Nestor A Espenilla, Jr: Collective and individual competitive advantages

Speech by Mr Nestor A Espenilla, Jr, Governor of Bangko Sentral ng Pilipinas (BSP, the central bank of the Philippines), at the POWWOW 2017, Cebu City, 17 November 2017.

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PhilExport Cebu Chairman Apolinar Suarez, Jr.; President Mr. Nelson Bascones; officers and members of PhilExport Cebu; special guests; ladies and gentlemen Maayong Gabii. I am grateful for the invitation to speak about the BSP's policies and thrusts, my first as BSP Governor, before this distinguished group of business leaders and exporters.

A major industrial hub, Cebu plays a crucial role in Philippine economic development. With at least 27 IT Parks and Centers; 7 manufacturing zones; 2 tourism economic zones; and 1 agro industrial economic zone, Cebu is a dynamic economic hub.

This evening's theme has three action verbs. Individually, the words sound like commands. As a unified phrase, it is a battlecry. "Create. Innovate. Compete."

Cebu is no stranger to the power of creativity and innovation. Because of efficiency and raw talent, the level of craftsmanship and creativity of the Cebu furniture industry, for example, allows it to produce high quality and unique custom-built pieces that cater to medium- to high-end markets, selling twice or thrice more furniture than competitors from Vietnam and China.

To outperform others — businesses must be creative and innovative. But creativity and innovation should not be pursued for their own sakes. (This is a reminder I have relayed to the BSP and the banking and financial sectors many times).

Efforts should be focused and strategic. In the context of business, creation and innovation should be concentrated on, and mindful of, competitive advantage. This brings about strategic competitiveness.

The Philippines' competitive sdvantage

Allow me to relay data on the Philippines' positive economic position which enables it to compete strategically in the global market.

Philippine macroeconomic fundamentals are solid and robust. These support local exporters and entrepreneurs. We have had uninterrupted GDP growth for 75 consecutive quarters (more than 18 ½ years). GDP expanded 6 percent annually during the past five years.

Prospects are favorable and growth is predicted to be between 6.5 to 7.5 percent this year and 7.0 to 8.0 percent over the medium-term. We are well on track with the recently announced third quarter GDP at 6.9 percent!

Since the BSP adopted the inflation targeting framework in 2002, inflation has become more manageable, with latest baseline forecasts showing it will likely settle around the middle of government's target range of 2 – 4 percent in 2017 to 2019.

Further, Philippine banks continue to be sound, stable and more efficient. The non-performing loan (NPL) and non-performing asset (NPA) ratios of universal and commercial banks have significantly declined from around 15 percent in 2001 to less than 2 percent in August 2017. Meanwhile, the capital adequacy ratios of banks are well above the BSP minimum as well international norm. Almost double, in fact.

On the exchange rate, the peso is expected to be broadly stable and market-determined, backed by strong underlying economic fundamentals, ready market access, sustained decline in external debt position, and robust international reserves. At the current range, export price competitiveness has improved back to 2008 levels as measured by the real effective exchange rate (REER) index. The recent controlled and moderate depreciation of the peso from last year is good for the economy.

As of end-October 2017, our foreign exchange reserves stood at US$80.6 billion, equivalent to 8.4 months of import cover (around 4 times larger than our total external debt). The sustained structural inflows from overseas Filipino remittances, business process outsourcing sector, foreign investments, tourism receipts, and the strong recovery in exports, insulate us from foreign exchange crisis.

Exports on the road to recovery

The past two years have been challenging for our exporters. There was a decline in global trade and growth. Our goods exports contracted by 5.3 percent in 2015 and 2.4 percent in 2016[1]. These difficulties were brought about by a range of factors such as: (1) fragile and uneven economic growth among major advanced and emerging economies; (2) bouts of financial market turbulence due to divergent monetary policies adopted by developed countries; and (3) cutbacks in capital investments because of the plunge in international oil and commodity prices.

But data for the second half of 2016 to the present show increased trade momentum! Goods exports expanded by 12.2 percent during the first nine months of 2017, owing to improved external demand from major trading partners such as the United States, Hong Kong, China, Thailand, South Korea and the European Union.

There is an 8.6 percent increase in outbound shipments of manufactured goods. These include electronics; machinery; transport equipment; garments and others. Exports of mineral products and agro-based products also recorded significant year-on-year rebounds of 74.1 percent and 19.9 percent respectively. This resurgence boosts prospects for the exports sector.

Vigilance and leveraging on competitive advantage

Ladies and gentlemen, the Philippine economy is showing sustainable growth momentum. It is also more resilient, benefitting from years of deliberate structural reforms. But this does not warrant complacency. We must all stay focused and pursue bolder reforms if we hope to catch up with our neighbors.

A strategic approach is important given megatrends in the economic landscape. These trends include demographic changes, rapid urbanization, climate shifts and the rise of disruptive technologies. Our increasing population of tech-savvy millennials demands innovation as they expect faster and more streamlined products and services.

The need for businesses and government to “up the ante” has never been more imperative.

As a country, we have unique natural endowments on which we can leverage: a young, skilled and mobile workforce; a predominantly English-speaking population, distinct and world-class Filipino craftsmanship and ingenuity. These will set our brand apart. But we have to take action to transform these to strategic competitive advantage.

BSP’s continuity plus-plus achieving competitive advantage

As a central bank, our traditional focus is to maintain price and financial stability. When I was appointed BSP Governor last July, I committed to the continuity of policies that brought about the sound macroeconomic stability we now enjoy. At the BSP, we vigilantly monitor vulnerabilities, formulate and implement monetary and financial sector policies and reforms supportive of economic development.

Upon my appointment, I also said that continuity will come with a "plus plus." This thrust is premised on the same factors of rapid technological changes and shifts in the economic and financial landscape that prompt innovation in the private sector. These "plus plus" initiatives support national competitive advantage, encourage cost-effectiveness, differentiation and focus.

As part of the "plus plus" agenda, we are pursuing more ambitious foreign exchange (FX) reforms, consistent with our efforts to reduce the cost of doing business and increase efficiency. These include rationalizing and further liberalizing foreign exchange rules. Currently, we are drafting a set of circulars that will remove prior BSP approval for most private sector transactions. We aim to simplify registration processes, significantly reduce documentary requirements, and enhance data capture for effective policy decision-making.

The amendments to FX regulations is just part of a broader thrust for a better organized FX market. Over the medium term, we shall be rolling out a sequence of reforms that will increase FX market transparency, improve price discovery, and enhance market conduct.

With these reforms, we hope to encourage FX flows from the parallel market to the formal market. Even as we strengthen oversight over Money Service Businesses (MSBs), we will streamline FX requirements for the banking system to reduce market fragmentation and increase FX liquidity. This allows individuals and businesses greater and easier access to foreign exchange.

Ultimately, a deeper FX market will enhance resilience of our domestic economy against external shocks. The goal is to increase its ability to absorb large flows even as the BSP continues to pursue a market-determined exchange rate and allow greater exchange rate flexibility.

We believe competitiveness can also be achieved on the firm and country-level through development of alternative sources of funding. In this regard, we are collaborating with other government agencies and private stakeholders to take measures to deepen our domestic debt market so that you, our esteemed businessmen and exporters can have a viable alternative to bank borrowing, supportive of economic growth.

Taken together, the FX and domestic debt market development initiatives are game changing reforms as these will increase availability of more financial products, especially hedging instruments. This is something that will benefit exporters, since hedging products can help protect you against interest rate and FX volatility. Hedging allows you to focus on your core business.

Another major reform we are pursuing is the digitization of the financial system.

Last November 8, 2017, the Philippine Electronic Fund Transfer (EFT) System and Operations network, also called PESONet, was launched at the BSP. The PESONet is the first Automated Clearing House (ACH) under the National Retail Payment System (NRPS). The NRPS lays down the principles that guide BSP's strategic initiatives to modernize our retail payment system and to shift from a cash-heavy to cash-lite digital economy.

The PESONet will be the electronic alternative to the paper-based check system. Businesses will be able to conveniently transfer funds maintained with banks and other non-banks such as electronic money issuers to any other account in our financial sytem. Full inter-operability. Good for payroll. Good for paying suppliers. Good for paying utilities and other services. In addition to the convenience of inter-operability, PESONet allows funds to be made available within the same banking day. This provides better liquidity management opportunities for private businesses. Moreover, payees receive the transferred funds in full and do not pay fees for electronic credit to their accounts. Indeed, costs will go down as we move away from a cash-heavy economy.

We are also working on the launch of another priority ACH, the real-time low value push payment scheme called InstaPay. InstaPay is designed to facilitate small value payments and enable merchants to accept digital payments from customer on real-time basis using cards or any digital device, especially a mobile phone scanning a QR code.

At the BSP, we have strategically opened up the banking system to competition. For instance, since the enactment of the Foreign Banks Liberalization Law in 2014, the Monetary Board has approved 11 foreign bank applications. Further, as early as 2004, we have adopted a "test and learn" approach, now called regulatory sandbox, to allow fintech innovations into our system. This approach encourages competition coming from new players, whether from banks or non-banks such as fintech companies.

Why is competition important? Healthy competition can make services more affordable, and expand consumer choices. The bottom line is that competition motivates banks to work harder to serve their customers. Banks are encouraged to go beyond just serving big blue-chip enterprises and companies. With greater competition, banks are compelled to be creative, be innovative, and go deeper into the market to work harder to better serve the public. Ultimately, increased competition increases financial inclusion. MSMEs will be a big winner.

Concluding remarks

Last Wednesday marked the conclusion of the 31st Association of South East Asian Nations (ASEAN) Summit and the Special Celebration of ASEAN's 50th anniversary. All throughout the year during various ASEAN related meetings, collective calls for partnership and greater economic integration were made. I came to Cebu directly from Singapore wher I signed a fintech cooperation agreement with my counterpart. Deepening our economic ties, as shown by rising intra-regional investments and intra-regional trade in final goods within Asia, is critical not only to cushion the potential negative impact of policy uncertainties from the global market, but also achieve and maintain our external competitiveness.

Here at home, greater collaboration and cooperation among ourselves – private businesses, firms and government agencies – will reinforce our competitive position. As you know, the BSP actively engages exporters through the regular conduct of the Conference on Gearing Up for External Competitiveness (CGUEC) and the annual Exporters' Forum. We also conduct consultative one-on-one meetings. These serve as venues for discussing prospects, as well as plans and initiatives for the sector. In fact, we held one conference here in Cebu last May 2017. This was followed by a series of consultation meetings with some of Cebu's top exporters of furniture, processed fruits, and garments in June 2017.[2] We hope to continue this active partnership with you.

On behalf of the Monetary Board and the BSP, I congratulate PhilExport for its 25 years of helping exporters succeed in international trade, and taking the lead in building strong alliances among export-related industries, government agencies, and non-governmental organizations. Daghang Salamat at mabuhay tayong lahat!

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1 Quoted actual exports numbers are latest available from the Philippine Statistics Authority.

2 Note: The Cebu-based firms/associations consulted by the BSP in June 2017 were the Cebu Furniture Industries Foundation, Inc., 7D Foods International, and Metro Wear, Inc.