

**DG's Speech for the
RBAP's 64th Charter Anniversary Symposium**

**“Rural Banks: Economic Frontliners of
Countryside Development”¹**

10 November 2021, 3:10PM to 3:30PM

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Honorable Vice President Leni Robredo, Secretary William D. Dar of the Department of Agriculture, officers and members of the Rural Bankers Association of the Philippines (RBAP) under the leadership of Atty. Albert T. Concha, Jr., distinguished speakers, esteemed colleagues from the banking industry, ladies and gentlemen, a pleasant afternoon to all of you!

First of all, allow me to congratulate the RBAP on its 64th Charter Anniversary Symposium! Your theme, “**Rural Banks: Strengthening the Economic Frontliners of the Countryside**,” truly captures the pivotal role of rural

¹ Speech delivered by Deputy Governor Chuchi G. Fonacier, Financial Supervision Sector, during the Rural Bankers Association of the Philippines (RBAP)'s 64th Charter Anniversary Symposium via zoom videoconference on 10 November 2021.

banks in countryside development and in the promotion of the BSP's financial inclusion agenda especially during the COVID-19 pandemic.

During this difficult time, the frontliners are our modern-day heroes for the significant role they play in our collective fight in this health crisis. The employees and officers of rural banks are one of the modern-day heroes. They stand as one of the economic frontliners for countryside development by extending the necessary credit and financial access to the underserved and vulnerable rural communities. On this note, I commend the rural banks for building strong relationships with the communities they serve and for taking proactive initiatives to continuously support the rural economy, even during crisis.

Rural banks have been the primary access point to financial services for individuals living in hard-to-reach areas. Indeed, you are at the core of economic growth supporting farmers, fisherfolks and micro-, small and medium entrepreneurs. In spite of having the thinnest slice of the banking system's loan portfolio, rural banks were able to cater to the needs of these key economic drivers – the backbone of the Philippine economy.

Equipped with an in-depth knowledge and geographic familiarity of the countryside service areas, and a vast network of more than 3,000 banking offices nationwide, rural banks could further facilitate countryside development through the optimal use of digital technology and financial innovations.

For this afternoon, allow me to cover three (3) areas for the rural banking industry. First, I will provide a

snapshot on the condition and performance of the rural banking industry. Second, I will discuss how rural banks' familiarity and geographical locations make you an ideal conduit for the efficient provision of financial access in the countryside. Lastly, I will underscore how the BSP considers the RBAP as its partner in providing an enabling environment for countryside development.

A Snapshot of a Sound and Stable Rural Banking Industry

To put things in perspective, I am happy to share that the rural banking sector remains sound and stable even in the midst of the pandemic.

For the first half of 2021, total assets of rural banks continued to expand and reached P272.6 billion level.

Loans² accounted for more than half of the total resources at 52.8 percent. The assets growth was funded by the double digit increase in deposits of P204.8 billion. Deposits were mostly savings account³ and sourced largely from individuals⁴. There is continued trust in the rural banking industry amid the pandemic as number of deposit accounts increased by 23.7 percent to 14.7 million accounts as of end-June 2021 from end-December 2019.

As economic frontliners, rural banks continued to extend credit recording an annual growth rate of 8.5 percent. The industry's loan portfolio were channeled mostly to individuals for household consumption⁵, wholesale and retail trade⁶ and agriculture, forestry and

² Refers to gross total loans of P143.9 billion.

³ This represents 77.9 percent of total deposits.

⁴ This represents 87 percent of total deposits.

⁵ This represents 36.3 percent share.

⁶ This represents 20.9 percent share.

fishery⁷, accounting for 71.7 percent of the rural bank industry's total loans.

The slowdown in economic activities has affected the industry's loan quality as non-performing loan (NPL) ratio rose to 13.7 percent. This is confirmed by the results of the latest Banking Sector Outlook Survey where respondent rural banks expect elevated NPL ratios over a two-year horizon.

Nonetheless, the rising soured loans remain manageable with NPL coverage ratio at 59.7 percent as of end-June 2021. The operationalization of the Financial Institutions Strategic Transfer or FIST Act⁸ will likewise reinforce financial institutions, including rural banks, to manage their non-performing assets level. This will

⁷ This represents 14.5 percent share.

⁸ Under Circular No.1117 dated 27 May 2021.

translate into new funding sources that could be extended to households and micro, small and medium enterprises.

Rural banks have also maintained ample levels of capital and liquidity registering well-above the required minimum of 10 percent capital adequacy ratio and 20 percent minimum liquidity ratio, respectively. Moreover, the industry's capital adequacy ratio stood at 12.0 percent after an assumed 20 percent write-off rate was applied to the industry's top three economic sector exposures.

In terms of earnings, industry figures fared better with high return on assets, return on equity and net interest margin of 1.4 percent, 7.5 percent, and 9.5 percent, respectively, for the first half of 2021.

Let us be guided by these data as we review and reset business strategies to remain resilient amid the increasing competition and evolving financial system landscape.

Expanded Reach as Economic Frontliners in the Countryside

The remote location of rural areas is one of the main factors that limit people's access to formal financial institutions. This means that access to financial products and services in the country particularly in the rural areas remains a huge challenge.

In this regard, rural banks are well positioned to respond to this challenge given their geographic advantage and expansive network⁹. While bigger banks

⁹ As of end-September 2021, there are 400 rural banks with a collective network of 2,801 branches.

are concentrating in highly urbanized and densely populated regions of the Philippines such as the National Capital Region, CALABARZON and Central Luzon, rural banks are thriving in regions where there is less access to financial services. In Cagayan Valley, MIMAROPA, Bicol, CARAGA and Cordillera, there are more rural banks compared with other bank types.

Rural banks are also the frontrunners in the establishment of branch-lite units¹⁰, particularly in unbanked cities and municipalities in the country, which currently remain at 30.5 percent as of end-June 2021¹¹.

Rural banks have the familiarity of the local community that other bigger players do not possess. Hence, rural banks can explore untapped opportunities

¹⁰ Branch-lite units were introduced to enable banks to have a presence in areas where it is not economically feasible to establish a full-blown branch.

¹¹ Source: Financial Inclusion Office (FIO)

in unbanked municipalities whose level of economic activity is high. For instance, 15 percent of unbanked areas in the country are 1st to 2nd class municipalities as of end-June 2021¹². These areas will surely benefit from financial intermediation to sustain the local economic growth and boost consumption and productivity.

The value of person-to-person contact will surely remain. Rural bankers can leverage on this position of strength: the relationship edge and market familiarity that you have established with rural communities through the years.

However, as we promote digital transformation in the financial system, we welcome efforts to increase capacity of rural banks in the digital financial ecosystem.

¹² Source: FIO

Rural banks can take advantage of fintech solutions to enhance operational efficiencies and customer experience. Such adoption of technology can therefore improve bottom-line figures and at the same time leapfrog financial inclusion agenda. For instance, there are rural banks that switched to cloud-based core banking solutions, and this has helped in the customer base expansion.¹³ There is also a growing network of rural banks partnering with fintech firm and remittance centers to facilitate an easy, secure, and convenient way of transferring funds and making payments backed by a distributor ledger technology (DLT)-based platform.¹⁴ Indeed, technology can be used as a tool to ultimately enhance customer relationships by enabling rural banks to be more responsive to the needs of rural customers as well as at par with market trends.

¹³ <https://www.adb.org/sites/default/files/publication/736741/cloud-based-core-banking-philippines.pdf>

¹⁴ <https://www.manilatimes.net/2020/11/30/public-square/unionbank-continues-digitizing-more-rural-banks/802882>

As the industry employs the mix of physical branches and fintech solutions to better serve financial consumers, there should be efforts to make this sustainable backed by good governance and effective risk management systems of banks.

The BSP's Enabling Regulatory Environment

And the BSP is your partner as we remain committed in providing an enabling regulatory environment, one that subscribes to the principle of proportionality, affords banks with flexibility to take risks within regulatory perimeters, and provides various opportunities to be more responsive to the evolving needs of banking clients.

We are pursuing key enabling policy initiatives that support sustainable expansion of the scope, scale and reach of digital financial services, especially to the most vulnerable segments of the population.

With the Open Finance Framework implementation, we anticipate the emergence of new business models and arrangements that will further push innovation and add value to customers. We are exploring the potential adoption of a “marketplace banking model”. The said model will be underpinned by a sound governance and risk management system, including an effective information sharing arrangement to ensure that attendant risks are adequately managed, and consumer interests are protected.

We will likewise formalize our “test and learn” approach or what we call the “regulatory sandbox”. We

have always adopted a balanced approach to innovation where pioneering technologies can be tested in a live, yet controlled and structured environment whereby potential benefits and risks are clearly demonstrated. The key elements of the regulatory sandbox include, among others, the eligibility requirements, oversight framework, and testing parameters.

The BSP is also drafting guidelines on fraud management systems of BSP-supervised financial institutions (BSFIs). As cyberthreat attacks continue to rise and evolve, we expect our supervised entities to adopt more robust systems to protect their infrastructure and proprietary and customer data as well as to ensure continuous delivery of financial services.

Aside from issuance of enabling regulations, the BSP is your partner in capacitating the industry in view

of emerging market trends. The BSP has embarked on cybersecurity awareness campaigns to equip financial institutions and alert the public of emerging cyberthreats and scams. The BSP has ongoing Financial Learning Seminars all over the country to educate the public. We also develop and manage content for *PisoLit* on social media, as well as create primers, advisories, and information materials for sharing with partners and the public. Lastly, the BSP Online Buddy or BOB for short was operationalized to handle financial consumer complaints and frequently asked questions on the BSP website.

On the area of sustainable finance, we recognize that banks are in varying degrees of implementation of sustainable finance. Several banks still lack understanding or have identified the lack of expertise or skill as a barrier to pursuing sustainable finance. The BSP

has rolled out and will continue to provide capacity building activities to deepen knowledge and enhance or develop skillsets of the banking community in relation to the management of environmental, social and governance (ESG) and climate risks. We view that understanding the climate and other environment-related risks will unlock the opportunities for banks and translate the same to further scaling up of green or sustainable finance. The recent issuance of the Sustainable Finance Guiding Principles will also provide opportunities and guidance to banks to identifying and financing economic sectors or activities that contribute to sustainable development.

Meanwhile, the BSP is likewise working closely with key government agencies to benefit the rural banking industry. In particular, the Rural Banking Industry Strengthening Program was launched as a holistic

approach aimed at contributing to the improvement in rural banking operations and compliance with relevant laws and regulations. Moreover, the Program will identify training needs in order to enhance skillsets of rural banking personnel and officers.

Through these reform programs and policy initiatives, rural banks will be better-equipped to remain as economic frontliners in the countryside and assist vulnerable rural communities from the adverse economic impacts of the COVID-19 pandemic.

Concluding Thoughts

Ladies and gentlemen of the rural banking sector, in an environment that is rapidly evolving, adaptability is the key.

In closing, allow me to share the famous quote from Jessica Hagedorn on adaptability, she said, ***“Adaptability is the simple secret of survival”***. Adapting to change does not necessarily mean changing your core and losing your relevance. In fact, as the push for financial inclusion continues to intensify, the role of rural banks today is even greater than it was then. Rural banks remain to be a key channel for delivering financial services to the countryside given our archipelagic geography and the challenges associated with it. Embrace this mission and the role which you were given more than six decades ago and nurture it by evolving and adapting to the demands of the times.

Indeed, the RBAP’s role as the unifying voice among rural banks makes you a key partner of the BSP in achieving development in the rural areas. For this reason, the BSP will continue to collaborate and partner with the

RBAP to ensure that our reform initiatives will result to a robust and resilient rural banking sector and a strong economy that fosters sustainable and inclusive growth.

Rest assured that the BSP will continue to create a conducive regulatory environment for digital innovation and financial inclusion to flourish while, at the same time, ensure the effective management of risks.

I wish everyone a fruitful symposium.
Congratulations RBAP! Thank you and Mabuhay!