

Amando M Tetangco, Jr: The BSP and the banking community – a partnership for a better year in 2007

Speech by Mr Amando M Tetangco, Jr, Governor of the Central Bank of the Philippines (Bangko Sentral ng Pilipinas), at the Annual Reception for the Banking Community, at the Central Bank of the Philippines, Manila, 16 January 2007.

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Distinguished members of the banking community, special guests, friends, ladies and gentlemen. On behalf of the Monetary Board, I welcome all of you to our Annual Reception for the Banking Community.

We at the Bangko Sentral ng Pilipinas always look forward to this yearly event because it gives us, central bankers, the opportunity to interact with you at the social level and - more importantly - because we have you as a captive audience as we deliver the banking sectors' report card for the past year, as well as our roadmap to the future.

To put these in perspective, I will review our economic performance in 2006, share our views on how the economy will perform in 2007, and what these imply for the monetary and banking policies of the Bangko Sentral ng Pilipinas.

Ladies and gentlemen. In plain language, 2006 was a good year for the economy. We saw GDP continue a pattern of broad-based expansion, with the services sector, to which banks belong, recording the strongest performance.

Fiscal reforms and government's prudent management of its resources continue to yield strong dividends, with revenue growth outpacing spending.

At the same time, monetary and banking policies generated positive results: slower inflation, declining interest rates, a stronger peso, and gross international reserves at an all-time high on the back of strong inflows from export receipts, OFW remittances, and foreign investments.

It is noteworthy that even with supply shocks from record-high domestic oil prices and the value-added tax reforms, we managed to grow the economy without fueling inflation.

It is equally noteworthy that in 2006, the consolidated assets of the Philippine banking sector reached a record high level, even as asset quality continued to improve with the implementation of the SPV Law. In fact, as of November 2006 and for the first time since the 1997 Asian crisis, the benchmark non-performing loan ratio of commercial banks dropped to less than seven per cent; similar trends are being observed in thrift and rural banks.

Let us therefore give the banking sector a well-deserved round of applause.

Moreover, the capital adequacy ratio of the banking system stands strong at about 16% in 2006, even as the banking system increased provisioning levels and made the transition to the demanding new international accounting standards.

I also wish to commend the banking sector for its growing support for microfinance, our special advocacy for alleviating poverty in our country. Latest data indicate that there are more than 200 banks providing microfinance services to 630,000 micro-borrowers with total loan portfolio of P3.7 billion. The average is P11,600 per borrower, more than double the 2006 figure of about P5,000 for each borrower. Let us thank these banks for their support through another round of applause!

Market reforms continued to take root in 2006 including the development of market infrastructure. Among others, we saw the full implementation of the third-party custodian system and the fixed income exchange. Another is the interconnection of the Bangko Sentral's real-time gross settlement system or Philippine Payments and Settlements System with the Philippine Dealing System and the Bureau of Treasury in line with the Delivery-versus-Payment settlement of government securities.

The BSP capped the year with the prepayment of \$1.4 billion in loans, including all its obligations to the International Monetary Fund (IMF). This ended 4 ½ decades of continuous borrowing from the Fund. This sends a clear signal to the international community that the structural reform process and macroeconomic prudence in the Philippines have firmly taken root and that Philippine authorities can

independently craft and pursue a credible and strong policy framework and reform program for sustaining the country's economic growth.

The year 2006 also saw the BSP implementing the following enhancements in our monetary and banking policies:

- Refinements in our inflation targeting framework to align it with practices in other inflation targeting countries.
- Streamlined access to our rediscounting facilities, one of our instruments for conducting monetary policy. In particular, we launched electronic rediscounting facility to ensure wider and faster delivery of credit to SMEs in the countryside.
- Continued alignment of domestic prudential standards with international benchmarks and best practices, particularly in upgrading the quality of corporate governance and disclosure as well as risk management.
- Issuance of guidelines on banks' internal credit rating systems, technology risk management, as well as market and liquidity risks management.
- The adoption of the prompt corrective action framework which provides a time bound setting to deal with problem banks.
- Adopted measures to improve access of SMEs to financing through lower reserve requirements and relaxed - but still prudent - regulations on bank branching, risk weights, single borrower's limit, connected lending and documentation.

Indeed, the continuing partnership between the BSP and the banking sector has produced very positive results in 2006.

Economic and monetary policy outlook

Moving forward, let me share with you our views on the likely economic prospects for 2007. With resilient personal consumption, strong exports performance and robust services and industry output, GDP growth is expected to rise to 5.7-6.5 percent for 2007. If our fiscal position continues to improve, we can look forward to stronger, more sustained long-term growth.

Inflation is seen to continue to slow down in 2007, with the government target of 4-5 percent likely to be achieved, in the absence of new shocks. Nevertheless, there are certain risks to inflation that need to be carefully monitored and assessed, including oil prices, possible impact of El Nino on agricultural output, wage adjustments, and possible liquidity expansion. The BSP will continue to keep a vigilant eye on these risks so that it could move pre-emptively against threats to price stability.

On the external front, dollar inflows from OFW remittances and foreign investments are expected to remain strong. This should continue to boost our external payments position and enable us to further build up our international reserves. These conditions, in turn, underpin our expectations of a strong peso in 2007. In fact, we are now reviewing foreign exchange regulations, with further liberalization as our goal.

Going forward, we will continue to support various legislative initiatives to foster the development of our financial markets, including the creation of a centralized credit information bureau system to improve the quality of financial information available to investors, enhance private sector access to credit, and minimize exposure to risks of financial intermediaries. We are hopeful that the bill will be approved by the Bicameral Committee and signed into law by the President as soon as possible.

The BSP will also continue to support additional legislative initiatives to hasten the development of the Philippine capital market, including the amendments to the BSP charter, Corporate Recovery Act, Revised Company Investment Act, and the Personal Equity Retirement Act.

In the banking sector, we expect further expansion of bank resources, improvement in banks asset quality through NPL disposal, and improved capitalization. We should also see a stronger banking system resulting from more mergers and acquisitions. This should make banks better financial intermediaries and risks managers.

Ladies and gentlemen. Improved macroeconomic conditions, accumulating banking reforms, and robust improvements in banks' profitability, set the stage for an even stronger performance of the Philippine banking system in 2007.

Finally, I wish to thank all the bank associations and all our partners in the retail and the business sector, including our media friends, for their support in making our joint program "Tulong Barya Para sa Eskwela" a resounding success! Clearly, the combined donations/savings of around P12.5 million which we generated sends a clear signal that coins are indeed valuable; that "ang barya, mahalaga." This should convince our schoolchildren to start saving up with their coins. Let us therefore give everyone who participated in "Barya Para sa Eskwela" a well-deserved round of applause. Salamat po sa inyo.

We look forward to your continuing support for the nationwide implementation of our economic and financial literacy program in cooperation with the Department of Education which should transform each child into regular savers.

Concluding remarks

Friends. 2006 was a good year for the economy and the banking sector. We are therefore primed for an even better and stronger performance in 2007.

While mindful of the challenges ahead, we at the Bangko Sentral ng Pilipinas are determined to move forward in partnership with the banking community.

And so, ladies and gentlemen, may I offer a toast to a strong and successful partnership between the Bangko Sentral ng Pilipinas and the banking sector. May we become a truly potent enabling force in moving the country forward and providing a better life for all Filipinos.

Cheers!!!

Thank you everyone and enjoy the rest of the evening.