

## **Amando M Tetangco, Jr: Rural banks – making a difference in financial inclusion**

Speech by Mr Amando M Tetangco, Jr, Governor of Bangko Sentral ng Pilipinas (BSP, the central bank of the Philippines), at the 63rd Annual National Convention and General Membership Meeting of the Rural Bankers Association of the Philippines (RBAP), Manila, 23 May 2016.

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Thank you for inviting me to this annual gational gathering of RBAP. The theme you have chosen for this year: “Rural Banks: Making a Difference in Financial Inclusion” speaks well of your important role in increasing access to financial services, a role which you have been performing even before the term financial inclusion itself gained attention.

### **Rural banks and the changing environment**

Let us briefly go back in history. The very reason for the creation of rural banks in 1952 when Republic Act 720 was enacted – was for them to be the key local financial institutions providing credit to farmers and people of rural communities, thereby promoting and expanding the rural economy in an orderly and effective manner. This was the original raison d’etre for the establishment of rural banks.

After six decades, there have been significant shifts in the financial system landscape. There are now many other financial service providers – banks and non-banks, formal and informal – that are already in or are planning to enter your space. The demands of your market and the conditions in which you operate have also evolved. Simply put, the operating environment now is very much different from before.

Change is inevitable. What matters is how we respond to change. Charles Darwin, who is best known for his theory of evolution, said and I quote “It is not the strongest or the most intelligent who will survive but those who can best manage change.” Indeed, adaptability or the ability to change to fit new circumstances is crucial to survival. Without the ability and agility to adapt, we will stagnate or lose our relevance.

In other countries, community banks are also struggling to find their rightful spot in a rapidly evolving environment, especially because of tough competition with other market players. But I believe that small banks can still thrive in this changing environment and remain relevant. Today, let me highlight two key existing factors that you can capitalize on to adapt to change: one is your current reach and immersion in the countryside, and the other one is the current enabling regulatory environment.

### **Reach and immersion in the countryside**

BSP data as of December 2015 show that there are 524 rural banks with a network of 2,086 branches and other offices. Rural banks are present in 59% of the country’s 1,634 cities and municipalities, which is more than double the reach of universal and commercial banks (23%) and thrift banks (28%). While bigger banks are concentrating in highly urbanized and densely populated regions such as NCR, CALABARZON and Central Luzon, rural banks are thriving in regions where there is less access to financial services. For instance, Cordillera, Cagayan Valley, MIMAROPA, and Caraga are among the regions where there are more rural banks than other bank types.

Noteworthy to mention is that rural banks are the frontrunners in the establishment of micro-banking offices (MBOs), which enable banks to set up presence in areas where it is not economically feasible to establish a full blown branch. Out of 540 operating MBOs, 78% are owned by rural banks. These MBOs are present in 338 municipalities, of which

66 municipalities are served by MBOs alone. Looking at previously unbanked municipalities which gained banking presence, most of them are now enjoying banking services because of MBOs.

The numbers that I have presented just show that rural banks are truly more accessible in the countryside. You are still in areas where other players are not. Take advantage of this position to strengthen your foothold so that you will be more resilient when competitors come.

While you already have a wide presence, there are also still untapped opportunities in terms of unbanked municipalities whose level of economic activity is not necessarily low. For instance, 15% of unbanked areas are 1st to 2nd class municipalities. These areas will surely benefit from financial intermediation to sustain local economic growth and boost consumption and productivity.

Admittedly though, some of you may be already satisfied with the current market that you are serving. If geographical expansion is not part of your game plan, you can always improve your products and services in terms of design and delivery.

As rural banks, what sets you apart from bigger banks is that you are more relationships driven. You have an intimate knowledge of the local economy and close ties with the community. Use this to be more responsive to the needs of customers as well as to market trends.

You can also introduce improvements in your operations. According to our National Baseline Survey on Financial Inclusion, more than 50% of adults who have transacted with banks are just “somewhat satisfied” with their transactions. The average waiting time before being served in a bank is 33 minutes which is twice the waiting time in pawnshops and e-money agents. There is certainly room for you to improve the quality of your services in order to enhance customer experience and satisfaction.

They say that technology is changing the way banks do their business. Some do not have to ever set foot in a bank branch if they have a fully enabled smart phone. Emergence of financial technology companies or “Fintechs” are also dramatically changing the delivery of financial services in payments and even in the underwriting of credit. While you can use these technologies to your advantage – to improve your efficiencies and value proposition – I believe that the value of person-to-person contact will never fully go away. For instance, if you call a customer service hotline, isn't it that you still prefer to talk to someone rather than hear default call answers from the other end of the line?

The point is, even in the face of technology, you can still build on your strength – which is the relationship that you have established with your community. It is possible for technology to enhance relationships rather than replace them. If you are able to effectively nurture the confluence between the two, you will be able to not only increase but also cement your customer base.

Finally, to be better positioned to serve your clients, always keep in mind that only sound and well-managed institutions can take advantage of new opportunities and have scope for more innovations. Promoting financial inclusion should not be at the expense of safety and soundness of operations. This is the reason why the BSP always emphasizes the importance of strengthening your bank's governance structure and institutional capacity, and continuously upholding best practices and performance standards.

### **Enabling regulatory environment**

On the part of the BSP, not only as your regulator but also your partner, we remain committed in providing an enabling regulatory environment that will support rural banks in overcoming emerging challenges and provide you with various opportunities to be more responsive to the markets that you would like to serve.

Our regulations allow you to partner with non-banks to offer new products and adopt new channels and technology. Many of you have already benefitted from establishing partnerships

with institutions that can assist you in the delivery of services which before were not offered by rural banks. For example, 39 rural banks have been given the authority to cross-sell microinsurance and 50 additional rural banks have already obtained a “no objection notice” from the BSP and are in the process of getting approval from the Insurance Commission. Based on RBAP data, there are almost 2 million insured clients of microinsurance, some of whom are purely microinsurance clients. They can naturally develop into loyal customers of your other products.

There are 52 rural banks with electronic banking facilities and e-money money services. I understand that there is still room for improvement in terms of maximizing the use of these platforms in your operations, but your openness is encouraging. Our hope is that our efforts on the establishment of a National Retail Payment System (NRPS) will be able to address some of the limitations that have impeded the scaled uptake of e-money and electronic payments in general.

Our regulatory environment also encourages rural banks to look for new markets, or serve old markets in new ways. A good example is the agricultural sector and the recent BSP circular on agri-value chain financing. This regulation provides you with more opportunities to finance the agriculture and fisheries sector. By encouraging the linking of various actors or players in an agricultural value chain, the credit risk of participating farmers or fishermen can be reduced, thereby facilitating increased access to credit. This unlocks the potential for financing at all levels from production to marketing. Rural banks can be ideal channels for such type of financing.

The BSP also looks forward to continue working with you in addressing the gaps in SME access to finance. Our guidelines on sound credit risk management (Circular 855) support lending to SMEs, wherein start-ups during the first three years of their operation or banking relationship are exempted from the submission of Income Tax Return (ITR) and other supporting financial statements. The objective here is to encourage SMEs to build banking relationships that will help them grow. However, available data shows that only 31% of our SMEs borrow from banks. Our experience in microfinance has proven that serving a low income segment can still be a viable and profitable undertaking, and we hope that we can apply the learnings in microfinance in serving the SME market.

In summary, our regulatory environment already offers many opportunities. This is the reason why the Philippines is ranked by the Economist Intelligence Unit (EIU) as the first in Asia and third in the world with the most conducive environment for financial inclusion. The challenge to rural banks is how to maximize these opportunities within the framework of the regulations that we have so far put together.

## **Closing**

Ladies and gentlemen of the rural banking sector, in an environment that is rapidly evolving, adaptability is key. But adapting to change does not necessarily mean changing your core and losing your relevance. In fact, as the push for financial inclusion continues to intensify, the role of rural banks today is even greater than it was then. You remain to be a key channel to deliver financial services to the countryside especially the unserved and underserved markets. Embrace this mission and role which you have been given more than 6 decades ago and nurture it by evolving and adapting to the demands of the times.

On our part, we will remain your partner in this important task. This partnership is integral as we work on our shared goal of a stronger, more competitive and more inclusive rural banking sector that can make a positive difference on the lives of the Filipino people.

I wish everyone a fruitful convention. Thank you and good day.