

Nestor A Espenilla, Jr: Returns

Speech by Mr Nestor A Espenilla, Jr, Governor of Bangko Sentral ng Pilipinas (BSP, the central bank of the Philippines), at the joint meeting of the Rotary Club of Makati with the Rotary Club of Makati North, Makati City, 29 August 2017.

* * *

Mr. Conrado Dayrit, Rotary Club of Makati (RCM) President, President Dennis Pe (RCM North), President Carol Mercado (RCM Premier District), RCM officers, members, guests, ladies and gentlemen, magandang hapon po sa inyong lahat. Thank you for the opportunity to keynote this meeting co-sponsored by RCM North.

I would like to begin with the word, “returns.” In this group of distinguished businessmen and professionals, it could readily mean “return on investment”— a financial metric indicating efficiency of a commercial venture.

At the same time, to this same group of community builders and philanthropists, “to return” could also mean, “to give back” and to work for society’s improvement and welfare. In this regard, RCM deserves commendation for its active engagement in public-spirited projects since its establishment in 1966.

RCM understands that businesses operate more successfully when society and its needs are considered. It knows that commerce fully succeeds in a society that is also successful. The reverse is also true.

We at the Bangko Sentral ng Pilipinas share this belief. Established for the public interest, we believe in first – providing a conducive business environment through promotion of price stability; banking and financial stability; and the operation of an efficient and reliable payments settlements system. We also have come to believe in, second, working for greater financial inclusion so that economic development and progress would be truly meaningful.

I would like to think of the BSP and RCM as partners in these two shared goals.

A positive environment for investment

The BSP cannot guarantee businesses’ a return on their investments. As you know, this is a function of many factors such as prudent management, quality of customer service, innovation, location, supply and demand and so on.

The BSP’s task is to work for a better and more stable operating economic landscape for commerce, banking and finance.

In that regard, I’m pleased to note, the numbers are quite positive. And my commitment as Governor of the Bangko Sentral is for there to be continuity in the policies that brought about this favorable economic environment, with space for improvements through bold and strategic financial sector reforms.

1. **Increasing gross domestic product** - Developments in 2017 point to overall economic resilience. Real GDP rose by 6.4 percent in the first half of this year with stronger economic activity expected in the second half.

2. **Manageable inflation**. - Although headline inflation rose to 2.8 percent in July (from 2.7 percent in June), the year-to-date average inflation rate is 3.1 percent. We expect it to stay that way. We therefore will meet the inflation target of 3 percent, +/- 1 percentage point allowance for 2017.

Fostering a stable business environment is primordial to the BSP. Keeping inflation low and stable does away with uncertainty and better enables businessmen and investors (like yourselves) to plan and make informed decisions about consumption, investment, saving, and production.

Moving forward, the BSP will continue to fine-tune its monetary policy framework to make it more market-oriented, while staying focused on inflation control. We deployed the interest rate corridor (IRC) system in 2016. Its objective is to make market interest rates move closer to the BSP policy rate. In the long run, this supports Philippine capital markets by encouraging money market transactions and better liquidity management.

3. Ample domestic liquidity - Latest data also shows ample domestic liquidity. Bank lending remains upbeat and continues to flow into productive sectors such as real estate; power and utilities; manufacturing; wholesale and retail trade; and information and communication.

4. Sound and Stable Banking System - Our banking sector is fundamentally sound. The reforms put in place by the BSP, along with banks' commitment to manage operational risks have resulted in significant improvements in the quality of bank assets and loan portfolios as well as strong capitalization. Also, I am pleased to note that as banks fund the domestic economy, they remain prudent in their lending activities.

The BSP will continue to review and align regulations with international standards to improve risk management and improve bank competitiveness in view of ASEAN integration.

Working towards a stronger and more stable banking system is a practical goal. Banks support the financing needs of our continuously growing economy and have a role in efficient allocation of resources.

5. Market-driven exchange rate and adequate GIR - Recent developments in the exchange rate reflects a confluence of factors. These are: strong import growth, reflecting a rise in dollar demand given expansion in private and government sectors, and expected U.S. Federal Reserve rate hikes due to their policy normalization. These factors notwithstanding, we expect the country's robust growth, stable inflation environment, strong and resilient banking system, and prudent fiscal position to provide underlying support to the peso.

It is also worth noting that inflow of cash remittances from overseas Filipinos (OFs) coursed through banks remain steady reaching US\$ 2.5 billion in June. This is a 5.7-percent increase from the level posted in the same period a year ago. Meanwhile, export growth has actually picked up to around 13%. As a result, the country's gross international reserves (GIR) as of end-July 2017 remains at more than US\$80 billion, equivalent to nearly nine (9) months' worth of imports of goods and services.

Need for vigilance

While the economic backdrop is favorable, the BSP remains vigilant given global and domestic challenges. An expected rise in US interest rates may drive portfolio capital outflows from emerging markets, including the Philippines, adding to exchange rate pressures in these economies. Moreover, US implementation of a conservative policy agenda on immigration, offshoring/outsourcing, trade, tax reform, labor/immigration laws, and financial and business regulation could impact exports as well as OF remittances. Finally, the ongoing rebalancing of the Chinese economy as it transitions from export-led growth to services and domestic consumption-driven expansion could impact Philippine exports.

Potential Economic fall-out from the ongoing tensions between the US and North Korea, as well as peace and order issues if not managed are also a source of concern.

These risks notwithstanding, In June 2017, Moody's affirmed its stable outlook on the Philippine banking system citing our: (1) robust real GDP growth; (2) broadly stable bank asset quality; (3) high capital buffers and loan-loss provisioning; (4) the banking system remaining fully deposit funded; and (5) high proportion of liquid assets held by banks. This is a good indication.

At any rate, the BSP has a broad policy toolkit to respond to the risks mentioned. We are also coordinating with other government agencies and regulators to further enhance our macro-financial surveillance capability. The BSP is watchful of shifts in market sentiment along with trends in commodity prices and other inflation drivers, refreshing its liquidity forecasting and inflation models so they are in tune with evolving impulses. In the spirit of "continuity plus plus," no significant deviation from previous monetary policy approach is anticipated.

Returning to the community

As the country experiences more economic success, it becomes imperative to allow a greater number of our fellow Filipinos to enjoy the gains. Financial inclusion translates to allowing more of our countrymen to save and borrow for productive uses...avail of investment and insurance products and send and receive payments securely and efficiently.

We believe this is the only way for economic growth to be truly meaningful. Filipinos from the grassroots must be given usage and access to financial services, and be provided with financial literacy and education empowering them to make informed financial decisions to better their lives and that of their families.

RCM has, through the years, made positive and lasting change in Philippine communities. We in the BSP will be glad to partner with you in the transformation of our country, perhaps in launching Public Information Campaigns and other endeavors. Imagine even our lowest socio-economic group as a financially literate populace! This is an exciting prospect that we hope you, our partners in business and industry, would support the BSP in achieving.

On the BSP's part, we have, among other initiatives, implemented the National Strategy for Financial Inclusion to make the financial system accessible and responsive to the needs of the entire population.

We are also working with other government agencies for the implementation of a national ID system. With this system, disenfranchisement will be a thing of the past, with the number of "unbanked" citizens shrinking faster and with more certainty. Individual biometric identification will give each one a voice to be recognized, to be heard and to participate in economic growth and development.

We are also continuously creating a more enabling regulatory environment for the development of fin-tech and digital finance. The digitalization of finance is essential to achieve significant inroads against financial exclusion and payments inefficiency. Soon, financial consumers and investors will be able to make more informed business decisions choosing from a longer, fresher and more innovative menu of available financial products and services.

We adopted the National Retail Payments System (NRPS), a flagship program for digital finance. With this, we hope to transition from a cash-heavy economy, where 99 percent of transactions are done in cash, to a cash-lite economy, with transactions becoming electronic. This move towards modernization supportive of e-commerce might be of particular interest to business people such as yourselves. On our part, we see the role innovations play in on-boarding currently excluded markets into the formal financial system.

But there is still much to be done. We count on you, RCM to help us in our financial inclusion efforts to collaborate with us towards maintaining a more stable, conducive and stronger business environment. I am confident that the returns on this, far from just being financial or proprietary, will be more satisfying and enduring.

I end with a simple but powerful quote from Deepak Chopra “ If you want something, give it.” . What one gives out, we know, returns somehow. As we work towards society’s positive transformation, we do not shirk at the possibilities of being at the receiving end.

Thank you for your kind attention.