Amando M Tetangco, Jr: Philippine banking – responsive and responsible

Speech by Mr Amando M Tetangco, Jr, Governor of Bangko Sentral ng Pilipinas (BSP, the central bank of the Philippines), at the Third Annual Asian Banker Philippine International Banking Convention 2013, Manila, 25 October 2013.

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Good morning everyone. I am pleased to join you at this 3rd Asian Banker Philippine International Banking Convention. This provides us the platform to share the continuing transformation of our banking industry in the midst of global challenges, the start of our compliance with Basel 3 in 2014, and issues related to expansion and competition.

Ladies and gentlemen. In our view, there are four Rs that define our banking community today: robust, resilient, responsive and responsible.

For instance, the three major international credit rating agencies that gave the Philippines investment grade status this year, acknowledged our sound and stable banking industry as a contributing factor. They view the Philippine banking system as well capitalized, profitable, and liquid, with deposit-funded balance sheets and sound loss-absorption capacities.

In fact, the Philippines is the only country whose banking sector is on positive outlook at Moody's; it raised the outlook to positive in December 2012. In January 2013, Moody's said it sees "positive credit trends in the Philippine banking system, one that has been and will stay relatively immune to global economic shocks, and is benefiting from steady credit growth and growing diversification opportunities."

On the other hand, Standard & Poor is in its February 2013 report said it believes that "the Philippine banking system is reasonably resilient to an external slowdown."

As the regulator of the banking system, we at the Bangko Sentral ng Pilipinas value such positive third party assessments which are of course, corroborated by relevant indicators. But more than being robust and resilient, our banking sector has become more responsive to the varied needs of differentiated stakeholders. Most of all, responsible behavior by our banking sector in handling the savings of our people continues to underpin the continued growth of our banks to record levels.

A responsive banking industry

Indicators clearly show a growing industry. But that cannot be the only measure of success. For the Bangko Sentral, it is the banks that must respond to the needs of their constituents, not the other way around. But let me make one thing clear: this is not meant to be a relaxation of standards; rather, it is a necessary calibration to ensure that the financial needs of the public are truly met by the industry.

The critical issue to determine then is how inclusive our banking system has become. Our ultimate goal is for banks to cover even the underbanked, the unbanked, and those that have been mis-labeled as "unbankable." This is quite a challenge in a country of 7,107 islands with a total population of 100 million and where only 20% of households have bank accounts.

Nevertheless, we continue to make progress in this area. While consolidation continues to reduce the number of our banks, the industry's network and reach continue to grow and deepen through branch banking, ATMs, ebanking, and innovations in marketing and service delivery.

Our initiatives to develop an inclusive financial system through financial education, consumer protection and providing access to financial services also continue to generate positive results.

For the 5th straight year, the Economist Intelligence Unit ranked the Philippine regulatory environment for microfinance as the best in the world. We now have 186 banks with microfinance operations, microfinance loans have more than tripled from 2002 to June 2013 at eight billion pesos, while the number of microfinance borrowers have also tripled to over one million. Even better, the combined savings of the banks' microfinance clients have reached 8.9 billion pesos, an amount surpassing their total loans. This tells us that these microentrepreneurs attained a level of financial independence because they gained access to microcredit. Indeed, the socio-economic impact of developing an inclusive banking system cannot be overemphasized.

Moving forward, there is one point about our population structure that should be highlighted. Based on 2015 population estimates, the median age of Filipinos nationwide would be at the upper end of the 20–24 years old bracket. By the years 2020 and 2025, the average age of Filipinos is estimated to move up to 25 years and 26 years old, respectively.

This information should matter to the banking industry. It reflects a steady but young core of the population whose main financing needs lie 10 to 15 years ahead. On the other hand, there is also the more mature half of the population who are today already savers, investors, borrowers and entrepreneurs.

Indeed, the needs of your market vary considerably across constituents, across geographical communities and across the dimension of time. This presents challenges as well as opportunities if banks are to be responsive to the needs of the public. Nevertheless, while having an array of products and services is necessary, this is also not sufficient. The diversity across constituents calls for consumer protection and customer care to be on top of our agenda. This is the responsible path to take.

At the Bangko Sentral, the drive to promote financial inclusion is balanced with programs to institutionalize redress mechanisms and financial education. Today, this balanced approach is part of global standards.

Nevertheless, the Bangko Sentral is taking consumer protection a notch higher. Soon, our supervised institutions will also be examined on how they provide consumer protection. Up for consideration by our Monetary Board is a consumer protection framework that outlines the modes of behavior and practices that should be adhered to by BSP-supervised institutions.

Responsible market conduct: a credit perspective

A central tenet of the financial consumer protection framework is the aspect of responsible market conduct. This, extends beyond consumer protection and is a critical pillar of our market.

I am pleased to share therefore that even with the high level of liquidity in the banking system and our own push towards a more inclusive banking industry, our banks, in general, adhere to high standards of credit discipline.

For instance, we note that while total loan portfolio increased by over a trillion pesos between December 2009 and March 2013, the amount of non-performing loans over the same period actually declined by over 11 billion pesos. And even with this improvement, banks further increased their allowance for credit losses on loans by more than 11.6 billion. The result is a declining NPL ratio and an NPL coverage ratio above 100 percent.

Likewise, the country's credit-to-GDP ratio does not show any sign of unwarranted expansion. In fact, within ASEAN-5 we remain at the low end of the spectrum on this measure, suggesting that there is room to grow within the tenets of sound credit standards.

In addition, stress tests, which we conduct every semester, tell us that the balance sheet of banks can absorb extreme credit shocks. Even at a 50 percent write off, capital positions are sufficient to take on the magnitudes of such losses. Ladies and gentlemen, all of these indicators suggest that Philippine banks manage their credit exposures quite well. They observe a degree of conservatism needed to stay within the so-called "discipline of target markets." This is evident by the declining levels of NPLs, high coverage ratio and moderate credit exposures vis-à-vis GDP. What makes these numbers even more impressive is the fact that banks have available liquidity that they can deploy, if they so choose.

The pursuit of financial stability

Perhaps, the crux of the matter lies in those last four words: "if they so choose". In a market that seizes opportunities, making the appropriate choices is critical, particularly since funds being deployed belong to the public.

The BSP sees these choices not only in the numerical indicators… but also in the ICAAP (Internal Capital Adequacy Assessment Program) document which universal and commercial banks submit annually. Indeed, risk management cannot be the domain of a few specialists in the bank. Strategic risk decisions must emanate from bank management and from there it should become everyone's business within the bank.

On our part, the Bangko Sentral does not hesitate to act accordingly in the event remedial and corrective actions are needed at the bank level.

Ladies and gentlemen. To us, the prudential objective for the industry is not only about banks being individually safe and sound; a clear lesson from the financial crisis of 2007–2009 is that the condition of the whole cannot be the simple sum of the respective parts.

Moreover, the bigger picture is defined not just by the complexities of finance. Rather, it is about the web of inter-connectedness between transacting parties, across products as well as the channels of risk that underpin the activities in the market.

This is the new prudential world of financial stability. It is not just about banks being safe and sound. For this reason, the norms for financial stability go beyond those of financial system stability. There are technical and policy nuances to consider under financial stability but these can be discussed at another opportunity.

For now, let us be mindful that all of us must bear collective responsibility for the actions each of us take in the market, day in and day out given that inter-connectedness is a central tenet of financial stability.

Final thoughts: managing change and moving forward

Moving forward, it is wise to remember that market conditions continue to evolve, opportunities are never permanent, incentives change and macro-financial situations can reverse.

We need therefore to continuously invest in ourselves as a market, if we are to sustain the banking sector's position of strength and adhere to the new prudential mandate of financial stability. This means that change is inevitable, at the national, regional and global scale.

A case in point is Basel 3, the new global standard for managing banking-related risks. In this connection, the Bangko Sentral has made clear repeatedly that we subscribe to the underlying principles espoused by the Basel 3 Accord. However, we have taken steps to calibrate its implementation here to align with local conditions.

At the Bangko Sentral, we do not instigate change for the sake of change. Rather, our policy initiation is calibrated to make the industry stronger against potential waves of shocks.

The same principle applies to other reform strands. The new framework for OTC derivatives, financial market infrastructure, changes in corporate governance standards, consumer protection, accounting and even the recent issue on the integrity of financial benchmarks are all in the context of addressing identified weaknesses under a financial stability mandate.

They represent global reforms that are meant to revise the international financial architecture and the market's intrinsic landscape.

At the regional level, the reforms emanate from the policy decision to pursue integration. For the banking community, this will be the ASEAN Banking Integration Framework or ABIF. The framework takes us to 2020 at which time we expect that the ASEAN banking community would be semi-integrated.

While this is six years away, the work under ABIF is well underway. Banks can choose to retain a domestic focus or choose to become a regional player. However you position your bank, be aware that either of the two choices has critical competition policy consequences. If one is to survive and thrive, international competitiveness is the way to go. This is because so-called Qualified ASEAN Banks (QABs) will operate within ASEAN. In the end, the size and strength of each bank's balance sheet as well as the quality of its management will become crucial factors under regional integration.

Ladies and gentlemen, we have covered quite a bit of ground in describing the Philippine banking industry in terms of both its current standing and its prospects. I can say that while we are in a clear position of strength today, calibrated reforms will continue to be a necessity.

At the end of the day, the real measure of strength and success is the ability to withstand difficulties that will arise in the future. We know that change will always be at a cost; consider this as investment for the future. For today, your prospective strength will be difficult to quantify.

Nevertheless, you can count on the Bangko Sentral in defining our shared vision of the future under the principle of collective responsibility. I believe we all want a banking system that is robust, resilient, responsive and responsible. How to achieve these in the midst of a constantly shifting and changing landscape is the challenge before us.

I look forward therefore to this International Banking Convention of The Asian Banker to provide some answers for us.

Thank you all and Mabuhay!