

Amando M Tetangco, Jr: Continuity in a time of change

Speech by Mr Amando M Tetangco, Jr, Governor of the Central Bank of the Philippines, at the 12th Anniversary of the BSP, Manila, 4 July 2005.

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Introduction

MB Member Valdepeñas, MBM Boncan, MBM Amatong, MBM Villafuerte, Outgoing MBMs Mr. Alindogan and Mr. Salazar, our esteemed former Central Bank Governors, our friends from the banking community and the business sector, distinguished guests, my family, our friends from media, my co-workers in the BSP, M.O., SPC and our regional offices and branches, ladies and gentlemen, good afternoon.

Today we celebrate the twelfth year of the Bangko Sentral ng Pilipinas and I wish everyone a Happy Anniversary!

This celebration is particularly significant for us. Governor Buenaventura, MBMs Quintos, Salazar and Alindogan are closing six years of outstanding work in central banking today. We salute them for their very important contributions to the relentless pursuit of the goals and objectives of this institution. I have been fortunate to participate in and personally witness the major changes made to advance monetary policy making and banking supervision during their watch. They, together with the MBMs who are staying behind, are one of a kind, a bold bunch of policymakers who were alien to the fear factor in introducing innovations to make the financial system and the BSP as an institution attuned to the new standards and requirements of a fast changing world.

Governor Buenaventura cannot join us in today's celebration, but the BSP is so close to his heart that he sent his taped message, so that even in spirit we shall all be complete. As he finishes his term, he leaves a legacy that, while towering, is at the same time edifying and inspiring for us to continue the tradition of excellence and hard work in the BSP.

As we bid farewell to our outgoing MBMs, we also extend a warm welcome to our incoming Board members: Mrs. Amatong and Mrs. Villafuerte who are not new to the Monetary Board. We all look forward to working with them in the period ahead.

This afternoon, I would like to share with you my thoughts about the two main pillars of central banking: monetary policy and banking supervision. I will also identify the challenges faced by a modern central bank and what they mean to the BSP in terms of our organization.

Sustaining the shift in monetary policy regime

The first pillar of price stability represents our contract with the Filipino people. When consumer prices are stable, we serve the cause of economic growth. Today, the issue of inflation strikes even closer to the hearts, or perhaps the guts of the public. Surveys by independent research organizations have, for example, consistently ranked high prices as the foremost concern of the lower income classes. A low and stable inflation preserves the purchasing power of the people's incomes. There is more food on the table and more services to buy.

In my earlier interviews with the media, I have stressed one important point that will be the hallmark of my stewardship. We will not try to reinvent the wheel. Instead, we shall strive to continually improve it and keep it running more efficiently. Our vision is to see that it brings us to where we want to go.

We shall therefore continue to adhere to inflation targeting as our monetary framework. Inflation targeting emerged at that point where monetary targeting started to fade. Since the implementation of inflation targeting in January 2002, we have seen how rigorous economic

analysis, discipline in the conduct of monetary policy and greater transparency in the thinking of the monetary authorities have contributed to reduced gyrations in consumer prices. The dynamics of inflation expectations has been largely anchored in the market's appreciation of the BSP's explanation of the factors driving inflation and what the BSP intends to do to address them. This is the face of continuity.

But you will agree with me that perhaps there is scope for change. We shall soup up the inflation targeting framework. We will not only reassess the various components of our forecasting models and the integrity of our databases, but we will also intensify our capacity to anticipate possible shocks in the system. The first is to make sure we have the right tools to deal with shocks; the second will give us the comfort that we will not be ossified by surprises. We have completed our early warning systems for various areas like currency, business cycles and the banking system, and we shall increasingly make use of them in our monthly review of the monetary policy stance. The results of our periodic environmental scanning exercises will be used in an attempt to more effectively incorporate political factors in assessing the risks to the inflation outlook. We are also reviewing our monetary tools that include the reserve requirement, open market operations and credit policy. If we may add, finally, the market can expect greater transparency in the conduct of monetary policy and this should reduce the gray areas in anchoring public expectation about inflation and enhance the functioning of the markets.

Strengthening the financial system

In the financial sector, the main challenges emerged from the overhang of the Asian financial crisis and the greater integration of the Philippines into the global financial system. In response, we have addressed these challenges precisely by strengthening the financial sector. Focus has been given to maintaining a sound and viable banking system and the development of the domestic capital market.

Efforts in this area have begun to show positive results. Banks' balance sheets are gradually recovering from the large burden of bad loans while the local bond market has received the initial shot from the reforms that include the now operational fixed income exchange. We shall sustain the Bangko Sentral's reform strategy on cleaning up banks' balance sheets, addressing remaining weaknesses in managing risks, and ensuring that our prudential regulatory standards are elevated to international benchmarks. We shall also continue to coordinate with other government agencies and the private sector in installing the remaining infrastructural requirements of a well-functioning capital market that would diversify our sources of funds and reduce our vulnerability to various shocks.

But we need to enhance a few things even as we have started to launch them. We are moving into consolidated supervision and risk-based approach to bank examination that are aligned with international best practices. Such innovations are necessary to allow regulators to effectively manage challenges posed by conglomerate structures and cross-border issues. We are improving corporate governance and market discipline. A crucial element for effective oversight of the banking system is for the regulator to have stronger supervisory and regulatory authority and this can only be done with the support of Congress in amending the BSP Charter. Finally, we realize that the BSP can enhance its effectiveness by establishing teamwork with the other financial regulators. Thus was born the Financial Sector Forum (FSF) that has elevated the cooperation among the regulators to pioneering levels. The FSF will help harmonize supervisory and regulatory efforts, improve the exchange of information among regulators and promote better consumer protection.

In the area of promoting the domestic capital market, the changes we would like to see are the fruits of the steps that have already been started in close collaboration with the private sector. We shall be pleased to see more robust trading of government and subsequently, private, debt securities at the Fixed Income Exchange, improved market confidence from the use of independent custodians, migration by the banks from the common trust fund to unit

investment trust fund, and lower borrowing cost with the installation of a credit information bureau, currently being discussed by Congress. We are excited to see the day when we are able to reduce our reliance on foreign borrowing because the domestic capital market is efficient enough to provide the critical mass to fund sustained economic growth.

Promotion of microfinance and literacy program-the social dimension of BSP policy

We shall also intensify the social dimensions of BSP policy. Foremost in this is our advocacy for microfinance. This program is the most effective tool for democratizing the access of the public to a portion of the nation's wealth, for empowering the poor and the economically-challenged group of small entrepreneurs and for scoring a dent on poverty alleviation. We shall also pursue economic and financial literacy program to reach out to our consumers, investors, overseas Filipino workers and their beneficiaries to help expand their options of where to put their money and ensure their economic future.

BSP organization

My fellow workers at the BSP, central banks have often been described as the most powerful institution in the economic sphere: the monetary policy decisions made by the monetary authorities "can lift markets overnight, bring people out of unemployment, keep growth on track and hold inflation in check."¹ Yet what central banks can do is ostensibly limited by a host of factors notably increasing globalization. Globalization has integrated international capital markets and with this, deregulation and technological progress have rendered traditional control-based approaches virtually ineffective. As market forces drive globalization, it has also increased the propagation of shocks in the world economy.

What then is the challenge for us?

It is important for us at the Bangko Sentral ng Pilipinas to be able to row with the current and if necessary at some point, to row against it. What is imperative is that the BSP is appropriately structured and equipped. Our commitment to building a more effective central banking organization is captured by our new vision and mission statements and they should serve as our guide for the next steps. We owe a great deal to the work in the past to instituting best practices, enhancing the bank's corporate image, and strengthening corporate governance within the BSP itself.

I know that we can always count on you my fellow BSPers, for our committed and professional men and women have been the strength of our organization through the years. Moving forward, let us continue to give our best to this institution, which has always looked after our welfare. We see this in the better facilities, comprehensive adjustment in pay scale and expanded opportunities through improved training programs and scholarships. These are elements that we should review from time to time to ensure they remain adequate and appropriate. As a great inventor once said: "...if we did all the things we are capable of doing, we would literally astonish ourselves."²

¹ Meyer, Laurence H. (2002) "A Term at the Fed, An Insider's View," Harper Business.

² Thomas Alba Edison.

The way forward

The BSP story of the last six years is ending today with a considerable amount of success. We are moving into the story of the next six years, complete with the template of new ideas and bold reforms. If we are to chart the roadmap in a “T” account, we will see that along the way, there are pluses and minuses, opportunities and challenges. The success of the last six years is punctuated by some unfinished agenda that needs to be pursued to achieve continuity in a period where change is the only constant. I recall what that celebrated columnist of the New York Times once suggested: it looks like some central banks find themselves with much less ability to move the economy than anyone expected.³ The reason is that some of them somehow cultivated the mystique of their invincibility that now turns out to be a handicap. In our case, while we deliver bold strokes to the market, we shall not throw caution to the wind. We shall be fully accountable for our efforts to keep prices stable and the banking system sound, but we shall also continue to inform the markets as necessary about the boundaries of what we can do. With this, the nation can be assured the BSP shall keep its end of the contract.

Thank you and good afternoon.

³ Krugman, Paul (2003), “The Great Unravelling,” Allen Lane, -.72.