Amando M Tetangco, Jr: Looking back to move ahead in 2016

Speech by Mr Amando M Tetangco, Jr, Governor of Bangko Sentral ng Pilipinas (BSP, the central bank of the Philippines), at the Joint Meeting between Rotary Club of Manila and Rotary Club of Forbes Park, Makati City, 7 January 2016.

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Distinguished officers and members of the Rotary Club of Manila under the leadership of President Eusebio Tan and the Rotary Club of Forbes Park represented today by Immediate Past President John Toing, special guests, ladies and gentlemen, good afternoon.

Thank you for inviting me to this joint membership meeting of the RCM and its younger counterpart RCFP. As the oldest Rotary Club in Asia, dating back to 1919, RCM will turn 97 years old this year. Few organizations last for nearly a century, much less remain dynamic, relevant and influential, like RCM. For this, the men and women of the RCM deserve our congratulations!

In this connection, I am delighted that you have made me a part of your history by inviting me every year since I became Governor of the Bangkok Sentra ng Filipinas to share my assessment of our economy – its past, present and future. In addition, since I have always accepted your invitation every year, I am marking today my 11th year as RCM's January speaker. Thank you RCM.

Now, what can I tell you about the Philippine economy?

Well, I can say that if the first seven days of this year is any indication, 2016 will be far from boring – it will be riveting and challenging.

Last Monday, in the first trading day of the year, stock markets across the globe did not simply drop; they plunged – in the US, in Europe and in Asia. In particular, China shut down trading for the day under its new circuit breaker rule when stocks tumbled beyond seven 7%. This has been described as the worst opening day for a new year in China, the world's second largest economy. This rattled currency markets as well. Today, Chinese stock market was shut down again.

Meanwhile, geopolitical concerns in the Middle East add to fears of volatility. Analysts warn of more wild price swings as the global economy slows down.

On the other hand, these are early days – just the first week in the year. It is way too early to tell if this trend will last. As the Greek philosopher Aristotle once said "one swallow does not a summer make."

From the Philippine perspective, we move forward in 2016 with cautious optimism. We are cautious – because we are mindful of the challenges ahead and of the possibility that our operating environment can change so swiftly at a scale we may not have anticipated. Yet we are optimistic because we start from a position of strength, having managed to address obstacles we encountered in 2015 and the great financial crisis in 2007–2008.

At this point, it will be helpful if I give an assessment of 2015 and then move on to 2016. After I complete my narrative, you can make your own judgment on the state of our economy.

Recalling 2015

2015 brought with it, its own challenges and opportunities. Global growth remained uneven, resulting in a divergence in policy responses from major central banks– the US Fed finally went ahead with its much-awaited "lift-off" and raised interest rates; China devalued its currency; while the European Central Bank provided further stimulus to its economy with interest rate cuts and an expanded bond purchase program.

These external headwinds made for some rough sailing for the Philippines in 2015 due to higher risk aversion among investors. Some capital flowed out particularly in the second half of the year, the Philippine stock market took a hit and the peso depreciated. There were similar shifts in financial markets across emerging Asia.

Nevertheless, domestic sources of resilience kept the Philippine economy on a steady non-inflationary growth. Low and stable inflation – 1.4% in 2015, the lowest since the BSP adopted the inflation targeting framework in 2002 – continued to encourage investments and business expansion. In the third quarter of 2015, our economy grew at an accelerated pace of 6.0 percent. This made the Philippines one of the fastest-growing economies in Asia in the first nine months last year.

At the same time, the country's sound, stable and liquid banking system provided solid support to our economy in 2015, with bank lending continuing to grow in double-digit rates, with credit flowing particularly to the productive sectors. And as a result of the continuing cooperation between the BSP and the banking sector to continue to enhance governance and risk management practices of banks, industry profitability improved further with return on equity rising from 9.67% in September 2014 to 10.04% in September 2015; asset quality got even better with gross NPL ratio improving to 2.32% in September 2015 from 2.56% in September 2014; while deposits reached record-high levels, increasing by over 9% year-on-year to nearly P 8.8 trillion as of September 2015.

Meanwhile, the country's strong external position continued to inspire confidence among investors and creditors, with the current account remaining in surplus, given the steady inflow of remittances from overseas Filipinos and receipts from BPOs, and a healthy level of gross international reserves that can support a robust economy.

I am pleased to inform you that preliminary GIR at end-December 2015 was reported at US$80.6B, over US$1B more than the level at end-December 2014. At $80.6B, the reserves can cover 10.3 months' worth of imports and payment for goods and services.

Third-party sentiment on the domestic economy's prospects also remained bullish. The international credit rating agency Fitch upgraded its outlook on the Philippine economy to "positive" from "stable" in September 2015. This is an indication of possibly yet another credit rating upgrade within 18 months.

In other words, ladies and gentlemen, the Philippines remained stable in 2015 and went on to post 67 quarters of uninterrupted economic growth against a harsh external environment.

Looking ahead to 2016

Looking ahead to 2016, there are at least three challenges that the BSP should focus on. We can summarize them into three key words – stability, liquidity, and opportunity.

Let us start with stability. In 2016, the BSP's primary concern will be to continue to provide a stable environment where inflation is low, stable and within target. Our latest forecasts show that the path of inflation will be consistent with the National Government's target range of 2 to 4 percent in 2016–2017.

However, there are potential upside pressures to inflation. Food prices are likely to be affected by El Niño, other weather disturbances, and increases in utility rates. On the other hand, downside risks could come from slower-than-expected global economic activities that could further lower oil and commodity prices. The BSP will continue to monitor national and global developments to ensure that our monetary policy stance remains appropriate.

In addition, the BSP will continue to find ways to further enhance the effectiveness of our monetary policy. Among others, we will adopt by the second quarter this year, what we call the interest rate corridor or IRC system. This is calibrated to keep interest rates within a reasonable range around the BSP's benchmark policy rates.

The second challenge we see in 2016 is liquidity and financial stability. Discussions on financial stability often revolve around liquidity. Where it comes from and where it goes, will determine its impact on the financial system and, ultimately, on the real sector.

As we have learned from recent episodes of financial crises, too much liquidity can cause potentially dangerous asset price bubbles; too little and the economy could contract. The ideal is when liquidity is adequate and it is channeled toward productive uses and opportunities.

Indeed, we need to ensure that the liquidity that is already in the financial system is channeled effectively toward productive uses.

Another concern is how domestic liquidity conditions could be affected by the US Fed's decision to raise interest rates, by the weakening Chinese growth prospects and by the heightened volatility in their financial markets.

Nevertheless, we have reasons to believe that the overall impact on our economy would be manageable due in large part to the "pull factor" of the Philippines' strong macroeconomic fundamentals.

At the end of the day, the move by the US Fed to raise rates also signals a relatively more vibrant outlook for the US economy which could have positive spillover effects through revitalized trade flows. Meanwhile, a more market-oriented Chinese market could also have positive long-term effects on the global economy by ushering in a more sustainable growth path.

It is also important to note that the BSP has policies and measures to help cushion the economy from external shocks. These include (1) upholding a market-determined exchange rate with an option to maintain its presence in the foreign exchange market to minimize volatility; (2) keeping a comfortable level of reserves and managing them prudently; and (3) providing access to domestic and foreign exchange liquidity through various facilities.

We will also align our supervisory policies with international standards, to provide a more level playing field for our local banks. This is crucial as we prepare for the entry of more regional and international banks under the ASEAN economic and financial integration program.

Indeed, we need to do much more to be competitive in the region. – we need be able to handle more complex financial transactions and instruments; and we need to strengthen our pricing conventions and price discovery mechanisms, so that reference rates and benchmarks accurately reflect market valuation.

The BSP has been consulting with industry stakeholders, other government regulatory agencies and our counterparts overseas, to help nurture the country's growing money and capital markets.

These efforts tie in closely with our third challenge: opportunity and financial inclusion. Given the healthy growth of our economy, there are many opportunities in the Philippines today. Our challenge is to bring these opportunities to the people who stand to benefit the most from them.

The National Strategy for Financial Inclusion provides us the platform to reach out to the unbanked and the underbanked by delivering suitable financial products to different market segments through responsible and innovative business models, while providing the citizens with adequate education and protection as clients of the financial system.

To be implemented by the BSP with 12 other government agencies, NSFI serves as the country's road map for catalyzing inclusive growth through the development of a more inclusive financial system.

To give you an idea of the challenges we face in our financial inclusion program, I will share some highlights of our maiden National Baseline Survey on Financial Inclusion. The survey, completed in 2015, showed the following results:

- 25% of Filipino adults (those aged 15 years and above) have never saved, 32% used to save, and only 43 % presently have savings.
- Of those who save, only 33% keep it in banks; the rest keep their savings at home.
- About 47 % of adults have outstanding loans. The main source of borrowing is informal – from family, relatives, friends and informal lenders. The share of bank loans is only 4.4% of the total.
- Only 3.2 percent of adults have microinsurance coverage.
- Clients rated themselves as only "somewhat satisfied" with how issues were resolved in most financial service access points.

Ladies and gentlemen. The survey results tell us that we have a long way to go to achieve financial inclusion and that there are plenty of opportunities for those looking to expand their business or to introduce meaningful game-changing innovations to help improve the lives of Filipinos.

Clearly, we need broad-based cooperation from local and international institutions to address these gaps. With more institutions as partners, we can make substantial gains on our financial inclusion targets.

Concluding remarks

Ladies and gentlemen of the RCM and the RCFP. In 2016, both external and domestic developments will compel us to remain watchful in guarding against threats to growth and stability. These challenges will revolve around promoting price stability through prudent and responsive monetary policy; channeling liquidity toward productive uses while maintaining financial stability; and delivering opportunities for growth and investment through financial inclusion and literacy.

We see continued economic challenges for the Philippines moving forward. Nevertheless, our success in keeping our economy on the growth path in the midst of global volatility gives us confidence that we have what it takes to deal with the challenges that will come our way.

Among others, our economy's non-inflationary growth momentum, sound banking system, and favorable external liquidity position provide your policymakers, including the Bangko Sentral ng Pilipinas, enough flexibility to respond appropriately to evolving domestic and global conditions.

We can look forward therefore to 2016 with cautious optimism. Let us also take heart from third party assessments that continue to give us high marks. In the past, the Philippines was called the sick man of Asia. In recent months, we have been described as a star among emerging economies. More recently, we were described by analysts as the region's economic strongman due, among others, to our resilient growth. This is well and good.

But we can make it better. Let us work together on spreading the benefits from sustained economic growth with those who need it the most. RCM and RCFP lead the way in such programs. Hopefully, we can get more advocates to work on financial inclusion that supports sustained inclusive growth.

If you are interested, we can provide a briefing on the National Strategy for Financial Inclusion so that you can assess how to support it as private sector partners.

With the collective wisdom, expertise and influence of the members of the RCM and RCFP, I have no doubt, you can increase your sphere of influence to benefit more areas and more people.

Finally, on behalf of the Bangkok Sentra ng Filipinas, I wish all the officers and members of the Rotary Club of Manila and the Rotary Club of Forbes Park, a happy, healthy, and prosperous 2016!

Mabuhay nag RCM and RCFP! Mabuhay nag Pilipinas!

Mabuhay pop toying lama! Maralinga salaam as into.