

Amando M Tetangco, Jr: The growing significance of rural banking in the Philippines

Keynote address by Mr Amando M Tetangco, Jr, Governor of the Central Bank of the Philippines (Bangko Sentral ng Pilipinas), at the inaugural reception of RBAP Board of Directors and Officers, Manila, 8 July 2008.

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Secretary Arthur Yap, Mr. Tomas Gomez IV, board of directors and officers of the Rural Bankers Association of the Philippines (RBAP), our friends in rural banking, good evening.

I am delighted to have this opportunity to keynote the inauguration of the new directors and officers of the RBAP. It is, indeed, an auspicious new day for the rural banking industry. Seeing the new set of directors and officers at RBAP's helm, I am certain that you will provide the impetus needed for the rural banking sector to once again forge ahead.

Rural banks have an important and challenging role in our country's economic development. In the law that created rural banks, they were envisioned to be catalysts for comprehensive rural development, channels of equitable distribution of opportunities and wealth, and support for expanded productivity in rural communities. The end goal was to raise the quality of life for all, especially the underprivileged. This task of great magnitude is relevant today, as it was then. In fact, with the shifts in the economic landscape, the increasingly changing needs of the market, the advent of new technologies and channels, it may be said that the demand on rural banks today is even greater than it was then. Rural banks must commit to continuously upgrade their capacity, efficiency and sustainability. Rural banks must uphold good governance and management practices to ensure that they are sound and well managed. Finally, rural banks must be dynamic and progressive to keep in step with these changes and developments.

I am happy to note, that by all measures, the rural banking sector has geared up to face the challenges and to seize the economic opportunities they present. Year on year, rural banks are exhibiting robust asset growth and strong capital build-up. As of end 2007, the sector's total assets reached PhP 149.5 Billion, an 18% increase from the previous year. Total capital accounts have also shown double digit growth of 13.4% from PhP 18.4 Billion in 2006 to PhP 20.9 Billion in 2007. The Capital Adequacy Ratio (CAR) has remained above the minimum 10% required by the Bangko Sentral at 15.7%.

The business of rural banking has also continued to show viability and profitability. Net Income After tax (NIAT) increased by 20% from PhP 2.3 Billion in 2006 to PhP 2.8 Billion in 2007. Return on Assets and Equity also continue to increase.

Savings mobilization and lending activities have also been on an uptrend. Deposit liabilities in 2007 were at PhP 108.1 Billion, a 21.5% increase from the previous year. Similar double digit increases were seen in the sector's lending activities. Total loan portfolio of rural banks increased to PhP 93.3 Billion from only PhP 77.1 Billion in 2006. While lending activities expanded, the high quality of the portfolio was maintained. As of the 4th Quarter of 2007, the Non Performing Loans (NPL) Ratio was 9.67% which is an improvement from the 11.11% for the same period for the previous year.

Using these indicators, rural banks are faring equally or even better than its universal, commercial and thrift bank counterparts while remaining true to its core mission of serving the needs of the countryside. Rural banks alone cover around 80% of the total municipalities in the Philippines with nearly 730 banks and over 2,000 branches nationwide. The real value added of rural banks, however, does not lie solely on their broad geographical presence but

just as importantly on their deep understanding of the character, peculiarities and needs of the rural customers.

At the Bangko Sentral, we have no doubt that rural banks are the ideal partners in invigorating local economies. Toward this end, we are working assiduously to ascertain that abundant opportunities are available for rural banks to ensure their institutional viability, expand their businesses and more importantly improve their products and services.

The issuance of the revised branching guidelines last December 2005 (Circular 505) aimed to enhance competition in the banking system and maximize the delivery of financial services especially in underserved areas. The new guidelines enable existing banks to further increase the depth and breadth of their outreach and better serve more and more clients both in the rural and urban areas. The benefits of such policy to the rural banking sector are immediately evident. As of end 2007, number of rural and cooperative bank offices increased to 2,133 offices from 2,075 in the previous year. While the number of banks decreased by 12, the number of branches and other offices increased by 58 from end 2006 to end 2007. What we are seeing is a consolidation of the sector where we are seeing stronger rural banks confidently expanding their operating networks.

To complement the liberalized branching regime, the Bangko Sentral has provided further opportunities for rural banks to expand their outreach beyond the brick and mortar structure of their head offices and branches. In 2007, we issued Circular 563 which granted rural banks the authority to invest in ATM networks. As of end 2007, the number of rural banks with ATMs reached 83 from 73 units in 2006 and just five ATMs in 2005. In addition, rural banks may provide electronic banking services, particularly mobile phone banking. As a result, a number of rural banks have already ventured into electronic banking to beef up their delivery of financial services. As of end 2007, a total of 46 rural banks started offering e-banking services such as cash card and mobile banking. Again, this is a significant increase from no rural banks with electronic banking in 2005.

What I am happy to see is that rural banks are not just simply using these new virtual networks and branches, as they are now available to them. They are going the extra mile in finding ways that are practical, as they are innovative, to make these new channels more attuned to the needs of their rural clients. Some banks are using available technology to place ATMs in hard to reach areas that do not even have telephone lines. Other banks, through a partnership with RBAP-Microenterprise Access to Banking Services (MABS) and G-Cash, have taken mobile phone banking to another level. The participating rural banks are now using the electronic cash platform in delivering financial services like deposits, withdrawals and loan payments. Indeed, mobile phone banking has the unique opportunity to reach a wider spectra of clients and tap those who are traditionally marginalized and “unbanked” – the lower income segments of the population. The successful experience, thus far, of the rural banks, mobile phone companies and the BSP have caught the attention of the international community who are lauding our efforts in using technology to increase access to finance. The BSP will continue to keenly monitor and support these innovations with a dynamic regulatory environment.

The Bangko Sentral is also expanding the products and services that rural banks can competitively provide. In 2006, through Circular 522, the BSP granted rural banks the authority to operate FCDUs. Rural banks have a distinct advantage to compete in the remittance business at the final mile by virtue of their close contact with countryside customers.

In addition, recent product approvals of the BSP such as the Micro-Agri Product and the Housing Microfinance Product provide rural banks with opportunities to expand the range of services they can provide to their clients. In particular, rural banks with microfinance operations are now provided with the opportunity to complement their present microfinance operations by offering these new products, to further diversify portfolios and reduce the risk of business loans being applied to agriculture or housing. Further, by recognizing the

microfinance component of these loans, they will now enjoy the same benefits of microfinance such as no collateral requirements or the acceptance of collateral substitutes, cash flow and character based lending, small and frequent amortizations as well as simple documentary requirements.

In the last two years, qualified rural banks were further granted the authority to engage in a wider range of activities. Through Circular 583, issued in 2007, rural banks may engage in limited trust activities. Just this year, rural banks have been allowed to participate in selected derivative activities. With the revised rules governing derivative activities of banks under Circular 594, rural banks that want to transact as end-user may apply for a Type 3 or Limited User Authority. Meanwhile, those rural banks that wish to facilitate derivative transactions of customers may apply for a Type 4 or Special Broker Authority.

Just two weeks ago, the Monetary Board approved the abolition of some fees charged for the participation in the Philippine Payments and Settlements System (PhilPaSS). The abolition of the annual license fee collected from the non-SWIFT members banks for the use of the Philippine Payment System – Front End System (PPS-FES) and the monthly access fee for the third party systems providers will allow free and open participation in PhilPaSS, by rural banks. By inter-connecting, rural banks may more readily participate in clearing with the Philippine Clearing House Corporation (PCHC), managing its government securities investments, participating in the exchange market, as well as participating in ATM networks and in the interbank market. Rural banks will also be able to instruct their depository bank to augment their demand deposit accounts (DDA) maintained in the BSP through PhilPaSS. Truly the potential for rural banks to be mainstreamed in the country's payment system is being realized.

Our policy stance is a clear indication that we consider rural banks to be ready, effective and important channels for economic development. We also recognize the crucial role that rural banks play in building a truly inclusive financial system. A system where there is not just universal access to financial services, but one where financial institutions provide responsive and competitively priced products and services to all, including those who were previously unbanked. Access to such services can invigorate local economies and improve the overall quality of life. This cuts to the heart of why rural banks were established. It is indeed a gargantuan task. But with an enabling policy and regulatory environment, strong rural banking fundamentals, and a new and vibrant RBAP board of directors and officers, I am confident that it can be achieved.

Good evening and more power!