

2024

FINANCIAL STABILITY REPORT



PDIC



Securities and
Exchange
Commission
PHILIPPINES

FINANCIAL STABILITY COORDINATION COUNCIL





2024 FINANCIAL STABILITY REPORT

FINANCIAL STABILITY COORDINATION COUNCIL



2024 FINANCIAL STABILITY REPORT

Prepared by:
FINANCIAL STABILITY COORDINATION COUNCIL
Bangko Sentral ng Pilipinas
5th Floor Multi-Storey Building, BSP Complex
A. Mabini Street, Malate 1004 Manila, Philippines
December 2024

TABLE OF CONTENTS

ABOUT THE FSCC	1
LIST OF CHARTS	2
LIST OF TABLES	3
LIST OF ACRONYMS AND ABBREVIATIONS.....	4
MESSAGE FROM THE FSCC CHAIRMAN and BSP GOVERNOR	6
EXECUTIVE SUMMARY	7
CHAPTER 1: OVERVIEW OF RISKS TO PHILIPPINE FINANCIAL STABILITY	9
Box Article 1: Emerging Risks to the Industrial Sector.....	20
CHAPTER 2: FINANCIAL SECTOR.....	22
2.1. Banks	22
2.2. Non-banks.....	26
2.3. Capital markets.....	30
CHAPTER 3: CORPORATES AND HOUSEHOLDS.....	37
3.1. Corporates	37
Box Article 2: Shifts and Headwinds to the Real Estate Sector ...	42
3.2. Households.....	44
CHAPTER 4: MEASURES TO SAFEGUARD FINANCIAL STABILITY.....	51
Box Article 3: Countercyclical Capital Buffer Framework in the Philippines.....	55
BIBLIOGRAPHY.....	58

Reproduction for educational and non-commercial purposes is permitted provided that the source is duly acknowledged.

ABOUT THE FSCC

We are an inter-agency council composed of the Bangko Sentral ng Pilipinas (BSP), the Department of Finance (DOF), the Insurance Commission (IC), the Philippine Deposit Insurance Corporation (PDIC), and the Securities and Exchange Commission (SEC). Our Executive Committee is made up of the heads of the five member agencies plus a senior official from each of our agencies. We regularly meet to assess possible systemic risks and to decide appropriate macroprudential policy interventions.

The Financial Stability Coordination Council (FSCC) was first convened on 4 October 2011 at the initiative of the BSP Governor. Though voluntary in structure, we formalized the Council through a Memorandum of Agreement on 29 January 2014. Upon the initiative of the BSP Governor and the Secretary of Finance, Executive Order (EO) No. 144 was signed by then President Rodrigo R. Duterte on 6 July 2021, institutionalizing the FSCC as well as outlining the powers and responsibilities of the Council. EO No. 144 provides the FSCC with a legal personality to set guidelines and regulations in line with the country's Financial Stability Agenda.

SITUATING EACH FSCC MEMBER AGENCY IN THE FINANCIAL STABILITY AGENDA

- **BSP** – The revised charter of the BSP (Republic Act No. 11211) specifically ascribes financial stability as one of its four mandates. Its focus on contagion-driven systemic risks naturally complements its other mandates on monetary policy, banking supervision, and payments system oversight. Since inception, the technical work of the FSCC has been provided by a unit of the BSP.
- **DOF** – As the fiscal authority, the DOF directs government financial institutions, and the operations of the government securities (GS) market. The DOF's tax-related policies have an impact on transactions in financial markets and the real economy.
- **PDIC** – As an attached agency to the BSP, the PDIC serves as a key pillar of the country's financial safety net by protecting depositors through deposit insurance coverage. This coverage fosters public confidence in the banking system and supports financial stability, particularly during periods of market stress. The design and level of deposit insurance can also influence banks' risk-taking behavior, making it a critical consideration in safeguarding systemic stability. Its role is essential in both normal and crisis conditions, ensuring depositors are protected while complementing prudential regulation and bank supervision.
- **SEC** – In supervising capital markets and the corporate sector, the SEC is essential in the pursuit of a stable financial system and sustainable economic activity. The risk preference of players in the non-bank financial sector and non-financial corporations (NFCs) drive growth but can amplify vulnerabilities.
- **IC** – The contingent claims market has broadened and created important interlinkages with other segments of the financial market. Bridging longer-term liabilities with shorter-term assets raises liquidity, valuation, and investment issues, all of which are central in mitigating systemic risks.

Taken collectively, the FSCC positions the financial system as an enabler of economic growth and stakeholders' well-being. The Council pro-actively mitigates evolving systemic risks, while instituting needed macroprudential policies that build the system's resilience.

LIST OF CHARTS

MAIN CHAPTERS

Figure 1.1	Transmission of Global Risks to Philippine Financial Stability	9
Figure 1.2	Systemic Risk Assessment Matrix	10
Figure 1.3	World Uncertainty Index	11
Figure 1.4	Global EPU Index	11
Figure 1.5	CBOT Rough Rice – Futures	12
Figure 1.6	Crude Oil – Futures	12
Figure 1.7	LME Copper – 3M Futures	12
Figure 1.8	Philippine Imports	13
Figure 1.9	China's share of US Imports	13
Figure 1.10	Refined Petroleum Oil Imports	14
Figure 1.11	NPL Coverage Ratio	15
Figure 1.12	PH Rate Decisions vs Market Movements in 2024	16
Figure 1.13	Macroeconomic Risk in Market Pricing	16
Figure 1.14a	Foreign Portfolio Investment (Inflows)	17
Figure 1.14b	Foreign Portfolio Investment (Outflows)	17
Figure 1.15	Corporate Debt Maturity	17
Figure 1.16	Range of Lending Rates to Corporations	17
Figure 1.17	Borrowings from Foreign Affiliates	18
Figure 1.18	Public Debt	18
Figure 1.19	General Government Debt Outstanding	19
Figure 1.20	Monetary Reserves	19
Figure 1.21	Foreign Public Debt	19
Figure 1.22	Public Debt-interest Payments	19
Figure 2.1	PBS Production and Household	23
Figure 2.2	PBS Total Loan Portfolio vs. Financial Assets	23
Figure 2.3	PBS Peso Deposit Composition	23
Figure 2.4	Net Interest Income	23
Figure 2.5	Unrealized Gains (Losses) on FVOCI Financial Assets	24
Figure 2.6	PBS Financial Assets	24
Figure 2.7	PBS Group NPL	25
Figure 2.8	Gross NPL Ratio per Banking Group	26
Figure 2.9	Baseline vs Breakeven Gross NPL	26
Figure 2.10	NBFI Loans	30
Figure 2.11	2024 Corp Issuances vs Reference Rates	32
Figure 2.12	Size of Bond Market (H1 2024)	32
Figure 2.13	ASEAN Equity Performance	33
Figure 2.14	Net Foreign Trading	33
Figure 2.15	PSEi and Net Foreign Flows	34
Figure 2.16	Bond Yield and Net Foreign Flows	34
Figure 2.17	PH Equity Risk Premium	34
Figure 2.18	Capital Raised Philippine Stock Exchange	34
Figure 2.19	US Dollar Index	35
Figure 2.20	PH-US Sovereign Spreads	35
Figure 2.21	PH Yield Curve	35
Figure 3.1	Firm Count by Net Income	38
Figure 3.2	Firm Count by Interest Coverage Ratio	38
Figure 3.3	Firm Assets by D/E Ratio	39
Figure 3.4	Firm Count by Current Ratio	39
Figure 3.5	Maturity of Corporate Debt of Top 15 Conglomerate Groups	39
Figure 3.6	Vulnerable Conglomerate-Related NFCs	40
Figure 3.7	Total Debt of Vulnerable Conglomerate-Related NFCs	41
Figure 3.8	Household Final Consumption Expenditure	45

Figure 3.9	Gain/(Loss) in Employment in Major Sectors	45
Figure 3.10	Income and Expenditure Growth by Income Decile	47
Figure 3.11	Household Loans	48
Figure 3.12	Overseas Filipinos (OF) Remittances	49
Figure 3.13	Non-Performing Consumer Loans	50

BOX ARTICLES

Figure A	Median Interest Coverage Ratio by Industry	20
Figure B	Interest Coverage Ratio	21
Figure C	Corporate Debt of Industrials Sector	21
Figure D	Segment Share Volume-Value	42
Figure E	Residential Real Estate Demand-Supply	42
Figure F	Key Ratios (EBIT, IE, ICR)	43
Figure G	Countercyclical Capital Buffer Framework	55
Table A	CCyB Indicators across Jurisdictions	57

LIST OF TABLES

Table 2.1	Selected Philippine Banking System Indicators	22
Table 2.2	Size of Selected Non-Bank Financial Institutions	27
Table 2.3	Assets of Selected Institutions of the Financial System	29
Table 2.4	Performance of the PH Bond and Equity Markets	31
Table 3.1	Outstanding amount of nonfinancial business and household credit	37
Table 3.2	Labor and Employment Statistics	46
Table 3.3	Household Use of Loan Proceeds	48
Table 3.4	Household Use of OFW Remittances	49

LIST OF ACRONYMS AND ABBREVIATIONS

AEs	-	Advanced Economies
AFASA	-	Anti-Financial Account Scamming Act
AFC	-	Asian Financial Crisis
ASEAN	-	Association of Southeast Asian Nations
AUROC	-	Area Under the Receiver Operating Characteristic
BCBS	-	Basel Committee on Banking Supervision
BES	-	Business Expectation Survey
BIS	-	Bank for International Settlements
BSP	-	Bangko Sentral ng Pilipinas
BSFIs	-	BSP-Supervised Financial Institutions
BTr	-	Bureau of the Treasury
CAR	-	Capital Adequacy Ratio
CBOT	-	Chicago Board of Trade
CCyB	-	Countercyclical Capital Buffer
CES	-	Consumer Expectations Survey
COVID	-	Coronavirus Disease
DBCC	-	Development Budget Coordination Committee
D/E	-	Debt-to-Equity
DGBs	-	Digital Banks
DIF	-	Deposit Insurance Fund
DLT	-	Distributed Ledger Technology
DOF	-	Department of Finance
DSIBs	-	Domestic Systemically Important Banks
DSMAC	-	Debt Securities Measured at Amortized Cost
DSR	-	Debt-Service Ratio
EBIT	-	Earnings Before Interest and Taxes
EO	-	Executive Order
EPS	-	Earnings Per Share
ERP	-	Equity Risk Premium
FCY	-	Foreign Currency
FIES	-	Family Income and Expenditure Survey
FISC	-	Financial Inclusion Steering Committee
FPI	-	Foreign Portfolio Investment
FOMC	-	Federal Open Market Committee
FRP	-	Financial Reporting Package
FSCC	-	Financial Stability Coordination Council
FSF	-	Financial Sector Forum
FSR	-	Financial Stability Report
FVOCI	-	Fair Value Through Other Comprehensive Income
FVTPL	-	Fair Value Through Profit or Loss
FX	-	Foreign Exchange
GDP	-	Gross Domestic Product
GEPU	-	Global Economic Policy Uncertainty
GMRA	-	Global Master Repurchase Agreement
GS	-	Government Securities
GSIS	-	Government Service Insurance System
HKMA	-	Hong Kong Monetary Authority
IBL	-	Interbank Loans Receivable
IC	-	Insurance Commission
ICR	-	Interest Coverage Ratio
ICs	-	Integrated Circuits
IFRS	-	International Financial Reporting Standards
IMF	-	International Monetary Fund
IPO	-	Initial Public Offering

IRS	-	Interest Rate Swap
LaR	-	Loans at Risk
LCY	-	Local Currency
LME	-	London Metal Exchange
LTNCTDs	-	Long-Term Negotiable Certificates of Time Deposit
LTV	-	Loan-to-Value
MBA	-	Mutual Benefit Associations
MORB	-	Manual of Regulations for Banks
MORNBFIs	-	Manual of Regulations for Non-Bank Financial Institutions
MSMEs	-	Micro, Small and Medium Enterprises
MTM	-	Marked-to-Market
NBFI	-	Non-bank Financial Institution
NFCs	-	Non-Financial Corporations
NPLs	-	Non-Performing Loans
NRoSS	-	National Registry of Scripless Securities
OFWs	-	Overseas Filipino Workers
PBS	-	Philippine Banking System
PD	-	Primary Dealer
PDIC	-	Philippine Deposit Insurance Corporation
PEPU	-	Philippine Economic Policy Uncertainty
PFRS	-	Philippine Financial Reporting Standards
POGOs	-	Philippine Offshore Gaming Operators
POS	-	Point-of-Sale
PSA	-	Philippine Statistics Authority
PSE	-	Philippine Stock Exchange
PSEi	-	Philippine Stock Exchange Index
QB	-	Quasi-Banking
RAM	-	Risk Assessment Matrix
RCBs	-	Rural and Cooperative Banks
REE	-	Real Estate Exposure
REL	-	Real Estate Loan
RREPI	-	Residential Real Estate Price Index
RRP	-	Reverse Repurchase
SBL	-	Single Borrower's Limit
SEC	-	Securities and Exchange Commission
SRCM	-	Systemic Risk Crisis Management
SSS	-	Social Security System
TBs	-	Thrift Banks
TLP	-	Total Loan Portfolio
TTBs	-	Tokenized Treasury Bonds
UNCTAD	-	United Nations Conference on Trade and Development
UKBs	-	Universal and Commercial Banks
US Fed	-	US Federal Reserve
US	-	United States
USD	-	US Dollar
VIX	-	Volatility Index
WUI	-	World Uncertainty Index
YoY	-	Year-on-Year

MESSAGE FROM THE FSCC CHAIRMAN and BSP GOVERNOR

There may be few times in recent economic history when Financial Stability Report is more important and when more people should go over it.

There is the prospect of trade wars – they may have already begun – and the wide-ranging effects they would have across the global economy. Governments and analysts are already cutting growth forecasts. There are continued geopolitical tensions in Europe, the Middle East, and even here in Asia, with little clarity about what will happen next and how this will affect supply chains around the world. Deregulation, including of the financial industry, may be making a comeback in the U.S.

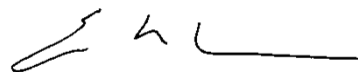
Uncertainty indexes – such as the World Uncertainty Index and Global EPU Index cited in the report – are close to their levels at the start of the COVID-19 pandemic and exceed the levels during the Global Financial Crisis.

As the report lays out, the good news is that, at present, global food inflation is declining, the local banking sector is well capitalized, and corporate earnings are reverting to pre-pandemic levels, among other positive factors. The BSP remains on a path to lower interest rates, which can help the economy further.

Concerns include how an economic slowdown could squeeze borrowers. This could harm banks and non-bank financial institutions exposed to non-performing loans, including credit card debt.

Knowing these strengths and vulnerabilities can help us navigate the upcoming turbulence and anxiety, and also identify opportunities for reform and growth. Key among the reforms discussed in the report is accelerating the development of the capital market. This can not only help fund government and private sector investment especially in infrastructure. It can also provide the “spare tire” we need if banks have to pull back on the loans our economy is overly reliant on.

Finally, this report is a map not only of risky terrain but also opportunities for growth. It is a guide for policymakers and businesses on the policies and investments that can build on the gains we have achieved in the past years, and keep us on a path of sustainable, resilient, inclusive growth.



ELI M. REMOLONA, JR.
FSCC Chairman and BSP Governor

EXECUTIVE SUMMARY

Overall Risk Assessment

The Philippine financial system remains resilient but faces moderate risks that warrant close monitoring. The propagation of global uncertainties, including heightened geopolitical tensions, evolving monetary policies in major economies, and potential shifts in the United States (US) following the outcome of the presidential elections could impact the Philippine economy.

Global risks arise from cost pressures and changes in trade and monetary policy. The World Uncertainty Index (WUI) and the Global Economic Policy Uncertainty (GEPU) Index are on an upward trend. The cost of production materials (especially in the industrial sector) may accelerate due to supply-chain disruptions amid geopolitical instability and lag-effects of global monetary policy easing.

Declining inflation, supply chain reconfiguration, and forward-looking domestic market players contribute to global resilience. Global food inflation is declining, easing pressures on household budgets. There is also potential for the reconfiguration of global trade and supply chains that could benefit the Association of Southeast Asian Nations (ASEAN) member states. This presents opportunities for increased trade and investment, especially on partaking the manufacturing share from China. Market volatility closely tracks economic policy uncertainty and indicates that expectations are anchored on policy rate movements.

There are local risks from debt refinancing and a high maturity wall. Dampened consumption and investment may increase credit risk. Firms with large short-term debt may face refinancing concerns. A “maturity wall” (or high debt approaching maturity) and concerns on debt-servicing capacities of borrowers could influence market sentiment and tighten credit conditions. On the upside, a “macro-market disconnect” (between economic uncertainty and financial market volatility) is not evident.

Sectoral Analysis

Strong local banking sector with ample buffers and stable financial markets underscore financial sector resilience. Banks have high capital buffers and ample liquidity, which would allow the financial system to absorb potential losses and/or support economic activity. Financial markets are stable with no signs of asset price misalignments and high share of domestic investor participation. Overall, the country’s adequate level of international reserves, (even exceeding the International Monetary Fund’s (IMF) reserve adequacy metric) could cushion the economy from external shocks.

But the financial sector faces some asset valuation risks. Banks are vulnerable to asset quality risks as reflected in non-performing loans (NPLs) and the expansion of unsecured consumer loans. Among non-bank financial institutions (NBFIs), the increase in leverage is prone to liquidity stress.

The real sector shows resilience but is subject to leverage and debt-servicing risks. Corporate earnings are reverting to pre-pandemic levels. However, increased leverage and sustained funding mismatches especially in large corporates pose vulnerabilities. Significant reliance on bank funding and the degree of interconnectedness among corporates with Domestic Systemically Important Banks (DSIBs) could amplify risks to the financial sector.

Monetary easing can bolster real sector resilience. The transition towards an accommodative interest rate environment could encourage investment in capital-intensive projects, business expansion, and household consumption. Looser financing conditions could pave the way for enhanced credit availability for businesses and consumers to ramp up investments and rebuild savings as buffer to shocks.

Policy Recommendations

Priority measures could enhance the stability and resilience of the Philippine financial system if aligned with monetary policy and banking supervision.

Further development of the capital market. Given that corporate debt remains highly bank reliant, a key initiative to alleviate the pressure on the banking system is the deepening of alternative sources of financing. This entails streamlining issuance requirements, particularly for small to mid-sized corporate borrowers, improving platform accessibility through technology, and increasing activity through engaging market-makers.

Continuous improvement of reporting frameworks. Improving the monitoring of NBFIs and regulating shadow banking activities start with addressing gaps in the availability of granular data that are necessary for systemic risk surveillance.

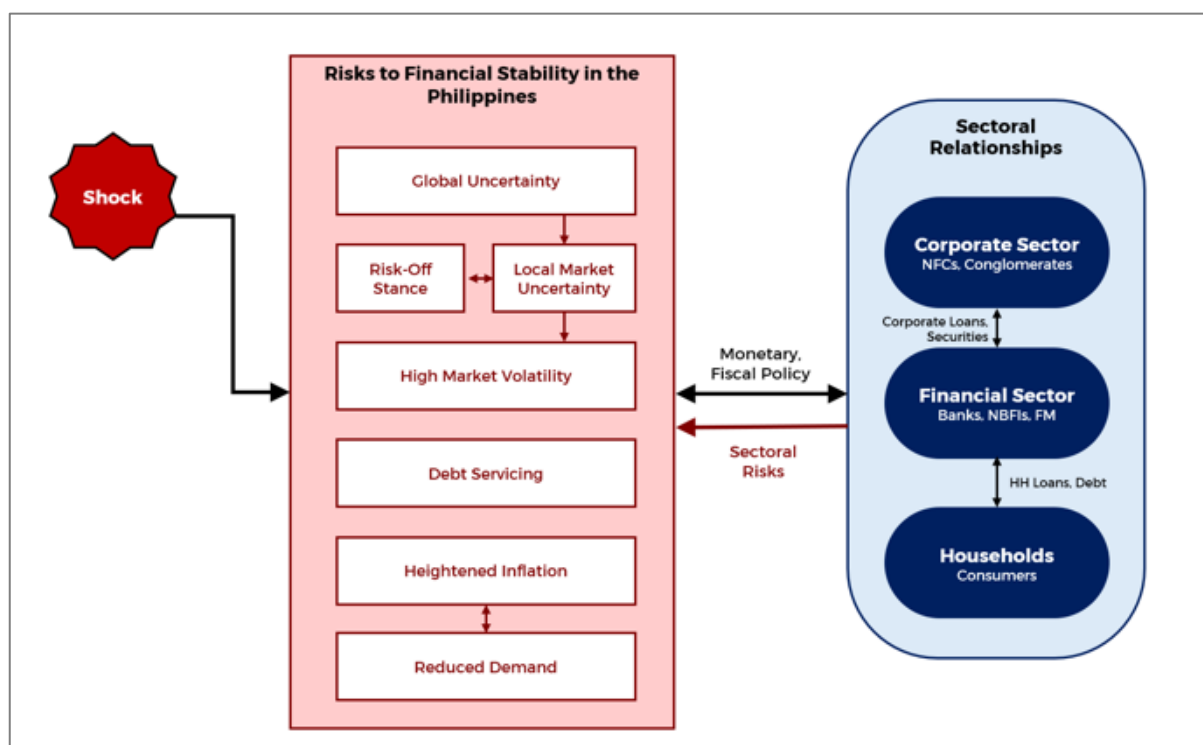
Development and adoption of macroprudential tools. The establishment of frameworks on macroprudential tools to preemptively address vulnerabilities is critical to manage systemic risks and reduce the likelihood of financial crises. A general framework on the countercyclical capital buffer (CCyB) guided by credit-to-gross domestic product (GDP) gap, loan-to-value (LTV), debt-service ratios, and other key leading indicators provides a precautionary measure contingent on economic and credit conditions.

CHAPTER 1: OVERVIEW OF RISKS TO PHILIPPINE FINANCIAL STABILITY

Recent global uncertainty stems from concerns on geopolitics and economic policies that affect international trade and investment flows. A “macro-market disconnect”¹—when macroeconomic risks are not properly priced in by market players—could affect asset valuations and may be subject to severe corrections. Excessive risk aversion can also exacerbate debt-servicing issues for corporates and households. While the Philippine banking system (PBS) remains in a position of strength, sector-specific vulnerabilities are evident in the increased NPLs in the trade and manufacturing sectors. These risks could interact with pockets of vulnerabilities.

Meanwhile, the corporate sector is generally resilient with profitability rebounding to pre-pandemic levels. But vulnerabilities could be triggered by increased leverage and funding mismatches. Corporates’ heavy reliance on bank funding could amplify credit risks to the financial sector. The provision of credit to corporates and households creates an interdependence where shocks from one sector could have destabilizing effects on other sectors. Government’s economic stabilization policies are crucial in managing vulnerabilities (Figure 1.1).

Figure 1.1
Transmission of Global Risks to Philippine Financial Stability



Note: Based on FSCC's overall risk assessment

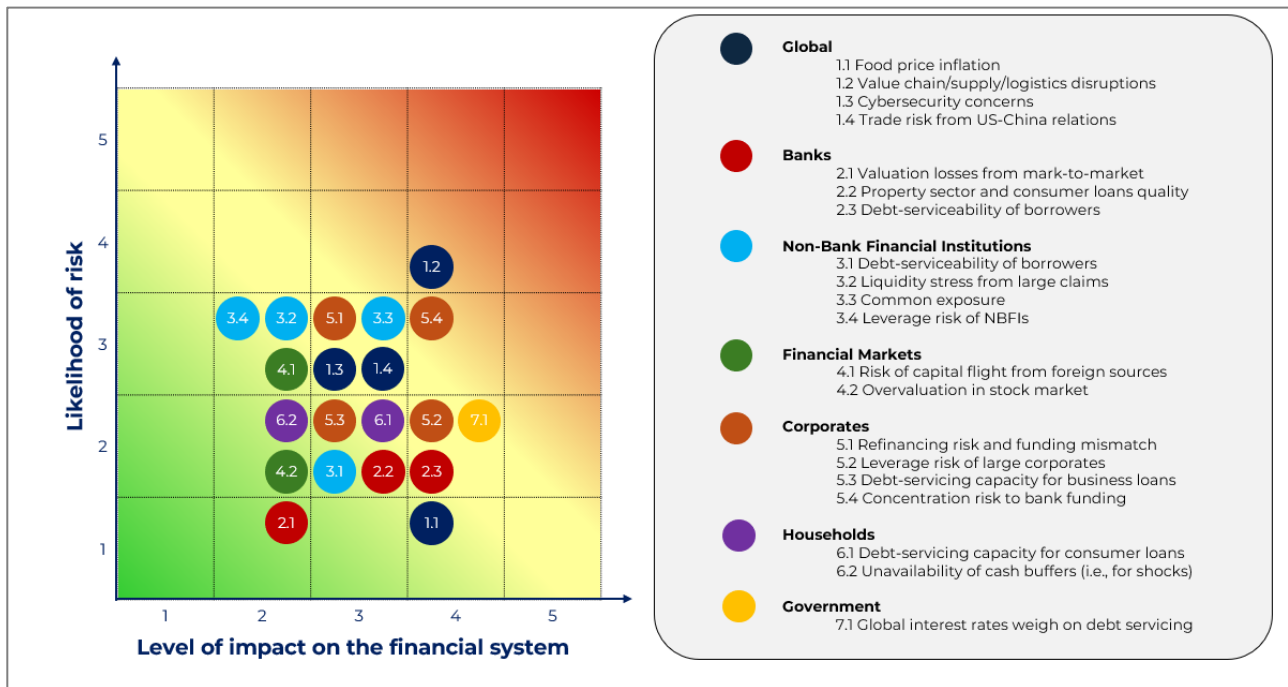
¹ The “macro-market disconnect” is a phenomenon highlighted in the IMF’s October 2024 Global Financial Stability Report. It refers to the divergence between economic uncertainty and financial market volatility. From a systemic risk and financial stability standpoint, this phenomenon could give economic agents a false sense of security, i.e., low financial market volatility could lead to investors’ complacency and excessive risk-taking. When economic uncertainty is high, any adverse shock could be amplified, leading to sudden and severe market corrections.

Figure 1.2 presents a Risk Assessment Matrix (RAM) based on two dimensions: (1) level of impact on the financial system; and (2) likelihood of risk. Based on the distribution of the identified systemic risks, the propagation of global risks to the Philippine financial system is expected to be *moderate*. As shown, most risks are concentrated on the *green* and *yellow* zones. The risks that lie on the *orange* or *red* zone are considered critical.

Key global risks stem from global value chain/supply/logistics disruptions amid protracted geopolitical tensions and uncertainty in global economic policies. Domestically, a risk that warrants close attention is the corporate sector’s heavy reliance on bank funding, particularly from Domestic Systemically Important Banks (DSIBs). The interconnectedness of large conglomerates to the banking system may expose the financial system to risks coming from the corporate sector given increasing leverage and funding mismatches.

On balance, the banking sector remains healthy as characterized by limited endogenous risks or internal weaknesses. Non-Bank Financial Institutions (NBFIs), although small compared with the size of the Philippine banking system, expose banks to common exposure risk through their shared investments and holdings. Meanwhile, various asset classes remain reflective of economic fundamentals (i.e., no compelling signs of asset price misalignments). For households, there may be concerns on the risk of elevated consumer prices and higher borrowing costs that could have implications on their ability to repay debt. Global interest rates may affect public debt-servicing. But government debt remains manageable, given ample levels of foreign exchange (FX) reserves as cushion against headwinds.

Figure 1.2
Systemic Risk Assessment Matrix²



Note: Based on FSCC’s overall systemic risk assessment

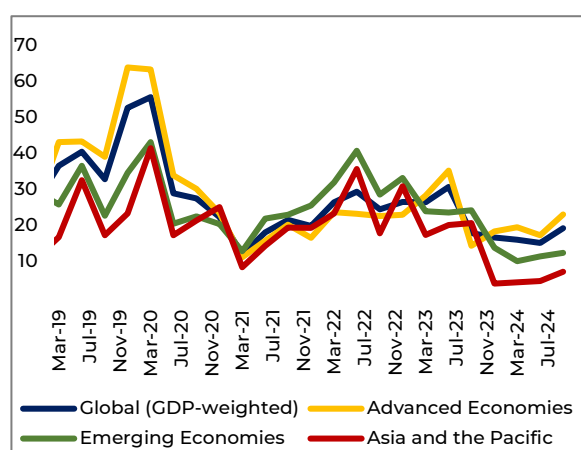
² Patterned after the RAM visualization of the Bank of Thailand in its Financial Stability Report. The placement of the identified risks within the RAM was a result of discussions and agreements within the FSCC.

Global risks

Geopolitical tensions drive economic uncertainty. The World Uncertainty Index (WUI)³ has been on an upward trend since Q4 2023, reflecting growing concerns over geopolitical stability and changes in economic policy that could affect global trade and investment flows, though uncertainty remains notably lower than the levels recorded just before the COVID-19 period (**Figure 1.3**). The downside risks to global growth could affect emerging markets, including the Philippines. Major contributors to this heightened uncertainty include escalating trade disputes between US and other major economies like China, Canada, and the European Union; regional conflicts in areas like Eastern Europe and the Middle East and shifts in international energy policies such as changes in oil production quotas by OPEC+ countries and priorities regarding exploring renewable energy. Despite the recent uptick, the WUI remains lower than levels observed in 2022 and the peak periods of 2019 and 2020.

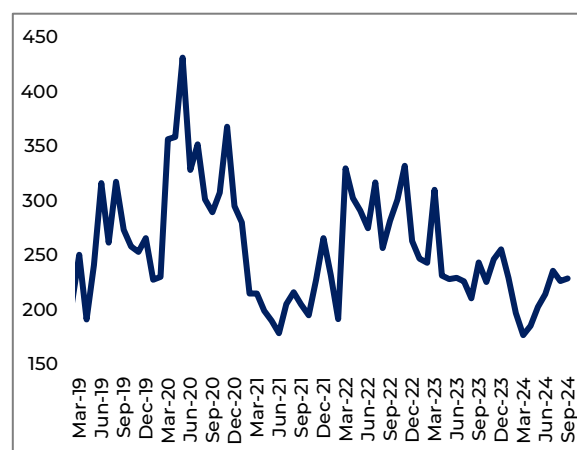
Meanwhile, the Global Economic Policy Uncertainty (GEPU) Index (**Figure 1.4**) captures the uncertainties arising from changes in economic policies in Advanced Economies (AEs), such as shifts in US trade policy following the 2024 presidential elections, tighter fiscal policies in the European Union amid inflation concerns, and Japan's recalibration of its monetary policy.

Figure 1.3
World Uncertainty Index
In x1000 index points



Source: Economic Policy Uncertainty Group

Figure 1.4
Global EPU Index
In index points



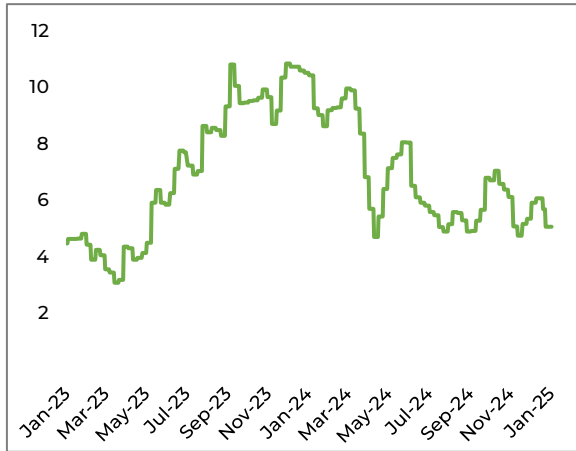
Source: Economic Policy Uncertainty Group

Fluctuations in global commodity prices could lead to inflation pass-through for imports of rice and oil. As an import-dependent nation,⁴ Filipinos are exposed to volatility in agricultural futures prices (**Figure 1.5**). Rice futures prices showed a sharp decline in mid-July 2024 due to expectations that India is easing its rice export bans. Oil prices have continued to move sideways (**Figure 1.6**) given the unwinding of voluntary cuts of oil-producing countries, continuous access to current shipping routes, and dampened demand in China. Oil price levels remain below the highs observed in September 2023 caused by short-lived low inventory of crude stockpiles in the US.

³ The WUI is constructed by counting the frequency of the word “uncertainty” in the quarterly Economist Intelligence Unit country reports for 143 countries. For each country, the number of times “uncertainty” is mentioned is divided by the total number of words in the report. These country-specific indices are then aggregated using GDP weights to produce the global WUI.

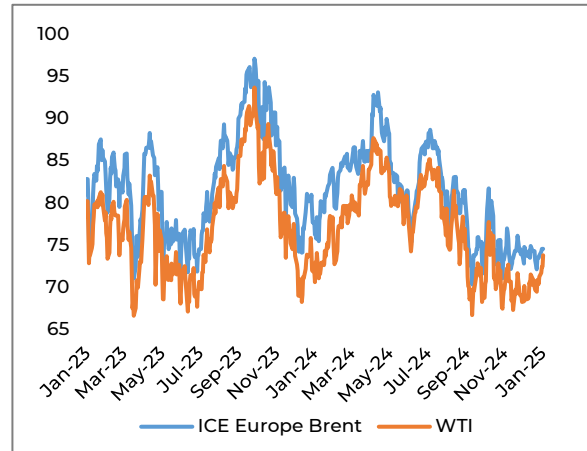
⁴ Based on the State of Commodity Dependence by the United Nations Conference on Trade and Development (UNCTAD) State of Commodity Dependence 2023.

Figure 1.5
CBOT Rough Rice - Futures
In USD per contract



Source: CME Group

Figure 1.6
Crude Oil – Futures
In USD per barrel



Source: CME Group

Disruptions in global supply chains and logistics are primary risk considerations. Volatility in commodity prices driven by geopolitical tensions can have first- and second-round effects. Industries such as electronics manufacturing are exposed to higher futures prices of base metals like copper, which have been rising amid the global transition to green energy (Figure 1.7). Disruptions can lead to increased production costs in electronics (i.e., integrated circuits or ICs using copper as conduits, which the Philippines heavily imports).

The financial sector is confronted with emerging risks associated with the rapid adoption of financial technology solutions and artificial intelligence technologies. While

innovations can enhance efficiency and financial inclusion, the increasing influence of technology also introduces new challenges, such as cybersecurity threats, operational risks, system failures or algorithmic errors, and biases that could undermine regulatory compliance. Concentration risks may arise if key financial services are dominated by a few providers. These factors could pose significant challenges to operational resilience and market stability. The passage of Republic Act No. 12010 or the Anti-Financial Account Scamming Act (AFASA) is expected to deter financial cybercrimes by strengthening the enforcement measures of relevant government agencies in investigating and sanctioning these acts. The BSP’s execution of the newly launched Financial Services Cyber Resilience Plan 2024-2029 by establishing baseline market protocols under various stressed scenarios and improving data sharing and collaboration between relevant offices.

Overseas Filipino Workers (OFWs) face downside risks to job security and employment prospects. More stringent immigration protocols, such as visa requirements, in the US could reduce the number of OFWs and dampen cash remittances. The year-to-date monthly average of the share of OFW remittances from the US is 40.83 percent in 2024, the highest among all countries.

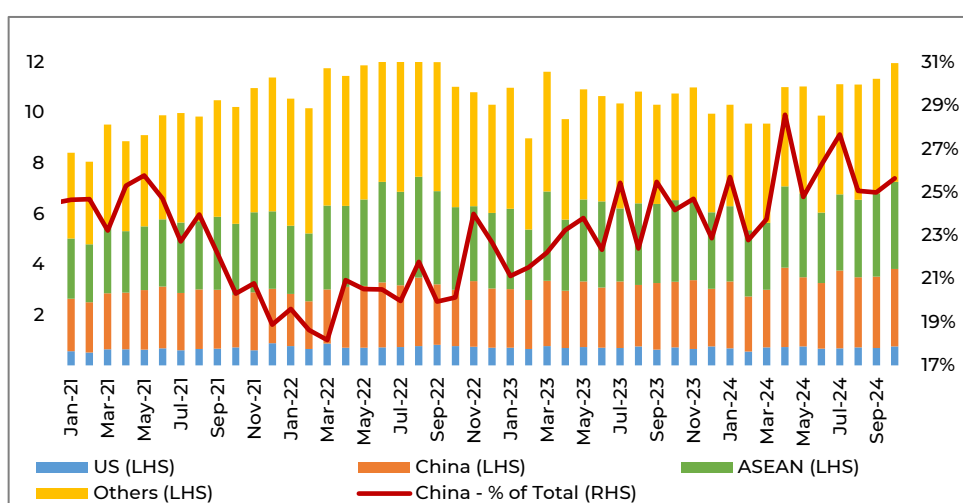
Figure 1.7
LME Copper – 3M Futures
In thousands USD per tonne



Source: LME

The change of leadership in the world's largest economy can increase economic fragmentation. If implemented to its proposed extent, US President Donald J. Trump's imposition of higher tariffs and the reactionary actions by Canada, Mexico, and China could lead to a rebalancing of international trade flows.⁵ An increase in tariff levels, particularly on China, can disrupt global supply chains and dampen manufacturing activity. **Figure 1.8** shows the increasing share of the Philippines' imports from China. However, the negative impact of higher tariffs on the cost of production and overall economic activity of the Philippines can be offset by domestic policies targeted to support affected industries and business sectors and stronger trade relations with the US and other advanced economies. Energy products are at the forefront of these trade tensions with moderate impact on commodity prices such as oil. Gains from concerns of supply shortages are offset by projected dampened global demand and President Trump's focus to boost domestic fossil fuel production in the US.

Figure 1.8
Philippines Imports
Source by country (In USD billion)

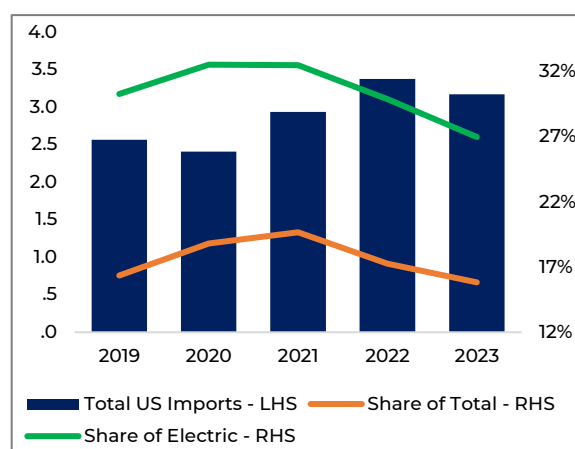


Source: PSA

Trade dynamics may present an opportunity for the Philippines to take a larger share of US imports. Prior to US President Trump's victory, bilateral trade between China and the US has declined. China's share of total US imports has shrunk from 19.7 percent in 2021 to 15.8 percent in 2023 (**Figure 1.9**). Electronic goods have been the top China imports of the US, but the share to total also declined from 32.5 percent in 2021 to 27.0 percent in 2023.

The Philippines is constrained from expanding its market share. Electronic goods⁶ are the Philippines' top exports with a share of 49.7 percent in 2021 climbing to 55.2 percent in 2023. From 2021-2023, Integrated Circuits (ICs) comprised two-thirds of total electronic exports and a third of total exports. **Box Article 1** features emerging risks to the industrial sector. Key

Figure 1.9
China's share of US Imports
Levels (In USD trillion),
In percent of total



Source: International Trade Center

⁵ Based on the US election preview of macro/market consequences by Capital Economics

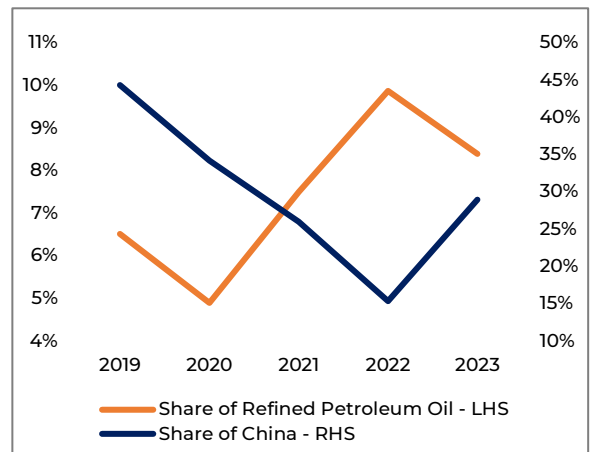
⁶ The official trade classification is "Electrical machinery and equipment and parts thereof; sound recorders and reproducers, television image and sound recorders and reproducers, and parts and accessories of such articles."

considerations for exports are the types of electronic goods demanded by the US and the presence of competitors. Nearly 50 percent of Chinese electronic goods imported by the US are telephone sets (i.e., smartphones). The Philippines may need to scale up and develop its manufacturing base to tap this market.⁷

A potential upside may come from an increase in export revenues to other countries. This possibility arises as the scope of the trade reconfiguration extends beyond the China-US trade relationship. Aside from China, Trump has imposed blanket and targeted tariffs on imports from other economies to balance trade in favor of the US. Other economies may react by seeking other import sources, particularly of electric goods, which comprises a large share of Philippine exports. This rebalancing may benefit the Philippines but there is strong competition from neighboring Asian states such as Hong Kong, Taiwan, Singapore, South Korea, Malaysia, Vietnam, and Japan.

The importation of refined petroleum could expose the Philippines to vulnerabilities. The Philippines' second-largest imports in 2023 were petroleum oils. In its refined state, petroleum is used in power generation, and transportation. With China as the main source accounting for 29.0 percent of supply (Figure 1.10), the Philippines' reliance on Chinese trade for refined petroleum could be a potential source of risk and vulnerability.

Figure 1.10
Refined Petroleum Oil Imports
Over total imports (In percent), over
Refined Petroleum Oil Imports (In percent)



Source: International Trade Center

Banks

The supply of credit is expected to remain stable as the PBS improved its profitability, coupled with a robust capital base and ample liquidity. Although growth is slower than pre-pandemic levels, the banking system is well-positioned to support the domestic economy, with an expansion in its lending portfolio. However, sector-specific vulnerabilities such as increase in NPLs within the trade and manufacturing sectors warrant close monitoring of credit risk. Mark-to-market (MTM) gains support banks' capital but remain exposed to interest rate risks. The PBS holds a substantial portfolio of financial assets, including GS and other debt instruments where their valuations are subject to market fluctuations.

Loan quality is a risk factor. The household sector's aggressive year-on year (YoY) loan growth of 23.4 percent in June 2024 has been driven by an expansion in unsecured lending such as credit cards and salary loans. The higher borrowing costs and reduced household income due to elevated interest rates and inflationary pressures may impair households' ability to service their debts, which increases the credit risk for banks. However, banks remain resilient with ample provisioning despite the decline of the NPL coverage ratio to 93.3 in September 2024 from 103.7 a year prior (Figure 1.11). The registered gains on unrealized MTM valuations on assets measures at Fair Value Through Other Comprehensive Income (FVOCI) can be attributed to lower interest rates and banks' strategic positioning. The PBS holds a substantial portfolio of

⁷ The Philippines' main imports are also ICs which are assembled or/modified before they are re-exported. The Philippines' top IC trading partners in 2023 were Taiwan (20.49%), South Korea (14.64%), the US (13.38%), and Japan (10.66%). A drop in China's share can be remedied by increasing trade with these other nations.

financial assets, including GS and other debt instruments where their valuations are subject to market fluctuations.

Non-bank financial institutions (NBFIs)

Asset size of NBFIs, although relatively small compared to the banking sector, has grown rapidly. NBFIs account for one-fourth of the total resources of the Philippine financial system as of June 2024, reflecting an increase of 0.6 percentage points over the previous year. The expanded lending activities of NBFIs through in-house financing (by real estate firms) and trust services (by firms with a trust license) may be accompanied by heightened credit risk. Growing activity in real estate in-house financing indicates that developers are capturing a larger share of the financing market and increases interconnectedness. The growth in loans released by NBFIs with trust activities could transmit corporate vulnerabilities to trustors and investors.

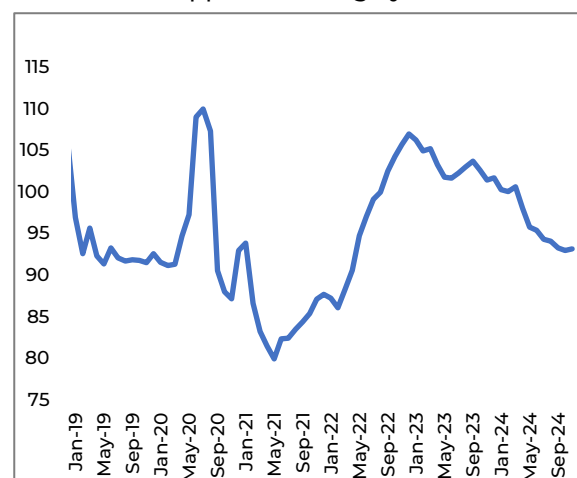
NBFIs' interconnectedness with other financial institutions through their common exposure to investment holdings poses a downside risk to the former's asset valuation if the latter conducts sell-off activities. Banks and NBFIs hold significant amounts of GS. In the event of significant negative market movements or defaults, the losses incurred by one institution could affect others through these common holdings. If pension funds sell large amounts of GS, valuations of similar assets held by banks and other NBFIs can decline.

Financial markets

Financial markets face the risk of capital flight. Foreign investors account for approximately 46 percent of trading in the Philippine Stock Exchange (PSE), and 4.1 percent in the bond market - up from 2.1 percent in 2023.

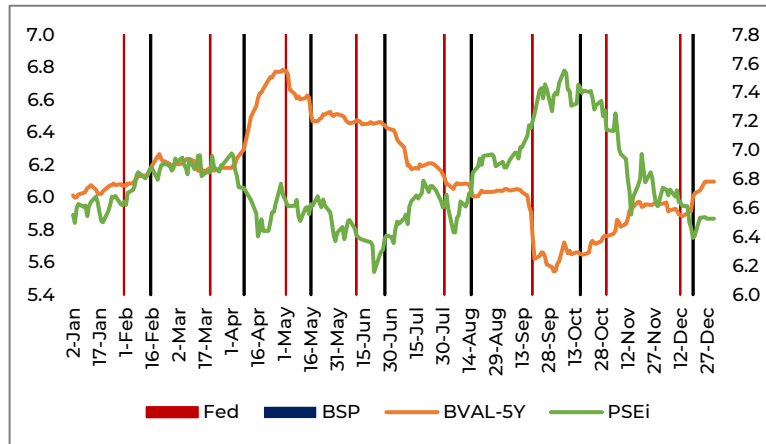
Financial markets exhibit sensitivity to foreign economic data releases. Markets are reacting swiftly to key US economic indicators such as non-farm payrolls and inflation data as shown by movements in bond yields and asset prices ahead of Federal Open Market Committee (FOMC) meetings. Investors extract and apply information on output and inflation (for macroeconomic announcements) in forming expectations on the path of future interest rates and the next move of the monetary authority. Market movements are anchored on monetary policy decisions. Figure 1.12 shows that adjustments in yields and the equity index occur ahead of policy announcements.

Figure 1.11
NPL Coverage Ratio
Philippine Banking System



Source: BSP

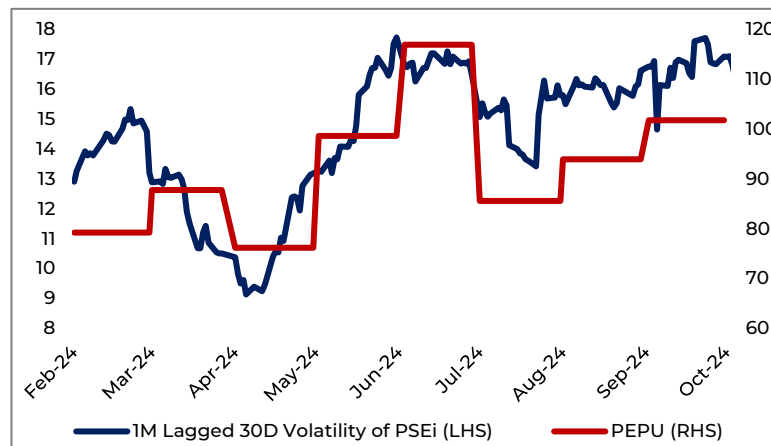
Figure 1.12
PH Rate Decisions vs Market Movements in 2024
 In percent annum (LHS), x1000 index (RHS)



Source: US Fed, BSP, PDS Group, PSE

There is no indication of a divergence between economic uncertainty and financial market volatility. The 30-day volatility of the Philippine Stock Exchange index (PSEi) plotted against the Philippine Economic Policy Uncertainty (PEPU) Index (Figure 1.13) indicates that market volatility closely tracks economic policy uncertainty. This suggests that market participants respond to economic data and policy developments. The forward-looking behavior (i.e., anticipating policy changes) and data-dependency of market participants ensure that asset prices track and preempt economic realities.

Figure 1.13
Macroeconomic Risk in Market Pricing
 In percent (LHS), In index points (RHS)

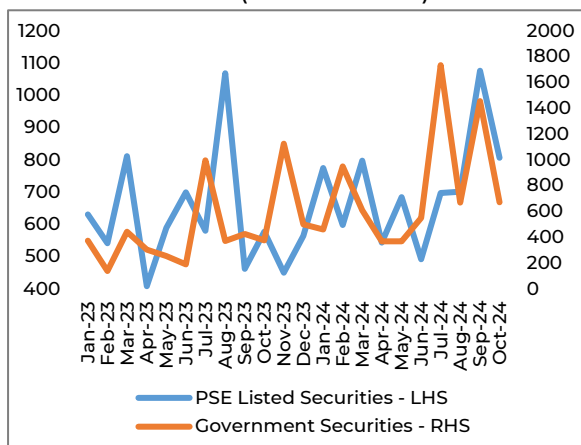


Source: Bloomberg PEPU Index from BSP-DER staff Calculation

Portfolio flows reflect investor risk sentiment and translate to FX movements.⁸ Portfolio investments are vulnerable to outflows. In mid-2024, the Philippines reached recent highs in the level of foreign portfolio investments (FPI) for GS and PSE-listed securities (Figure 1.14a). However, an increase in outflows began in August (Figure 1.14b) amid fears of persistent inflation over the policy horizon and the Chinese economy showing more signs of economic slowdown.

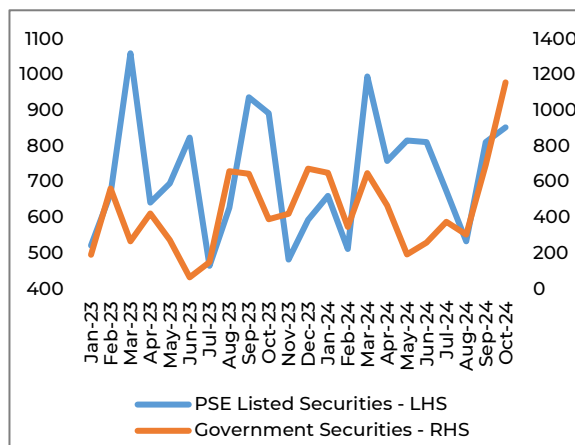
⁸ Gelos et al. (2024) found that USD is a better proxy for risk sentiment than the Volatility Index (VIX) and has a more prominent role in influencing capital flows compared to interest rate differentials.

Figure 1.14a
FPI (Inflows)
Levels (In USD million)



Source: BSP

Figure 1.14b
FPI (Outflows)
Levels (In USD million)



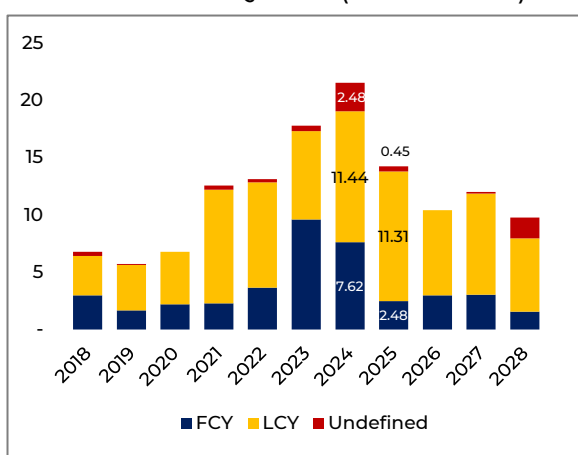
Source: BSP

Corporates

Many corporates continue to face persistent funding mismatches where current liabilities exceed current assets. The reliance on short-term funding for long-term investment adds to this risk. Firms with high short-term debt that will mature in 2024/25 (Figure 1.15) may be subject to a maturity wall. The availability of information on debt refinancing may temper investors' negative perception.

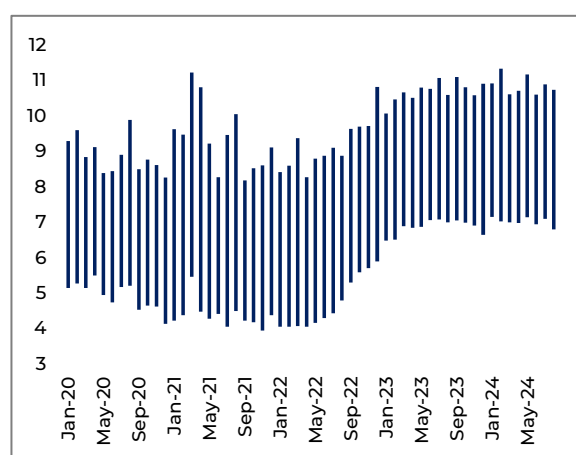
High leverage amplifies vulnerability to adverse shocks as elevated debt levels intensify the impact of earnings fluctuations on firms' ability to meet obligations. While overall debt-servicing capacity has improved amid increased profitability, a maturity wall and higher leverage may make refinancing challenging at higher interest rates (Figure 1.16).

Figure 1.15
Corporate Debt Maturity
PH NFCs as of Q3 2024 (In PHP trillion)



Source: S&P Capital IQ, OSRM Calculation
Note: FCY = Foreign Currency, LCY = Local Currency, Undefined = No Data Available

Figure 1.16
Range of Lending Rates to Corporations
PH UKBs (In percent annum)



Source: BSP
Note: Top/Bottom of Column are the Effective High/Low Rates for the Period

Corporates are reliant on bank funding. The close interlinkages between corporates and DSIBs amplify risks within the financial network. If any of these large corporates experience financial distress due to elevated leverage, funding mismatches, or refinancing difficulties, asset quality and capital adequacy of banks can decline. A common practice within conglomerate structures is to lend to a subsidiary/affiliate (Figure 1.17). While such related-party transactions are allowed, this must be conducted in an arm's length basis within prudential limits.

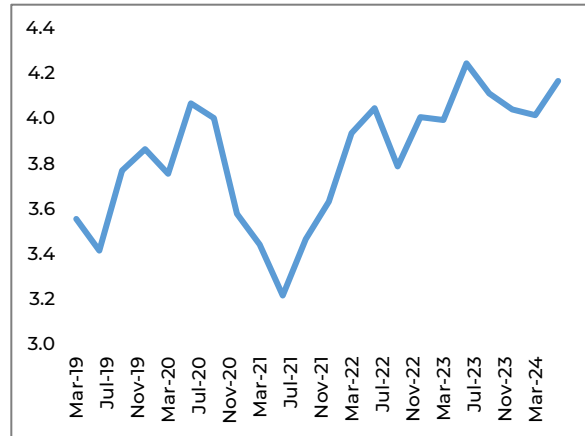
Households

Households are faced with debt-servicing risks given unavailable cash buffers. With limited savings and exposure to uncertainties, households may face difficulties in meeting debt obligations. Households' unsecured borrowing such as credit cards and salary loans have increased.

Government

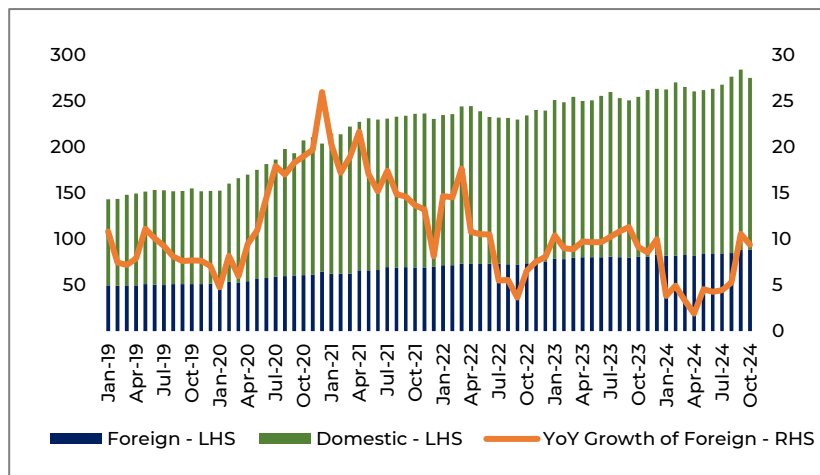
The growth in foreign loans at the start of the pandemic accelerated but public debt continues to be primarily domestic. The government's low and manageable share of short-term and foreign debt permits a stable fiscal position (Figures 1.18 and 1.19). Public debt-to-GDP ratio has declined from its peak of 63.6 percent in September 2022 to 61.3 percent in September 2024. Meanwhile, FX reserves are robust allowing higher import cover, maintenance of its manageable share of foreign debt, and resilience against FX fluctuations, which can impact the cost of interest payments for foreign debt (Figure 1.20). Nonetheless, the growing share of USD-denominated debt warrants monitoring, as it subjects the country's fiscal position to FX fluctuations, on top of increasing debt-servicing obligations post-pandemic (Figures 1.21 and 1.22).

Figure 1.17
Borrowings from Foreign Affiliates
PH Firms (In USD billion)



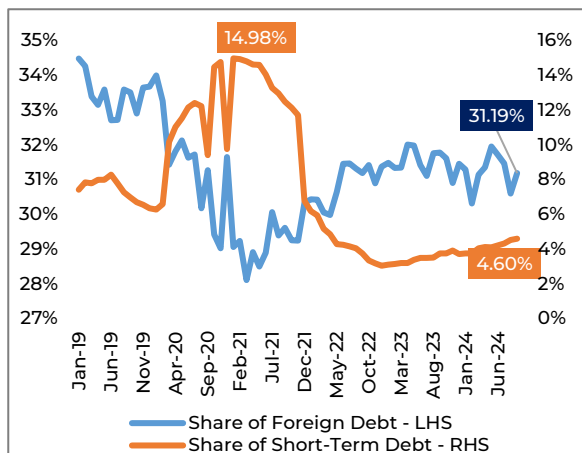
Source: S&P Capital IQ, OSRM Calculation

Figure 1.18
Public Debt
Levels (In USD billion), YoY Growth (In percent)



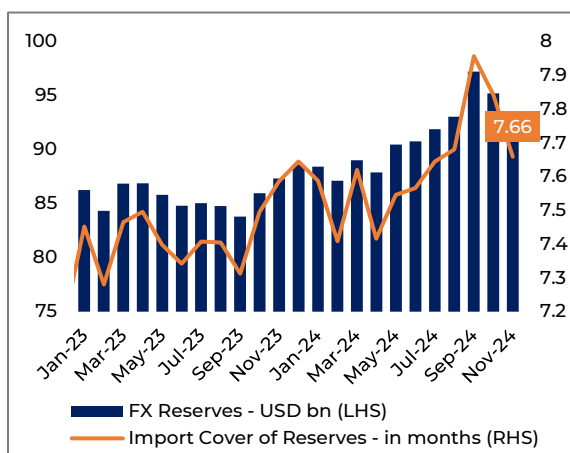
Source: CEIC Data

Figure 1.19
General Government Debt Outstanding
 Share of Total Outstanding Debt (In percent)



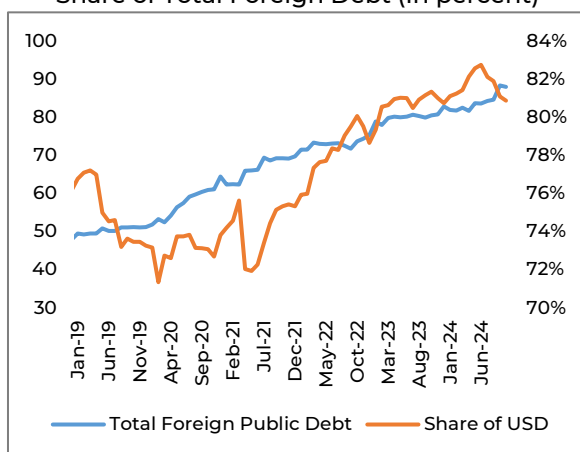
Source: World Bank

Figure 1.20
Monetary Reserves
 PH Firms (In USD billion)



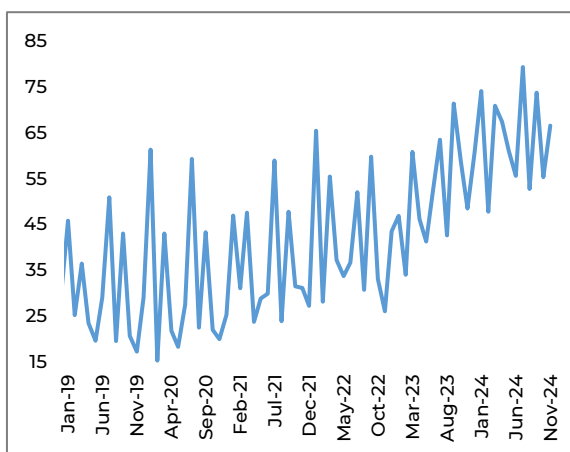
Source: BSP

Figure 1.21
Foreign Public Debt
 Levels (In USD billion),
 Share of Total Foreign Debt (In percent)



Source: World Bank

Figure 1.22
Public Debt-Interest Payments
 Levels (In PHP billion)



Source: BSP

Climate risks

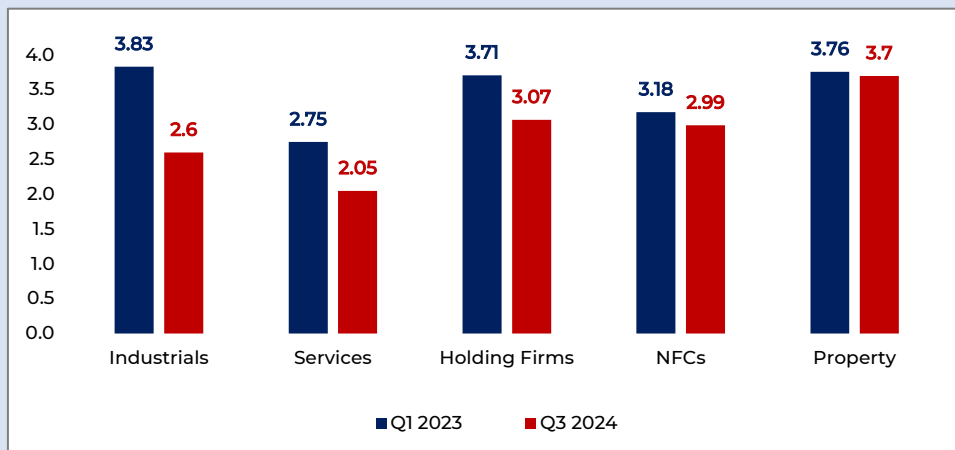
Households, businesses, and governments face climate-related risks. While natural disasters are common in the Philippines, rising temperatures have increased its unpredictability. As climate change effects are seen to be more severe, the impact on economic growth could compound over time. The Philippines lies on the Pacific Ring of Fire, and the typhoon belt, where nearly one-third of the world’s tropical cyclones form. Shocks, as seen during calamities, result in large economic losses and cause stress on the financial system.

Building upon this assessment, the next sections of the report provide a more granular analysis of the identified risks and their implications on segments of the Philippine financial system. Chapter 2 focuses on the financial sector covering banks, non-banks, and capital markets, while Chapter 3 covers the corporate and household sectors highlighting their resilience and sources of vulnerabilities that require close monitoring. Chapter 4 discusses selected policy measures and macroprudential tools, including efforts to further develop the capital market and a countercyclical capital buffer to support financial stability.

Box Article 1: Emerging Risks to the Industrial Sector

The average YoY expansion of the industrial sector for the past three quarters (6.0 percent) has exceeded GDP growth (5.8 percent). But the industrial sector is vulnerable to economic cycles, being reliant on the performance of the upstream and downstream supply chain, while facing pressure from weakening demand and trade rebalancing. However, the vulnerability of the industrial sector can be traced to two emerging risks. First, the sharp deterioration in the sector's twelve-month rolling interest coverage ratio (ICR) may signal an emerging risk (Figure A).

Figure A
Median Interest Coverage Ratio
by Industry



Source: S&P Capital IQ, OSRM Calculation

Manufacturing, under the industrial sector, is an important driver of economic growth. Production of electrical components employed an average of 14.1 percent⁹ of total manufacturing workers¹⁰ or approximately 154,000 workers. Electrical components & equipment are the main export products of the Philippines, with the share to total exports growing from 49.3 percent in 2019 to 55.7 percent in 2023.

The sector faces debt-servicing risk amid potential difficulty to generate sufficient revenues to service future debt obligations. The decline in ICR of *electrical components & equipment subsector* (Figure B) is driven mainly by the decline in *earnings before interest and taxes (EBIT)*—as a main measure of corporate profitability—from Q4 2022 to Q3 2024.¹¹

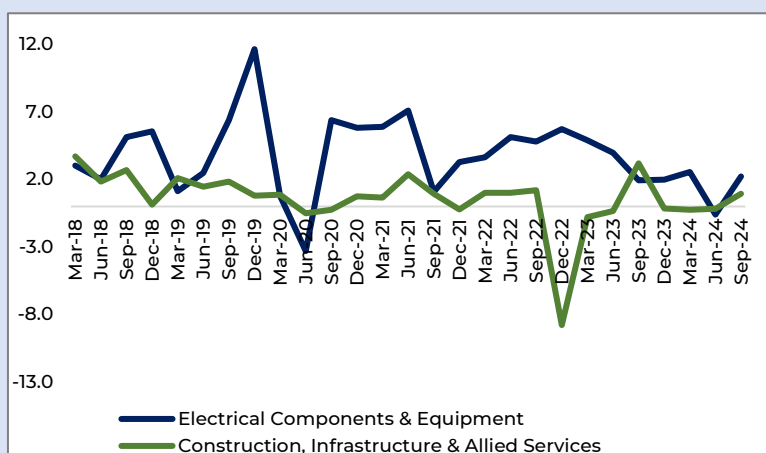
Another downside risk to corporate profitability in the electrical components & equipment subsector is the inability of local firms to meet the shifting global preference from intermediate electronic goods to finished goods (for end-users) particularly gadgets, appliances, and advanced technology solutions. Over time, the demand for finished electronic goods, as measured in the annual growth in imports of broadcasting equipment, television sets, etc., has already outpaced that for intermediate outputs. Based on domestic company disclosures, corporate profits from appliances (mainly from production of air conditioning units) and advanced technology solutions (i.e., component parts for radar and radio frequency technology for telecommunications) business segments have been growing, whereas profits from intermediate goods (i.e., semiconductors and printed circuits) have declined. This drastic shift in preference may be due to the rising pace of technological expansion in AEs across the globe. To capture global demand, domestic companies need to upscale their manufacturing base to diversify products in line with shifts in importers' preferences. Upscaling would require large amounts of capital financing.

⁹ The next largest share of manufacturing employment is *other food products*, with a four-year average of 10.29 percent.

¹⁰ Relevant subsector data available is from 2019-2022 as of 18 December 2024.

¹¹ Meanwhile, the ICR of the *construction and infrastructure subsector* has historically remained below the acceptable threshold of 2.0 due mainly to subdued earnings and consistently high and increasing interest expense. The *subsector* often involves large-scale and gestating projects with significant financing needs. Its ICR historically remaining below 2.0 could dampen investor confidence that could present challenges with respect to attracting direct investments that is essential for the subsector's growth and expansion.

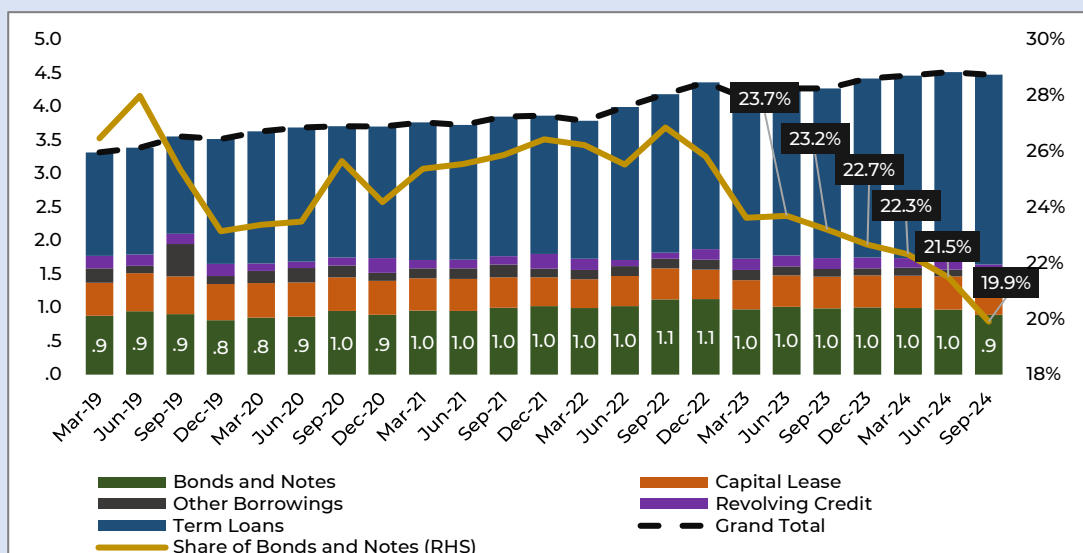
Figure B
Interest Coverage Ratio
by Industrial Subsector



Source: S&P Capital IQ, OSRM Calculation

Overall, the industrial sector’s limited source of financing and heavy reliant on bank loans, make it susceptible. As of Q4 2024, out of 70 industrial firms,¹² 11 firms, mostly from the *electricity, energy, power & water subsector* and with holding companies, were able to issue securities, amounting to approximately PHP 233 billion¹³ (roughly 7.5 percent of total historical bond issued amounts). Despite the need for large sums of capital and time to recoup that investment, only a single firm from the *electrical components & equipment subsector* has accessed the capital market. **Figure C** shows that total leverage has grown but the share of bonds and notes in its capital structure has declined.

Figure C
Corporate Debt of Industrials Sector
Philippines, (In PHP trillion)



Source: S&P Capital IQ, OSRM Calculation

¹² Following S&P Capital IQ’s classification.

¹³ Source: Philippine Dealings & Exchanges Corp. Total reflects the total of peso-denominated bond issuances of firms classified as *Industrials* under S&P Capital IQ. Data was extracted as of end-2024.

CHAPTER 2: FINANCIAL SECTOR

2.1. Banks

The PBS performed strongly in 2024 with sustained asset growth and improved profitability as well as robust capital base and ample liquidity levels. Banks showed resilience with increased lending activities and deposit-taking (Table 2.1). Year-to-date net income stood at ₱290.1 billion in September 2024, equivalent to a YoY increase of 6.4 percent. Capital Adequacy Ratio (CAR) stood at 16.4 percent while liquidity coverage ratio reached 185.8 percent, both above the minimum requirements.

Table 2.1
Selected Philippine Banking System Indicators

1. Financial Highlights			
Item	Levels (In PHP billion) as of Q3 2024	Growth (Percent) Q3 2023 to Q3 2024	Average Annual Growth (Percent) 2019-2024 ¹⁴
Total Assets	26,737.4	11.4	8.8
Total Loan Portfolio (TLP), gross (excl. of IBL and RRP)	13,620.8	11.0	7.2
Financial Assets, gross (net of amortization)	7,432.0	10.2	14.8
Deposits	19,581.1	7.1	8.1
Annualized Net Profit	374.0	10.7	16.1
2. Number of Institutions by Banking Segment ¹⁵			
Universal and Commercial Banks (UKBs)	Thrift Banks (TBs)	Rural and Cooperative Banks (RCBs)	Digital Banks (DGBs)
44	41	383	6

Source: BSP

Bank assets expanded with loans maintaining moderate growth. As of September 2024, PBS' total assets stood at ₱26.7 trillion with UKBs holding 93.9 percent. PBS total loan portfolio (TLP) grew by 11.0 percent YoY, lower than the pre-pandemic average¹⁶ of 15.1 percent (2015-2019). On a per group basis, UKBs saw the least growth in lending activities with 10.7 percent YoY. Meanwhile, Thrift Banks (TB), Rural/Cooperative Banks (RCB), and Digital Banks (DGB) expanded their lending activities by 14.5 percent, 18.2 percent, and 28.8 percent YoY, respectively. Lending growth is driven by the aggressive expansion in household consumption loans but tempered by the slower growth in loans to production (Figure 2.1).

Loans regained momentum while the growth of financial assets is lackluster. This trend is a departure from the prior years when financial assets saw significant growth reaching share to total assets of 27.8 percent compared to pre-pandemic average (2015-2019) of 20.5 percent.¹⁷ This is primarily due to rising interest rates in 2022 which prompted banks to rebalance their portfolios toward fixed-income securities to maintain viable interest spreads. As interest rates eased in 2023 to 2024, average growth in financial assets slowed to 10.0 percent. In September 2024, YoY growth was 10.2 percent (Figure 2.2).

¹⁴ Average growth is calculated as the average YoY growth across all quarters from 2019 to 2024.

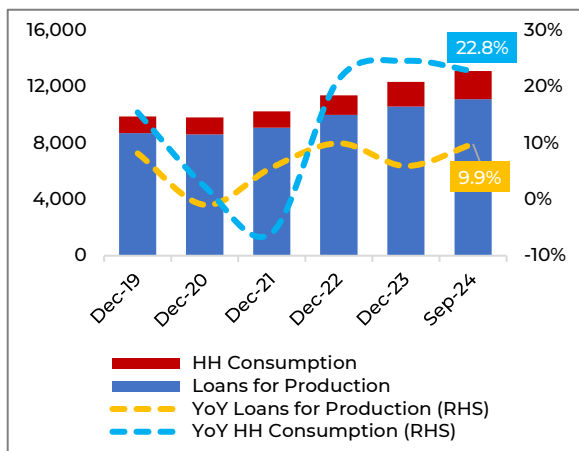
¹⁵ Preliminary data as of December 2024

¹⁶ Pre-pandemic average is calculated as the average YoY growth across all quarters from 2015 to 2019.

¹⁷ Pre-pandemic average is calculated as the average share of financial assets to total assets across all quarters from 2015 to 2019.

Figure 2.1
PBS Production and HH

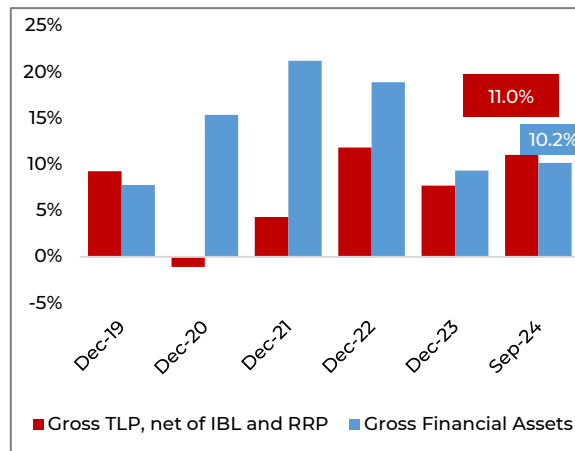
Levels, In PHP billion (LHS), YoY Growth (RHS)



Source: BSP

Figure 2.2
PBS TLP vs. Financial Assets

YoY Growth



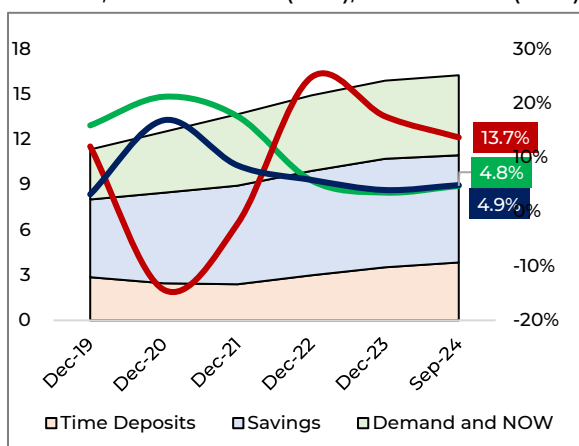
Source: BSP

Growth in savings deposits has been slower at 4.9 percent compared to time deposits which grew by 13.7 percent (Figure 2.3).¹⁸ Banks also sought other sources of funding through bond issuances and bills payable, the latter posted a YoY growth of 76.1 percent. In 2024, six banks have issued bonds for a total of ₱195.7 billion.¹⁹

Higher interest rates tempered banks' net interest margin. The high-for-long interest rate period affected bank profitability given higher interest expense. Consequently, the growth in net interest income slowed as the expansion in interest expense (28.1 percent) outpaced interest income (18.1 percent) (Figure 2.4). Competition for deposits among banks amid projected expansion in loans could add pressure on banks' net interest income.

Figure 2.3
PBS Peso Deposit Composition

Levels, In PHP billion (LHS), YoY Growth (RHS)

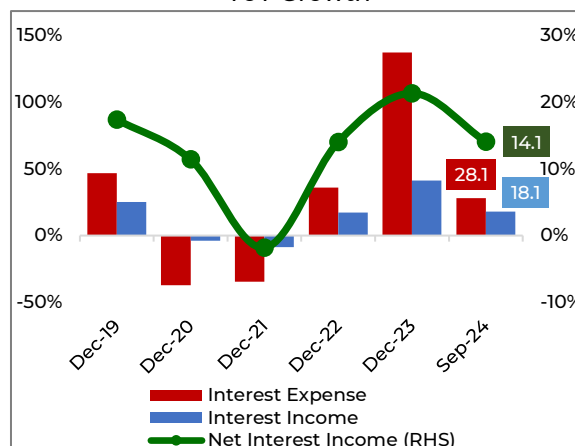


Source: BSP

Notes: As of September 2024, LTNCDs declined to ₱37 billion or 62.1 percent lower than the prior year.

Figure 2.4
Net Interest Income

YoY Growth



Source: BSP

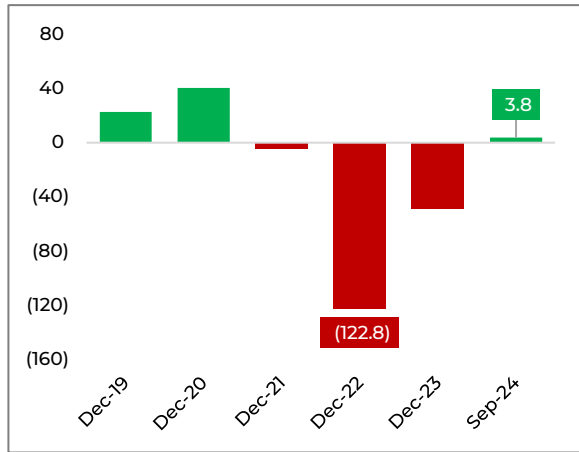
¹⁸ Under Circular No. 1059, the issuance of long-term negotiable certificates of time deposit (LTNCTDs) has been subject to an indefinite moratorium.

¹⁹ PDS listings and enrollments by banks as of November 2024.

Year-to-date non-interest income registered ₱171.9 billion in September 2024, a 2.3 percent improvement a year prior, with fees and commissions mainly contributing at ₱118.6 billion. Trading income generated ₱18.9 billion, ₱4.2 billion of which are realized gains from FX transactions. However, FX losses under Other Income (i.e., revaluation of FX assets and liabilities) reached ₱3.4 billion, a decline from a registered gain of ₱8.4 billion a year prior.

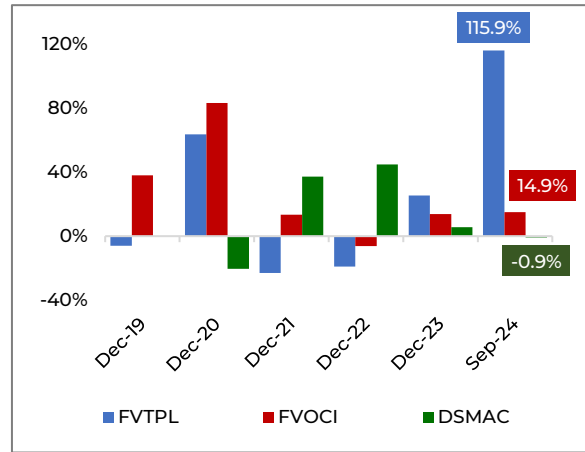
Declining interest rates resulted in asset portfolio gains. As of September 2024, banks registered gains on unrealized MTM valuations on financial assets measured at FVOCI (Figure 2.5). The improvement, mainly attributed to declining interest rates and increased trading activity, helped banks manage MTM losses. By the end of 2023 (Figure 2.6), banks tilted their portfolios in favor of securities classified as FVOCI and Fair Value Through Profit or Loss (FVTPL) against Debt Securities Measured at Amortized Cost (DSMAC). This trend persisted in 2024, with significant growth in FVTPL allocations, reflecting banks' strategic positioning.

Figure 2.5
Unrealized Gains (Losses) on FVOCI Financial Assets
In PHP billions



Source: BSP
Notes: As of September 2024, LTNCTDs declined to ₱37 billion or 62.1 percent lower than the prior year.

Figure 2.6
PBS Financial Assets
YoY Growth



Source: BSP

Tight financial conditions and global uncertainties impact loans to certain industries. Loans for production rose by 9.9 percent YoY at 11.1 trillion in September 2024, lower than the pre-pandemic average of 14.6 percent (2017-2019).²⁰ Real estate activities remain the major recipient of production loans with 18.0 percent loan portfolio allocation as of September 2024, followed by trade and manufacturing.²¹ These are the same sectors that registered the highest loan growth: real estate (+13.9 percent), wholesale and retail trade (+12.3 percent), and manufacturing (+10.8 percent). Notably, they are also the top contributors to NPL. YoY growth of UKB NPL in the wholesale and retail trade in September 2024 reached 44.9 percent. These sectors are also likely to be affected by offshore shocks such as oil price swings exacerbated by geopolitical tensions, supply chain disruptions, and interest rates volatility.

Real estate loan (REL) exposures need closer monitoring amid evolving market conditions. The high-interest rate environment, shifting consumer preferences, remote work arrangements and recent government pronouncements banning Philippine Offshore Gaming Operators

²⁰ Pre-pandemic average is calculated as the average YoY growth across all quarters from 2017 to 2019.

²¹ Recently surpassed by Electricity, Gas, Steam, and Air-Conditioning since January 2024.

(POGOs) have implications on the sector's loan quality. Recent data also indicate oversupply, particularly in the condominium segment, which could take 34-months before it can be sold.²²

These factors contribute to rising NPLs in the real estate sector, along with the expansion of RELs (Figure 2.7). This portfolio is mostly comprised of commercial real estate (62.5 percent). However, majority of the non-performing RELs are residential RELs at 65.2 percent against commercial RELs at 34.8 percent as of September 2024.²³ Based on the results of the Consumer Expectations Survey (CES) as of Q4 2024, 5.0 percent of households plan to buy/acquire real property in the next 12 months, a slight improvement from 4.8 percent recorded in the previous year. Further details on the state of the real estate sector can be found in Box Article 2.

An aggressive expansion has also been observed in consumer loans.²⁴

Consumer loans grew by 16.5 percent YoY in September 2024. The share of consumer loans to total loans has increased to 22.0 percent from 18.0 percent in September 2019.²⁵

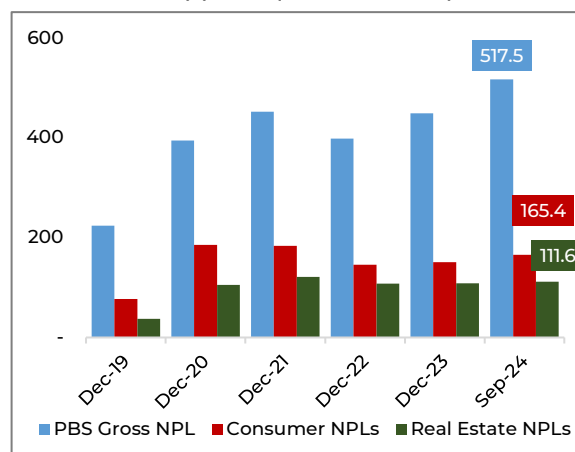
As growth of production loans decelerated, consumer loans picked up as a strategy to maintain a viable interest spread. This shift reflects the imposition of higher interest rates on consumer loans to compensate for the higher credit risk associated with this segment. Meanwhile, factors such as inflationary pressures, higher borrowing costs, debt repayment capacity, among others, have contributed to the rise in consumer NPLs. In September 2024, consumer NPLs increased to ₱165.4 billion or 9.9 percent YoY growth (Figure 2.7).

The uptick in consumer related NPLs is largely attributed to credit cards and salary loans. Impairments on credit card receivables and salary loans contributed 6.4 and 4.0 percentage points to the growth of consumer NPLs, respectively. This development warrants close monitoring of consumer related NPLs alongside the growing concern over debt servicing capacity of households (refer to Chapter 3: Corporates and Households).

Overall asset quality has remained satisfactory. PBS NPL ratio remained manageable at 3.5 percent as of September 2024. While UKB NPLs are elevated for the wholesale and retail trade (6.5 percent), real estate (3.6 percent), and manufacturing sectors (4.4 percent), the UKBs' gross NPL ratio stood at 3.2 percent. NPL ratios of other banking groups, namely TBs, RCBs, and DGBs, ranged between 6.9 percent and 11.2 (Figure 2.8). NPLs have a coverage ratio²⁶ of 93.3 percent, lower than the NPL coverage ratio in 2023 at 103.7 percent.

High capitalization allows banks to absorb unexpected losses despite rising NPL ratios. A break-even NPL ratio²⁷ was simulated to generate the level that would bring down CAR to a regulatory

Figure 2.7
PBS Group NPL
Philippines (In PHP billion)



Source: BSP

²² Based on the November 2024 monthly report released by Leechiu Property Consultants, the oversupply will take 34 months to be sold driven by the increase in available units. This is an increase from the 29 months oversupply posted in the October 2024 report.

²³ Based on the Report on PBS Real Estate Exposures (REEs).

²⁴ Inclusive of Residential Real Estate Loans

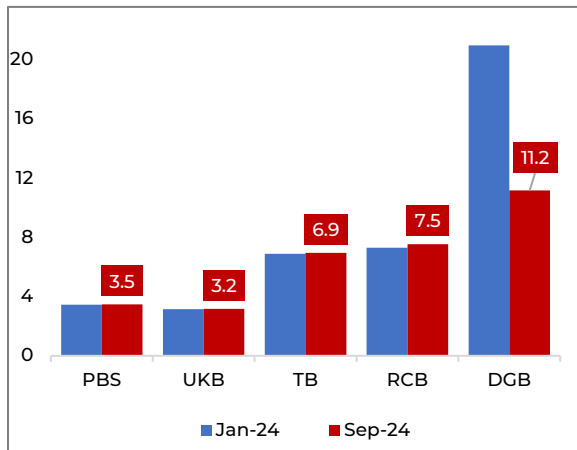
²⁵ Total Consumer Loans to TLP, net of IBL

²⁶ Ratio of allowance for credit losses to gross NPL.

²⁷ Based on the AMRO Country Report ACR/22-06, the reverse stress test calculates the additional NPL needed to reduce CAR to 10.0 percent. This models the impact of a decline in asset quality, through provisions, on banks' capital adequacy. The simulation, both qualifying capital (numerator) and risk-weighted assets (denominator), are reduced by 75.0 of additional NPL.

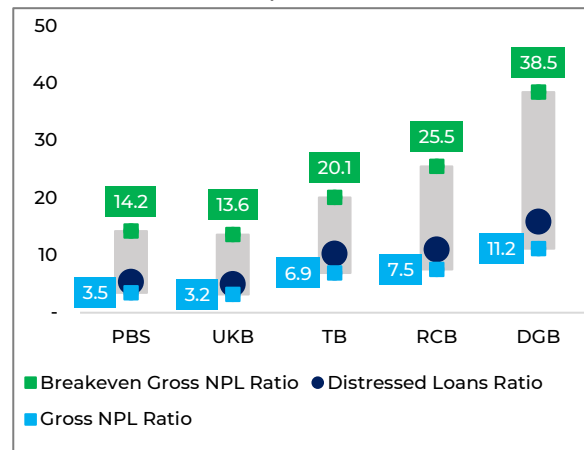
minimum of 10.0 percent. Results showed a break-even NPL ratio of 13.9 percent indicating adequate buffer compared to a baseline NPL of 3.5 percent. Similarly, banking groups maintained ample loan quality buffer as their respective gross NPL ratios are way below the breakeven NPL ratio (Figure 2.9).

Figure 2.8
Gross NPL Ratio per Banking Group
In percent



Source: BSP

Figure 2.9
Baseline vs Breakeven Gross NPL
In percent



Source: BSP
Data as of September 2024

Forward-looking indicators stayed below break-even NPL ratio. Distressed loans ratio²⁸ of 5.4 percent and loans at risk (LaR) ratio²⁹ of 4.7 percent are well-below break-even NPL ratio. These indicators are assessed to project further deterioration in loan quality by considering past due and restructured loans which, if not managed properly, could turn into NPLs. Even with forward-looking indicators, banks appear well-positioned to absorb expected credit losses.

Prudential regulations provide necessary guardrails. Regulatory frameworks and other risk management tools are in place to mitigate concentration risks and improve resilience against risks. For example, the case of real estate industry is subject to ceilings such as the 25.0 percent REL limit. The Real Estate Stress Test results also show that exposures are well within desirable levels.³⁰

2.2. Non-banks

This section highlights the growing importance of NBFIs in providing specialized financial products and services. Increasing asset size (Table 2.2), widening reach and innovative offerings underscore their complementary role in the financial system and in supporting economic activity. However, growth of NBFIs also brings in potential risks, including interconnectedness with banks and exposure to the broader market ecosystem. This necessitates closer monitoring to ensure that risks are well-managed.

²⁸ Ratio of total past due loans and current restructured loans to gross TLP.

²⁹ Ratio of gross NPL and performing restructured loans (current and past due restructured loans but not yet non-performing) to gross TLP.

³⁰ Under Section 363-A of the Manual of Regulations for Banks (MORB), a stress test will be undertaken on a UB's/KB's REEs and other real estate property under an assumed write-off of 25 percent, of which such bank is subject to a regulatory limit of 10-percent CAR after the write off.

Table 2.2
Size of Selected Non-Bank Financial Institutions

Item	No. of Firms	Total Assets (In PHP billion as of 30 June 2024)	Growth (Percent) Q2 2023 to Q2 2024	Average Annual Growth (Percent) Q1 2020 to Q2 2024
Non-Banks with Quasi-Banking (QB license)	4	170.9	10.4	-9.7
Non-Bank without QB license	108	2,936.5	33.3	17.0
<i>With Trust Authority</i>	9	2,496.9	39.5	19.8
<i>Without Trust Authority</i>	99	439.7	6.4	7.9
Government Pension Funds	2	2,732.9	11.6	8.6
Insurance Companies	131	2,363.9	6.0	6.8

Sources: CEIC, IC, BSP, GSIS and SSS

NBFIs provide intermediary services but without a full banking license. NBFIs cannot accept deposits from the public so funds are sourced through other means like general borrowings, deposit substitutes, regular premiums and contributions from members. NBFIs complement banks in providing financial products and services to firms and households. While banks have the capacity to act like a “one-stop shop” that offers a range of financial services, NBFIs tend to offer specialized products to targeted customer segments.

NBFIs provide specialized services (i.e., risk pooling, fund management, brokerage, infrastructure services) to niche markets. Differences in regulations applied on different NBFIs provide opportunities to have greater flexibility to innovate. NBFIs face competition from banks and their subsidiaries. UKBs and their subsidiaries have etched a strong foothold in major urban centers and have expanded their operations in other areas that are also catered to by other banks and NBFIs.

NBFIs’ services cut across banking, insurance, and securities that are under the purview of various regulators. The BSP supervises/regulates quasi-banks and NBFIs which are part of banking groups.³¹ These include financing companies, investment companies, and security dealer-brokers.³² The IC oversees life and non-life insurers, and mutual benefit associations, while the SEC regulates stand-alone investment companies, financing firms, and securities brokers/dealers. Government pension funds—the Government Service Insurance System (GSIS) and Social Security System (SSS)—are under the purview of the DOF. Given their varied functions and regulatory oversight, NBFIs consist of a broad range of institutions with diverse roles and financial profiles. This may open some leeway for potential regulatory arbitrage. Key categories of NBFIs and their contributions to the financial system are described below.

Non-Bank with Quasi-Banking (QB) License. QB refers to a type of financial activity where a bank or financial institution borrows money from 20 or more lenders at the same time, using debt instruments like promissory notes or trust certificates, rather than traditional deposits. The borrowed funds are then used for relending or buying receivables and other financial obligations. This sector, with five firms, hold ₱170.9 billion in assets as of June 2024.

³¹ MORB and the Manual of Regulations for Non-Bank Financial Institutions (MORNBFII)

³² Among the entities supervised by the BSP that neither have trust nor QB licenses, only financing companies, investment houses, and non-stock saving and loan associations are covered in the discussion.

Non-Bank without QB License. This sector holds substantial assets and grew 33.3 percent YoY in 2024. Annual average growth rate was 16.9 percent since 2020. The 108 firms³³ can further be divided into two types: those with trust authority and those without.

With Trust Authority. A trust license is an authorization granted to a financial institution, allowing it to engage in fiduciary business activities. Main services include investment management, custodianship, and estate administration. The seven trust corporations and two investment houses hold ₱2,496.6 billion in assets under management as of June 2024 or 39.5 percent higher YoY.

Other NBFIs. There are 99 non-bank entities with neither QB nor trust authority. They are either financing companies, investment houses, non-stock savings and loans association, security dealer-brokers, or credit card companies. With ₱439.7 billion in aggregate assets, they grew 6.4 percent YoY, with an average annual growth rate of 7.9 percent since 2020.

Government Pension Funds. The GSIS and SSS manage a combined ₱2,732.9 billion in assets as of June 2024, reflecting an 11.6 percent growth YoY and an annual growth of 8.6 percent since 2020. Among the NBFIs, they are the largest holders of GS to match their long-term liabilities. Other than debt securities, their financial asset portfolio is also allocated to equities, mutual funds, externally managed funds and other financial assets. They also offer various types of loans to their members and pensioners. Loans are 16.0 percent of their assets as of December 2023. Profits increased by 40.3 percent from 2022 to 2023 owing to a rise in service and business income.³⁴

Insurance Companies. The insurance sector, with 131 firms, held ₱2,363.9 billion in assets as of June 2024, growing 6.0 percent YoY and 6.8 percent annually since 2020. It includes life insurers, non-life insurers, and mutual benefit associations (MBAs). Life insurers offer savings-linked policies and retirement plans, while non-life insurers provide asset and liability protection. MBAs focus on affordable insurance for underserved groups. The sector enhances financial resilience by pooling a wide variety of risks and supporting recovery from unexpected events. Like pension funds, insurance companies' core investments are mostly GS. The insurance industry recorded a 4.2 percent increase in annual income. Majority of their income came from premiums earned from insurance contracts, and investment income, which averaged 5.8 percent of their total revenues.

Vulnerabilities of NBFIs may emerge particularly in the areas of leverage and asset valuation. NBFIs' expansion in lending activities against the highly regulated banking sector increased leverage in the financial system. This risk arising from interconnectedness between NBFIs, and the broader financial system could be transmitted through common exposures (**Table 2.3**).

NBFIs' loan portfolios have recovered. After an average annual contraction of 1.1 percent from year 2020 to year 2022, loans stood at ₱1.3 trillion in December 2023 — equivalent to a 5.2 percent increase YoY. However, the upward trajectory in leverage heightens credit risk.

³³ There are 2,244 entities under BSP regulation with pawnshops, money service businesses, and remittance agents comprising the majority. The values presented only covers 108 reporting firms.

³⁴ For SSS, accounting for the changes in policy reserves will result into a net loss. Accounting for changes in policy reserves are not conventionally included in the computation of net income.

Table 2.3
Assets of Selected Institutions of the Financial System

	Loans		Financial Assets					
	2023	2022	Debt Securities		Equity Securities		Other Financial Assets	
			2023	2022	2023	2022	2023	2022
Non-Bank with Quasi-Banking License	141.3	128.2	3.3	2.9	2.1	1.5	NA	NA
Non-Bank without Quasi-Banking License	382.0	368.2	36.7	34.4	22.0	20.1	1,637.9	1,227.6
<i>With Trust Authority</i>	54.6	51.8	NA	NA	0.0	0.0	1,637.9	1,227.6
<i>Without Trust Authority</i>	327.3	316.4	36.7	34.4	22.0	20.1	-	-
Government Pension Funds	358.7	354.4	1,054.3	901.1	436.4	410.6	78.9	56.4
Insurance companies	41.5	39.1	399.8	403.7	NA	NA	1,326.3	1,318.3
In-House Financing by Real Estate Developers	385.7	354.8	NA	NA	NA	NA	NA	NA
Total	1,309.2	1,244.7	1,494.1	1,342.2	460.4	432.1	3,043.1	2,602.3

Source: BSP, AsianBondsOnline, CEIC, IC, GSIS.

Notes: Loans data are as of December 2023 and may include other receivables for some institutions; Insurance companies' financial assets are as of 2021 and 2022; NA – not available

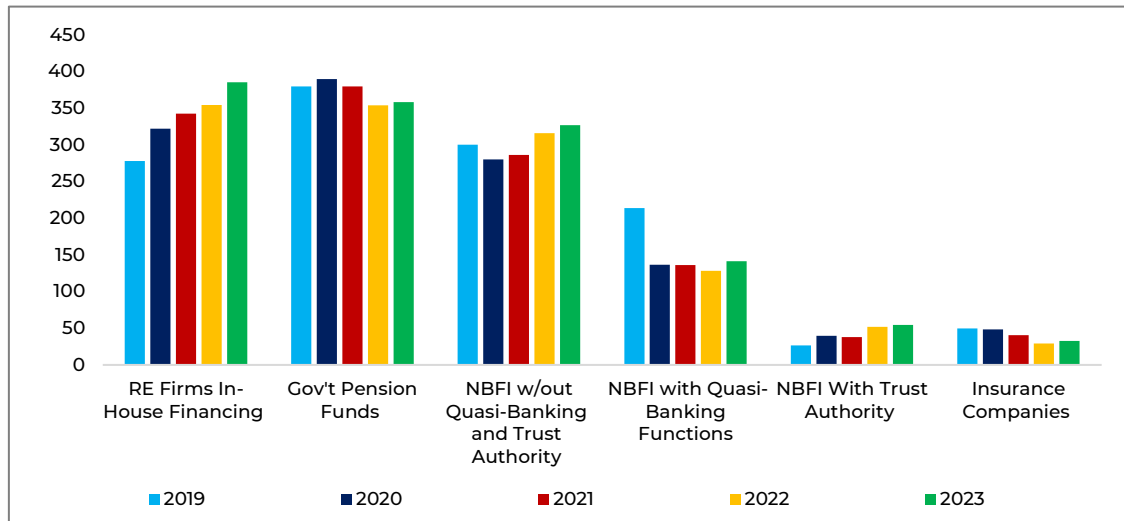
Credit as an asset class is particularly affected by the high-for-long interest rate regime. Using a sample of life insurance companies³⁵ and government pension funds, the calculated YoY increases in loans are 6.2 percent and 1.2 percent, respectively. There is also a 65.1 percent increase in loans of BSP-Supervised NBFIs with Trust Authority (₱88.7 billion). Meanwhile, based on a sample of in-house financing of real estate firms,³⁶ loans rose 8.7 percent YoY to ₱385.8 billion in 2023 (**Figure 2.10**). The quality of these exposures must be monitored given the increasing NPL ratio in the banking system particularly on household loans and certain segments of production sectors, to which these NBFIs may be similarly exposed.

NBFIs that are focused on consumer finance and micro, small and medium-sized enterprises (MSMEs) are gaining ground, along with innovative solutions to extend borrower reach. These lenders have experienced rapid growth in recent years, with some being supported by domestic and foreign banks through loans or equity. These funds are then typically re-lent to households and MSMEs, often in underserved sectors. This trend brings with it innovations such as point-of-sale (POS) loans in conjunction with traditional financial products. While these enable broader access to credit, it also exposes NBFIs to higher credit risk due to the nature of their target market. Consequently, banks acting as fund providers may face indirect exposure to both credit and liquidity risks.

³⁵ The sample consists of top six life insurance companies in terms of asset size. This includes Sun Life of Canada (Philippines), Inc.; AIA Philippines Life and General Ins. Co. Inc.; Philippine AXA Life Insurance Corporation; Insular Life Assurance Company, Limited; Pru Life of UK Philippines; and Manulife Philippines.

³⁶ The sample consists of top 11 real estate and development management firms in terms of assets from S&P capital IQ, accounting for 83 percent of all listed real estate and development management firms.

Figure 2.10
NBFi Loans
In PHP billion



Source: BSP, IC, GSIS, and SSS, RE Firms' Company Filings

Common exposures are relatively low, in terms of amount, between banks and NBFIs but these are possible sources of price and valuation risks. Majority of government issuances are held by banks followed by government pension funds and insurance firms (life and non-life). If these GS are tradable, decrease in market value may materialize if a large number of firms face a significant liquidity stress, i.e., when firms are forced to liquidate their asset holdings in a fire sale. A decrease in the market value of these assets can spillover to the banking system. Changes in market value also impact other investors.

The expected global transition to a more accommodative monetary policy environment may affect insurers and pension funds. Lower interest rates may depress future profitability, particularly on interest income since a large fraction of their portfolios are invested in debt securities. Low interest rates will impact pension funds and insurance companies by affecting re-investment returns on their fixed-income portfolio. This may also cause pension funds and insurers to search for higher yields from riskier investments.

The increasing importance of NBFIs may require closer monitoring. The significant expansion of NBFi activities complement banks. Insurance companies have continued to maintain their Risk-Based Capital Ratio above 100.0 percent for the past three years while government pension funds have extended the life of their respective funds. With increased interdependence between banks and non-banks, systematic monitoring and assessment of these interlinkages necessitates the closure of existing data gaps. Inter-agency bodies such as the Financial Sector Forum (FSF) and FSCC provide a common venue to address regulatory issues and cross-cutting risks.

2.3. Capital markets

Capital markets provide source of funding as an alternative to banks and non-bank financial intermediaries. In the corporate sector, preference on bank loans as a source of funding persists. Foreign debt exposures, mostly USD-denominated, have likewise risen among large conglomerates. Deepening the capital markets could reduce concentration risks in the banking sector and offer solutions to mitigate FX risks. Enhancing the capital markets would strengthen the resilience of the financial system as a whole.

While there have been significant developments in both equity and fixed income markets over the years (**Table 2.4**), structural issues remain. Key factors affecting the current state and outlook of the domestic capital market are discussed below.

Deepening the domestic capital market could lessen dependence on banks for funding requirements. Diversifying the sources of funds by providing alternative options in the capital market could reduce concentration risks in the banking sector. Bank loans have historically been the preferred source of funding for Philippine corporations, accounting for 84.7% of total corporate borrowings.³⁷ The preference to secure loans has risen in 2024, with the 12-month average ratio of corporate loans to debt securities reaching 5.1, up from 4.3 over the same period in 2023.³⁸ This increase is commonly not a concern during an economic boom, but it can trigger significant challenges during a slowdown. An economic downturn reduces corporate revenues, makes banks more cautious in lending, and worsens overall liquidity conditions. The confluence of heightened risk aversion and liquidity pressures could lead to the deleveraging of banks during periods of stress.

Table 2.4
Performance of the PH Bond and Equity Markets

	Value (In PHP billion) as of Q3 2024	Growth (Percent) Q3 2023 to Q3 2024
Bond Market		
Total Outstanding Bonds	13,008.4	9.3
Government	10,800.8	11.7
Corporates	1,321.9	(14.9)
Central Bank (Bills)	885.7	30.7
	Value (In PHP billion) as of end 2024	Growth (Percent) Q4 2023 to Q4 2024
Equity Market		
Market Capitalization	14,281.6	11.7
Financial	2,063.2	28.1
Services	2,071.4	34.6
Mining & Oil	117.9	(20.1)
Industrial	2,318.6	5.1
Holding Firms	2,542.0	(8.6)
Property	1,677.5	(11.7)
	Turnover (In PHP billion) Average, 2024	Foreign Participation 2023 / 2024 (Percent)
Market		
Bonds	1,648.8	2.2 / 4.1
Equities	249.2	43.9 / 46.4

Note: Foreign Participation is the ratio of foreign activity to total market activity. Market Capitalization cited is domestic market capitalization. Total capitalization, which includes foreign companies, is 20.01Tn. Sector indices consist of representative stocks and do not necessarily add up to market capitalization.

The size of the bond market has grown substantially but unevenly across segments. Total outstanding bonds expanded from ₱6.6 trillion in 2019 to ₱13.0 trillion in 2024. However, the expansion has been concentrated in GS, while corporate issuances have struggled to gain momentum. In 2024, new corporate issuances have been outpaced by maturing bonds, reflecting stagnant utilization of debt instruments. Moreover, access to bond financing remains skewed to large corporations. Corporate issuances have consistently been investment grade,

³⁷ Based on data from Asia Bonds Online and FRP as of Q3 2024.

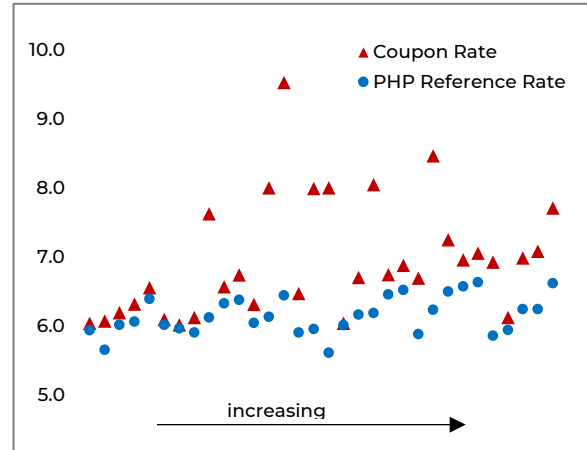
³⁸ The coverage compares September 2023–2024 to September 2022–2023. As of September 2024, the latest ratio of corporate loans to securities is 5.5.

with 85.8 percent of outstanding bonds rated Aaa and 12.0 percent rated Aa.³⁹ The lack of diversity in the market presents an opportunity to provide access beyond low-risk firms. There remains untapped potential for the private sector to utilize the debt instrument as a source of financing.

Corporate bond issuances have maintained a premium over treasuries, but secondary market activity has been timid. At the time of issuance, coupon rates of new corporate securities in 2024 have had a considerable premium over the prevailing market rates of GS of the same tenor (Figure 2.11).⁴⁰ Spreads are dependent on individual company fundamentals, but on the aggregate level the median premium is 0.4 percent.

Sectors such as industrials and real estate exhibited higher premiums. The former had premiums ranging from 0.6 percent to 2.2 percent, whereas the latter recorded premiums from 0.2 percent to 3.1 percent. Overall, corporate bonds retain some attractiveness, resulting in a healthy primary market take-up.

Figure 2.11
2024 Corp Issuances vs Reference Rates
In percent

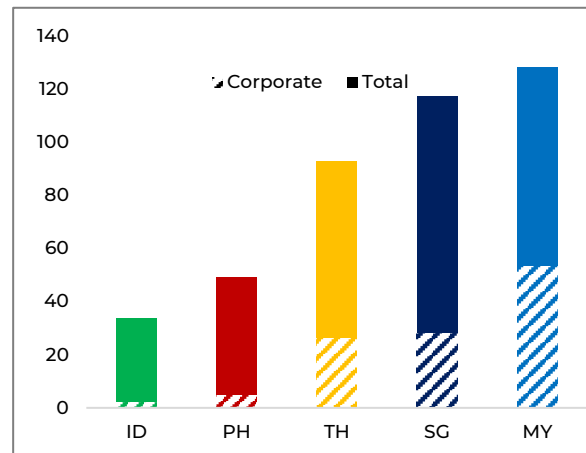


Source: PDS

However, activity has been sparse in the secondary market. Bid-ask spreads remain wide, the rate at which trades are executed is infrequent, and trading depth has been shallow relative to GS. To illustrate, the total trading volume of corporate bonds in 2024 is only 1.4 percent of the total volume of GS. The lack of trading activity suggests that bondholders of corporate issuances prefer to hold their securities to maturity. As a result, the price discovery of corporate bonds beyond its issuance date remains a focal concern.

Aside from uneven growth, the local bond market continues to lag relative to its regional peers. Among ASEAN-5, the Philippine bond market remains one of the smallest in terms of absolute size. This mostly holds true when scaled to GDP, only being marginally ahead of Indonesia (Figure 2.12). Furthermore, the development of corporate bond markets in other member states has progressed significantly, as evidenced by a greater share of corporate issuances. Other jurisdictions have leveraged digital innovations to expand market accessibility, particularly towards retail investors. For instance, Thailand has utilized distributed ledger technology (DLT) for both corporate and government bonds which started in 2019. These DLT bonds have been incorporated

Figure 2.12
Size of bond Market (H1 2024)
As percent of GDP, In percentage points



Source: AsianBondsOnline

Note: ID = Indonesia, PH = Philippines, TH = Thailand, SG = Singapore, MY = Malaysia

³⁹ The credit rating scale is based on PhilRatings, and the composition is based on rated outstanding PHP-denominated bonds as of 31 December 2024. The remaining 2.2 percent of outstanding bonds have ratings of A+, A-, and Baa+.

⁴⁰ Issuances in the chart are arranged by tenor ranging from 2-year to 10-year bonds.

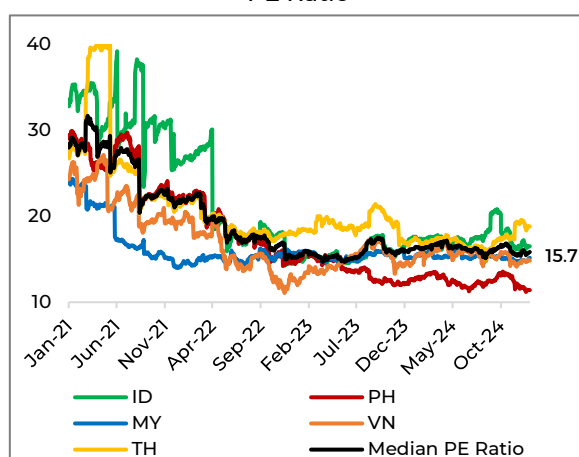
in a mobile application called Pao Tang,⁴¹ which allows market participants to trade their bonds in the secondary market. In effect, digital technology expands the accessibility of bonds and enhances liquidity in the secondary market.

The local equity market briefly exceeded pre-pandemic levels but has since lost momentum. PSEi market capitalization has exceeded that of 2023, but with some sectors showing mixed performance. Equity returns averaged -3.1 percent across the six sector indices relative to 2020, while the broader PSEi recorded a deeper decline of 15.7 percent. Persistent underperformance has been observed in holding companies and the property sector, with the latter about 40.0 percent lower than pre-pandemic levels. Furthermore, the property sector's earnings-per-share only grew 6.8 percent since 2020 while the rest of the sectors are logging double-digit growth. Another facet of equity market growth is the primary market, showing modest growth from 268 listed companies in 2019 to 286 in 2024. For the same time period, IPOs in the ASEAN region averaged 137 issuances annually, vis-à-vis three IPOs in the Philippines in 2024. This reflects the disparity in market size between the Philippines and other markets.⁴²

Post-pandemic equity market valuations appear lower compared to peers. Equity valuations in 2024 modestly increased after a dip in H1 2024 as earnings grew at a faster rate. Compared to ASEAN counterparts, PH equities are slightly below the median PE ratio. Forward valuations also suggest that corporate earnings will continue to be strong in 2025, with forward earnings per share (EPS) in 2024 trending higher compared to regional peers. (Figure 2.13).

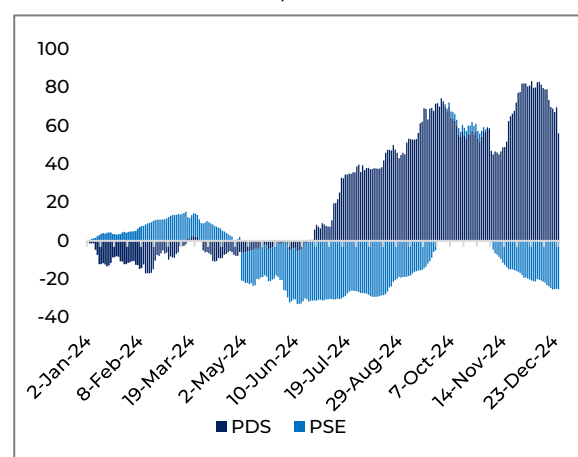
Substantial foreign activity in the equity market exposes it to global developments (Figure 2.14). Foreign participation plays a material role in the domestic capital markets as it makes up roughly half of the total trading value in equities. The flow of foreign funds, while influenced by domestic factors, is inherently tied to global volatility. In 2024, the movements in capital flows have largely followed the changes in market perceptions related to the Fed Funds rate, inflation, and GDP expectations. These movements, in turn, are also correlated with the direction of the local equity market index (Figure 2.15).

Figure 2.13
ASEAN Equity Performance
PE Ratio



Source: National Exchanges, Bloomberg

Figure 2.14
Net Foreign Trading
In PHP billion, YTD Cumulative



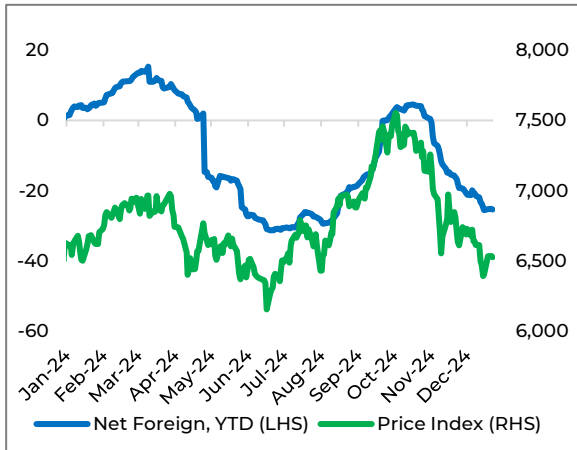
Source: PDS, PSE, OSRM Calculation

⁴¹ Pao Tang is a digital platform developed by Krungthai Bank, a state-owned bank. From 2022-2023, 17 digital corporate bonds with a size of THB 36.6 billion were offered through the platform.

⁴² The Philippines ranked 5 out of 6 in terms of the number of Initial Public Offerings on average for the last five years. It has more IPOs only to Vietnam which did not record any new public equity issuances since 2019, Source: London Stock Exchange Group (LSEG)

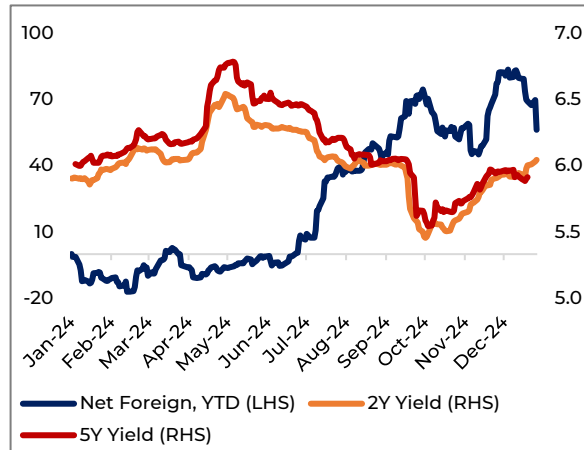
Local fixed income markets are more domestically driven with foreign share in total trade value accounting for only 4.1 percent of the total in 2024, albeit above its four-year median. The direction of foreign trading has been inversely correlated with bond yields (**Figure 2.16**). Yields on both the short and long end have fallen against its yearly highs, while foreign flows have turned net positive, rising to ₱56.3 billion.

Figure 2.15
PSEi and Net Foreign Flows
In PHP billion (LHS), In index points (RHS)



Source: PSE, OSRM Calculation

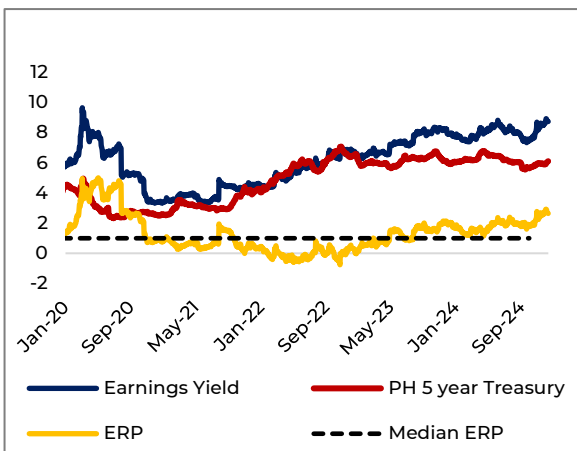
Figure 2.16
Bond Yield and Net Foreign Flows
In PHP billion (LHS), In percent (RHS)



Source: PDS, OSRM Calculation

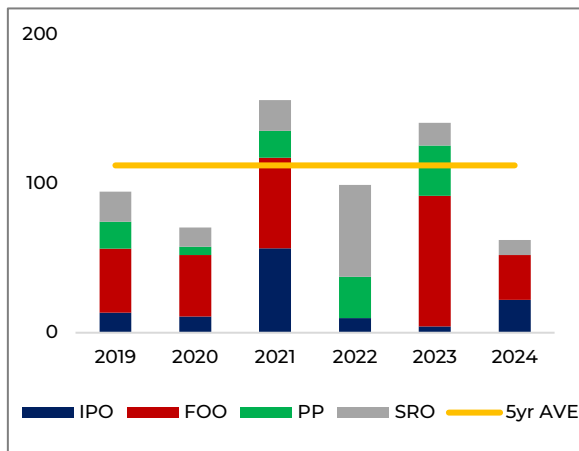
An improving, yet still narrow equities risk premium presents barriers to funding access. The current premium from holding risk assets sustained its rise above pandemic lows and is comfortably above its median. Such levels of premium over the risk-free rate (**Figure 2.17**), however, does not seem to be sufficient in attracting foreign investors in the stock market. The Philippines' equity risk premium (ERP) of 2.7 percent as of end 2024 is below the ASEAN average of 6.9 percent and US at 5.4 percent. Low risk-adjusted returns could explain outflows in PH equities. This is evident in **Figure 2.16** showing more foreign funds flow into fixed income securities.

Figure 2.17
PH Equity Risk Premium
In Percent



Source: Bloomberg, LSEG, OSRM Calculation

Figure 2.18
Capital Raised PSE
In PHP billion



Source: PSE
Note: IPO - Initial Public Offering, FOO - Follow-on Offering, PP - Private Placement, SRO - Stock Rights Offering

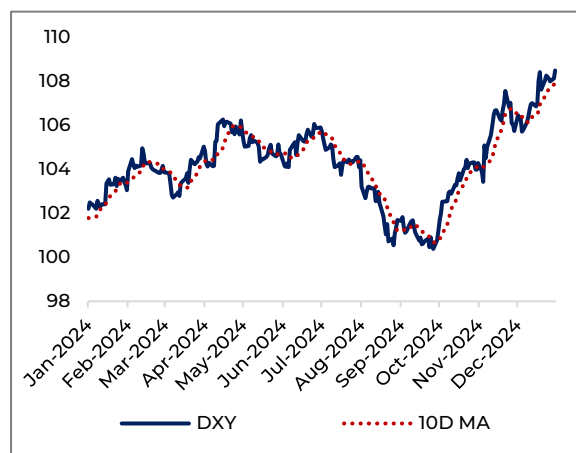
High interest rates, low market liquidity, and geopolitical tensions have dampened investor sentiment in the past few years. These contributed to the below-target IPO listings on the PSE (Figure 2.18). The cautious approach reflects broader concerns across ASEAN, where regional equity markets have experienced weakened investor confidence.

FX markets reflect investor sentiment. Uncertain outlook is likewise manifested in the FX dynamics. The general flight-to-safety tendency has fueled the greenback’s ascent since Q3 2024, gaining about 6.0 percent (Figure 2.19). Still widely considered the world’s primary safe haven currency, the USD strengthened 6.2 percent in 2024 while the PHP depreciated (4.8 percent). A stronger greenback effectively increases the burden on USD-denominated liabilities.

The US-PH sovereign spreads have tightened in the past five years. Attractive US yields have led to a narrow gap in both the short-end and long-end—2Y and 10Y spreads have hovered below its five-year median (Figure 2.20). While the US Fed began its rate cut cycle with a 50-basis points cut,⁴³ the outlook on its future policy path remains uncertain. In a scenario where the tightening of spreads persists, the country risk premium will continue to be less attractive, potentially adding to the Philippine market’s vulnerability to liquidity risks. Manifestations of such include weaker trade activity and capital outflows, with the latter having direct consequences to FX movements.

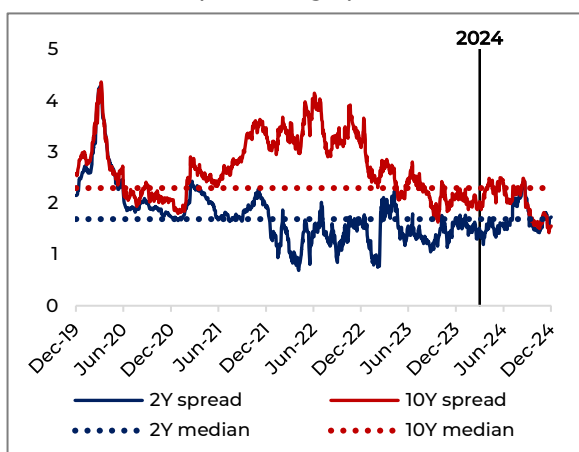
A shift in global monetary policy expectations by the fourth quarter of 2024 have contributed to an upward movement in the domestic bond yield curve. Both foreign and local monetary authorities began easing cycles in the third quarter, resulting in a downward shift in the yield

Figure 2.19
US Dollar Index
In index points



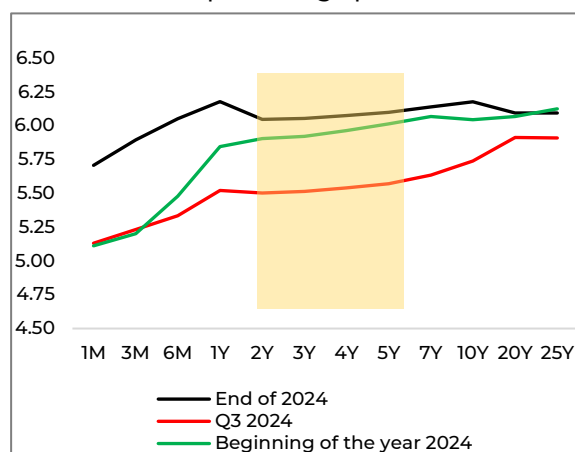
Source: Bloomberg

Figure 2.20
PH-US Sovereign Spreads
In percentage points



Source: PDS, OSRM Calculation

Figure 2.21
PH Yield Curve
In percentage points



Source: PDS

⁴³ On the 18 September 2024 US Federal Reserve Meeting, the Fed lowered interest rates by 50 basis points effective 19 September 2024. This is the first time the Fed cut rates for more than four years. The last Fed interest rate cut was on 24 July 2019.

curve (**Figure 2.21**). However, market sentiment in the fourth quarter have leaned towards a slower pace of future Fed funds rate cuts. With net outflow of ₱26.1 billion in December, domestic yields have likewise adjusted back upwards. Despite market volatility in Q4, the path of policy rates has remained tilted towards monetary easing, albeit at a slower pace.

Monetary easing cycle provides boost to capital market expansion. With the combined expectations of strong growth and falling policy rates, the viability of securities issuance as an alternative funding source becomes more pronounced. Prevailing conditions provide the window for fund seekers to broaden their options and consider tapping the bond and equity markets.

The BSP, alongside the other FSCC member agencies, has recently implemented significant initiatives to deepen our capital markets. The enhanced Peso Interest Rate Swap (IRS) market, which seeks to create a more accurate benchmark for risk pricing, was opened to market participants in November 2024. Positive and consistent adoption of the derivative market could lead to a more accurate basis for financial instruments, including corporate bonds and other debt securities. Similarly, the adoption of Global Master Repurchase Agreement (GMRA) contracts is being prioritized to boost repo transactions on Treasury bonds. These initiatives could facilitate improved pricing, build greater investor confidence, and enhance domestic trading.

CHAPTER 3: CORPORATES AND HOUSEHOLDS

Table 3.1
Outstanding amount of non-financial business and household credit

Item	Outstanding (In PHP billion); as of 30 Sept 2024	Growth, 2023: Q3-2024: Q3 (percent)	Average Annual Growth, 2019-2024: Q3 (percent)
Total private nonfinancial credit	13,316.36	5.08	6.06
Total nonfinancial business credit	10,399.54	2.26	4.97
Corporate business credit	8,622.62	1.20	4.43
Bonds	1,321.89	-14.89	0.35
Bank lending	7,300.73	4.79	5.43
Commercial real estate credit	1,776.92	7.75	7.96
Total household credit	2,916.82	16.54	10.82
Residential Real Estate	1,061.79	8.07	8.19
Motor Vehicle Loans	577.68	17.29	3.02
Credit Cards	845.39	27.71	21.74
Salary Loans	385.50	18.48	19.53
Others	46.47	14.56	12.76
Nominal GDP	6,253.98	8.52	7.03

Source: OSRM Calculation, AsiaBondsOnline, CEIC, BSP

3.1. Corporates

Corporates⁴⁴ remain largely resilient despite a slowdown in economic conditions and a high-interest rate environment. Bottom lines rebounded to pre-pandemic levels. However, there are notable vulnerabilities, especially for NFCs within conglomerates.⁴⁵ The increasing leverage and funding mismatch, though not excessive or alarming, highlights the need to monitor debt levels and liquidity gaps to service near-term maturities. Global uncertainties could also heighten the currency risks, especially those with significant foreign currency debt exposures. Conglomerate-related NFCs have large debt exposure to banks, which could amplify risks to financial system, when faced with adverse stress or shocks. Inherent vulnerabilities of conglomerate-related NFCs are also reflected in the health of the sectors where they operate, which underscores their broader role in the stability of the economy. Overall business sentiments are positive; however, downside risks are likely to stem from inflation, slower global growth, geopolitical tensions, and geoeconomic fragmentation. Policy rate cuts by the central bank, however, may ease pressures on firms.

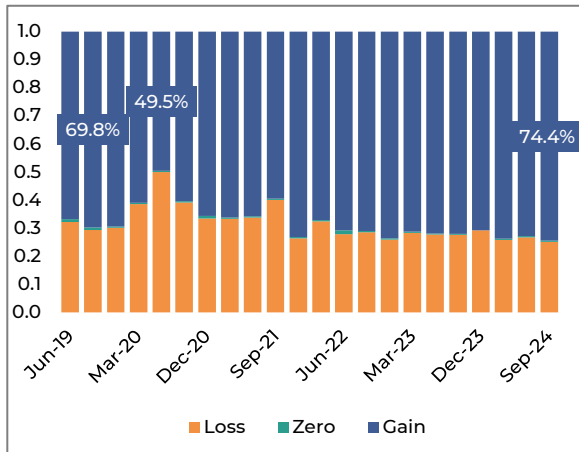
⁴⁴ All Philippine publicly listed NFCs with available data from S&P Capital IQ (242 NFCs). The period covered is from June 2019 until September 2024 to cover both pre-pandemic and post-pandemic trends. There are listed parent companies in the data set that report consolidated financials, which may result to double counting when aggregated with their listed subsidiaries.

⁴⁵ Conglomerates are multi-industry corporations composed of two or more business units engaged in diverse sectors. NFCs operating under a conglomerate group are referred to as **conglomerate-related NFCs**.

Profitability and Debt-Servicing Capacity

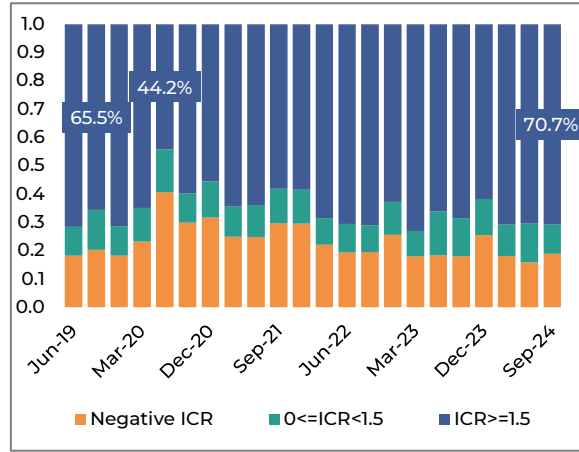
More corporates posted a positive bottom line in September 2024 compared to 2020 and 2019 (Figure 3.1). Debt servicing also improved,⁴⁶ with several corporates having operating profits that are more than sufficient to cover interest expenses (Figure 3.2).

Figure 3.1
Firm Count by Net Income
All NFCs, Share to Total



Source: S&P Capital IQ, OSRM Calculation

Figure 3.2
Firm Count by ICR
All NFCs, Share to Total



Source: S&P Capital IQ, OSRM Calculation

Leverage Risks

The rising share of total conglomerate-related assets with elevated leverage⁴⁷ suggests increased risk-taking (Figure 3.3). The observed higher risk taking in 2021 continued in 2022 amid the Russia-Ukraine war, higher inflation, and worsening global economy. At the aggregate, Debt-to-Equity (D/E) ratios have moderated recently. While the total assets of firms with higher D/E ratios have remained elevated, the increase in the D/E ratios have tapered.

Funding mismatch⁴⁸ is noted among firms with current ratios of below 1.5x (Figure 3.4). However, the likelihood of default given funding mismatches is low as these firms have access to markets or their parent entity for funding and liquidity. This highlights that the demand for refinancing and managing liquidity gaps may remain high for the foreseeable future.

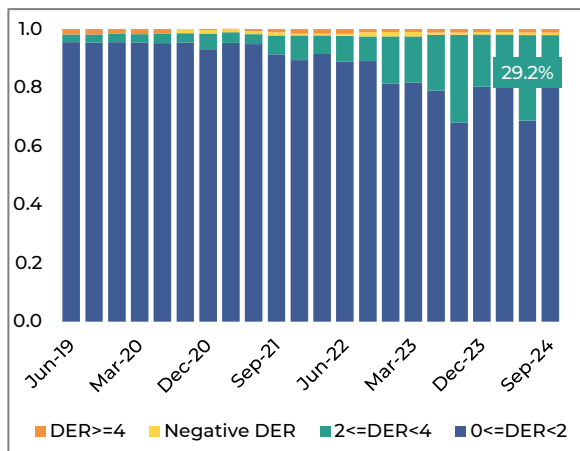
While increased risk-taking and leverage are not seen as excessive, the high level of debt incurred by corporates warrant close monitoring. These vulnerabilities could spread and heighten the risk of creditors and investors, but it is plausible that being part of a broader conglomerate structure could provide stability.

⁴⁶ As implied by an interest coverage ratio (ICR) higher than the critical level of 1.5x (blue bars in Figure 3.2). ICR equals EBIT divided by Interest Expense. The thresholds for this report are on the more conservative side, since the latest financial stability reports of the International Monetary Fund and the ASEAN+3 Macroeconomic Research Office have ICR thresholds of 1.0x and 1.25x, respectively.

⁴⁷ As implied by D/E Ratio between 2.0x and 4.0x (green bars in Figure 3.3). D/E Ratio equals Total Debt divided by Total Equity.

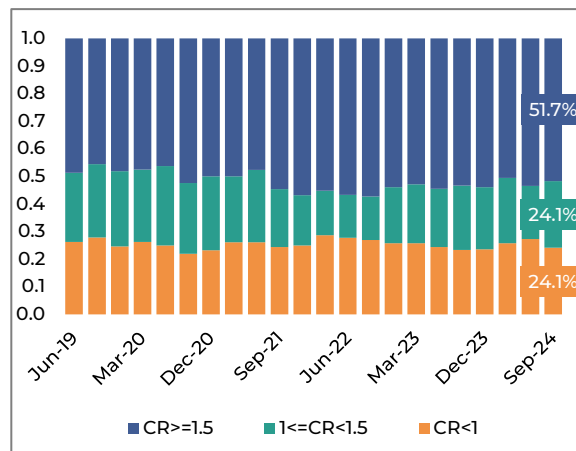
⁴⁸ As implied by Current Ratio below the critical level of 1.5x (green and orange bars in Figure 3.4). CR equals Total Current Assets divided by Total Current Liabilities.

Figure 3.3
Firm Assets by D/E Ratio
 Conglo-Related NFCs, Share to Total



Source: S&P Capital IQ, OSRM Calculation

Figure 3.4
Firm Count by Current Ratio
 Conglo-Related NFCs, Share to Total



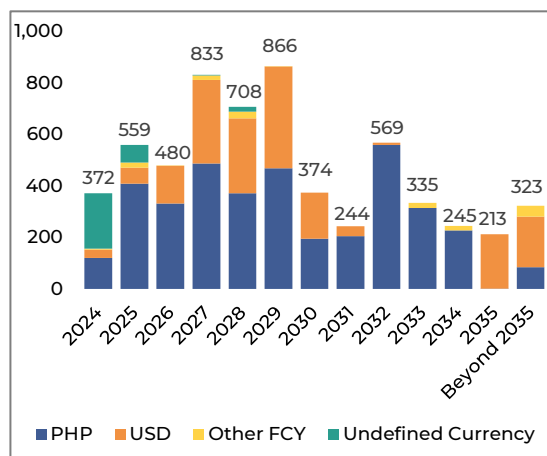
Source: S&P Capital IQ, OSRM Calculation

Refinancing Risk and Funding Mismatch

Conglomerates can access debt for productive endeavors, but high debt exposures and near to mid-term maturities could heighten refinancing risks. For instance, the total debt exposure of the top 15 conglomerate group accounts for ₱9.7 trillion or 93.0 percent of the total corporate debt. Corporates may refinance or roll-over loan positions towards a longer term, but subject to revaluation risk. Majority of foreign currency debt are USD-denominated (**Figure 3.5**), even for local-based firms who earn revenues mostly in PHP. Foreign currency exposure risk is another consideration.

Firms with access to foreign markets can tap lower cost of capital in other markets, but unhedged positions are revalued against a stronger USD. The greenback is expected to remain strong relative to other currencies. Geopolitical risks, global uncertainty, and developments in the US, may affect currency volatility. Balance sheet sensitivity to FX exposure needs to be considered as well. Highly leveraged firms, especially those significantly exposed to FCY debt but generate income in the local currency are susceptible to revaluation on top of risks related to cost of capital. Even those generating profits in foreign currencies may get hit with translation losses if the debt burden is not proportional to profitability measures. On the other hand, asset-sensitive and profitable firms with managed leverage positions enjoy a natural hedge as foreign currency appreciation enhances bottom-line figures.

Figure 3.5
Maturity of Corporate Debt of Top 15 Conglomerate Groups
 As of Sep 2024, In PHP billion



Source: S&P Capital IQ, OSRM Calculation

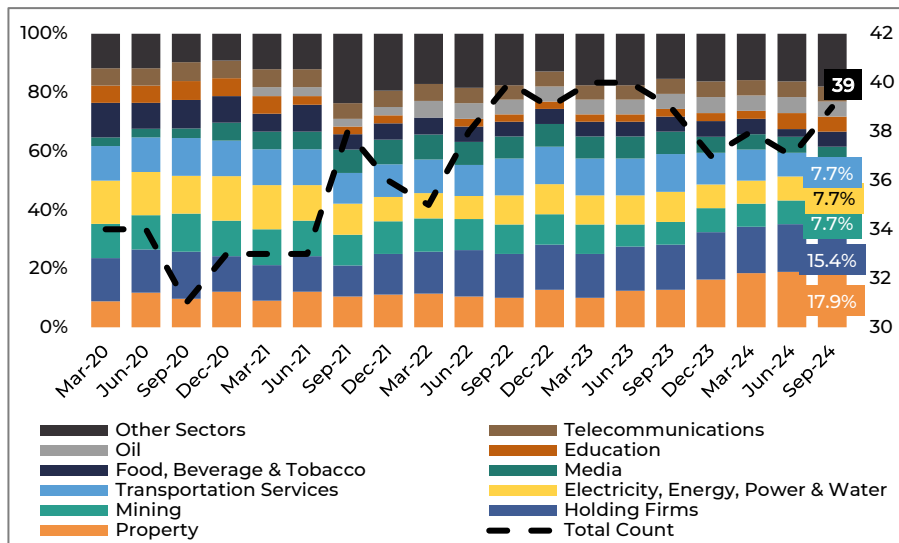
Concentration Risk to Bank Funding

Conglomerates heavily rely on bank funding. On the aggregate, corporates rely heavily on loans rather than corporate securities.⁴⁹ 56.2 percent of PBS loans are driven by corporate borrowings,⁵⁰ with the top 15 conglomerates accounting for a significant portion of the total exposure.⁵¹ Banks also have exposures to conglomerates through investments in debt securities, but these remain smaller compared to bank loans. Some of the top conglomerates also own banks as subsidiaries. DSIBs exposures to multiple conglomerates are managed through exposure and prudential limits. Concentration to bank funding and connections to DSIBs may amplify risk amid inherent vulnerabilities especially during downturns.

Sectoral Breakdown

Figure 3.6 shows a sectoral view of conglomerate-related NFC vulnerabilities on a debt-servicing / leverage / liquidity standpoint.⁵² Leverage vulnerability refers to D/E ratio higher than 2.0x / negative D/E ratio amid capital deficiency while debt-servicing and liquidity vulnerabilities are implied by an ICR and current ratio, respectively, of less than the critical level of 1.5x. The firm is considered vulnerable if at least one of the vulnerabilities is present for the past four consecutive quarters. The number of conglomerate-related NFCs with vulnerabilities has picked up in the third quarter of 2024.⁵³

Figure 3.6
Vulnerable Conglomerate-Related NFCs
 Share by sector, Total count (RHS)



Source: S&P Capital IQ, OSRM Calculation

The top five sectors with the highest vulnerabilities as of September 2024, accounted for 56.4 percent share to total are property (17.9 percent); holding firms (15.4 percent); electricity, energy, power, and water (7.7 percent); mining (7.7 percent); and transportation services (7.7 percent).

⁴⁹ Asian Bonds Online and Financial Reporting Package (FRP) data as of September 2024.

⁵⁰ FRP data on PBS Loans to Resident Private Corporations vs PBS Gross TLP (exclusive of IBL and RRP with BSP and Other Banks) as of September 2024.

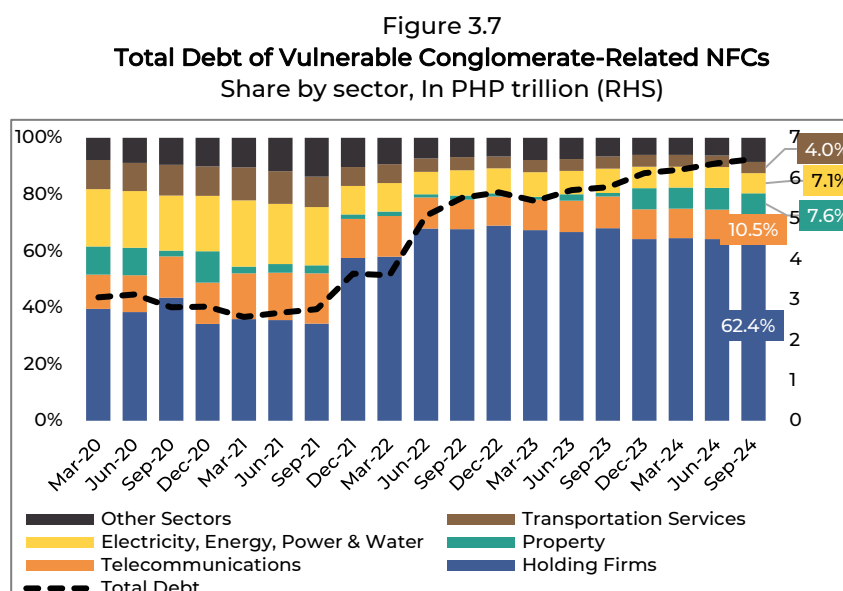
⁵¹ Comprehensive Credit and Equity Exposures Report (COCREE) data as of June 2024.

⁵² This methodology using financial ratios only provides a limited view of the firm’s debt servicing / leverage / liquidity constraints and cannot be used as a substitute for a comprehensive firm-level risk assessment. Key mitigants to vulnerabilities, such as risk management strategies and governance frameworks may be in place. Higher leverage and lower liquidity ratios may also be part of a broader strategy for corporates.

⁵³ Count of conglomerate-related NFCs with vulnerabilities may however be understated as firms without data either in the numerator or denominator will have no financial ratio and will not be accounted for a specific quarter.

Notably, the vulnerable conglomerate-related NFCs under the mining sector were not as indebted compared to the other sectors with the highest number of firms exhibiting debt-servicing / leverage / liquidity constraints.

The increase in total debt of vulnerable conglomerate-related NFCs has moderated (**Figure 3.7**). The most indebted sectors with vulnerabilities, comprising 91.5 percent share of total debt as of September 2024, are holding firms (62.4 percent); telecommunications (10.5 percent); property (7.6 percent); electricity, energy, power, and water (7.1 percent); and transportation services (4.0 percent).



Debt accumulation among holding firms is common as parent or ultimate parent entities are engaged in diversified businesses that are capital intensive such as fuel and oil, transportation, property, infrastructure, construction, financial services, automotive, and manufacturing. These holding firms are susceptible to supply chain disruptions, volatility in commodity and input prices, and changes in funding costs.

The property/real estate sector exhibited an uptick in vulnerable conglomerate-related NFCs while total debt rose after its substantial contraction within the period 2021 to 2023. This sector accounts for the largest share of loans outstanding for production. The larger and more diversified firms in this sector generally remain resilient as evidenced by their financials. However, downside risks remain as demand continues to be subdued while supply grows leading to high vacancy rates. Prices and rents likewise stayed muted. The real estate sector is highlighted in **Box Article 2**.

Another sector of interest is telecommunications, which is also capital-intensive. However, share to total debt of vulnerable conglomerate-related NFCs has declined since 2022 after steeply rising from 2019 until 2021. The sector is concentrated to only a few players.

Box Article 2: Shifts and Headwinds to the Real Estate Sector

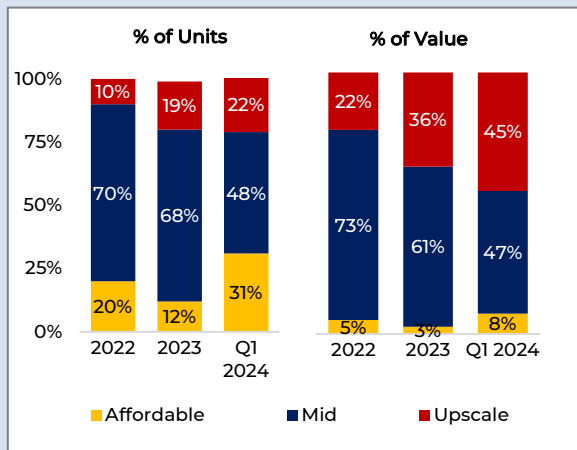
Market Landscape

Over the past few years, the Philippine real estate sector underwent significant changes, including demand for real estate especially after the pandemic. For example, the prevalence of alternative work arrangements, economic uncertainties post-COVID, accelerated inflation and higher interest rates dampened demand for real estate.

Following a rebound in demand beginning in 1st Quarter 2021, RRE prices including rents, have largely recovered, even as the Residential Real Estate Price Index (RREPI) fell in Q3 2024.⁵⁴ This is driven primarily by a strong upscale market. Based on the Frank Prime Global Cities Index,⁵⁵ as of 3rd Quarter 2024, the price of high-end residential real estate market in Metro Manila increased by 29.2 percent YoY compared to the 2.9 percent increase of the index overall. **Figure D** shows a market buoyed by upscale segments. The share of upscale segments in terms of take-up units has continued to climb. This is more apparent in terms of total take-up value. Improvements are also noted in the affordable segment. Meanwhile, the change in the mid-segment is characterized by a decreased share both in terms of take-up units and value.

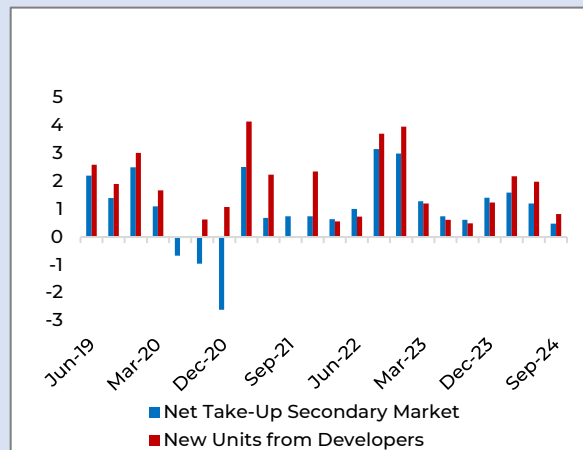
Despite recovery in prices, vacancies remain elevated amid the increase in residential real estate supply. **Figure E** shows that the rise in new units from developers outpaced net-take ups in the secondary market. This is also observed in the office and retail space markets. Metro Manila office vacancy rates are expected to remain elevated (below 20 percent) and may lead to a slower growth in real estate rents. Given these, prices are expected to return to pre-COVID levels by 2028-2029.⁵⁶

Figure D
Segment Share Volume-Value
In percent to totals for period



Source: Colliers International, OSRM Calculation

Figure E
RRE Demand-Supply*
In thousand units



Source: Colliers International
Note: Demand is represented by the net take-up in the secondary market (in units), Supply is represented

Meanwhile, the gradual exit of POGOs tempers the recovery in real estate prices. Even prior to recent Presidential directive to ban POGOs, the demand for commercial real estate from POGOs has been declining since the pandemic. Developers have managed direct exposures even prior to the directive as

⁵⁴ Based on the BSP RREPI and Various Market Reports on real estate prices

⁵⁵ Knight Frank Q3 2024. The Prime Global Cities Index (PGCI) is a valuation-based index tracking the movement of prime residential prices across 44 cities worldwide.
<https://content.knightfrank.com/research/323/documents/en/prime-global-cities-index-q3-2024-11650.pdf>

⁵⁶ Colliers. Manila Q3 2024 Property Market Report- Residential, <https://www.colliers.com/en-ph/research/colliers-quarterly-property-market-report-residential-q3-2024-philippines>, Colliers. Manila Q3 2024 Property Market Report-Office, <https://www.colliers.com/en-ph/research/colliers-quarterly-property-market-report-office-q3-2024-philippines>

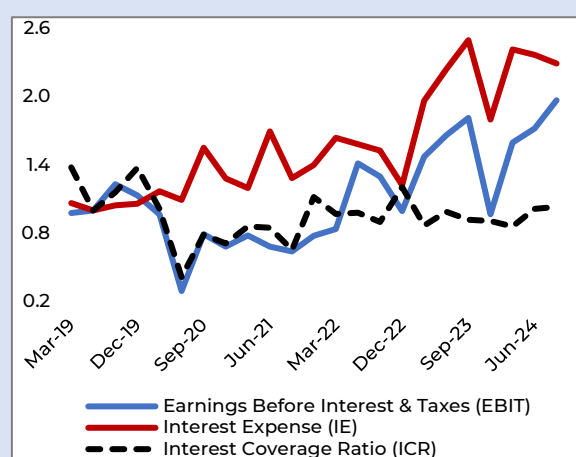
POGOs account for less than 3 percent of total gross leasable office spaces of majority of developers. As such, the adverse impact of the pullout of POGO will be stronger on residential real estate than on office real estate given elevated secondary market vacancies and remaining uncertainty on how much POGO have driven total demand for condominium units.

Risks to the financial system

The REL portfolio as of September 2024 is comprised mostly of commercial real estate (62.5 percent), where NPL stands at 2.18 percent. This is significantly lower than NPLs for residential real estate (6.82 percent). Among residential unit developers, the mid- and low-cost housing segments have driven the rise in NPLs, which also account for a large part of residential real estate loans. What does not show up as higher NPLs for commercial real estate are likely to be seen in the financial statements of real estate developers.

Data depicted in **Figure F** show signs of real estate resilience. Despite slower inventory turnover, lower cash flows from operations, and higher interest expense, developers reported growth in earnings driven by higher margins, strong sales outside Metro Manila and higher revenues from leasing. A potential risk is the build up of in-house financing as reflected in the installment contracts receivables of real estate developers. These contribute to revenues but also expose developers to credit risk. Past due and impaired receivables remain elevated including in real estate developers exposed to POGO. Overall, the real estate sector shows signs of resilience with continued profitability, liquidity, and diversification especially among larger firms.

Figure F
Key Ratios (EBIT, IE, ICR)
Property Firms, Indexed Jun 2019 = 1



Source: S&P Capital IQ OSRM Calculation

Business and Consumer Sentiment

The Business Expectations Survey (BES)⁵⁷ reported that business confidence is higher in the fourth quarter of 2024 and less upbeat for the first quarter of 2025 and in the next 12 months. Business sentiment is more favorable across all sectors except in construction.⁵⁸ Favorable expectations among firms in the industry,⁵⁹ wholesale and retail trade,⁶⁰ and services⁶¹ sectors are driven by the uptick in demand during the holiday season, easing inflation, interest rate cuts, business expansions, and improved business operations.

For the first quarter of 2025, sentiment across all sectors is less optimistic as firms expect the normalization of demand, heightened economic uncertainty leading up to the midterm elections, and tight foreign and domestic competition. In the next 12 months there is a mixed

⁵⁷ The BES is a quarterly survey of firms drawn at random from the list of top 7,000 corporations ranked based on total assets. The Q4 2024 BES was conducted during the period of 4 October to 14 November 2024. For detailed information on the methodology, please refer to the BES documentation.

⁵⁸ Construction sector is comprised of firms engaged in general construction and specialized construction activities for buildings and civil engineering works.

⁵⁹ Industry sector is composed of manufacturing; mining and quarrying; electricity, gas, and water; agriculture; fishery; and forest subsector.

⁶⁰ Wholesale retail trade is made up of businesses engaged in wholesale and retail sale (without transformation) of any type of goods and rendering services incidental to the sale of these goods.

⁶¹ Services sector is composed of firms engaged in financial intermediation; real estate; renting and business activities; hotels and restaurants; transport, storage, and communications; and community, social, and personal services sub-sectors.

outlook across sectors. Firms in the industry sector are more optimistic as they expect higher sales and orders, improved business operations, and a more conducive business environment. Construction and retail trade firms on the other hand are less optimistic amid geopolitical conflicts.

Consumer Expectations Survey (CES)⁶² meanwhile reported an increase in the percentage of households that plan to buy/acquire real property within the next 12 months. This shows improvement from the reported decrease in the Q3 2024 CES.

Improvement in business conditions are reflected in the revised growth assumptions for 2025 to 2028 of the Development Budget Coordination Committee (DBCC),⁶³ which anticipates the economic impact of reforms to accelerate infrastructure investments, enhance ease of doing business, and boost national competitiveness. The outlook is more upbeat for retail trade, tourism, information technology – business process outsourcing, construction, and manufacturing sectors. These are also identified as the key drivers of Philippine growth for 2025 by the Asian Development Bank.⁶⁴

Outlook

Recent policy rate cuts by the central bank offer financial relief to corporates and ease liquidity pressures among firms. Availability of lower-cost funding can stimulate further consumer spending and improve prospects for businesses. Corporate debt issuances may pick up as rates ease. These are likely to lead to lower cost of capital for firms and propel productive activities. Build up of risk-taking and excessive leverage will need to be monitored as more accommodative credit conditions perpetuate. Government policies targeted to improve ease of doing business will attract investments and foster market competition. Such measures are enablers to sustain demand.

Downside risks to corporates may stem from upside risks to inflation, slower global growth, geopolitical tensions, and geoeconomic fragmentation. These challenges can lead to weakened export demand, disruptions in global supply chains, and increased commodity price volatility.

3.2. Households

The economic landscape of 2024 presented households with a mix of welcome relief and persisting challenges. While inflationary pressures have moderated and unemployment rate has declined, broader financial pressures remain, particularly in terms of debt repayment and maintaining cash buffers, as households. Despite difficulties, consumers are optimistic about the near future, with expectations of higher income and more jobs. There is also an increase in household usage of loans to purchase necessities. Increasing household debt along with diminished buffers raises concerns on debt servicing capacity. However, remittances from OFWs add a layer of resilience for some households as reliable support for consumption and reduce financial pressures. The risks that could trigger vulnerabilities in the household sector are manageable.

⁶² The CES is a quarterly survey conducted on a randomized sample of approximately 5,000 households across the Philippines. The Q4 2024 CES was carried out from 4 to 16 October 2024. For detailed information on the methodology, please refer to the CES documentation.

⁶³ 189th DBCC Joint Statement on the Review of the Medium-Term Macroeconomic Assumptions for Fiscal Years (FY) 2024 to 2028.

⁶⁴ Asian Development Outlook, December 2024.

Consumer Sentiment and Household Expenditure

In Q4 2024 CES, households reported an improved overall confidence index for the next 12 months. Consumer sentiment was less pessimistic at -11.1 percent compared to -19.0 percent in Q4 2023 and -15.6 percent in Q3 2024. The improvement in consumer sentiment was driven by expectations of increased income from wages through permanent employment and more job availability, more working family members, and additional income sources. Consumer confidence for the next 12 months also improved.

Household consumption growth moderated but remained a key driver of the economy contributing approximately 3.7 percentage points to the overall 5.2 percent GDP growth in Q3 2024. High consumer prices weighed on household demand, slowing to 4.6 percent and 4.7 percent during the first and second quarters of 2024 (Figure 3.8). In the third quarter, consumption improved to 5.1 percent as prices started to ease. However, the first nine months' growth was slower at 4.8 percent compared with 5.7 percent in the same period in 2023.

Inflation averaged at 3.2 percent in 2024, versus 6.0 percent in 2023. This brings inflation within the 2 to 4 percent target range of the government from 2024 to 2026. The slowdown in overall consumer price index growth was primarily driven by the slower inflation in food items supported by improved agricultural output and reduced tariffs on rice imports. Global fuel prices have also decreased amid weak demand in major economies and increased supply from Libya.

Household Employment and Income

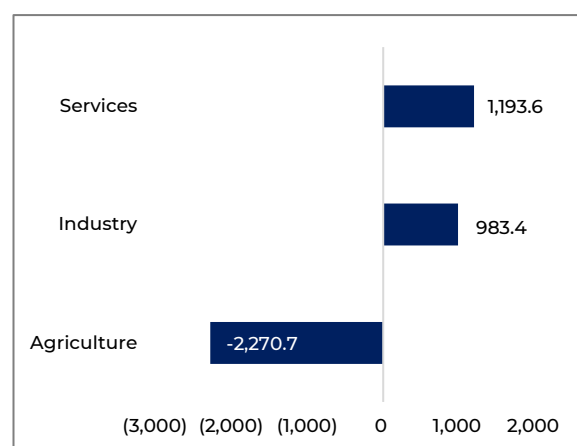
Sustained growth has supported increases in employment. GDP grew by 5.8 percent in the first nine months of 2024, faster than the 5.6 percent in the same period last year. Services contributed the most to growth, followed by the industry sector, with a contribution of 4.1 and 1.3 percentage points, respectively. Output growth helped reduce the unemployment rate to 3.2 percent as of November 2024, from 3.6 percent a year ago (Table 3.2). The services sector recorded the largest employment gains, with 1.2 million new jobs (Figure 3.9). Among the services subsectors, job gains were led by accommodation and food service activities, human health and social work activities, and other service activities. The industry sector added 983.4 thousand jobs mainly attributable to the manufacturing and construction subsectors. Meanwhile, the agriculture sector lost 2.3 million jobs.

Figure 3.8
Household Final Consumption Expenditure
Growth rate (In percent) at
Constant 2018 Prices



Source: PSA

Figure 3.9
Gain/(Loss) in Employment in Major Sectors
November 2023 vs. November 2024
Number (In thousands)



Source: PSA, OSRM Calculation

Table 3.2
Labor and Employment Statistics
 In percent

	Nov 2023	Oct 2024	Nov 2024
Labor Force Participation Rate	65.9	63.3	64.6
Employment Rate	96.4	96.1	96.8
Underemployment Rate⁶⁵	11.7	12.6	10.8
Visible Underemployment Rate	6.8	7.1	6.1
Invisible Underemployment Rate	4.8	5.5	4.7
Unemployment Rate	3.6	3.9	3.2

Source: PSA, OSRM Calculation

Labor productivity could be driving the shift in employment patterns as workers move from the agricultural sector to higher-productivity sectors. The job separation rate in the agricultural sector has been on a steady rise over the past few years, while the job-finding rate in non-agricultural sectors (services and industry) has been increasing.⁶⁶ Labor migration from agriculture to non-agricultural sectors is driven by the widening wage differentials and facilitated by improvements in labor market efficiency and transport infrastructure. However, inadequate education and the presence of agricultural clusters dampen the process.

The Philippines faces a demographic window of opportunity but must manage various challenges to maximize its demographic dividend.⁶⁷ Data show that the Philippines is in a demographic sweet spot, evidenced by a larger share of persons aged 15-64 years (working-age population) versus the proportion of persons under 15 years of age and 65 years and over (dependent population).⁶⁸ However, various challenges are hindering the country from fully exploiting this opportunity, such as the slow reduction in fertility rates, access to quality education, and employment opportunities for young workers. Without supportive policies that provide the young population with better access to quality healthcare, education and skills development programs, employment opportunities, and financial services, the country cannot maximize the potential demographic dividend.⁶⁹

⁶⁵ The underemployment rate consists of visible and invisible underemployment. Visibly underemployed persons are those who worked for less than 40 hours a week during the survey period and want additional hours of work or an additional job. On the other hand, persons classified under invisible underemployment are those who worked for 40 hours or more a week and want additional hours of work or an additional job.

⁶⁶ Cerutti and Li. (2021). *The Agricultural Exodus in the Philippines: Are Wage Differentials Driving the Process?* International Monetary Fund.

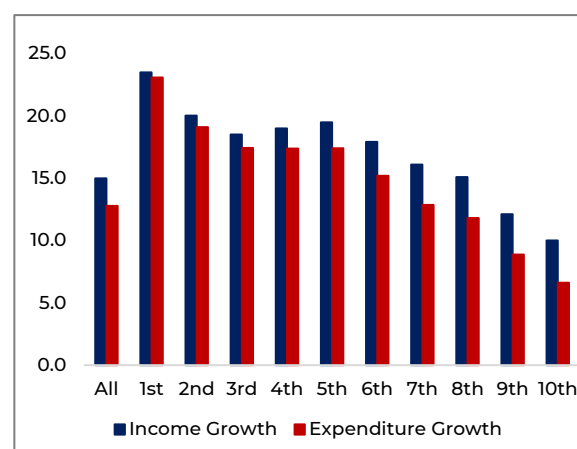
⁶⁷ See Mapa, D. (2015). *Demographic sweet spot and dividend in the Philippines: The window of opportunity is closing fast. Demographic Sweet Spot and Dividend in the Philippines_FINAL_DRAFT_Ver4_OCT2015-withcover_0.pdf*; United Nations Population Fund. unfpa.org/data/demographic-dividend/PH

⁶⁸ *Age and Sex Distribution in the Philippine Population (2020 Census of Population and Housing)*

⁶⁹ See International Monetary Fund. (2013). *Jobs and Growth - Analytical and Operational Considerations for the Fund. Policy Papers, 2013(018)*. <https://doi.org/10.5089/9781498342148.007>

Household expenditures grew nearly as fast as incomes, especially in lower deciles. According to the 2023 Family Income and Expenditure Survey (FIES),⁷⁰ while average household incomes increased by 15.0 percent from the previous FIES year (2021), expenditures grew 12.8 percent (**Figure 3.10**). The gap is even narrower in the case of the bottom 30 percent income households, with an average expenditure growth of 19.9 percent against a 20.7 percent improvement in income. This leaves many households with little buffer and flexibility to manage expenses beyond their immediate expenditures, such as health-related emergencies that require a significant cash outlay. Despite dropping unemployment rates, income from existing jobs (especially for the lower-middle to lower deciles) are just sufficient for households to get by.

Figure 3.10
Income and Expenditure Growth by Income Decile
Comparison of FIES years 2021 vs 2023
In percent



Source: PSA

Household Financial Buffers and Debt Obligations

Fewer households are also able to save amid rising cost of living and growing expenses. The CES showed that only 28.7 percent of all households were able to save in Q4 2024, a sharp drop from the pre-COVID level of 41.8 percent in Q1 2020.⁷¹ The percentage of savers for low-income (16.7 percent) and middle-income households (29.1 percent) is even smaller in contrast to 40.6 percent of high-income households. The low propensity of low- and middle-income households to save or invest perpetuates the disparity between low- and high-income groups.

The PSA reported households' gross savings⁷² of one percent of total income in 2023 from negative levels in 2020 to 2022.⁷³ Although this is higher than pre-pandemic level in 2019, a general slowdown in the ratio of savings to income is observed for the past two decades. A weak propensity to save raises concerns about the availability of sufficient cash buffers. With limited financial buffers, households are vulnerable to unexpected income disruptions and unanticipated expenses, leaving loans as funding source.

Household debt has continued to increase along with access to credit. CES showed that one in every four households have availed loans in the last 12 months, while 13.7 percent of respondents expressed intent to apply for a loan in the same period.⁷⁴ Households' access to credit has eased since the Q1 2020⁷⁵ following the growth of digital finance in the Philippines. In August 2024, the BSP announced the granting of additional licenses for digital banks beginning in 2025⁷⁶ that will increase the number of digital banks from six to ten. Also, an increasing number of digital lending platforms offer convenient and accessible financial services to households, especially to the unbanked.

⁷⁰ Previously a triennial survey, FIES will now be conducted every two years starting the 2023 conduct <https://psa.gov.ph/content/philippine-statistics-authority-conducts-2023-family-income-and-expenditure-survey>

⁷¹ Figures extracted from Table 10 of the Q4 2024 CES report

⁷² Including non-profit institutions serving households (NPISHs) which, according to the System of National Accounts, consist of NPIs that are not predominantly financed and controlled by the government and that provide goods and services to households for free or at prices that are not economically significant.

⁷³ Consolidated Accounts and Income and Outlay Accounts (CAIO). The CAIO Accounts serve as the compilation through the income approach of the GDP as it provides information on income receipts and disbursements.

⁷⁴ Figures extracted from Table 15 of the Q4 2024 CES report

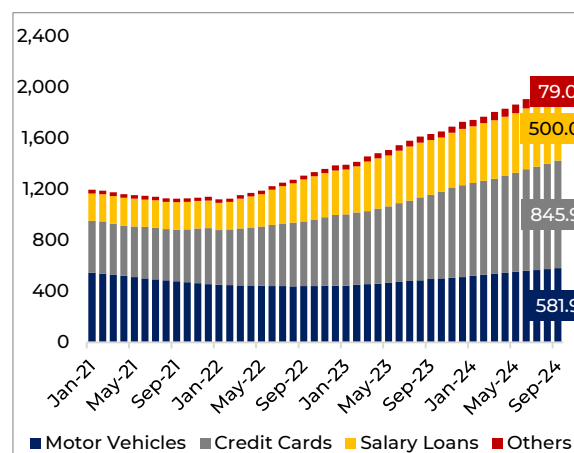
⁷⁵ Based on the Index on Debt Application Experience series from Table 15 of the Q3 2024 CES report.

⁷⁶ BSP announced lifting of moratorium on issuing new digital banking license starting January 2025.

Outstanding loans for household consumption⁷⁷ in the PBS totaled ₱2.0 trillion in September 2024, up by 22.8 percent from ₱1.6 trillion a year ago. Credit card loans have been growing strongly in the last two years and have overtaken motor vehicles in terms of share to total household loans (Figure 3.11). Credit card loans grew 27.8 percent to ₱845.9 billion in September 2024, accounting for 42.2 percent of total household loans.

More households use loan proceeds to finance essential needs and pay off debts. CES results indicate that households that used their loan proceeds to purchase basic goods stood at 57.3 percent, up from 35.4 percent in Q1 2020 (Table 3.3).⁷⁸ The proportion of households using loan proceeds for educational expenses and repayment of other debts also increased. However, fewer households had loans to buy big-ticket items like real estate and vehicles.

Figure 3.11
Household Loans
In PHP billion



Source: BSP, OSRM Calculation

Table 3.3
Household Use of Loan Proceeds
In percent

Category	Q1 2020	Q4 2024
Purchase of basic goods	35.4	57.3
Business start-up/expansion	24.1	24.2
Education-related expenses	16.2	22.1
Health-related expenses	11.0	11.0
Payment of other debts	6.9	11.3
Real estate	6.0	3.1
Motor vehicle	7.0	4.5

Source: BSP, Q4 2024 CES

Remittances as a Source of Household Resilience

Remittances remain a vital source of household funding. The remittance outlook remains positive with remittance flows to the Philippines expected to rise by 3.0 percent in 2025.⁷⁹ Cash receipts from abroad⁸⁰ constituted 7.8 percent of household income in the 2023 FIES. Personal remittances reported through the Balance of Payments account for about nine percent of the GDP over the last decade.

⁷⁷ Figures extracted from PBS Loans Outstanding for Production and Household Consumption

⁷⁸ Figures extracted from Table 15 of the Q4 2024 CES report. The table provides the percentage of households who utilized their loan proceeds in the specified categories.

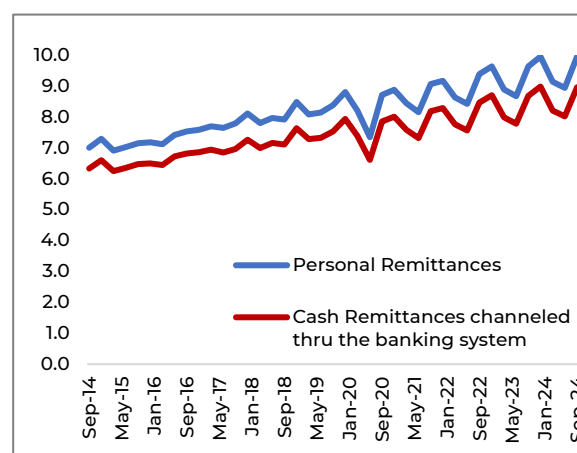
⁷⁹ World Bank, Migration and Development Brief 40: Remittances Slowed in 2023, Expected to Grow Faster in 2024.

⁸⁰ Cash receipts from abroad include (i) cash received from family members who are contract workers abroad, (ii) cash receipts from family members abroad (e.g., immigrant, tourist), (iii) pensions, retirements, and other benefits from other foreign government and enterprises, (iv) cash gifts, support, relief, etc., from abroad, and (v) income and dividends from investments abroad.

In November 2024, personal and cash remittances⁸¹ grew by 3.5 percent and 3.3 percent YoY, respectively. From January to November 2024, personal remittances reached US\$34.6 billion, of which US\$31.1 billion were cash remittances (Figure 3.12). The US comprises the highest share of cash remittances to the Philippines (40.9 percent) followed by Singapore (7.1 percent) and Saudi Arabia (6.3 percent).

The 2023 Survey on Overseas Filipinos reported that the stock of OFWs reached 2.16 million, a 9.8 percent increase from the previous year. In terms of country of destination, OFWs remain heavily concentrated in Asia (77.4 percent), followed by the Americas (9.8 percent), Europe (8.4 percent), and Australia (3.0 percent).

Figure 3.12
Overseas Filipinos (OF) Remittances
In USD billion



Source: Balance of Payments, BSP

Most OFW households allocate remittances towards basic needs. The CES reported usage of OFW remittance towards essential goods such as food and other household items, education, and medical expenses. Some households also allot remittances towards savings, debt repayment, and purchase of big-ticket items (Table 3.4).⁸² This spending pattern among OFW households suggests a dual purpose: meeting immediate needs while striving for upward mobility.

Table 3.4
Household Use of OFW Remittances
In percent

Category	Q1 2020	Q4 2024
Food and other household needs	93.9	95.2
Education	66.8	69.3
Medical expenses	51.0	55.4
Savings	44.7	38.6
Debt payments	17.2	17.8
Purchase of real estate	13.6	12.7
Purchase of motor vehicle	5.9	10.5

Source: BSP, Q4 2024 CES

Risks to the Outlook

Moody's Ratings reported⁸³ that in 2023, household debt outpaced income growth in most ASEAN member states including the Philippines. A wide gap between debt and income growth leaves households vulnerable and unable to manage their financial obligations.

⁸¹ Cash remittances refer to cash sent by land-based and sea-based workers through the banking system.

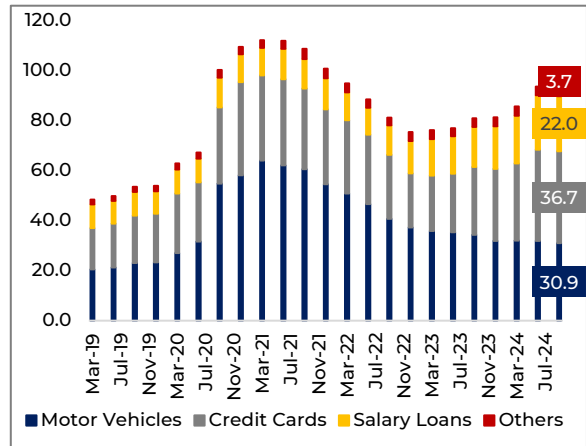
⁸² Figures extracted from Table 12 of the Q4 2024 CES report. The table provides the percentage of OFW households who utilized their remittances in the specified categories.

⁸³ Moody's Investors Service, Sector In-Depth: Banks in Southeast Asia – Rising Household Debt Adds to Asset Risks.

The sustained rise in consumer loans highlights the growing reliance of households on credit to finance essential and discretionary expenditures. The increase in consumer loans led to an uptick in credit risk. NPLs rose by 9.9 percent YoY to ₱165.4 billion as of September 2024. Excluding residential RELs, the largest contributors to the consumer NPLs were credit card receivables and salary loans (Figure 3.13).

The reported consumer loans cover only those from the banking sector. The growing number of online loan facilities in the Philippines has increased households' access to credit, reaching even the underserved and unbanked population who have access to mobile phones. Digital credit supports financial inclusion and access to financial services but also pose risks to the financial system given the increasing number of unsecured and unmonitored loans.

Figure 3.13
Non-Performing Consumer Loans
 In PHP billion, net of RREL



Source: BSP, OSRM Calculation

CHAPTER 4: MEASURES TO SAFEGUARD FINANCIAL STABILITY

Lessons learned from past crises

Lessons from the past crises highlight the importance of detecting early signs of build up in vulnerabilities, which when not monitored or acted upon promptly and swiftly, could induce shocks to the financial system.⁸⁴ During the Asian Financial Crisis (AFC) of 1997, a slow-burn build up of vulnerabilities has manifested through a slow-burn contagion risk that is characterized by the gradual and prolonged tightening of international credit conditions. In the context of the ASEAN+3 during the AFC, slow-burn contagion risk was relevant due to the interconnectedness of these economies particularly through the common lender channel—where financial shocks in one country have led to a tightening of credit conditions in others. Such slow-burn contagion during the AFC highlighted the need for developing deeper and more diversified financial markets to alleviate heavy reliance on banks as source of financing.⁸⁵ Meanwhile, slow-burn contagion during the Global Financial Crisis of 2008-2009 was characterized by decades of lack of regulation, particularly on securitization, that exposed a variety of financial institutions to subprime lending—where investment banks bought mortgage loans from banks and sold them to investors in the form of complex financial derivatives.

While digitalization streamlines financial processes, reduces costs, and increases the speed of transactions, risks to financial stability remain the same, but the speed at which they could propagate is faster. In recent times, amid greater digitalization, it also presents new sources of risk. For instance, cybersecurity threats, operational risks (from system failures and data breaches), and herding behavior (as information and sentiments spread faster) could disrupt markets or cause asset mispricing. If not properly managed, these can lead to new systemic vulnerabilities or financial distress.

In this evolving landscape, a paradox emerges: while vulnerabilities accumulate gradually and often unnoticed over time, the slow burn,⁸⁶ the ability of these risks to spread across borders and sectors accelerates with advancing digitalization. Structural weaknesses, such as excessive leverage, funding mismatches, and interdependencies may incubate for years. However, once triggered, shocks can now ripple through the financial system faster.

To address this challenge, policymakers can consider a suite of measures and interventions that can help ensure that slow-burning vulnerabilities do not evolve to rapid, systemic distress. Policy measures should then be geared at a preemptive and proactive stance rather than at a reactionary stance; monitor, if not temper, the level and spread of false narratives; reduce the likelihood of emerging risks; and strengthen the resilience of the Philippine financial system.

⁸⁴ This phenomenon is known as a *Minsky moment*, named after economist Hyman Minsky, where a sudden drop in asset prices after a prolonged period of economic growth could lead to excessive borrowing weakening financial stability.

⁸⁵ Remolona, E. (2021). Sailing the same stormy seas: Slow-burn contagion risk in ASEAN+3. In Redefining strategic routes to financial resilience in ASEAN+3. ASEAN+3 Macroeconomic Research Office.

⁸⁶ While the “slow burn” typically refers to structural imbalances such as sustained growth in unsecured consumer lending or gradual increases in corporate leverage, other vulnerabilities may emerge abruptly from external shocks (e.g. geopolitical tensions or commodity price volatility) and propagate swiftly. The former tests the system’s ability to detect and adjust gradually; the latter challenges its capacity to respond decisively and immediately.

Holistic approach to macroprudential policy

Development and subsequent adoption of macroprudential tools. As part of systemic risk management, it is important to develop buffers that dynamically shift based on business and financial cycles. *The CCyB is the main operational macroprudential tool of the BSP, which is designed to align banking sector capital requirements with the macrofinancial environment.* The CCyB mitigates systemic risks and addresses procyclicality concerns. By requiring banks to hold extra capital during economic upturns (boom periods), their ability to absorb potential losses during downturns (bust periods) is enhanced. In Q4 2024, the BSP has decided to maintain the CCyB at zero percent based on the assessment of prevailing economic conditions—including subdued credit growth and stable financial markets.

Ensuring adequate reserves and buffers. With ample capital and liquidity reserves, institutions such as banks are better equipped to absorb potential losses. Given lessons from past global crises, well-capitalized banks with liquid reserves are in a better position to withstand economic shocks and support economic activity.

Financial system liquidity is supported by looser reserve requirements which affect the supply of banks' loanable funds. Current conditions highlight the need for a market-based approach to managing liquidity. Loosening required reserves would also reduce distortions in the financial system, lower intermediation costs and promote better pricing for financial services. As necessary, reserve requirements can be used for macroprudential purposes to reduce the probability of financial stress episodes during times of high procyclicality.⁸⁷

The PDIC's Deposit Insurance Fund (DIF) safeguards public savings. It provides a maximum deposit insurance coverage (MDIC) of ₱1,000,000 per depositor per bank drawn from the reserves of the DIF. The increase in MDIC considered inflation and other macroeconomic developments. In line with this, the PDIC may consider a mechanism to adjust the assessment rate, which is the premium charged to banks to build up the DIF's reserves. PDIC is studying the feasibility of a risk-based assessment system to replace its flat-rate mechanism and align member-banks' deposit insurance fees with their risk profiles or creditworthiness. This will incentivize more stringent risk management by the banks.

Adoption of sectoral and other macroprudential limits. In addition to time-varying risks, there could be cross-sectional/sectoral risks, which led the BSP to adopt sectoral loan limits, (specifically for RELs) to help banks manage their exposure to the sector. This allows the banking system to maintain resilience even during a downturn. Meanwhile, other jurisdictions have adopted LTV ratios which are limits based on the market/appraised value of an asset being purchased, while the BSP sets a cap on values of real estate collateral.⁸⁸ These measures ensure that there is enough buffer for banks in the event of declines in property values. The BSP has also adopted the Single Borrower's Limit (SBL)⁸⁹ and the Large Exposure Limit⁹⁰ to manage concentration and contagion risk. Relatedly, other jurisdictions employ the use of debt-service ratio (DSR) limits, which could help prevent excessive leveraging and growth in unsecured lending. The implementation of limits or other related policies in other jurisdictions should be

⁸⁷ Cantu, C., Gondo, R., & Martinez, B. (2024). Reserve requirements as financial stability instruments. *BIS Working Papers*. Bank for International Settlements.

⁸⁸ The value of real estate collateral is capped at 60 percent of its appraised value; the cap of 60 percent is used to determine if a loan is secured or unsecured. See Circular No. 855, dated 29 October 2014, on the Guidelines on Sound Credit Risk Management Practices (Amendments to the MORNBFIs).

⁸⁹ The SBL for credit accommodations and guarantees extended is set at 25 percent of the net worth of the bank. See Section 362 of the MORB.

⁹⁰ See Section 361/341-Q of the MORB/MORNBFIs reflecting the amendments to the prudential guidelines on large exposures as approved by Circular 1150 dated 23 August 2022. Notably, the expansion of the coverage of counterparties treats a group of counterparties connected through direct or indirect control over another or through economic dependencies as a single counterparty.

done after careful consideration of their effects on the market amid differing conditions and risks.

Need to further develop the capital market. Acting as a "spare tire," especially during periods of economic stress, a resilient and deep capital market is essential for financial stability. In the primary market, initiatives of the SEC to streamline securities issuance including the application of proportional requirements for SMEs could encourage wider use of capital markets, also widening the spectrum of credit quality. Initiatives to further streamline requirements consider the need for adequate public disclosure and transparency on these firms' financial health. The BTr's launch of Tokenized Treasury Bonds,⁹¹ leveraging DLT, showcases how digitalization can improve bond issuance efficiency, reducing settlement risk, and attract younger, tech-savvy investors.

In the secondary market, enhancing the Primary Dealer (PD) system with stricter obligations, along with corresponding incentives, could improve market liquidity and support price discovery by narrowing bid-ask spreads and increasing trading volume. Additionally, expanding the repo market to include NBFIs, along with the BSP's commitment to adopting the Global Master Repurchase Agreement and actively participating in the repo market, strengthens liquidity, enhances collateral management, and fosters market-making.

Efforts to develop the primary and secondary markets should be complemented by initiatives to expand the investor base and attract foreign participation. The Philippines' inclusion in the JP Morgan Government Bond Index – Emerging Markets, along with the addition of Philippine corporations to global indices, would enhance the visibility and appeal of its securities. Additionally, the 3BTr's streamlined tax treaty avilment process further simplifies the investing process for non-residents by automatically applying treaty rates through the National Registry of Scrippless Securities (NRoSS) tax tracking system. Each initiative to enhance aspects of the capital market builds market confidence and supports the development of related financial instruments, such as interest rate swaps and other future derivatives.⁹²

Promoting financial inclusion. Broadening access to formal financial services not only fosters inclusive growth but deters the growth of informal lending. Financial inclusion initiatives such as digital payment platforms and microfinance solutions expand the reach of regulated financial services to underserved and rural communities. Within the financial system, this reduces lending concentration to specific creditors and regions. The Financial Inclusion Steering Committee (FISC), an inter-agency body chaired by the BSP, is tasked with the development of financial inclusion initiatives, campaign, regulations, and other policies. FISC member agencies [e.g., BSP, DOF (with BTr attached), IC, SEC, and PDIC] in this body execute initiatives aligned with their unique mandates. PDIC leverages its role to build depositor confidence in banks through the protection provided by deposit insurance. Its public awareness and financial literacy campaigns underscore the value of savings and formal banking channels. An expansion of both the coverage and scope of deposit insurance contributes to both financial inclusion and stability. The increase in the maximum deposit insurance coverage is expected to encourage more people to deposit in banks. With other industry leaders, the FISC is also committed to improving the resilience of payments systems and basic deposit account towards an inclusive financial system built on innovation, with prudential safeguards.

Strengthening risk management and financial supervision. Past crises underscored the need for enhanced risk management and financial supervision that involves greater transparency and disclosure for complex financial products as well as regular stress testing. This aligns with current initiatives led by the BSP, in coordination with the DOF, SEC, IC, and PDIC as members

⁹¹ Introduced in November 2023, the TTBs were issued in the form of digital tokens and are securely maintained in the BTr's DLT registry.

⁹² On 18 November 2024, the BSP and Bankers Association of the Philippines launched the enhanced PESO interest rate swap market, with several of the latter's members serving as market-makers.

of the FSCC and the SEC, IC, and PDIC of the FSF aimed at strengthening oversight of financial conglomerates. The ongoing conduct of supervisory colleges—forums where domestic regulators coordinate supervisory strategies and exchange information with respect to planned amendments to reporting requirements—seek to enhance transparency and ensure that financial conglomerates are managed in a manner that upholds the integrity of the financial system.

Strengthening consumer protection protects households from predatory lending and other forms of financial fraud. The BSP, with other regulators, continues to enhance measures, such as disclosure requirements and complaint-resolution mechanisms, which ensure fair treatment of borrowers and promote transparency in lending transactions. In addition to minimizing household debt vulnerabilities, improving market conduct practices builds general confidence in the strength and integrity of the financial system.

The BSP continues to regulate banks and other BSP-Supervised Financial Institutions (BSFIs) through periodic, thorough examinations and offsite surveillance. Greater digitalization enables the growth and proliferation of non-bank institutions with the benefits of accessibility, cost-efficiency, and agility. This type of financial innovation is a major contributor to economic growth. However, non-bank institutions operating outside the radar of regulatory authorities could be a potential source of vulnerabilities through their interconnection with the financial system. Aside from improvements in coordination, and reporting frameworks as discussed subsequently, capacity-building for financial institutions to manage risks is a necessary to ensure the effectivity of regulations. The BSP is currently developing a money service provider (MSBs) and pawnshop strengthening (MaPS) program to improve awareness of regulations and boost compliance with the same. PDIC is also committed to enhancing institutional resilience through its training programs. It will conduct in partnership with bankers' associations on matters such as governance, internal controls, risk management, and compliance, particularly on deposit operations. The content of these programs is responsive to advances in technology and changes in legislation such as the AFASA.

Advancing crisis preparedness. Building on previous FSRs, the FSCC continues to advance the Systemic Risk Crisis Management (SRCM) initiative to ensure readiness even under normal conditions. The PDIC, for its part, is aligning its Financial Crisis Management and Resolution (FCMR) Handbook and Financial Crisis Management Plans (FCMPs) with the 2022 SRCM Framework issued by the FSCC. These measures may undergo internal and external simulations between 2026 and 2027, which will ensure that these plans are rigorously tested and continuously improved. This ensures that the financial system remains vigilant against the pitfalls of irrational exuberance as conditions evolve and perceptions adapt to those changes.

Addressing data gaps. Within the realm of systemic risk surveillance that deals with complex and firm-level interconnections between the financial and real sector, there are data gaps that need to be continuously addressed. This requires the collection of more granular data that would aid in the early detection of vulnerabilities as well as serve as inputs to various stress testing exercises.

In addressing these gaps, the IC mandates that all regulated entities, unlisted NBFIs such as insurance companies, health maintenance organizations (HMOs), pre-need companies, and mutual benefit associations, submit annual statements and other mandated reports. These regulatory obligations, prescribed by the Amended Insurance Code (Republic Act No. 10607),⁹³

⁹³ Further detailed in Circular Letter No. 2024-05, 2024-06, 2024-07, 2024-08, 2024-12. In addition, Circular Letter No. 2023-10 requires the submission of Enhanced Quarterly Reports on Selected Financial Statistics (EQRSFS), detailing the company's financial condition, including premiums, claims, investments, and reserves on a quarterly basis.

Pre-Need Code (RA No. 9829),⁹⁴ and Executive Order No. 192.⁹⁵ Non-compliance is met with penalties,⁹⁶ including fines and potential suspension of operations. The IC's reporting framework⁹⁷ enhances its prudential standards for systemic risk monitoring.

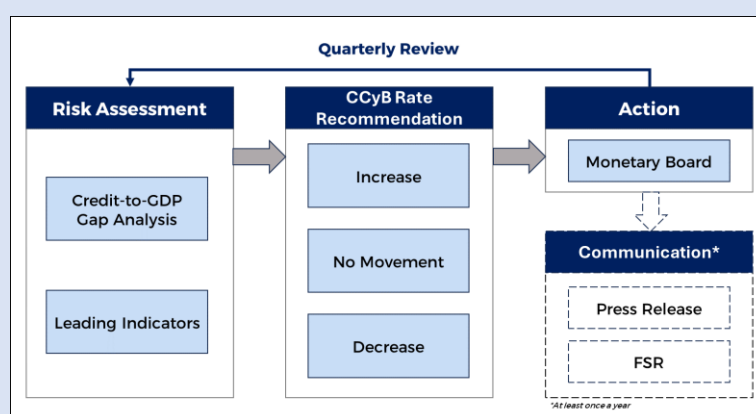
Box Article 3: Countercyclical Capital Buffer Framework in the Philippines

The CCyB is a regulatory measure under the Basel III framework designed to align banking sector capital requirements with the macrofinancial environment in which banks operate.⁹⁸ It aims to mitigate systemic risks and to safeguard financial stability by requiring banks to hold additional capital during economic upturns (boom periods), enhancing their ability to absorb potential losses during downturns (bust periods).

Introduced through BSP Circular No. 1024, series of 2018, the CCyB framework provides the Monetary Board the authority to adjust the buffer level. Having been set to zero percent since its inception, the BSP has decided to maintain it at its current settings for Q4 2024 based on the assessment of prevailing economic conditions.

CCyB Framework

Figure G
Countercyclical Capital Buffer Framework



Source: OSRM

The CCyB framework is designed to systematically monitor and address systemic risks. As illustrated in the framework (Figure G), the process begins with risk assessment, analyzing the credit-to-GDP gap—a key measure of deviations in credit growth from its long-term trend—along with the analysis of a broader set of macrofinancial leading indicators. These indicators are examined complementarily with the credit-to-GDP gap to provide a more comprehensive view of credit risk build up in the financial system.

Any adjustment in the CCyB rate shall be based on the regular risk assessment. The rate of buffer is to be decided by the Monetary Board at Financial Stability Policy Committee meetings. Decisions are communicated through press releases and the FSR. Even in the absence of rate changes, annual updates are provided to maintain transparency.

⁹⁴ Republic Act (RA) 9829 states that the IC is the primary and exclusive supervisor and regulator of pre-need companies.

⁹⁵ Executive Order (EO) 192, s. 2015, transfers the supervision and regulation of HMOs from the Department of Health to the IC to ensure capital adequacy and solvency, among others.

⁹⁶ Under Section 438 of the Amended Insurance Code.

⁹⁷ As outlined in Circular Letter No. 2024-04 (dated March 1, 2024) on the adoption of Philippine Financial Reporting Standard (PFRS) 17

⁹⁸ Basel Committee on Banking Supervision. (2010). *Basel III: A global regulatory framework for more resilient banks and banking systems*. Retrieved from: www.bis.org/publ/bcbs189_dec2010.pdf

With respect to CCyB practices of other jurisdictions, the Hong Kong Monetary Authority (HKMA) provides valuable insights into the dynamic application of the CCyB for the Philippine economy, given shared regional dynamics like trade dependence and property expansion. From Q1 2016 to Q3 2019, HKMA progressively increased the CCyB rate to 2.5 percent to address risks from rapid credit growth and rising property prices. However, HKMA began releasing the buffer by Q4 2019, citing a deteriorating economic environment, to enable banks to provide support to the local economy and smoothen the financial cycle. The HKMA buffer reduction was further accelerated in March 2020, when the CCyB rate was lowered to 1.0 percent in response to the COVID-19 outbreak, freeing up capital to sustain lending and stabilize the economy. For the Philippines, should similar risks persist, these adjustments demonstrate how the CCyB can be effectively calibrated to manage systemic risks.

Key Components of Risk Assessment

Credit-to-GDP gap is the most common metric recommended by the Basel Committee on Banking Supervision (BCBS) serving as an early warning indicator for financial imbalances. To estimate the gap, various filtering techniques are employed, each with unique characteristics that influence their ability to capture the credit cycle. Following BCBS recommendation, Hodrick-Prescott (HP) filter trend is used in majority of the countries in filtering the credit-to-GDP. The BCBS uses the HP filter to compute the credit-to-GDP gap, removes trends from data using a smoothing parameter,⁹⁹ (λ) to balance flexibility and accuracy. A one-sided filter avoids forecast bias but is less adaptive to trend changes, while a two-sided filter improves accuracy but requires future data. Criticism post-global financial crisis led to adaptations like adjusted parameters, hybrid filters, and shorter cycles. The Christiano-Fitzgerald (CF)¹⁰⁰ filter separates short-term fluctuations from long-term trends in credit-to-GDP ratio, identifying potential credit bubbles. It assumes linearity and stationarity, which can limit accuracy in volatile or structurally shifting economies. The Corbae-Ouliaris (CO)¹⁰¹ filter handles non-linear trends and structural breaks, addressing limitations like end-sample bias observed in traditional methods.

Area Under the Receiver Operating Characteristic (AUROC) analysis¹⁰² evaluates the predictive power of different filtering techniques as an early warning signal by balancing accuracy and timing. The AUROC curve plots the true positive rate (correctly identified crises) and the false positive rate (misclassified negatives), enabling identification of the optimal threshold to balance correct and incorrect predictions. Conditional probabilities, which measure the likelihood of correctly identifying a crisis given a specific threshold, are calculated to evaluate the predictive accuracy of the model.

Supplemental indicators are integral to the risk assessment framework for CCyB. BCBS underscores the importance of considering a wide range of macroeconomic and financial indicators. This holistic approach ensures that buffer decisions are informed on comprehensive and relevant information, acknowledging potential implications of CCyB adjustments to monetary and fiscal policies.

Globally, central banks enhance the credit-to-GDP gap analysis with a variety of indicators. For instance, indicators related to the credit sector, such as the Debt-to-GDP ratio, are used to track leverage and credit imbalances, while banking sector metrics like the Tier 1 Capital Ratio and Leverage Ratio assess the health and resilience of financial institutions. Financial market metrics, including corporate bond spreads and the VIX, offer insights into market stress and sentiment. Real estate metrics, such as LTV ratios and asset

⁹⁹ $\lambda = (\text{times the business cycle})^{4*}(1600)$. Larger λ values result in smoother trends, wider cycle amplitudes, and longer durations.

¹⁰⁰ CF filter estimates the cyclical component c_t of a time series y_t using a weighted moving average: $c_t = \sum_{k=-K}^K w_k y_{t+k}$ where c_t is the cyclical component at time t , y_{t+k} is the observed value of the time series at time $t+k$. w_k are the filter weights designed to extract the desired frequency components, while K is the number of leads and lags or half of the filter length.

¹⁰¹ In the CO Filter, the time series, y_t , is decomposed into a trend component τ_t , cyclical component c_t and irregular component ε_t where $y_t = \tau_t + c_t + \varepsilon_t$. The cyclical component c_t is obtained by applying an inverse Fourier transform to the filtered frequency components: $c_t = F^{-1}[Y(f) * I(w_L \leq f \leq w_U)]$ where F^{-1} is the inverse Fourier transform and $I(*)$ is an indicator function that isolates frequencies within the desired range. It uses Fourier transforms to isolate desired frequency bands, accommodating both stationary and non-stationary data, making it flexible for complex trend analysis.

¹⁰² AUROC is defined also as: $AUROC = \int_0^1 TPR(FPR^{-1}(t))dt$ where $TPR(FPR^{-1}(t))$ represents the TPR for each FPR value t . The BCBS outlines two criteria for evaluating filter performance: Criterion 1 ensures the early warning indicator (EWI) has the right timing if $AUROC > 0.5$, and Criterion 2 requires the EWI demonstrates stability, with consistent or improving predictive accuracy over time.

price growth, capture potential property market vulnerabilities. These indicators provide a robust foundation for calibrating their respective CCyB rates (Table A).

Table A
CCyB Indicators across Jurisdictions

Indicator	HKMA	MAS	BI	BoE	ECB	BDF	US Fed	BoC	RBA	Total
Credit										
Credit-to-GDP (Ratio)				✓	✓	✓	✓	✓		5
Credit-to-GDP (Gap)	✓	✓	✓	✓	✓	✓	✓	✓	✓	9
Debt-to-GDP ¹⁰³	✓			✓	✓	✓	✓	✓		6
Real interest rate	✓			✓		✓	✓	✓		5
Financial Market										
VIX				✓			✓	✓		3
Global corp bond spreads				✓		✓	✓	✓		4
Banking Sector										
Tier 1 capital ratio			✓	✓		✓	✓	✓		5
Leverage ratio	✓			✓	✓	✓	✓	✓	✓	7
Liquidity coverage ratio	✓		✓	✓		✓	✓	✓		6
Return on assets		✓		✓		✓	✓	✓		5
Credit growth (Market) ¹⁰⁴	✓	✓	✓		✓	✓	✓	✓	✓	8
Loan-to-deposit ratio			✓	✓	✓	✓	✓	✓		6
Real Estate										
Loan-to-value	✓		✓			✓	✓	✓		5
Asset prices growth	✓	✓				✓	✓	✓	✓	6

Source: Central Banks websites

Note: HKMA - Hong Kong Monetary Authority; MAS - Monetary Authority of Singapore; BI - Bank Indonesia; BoE - Bank of England; ECB - European Central Bank; BDF - Banque de France; US Fed - US Federal Reserve; BoC - Bank of Canada; RBA - Reserve Bank of Australia

The BSP employs a forward-looking, data-driven approach to its CCyB framework consistent with global guidelines and practices, tailored to the unique characteristics of the Philippine economy. In line with the BCBS guidance, the BSP supplements its credit-to-GDP gap with a comprehensive set of indicators that assess the risks in areas such as credit, economic conditions, financial markets, real estate, and external factors. The robust framework enhances the ability to preemptively identify credit risk build up and guide macroprudential policies effectively.

The decision to maintain the CCyB rate reflects the prudent assessment of prevailing economic conditions, including subdued credit growth and stable financial markets. This approach allows banks to allocate capital to increase credit provisions and support the real economy proactively. Looking ahead, the BSP will remain vigilant by closely monitoring macrofinancial developments. With the easing of monetary policy and anticipated pick-up in investments, credit demand may rise, necessitating close oversight. As the economy continues to grow, the gradual phase-in of higher capital requirements will be considered, subject to global and local market developments, to mitigate excessive credit growth and enhance the ability of banks to absorb potential losses.

¹⁰³ Debt-to-GDP is a metric used in economics to measure the ratio of a government debt to its GDP

¹⁰⁴ Credit growth is the annual percent change in the total outstanding loans issued by individual banks. Bank Indonesia (BI) adjusts monetary and macroprudential policies based on bank credit growth and inflation, loosening them during low levels, as seen during the 2008 global financial crisis and COVID-19 pandemic.

BIBLIOGRAPHY

- ASEAN+3 Macroeconomic Research Office (October 2024). ASEAN+3 Financial Stability Report 2024. Retrieved from: www.amro-asia.org/asean3-financial-stability-report-2024/
- Asian Development Bank (October 2024). Asia-Pacific Climate Report 2024: Catalyzing Finance and Policy Solutions. Retrieved from <https://www.adb.org/publications/asia-pacific-climate-report-2024>
- Asian Development Outlook. (December 2024). Steady Growth Amid a Shifting Global Policy Landscape. Retrieved from: www.dx.doi.org/10.22617/FLS240598-3
- Bank of Thailand (2022). Financial Stability Report. Retrieved from <https://www.bot.or.th/content/dam/bot/documents/en/research-and-publications/reports/financial-stability-report/FSR2022e.pdf>
- Bangko Sentral ng Pilipinas. (2020). 303 Secured Loans and Other Credit Accommodations. Retrieved from <https://morb.bsp.gov.ph/303-secured-loans-and-other-credit-accommodations-3/?hilite=%27303%27>
- Bangko Sentral ng Pilipinas. (2020). 363-A Limits on Real Estate Exposures and Other Real Estate Property of UBS/KBS. Retrieved from <https://morb.bsp.gov.ph/363-a-limits-on-real-estate-exposures-and-other-real-estate-property-of-ubs-kbs-2/>
- Bangko Sentral ng Pilipinas, Monetary and Economics Sector, & Department of Economic Statistics. (2024). Business Expectations Survey Report 4th Quarter 2024. Retrieved from: https://www.bsp.gov.ph/Lists/Business%20Expectations%20Report/Attachments/22/BES_4qtr2024.pdf
- Bangko Sentral ng Pilipinas, Monetary and Economics Sector, & Department of Economic Statistics. (2024). Consumer Expectations Survey Report 4th Quarter 2024. Retrieved from: https://www.bsp.gov.ph/Lists/Consumer%20Expectation%20Report/Attachments/23/CES_4qtr2024.pdf
- Basel Committee on Banking Supervision. (2010). Guidance for national authorities operating the countercyclical capital buffer. Retrieved from: www.bis.org/publ/bcbs187.pdf
- Basel Committee on Banking Supervision. (2010). Basel III: A global regulatory framework for more resilient banks and banking systems. Retrieved from: www.bis.org/publ/bcbs189_dec2010.pdf
- Bayangos, V., Cachuela, R., & Del Prado, F. (June 2020). Impact of extreme weather episodes on the Philippine banking sector: Evidence using branch-level supervisory data.
- Bayangos, V., & Lubangco, C. (October 2024). Do remittances boost household spending? New evidence from migrants' household survey.
- Board of Governors of the Federal Reserve System. (18 September 2024). Federal Reserve issues FOMC statement [Press release]. Retrieved from <https://www.federalreserve.gov/newsevents/press-releases/monetary20240918a.htm>
- Cantu, C., Gondo, R., & Martinez, B. (2024). Reserve requirements as financial stability instruments. BIS Working Papers. Bank for International Settlements.
- Capital Economics (2024). Trump's second term. Retrieved from <https://www.capitaleconomics.com/key-issues/trumps-second-term>
- Cerutti, E. M. C., & Li, Y. L. (August 2021). The Agricultural Exodus in the Philippines: Are Wage Differentials Driving the Process? In IMF. Retrieved from <https://www.imf.org/en/Publications/WP/Issues/2021/08/20/The-Agricultural-Exodus-in-the-Philippines-Are-Wage-Differentials-Driving-the-Process-463355#:~:text=We%20find%20that%20the%20widening,presence%20of%20agricultural%20clusters%20hinder>
- Colliers. (October 2024) Manila Q3 2024 Property Market Report- Residential, <https://www.colliers.com/en-ph/research/colliers-quarterly-property-market-report-residential-q3-2024-philippines>
- Colliers. (October 2024) Manila Q3 2024 Property Market Report-Office, <https://www.colliers.com/en-ph/research/colliers-quarterly-property-market-report-office-q3-2024-philippines>
- Department of Budget and Management. (December 2024). 189th DBCC Joint Statement on the Review of the Medium-Term Macroeconomic Assumptions and Fiscal Years. Retrieved from: www.dbm.gov.ph/index.php/management-2/3118-189th-dbcc-joint-statement-on-the-review-of-the-medium-term-macroeconomic-assumptions-and-fiscal-years
- Gelos, G., Patelli, P., & Shim, I. (September 2024). The US dollar and capital flows to EMEs.
- Hong Kong Monetary Authority. (April 2019). Monetary Authority Announces Countercyclical Capital Buffer for Hong Kong. Retrieved from: www.hkma.gov.hk/eng/news-and-media/press-releases/2019/04/20190416-4/
- Hong Kong Monetary Authority. (October 2019). Monetary Authority Announces Countercyclical Capital Buffer for Hong Kong. Retrieved from: www.hkma.gov.hk/eng/news-and-media/press-releases/2019/10/20191014-4/
- Hong Kong Monetary Authority. (March 2020). Monetary Authority Announces Countercyclical Capital Buffer for Hong Kong. Retrieved from: www.hkma.gov.hk/eng/news-and-media/press-releases/2020/03/20200316-5/
- Hordahl, P., Remolona, E., & Valente, G. (September 2015). Expectations and risk premia at 8:30 AM: Macroeconomic announcements and the yield curve.

- International Monetary Fund. (October 2024). Global Financial Stability Report: Steadying the Course. Uncertainty, Artificial Intelligence, and Financial Stability. Retrieved from: www.imf.org/en/Publications/GFSR/Issues/2024/10/22/global-financial-stability-report-october-2024#Overview
- International Monetary Fund. (2024). Corporate Sector Vulnerabilities and High Levels of Interest Rates. IMF Departmental Papers.
- Jobs and Growth - Analytical and Operational Considerations for the Fund. (March 2013). IMF Policy Paper, 2013(18). Retrieved from <https://doi.org/10.5089/9781498342148.007>
- Leech Property Consultants. (2024). FY 2024 PH Property Market Report: Turning Challenges Into Opportunities. Leech Property Consultants. Retrieved from <https://www.leechiu.com/market-insights/>
- Mapa, D., United Nations Population Fund, & National Economic and Development Authority. (2015). Demographic Sweet Spot and Dividend in the Philippines: The Window of Opportunity is Closing Fast (By University of the Philippines – Diliman).
- Moody's Investors Service. (2024). Household Debt and Economic Growth in Southeast Asia. In Moody's Investors Service.
- Obstfeld, M., & Zhou, H. (2022, Fall). The global dollar cycle. Brookings Papers on Economic Activity. Retrieved from <https://www.brookings.edu/articles/the-global-dollar-cycle/>
- Organization for Economic Co-operation and Development (2024). Corporate Bond Markets in Asia. https://www.oecd.org/en/publications/corporate-bond-markets-in-asia_96192f4a-en.html
- Philippine Dealing System Group. (2024). Listed Corporate Securities as of 05 December 2024. Retrieved from <https://www.pds.com.ph/wp-content/uploads/2019/04/Listed-Securities-Database-as-of-December-05-2024.pdf>
- Philippine Statistics Authority. (August 2022). Age and Sex Distribution in the Philippine Population (2020 Census of Population and Housing) (pp. 2-7) [Report]. Retrieved from https://psa.gov.ph/system/files/phcd/2022-12/1_Press%2520Release%2520on_Age%2520Sex_RML_18July22_rev_mpe_RRDH_CRD-signed.pdf
- Philippine Statistics Authority. (March 2023). Consolidated Accounts, and Income and Outlay Accounts. Retrieved from <https://psa.gov.ph/content/consolidated-accounts-and-income-and-outlay-accounts>
- Philippine Statistics Authority. (August 2024). Family Income and Expenditure Survey. Retrieved from <https://psa.gov.ph/statistics/income-expenditure/fies>
- Philippine Statistics Authority. (January 2025). Labor Force Survey. Retrieved from <https://psa.gov.ph/statistics/labor-force-survey/node/1684065452>
- Philippine Statistics Authority. (January 2025). Inflation Report Consumer Price Index. Retrieved from <https://psa.gov.ph/price-indices/cpi-ir>
- Philippine Statistics Authority. (November 2024). National Accounts of the Philippines. Retrieved from <https://psa.gov.ph/statistics/national-accounts>
- Philippine Statistics Authority. (September 2024). 2023 Overseas Filipino Workers (Final Results). Retrieved from <https://psa.gov.ph/statistics/survey/labor-and-employment/survey-overseas-filipinos>
- Ratha, D., Chandra, V., Kim, E. J., Plaza, S., & Mahmood, A. (June 2024). Remittances Slowed in 2023, Expected to Grow Faster in 2024. In World Bank, Migration and Development Brief 40 [Journal-article]. World Bank. Retrieved from <https://documents1.worldbank.org/curated/en/099714008132436612/pdf/IDU1a9cf73b51fcd1425a1a0dd1cc8f2f3331ce.pdf>
- Remolona, E. (June & December 2019). The monkey in the mirror and other tales of central bank forward guidance. The Philippine Review of Economics.
- Remolona, E. (2021). Sailing the same stormy seas: Slow-burn contagion risk in ASEAN+3. In Redefining strategic routes to financial resilience in ASEAN+3. ASEAN+3 Macroeconomic Research Office
- Sheshadri, A., Borrus, M., Yoder, M., & Robinson, T. (November 2021). Midlatitude error growth in atmospheric GCMs: The role of eddy growth rate. Geophysical Research Letters
- The evolution of blockchain in bond issuance. (January 2021). International Finance.
- Thai Bond Market Association. (2021). 2020 Annual report. Thai Bond Market Association. Retrieved from <https://www.thaibma.or.th/pdf/annualreport/Annual2020.pdf>
- _____. (2023). 2022 Annual report. Thai Bond Market Association. Retrieved from <https://www.thaibma.or.th/pdf/annualreport/Annual2022.pdf>
- _____. (2024). 2023 Annual report. Thai Bond Market Association. Retrieved from <https://www.thaibma.or.th/pdf/annualreport/Annual2023.pdf>
- United Nations Conference on Trade and Development (June 2023). The State of Commodity Dependence 2023. Retrieved from https://unctad.org/system/files/official-document/ditccom2023d3_en.pdf



FINANCIAL STABILITY COORDINATION COUNCIL

Bangko Sentral ng Pilipinas

5th Floor Multi-storey Building, BSP Complex

A. Mabini Street, Malate, 1004 Manila, Philippines

Telephone No.: (+632) 53062938

Fax No.: (+632) 53062448

E-mail: fsc@bsp.gov.ph

Facebook: www.facebook.com/FSCCph