Amando M Tetangco, Jr: Continuing growth amidst recurrent risks and uncertainty

Speech by Mr Amando M Tetangco, Jr, Governor of Bangko Sentral ng Pilipinas (BSP, the central bank of the Philippines), at the Joint Meeting of the Rotary Club of Manila and the Rotary Club of Makati-Forbes Park, Manila, 9 January 2014.

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Rotary Club of Manila (RCM) President Rudy Bediones, Rotary Club of Forbes Park (RCFP) President Ruben Torres, other officers and members of RCM and RCFP, ladies and gentlemen, good afternoon.

Thank you for the invitation to be part of the Joint Meeting of the Rotary Club of Manila and the Rotary Club of Forbes Park. It's always a privilege to be included in your New Year tradition and your celebration of the Rotary Awareness Month, which I understand is commemorated in all Rotary Clubs across the globe.

Today isn't really the first Thursday of the year, which is when you normally invite me to speak. But January 2 would have been too close to New Year's day, and most of you would still have been in the holiday mood. Today, I think everyone is on rev mode and ready to tackle the challenges of 2014.

Quite a few things happened in 2013 that have elevated the potential challenges of 2014. Of these, the one most felt by the country is the trilogy of natural and man-made events – the earthquake in Bohol and Cebu, the armed conflict in Zamboanga and from Yolanda – which we experienced in the second half of 2013.

While these three events literally changed the landscape of the country, I think these events also, in the process, showed the best in the Filipino – our resilience and how we are at our very best when we work together.

In this spirit of working together, the BSP also did its part to help ease the impact of Yolanda by putting in place regulatory relief for banks in the affected areas, so they could extend the same to their customers. Among others, the temporary relief measures include the following:

For all banks

- Allowing banks to provide financial assistance to their officers and employees who were affected by the calamity including those types of assistance that may not be within the scope of the existing BSP-approved Fringe Benefits Program.

For thrift banks/rural banks/cooperative banks:

- Excluding existing loans of borrowers in affected areas from the computation of past due ratios provided these are restructured or given relief; and
- Reducing the 5-percent general loan-loss provision to 1 percent for restructured loans of borrowers in the affected areas.

For all rediscounting banks

- Granting of a 60-day grace period to settle the outstanding rediscounting obligations as of 8 November 2013 with the BSP of all rediscounting banks in the affected areas; and
- Allowing banks to restructure with the BSP, on a case-to-case basis, the outstanding rediscounted loans of borrowers affected by the calamity.

For quite a few other reasons, besides the calamities, 2013 has been described as a year of challenges, due to:

1. Failing to reach a consensus on a fiscal legislation, the US government shut down for several days.
2. Eurozone recovery remained weak and uneven across the member-countries.
3. China had to deal with growing shadow banking and rapid credit growth.
4. Market anticipation of the Fed's policies added uncertainty in the financial markets and led to greater volatility of capital flows.

Nonetheless, the Philippine economy was able to ride out turbulence in the global financial markets due to significant sources of strength. Notwithstanding the slowdown in global economic growth, the Philippine economy continued to have vibrant growth. For the first three quarters, GDP increased by 7.4 percent, higher than the 6.7 percent in the same period in 2012. Growth was boosted by the strong performance of services, manufacturing and construction. On the expenditure side growth came mainly from consumer and public spending buttressed by increased investments in Fixed Capital; exports contributed in the third quarter.

This was supported by a benign inflation environment. The full-year 2013 average inflation rate of 3.0 percent was at the low end of the Government's inflation target range of 3–5 percent for 2013. This is the fifth consecutive year that the country has been able to keep inflation within the Government's target inflation range.

Moreover, the Philippines has substantial cushions to ride out potential turbulence in the global financial markets:

- Our gross international reserves reached US$83.7 billion as of end-December 2013.
  - can adequately cover 12.1 months' worth of imports of goods and payments of services and income
  - equivalent to 8.4 times the country's short-term external debt based on original maturity and 5.8 times based on residual maturity
- We enjoy a current account surplus owing to structural sources – BOP position yielded a surplus of US$4.7 billion for January-November 2013. The current account surplus was mainly on account of increased net receipts of primary and secondary income and in other services accounts.
- Our banking system is stable and strong with capital adequacy ratios well above international standards. As of end-June 2013, the capital adequacy ratio (CAR) of UK/Bs stood at 18 percent on solo and 19.3 percent on consolidated bases.
- External debt dynamics are favorable – external debt-to-GDP ratio decreased to 21.9 percent in the third quarter (2013) from 25.6 percent in September 2012 and 24.1 in December 2012. Moreover, more than four-fifths of our external debt has medium- to long-term maturities.[1]

The Philippines' strong economic performance has been validated internationally.

1) Credit Rating Upgrades. The year 2013 saw the Philippines achieve investment grade credit rating – not just from one, but from all the three major credit rating agencies. These rating agencies have cited the disciplined fiscal management with the declining reliance on foreign currency debt, strong external position, and low and stable inflation levels as bases for the score. In a recent report, Moody's maintained its positive outlook on the Philippine banking system. In fact, in that report, Moody's stated that the Philippines' banking sector is the only one in the Asia-Pacific region which they have given a "positive" outlook.

[1] Average Maturity: Public Sector: 20.1 years Private Sector: 9.8.

2) The IMF. An IMF mission report in September 2013 cited that the country's strong fundamentals would enable it to deal with any capital outflows when the U.S. Federal Reserve cuts its stimulus program.

3) Doing Business 2014. In the latest World Bank and International Finance Corporation report (October 2013), the Philippines was ranked among the top 10 countries that made the biggest improvement in business regulation. The report took note of the government's regulatory reforms in three areas: introduction of a fully operational online tax filing and payment system, simplified occupancy clearances for construction, and new regulations that guarantee borrowers' right to access credit information.

While most of the sources of risks have dissipated, in particular with clearer forward guidance from the US Federal Reserve (Fed), resolution efforts in Eurozone gaining broad agreement, and accommodative policies in Japan bearing fruit, risks still remain.

First, due to these lingering concerns, global economic growth remains subdued. As a whole, the world economy is projected to have higher growth in 2014 but as the IMF puts it, global growth is "in low gear." Of course, just yesterday, the IMF said it would raise its economic growth forecast.

- According to the IMF's World Economic Report of October 2013, advanced economies are showing signs of gradual, but steady, growth.
- Although emerging market economies, particularly those in Asia, continue to do better than advanced economies, China is seen to have slowing growth. In addition, ASEAN-5 countries' projected growth rates, while projected to be higher for 2014 than in 2013, these rates are still lower than those registered in 2012.[2]

Second, market reaction to the Fed's actions. The Fed has consistently pointed out that their decisions on these matters will be dependent on incoming data, particularly US employment data. The Federal Reserve has announced a reduction of its monthly bond purchases to US$75 billion from US$ 85 billion as the start of its exit from the stimulus measures, beginning January this year. Accompanying the reduction is the Fed's commitment to maintain accommodative policy. The withdrawal of the stimulus (including QE tapering) could impact on global markets in a number of ways:

- On one hand, policy normalization in the US could mean that the major driver of the global economy – and trade partner to many EMEs – is indeed seeing growth renewal, which would in turn be positive for EMEs, including the Philippines.
- On the other hand, as markets expect interest normalization, this could lead to global portfolio rebalancing. Should this happen, a weakening of capital flows to or even a pull-out of capital from emerging markets could ensue.
- And, the financial stability implications of global funds movements could prove stressful for less resilient economies – those with weak external positions and those with less developed financial systems. For the Philippines, the Fed taper may lead to greater volatility in domestic financial markets. But given sound fundamentals, we expect the price movements to be broadly manageable.

Across the other part of the globe, efforts to improve Europe's debt position as well as the discussion towards completing the EU banking union continue. The full banking union reform deal includes a single supervisory mechanism, a single resolution mechanism and common deposit insurance. The single supervisor has been approved by the EU Parliament, and the ECB will perform this role. The single resolution mechanism has received broad agreement

[2] Emerging Asia includes China, India, and the ASEAN-5 countries (Indonesia, Malaysia, the Philippines, Thailand, and Viet Nam).

at the finance and EU leaders level, but this is still for ratification in the EU Parliament in May. Market volatility may heighten as markets carefully watch how the issues will be resolved.

In the face of these risks, the BSP has a menu of options that could be deployed:

- We have standing facilities to ensure adequate domestic liquidity for banks should funding sources dry up.
- We would maintain a strategic presence in the FX market, while keeping the value of the exchange rate essentially market-determined.
- We could implement targeted macroprudential measures.
- In addition:
  1. Timely and clear communication with market players would quell anxieties.
  2. The careful and regular surveillance of risks would allow for prompt and appropriate responses.
  3. In the event of liquidity problems, there are regional financial arrangements that the Philippines can use.

In light of all these, the outlook on Philippine growth and inflation remains favorable.

- The economy is expected to grow between 6.5 to 7.5 percent in 2014, despite the chain of untoward incidents. Recovery and rehabilitation efforts are expected to bolster growth. For the medium-term, growth would be supported by stronger performance from the construction, manufacturing, business process outsourcing and private services. The country's attainment of investment grade status may attract foreign direct investments that would in turn generate jobs.
- Inflation is expected to remain within the target range over the policy horizon.
- In 2014, inflation is seen to be slightly higher than the mid-point of the target range of 3–5 percent, due mainly to higher food prices and possible increases in utility rates but comfortably within the target range.

Moving forward, the BSP will remain committed to staying the course toward sustained growth, while firmly adhering to its mandate of safeguarding price stability and ensuring the financial system remains resilient.

- On monetary policy, we will ensure that liquidity remains adequate to support economic growth with manageable inflation.
- On financial sector policy, the BSP commits to maintain the stability of the financial system by continuing to craft banking regulations that are responsive, consistent with best practice and in line with the international market reform agenda.
- On the external front, the BSP remains supportive of policies that will help cushion the economy from external shocks. We will continue to maintain a market-determined exchange rate and a comfortable level of reserves. The BSP will also continue to promote external debt sustainability by keeping the country's outstanding external debt manageable and within the economy's capacity to service its debt in an orderly manner.

We will continue to monitor developments to keep ahead of emerging risks.

Before I conclude, I would like to spend a couple of minutes on an advocacy of the BSP that we believe helps to translate the positive macroeconomic developments into the overarching goal of inclusive growth. Here, I refer to efforts towards financial inclusion that are within the area of the BSP. This advocacy is of particular importance now, in light of recent calamities, as these calamities have resulted in a number of families losing their savings and needing vital access to financial services to rebuild their lives.

The BSP financial inclusion framework is built on three areas:

1. broad access to appropriate credit at reasonable rates through responsible and proportionate regulation that encourages market innovation,
2. timely and relevant economic and financial learning, and
3. well-founded financial consumer protection.

How have we impacted the macroeconomy? Let me cite some examples:

First, financial access. Our policies on simplified or scaled down branches called microbanking offices (MBOs) have enabled banks to have a presence in areas that were previously unbanked. There are now 50 municipalities from 37 in 2011, an increase of 35 pct, that are served by MBOs alone.

We have also continued to leverage off mobile technology by enabling alternative financial service providers (FSPs) as effective touch points to banking services. FSPs, including pawnshops, remittance and e-money agents, which tend to be available even in areas with small population and have high incidence of poverty, now total over 46,200 from about 38,400 in 2011, or a growth rate of 20pct.

If we consider only banks (including MBOs), thirty-seven pct of municipalities would be without such presence. But if we now include FSPs, only 13.2 pct of municipalities would not have any form of access to financial services.

Second, financial education. Since we revitalized this program in 2008 we have conducted numerous domestic and international roadshows and financial expos. Our international roadshows have targeted cities where most of our OFWs are deployed, including those in Asia, Europe and the United States.

We have a number of advocacy programs, including the Credit Surety Fund, the savings programs for the youth, i.e., Kiddie Savings Program, Bamboo to Bangko, Tulong Barya Para sa Eskwela, among others. This year, we plan to leverage on this strength to reach out to more sectors and regions across the country.

Finally, financial consumer protection. We have strengthened our financial consumer protection efforts by creating a consumer redress mechanism within the BSP. We are also in the final stages of completing a consumer protection framework that will formally rate the CP efforts of banks, and provide specific guidance on how banks can scale their efforts up.

We are strong advocates of financial inclusion because in this way, we are able to empower our citizens, and therewith make them more effective partners in nation-building.

Concluding remarks

As I mentioned at the beginning of my remarks, the recent natural calamities once again proved the Filipino is resilient thru the Bayanihan spirit which we saw work so excellently during our natural calamities. I know Rotarians know this very well… for you follow your motto is “service above self.”

The painting by national artist Botong Francisco illustrates this point quite exquisitely. As we appreciate this masterpiece, we also appreciate each stroke of the brush that was skillfully made… how deliberate Botong was in building one brush stroke over the other to bring to life what he had imagined in his mind to do.

Think about what we have done in 2013… And then imagine, what more we can do in 2014, if we continue to work together with the same purpose and goal.

The BSP, national and local governments, and you, the private sector – we are all called to step forward and do our share in the rebuilding, not merely houses or even communities, but precious lives of our people.

I salute you, ladies and gentlemen of the Rotary Club of Manila and the Rotary Club of Forbes Park, for your service to the Filipino people.

May your productive work continue this and the coming years. Thank you very much.