

Amando M Tetangco, Jr: Towards a shared vision for capital market reforms

Speech by Mr Amando M Tetangco, Jr, Governor of the Central Bank of the Philippines, at the Testimonial Luncheon of the AB Capital and Investment Corporation, Makati City, 1 March 2006.

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Distinguished directors, officers and staff of the AB Capital and Investment Corporation led by Chairman and Chief Executive Officer Ramon R. Del rosario, Jr.; President and Chief Operating Officer Francis M. Varela; former President Filomeno G. Francisco; ladies and gentlemen: Good afternoon!

Congratulations on your 25th year anniversary! It is indeed an honor for me to join all of you today as you celebrate this momentous occasion.

For more than two decades, AB Capital and Investment Corporation has positioned itself as a prominent player in the capital market industry. Specifically, you have carved your place in corporate finance, fixed-income securities dealership, stock brokerage and fund management. You also hold a creditable track record in equity and debt securities underwriting, having acted as issue manager and/or lead underwriter for several of the country's most prestigious and most successful debt and equity offerings. It's no wonder you have earned various local and international distinctions for your financial savvy backed by a solid financial standing, as well as for your significant contributions to capital market development.

I am positive that you owe much of this success to the competence and foresight of your leaders and the dedication and zeal of your workforce.

In the pursuit of your institutional aspirations, you also have significantly contributed to our shared goal of promoting stability and efficiency in the Philippine financial system for a sustainable economic growth. In return, let me take this opportunity to share with you our continuing reform initiatives which could be useful guideposts in fine-tuning your chosen path.

The economy at a glance

To put things in perspective, let me start with an overview of the economy.

In 2005, the economy proved its resilience and fundamental strength, despite the prevailing difficult macroeconomic conditions.

The country's economic performance is benefiting directly from improving fiscal discipline and sound monetary policies.

For 2006, we expect to keep the momentum going. We realize, of course, that sustaining economic growth over the long term would depend, to a large extent, on the resilience of the financial system which forms the backbone of the economy.

Thus, we are taking parallel actions on key fronts.

The promotion of a sound and stable financial system is the centerpiece of this agenda. Within this framework, the development of the Philippine capital market is being given high priority alongside the continuous reform of the banking system.

Capital market initiatives

Already underway is a series of reforms in the Philippine capital market intended to: create a sound market infrastructure, enhance transparency and market discipline mechanisms, promote greater investor protection, and strengthen the legal and regulatory framework.

Toward this end, the following are some of our key contributions:

Delivery of securities

In July 2003, the BSP issued regulations mandating the proper delivery of securities by dealer banks and non-banks to the investor. This is meant to promote transparency and discourage proliferation of manipulative practices.

Accreditation of third party custodians

The BSP subsequently issued regulations on the pre-qualification criteria for banks and NBFIs that will operate as securities custodians and defined the functions and responsibilities of each. It is important that we develop the custodian as an important agent in the capital market that can facilitate the lending and borrowing of securities.

Market infrastructures

The BSP also supported private sector-led initiatives to establish a fixed income exchange (fie) intended to improve the current market infrastructure. The fie centralizes trading of securities for enhanced transparency and efficient price discovery.

At present, transparent pricing has been achieved for the interdealer market, as quotations are available on a per security basis, and executions are at the best bid and offer. In the future, we hope to see efficient price discovery for the common investor in the public market phase, as price and trading data will be made available on a timely basis.

Expansion of the menu of financial products

The domestic capital market remains shallow and underdeveloped. In response, the BSP has issued various circulars diversifying the menu of financial products available in the capital market. Traded papers like unsecured subordinated debts (as tier 2 supplementary capital), long-term negotiable certificates of deposits or LTNCDs, documented repos, and securitization structures create market-oriented opportunities for banks and other players and deepen the capital market. Recently, we have issued circular 503, amending the guidelines on risk-based capital framework to include Hybrid Tier I instruments as part of qualifying capital. Hybrid capital instruments that have equity-like features enable them to absorb losses similar to common equity. However, these instruments must be perpetual and redeemable by the issuer subject to prior BSP approval.

Moreover, we have also started revitalizing the trust business to widen investor base with the gradual phase out of Common Trust Fund (CTF) for a better product called Unit Investment Trust Fund (UITF). Uitfs enhance the credibility of pooled funds to investors as the value of investments is mark-to-market, paving the way for long-term investment opportunities.

Credit rating agencies

We are encouraging the entry of more rating agencies. Rating agencies play an important role in guiding investors towards informed decision-making and in ensuring the proper disclosure of investment information. Accordingly, we have issued circulars which set the criteria for accreditation of domestic and international credit rating agencies. To date, the BSP has authorized one domestic credit rating agency to issue ratings for bank supervisory purposes. Likewise, we have recognized one internationally accepted credit rating agency with a representative office in the Philippines to undertake local or national credit ratings.

Legal and regulatory framework

We are also advocating the passage of key legislative measures that will spur the development of the capital market and strengthen the regulatory framework.

A key priority is the approval of the extension of the Special Purpose Vehicle (SPV) law for another two years to complete the cleanup of Non-Performing assets (NPAs) in the banking system and restore credit supply to the economy.

Following a succession of asset dispositions under SPV I, Bnks' NPL/NPA ratios declined to single-digit levels. As of end-December 2005, NPL/NPA ratio of the commercial banking system stood at 8.5 percent and 8.6 percent, respectively.¹

We will also continue to lobby for the enactment of the credit information system act that will establish a central credit information system for improved discipline in the credit process. Credit bureaus will be able to serve as a reliable source of information to allow lenders to accurately evaluate risks and select between creditworthy and poor-quality borrowers.

Another vital legislation is the Revised Investment Company Act (RICA) that will establish a comprehensive regulatory framework to enable investment companies to play a key role in capital formation. Moreover, this bill is aimed at protecting the interests of the investing public by preventing the misuse of customer funds.

Other legislative measures that we would like to see enacted in the near term are the Personal Equity Retirement Account (PERA), the Pre-Need Code and the Corporate Recovery Act.

With these reforms in various stages of implementation and others more that are in the pipeline, we can expect better prospects for the growth of the Philippine capital market.

Undoubtedly, the continuing support of all financial industry players will ensure for us greater success in this endeavor.

As a final note, I call on you to assist us in fostering an environment conducive to a vibrant domestic capital market. You are, undoubtedly, one of the major players in the capital market today. We will be relying on your experience in helping provide order and depth in the market.

Although the road ahead is considerably tough, I am confident that AB Capital - armed with vision, a strong resolve and with sound leadership at the helm - will be more than prepared to meet the challenge.

Let us all do our share in responding to the call for building a deep, dynamic and liquid capital market - a precondition for achieving sustainable economic growth.

Once again, happy anniversary and I wish you all more success in the years to come!

¹ Comparatively lower than the 12.7 percent NPL ratio and 11.4 percent NPA ratio as of end-December 2004.