

“A Brave New World” – Facing Up to the New Competitive

Realities of Rural Banking^{*}

Ms. Marie Aimee Samson-Maramba, President of the Confederation of Central Luzon Rural Banks, Inc. (CCLRBI), officers and members of the confederation, friends in the rural banking sector, ladies and gentlemen, good morning. I would like to thank the confederation for inviting the BSP in your Annual Management conference. This year’s theme, “A Brave New World” – Facing Up to the New Competitive Realities of Rural Banking, is indeed timely as we observe mounting competition in the banking sector at the back of a growing Philippine economy and regulatory reforms liberalizing the market.

As you may recall, back in 2005, the Monetary Board approved the phased liberalization of bank branching policy, effectively lifting the moratorium on the establishment of branches and other banking offices, except for certain “restricted areas”. In 2011, the

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BSP lifted the moratorium on the “restricted areas”, with full effectivity this year. As a result, we see big banks expanding not only within NCR, but also in areas outside NCR, indicating increased competition in the banking industry. These trends reflect the current competitive realities facing rural banking. So, how do we overcome these challenges? Allow me to share the wisdom of Nelson Mandela and I quote: “Courage is not the absence of fear, but the triumph over it. The brave man is not he who does not feel afraid, but he who conquers that fear.”

Increased market competition, particularly from big players, may well be considered by some as a threat to the rural banking industry. Rather than considering this a threat, however, let us overcome this challenge by recognizing that along with competition come opportunities for improving financial services. Rural banks can thrive in this environment by taking advantage of these opportunities. Innovation, technology, new markets and non-traditional delivery mechanisms, when appropriately leveraged and

prudently managed, can increase outreach and revenues, as well as improve services to customers.

Further, as rural banks, you have inherent competitive advantage that cannot be taken away from you. You are strategically located in municipalities where financial services are much needed to support local economic growth. You have intimate knowledge of the local economy and close relationship with the community. This first-hand knowledge of local markets gives you an edge over the bigger players that are already in or are planning to enter your space. While many may fear the entry of these big players, we believe that strength of a bank is not in its size alone. The determinants of success still rest on sound governance, adequate risk management and clear business models that will allow you to maintain efficient operations while seizing opportunities for growth.

The market itself is replete with opportunities. Based on statistics, 610 municipalities are currently untapped by banks. Only

about 2 out of 10 Filipino households have a deposit account (BSP Consumer Finance Survey, 2009) while only about 10.5 percent of Filipino adults obtained a loan from a formal financial institution (World Bank Financial Inclusion Index, 2011).

With 569 head offices and over 2,000 branches dispersed across rural areas of the country, rural banks are ideal access points where people and businesses in those areas can get financial services. In Central Luzon alone, there are 92 rural banks with a network of 891 branches.

These data point to niches where rural banks can focus on, but in order to take full advantage of market opportunities, your institutions have to be strong, stable and well-managed.

At present, there are still market segments that remain underserved or unserved by the banking system. One good example is the Small and Medium Enterprises (SMEs) sector. The SME sector provides a stable source of employment and a more meaningful linkage to broader value-chains and markets.

Considering that Central Luzon is one of the regions with most number of SMEs, rural banks here can be catalysts in finding market-oriented ways that will help support SME lending.

On our end, the BSP remains committed in providing enabling policy and regulatory environment to support the rural banking industry in overcoming emerging challenges. The implementing rules on R.A. No. 10574 allowing foreign equity into the rural banking system, for example, can provide opportunities to form strategic partnerships to increase operational efficiency and improve risk management practices. Other recent issuances include guidelines on compliance, corporate governance and capital adequacy. We have also extended the Strengthening Program for Rural Banks Plus (SPRB Plus) up to the end of this year to allow willing banks to avail of the benefits of this meaningful program.

These regulations are designed to empower your banks to establish the mechanisms within your institutions that are fit to your respective operations. The BSP recognizes that rural banks are

distinct from other types of banks in terms of size, capacities, magnitude of operations and niche markets. These regulations are intentionally calibrated because of such distinctions, in order to provide rural banks with enough space for compliance, as well as adequate opportunities for business improvement. For instance, in the compliance and corporate governance guidelines, we distinguish simple from complex banks, providing more flexibility for simple banks by relaxing various requirements, given their limited scope of operations and resources.

There are many more initiatives in the pipeline aimed at providing banks with more flexibility in pursuing growth, but at the same time strengthening standards of governance and risk management. For instance, we are currently working on a comprehensive framework on credit risk management, including loan loss provisioning. Among others, these guidelines will provide more flexibility in how banks identify their target market, develop loan products, and grant credit on the basis of well-defined criteria,

including the use of available and credible financial statements and other relevant sources of information. At the same time, the guidelines set out BSP's expectations with respect to the comprehensive management of credit risk, commensurate to the bank's credit risk-taking activities. As we prepare to expose these guidelines for comments to the industry, we hope for an engaged interaction and dialogue so that we can fully understand your position and the impact of new standards on your operations, and at the same time allow us to explain the rationale behind the framework. In the end, we recognize that adjustments need to be made in order to further improve the proposed guidelines and make it more reflective of local operating environment.

The BSP envisions a strong, inclusive and competitive rural banking system. As you further discuss the challenges and identify ways of moving the Central Luzon rural banking industry forward, may you come up with innovative solutions and pioneering initiatives that can help you beat the odds and conquer this brave

new world. We look forward to an enduring partnership between the BSP and the Confederation of Central Luzon Rural Banks, Inc. As I close, I'd like to share with you words from Franklin D. Roosevelt:

“Competition has been shown to be useful up to a certain point and no further, but cooperation, which is the thing we must strive for today, begins where competition leaves off.”

More power to the rural banks of Central Luzon. Thank you and good morning.