Nestor A Espenilla, Jr: Beginning a meaningful conversation - first coordination dialogue on developing the local debt market

Speech by Mr Nestor A Espenilla, Jr, Governor of Bangko Sentral ng Pilipinas (BSP, the central bank of the Philippines), at the Local Debt Market Development Workshop, Manila, 25 August 2017.

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The Securities and Exchange Commission, the Bureau of Treasury, and the Bangko Sentral ng Pilipinas are no strangers to coordination and collaboration (Many of our achievements come from working together!) and while this is not our first time to collaborate, it IS the beginning of a new and meaningful conversation. Today, we mark a milestone as we unveil the Philippine roadmap for developing the local debt market. At the same time, we look forward to engaging in an initial discussion with market participants.

This is a great time to begin this conversation!

Recently, our capital market was recognized as an emerging investment hub in Asia by three (3) major debt watchers – Moody's, Standard and Poor's, and Fitch.

Robust economic conditions coupled with Government's thrust to promote infrastructure create favourable conditions for capital market deepening. Government's vision of a "Golden Age of Infrastructure" to support value-added output to the housing, manufacturing, connectivity and agricultural sectors is a game changer.[1] A deeper capital market will mobilize long-term savings for the financing requirements of these priority industries.

Moreover, GDP is projected to grow at 6.8 percent in the medium term, with the inflation outlook for the next two (2) years manageable and within the Government's three (3) percent ± one (1) percentage point target.

Our international reserves are at a level of eighty point eight billion US Dollars (USD80.8B) as of end-July 2017 — enough to cover eight point six (8.6) months of imports and payments of goods and services.

As if these are not encouraging enough, our discussion on capital market reform received support via technical assistance from the IMF. The time is right to talk and take up reforms.

Colleagues and friends, it is our pleasure to start this conversation with you and to make local history. I am honoured to represent the BSP in this regard.

SEC Commissioner Ephyro Amatong, Treasurer of the Philippines, Rosalia De Leon, representatives of the Bankers Association of the Philippines (BAP), headed by President Nestor Tan and BAP Open Market Committee Chairman Wick Veloso, the Money Market Association of the Philippines under President Michael Joseph Delfino Government Securities Eligible Dealers (GSEDs), esteemed guests, on behalf of the Monetary Board and the Bangko Sentral ng Pilipinas, I welcome you to the BSP. Magandang hapon sa inyong lahat.

Allow me to share some pointers on how to make common-ground conversations more meaningful.

These tips are borne not just out of my thirty-six (36) years of experience as a Central Banker not just as Deputy Governor of the Supervision and Examination Sector for twelve (12) years but these points were learned chiefly in my capacity as a friend and colleague (perhaps even as a husband and father!).

In my experience, a conversation is more meaningful when: First, it is between those with the same goals.

In this, there is no issue. As mentioned earlier, the SEC, BTr and BSP have always been partners. For one, together with other institutions,[2] we are members of the Financial Stability Coordination Council (FSCC). The FSCC's key objective is to identify, manage and mitigate the build-up of systemic risks. Our institutions share the prudential objective of financial stability and development. Our being here today is just a step-up an expression and a specific operationalization of our original goals. In this particular case, we share the same vision of developing our local currency debt market to support our growing economy in a sustainable manner.

As a result, the Capital Market Working Group of the BSP, the BTR, and the SEC, with the support of the Department of Finance, joined hands in developing the Philippine Roadmap to accelerate the development of the domestic debt market. Three areas are prioritized: (1) deepening the local bond market by adopting reforms to incentivize market-making, increasing supply of short-term debt securities, and developing an effective regulatory framework for the repo and OTC government securities markets; (2) the creation of reliable financial benchmarks and valuation of financial instruments; and (3) the establishment of an integrated financial market infrastructure to promote price discovery, transparency and orderly trading, clearing, and settlement of the full range of financial transactions.

Second, the value of a conversation is greater when those who engage in it understand its relevance and importance. Otherwise, discussion is just chatter, intellectual calisthenics or a venturing into hypothetical thinking.

Thankfully, we are here not just to engage in an academic exchange. While there are scholarly points to be made and learned, we all agree that debt market development is a pressing concern one that has real-life implications, deserving of our particular attention.

We understand there is greater demand for more active debt markets as financial systems require funding sources from outside the banking system. We know that a vibrant capital market can serve as an alternative source of industry financing and act as a powerful complement to bank lending.

We appreciate that a developed local currency debt market is essential for efficient fiscal operations, supporting a sustainable market-oriented debt strategy at reasonable costs and desirable mix of maturities. A liquid money market likewise can help strengthen BSP's monetary transmission mechanism. Development of the domestic currency debt market will also broaden investment opportunities and pave the way for increased availability of financial products, including hedging instruments. This boosts economic resilience to external shocks.

My third tip is that a dialogue becomes productive when it is open and honest when even hard questions are respectfully asked and when responses are heard and listened to. This is perhaps the most important tip to follow. When adhered to, this is when real connections are made.

And what are some of the hard questions? Perhaps we can begin by asking, "What does it really mean to deepen the bond market, to develop it? What are the barriers to an efficient, transparent and fair market?"

How can we enable more people to have access to capital? How do we increase scale and efficiency?

Should we take a deeper look at the secondary retail market? It is common knowledge that with bond sales there is not much incentive to serve retail customers. The issue is cost as it is cheaper to deal with institutional investors transacting in large sums rather than with retail investors, who (despite their potential number) have smaller transaction sizes. The barrier of minimum investment requirements in T-bills and bonds exclude many. Also, there is disparity as while institutional investors could manage the information asymmetries (with respect to price discovery), retail investors are limited to deal only with their own banks.

My take away from this is that while a deepening of the financial market might translate to financial inclusion, the two may not be automatically synonymous as they have different policy implications. As a staunch proponent of financial inclusion, I suggest we bear these nuances in mind when crafting regulations, with a commitment to financial inclusion as part of a broader agenda.

There is a need to be pragmatic, but we must be open to out-of-the-box ideas, balancing regulation and innovation. We must be mindful of the changes brought about by digitization and technological innovation. We might explore encouraging on-line bond trading even for individuals in the secondary market, perhaps doing away with cumbersome paper work to complete transactions. We can also look into how we can build capacity and acquire the individual and institutional expertise to deepen capital markets.

Finally, I have learned that a conversation is only as good as the actions and changes that follow it. Parties must move the dialogue forward, with a clear identification and fulfilment of their corresponding roles to add value to the objectives sought.

Winston Churchill said, “to improve is to change; to be perfect is to change often.” This is a good note to end on since this afternoon, SEC, BTr and BSP, will be announcing some changes aimed at improving our local currency debt market. I also like the quote as it implies constant improvement.

I hope I have sufficiently set the stage for beginning our dialogue. Although now, I can see from your faces that very little motivation is needed for this group to move forward with excitement. You are excited enough!

Looking at the participants – prime movers and stakeholders in our debt market, from both the government and private sectors – it is evident that discussions will be interesting, meaningful and engaging.

I wish us all Godspeed in our important task, not just for today, but in the days to follow. Thank you and good afternoon.

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[1] The Philippine Development Plan. 2017 to 2022.

[2] The Insurance Commission, the Philippine Deposit Insurance Corporation and the Department of Finance