clear performance metrics.
  - ✓ Tariffs allowed to adjust to at least cover costs.
  - ✓ Subsidies, if any, will be better targeted and focused on those needing it most.

Concluding Remarks

- Aquino Administration's focus on governance reforms augurs well for the management of fiscal risks emanating from guarantees and onlending activities.
- DOF under the leadership of Finance Secretary Cesar Purisima is committed to governance reform and is driving the fiscal reform process.

THANK YOU!