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BANKING ON BANKING

Issues and Challenges Facing the Banking Sector

Introduction

In 2004, the banking sector grew by 8.3%, its fastest growth rate in the last seven years. The sector's growth explains most of the impressive growth of the financial services sector of 8.4% in 2004. In the past two years, banks expanded by an average of 7.5%, a recovery from its sluggish average growth rate of 1.7% between 1998 and 2002 after the Asian financial crisis.

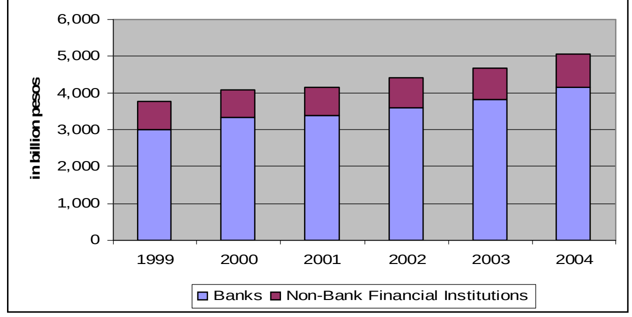
Despite its growth in recent years, the financial health of the banking sector remains volatile due to the high levels of non-performing assets in the balance sheets of banks, which have resulted in a slowdown in bank lending. Further, the profitability of Philippine banks remains inferior and lags behind other Asian banks. Considering the foregoing, it may be argued therefore that while the sector posted positive growth rates, much remains to be done to strengthen our banks.

This paper aims to provide a quick overview of the role of the banking sector in economic development, and examine its performance and the threats to the stability of the banking system.

Role of the Banking Industry

Banks play a significant role in mobilizing savings to fuel investments and growth. This role is particularly significant in the Philippines where banks continue to dominate the financial markets. In 2004, banks accounted for 82% of the total resources of the financial system (see Figure 1). Expansionary economic activities by corporations and the government are mostly financed by the banking sector. About 98% of the credit requirements of local companies in the Philippines are supplied by banks while only two percent comes from the capital markets.[1] The dominance of banks can be explained by many factors, among which is the continued underdevelopment of the capital markets. Table 1 shows that compared with other countries, the Philippine equities market is still underutilized and bond markets are highly dominated by government securities. This only stresses the relevance of banks in the national goal of sustaining and stabilizing economic growth.

Figure 1. Resources of the Philippine Financial System



Source: Selected Philippine Economic Indicators, February 2005

[1] *The Manila Times*, "Foreign Rating Firms Eyed for RP", January 2005

Table 1. Non-Bank Accounts

	Domestic Market Capitalization (% to GDP), 2003	Gov't Securities to Outstanding Debt Issues, 2004
Philippines	28.83	93.11
Malaysia	156.04	58.51
Singapore	162.58	n.a.
Thailand	83.12	82.1
Indonesia	26.24	n.a.
Korea	49.27	60.94
Hong Kong	456.17	n.a.
China	n.a.	n.a.

Source: 2004 Medium Term Philippine Development Plan, NEDA

Apart from its role in financial intermediation, banks have been shown to contribute to general economic stability. This integral link has been most evident in the Asian financial crisis where the economy was adversely affected when banks were left weak and vulnerable to external shocks. Studies suggest that the fragilities in the banking system played a key role in propagating the financial crisis that halted the momentum of the so-called East Asian growth miracle of the mid-1990.[2] The crisis caused the affected economies, the Philippines included, to slow down arising from, among others, the pull out of investors, currency depreciations, higher interest rates and larger debt overhang.

Table 2. Selected Indicators of the Philippine Banking System*

ACCOUNTS	2003	% growth	2004	% growth
Levels				
Total Assets	3,297.2	5.0	3,617.6	9.7
Investments, net	942.9	12.2	1,188.1	26.0
Total Loan Portfolio (TLP), gross	1,747.2	6.6	1,784.2	2.1
Non-performing Loans (NPL)	245.5	0.2	227.0	-7.5
ROPOA, gross	202.3	10.5	210.8	4.2
Non-performing Assets (NPAs) [a/]	442.3	3.3	430.4	-2.7
Ratios (in percent)				
NPL Ratio (inclusive of IBL)	14.1		12.7	
NPL Ratio (exclusive of IBL)	16.7		14.8	
Distresseds Assets [b/]	27.1		25.2	
Return on Assets (ROA)	1.2		1.0	
Return on Equity (ROE)	9.3		7.6	
Capital Adequacy Ratio (CAR)	17.3		n.a.	

Source: Bangko Sentral ng Pilipinas (BSP)
*Data include universal and commercial banks (UKBs) only. UKBs account for about 90% of the banking industry.
[a]Refers to NPLs plus ROPOA as defined per BSP Circular No. 351 and 380, respectively
[b]Refers to the ratio of Distressed Assets to TLP plus ROPOA, gross

Table 3. Return on Equity and Return on Assets of Asian Banks, 2000-2004

	Return on Equity					Return on Assets				
	2000	2001	2002	2003	2004	2000	2001	2002	2003	2004
Hong Kong SAR	13.5	13.9	13.3	13.5	n.a	0.8	0.8	0.8	0.8	n.a
India[b]	12.8	10.4	11.9	13.1	n.a	0.7	0.5	0.8	1.0	1.2
Indonesia[c]	19.6	13.4	22.7	22.1	n.a	0.3	0.6	1.4	1.6	2.8
Korea[b]	-9.7	16.9	14.4	2.8	19.7	-0.5	0.8	0.6	0.1	0.9
Malaysia	19.3	13.1	16.3	17.1	17.5	1.4	1.0	1.3	1.4	1.5
Philippines	**2.6**	**3.2**	**5.8**	**8.5**	**8.3**	**0.4**	**0.4**	**0.8**	**1.1**	**1.1**
Singapore	n.a	9.7	7.6	10.1	10.5	1.3	0.8	0.8	0.9	1.4
Thailand	-4.8	32.8	4.2	10.5	20.5	-0.2	1.5	0.2	0.7	1.5

Source: Global Financial Stability Report, 2005
[a] State commercial banks.
[b] Before tax.
[c] Ratio for the top 16 banks.

How have banks performed?

There were positive developments in the banking industry in 2004. As shown by Table 2, overall assets grew by 10%, an increase from the previous year's growth of 5%. Efforts to decrease banks' bad assets through Special Purpose Vehicles (SPV) deals have brought down the industry's non-performing loans (NPL) ratio to 12.7%. Investments grew by 26%. In contrast, lending activity remains sluggish at 2.1%.

The banks' profitability continued to struggle in 2004. Both return on equity (ROE) and return on assets (ROA) decreased from last year's 1.2% and 9.3% to 1.0% and 7.6%. Table 3 below indicates how Philippine banks have performed poorly in terms of generating profits compared to other Asian banks.

In recent years, the volume of credit extended by banks has been contracting. Table 4 shows that in 2000 and onwards, bank credit contracted by an average of 2% in real terms. This can also be seen in the decrease in the banks' loan to asset ratio from 52% in 2000 to just 47% in 2004 (see Table 5). In contrast, investments' share in total assets rose to 31% of total banks' assets in 2004 from just 20% in 2000. Forty-nine percent of total investments are placed in government securities, while private securities had a meager share of 2% as of the first semester of 2004.[3] Banks' preference to invest in securities than lend to businesses has become an emerging trend. The reasons for the meager growth of loans can be attributed to the combination of supply and demand-side variables. On the one hand, banks have become

[2] Ocampo, Roberto. "Monetary policies and economic growth"prepared for the Special Session on Monetary Policies And Economic Growth BFA Summit 2005, Hainan, China, April 24, 2005

[3] Status Report on the Philippine Financial System, First Semester 2004

more cautious in lending due to their high levels of NPLs. On the other, there is lower private sector demand for loans as firms refrain from undertaking expansion plans or making new investments because of spare manufacturing capacity.[4]

The ability to extend credit is an essential part of banks' intermediary function. If the independent opinions given by various credit rating agencies are used to measure how well financial institutions make their investments and financing decisions, the recent downgrade and

Table 4. Bank Credit Growth Rate (in real terms)

	Indonesia	Malaysia	Philippines	Singapore	Thailand
2000	10.21	4.64	(1.16)	3.74	(17.16)
2001	(1.33)	3.30	(5.64)	17.02	(11.07)
2002	7.41	5.04	(1.78)	(9.01)	14.91
2003	15.29	4.63	(1.94)	4.63	4.95
2004	18.88	20.56	0.63	2.91	2.38
2000-04	10.09	7.63	(1.98)	3.86	(1.20)

Source: Asian Regional Information Center (ARIC) – Asian Development Bank

Table 5. Loans, Interest Income, Investment and Non-Interest Income - Philippine Banking Industry, 2000-2004

	Loans, as % of assets	Income from Loans (as % of Total Income)	Investments, as % of assets	Income from Investments (as % of Total Income)
2000	52.2	65.4	20.3	16.6
2001	51.3	60.7	23.3	20.3
2002	49.0	51.0	25.3	20.9
2003	49.7	50.4	27.1	21.1
2004	46.5	53.6	31.0	24.2

Source: Bangko Sentral ng Pilipinas (BSP)

adverse outlook expressed by Fitch, Moody's and Standard and Poor (S&P) could very well indicate that much remains to be done in terms of ensuring that banks operate efficiently and are effective in monitoring their risk exposures. Reforms to address such instabilities should be earnestly sought to strengthen the banking system's role in promoting economic growth.

Persistence of NPLs… NPAs

High levels of NPLs exacerbate the risk-averse lending behavior of banks, limiting their ability to increase their interest income. Since the enactment of the SPV Law in 2002, 42 SPVs have registered with the Securities and Exchange Commission (SEC). As of end-April this year, P52 billion worth of assets have been disposed by banks through these vehicles. Moreover, it is expected that a total of P104 billion worth of bad assets will be sold for this year. This represents only 21% of the total P500 billion non-performing assets (NPAs) in the banking system.

Table 6. Non-Performing Loans Ratio of Philippine Banks, 1996-2004

	NPL Ratio
1996	3.5
1997	5.4
1998	11.0
1999	12.7
2000	14.9
2001	16.9
2002	14.6
2003	13.8
2004[a]	13.9

[a]*data as of 3rd Q 2004*

Source: Bangko Sentral ng Pilipinas

The reduction of NPL levels is viewed as progressing slowly and failing to keep up with the pace of other neighboring Asian countries. The NPL ratio of the Philippines stood at 13.9%[5] as of September 2004. The ratio is estimated to climb to 26.1% for the same year if real and other properties owned or acquired (ROPOA) will be included in the measure.[6] It remains to be among the highest among Asian countries (see Table 7).

The most often cited culprit for this slow progress is the wide disparity in price offers in SPV transactions, where the discounts being asked by buyers remain at a steep average of 70%. This poses difficulties for banks in disposing its bad assets as they will have to book these discounts/losses in their balance sheets. Banks cannot afford to bear additional losses because they already have too many delinquent accounts in their books. They also fail to arrive at deals with acceptable terms with prospective buyers due to its weak bargaining power.

[4] Asian Development Outlook 2004

[5] NPL data available for all banks is only that as of September 2004. For commercial banks, the NPL figure as of February 2005 is 11.8%, lower than in the NPL level of 14.2% in February 2004.

[6] Estimate of the Global Financial Stability Report (April 2005)

Table 7. Non-Performing Loans (NPLs) of Asian Countries

	2000	2004
Bangladesh	34.9	22.1 ('03)
China[a]	22.4	17.9 ('03)
Hong Kong	7.3	2.7
India	12.8	6.6
Indonesia[b]	34.4	14.9
Japan[c]	5.3	4.7
Korea	8.9	2.4
Malaysia	15.4	12.6
Philippines	**14.9**	**13.9**
Singapore	3.4	2.9
Thailand	17.7	12.4

Source: Global Financial Stability Report (2005)
[a]State Commercial banks
[b]Compromised assets include reported NPLs, restructured loans classified as pass or special mention, and foreclosed real estate and equities. The denominator includes foreclosed real estate and surrendered equities.
[c]Ratio for the major banks

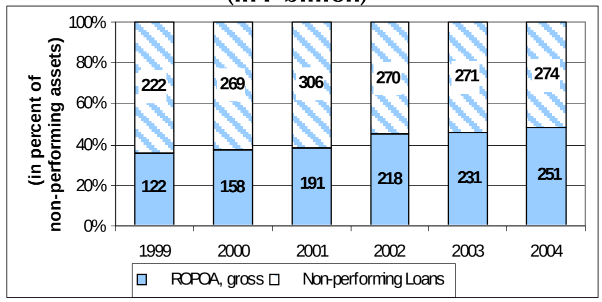
It must be pointed out, however, that other countries have been able to reduce their NPLs because of sufficient fiscal room for the creation of state-owned asset management companies (AMCs). These AMCs played an important role in reducing the NPLs in their banking systems. The government has not been able to intervene in this manner owing to its huge fiscal deficit problems.

Another reason being raised for the slow reduction in NPL's was the inability of the Bureau of Internal Revenue (BIR) to immediately come up with the Internal Rules and Regulations (IRR) for SPV transactions. The law was passed in December 2002 but the guidelines were released only in May 2004.

Apart from the slow reduction of NPLs, of similar concern is the increasing level of ROPOA. In the past five years, even as NPLs were reduced, ROPOA's share to total NPAs increased from 36% in 1999 to 49% as of end September 2004, during which period, its total value has increased from P122 billion to P251 billion.

Given the unfavorable environment for disposing NPLs, banks are more inclined to hold on to ROPOAs. Banks can just wait for the real estate markets, for example, to become more

Figure 2. Asset Quality Indicator, All Banks (in P billion)



Source: Bangko Sentral ng Pilipinas (BSP)

favorable before disposing this type of asset. Apparently, the rules of the Bangko Sentral ng Pilipinas (BSP) also favor banks holding on to ROPOAs. The rules require banks to book the losses beginning only on the sixth year when these were incurred, to be spread over the next five years. Likewise, only 50% of the loss incurred, which is difference between the appraised value and the acquisition price, is required to be booked. In contrast, NPLs must be booked on the first year these were incurred, spread over ten years, by which time, 100% of the NPLs must have been fully provisioned as loss.[7]

Increasing interest rates

In an environment of increasing interest rates, banks are placed in an unfavorable situation as the value of their bond holdings is reduced. At present, banks' exposure to government securities already stands at 29% of their assets.[8]

In the past, Philippine banks were able to benefit from the soft interest rate environment to reap robust bond trading gains, which bolstered bottom line figures.[9] Interest earnings from investments' share increased from 17% to 24% between 2000 and 2004 (see Table 5). In contrast, interest income from loans as a percentage of total income has declined from 65% in 2000 to just 54% in 2004. This situation is favorable for as long as

[7] Pasadilla, Gloria O. "Special Purpose Vehicles and insolvency Reforms in the Philippines", Philippine Institute for Development Studies, March 2005.
[8] Fitch estimates that this could actually reach as much as 34% if off-balance sheet deposits, which are invested in government securities, are accounted for.
[9] Moody's Banking System Outlook

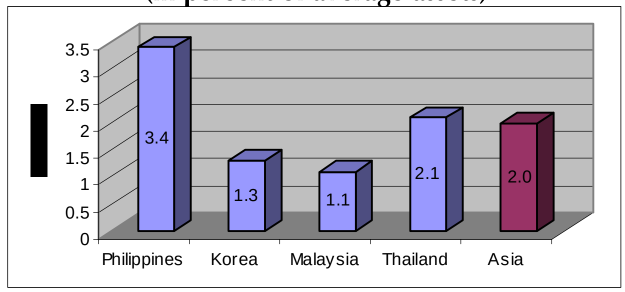
interest rates are kept low. However, once interest rates increase, especially if it is due to exogenous variables as fiscal problems and not due to economic growth and increased credit demand, the losses that may be incurred from bond trading could impact on the over all profitability of banks. This happens because as interest rates increase, the value of bonds decline when these are marked-to-market.[10] BSP guidelines require that trading asset securities must be marked-to-market when reported in the financial statements.

This becomes a particular concern when earnings from interests on loans lack the potential to generate strong earnings to cover for the probable losses. The vulnerability of banks' profitability to the rise and fall of interest rates is further worsened by the fact that pre-tax profitability is only 1% of average assets if trading gains are excluded.[11]

High operating expenses

The high operating expenses contribute to the inability of the banking system to generate profits. On average, operating expenses have eaten up 89% of the operating income for the last five years. As of the third quarter of 2004, operating expenses have grown by 5% from the same period in 2003. Figure 3 shows that compared with other Asian economies, the ratio of operating expenses to average assets of Philippine banks is quite high at 3.4% as against the regional average of 2% among Asian countries. This problem reflects the inefficiencies in the banking system that threaten its operating fundamentals.

Figure 3. Operating Expense of Asian Banks, 2003 (in percent of average assets)



Source: Beshouri (2004)

Undercapitalization

The BSP imposes a minimum 10% capital adequacy ratio (CAR) for Philippine banks, a ratio well above the requirement under international best practices of at least 8%. Despite this, there are views that banks may have to further capitalize. For one, BSP plans to impose Basel II requirements that will entail higher risk-weights on certain bank assets (e.g., NPLs will be assigned a risk weight of 15% from the present weight of 12.5%) in 2007. Assets, which serve as the denominator in computing for CAR, will then have a higher value, thus reducing the current CAR of banks if they do not increase their capital.

Another issue being raised is the deficiencies in the accounting practices and loan classification that raise suspicions that there may be a problem of undercapitalization among banks. When these are properly corrected, the accounts of banks may expose a lower CAR.

Corporate Governance Problems

Corporate governance problems in the banking sector are evidenced by the prominence of a few bank auditors, absence of domestic credit rating agencies, and lack of proper disclosure and reporting of information, and compliance with international accounting standards. The presence of family and conglomerate ownership coupled with the lack of stringent regulations poses risks of distorting bank decisions to favor certain vested interests. In fact, some even see the lingering NPL problem as a reflection of lax corporate governance standards.[12]

[10] The general dynamics in the valuation of bonds is that when interest rates increase, the value of a bond decreases and vice versa. This happens because a bond with a 5% yield, for example, is traded in a market where the going interest rate for bonds is 10%, the lower yield bond will have to be sold at a discount for it to be purchased. Otherwise, investors will opt to buy the bonds being offered with a 10% interest rate.

[11] Fitch ratings 2004

[12] *The Manila Times,* "Rate Hike to Slow NPA Sale," January 2005.

It must be noted however, that efforts to strengthen corporate governance in banks have been initiated. On top of the existing corporate governance code set by the SEC, banks have started to institutionalize the framework for a corporate scorecard that aims to apply "peer pressure" in raising the standards in professional and ethical practice and improving the competencies of bank directors, audit committees, and risk management committees.

Necessary Reforms

The recent upgrade by Fitch on the credit ratings of the bigger commercial banks in the country from 'negative' to 'stable' is a welcome development for the financial sector. It must be noted, however, that the upgrade was due to the upgrade in the credit rating of the Philippines' sovereign borrowings. Banks must still contend with their inherent problems. Banks have to clean up their balance sheets and find ways to best facilitate the absorption of losses involved in NPL sales.

The key is for banks to manage the risks properly while still being able to serve the credit needs of the economy. Weak bank lending has undesirable consequences for the economy. If financing will be limited to only a few large corporations, this would negatively affect investment growth, thereby limiting output growth and employment. The following reforms are therefore necessary to ensure that the banking system is profitable, stable and is growing at a sustainable rate.

Address NPL Problem

Successful financial reform efforts in other countries usually involved an influx of investments in an NPL market and an accompanying prudential regulatory effort on the part of the government to ensure that banks will be rid of their bad loans. The success of Taiwan in lowering its NPLs was due to the creation of an investor-friendly environment which involved instituting a simple system for disposing of bad assets, protecting creditor rights, and lowering transaction costs. Thus, policies that aim to establish an attractive NPL market for investors will be most helpful to address the NPL problem of the Philippines.

A centralized, government-owned asset management company is not likely to solve the NPL problem if it will merely transfer the NPLs from one institution to another. Further, due to fiscal constraints, the government cannot absorb the industry's NPAs. The SPV can be an effective mechanism if only more pressure is applied on banks to unload their bad assets. If the incentives provided in the SPV law are not pushing banks to dispose their NPLs, then perhaps BSP should consider giving disincentives such as imposing sanctions on banks that fail to meet the targets. A common policy in other countries was to set a targeted NPL ratio that should be strictly met by the banks. This is usually accompanied by other numerical targets such as a higher CAR or ROE. If the BSP is serious in its goal to reduce the Philippines' NPL to less than 10% by the end of 2005, then regulatory policies should be decisive, stringent and prohibitive. A relevant legislation to support this action by the BSP is Senate Bill 1943, which proposes amendments to the New Central Bank Act (RA 7653). The bill proposes to strengthen the powers of BSP to impose higher capital adequacy requirements on banks exposed to higher risks. This should help augment BSP's efforts in forcing banks to reduce their NPLs. Another alternative is to impose a higher ROE to promote diligence among banks to improve its profitability.

Another proposed legislation is Senate Bill 1830, which pushes for the extension of the SPV. A justifiable extension, however, should only cover the lag in the release of the IRR, considering the revenue implications of such measure to the government and the need to apply pressure for banks to unload their NPLs soon. Thus, two years may be enough to create a net positive impact in this effort of BSP to entice banks to seriously address its NPL problems. The BSP estimates an additional P100 billion of bad assets sales if the bill will be enacted. However, the SPV extension will only bring down NPAs of banks by another 20%. Banks will still have to contend with P300 billion worth of NPAs in their books.

Discussion Box

FINANCIAL REFORMS TO ADDRESS NPL PROBLEM IN SELECTED COUNTRIES

Japan

The Financial Services Agency (FSA), Japan's principal government agency responsible for ensuring its financial system's stability, launched the Financial Reconstruction Program, also dubbed as the "Takenaka Plan," to address its NPL problem. Under the program, Japanese banks were asked to halve their NPL ratio on March 31, 2005 reported for the March 2002 fiscal year. To comply with the requirement, several banks completed sales of large-scale NPL portfolios consisting of more than 200 small and medium-sized borrowers. The government agency Resolution and Collection Corporation (RCC) also played a strategic role in absorbing banks' NPL in bulk, securitization of NPLs, and sales or joint ventures with global opportunity funds.

Taiwan

Taiwan has been considered as the most active NPL market in Asia. Its financial reform efforts include the passage of the Financial Institutions Merger Law in 2000 and the Financial Holding Company Law in 2001. The enactment of the said laws promoted the consolidation in the financial sector through tax and non-tax incentives, permitting foreign financial institutions to acquire 100% ownership in local financial institutions, and establish financial holding companies. Taiwan has also been aggressively conducting competitive auctions. Since the inception of Taiwan's NPL market in March 2002, its banks have held more than 25 public and limited auctions to dispose of NPLs with a face value in excess of NT $350 billion. Nearly US$4 billion has been invested in Taiwan NPLs with foreign investors accounting for approximately two-thirds of this investment.* The spur in the NPL market activity caused by significant investor interest is due to the comparatively low due diligence costs, methodical foreclosure system, strong creditor rights, simplicity of establishing asset management companies and its strong deal flow.

In August 2002, the 2-5-8 plan aimed for financial recovery was launched. Under the plan, financial institutions must have NPL ratios below 5% and capitalization of more than 8% within two years. Although not a law, the 2-5-8 plan subjects the banks who fail to meet the standards to certain sanctions such as restrictions on establishing new branches, domestically or internationally, restrictions on the payment of directors' or supervisors' remunerations and other compensation, restrictions on the allocation of earnings, restrictions on long-term investments and restrictions on new loans for related parties.

Korea

The government of Korea responded to the 1997 financial crisis by injecting public funds into the banks. The injection was accompanied by the resignation of existing management and capital reductions to avoid moral hazards; the involvement of the government in management through the setting of numerical targets such as NPL ratios, capital adequacy ratios, return on assets (ROA) and return on equity (ROE), and; the injection of funds through purchases of common shares which ultimately are to be sold to private investors.

The Korea Asset Management Corporation (KAMCO) also began to purchase new classes of distressed debt–consumer loans from financial institutions. It raised funds primarily by issuing government-guaranteed bonds, and purchased NPLs at market prices. To dispose the NPLs, KAMCO used a variety of means such as direct collection, auction, asset-backed securities issuance, international bidding, and sales to asset management companies, corporate restructuring companies, and corporate restructuring vehicles.

Singapore

The NPL ratio of Singapore banks rose from 3% to 12% at the height of the Asian financial crisis. The increase was modest compared to other countries in the region due to Singapore's strong economic fundamentals. As a policy response, Singapore implemented financial reforms that centered on liberalizing its financial system. In 1999, the Singapore market was opened to foreign competition. This aimed to make local banks measure up to international standards in terms of size, expertise, range, and quality of service, as well as shareholders' returns.

Aside from the liberalization thrust, reforms on banking supervision were also pursued. First, the required capital adequacy ratio (CAR) for local banks was set at 12%. The prescribed CAR ratio is to be lowered gradually until reaching the 8% threshold of Bank for International Settlements (BIS).

*Global Non-Performing Loans Report 2004

Capitalize

When the Philippine banks adopt the Basel II framework as embraced by banks in other countries, they will have to increase their capital if their CAR falls below the minimum standard. Individual banks may face difficulties in meeting the new requirements.[13] To prepare banks for this eventuality, stronger pressure on raising new capital must be applied to ensure stability in the future. Otherwise, banks may have to merge and consolidate.

Improve Corporate Governance

The institutional aspects of banking operations must be strengthened to enhance efficiency, transparency, and accountability. As earlier noted, banks have taken strides in implementing sound corporate governance practices. Similar efforts should then be undertaken to enhance transparency, which include, among others, the shift to international standards of financial accounting to align our policies with global conventions as already observed in other jurisdictions.

Another corollary effort to promote corporate governance is the proposed amendments to the New Central Bank Act, which also include reforms that address corporate governance issues. The bill strengthens BSP's supervisory authority with respect to control ownership of banks. Under the bill, BSP is empowered to screen incoming substantial stockholders of banks and direct capital infusion. Likewise, the proposed amendments waive the rights on secrecy of bank deposits on Directors, Officers, Stockholders and their Related Interest (DOSRI) loans and extend BSP's supervision to include trust entities, quasi-banks, affiliates and subsidiaries of banks.

The establishment of credit information and credit ratings agencies will also be beneficial to promote responsible borrowing and strengthen market discipline and social responsibility. To improve the standards for accountability, setting up compliance systems and the appointment of compliance officers will be beneficial to ensure banks' conformity with corporate governance practices. And lastly, stakeholders such as accountants, auditors, compliance officers, financial analysts, corporations, business media, and minority shareholders must be engaged in the cause for good corporate governance.

Fill Gaps in the Regulatory Framework

One of the important lessons from the financial restructuring experience in developing Asia is the need for strong legal and institutional support, accompanied by government resolve to improve the financial system.[14] Improved insolvency laws and enhanced efficiency of judicial systems are needed. Consolidating the financial supervision and regulations must likewise be encouraged to complement the emergence of different financial instruments available in the market. This should also boost the confidence of the public in the capital markets and unload the burden from banks in financial intermediation. Meanwhile, reforms geared to strengthen the regulatory powers of the BSP can be pursued. These include providing adequate protection from lawsuits for bank examiners, empowering BSP to impose administrative sanctions on subsidiaries and affiliates of banks and quasi-banks, and increasing the maximum amount of administrative fines the BSP can administer on erring banks to serve as deterrent for any violation of regulations. These reforms are included in the proposed amendments to the New Central Bank Act under Senate Bill 1943.

[13] Businessworld, "More Bank Mergers, Consolidation Seen This Year", March 2005

[14] Asian Development Outlook 2004

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