

FINANCIAL ANALYSIS

A. Introduction

1. The Asian Development Bank (ADB) is preparing the Health System Enhancement to Address and Limit COVID-19 project (HEAL). This responds to the government's request for a dedicated loan in the amount of \$125 million, to fight the outbreak of the coronavirus disease (COVID-19) in the Philippines. The financial analysis was conducted for HEAL's proposed financing. It analyzed historical and projected expenditures to evaluate the impact of HEAL on the Department of Health (DOH) particularly on its overall expenditure and capacity to operate and maintain the project after completion. The financial analysis was prepared in accordance with the Technical Guidance Note of Financial Analysis and Evaluation by ADB issued in October 2019.¹

2. HEAL outputs will include: (i) provision of patient transport vehicles to deliver specimens to molecular laboratories; (ii) construction of two biosafety level 2 laboratories and upgrading equipment in one biosafety level 3 laboratory and nine other level 2 laboratories; (iii) renovation and/or new construction of negative pressure isolation wards and hazardous waste treatment facilities, and provision equipment in 12 hospitals; and (iv) provision of ventilators.

3. DOH will be the executing and the implementing agency. All assets generated from HEAL will be recorded in the books of DOH. The operations and maintenance (O&M) of the assets will be managed by hospitals, which are under the direct supervision and control of DOH. This financial analysis is based on the consolidated financial statement of DOH which includes the financial performance of its national office and all attached hospitals and agencies.

B. Methodology

4. HEAL has no revenue-earning component. The financial costs and benefits were therefore not analyzed and an incremental recurrent cost analysis was instead conducted. This approach assesses the ability of the asset owner or operator to meet its total recurrent costs including the incremental O&M expenditure of the ADB-supported project out of its revenue stream and/or budget allocation. Its purpose is to get reasonable comfort that the project will be properly maintained and will be in operation throughout its economic life. The analysis included: (i) a review of DOH's historical five years O&M expenditure, and budget allocation and utilization; and (ii) financial forecast for the next 8 years from 2021 to 2028 for the DOH to determine its financial strength to operate and meet its O&M expenditures from the project facilities.

C. Incremental Recurrent Cost Analysis

5. To establish the financial sustainability of HEAL, the following were analyzed: (i) previous years' recurrent O&M cost of DOH (Table 1);² and (ii) the future recurrent O&M costs of DOH and those specific to HEAL for the next 8 years (Table 2). The consumer price index inflation in the previous years stayed between 1% in 2015 to 2.6% in 2019.³ For future years, consumer price inflation (forecast) was assumed to be 2.2% in Year 2020;⁴ 2.4% in 2021; and 3% from 2022 onwards.

¹ ADB. 2019. [Financial Analysis and Evaluation: Technical Guidance Note](#). Manila.

² DOH. [DOH Budget](#).

³ Statista. [Philippines: Inflation rate from 1984 to 2024](#).

⁴ ADB. [Philippines and ADB](#).

6. **Sustainability analysis past 5 years:** Inadequate O&M of the network leads to progressive build-up of a maintenance backlog and could shorten the economic life of the network compared to the design life. The financial analysis indicates insufficient funds for O&M costs of project investments and activities for sub-national hospitals, facilities (medical and laboratory equipment), and continuing supply of health services. As shown in Table 1, DOH's budget allocation has decreased from ₱109.7 billion in 2018 to ₱102.7 billion in 2019, a dip of ₱6.9 billion. The unutilized budget from 2015 to 2019 was between 5% to 15%. The O&M shortfall of DOH between these years ranged from 16% to 48%. The historical O&M shortfall against the unconstrained O&M requirement from 2015–2017 was from 36% to 48%, although it has considerably reduced in 2018–2019 to 16%. DOH's trend in the last 5 years indicates continuous O&M shortfall in its unconstrained requirement and allocation. This has adversely affected the sustainability of its project facilities.

Table 1: Previous Years Fiscal Analysis of Operations and Maintenance Allocations (Php '000)

Indicator	2015	2016	2017	2018	2019
DOH unconstrained O&M requirement	107,096,008	109,709,250	148,829,619	122,302,545	112,573,057
DOH allocation	64,363,058	78,636,848	99,825,041	109,665,982	102,697,686
DOH utilization or execution	55,921,366	67,050,791	95,114,308	103,294,767	91,758,332
Unutilized budget	13%	15%	5%	6%	11%
DOH O&M shortfall (unconstrained requirement)	48%	39%	36%	16%	18%
Other information					
Increase in budget allocation		22%	27%	10%	(6%)
Annual inflation	1%	1%	3%	5%	2.6%

DOH = Department of Health, O&M = operations and maintenance.

Source: Department of Finance, Finance Department; and Statista. [Philippines: Inflation rate from 1984 to 2024](#).

7. **Sustainability analysis in 2020.** Table 1 shows that the historical execution shortfall against the unconstrained O&M requirement in the year 2019 was 18%. Table 2 shows that “with ADB project” in 2020, the unconstrained O&M requirement will increase by ₱14.4 billion but the budget allocation will be decreased by ₱3.9 billion. The execution shortfall will then increase from 18% to 28% in 2020. Although HEAL requires less than 1% of the unconstrained O&M requirement, allocation will be 5% lower, which will keep the shortfall at 28%. In 2020, available evidence indicates that if O&M of the project facilities is not fully funded and/or executed, HEAL may not likely be sustainable. A provision for recurrent expenditures was therefore included as part of the loan to ensure sufficient operations and maintenance during project implementation.

8. **Sustainability analysis from 2021 onwards.** From 2021 onwards, the unconstrained O&M requirement was based on the Universal Health Care program proposed by DOH. With this, there will be an annual increase of about 6–9% or ₱143.8 billion in 2022 to ₱256 billion in 2029. The budget allocation is also expected to increase alongside the O&M requirement. However, the budget shortfall will remain at 29% until 2028. As with the 2020 analysis, Table 2 suggests that O&M funding and/or execution of the project facilities can adversely affect the sustainability of HEAL.

9. Similar to most ministries in the Philippines, DOH depends on government funding through the Department of Budget and Management. The financial analysis shows that fiscal impacts are not within the government's projected revenue capacities in the last five years and the same increasing trend is seen in future projections for DOH. This puts the financial sustainability of

HEAL at risk. However, the hospitals' ability to cover O&M costs out of their respective revenues and/or request from the National Treasury will mitigate this risk. All DOH hospitals are earning service fees from their respective operations. In 2003, they were given fiscal autonomy which allows them to retain 100% of their income for the improvement of health facilities. They also receive additional budget for personnel services and O&M directly from the National Treasury. If there is a shortage of funds, DOH will provide the needed subsidy. The isolation buildings and equipment will be operated by the hospitals and they will be primarily responsible in ensuring the provision of O&M either from internally generated funds, allocation from the National Treasury, or subsidy from DOH.

10. The project cost and financing estimates include O&M of facilities. This will also be included in DOH's expenditure framework and budget request from the Department of Budget and Management and Congress. HEAL will strengthen DOH capacity to monitor budget allocations and utilization to help meet O&M recurrent costs of sub-national hospitals and facilities. The government has committed to provide the necessary recurrent funds following project completion to ensure the benefits of the investment are not lost. This commitment was also reflected in the loan agreement for HEAL, between the Borrower and ADB.

Table 2: Future Projections Fiscal Analysis of Operations and Maintenance Allocations (Php '000)

Indicator	2020	2021	2022	2023	2024	2025	2026	2027	2028
DOH Unconstrained O&M requirement	126,931,550	130,650,000	143,790,000	157,670,000	172,390,000	188,020,000	204,650,000	222,390,000	236,660,000
DOH Allocation	98,706,577	101,907,000	112,156,200	122,982,600	134,464,200	146,655,600	159,627,000	173,464,200	184,594,800
DOH Utilization or Execution	93,771,248	96,811,650	106,548,390	116,833,470	127,740,990	139,322,820	151,645,650	164,790,990	175,365,060
Percentage of Unutilized Budget	5%	5%	5%	5%	5%	5%	5%	5%	5%
Other information:									
Increase in budget		3%	10%	10%	9%	9%	9%	9%	6%
Annual inflation	2%	2%	3%	3%	3%	3%	3%	3%	3%
Inflation-linked increase in O&M requirement for existing network each Year (A)	2,476,607	3,046,357	3,919,500	4,313,700	4,730,100	5,171,700	5,640,600	6,139,500	6,671,700
Incremental requirement for ADB project each Year (B)	196,952	201,679	202,861	202,861	202,861	202,861	202,861	202,861	202,861
Total increase in O&M requirement	2,673,559	3,248,036	4,122,361	4,516,561	4,932,961	5,374,561	5,843,461	6,342,361	6,874,561
Total Shortfall - with ADB Project	35,833,861	37,086,386	41,363,971	45,353,091	49,581,971	54,071,741	58,847,811	63,941,371	68,169,501
Total Shortfall - with ADB Project	28%	28%	29%	29%	29%	29%	29%	29%	29%

DOH = Department of Health, O&M = operations and maintenance.
Source: Asian Development Bank.