

Nestor A Espenilla, Jr: Revisiting the role of rural banks in countryside development and financial inclusion

Speech by Mr Nestor A Espenilla, Jr, Governor of Bangko Sentral ng Pilipinas (BSP, the central bank of the Philippines), at the 65th Annual Convention and General Membership Meeting of the Rural Bankers Association of the Philippines (RBAP), Davao City, 21 May 2018.

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Davao City Mayor Sara “Inday” Z. Duterte, Secretary of Finance Carlos G. Dominguez, PDIC President Roberto B. Tan, Land Bank President Alex Buenaventura, RBAP President Giovanni D. Gabriento, RBAP members, colleagues from the Bangko Sentral, fellow workers in government, esteemed guests, ladies and gentlemen, a pleasant good morning to everyone!

I am honored to visit Davao again, for RBAP’s 65th Annual Convention and General Membership Meeting. It is always a pleasure to see and appreciate the city’s beauty. I also look forward to sampling some durian. And as Mayor Sara said, let us support Davao’s Buy Buy Buy to support the local economy.

I commend the outgoing set of RBAP officers and directors for their commitment and exemplary performance to promote a sound rural banking industry. RBAP’s milestones under your leadership are vital to promoting broader countryside development through financial inclusion. Your consistent service to our farmers, fishermen, and MSMEs has become RBAP’s trademark of service excellence.

I remember during last year’s charter anniversary symposium in October, we talked about how rural banks have become customers’ best financial friend or BFF¹. Now, we celebrate how rural banks are #LODIs in bringing necessary financial services to the underserved, unserved, and unbanked Filipinos.

This term “LODI” is Filipino millennial speak for “IDOL” and takes off from your theme, “Leading onwards to development and inclusion #LODI.” To me, this theme indicates the industry’s willingness to reposition itself to the growing needs of a new breed of financial customers and to leverage on digital financial technology to advance economic development and financial inclusion objectives. That you have one of the youngest RBAP presidents to steer the rural banking industry into this direction is very promising.

Rural Banks as #LODIs for Financial Inclusion

Rural banks have proven themselves to be LODIs in their own right — exemplary models of customer outreach, demonstrating a genuine commitment to bringing progress to rural areas. Rural banks may be smaller in size compared to commercial and even thrift banks, but they have proven their mettle and invaluable contribution to countryside development through financing of rural communities.

With RBAP’s extensive network of 2,745 banking offices nationwide, the industry is strategically positioned to be a catalyst for greater financial inclusion. Your close ties and familiarity with the rural communities you serve make you effective providers of rural financing and other corollary microfinance products and services. Almost 97 percent of the industry’s network is spread across provinces. In fact, one in every three banking offices located in Davao Region and in Mindanao is a rural bank.

However, there is much scope for expansion towards countryside development. 554 cities and municipalities, or almost a third of the total, in the country are still unbanked as of December

2017. Moreover, the 2017 Global Findex by the World Bank showed that only 34.5 percent of Filipino adults have formal accounts, ranging from bank deposits to e-money accounts.

Given RBAP's strategic role and familiarity with rural communities, it is crucial for the industry to leverage on innovative technologies and liberalized branching rules that BSP has initiated. This will further expand market reach and enhance existing service delivery channels in the rural areas.

That rural banks enjoy public trust and confidence is evident in your deposit profile. Accounts maintaining less than P10,000 make up 87.3 percent of your retail depositors.

As a conduit of rural financing, almost a third of your loans are granted to households. Most of them are salary loans to the working class, with farmers and fisherfolks among the biggest recipients of rural bank loans. No less important, these are quality loans. Because of this, your return on equity was solid at 9.0 percent in 2017, when net profit stood at P3.4 billion for the year.

These strengths affirm your status as a dependable partner in helping rural communities and in building a more dynamic and inclusive financial system – a system where there is effective access to a wide range of financial products and services that are appropriate to the needs of the local communities.

Consistent with the government's thrust under the Medium-Term Philippine Development Plan (MTPDP) to spread economic development to the countryside, there are now more opportunities for rural banks to grow and provide the financing needs of their clientele.

As the economy grew more than six percent for the last six years (6.7 percent in 2017), the latest GDP data likewise showed that the National Capital Region (NCR), at 6.1 percent, grew less than the national average. This certainly means that economic activities in the provinces are expanding and growing.

In recent years, the Davao Region has consistently posted growth above the national average, being the second fastest growing region of the country in 2017, at 10.9 percent GDP growth.

We are counting on our rural banks to assist in further bringing about economic progress to the rural communities.

BSP's Reform Agenda for an Inclusive Banking System

For our part, the BSP remains strongly committed in providing an enabling regulatory environment for the overall safety and soundness of the banking system. We always emphasize the importance of prudent banking operations, highlighted by strong capitalization and adequate liquidity position as buffers against unforeseen shocks. We also continuously encourage banks to aspire to the highest standards of corporate governance and risk management; to go beyond just complying with banking regulations so you can proactively respond to emerging banking developments and challenges.

As part of continuing reforms, the BSP approved the adoption of minimum prudential liquidity requirements (MLR) for stand-alone thrift banks, rural banks, cooperative banks, and quasi-banks. These requirements are designed to enhance covered institutions' resilience to liquidity stress events and is a significant step in aligning our supervisory framework with international standards. It also illustrates the BSP's commitment to the application of proportionality in our approach to supervision.

We also wish to leave no banking institution behind. Together with the Philippine Deposit Insurance Corporation (PDIC) and the Land Bank of the Philippines (LBP), we have re-launched the Consolidation Program for Rural Banks. This will further strengthen the industry through

stronger financial condition, enhanced management and governance, more synergies and economies of scale, and wider market reach.

The continuing prudential reforms have given us the confidence to further liberalize our rules to allow more business with operational flexibility. Towards this end, we allowed banks to utilize cash agents as cost-efficient service delivery channels. Rural banks can now establish branch-lite units to offer a defined set of services with less regulatory requirements. The framework for basic deposit account further enhances the smooth onboarding of unbanked clients.

I am happy to share also that the BSP has made significant inroads with the implementation of the National Retail Payment System (NRPS). The NRPS implements our commitment to upgrade the country's retail payment system by promoting electronic retail payments and facilitating inter-operability for faster settlement of transactions.

The NRPS will facilitate our transition from being a cash-heavy to a cash-lite economy. This will eventually bring benefits to the economy – in terms of speed and efficiency of transactions, reduced costs, improved transparency, enhanced security, and expanded access to financial services.

Last April, we launched Instapay, the second automated clearing house under the NRPS following the launch of PesoNet. Via InstaPay, Filipinos can enjoy safe and affordable account-to-account electronic retail payments in real-time. Transactors may send and receive funds or make payments in real time of up to P50,000 per transaction. The transferred funds are instantly received in full as no fee is charged for the electronic crediting of funds to the receiving party's account in InstaPay participating institutions. There is no reason why rural banks should not want to be part of PesoNet and Instapay.

Leveraging on Technology and Value Chains

With the digital transformation of the banking system, we, at the BSP, are optimistic that the rural banking industry can emerge as a strong and dependable delivery channel in the provision of banking services. It can do so by taking advantage of available technology.

Opportunities for growth may be seized should you cater to the needs of the young generation. Studies show that fintech has great potential to transform financial services given the country's young demographic profile.

According to the World Bank Findex, 23.5 percent of our population are composed of young adults (between 15 to 24 years old). The domestic digital money ecosystem certainly needs players, big and small, to meet the exacting demands of this new breed of clients.

On this note, I am happy to report that one rural bank is already pilot-testing a cloud-based banking solution in managing its day-to-day operation more effectively and serving its clients more efficiently, thereby upgrading its competitiveness.

Meanwhile, several banks, including rural banks, and non-bank financial institutions are already utilizing the Lendr platform to facilitate credit origination processes. Still others are hooked up with a commercial bank on a block chain pilot.

Rural banks can also certainly leverage on technological innovations and value chains to contribute to the growth of the agricultural sector. This sector certainly needs a helping hand from its #LODIs.

Rural banks have been entrusted by the law with the vital and noble role of serving the financing needs of farmers, fisherfolks and the people of rural communities to achieve inclusive economic growth. We believe that with an increasing recognition of the necessity for innovation, coupled

with proximity to and intimate knowledge of the market, rural banks can now, more than ever, reinvigorate and blaze new trails for agriculture financing in the country.

Innovations enabled by digital technology and value chain approach can not only make agri-financing more viable but also unlock new opportunities for rural banks to deliver a whole range of financial services catering to the unique needs of farmers and their communities. Tapping these opportunities and backed by a solid culture of governance, rural banks can evolve into these valuable full-service community banks – a true pillar of countryside development.

Towards this end, we have been promoting value chain financing through guidelines and incentives (as contained in Circular No. 908). The Agricultural Value Chain Financing Framework provides an opportunity to improve the lives of 10.9 million Filipinos employed in the agriculture industry, as well as MSMEs that are engaged in production and related activities such as processing, distribution and trading. Furthermore, we have been supporting programs that build awareness and capacity, including last year's 2-day agri-value chain conference and the publication of an ongoing study, as funded by the Asian Development Bank. This study can serve as an important reference and guide for banks wishing to implement agri-value chain financing.

The areas where rural banks can incorporate fintech in their operations are wide open. Let us embrace responsible use of technology and innovation to become better bankers.

Closing Remarks

In closing, I wish to express BSP's appreciation to RBAP for its enduring commitment to support its members. It is this support that helps enable our rural banks to offer quality banking services to their constituencies.

With this mission in mind, the next generation of RBAP leaders can further enhance the rural banking industry's resilience to meet the challenges of a rapidly evolving financial services industry. Congratulations to the new leaders of RBAP!

I trust that RBAP will remain as the BSP's proactive and staunch partner in expanding touch points and in digitizing more products and services to onboard more of our countrymen into the banking and financial system.

Maraming salamat. Mabuhay ang RBAP! Mabuhay ang rural banking! Mabuhay ang Pilipinas!