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**A: Investment Concept Title: Trade and Inclusive Economic Growth Facility (DRAFT)**

**Start date: Mid-2017; Timeframe: 4 + 4 = 8 years**

**Proposed funding allocation: \$80m over 8 years**

**Risk and Value assessment result: Low Risk / High Value**

**B: Problem/Issue definition and rationale for investment (Why)**

The Philippines' economy has been growing well over recent years, and faster than other economies in Southeast Asia. Since 2010 growth averaged about 6 per cent, government revenue has nearly doubled, and international perceptions of the Philippines have improved. Strong remittance flows have boosted domestic consumption, and business process outsourcing has boomed (creating a million new service jobs). However, population growth has remained high (slowing per capita growth), job growth has been sluggish, and poverty has fallen only slightly (from 28.6 per cent in 2009 to 26.3 per cent in 2015). The Philippines has one of the highest rates of inequality in South-East Asia.

While there has been important reforms in social policy and the quality of public administration, several key economic constraints need to be addressed. There is low productivity in agriculture and of particular importance to poverty reduction is the 'missing middle' in low to medium skilled manufacturing which has not emerged. Investment remains weak, especially due to restrictions on Foreign Direct Investment (FDI). The Philippines also remains relatively less connected to the regional and international economy than some of its neighbours. It is ranked 95 out of 189 countries on the World Bank's Trading Across Borders ranking, and FDI net inflows as a proportion of GDP is the third lowest out of all countries in ASEAN.

Continuing to invest in the Philippines' development remains in Australia's interests. Australia has been a long-time development partner of the Philippines, with a history of working in a broad range of relevant sectors such as governance, infrastructure, public financial management, social protection, land reform and education.

There are reasonable foundations for the next phase of our work. The President has signalled an intention to reform FDI rules, expand the country's conditional cash transfer program, improve the business environment and increase infrastructure spending. Better engaging with the global economy including through seeking entry to the Trans-Pacific Partnership is also a goal of the Philippines. Improved revenue flows could also enable a variety of new initiatives.

In response to the changing local environment, and our Aid Investment Plan published last year, we are re-casting our economic governance programs in the Philippines within the broader framework of a new, bilateral economic partnership. The proposed facility would be the centrepiece of a suite of economic initiatives which share the overarching objective of supporting sustained inclusive growth. They are:

- Trade and Inclusive Economic Growth Facility: the subject of this note;
- Connecting Transport Infrastructure for Economic Development Investment: to assist the Philippines to spend its increased revenues effectively on new transport infrastructure, through improvements to planning, budgeting and implementation;
- Energy: in which we are exploring opportunities for interventions which would increase supply and decrease the price of electricity, and which may be implemented through the proposed facility or separately; and
- Investing in Women (IWI): the key women economic empowerment investment in the Philippines which will help achieve gender equity in workplaces and increase investment in women-led small and medium sized enterprises.

This suite of programs is complemented by BEST, a six year program supporting implementation of K-12 education, and our innovative Coalitions for Change program which will increase its focus on economic policy objectives and work closely with the new programs. The new shape of our programs, including the proposed facility, will give us a coherent, well-integrated, and efficient approach to our economic growth/governance programming. It will be managed within a new steering arrangement, and connected to the Australia-Philippines *Comprehensive Partnership and Plan of Action*, and trade and economic talks launched in late 2015.

**C: Proposed outcomes and investment options (What)**

The broad goal of the Trade and Inclusive Economic Growth Facility will be to help the Philippines achieve sustained and

inclusive growth (see annex A for a preliminary logic framework). Five complementary areas of engagement underpin the facility and contribute to this goal:

- 1. Connecting the Philippines with the global economy: aid for trade**
- 2. Improving competitiveness through domestic regulatory reform**
- 3. Better jobs and increasing inclusiveness**
- 4. Responding to emerging economic issues**
- 5. Strengthening economic institutions**

Consistent with DFAT's *Effective Governance Strategy* in managing for inclusive growth in a fluid political environment, this investment needs to be flexible and design interventions in a range of policy and program areas. A flexible facility approach is critical to balancing the risk/return of our investments. Working more narrowly in just one or two of the above areas would be high risk due to political uncertainties, and would not coherently address the multifaceted nature of poverty. Noting that Australia's aid is small compared to Philippine government revenue, our impact on poverty through this facility is dependent on how we position ourselves to help the Government and local actors frame and implement its own inclusive growth agendas.

The facility will consolidate ongoing work streams of the current Philippines Program including – the Human Resource and Organisational Development Facility (HRODF), social protection, competition policy and economic research. The design process of the facility will consider how existing work streams will be absorbed and improved, and plan new activities in the engagement areas as detailed below. We envisage a mix of delivery modalities. In some cases, the facility will provide grants to non-government partners (e.g. multilateral banks, civil society, private sector or academia) that are important for policy debate, advice and building coalitions, whereas in others the managing contractor will design and implement activities.

1. Connecting the Philippines with the global economy: aid for trade - We propose to use the facility to implement a new aid for trade program which will help the Philippines better connect to the global economy. The design of two key activities are advanced and will achieve the following outcomes - (a) help the Philippines successfully negotiate trade agreements, and (b) increase exports/imports by Philippine businesses through better National Quality Infrastructure.

Trade negotiation capacity development will improve the capabilities of the Philippine government to negotiate Free Trade Agreements (FTAs). When implemented, these agreements will help businesses better access international markets and the Philippines to become more globally competitive through the economic reform it encourages. Reforms negotiated through external agreements can drive/supplement the domestic reform process. Aid activities under this component of the facility will include improving the Philippines' capability to research the impact of FTAs; understand and negotiate technical issues related to agriculture, competition and investment policy amongst others; communicate with the private sector including women-led businesses; build a trade competency framework that underpins a trade professional development program; and recruit and maintain staff, especially women. The Philippines Department of Trade and Industry (DTI) has identified trade negotiation capacity building as an area of high need and has requested Australia's support. It notes that existing training provided by donors including through RCEP and WTO are ad-hoc and do not sustainably boost DTI's longer-term capabilities. Rather than once-off and FTA specific training, DTI is seeking a solution that boosts the capabilities of the entire agency and has raised the idea of a trade negotiation training centre.

Aid for trade on National Quality Infrastructure (NQI) will provide support to key Philippine government agencies involved in standards, certification, accreditation, and metrology for traded goods and services. Priority will be placed on ensuring that businesses are well serviced and able to meet technical requirements and standards abroad. The World Economic Forum *Global Trade Enabling Report 2014* highlight that NQI is one of the top three concerns for exporting businesses in the Philippines. The facility will also seek to improve communication between government and businesses including in the development of standards, coordination between different NQI agencies, and collaboration between Philippine organisations and their relevant Australian/international counterparts. DFAT will also consider providing focused aid to small and medium sized enterprises (SMEs) including women-led businesses, and technical assistance across a particular value chain (e.g. cacao). The Facility can also be a vehicle to support the improvement of food standard regulations and processes for assessment of food imports.

Other aid for trade activities to be investigated for possible support include addressing restrictions on foreign investment (to improve the country's growth through increased access to capital, a priority for the new Administration), trade facilitation (better export/import procedures which lower the cost of trading) and liberalisation of the professional services sector.

2. Improving the competitiveness of the Philippine economy: domestic regulatory reform - This area of the facility will help the Philippines implement key domestic reforms that will improve the competitiveness of the Philippine economy and reduce business cost. A priority of the facility will be to expand Australia's current assistance on competition policy.

Implementation of the Philippines' new Competition Policy Act has the potential to reshape the Philippine economy which is currently characterised by private conglomerates with strong ties to the political elite. The Act, if implemented well, could provide significant poverty reduction benefits including by - reducing the costs of consumption including food; increasing job opportunities in small business; and reducing the cost of business inputs including for farmers. Australia is currently providing ad-hoc assistance to the newly established Philippine Competition Commission (PCC) which is mandated to implement the Competition Policy Act. The facility would seek to design and implement a more comprehensive program of support including technical assistance linked to the PCC business plan and helping it to access international competition policy experts.

Other economic reforms under investigation for support are - doing business (simplifying the steps to register a business, a priority for the new Administration); deregulation (reducing the cost of unnecessary or inefficient regulation imposed on business) and energy policy (reducing business and consumer cost by delivering sustainable and affordable electricity).

3. Better jobs and increasing inclusiveness - The facility will provide targeted support aimed at improving incomes of those below/at the poverty line, and other vulnerable groups. Australia's social protection aid in the Philippines will be continued, including our support to the Philippines' Conditional Cash Transfer (CCT) Program which has lifted 7.5 million individuals from poverty since 2010. Australia's social protection support will help the Philippine government to further improve CCT coverage to better encompass vulnerable groups including women, homeless families, indigenous people and the disabled, and to better facilitate employment outcomes. To sharpen the facility's gender focus, we will design a key project whose principal goal is to improve women's economic empowerment. This project could be trade related, and will complement activities implemented under Investing in Women, the Philippines Program's main vehicle for economically empowering women.

Other areas under investigation for support are - labour market reform (improve employment conditions for the working poor); and micro and small enterprise development (help entrepreneurs, for example farmers, to grow their business).

4. Responding to emerging economic issues - Our economic partnership with the Philippines needs to be flexible and responsive, adapting to the priorities of the Philippine administration and policy opportunities that may emerge. This has additional importance given that the facility will commence within a year of the inauguration of a new Philippine government administration following general elections in May 2016. The facility will have the capability of providing technical assistance and policy development support on emerging and priority economic issues identified through dialogue with the new Government (for example, land reform). A policy priority fund will also provide a vehicle to support aid activities identified in the *Australia-The Philippines Comprehensive Partnership – Plan of Action, Australia' Economic Diplomacy Strategy* and through our bilateral *Philippines-Australia Trade Investment and Industry Dialogue*.

5. Strengthening economic institutions - The facility will help targeted economic agencies improve their service delivery capabilities by addressing their human resource and organisational development needs. Economic agencies may not only be constrained by a lack of technical skills, but by the capacity and capabilities of the bureaucracy and its staff. Agencies may have difficulties in managing their budget, planning strategically, offering training programs, and hiring and retaining staff. Improving the human resource and organisational capabilities of the economic agencies that we work with will increase the sustainability of Australia's aid interventions. Human resource and organisational development support will be offered to all economic agencies that Australia partners with under areas 1 to 4 above. The facility will build on the achievements of HRODF, which independent evaluations have found to be effective and highly valued by Philippine government partners.

Political Economy - Some reform issues that the facility will address are politically sensitive. A political economy analysis will be incorporated in the design of each activity. Manila Post has a lead governance specialist who can guide/review the analysis. If warranted, the activity's implementation plan could include a partnership with the Coalitions for Change Program, to help form alliances between civil society, private sector, academia and government to advocate for economic reform and complement technical assistance provided by the facility.

Governance Committee - The facility's strategic direction will be overseen by a committee composed of: 1) DHOM Australian Embassy; 2) a senior officer from a trade/economic division in Canberra; 3) senior officers from the Philippine National Economic Development Agency and Department of Trade and Industry; and 4) a representative from the managing contractor. In addition, a private sector representative, a gender expert, and one or more senior economists/poverty reduction specialist(s) will advise the committee in their areas of expertise, and on improving facility coherency including opportunities for aid activities to better support each other. The Governance Committee will also be informed by technical committees (drawn from local think tanks, private sector and international experts) focused on key aid interventions including trade negotiation, NQI, economic reform, and inclusive growth. A key function of the governance committee is to approve a strategic framework and annual work plans that will be used as a basis to design and implement aid activities respectively.

The Committee will be responsible for ensuring facility coherence through activities that are mutually reinforcing. This facility seeks not only to help the Philippines achieve growth, but also to address the underlying economic policy issues that impact on poverty (e.g. lack of competition and quota restrictions on rice imports), create jobs for the poor and less-skilled (e.g. in agriculture, construction and manufacturing sectors) and improve the conditional cash transfer program.

**Budget** – The proposed budget that the facility will manage is expected to be \$80m over eight years. There will also be capacity for the facility to be scaled up if new energy work or aspects of our new infrastructure investment, currently in design, are determined to be best implemented from this facility.

**Monitoring and Evaluation** - An overarching evaluation framework for the facility will be drafted in the design phase and aligned with DFAT's *Development Policy and Performance Framework*, aggregate development results, and program logic for aid for trade, private sector development and social protection. A preliminary framework setting out the logic of the facility has been drafted and can be found in annex A. In keeping with the inclusive economic growth objective of the facility, key outcomes to be monitored are - reduced business costs (especially for SMEs); increased trade and investment; more jobs and increased incomes (especially for those below the poverty line); and economic growth. Each aid activity will have its own monitoring plan that is linked to the facility's overarching evaluation framework.

**Beneficiaries** - The direct beneficiaries of the facility are Philippine government departments. This includes the Bureau of International Trade Relations (on trade negotiation); Bureau of Philippine Standards (on NQI); Philippine Competition Commission and National Competitiveness Council (on competition policy) and Department of Social Welfare and Development (on social protection) amongst others. The ultimate beneficiaries of Australia's assistance include businesses including micro and small enterprises (NQI, competition policy); consumers (competition policy); and impoverished households (social protection).

**Gender** – Women's economic empowerment will be progressed through a two-pronged approach. The design of each activity will consider how women can be economically empowered (i.e. gender as a cross-cutting issue). Examples include building the capacity of female trade negotiators, helping women led-business meet international standards for improved trade, and increasing job outcomes for women through conditional cash transfers. In collaboration with IWI, this facility will also design a key activity whose principal objective is to economically empower women. This activity will be implemented under area 3 of the facility.

**Other Donors and Australia's Value Add** - There are three bilateral aid investments in the Philippines which are focussed on economic growth. They are USAID's Advancing Philippine Competitiveness Project (COMPETE) and Trade-Related Assistance for Development Project (TRADE), and the European Union's Trade-Related Technical Assistance Project (TRTA-3). The World Bank Group also provides assistance through its trade and competitiveness, and macroeconomics and fiscal management global practices. The scope of work that donors can provide to the Philippines on trade and economic growth is significant but no one agency can assist the Philippines in all its needs. A point of differentiation of Australia's facility will be our focus on inclusive growth and provision of flexible and tailored organisational capacity building in complement to our policy technical assistance. In addition, the facility's emphasis on women's economic empowerment will be a key distinction of Australia's value-add.

#### **D: Implementation/delivery approach (How and with whom?)**

A facility, implemented by a managing contractor and supported by a strategic framework and annual work plans will:

- provide strategic advice and analysis to Australia and the Philippines through the governance committee;
- draft and implement a strategic framework that outlines program principles and end of program outcomes;
- recommend and design, in collaboration with DFAT, aid activities under each of the five areas of engagement of the facility. Disburse funding to relevant implementing partners and manage activities as necessary;
- consider risks associated with each identified aid activity;
- develop annual work plans identifying interventions for endorsement by the governance committee;
- establish a feedback and review process to ensure that the facility has capacity for redesign and is responding to changes in context;
- have access to contractors who can provide organisational development, human resource capacity building, and public financial management support to Philippine government departments;
- ensure that all facility aid activities meet Australian aid program's compliance obligations, including those related to managing risk; work, health and safety; safeguards; and fraud. Investment guidelines will be drafted and activities screened prior to approval to ensure compliance obligations are met;
- set-up the facility governance committee and operate its secretariat;
- provide program management services including financial reporting and evaluation across the entire facility; and
- provide corporate services, including office set up, management of human resources, procurement, finance,

logistics/fleet management, audit and risk, information technology, and public diplomacy services.

A facility represents the best means of organising our trade and inclusive economic activities because:

- It enables us to put in place an overarching managerial framework, and develop and maintain policy coherence in which we can direct and adapt our economic partnership with the Philippines.
- It allows us to have flexible and responsive arrangements for programming, in which we can move quickly and adapt to changing circumstances (e.g. to better leverage the Philippine's reform agenda and adapt to changes in donors' priorities).
- It can contain a mix of longer-term programs (such as in aid for trade or social protection), exploratory ones (such as investment policy, where we can be innovative and see what works and adapt) and shorter interventions that meet particular needs or opportunities. It enables a mix of risks, rather than narrowing the focus on a particular sector or aid intervention.
- It allows iterative management by trial, experience and adjustment. And, when activities work, they are easily and quickly scalable. When activities fail they can be easily terminated.
- The facility will equip us with a set of tools which can be deployed according to the specific problems we tackle.
- Importantly, the facility consolidates a variety of agreements and activities into an efficient management structure, reducing our administrative and process burden, and maximising staff time for policy engagement. But, of course, it does require ongoing engagement and programming, in depth.

Manila Post's Economic Section will oversee implementation of the facility. Responsibility of staff at Manila Post includes: strategic oversight of activities, quality assurance, contact management, and leading policy dialogue with Philippine government officials. The facility will fall under the responsibility of the Economic Counsellor at Manila Post. To be considered in the facility's design is the recruitment of an international specialist (development economist) to provide Manila Post with ongoing policy and technical support, which will improve DFAT's ability to manage the facility.

#### **E: Risk assessment approach (What might go wrong?)**

Using DFAT's risk matrix, the facility is assessed as a low risk investment due to its technical assistance nature. Issues and mitigation measures highlighted by the risk assessment include:

- vested interests impede economic reform – to mitigate this, planning of facility activities will be informed by a political economy analysis and opportunities to engage the Coalitions for Change program (to form alliances between civil society, private sector, academia and government to advocate for reform) will be investigated.
- gender is treated as a peripheral issue – to mitigate this, activity designs and monitoring and evaluation frameworks will be informed by gender analysis/considerations. The facility will implement aid activities in which the principal objective is to empower women.
- shifts in Philippine government priorities – to manage this, we will ensure that the facility can adapt through its iterative annual plan process;
- fragmentation – the program will increase coherence by designing key aid interventions to complement smaller value activities;
- ensure Philippine government buy-in – DFAT will consult early with the Department of Trade and Industry (DTI) during the design phase and include DTI's representation in the steering committee; and
- ensure Post will be adequately staffed to administer the facility, manage contracts and lead the policy dialogue.

Activities will not directly involve work with children, displacement and resettlement of people, or detrimental impacts on the environment. As the facility will support several aid interventions, clear guidelines will be drafted and activities screened prior to approval to ensure that all of DFAT's safeguards requirements are met. Guidelines will also be drafted to ensure funds are protected from fraud and directed to their intended purposes.

## Safeguards Screening Checklist

	Yes	No	Not Sure
<b>Child protection</b>			
1.1 Did the outcome of the child protection risk context assessment indicate a full assessment is required?			X
1.2 Is the investment likely to involve contact with or access to children (0-18 years old) due to the nature of the activity or the working environment?		X	
1.3 Will the investment involve personnel working with children?		X	
<b>Displacement and resettlement</b>			
2.1 Does the investments involve construction on: exclusion from: or repurposing of land that is occupied, accessed to generate livelihoods or of cultural or traditional importance?		X	
2.2 Does the investment's success depend on other development activities that may involve construction on; exclusion from; or repurposing of land that is occupied, accessed to generate livelihoods; or of cultural or traditional importance?		X	
2.3 Does the investment involve planning for, advising on or designing the economic or physical displacement of people to make way for infrastructure development, disaster risk reduction or exclusion of the local population from land accessed to generate livelihoods?		X	
<b>Environment</b>			
3.1 Will the investment support any of the following: <ul style="list-style-type: none"> <li>• medium to large-scale infrastructure such as roads, bridges, railways, ports, infrastructure for energy generation; or</li> <li>• development of irrigation and drainage, diversion of water; or</li> <li>• land clearing, intensification of land use; or</li> <li>• hazardous materials and wastes; or</li> <li>• activity in mining, energy, forestry, fisheries, water supply, urban development, transport, tourism or manufacturing sectors?</li> </ul>		X	
3.2 Will the investment support any of the following: <ul style="list-style-type: none"> <li>• small to medium scale infrastructure such as localised water supply and/or sanitation infrastructure; irrigation and drainage; rural electrification, rural roads; or</li> <li>• construction/renovation/refurbishment/demolition of any building for example: schools, hospitals or public buildings; or</li> <li>• localised use of natural resources, including small-scale water diversion, agriculture, or other types of land-use change?</li> </ul>		X	
3.3 Will the investment contribute to, directly or indirectly, or facilitate, activities such as those listed above, including through: <ul style="list-style-type: none"> <li>• trust funds, procurement facilities; or</li> <li>• co-financing contributions; or</li> <li>• support for planning, change to regulatory frameworks, technical advice, training or;</li> <li>• applied research?</li> </ul>			X
3.4 Has an environmental review of the proposed investment already been, or will be completed by an implementing partner or donor?		X	
3.5 Does this investment need to meet any national environmental standards or requirements?		X	

Annex A - Preliminary Logic Framework

