

## **Benjamin E Diokno: The road to financial inclusion and sustainable economy**

Speech by Mr Benjamin E Diokno, Governor of Bangko Sentral ng Pilipinas (BSP, the central bank of the Philippines), at the Philippine Exporters Confederation, Inc. (PHILEXPORT) 3rd General Membership Meeting, Manila, 16 August 2019.

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To Chairman Paterno Dizon, Dr. Sergio Ortiz-Luis, Jr., President, officers and members of PHILEXPORT; colleagues from the government; partners in development; and distinguished guests: good morning.

I am pleased to join you for the 3rd General Membership Meeting of PHILEXPORT as we recognize the country's export industry as a key driver of growth and employment generation.

I am equally pleased be invited to speak on financial inclusion and economic growth. By bringing financial products to the unserved and underserved, we can empower them and at the same time, nurture economic activity and invigorate static industries by linking businesses to new and untapped markets. I also believe that financial inclusion is vital in bringing about a sustainable economy.

For this occasion, allow me to tell you about the BSP's financial inclusion journey, which has been filled by highlights, milestones, and interesting developments. It is, however, by no means a smooth sailing one – we at the BSP are aware of the challenges to serving the financially excluded that persist until today.

Nevertheless, as I recount BSP efforts and share our current initiatives, I hope you will realize new opportunities for enterprise and collaboration. I also hope to drive the message that our recognition of micro, small, and medium enterprises (MSMEs) lies at the heart of our steadfast push for financial inclusion.

The BSP financial inclusion journey started in the 2000s with the adoption of microfinance as a flagship program for poverty alleviation. This was reinforced by the General Banking Law of 2000 that recognized microfinance as a unique banking activity.

When the BSP embraced microfinance as an advocacy, it sought to expand access to credit among the entrepreneurial poor (e-poor). The BSP has always believed in the viability of the country's e-poor as a market segment, especially when they are provided with financial products and services appropriate to their needs and capacities. Such mindset has led BSP to issue over 40 microfinance-related circulars and foster an enabling regulatory environment.

The BSP's microfinance work gradually expanded into financial inclusion. In fact in 2007, the BSP was the first central bank in the world to establish an inclusive finance unit.

Today, financial inclusion is not merely an institutional advocacy—it is a strategic imperative. Our amended charter states that we in BSP should increase access to financial services and consider the interest of the general public.

But BSP cannot do it alone. BSP has to reach out and collaborate with various stakeholders to synergize all efforts in financial inclusion.

BSP is spearheading the implementation of the National Financial Inclusion Strategy (NSFI), an important mechanism for multi-stakeholder coordination of financial inclusion initiatives.

As the principal driver of the NSFI, the BSP serves as Chair of the 17-agency Financial Inclusion Steering Committee (FISC) which adopted MSMEs and agriculture as priority sectors.

This is because we recognize the immense potential and unique challenges of MSMEs. Together with agriculture, MSMEs form the backbone of the Philippine economy. In fact, MSMEs account for 99.6% (911,768) of the country's enterprises and generate 61.6% of employment.

Despite having considerable growth prospects and being a source of livelihood for millions of Filipinos, the MSME sector has not realized its potential. MSMEs only account for 3.32% of the country's gross domestic product (GDP), while their gross value added (GVA) sits at 35.7%. Capital investment remains low, with MSME loans in the banking system accounting for only 6.2% and 9.2% share in total business loans.

Knowing that a significant number of members of Philexport are MSMEs, I'm sure you know that the lack of access to credit remains a fundamental obstacle to the further development and sustainability of our MSMEs.

On the supply side, issues include the prevalent perception that MSMEs—compared to the corporate and consumer markets—are low-profit and high-risk. This aggravates the lack of understanding of the MSME segment. It results in the scarcity of appropriate financing products and inability of banks to cater effectively to MSMEs.

On the demand side, MSMEs are reluctant to approach banks due to the lack of collateral and credit history needed for loan application. They have limited business capacity and financial management skills to capably meet loan requirements. In addition, they have limited knowledge of alternative modes of financing.

Recognizing these challenges, the BSP is set on strengthening the country's financial infrastructure, supporting innovation, and bridging the information gap.

To build the foundation for a robust financial infrastructure, we work in close coordination with government agencies and partners in development.

Let me go through each one briefly.

The BSP has been working with the Credit Information Corporation (CIC) in building a strong and reliable credit information system. Likewise, we are working with the Government of Japan to establish a Credit Risk Database (CRD) that will produce scoring models predicting the creditworthiness of SMEs to help improve their access to finance through risk-based lending and lessen the dependence of banks on collateral.

The BSP also supports law relevant to financial inclusion. One of which is the Philippine Identification System Act (PhilSys Law, RA 11055) passed in August 2018. This will overcome the problem of the lack of verifiable identity documents faced by many Filipinos.

Meanwhile, the Personal Property Security Act (PPSA, RA 11057) – also passed in August of last year – will enhance the access of MSMEs to business and consumer credit by enabling the use of alternative collateral such as equipment, inventory, and warehouse receipts.

Following these developments, the BSP is also supporting the passage of a new Warehouse Receipts Law, as well as the review and amendment of the Agri-Agra Reform Credit Act of 2009 (RA 10000). The introduction of updated and more flexible provisions in these laws would help MSMEs, especially those that are agriculture-related, to gain access to credit; leverage innovative models; and induce banks to venture into MSME and agriculture financing with better terms and standards for compliance.

In addition to lending legislative support, the BSP implements the Credit Surety Fund (CSF) together with the Cooperative Development Authority (CDA). The CSF program enables cooperatives, businessmen, and MSMEs to boost their credit worthiness by providing surety cover of up to 80% for bank loans. As of September 2018, there are 54 CSFs throughout the country with over 17,000 loan beneficiaries.

In 2015, the BSP also launched the National Retail Payment System (NRPS, Circular 980). As part of this, PESONet and InstaPay were launched in 2017 and 2018 with the aim of boosting interoperability among banks and propelling electronic retail payments to at least 20% by 2020. As of December 2018, there are 47 participating institutions for PESONet and 36 for InstaPay.

PESONet transactions reached approximately PHP 86.8 billion while InstaPay transactions totaled approximately PHP 8.2 billion. We foresee a healthy rise in these figures with greater use of the funds transfer schemes by the public. And I encourage everyone here to try and make use of these systems.

Towards achieving financial inclusion in the country, the BSP likewise continues to champion innovation.

In 2014, the BSP issued Circular 855 on risk-based lending, which provides banks the latitude to focus on capacity to pay rather than collateral, waives documentary requirements (e.g., income tax return and financial statements) for microfinance loans, and provides reasonable loan options for start-up businesses.

In 2016, the BSP issued Circular 908 on the agriculture value chain financing (AVCF) framework, which identifies guidelines and incentives for banks planning to engage in AVCF. This policy was designed to encourage banks to adopt new financing approaches so that much needed funds can be directed towards enterprises in the ambit of the agriculture sector.

As part of the push for AVCF, the BSP has pursued a number of projects in recent years. These include the conduct of a study and forum on AVCF.

This year, the BSP will be undertaking a pilot AVCF project for selected banks and value chain commodities, with the aim of building the technical capacity of banks in AVCF and optimizing existing government programs on value chain development.

By aligning with priority commodities for this project, we hope that further development can enable the country's participation in regional and global value chains. The project is set to be launched in September.

In the last two years, the BSP has also created a policy package to address the commonly cited barriers to participation in the formal financial system, such as the lack of funds, documentary requirements, and means to travel to financial institutions. These policies aim to help the unserved and underserved establish a financial footprint that would enable them to avail of and maximize products and services in the market.

In 2017, the BSP issued a pair of regulations: Circular 940 on cash agent operations and Circular 987 on the establishment of branch-lite units (BLUs). These policies were crafted with the goal of expanding the network of low-cost touch points to efficiently deliver financial products and services to the public.

Cash agents and branch-lite units, with their high visibility and convenient setup and functions, allow small business owners and country folk to save on time, travel, and transaction costs.

There are currently 1,874 BLUs and over 40,000 cash agents actively operating in the country.

In February last year, the BSP issued one of its most pivotal policies for financial inclusion –

Circular 992, which outlines the framework for Basic Deposit Accounts (BDA). By easing financial and documentary requirements, the BDA aims to encourage account ownership among the country's unbanked and low-income population, and provide them an entryway into the country's financial ecosystem.

Since the issuance of Circular 992, the BDA has garnered considerable interest from the public and key industry players. To date, there are 77 banks offering BDA. We hope and expect an even greater take-up in the coming years as the BDA enters the market mainstream.

With the advent of the digital age, the BSP has also turned to innovation to take central banking to the next level. As a regulator, we strive to stay ahead of the curve and keep abreast of industry developments and trends.

The BSP was in fact one of the early adopters of the "test-and-learn" approach, which has allowed the entry of pioneering technologies, business models, and products such as e-money into the domestic market. The test-and-learn approach remains a cornerstone of our innovation mindset and enduring pursuit of an enabling regulatory environment.

As the BSP leverages on digital technology to fast-track financial inclusion, it continues to open doors to new players such as fintechs that can diversify and transform the market, as well as pave the way for the banking industry to make the technological leap forward by laying the regulatory groundwork for digital financial services (DFS).

In 2017, the BSP endorsed the country's first cloud-based banking project for one of the largest rural banks in Mindanao. I am pleased to share that this project has been very successful.

The bank now fully operates on a cloud-based system and has also participated in a cross-border remittance scheme. We see this project as a model for large-scale replication and one that will encourage greater receptiveness to banking innovations.

In February this year, the BSP issued Circular 1033 to streamline the licensing requirements of our supervised institutions intending to offer electronic payment and financial services (EFPS).

These initiatives, together with the passage of the National Payment Systems Act (NPSA, RA 11127) that grants the BSP with regulatory oversight over payment systems, will significantly advance our digitization agenda.

But in order for these developments and initiatives to be relevant, there needs to be a systematic collection and dissemination of relevant data, one that would inform policymaking and lead to a better, deeper understanding of the MSME market.

With this in mind, we have embarked on two initiatives designed to bridge the information gap – the national demand side survey on MSME finance and the strategic partnership with the Department of Trade and Industry (DTI), Microfinance Council of the Philippines, Inc. (MCPI), and Alliance of Philippine Partners for Enterprise Development, Inc. (APPEND) to expand the Negosyo Center financing ecosystem.

The national demand side survey on MSME finance, which is currently under development, will enable us to address the need for comprehensive data on the MSME sector and formulate responsive policies and programs.

Meanwhile, an essential component of the Negosyo Center partnership is the creation of an information database on Negosyo Centers and microfinance institutions (MFIs) nationwide. This database will enable Negosyo Centers to refer clients to various financing options and help microfinance institutions design products and services appropriate to clients' needs.

Finally, let me say this again. Financial inclusion is a necessary condition for a sustainable

economy. To realize this vision means pursuing change and reform however difficult they may be. The BSP's enduring financial inclusion journey attests to this. We craft our policies not only for the present, but also with the future in mind.

I am optimistic that the various financial inclusion initiatives of the BSP that I discussed this morning will help improve access of MSME exporters to financial services, and consequently enhance our country's export competitiveness.

With these thoughts, let me say that the best for all of us is yet to come. Maraming salamat po.