

## **Amando M Tetangco, Jr: Turning challenges into opportunities – the key to sustainable growth**

Speech by Mr Amando M Tetangco, Jr, Governor of the Central Bank of the Philippines (Bangko Sentral ng Pilipinas), at the BAIPHIL's Induction of Officers, Directors and Committee Chairpersons and the General Membership Meeting, Makati, 15 July 2008.

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Distinguished officers and members of BAIPHIL (led by outgoing President Dolly Yuvienco and incoming President Lydia King), fellow bankers, co-workers in the BSP, special guests, good afternoon!

I am pleased to join BAIPHIL today on the induction of its new set of officers. I do welcome the opportunity to meet BAIPHIL's officers and members, as you count among the partners of the Bangko Sentral ng Pilipinas in our continuing pursuit of reforms for a strong and vibrant banking system.

In addition, BAIPHIL has emerged as one of the Bangko Sentral's consistent partners in corporate social responsibility projects that directly benefit our marginalized sector.

Among others, I remember that BAIPHIL organized other financial industry associations in providing financial support, as well as sweat equity, for the BSP-St. Paul GK Village in Paranaque City. You will be happy to know therefore that over the weekend, we turned over 16 GK units to new homeowners in our Paranaque GK village. For this, ladies and gentlemen of the BAIPHIL, you all deserve a long round of applause! Salamat sa inyong tulong.

To the newly inducted officers, directors and committee chairpersons, I offer my congratulations! We at the Bangko Sentral ng Pilipinas look forward to working with you as our banking sector deals with domestic and global challenges.

In my previous meetings with members of the financial community early this year, I discussed the outlook for the economy and the banking sector in 2008. I remember having said that the Philippine economy is headed for a more challenging environment – one that is fraught with headwinds. Indeed, our economy has to contend with “rough patches” emanating primarily from the turbulence in global financial markets, the slowdown in the US and other economies, and the unprecedented rise in global food and energy prices.

While we continue to see challenges and risks arising from adverse global developments, we remain optimistic and confident that we can ride out this turbulence and sustain the economic gains achieved in recent years. Why do I say this? Well, because we do our homework; together, we have built up domestic buffers that should continue to help us withstand headwinds which are mainly external in origin.

Let me cite some of these buffers and how exactly these have insulated the economy from external risks.

First, we have fortified our domestic financial system. In terms of resources, for instance, the Philippine banking system's asset base has grown steadily from P3.4 trillion in 2001 to P5.1 trillion as of the first quarter of 2008 on the back of sustained increases in deposits and capitalization. This is equivalent to a 50% increase.

In addition, overall asset quality of Philippine banks has made a dramatic turnaround, with the NPL ratio dropping from 16.9 percent in 2001 to 5 per cent as of March 2008.

Meanwhile, banks' capital adequacy ratio on both solo and consolidated bases remained well above the regulatory minimum of 10 percent and the international benchmark of 8 percent.

We also have in recent years put in place structural reforms in the banking system, such as the adoption of international accounting standards and the enforcement of stricter corporate

governance standards, which have made it more resilient and able to withstand volatilities in financial markets.

Ladies and gentlemen, all these indicators point to a fundamentally sound banking system.

Yet another strong buffer we have going for us is the country's favorable external position.

Among others, our first quarter 2008 balance of payments yielded a surplus of US\$1.7 billion. This is 20.8 percent higher than our surplus in the same period last year, as both the current and the capital and financial accounts continued to post surpluses. While the merchandise trade deficit widened due to higher oil and food costs, the current account was in surplus of about 3 percent of GDP mainly as remittances sustained their expansion. Based on the latest figures, in May this year, remittances amounted to \$1.4 billion or a 15.6 percent increase year-on-year. Total remittances for the first five months of 2008 reached \$6.8 billion or 14.7 percent up from the same period last year.

As a result of the BoP surplus, the country's gross international reserves (GIR) continued to reach peak levels, hitting a new record high of US\$36.7 billion in June this year. At this level, our GIR can cover 6 months of imports of goods and payments of services, way above the global standard.

Similarly, the country's major external debt ratios have been improving, an indication of the country's enhanced capacity to service its maturing foreign obligations.

These positive indicators make us confident about the prospects for our economy in general and our banking sector in particular. Moreso, if we are to continue our efforts to strengthen the banking sector and our economy.

It is in this context that I find BAIPHIL's theme for this occasion as a most appropriate rallying point: "Turning challenges into opportunities."

I believe we are in a position to continue to fortify our buffers by remaining proactive in our response and deeply committed to pursue our reform agenda.

In this connection, our key policy thrusts at the Bangko Sentral ng Pilipinas are as follows:

First, our monetary policy will continue to focus on our core mandate of maintaining stable prices. We will keep our eye on the inflation ball, being mindful that as we do this, we are able to foster an environment conducive to sustained economic growth.

In recent months, we have seen inflation moving up steadily on account of record high oil and food prices, hitting 11.4% in June this year, the highest in more than 14 years. This brought the year-to-date average inflation to 7.6 percent. Although this is still consistent with the BSP's view of a hump-shaped path for inflation in 2008 and 2009, we cannot afford to underestimate this old adversary of central banks. Inflation is at the very top of the BSP's policy priorities. We will continue to intensify environmental scanning and surveillance of key macroeconomic developments to ensure that our assessments of the inflation outlook and the risks to inflation remain fresh. The Monetary Board will take the necessary and decisive action to address the threat of high inflation.

Second, on the external sector, our policies will be geared toward ensuring the sustainability of the country's external debt and maintaining a comfortable level of reserves. In recent months, we have witnessed a depreciation in the peso's value. This has not been unexpected, given the significant upmove last year and the changing environment we operate in this year. We believe that the current exchange rate levels reflect a healthy correction in the market, and market players should take advantage of this. As we expect to still have a surplus in the balance of payments for the year, the peso should be supported, particularly in the last quarter of this year when remittances are traditionally strong.

Third, reforms in the financial sector will continue to be directed toward maintaining a strong banking system and a robust domestic capital market. Specifically, we will focus on: further enhancing the regulatory framework through the implementation of the BASEL II roadmap;

improving corporate governance by promoting compliance with international accounting and financial reporting standards; accelerating the implementation of risk-based supervision technology; and continuing support for the development of a deep and efficient capital market, including support for necessary legislative reforms.

Moving on, another priority for the BSP is our continuing efforts to broaden access to credit of micro, small and medium enterprises or what we call MSMEs. BSP's recent reform initiatives toward this end include liberalized branching; expansion of foreign currency deposit unit (FCDU) and trust licenses to include qualified rural banks; the re-opening of quasi-banking license; and the introduction of the breakthrough housing microfinance product.

We will also continue to work on a sound market infrastructure that will promote secure and timely completion of transactions, thereby minimizing systemic risk and enhancing the integrity of financial transactions. This is being implemented through the promotion of progressive policies on e-commerce and payments system innovation.

Summing up, the critical task ahead of us is to preserve the momentum for economic reforms. This way, we can be assured of the economy's sustained growth in the long run.

As in the past, we will continue to rely on BAIPHIL's steadfast support in terms of providing training assistance to bank professionals to ensure that they are better skilled and equipped to handle the demands of a sophisticated and competitive financial arena.

Ladies and gentlemen, equal measures of challenges and opportunities abound in the banking sector. I am confident that with your newly-elected officers and directors, BAIPHIL is in a strong position to take on the challenges upfront and turn these into opportunities that will benefit your respective banks and the economy as a whole.

Together, we can pursue a higher growth path for the economy, even in the face of formidable challenges.

Again, my congratulations to BAIPHIL and its new set of officers led by its President Lydia King

Mabuhay ang BAIPHIL! Mabuhay ang ating mahal na bansang Pilipinas! Maraming salamat sa inyong lahat.