A Status Report on the Philippine Financial System
This semestral report is prepared pursuant to Section 39(c), Article V of R.A. No. 7653
(The New Central Bank Act) by the Office of Supervisory Policy Development, Supervision and Examination
Sector, Bangko Sentral ng Pilipinas. A synopsis of the report is available online at
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Glossary

A. SELECTED ACCOUNTS

1. **Financial Reporting Package (FRP)** is a set of financial statements for prudential reporting purposes composed of the Balance Sheet, Income Statement and Supporting Schedules. The FRP is primarily designed to align the BSP reportorial requirements with the provisions of the Philippine Financial Reporting Standards (PFRS)/Philippine Accounting Standards (PAS) and Basel 2-based Capital Adequacy Framework. It is also designed to meet BSP statistical requirements.

2. **Total Assets** refer to the sum of all assets, adjusted to net of “Due from Head Office/Branches/Agencies” and “Due to Head Office/Branches/Agencies” of foreign bank branches.

3. **Financial Assets (Other than Loans and Receivables)** refer to the sum of all investments in financial assets, net of equity investments. These include financial assets held for trading (HFT), designated at fair value through profit or loss (DFVPL), available-for-sale (AFS), held-to-maturity (HTM), unquoted debt securities classified as loans (UDSCL) and investments in non-marketable equity securities (INMES).

4. **Equity Investments** refer to equity investments in subsidiaries, associates and joint ventures.

5. For purposes of computing the average, one period covers 12 months.
   a. **Average assets** refer to the sum of total assets as of end of two periods divided by 2.
   b. **Average capital** refers to the sum of total capital accounts as of end of two periods divided by 2.
   c. **Average earning assets** refer to the sum of earning assets as of end of two periods divided by 2.
   d. **Average interest-bearing liabilities** refer to the sum of interest-bearing liabilities as of end of two periods divided by 2.

6. **Financial Liabilities Held for Trading** refer to the sum of derivatives with negative fair value held for trading and liability for short position.

7. **Financial Liabilities Designated at Fair Value Through Profit or Loss (DFVPL)** refer to financial liabilities that upon initial recognition are designated by the bank at fair value through profit or loss.

8. **Unsecured Subordinated Debt** refers to the amortized cost of obligations arising from the issuance of unsecured subordinated debt which may be eligible as Tier 2 (supplementary) capital of the bank, subject to certain terms and conditions.

9. **Re redeemable Preferred Shares** refer to preferred shares issued which provides for redemption on a specific date.

10. **Total Capital** refers to the sum of paid-in capital of locally incorporated banks, assigned capital and the allowable qualified capital component of the net “Due To/Due From Head Office/Branches/Agencies” accounts of branches of foreign banks, other equity instruments, retained earnings and undivided profits, other comprehensive income, and appraisal increment reserves.
11. **Earning Assets** refer to the sum of loans (net of allowance for probable losses) and other financial assets (net of allowance for credit losses and accumulated market gains or losses), net of equity investments.

12. **Interest-Bearing Liabilities** refer to the sum of deposit liabilities, bills payable, unsecured subordinated debt, bonds payable and redeemable preferred shares.

13. **Liquid Assets** refer to the sum of cash and due from banks and other financial assets (net of allowance for credit losses)

14. **Total Operating Income** refers to the sum of net interest income and non-interest income.

15. **Net Interest Income** refers to the difference between interest income, provisions for losses on accrued interest income from financial assets and interest expense.

16. **Provision for Losses on Accrued Interest Income from Financial Assets** refers to the impairment loss on accrued interest income from loans and other financial assets, net of equity securities, charged against current operations.

17. **Non-Interest Income** refers to the sum of dividend income, fee-based income (including income from fiduciary activities), trading income, foreign exchange profits, profits from sale/derecognition of non-trading financial assets and liabilities, profits from sale/derecognition of non-financial assets, profits on financial assets and liabilities DFVPL, profits on fair value adjustment in hedge accounting and other non-interest income.

18. **Dividend Income** refers to cash dividends earned on equity securities held as HFT, DFVPL, AFS and INMES.

19. **Fee-Based Income** refers to the sum of income from payment services, intermediation services, custodianship, underwriting and securities dealership, securitization activities, fiduciary activities and other fee-based income.

20. **Trading Income** refers to the sum of realized gains/(losses) from sale/redemption, and unrealized gains/(losses) from marking-to-market of HFT financial assets, and realized gains/(losses) from foreign exchange transactions.

21. **Non-Interest Expenses** refer to the sum of compensation and fringe benefits, taxes and licenses, other administrative expenses, depreciation and amortization, impairment losses and provisions.

22. **Losses or Recoveries on Financial Assets** refer to the sum of provision for credit losses on loans and receivables and other financial assets, bad debts written off and recovery on charged-off assets.

23. **Income Tax Expense** refers to provision for income tax.

24. **Net Profit or Loss** refers to the difference of total operating income and non-interest expenses, plus (less) the recoveries (losses) on financial assets, share in the profit (loss) of unconsolidated subsidiaries, associates, joint ventures and minority interest in profit (loss) of subsidiaries.

25. **Non-Performing Loans (NPL)** refer to past due loan accounts whose principal and/or interest is unpaid for thirty (30) days or more after due date. This applies to loans payable in lump sum and in quarterly, semi-annual or annual installments, including: the outstanding balance of loans payable in monthly installments when three (3) or more installments are in arrears;
the outstanding balance of loans payable in daily, weekly or semi-monthly installments when
the total amount of arrearages reaches 10 percent of the total loan receivable balance; and
restructured loans which do not meet the requirements to be treated as performing loans
under existing rules and regulations, including all items in litigation. Effective September 2002,
NPLs exclude loans classified as “Loss” in the latest BSP examination which are fully covered
by allowance for probable losses and applicable to a bank with no unbooked valuation reserves and
other capital adjustments required by the BSP (Circular No. 351).

26. **Real and Other Properties Acquired (ROPA)** refer to real and other properties, other than those
used for banking purposes or held for investment, acquired by the bank in settlement of loans
through foreclosure or **dacion** in payment and/or for other reasons, whose carrying amount will
be recovered principally through a sale transaction.

27. **Non-Performing Assets (NPA)** refer to the sum of NPL and ROPA, gross. Effective March 2003,
NPAs exclude performing sales contract receivables, which met certain requirements under
Circular No. 380. Based on the new FRP framework provided for under Circular No. 512 dated
03 February 2006 effective 31 December 2006, NPA should also include non-current assets held
for sale.

28. **Distressed Assets** refer to the sum of NPLs, ROPA, gross, non-current assets held for sale, past
due loans and receivables but not yet non-performing, and current restructured loans. Effective
end-July 2004, performing restructured loans replaced current restructured loans.

29. **Gross Assets** refer to total assets plus “Net of Due to Head Office/Branches/Agencies” of foreign
bank branches, if any, plus allowance for credit losses on loans plus allowance for credit losses
on sales contract receivables (SCR) plus allowance for losses on ROPA minus loans classified as
loss fully covered by allowance for credit losses.

30. **Allowance on NPAs** refers to the sum of allowance for credit losses on loans, allowance for credit
losses on SCR, allowance for losses on ROPA.

31. **Non-Current Assets Held for Sale** refer to ROPAs that are available for immediate sale in their
present condition subject only to terms that are usual and customary for sales of such assets and
the sale must be highly probable.

32. **Sales Contract Receivable (SCR)** refers to the amortized cost of assets acquired in settlement
of loans through foreclosure or **dacion** in payment and subsequently sold on installment basis
whereby the title to the said property is transferred to the buyers only upon full payment of the
agreed selling price.
B. FINANCIAL AND OTHER RATIOS

1. **Capital adequacy ratio (CAR)** refers to the ratio of capital to risk weighted assets computed in accordance with the risk-based capital adequacy framework that took into account credit risks effective 1 July 2001 under BSP Circular No. 280 dated 29 March 2001. Under BSP Circular No. 360 dated 3 December 2002, which took effect on 1 July 2003, the computation of CAR for universal and commercial banks incorporates market risks in addition to credit risks. Under Circular No. 538 dated 4 August 2006, which took effect on 1 July 2007, universal/commercial banks incorporate operational risk in addition to credit and market risks.

2. **Cost-to-Income ratio** refers to the ratio of non-interest expenses to total operating income.

3. **Density ratio** refers to the ratio of the total number of domestic banking offices to the total number of cities/municipalities in the Philippines.

4. **Distressed assets ratio** refers to the ratio of distressed assets to total loans (gross of allowance for probable losses), inclusive of interbank loans, plus ROPA (gross of allowance for losses).

5. **Earning asset yield** refers to the ratio of interest income to average earning assets.

6. **Funding cost** refers to the ratio of interest expense to average interest-bearing liabilities.

7. **Interest spread** refers to the difference between earning asset yield and funding cost.

8. **Liquid assets ratio** refers to the ratio of liquid assets to total deposits.

9. **Net interest margin** refers to the ratio of net interest income to average earning assets.

10. **NPA coverage ratio** refers to the ratio of allowance on NPA to total NPA.

11. **NPA ratio** refers to the ratio of NPA to total assets, gross of allowance for probable losses.

12. **NPL coverage ratio** refers to the ratio of allowance for credit losses on loans to total NPL.

13. **NPL ratio** refers to the ratio of NPL to total loans (gross of allowance for credit losses), inclusive of interbank loans.

14. **Population-to-banking offices ratio (Customer Ratio)** refers to the ratio of the total population to the total number of domestic banking offices.

15. **Return on assets** refers to the ratio of net profit or loss to average assets.

16. **Return on equity** refers to the ratio of net profit or loss to average capital.
The Status Report on the Philippine Financial System is a semestral report prepared by the Office of Supervisory Policy Development, Supervision and Examination Sector, Bangko Sentral ng Pilipinas (BSP), and is submitted by the Governor to the President and the Congress in compliance with Section 39 (c), Article V of Republic Act (R.A.) No. 7653 or The New Central Bank Act.

This report is basically culled from the various periodic reports submitted by BSP supervised/regulated institutions to the Supervisory Data Center, Supervision and Examination Sector. At end-June 2010, BSP supervised/regulated financial institutions consisted of 773 banks with 7,912 branches and other offices, 6,471 non-bank financial institutions (NBFIs) with 8,911 branches and five offshore banking units (OBUs). (Schedule 1)

Effective 3 July 1998, the supervision and regulation of the BSP over non-banking entities were turned over to the Securities and Exchange Commission (SEC) for corporations and partnerships, and to the Department of Trade and Industry (DTI) for single proprietorships, in accordance with Section 130 of R.A. No. 7653, except the following: non-banks with quasi-banking functions and/or with trust or Investment Management Activities (IMA) license, non-banks which are subsidiaries/affiliates of banks and quasi-banks, non-stock savings and loan associations including pawnshops.

Likewise, the supervision and regulation over building and loan associations were transferred to the Home Guarantee Corporation (HGC) effective 7 February 2002, in accordance with Section 94 of R.A. No. 8791 (The General Banking Law of 2000).

Finally, pursuant to Circular No. 512 dated 3 February 2006 (as amended) and Circular No. 644 dated 10 February 2009, and in line with the adoption of the Philippine Financial Reporting Standards (PFRS) and Philippine Accounting Standards (PAS), the BSP amends the Manual of Accounts and the BSP reportorial requirements consisting of the Consolidated Statement of Condition (CSC), Consolidated Statement of Income and Expenses (CSIE) and their supporting schedules issued under Circular 108 dated 9 May 1996 (as amended) for universal and commercial banks, Circular No. 270 dated 19 December 2000 (as amended) for thrift banks, and Circular No. 249 dated 26 June 2000 (as amended) for rural and cooperative banks, through the issuance of the new Financial Reporting Package (FRP) for banks. The FRP is designed to align the Manual of Accounts and the BSP reportorial requirements with the provisions of the PFRS/PAS.
“Key performance indicators for the first half of 2010 showed the sustained strength of banks’ core balance sheet accounts: steady asset expansion, credit growth, growing deposit base, ample liquidity, continuing improvement in overall asset quality and above standard solvency ratios”
The Philippine financial system emerged in reasonable shape from the worst trails of the 2007-2008 global financial crisis and remained largely unaffected as it ran on a steady pace of growth and stability.

During the semester in review, the system endeavored to strategically position itself to overcome all the potential pitfalls of the track but instead enjoyed support from improving external and internal environment. On the external front, sovereign risks in the Euro area particularly the PIIGS (Portugal, Ireland, Italy, Greece and Spain) sovereigns may have remained elevated and tend to decelerate the pace of ongoing stabilization of the global financial system but acute market strains have somewhat cooled down. ‘Safe’ investment choices such as US treasuries, German bonds and gold appreciated in value and overall market volatility relatively subsided for the first half of 2010 (IMF Global Financial Stability Report-Market Update, July 2010).

The local operating environment was similarly favorable. The advent of the new administration following the conclusion of peaceful elections last 11 May 2010 and smooth turnover thereafter generally improved investor confidence and public sentiment for much needed reforms. As of end-June 2010, the Philippine Stock Exchange Index (PSEi), a stopwatch to measure investor and market sentiment, rose by 43.3 percent to 3,311.8 index points from 2,310.3 index points a year ago.

The Philippine economy performed better this semester as it grew on a much faster pace of 7.9 percent from 0.9 percent at end-June 2009. The positive macroeconomic performance was attained on account of healthy remittance inflows from migrant overseas Filipinos (OF) which supported domestic demand particularly for consumer goods and real estate properties. Moreover, BSP’s accommodative monetary policy, benign inflation environment, strong external position as well as a stable domestic currency and financial system all helped to keep market speculations in check and curbed sharp asset price corrections felt in other economies post crisis.

Key performance indicators for the first half of 2010 showed the sustained strength of banks’ core balance sheet accounts: steady asset expansion, credit growth, growing deposit base, ample liquidity, continuing improvement in overall asset quality and above standard solvency ratios. Banks likewise managed to register a positive bottom line on account of cost-efficient operations and maximization of e-banking technologies.

Other Bangko Sentral ng Pilipinas (BSP) supervised financial institutions similarly exhibited sustained resilience on the back of prevailing favorable operating environment.

While the domestic financial system remains largely in good shape, some strength training is still required to continuously build its stamina for the financial stability marathon:

First, banks have to continually reassess their investment portfolio and periodically monitor their exposures as part of effective risk management practice. As of end-May 2010, banks’ exposure to ROPs amounted to P326.4 billion ($7.2 billion). These holdings accounted for 5.2 percent of total assets and 45.3 percent of capital. While ROP prices generally improved on favorable yield differential, i.e., prices for 10-year ROP earned 264.9 basis points to 101.6 as of end-June 2010 from year ago’s 98.9 (Source: Bloomberg), banks’ considerable holdings of ROPs nonetheless expose them to market risk and to some extent, sovereign risk. Banks’ exposures to other sovereign debt, on the other hand, remained minimal at $2.2 billion. These accounted for only 1.6 percent of total assets and 13.9 percent of total capital of the banking system.

Moreover, fiscal consolidation initiatives experienced a slow twitch as the new administration prioritized pump-priming activities for the economy like
Box 1: Basel 1.5 Framework for Stand-alone Thrift Banks, Rural Banks and Cooperative Banks

The so-called Basel 1.5 framework involves the application of higher capital adequacy standards for stand-alone thrift banks (TBs), rural banks (RBs) and cooperative banks (CBs) or those banks that are not subsidiaries of universal/commercial banks (U/KBs). These stand-alone banks are currently covered by Circular No. 280 dated 29 March 2001, as amended, which deals with the risk-based capital adequacy framework under Basel 1.

The Basel 1.5 framework was issued under BSP Circular No. 688 dated 26 May 2010 and shall take effect on 1 January 2012. Unlike the full Basel 2 framework which is a more exacting standard that applies to U/KBs and their subsidiary banks and quasi-banks, Basel 1.5 involves only a few key changes to the existing Basel 1 framework.

Assignment of Risk Weight
On credit risk, the foreign currency (FCY)-denominated credit exposures to the Philippine National Government (NG) and BSP will now carry a 100% risk weight, based on the country’s current sovereign rating of “BB-”, from the existing 0% risk weight. The assignment of the new risk weight will be phased-in over a three-year period, i.e., only 1/3 of the applicable risk weight will be applied starting 1 January 2012, 2/3 starting 1 January 2013 and the full risk weight starting 1 January 2014. Peso-denominated exposures to the Philippine NG/BSP will continue to be 0% risk-weighted.

Meanwhile, exposures to government corporations which carry an explicit guarantee of the NG shall be 0% risk-weighted only if peso-denominated. Those that are FCY-denominated will follow the risk weight of the FCY-denominated exposures to NG/BSP.

Real and Other Properties Acquired (ROPA) shall be assigned a higher risk weight of 150% from the previous risk weight of 100%. The new risk weight shall be gradually implemented over a three-year period, i.e., 115% risk weight shall be applied by 1 January 2012, 130% by 1 January 2013 and 150% by 1 January 2014. The rationale behind this revision is to enable stand-alone TBs, RBs and CBs to reduce the level of their non-performing assets and in the process, strengthen overall asset quality of these banks.

Capital Requirement for Operational Risk
Stand-alone TBs, RBs and CBs shall use the simplest approach or the Basic Indicator Approach (BIA) in determining capital charge for operational risk, with minor modification. The modification entails a capital charge of 12% of the average positive annual gross income of a bank during the last three years. This was originally proposed at 15% but has been lowered to be consistent with the generally retail portfolio of the smaller banks. To give banks sufficient time to adjust, this requirement shall also be subject to staggered implementation over a three-year period, i.e., 4% capital charge shall be applied by 1 January 2012, 8% by 1 January 2013 and 12% by 1 January 2014.

Disclosure Requirements
Stand-alone TBs, RBs, and CBs are required to disclose new items in the Annual Reports and in the quarterly Published Balance Sheet (PBS), namely: (a) components of qualifying capital; (b) capital requirements for credit, market and operational risks; and (c) total and tier 1 capital adequacy ratios. The required disclosures shall commence with the banks’ Annual Reports for 2012 and quarterly PBS from end-March 2012.

The implementation of the Basel 1.5 framework is seen to further enhance the soundness and stability of stand-alone TBs, RBs, and CBs. Ultimately, this will aid in creating stronger financial institutions that can vitally support economic development objectives.

References:

BSP Circular No. 688 dated 26 May 2010
investments in infrastructure. Accordingly, budget deficit rose by 22.0 percent to P229.4 billion from year ago’s P188.0 billion, which is equivalent to 4.9 percent of the country’s gross domestic product or GDP (vs. 4.3 percent at end-June 2009). These ratios though were still measurably compared to the double to triple-digit deficit-to-GDP ratios of the United States and some troubled countries in the Euro area. For a small economy like the Philippines, however, increasing public debt creates funding pressures. The financial stability implications of sovereign risks in the Euro area, therefore, should provide some early head start for banks to re-think their investment strategies outside safe havens like ‘risk-free’ government securities over the medium-term.

Second, the recent crisis showed that over leveraged (e.g., loans-to-deposits or LTD ratio of more than 100 percent) financial institutions without sufficient capital buffers for their risk-taking activities have a higher likelihood of hitting the ground. In this regard, the Financial Stability Board (FSB) and the Basel Committee on Banking Supervision (BCBS) put forward some proposals for countries to consider the introduction of counter cyclical capital rules (Basel III) to be phased-in starting 01 January 2013 to 01 January 2015. Periodic stress testing, both on an aggregate and on an individual bank basis, is similarly proposed to capture tail-end risks not covered by existing risk-based capital frameworks.

Fortunately, Philippine banks are coming from a strong capital position as capital adequacy ratio (CAR) as of end-March 2010 on a consolidated basis stood at 16.0 percent. The bulk of which was core capital as Tier 1-to-risk weighted assets ratio remained strong at 12.6 percent. Even smaller market players like stand-alone thrift banks, rural and cooperative banks have upgraded their capital standards under Basel 1.5 (Circular No. 688 dated 26 June 2010 or Box Article No. 1). Moreover, some of the top tier banks have already taken the initiative to further strengthen their capital base through fresh equity stock offering. Hence, domestic supervisors do not foresee any difficult adjustments for the banking system’s eventual migration to the Basel III regime.

Third, liquidity is a key component of financial stability. Fortunately, high reserve requirement (19 percent of peso deposit liabilities and deposit substitutes effective 14 November 2008 pursuant to Circular No. 632 dated 13 November 2008) and prudent credit allocation (LTD ratio of 66.1 percent as of end-June 2010) of banks led to ample liquidity in the system. Parallel to this, the BSP has implemented various liquidity management measures to ensure liquidity in the system (i.e., peso and dollar repo windows) and currently reviewing the liquidity risk management framework of banks.

Fourth, the prevailing instability in the Euro area may either cause investors to pull out their investments in foreign markets or further increase capital flows to emerging markets including the Philippines as these investors look for alternatives from a much volatile advanced markets. In this regard, existing micro prudential approach to supervision needs to be supplemented with macroprudential policies to ensure the resilience of the Philippine financial system against possible volatile capital flows, which could lead to build up of credit or asset prices.

Fifth, market speculation and panic during the subprime meltdown of 2008 stemmed from asymmetry of information and lack of public disclosure. Post crisis, bank reporting and disclosure standards have to be continually improved and supplemented by industry surveys particularly for those financial institutions that are not publicly traded. In this way, market participants can get accurate and timely picture on the health of the financial system.

Moreover, financial institutions must always ascribe to the highest ideals of corporate governance particularly for banks operating in the Philippines where 75.5 percent of operations were funded by deposit liabilities. These deposit liabilities were mostly sourced from individual savers whose saving accounts remained largely skewed towards ‘P5,000 and below’ category.

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1/ Also includes BSP’s special deposit accounts or SDAs. Funds placed in SDAs amounted to more than P830 billion as of end-June 2010. SDAs are liquidity management tool of the BSP to siphon off excess money from the system.
Box 2:  

Building an Inclusive Financial System through Microfinance

The BSP has adopted an enabling and responsive approach to microfinance in its aim to create a policy environment supportive of broad-based and sustainable development. The delivery of financial products and services to microentrepreneurs who were previously underserved by the mainstream financial sector has paved the way for a more inclusive financial system.

Recognizing the need of microfinance clients for a wider range of financial products and services and to enable banks to fully cater to these needs, the BSP issued new regulations that address product innovations in the microfinance industry. The BSP also issued rules and regulations on the recognition and derecognition of Microfinance Institution Rating Agencies (MIRA) in a move to strengthen transparency and disclosure standards in the microfinance sector.

Recent Policy Initiatives

Approval of the Housing Microfinance Product

The housing microfinance initiative is envisioned as a vehicle for helping boost the government’s efforts of reducing the backlog in housing by addressing pro-poor shelter. The housing microfinance product involves the application of microfinance principles and best practices to the provision of housing finance for home improvement/repairs, house construction and house/lot acquisition. Banks that are currently engaged in microfinance can now further complement their business with the approval of the housing microfinance product, subject to prudential requirements.

BSP Circular No. 678 includes provisions on:

1. the minimum criteria to ensure that banks have the capacity and technological capability to offer housing microfinance;
2. basic characteristics of a housing microfinance product;
3. appropriate risk management;
4. application procedure for product approval by the BSP; and
5. regulatory treatment of housing microfinance loans.

Provision of Micro-Agri Loans

This product innovation specifically caters to the small farmers or those engaged in agri-business, provided they meet the requirements for application. Existing microfinance borrowers who have established a good track record with a financial institution may also avail of this product. The maximum loanable amount for micro-agri loans whether it is used for farm activities, agri-business or agri-related fixed assets is P150,000 with a term of up to 12 months.

To ensure the delivery of financial services in a sound, prudent and sustainable manner, banks that will offer micro-agri loans need to pass the stringent qualifications set forth under BSP Circular No. 680 such as having the capacity and technical know-how to offer micro-agri loans and the appropriate risk management mechanisms in place.

Marketing, Sale and Servicing of Microinsurance Products

Under BSP Circular No. 683, a thrift, rural or cooperative bank, including its authorized branch/es, extension office/s and other banking offices (OBOs), can present, market and sell microinsurance products, provided that the microinsurance product is duly approved by the Insurance Commission.

Microinsurance refers to the insurance business activity of providing specific insurance products that meet the needs of the disadvantaged for risk protection and relief against distress or misfortune.”

*As defined under the IC's Insurance Memorandum Circular No. 9-2006 dated 25 October 2006.
Microinsurance products shall serve as a “financial product of an allied undertaking” under Section 20 of the General Banking Law (GBL). A thrift, rural or cooperative bank can also service (i.e., collect premiums and pay claims) microinsurance products as collection and payment agents pursuant to Section 53.3 of the GBL. As with any financial product, the presentation, marketing and sale of microinsurance products are subject to prudential requirements.

This regulation was issued in line with the government’s thrust of facilitating the safe and sound provision of microinsurance products and services by the private sector and ensuring protection of the rights and privileges of the insured public, particularly the disadvantaged sector.

**Recognition and Derecognition of Microfinance Institution Rating Agencies (MIRA)**

The BSP adheres to the policy of promoting an enabling environment for the appropriate use of objective, credible and competent third-party ratings of microfinance institutions. For this purpose, the BSP has issued the rules and regulations under Circular No. 685 to govern the recognition and derecognition of MIRA.

As part of the minimum eligibility criteria, the MIRA must be duly registered with the Securities and Exchange Commission (SEC) and have at least five years track record in the issuance of reliable and credible ratings with expertise in microfinance operations. The MIRA must establish a Rating Committee that is independent of its analysts. The Committee’s directors, officers and members must possess a high degree of competency and integrity. Meanwhile, international MIRA that will undertake local ratings should have a representative office in the Philippines.

**Capacity Building within the Banking Sector**

**Advocacy on Financial Literacy and Consumer Protection**

The recent policy initiatives on microfinance are further complemented by efforts to promote financial education as an empowering tool to address misinformation, misrepresentation and other forms of abuses and financial fraud that exploit basic consumer rights. The BSP conducts financial learning seminars for banks with microfinance operations and their clients on a regular basis.

To further pursue reforms for the domestic capital market, the BSP encourages its supervised financial institutions to adhere to the code of ethics for financial market activities in the Philippines (Circular Letter No. 2010-13 dated 24 February 2010).

Sixth, a credible crisis management framework that is anchored on the twin objectives of crisis prevention and crisis resolution became highly important post crisis. Ideally, it should provide liquidity and restore normalcy in the most expedient and transparent manner during a crisis. While the country has existing financial safety nets like BSP’s lender of last resort (LOLR) function and prompt corrective action framework including the deposit insurance coverage from the Philippine Deposit Insurance Corporation (PDIC), these were centered on crisis prevention and can be further expanded into a full-blown crisis management framework in the near term.

Lastly, bank density remained skewed towards populous and urbanized areas of the archipelago leaving 13 out of 17 provinces either under banked or unbanked. Toward this end, the BSP pursued a sustained advocacy to promote inclusive finance in the countryside (Box Article No. 2) aimed at expanding the array of microfinance products such as housing microfinance (Circular No. 678 dated 06 January 2010), micro-agri loans (Circular No. 680 dated 03 February 2010) and micro insurance products (Circular No. 683 dated 23 February 2010) as well as promoting market discipline and price discovery through the recognition/de-recognition of Microfinance Institution Rating Agencies or MIRAs (Circular No. 685 dated 07 April 2010). As of end-June 2010, there were 200 microfinance banks serving 869,763 micro borrowers for a total loan portfolio of P6.6 billion.

Summing up, the Philippine financial system may not be the fastest or biggest of contenders but it has one distinct advantage: it has built on its endurance throughout the years through long distance races of reforms and achieved a steady pace of growth. This is from knowing full well that to triumph in the financial stability marathon, sprinting early at full speed or bulking on size may not necessarily lead to victory. The recent global financial crisis showed that even the ablest of contenders can drop out in the race if not supported with fundamental reforms. Hence, those who want to reach the finish line have to train hard to learn from past mistakes and weaknesses, to endure the grueling demands of the track and to develop a warrior’s mindset. After all, financial stability marathon is meant for those who can finish the race.