Review of Financial Laws and Regulations Affecting the Provisions of Financial Services to the Basic Sectors[1]

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Introduction

Laws and regulations have been issued in recent years to direct the flow of credit to the basic sectors. Some of these have promoted greater efficiency in the pricing and allocation of financial resources while others have perpetuated the distortions plaguing the financial markets in the 70s. This study reviews existing laws and regulations affecting the provision of financial services to the basic sectors. It provides a baseline overview of the financial laws and regulations, and a general assessment of these, in the context of the government's overall policy framework. Only existing laws and regulations with specific provisions relating to the delivery of financial services to the basic sectors are included. Past laws are also included to the extent that they relate to or affect the present. Financial laws that do not affect the basic sectors are excluded.

2 Conceptual Framework

A. Conceptual Approaches to Regulation

The government has relied on both legislation and regulation to direct the flow of financial services to target sectors. These two basic tools have invariably been used in response to the demands of those whose welfare are perceived to have been reduced by the behavior of agents in the market.

One conceptual approach to regulation holds that the very existence of this demand creates a "political" market for regulation and establishes incentives for politicians and bureaucrats to supply regulation services (*Kane, 1977*). For example, a mandatory credit allocation on banks' loanable funds is employed to address the financing needs of small farmers. The demand for this allocation is a demand by, or on behalf of, small farmers for government intervention in their favor. It is a demand to assist so-called "losers" in the credit market.

The rationale often quoted by lawmakers for the formulation of financial laws is that laws are essential in attaining the government's avowed development objectives. The views on the creation of these laws are mixed. One view is that legislators enact financial laws to protect the public at large or some large subclass of the public. The other view is that the creation of laws is motivated by self-interest to win votes (*Kane, 1977*).[2]

Whichever motive drives the legislator, these laws are able to, for instance: force financial institutions to channel credit to target sectors through mandated credit quota; grant regulatory bodies the appropriate police power; and direct government line agencies to perform banking functions. In other words, these laws have the power to move resources and affect the economic decisions of households and firms. In the process, they affect financial intermediation and could even distort the operation of the market. One such distortive regulation is the interest rate ceiling on loans to specific sectors. Another is the legislated credit allocation that coerces financial institutions to set aside a fixed proportion of their loan portfolio for a particular sector. Several studies have found these interventions ineffective and counter-productive. Yet, they continue to be popular in financial legislation (*Adams, Graham and Pischke, 1984*; *Abiad and Llanto, 1989*).

Regulation oftentimes generates unintended or undesirable effects. These occur when government regulation leads to "financial innovation" creating incentives for firms to skirt regulations that restrict their ability to earn profits. This process of avoiding regulations is called "loophole mining." (*Kane, 1981*). When regulatory constraints become so burdensome that large profits can be made by avoidng them, loophole mining and innovation are more likely to occur. Over time, avoidance schemes are identified and spread to more and more regulatees. Hence, the longer a given regulation remains in force, the more important the unintended effects

2 *Coalitions are formed to persuade lawmakers to set up and to oversee for their benefit detailed systems of regulation (Stigler, 1971). To this, lawmakers often submit.*

become. (*Friedman, 1962*) A concrete example is the Agri-Agra Law (PD 717) in the Philippines which legislators are trying to amend due to psuedo compliance among banks.[3]

Just as regulation leads to regulatee avoidance, circumvention generates political pressure for re-regulation (*Stigler, 1971; Kane, 1984*). This sets the stage for a fresh cycle of regulation and avoidance. Re-regulation occurs because sponsors and proponents of regulation become aware of the unintended effects and are increasingly frustrated. The precise timing and details of avoidance schemes are unpredictable. This makes re-regulation necessary.

A second approach to understanding regulation highlights the role of information in credit markets. Unlike the goods market, credit markets are characterized by an exchange of financial resources and services for a commitment to pay a specified amount in the future. The actual realization of the commitment depends on both the ability and the intentions of the individual or firm making the commitment. One party often does not know enough about the other party to make accurate decisions. This inequality is called asymmetric information (*Stiglitz and Weiss, 1981*).

A borrower, for example, would usually have better information than the lender about the potential returns and risk associated with the investment project for which funds are earmarked. Lack of information creates problems of adverse selection and moral hazard in the financial system. Adverse selection occurs when potential borrowers who are the most likely to produce undesirable outcomes (bad credit risks) are the ones

3 *Several revisions have already been proposed by legislators both at the Senate and the House of Representatives.*

who most actively seek out loans and are thus, most likely to be selected. Because of adverse selection, it is more likely that loans will be made to bad credit risks. As a result, lenders may decide not to make any loans even if there are good credit risks in the market.

Moral hazard in financial markets is the risk that the borrower might engage in activities that are undesirable from the lender's point of view because these activities make it less likely that the loan will be repaid. Because moral hazard lowers the probability that the loan will be repaid, lenders may decide that they would rather not provide loans. A result of asymmetric information is non-interest rate rationing. Because raising the interest rate to the equilibrium level will lead to adverse selection and moral hazard problems, lenders opt to ration credit instead.

Asymmetric information and the problems associated with it are critical in understanding the regulation of financial markets. Government can reduce these problems in financial markets and increase their efficiency by increasing the amount of information available to investors. Asymmetric information can also lead to widespread collapse of financial intermediaries. Depositors or provider of funds may not be able to assess whether the institutions holding their funds are sound. If they have doubts about the overall condition of financial intermediaries, they may want to pull their funds out of both sound and unsound institutions. The possible outcome is a financial panic that produces large losses for the public and causes serious damage to the economy.

To protect the public and the economy from financial panics, the government has to install regulations. These regulations usually include deposit insurance, restrictions on bank asset holdings, capital requirements, chartering, bank examination, and separation of banking and securities industries (*Mishkin, 1995*).

Still another reason for regulating financial institutions is the role that banks play in determining the supply of money. Much regulation of these intermediaries is intended to improve government's control over money supply. One such regulation is the reserve requirement which helps the Central Monetary Authority exercise more precise control over liquidity. Likewise, deposit insurance regulation gives depositors confidence in the banking system and eliminates widespread bank failures, which cause large, uncontrollable fluctuations in the quantity of money.

B. Regulation and the Basic Sectors under the SRA

Figure 1 shows the general framework for analyzing how financial laws and regulations in the Philippines affect the provision of financial services to the basic sectors. Under the government's Social Reform Agenda (SRA), the basic sectors are the following: (1) farmers and landless rural workers; (2) fisherfolk; (3) urban poor; (4) indigenous cultural communities; (5) workers especially in the informal sector; and (6) other disadvantaged groups such as women, disadvantaged students, children and community youth, persons with disabilities, the elderly and victims of disasters and calamities. The overall vision is to grant these sectors access to quality basic services, productive resources and economic opportunities. For the sectors to be able to choose and for the vision to be sustained, the SRA asserts that there must be strong grassroots institutions that can effectively participate in self-governance.

There are laws that mandate government and non-government institutions to provide basic sectors access to financial services. These laws are directed either to institutions in the financial system or to non-financial government institutions, or both. Also, in many instances non-financial government agencies are directed to provide seed funds to institutions in the financial system for credit, guarantee, insurance, institution building and other financial services for the basic sectors. Sometimes, these agencies are even asked to lend directly to end-borrowers at concessional rates. These laws, while not strictly financial laws, affect the effective functioning of the financial market.[4] On the other hand, regulatory agencies are directed by law to ensure the compliance of concerned institutions to specific regulations. For example, the Bangko Sentral ng Pilipinas (BSP) monitors the compliance of banks to mandatory credit allocations and applies appropriate penalties for non-compliance.

The laws and regulations target formal financial institutions (such as banks and insurance corporations), cooperatives and non-government organizations (NGOs) for the delivery of financial services. The BSP regulates the formal financial institutions while the Cooperative Development Authority regulates cooperatives. . There is no clear oversight body that regulates the activities of NGOs. The Securities and Exchange Commission (SEC) regulates only in terms of registration and disclosure requirements (financial and organizational information).

As shown in ***Figure 1***, laws and regulations in the financial system affect the behavior of agents in the financial market. Financial institutions will make the appropriate adjustments

4 *These laws are usually part of laws that address a bigger or sectoral concern.*

to cover risks and costs associated with different characteristics of agents in the market . Since the basic sectors are viewed as disadvantaged (i.e., they are small and do not have collaterals to offer), government intervention was deemed needed to influence the allocation and pricing of credit.

The problem with the former (e.g., mandatory credit allocation) is that it forces lenders to act against their economic interests. Rather than put funds to the most profitable use, institutions are supposed to lend funds to targeted beneficiaries. But the more profits a lender forgoes, the greater the economic pressure it feels to allocate current fund flows away from the targeted population.

On the other hand, influencing the price of credit (e.g., a ceiling on interest rate) may achieve a good portion of its intended distribution effects in the short run. Beyond that unintended costs are incurred. For one, the excess demand resulting from a ceiling will lead financial institutions to ration credit resources towards the relatively bigger borrowers. Second, because of the ceiling, the price of credit would not be sufficient to cover the cost of administration. Third, the interest ceiling will discourage savings mobilization because the return on deposits is not enough to attract depositors. In essence, the main welfare cost results from inefficient financial intermediation between savers and investors.

Preferential credit allocation to specific sectors and interest rate ceilings or subsidies are characteristics of a supply-led policy environment. Savings mobilization is not viewed as an essential function of financial institutions since rural people do not save anyway and, thus, do not respond to price incentives. Hence, the government provides most, if not all, of the funds. As previously discussed, this approach to credit delivery taxes the financial system since it leads to inefficient allocation of financial resources (*Shaw, 1973; McKinnon, 1973*).

The current credit policy framework of the government is a reversal of the supply-led strategy implemented in the 60s and 70s. The basic elements are: (a) greater reliance on market mechanisms in the allocation and pricing of financial resources; (b) termination of direct lending activities of non-financial government institutions; and (c) greater private sector participation in the delivery of financial services. This approach is envisioned to result in greater financial market efficiency (*Fry, 1982*). However, its realization may be thwarted by a "political" market for regulation that perpetuates inefficiencies.[5]

As institutions are directed to deliver credit to the basic sectors, transaction costs are expected to be higher due to the small loan sizes. This may cause lending institutions to shift their loan portfolio away from small and towards large borrowers. However, lenders who want to continue providing micro-credit to small borrowers will have to introduce financial innovations to cope with transaction costs and risk problems. On the other hand, beneficiaries must learn to deal with financial institutions and develop their credit-worthiness given their relative inexperience in handling formal credit. Institution and capacity building will play a major role in addressing this concern. Appropriate interventions in this area will facilitate the steady access of beneficiaries to the services of financial institutions.

A legal mandate to lend to a targeted group will not necessarily result in an individual securing a loan even though

5 *This has been thoroughly discussed in the previous section.*

his objective characteristics are identical, or nearly so, with other applicants who are able to obtain loans. The basic assertion is that credit rationing occurs because of asymmetric information about the factors that influence the outcome of investment projects and the relative riskiness of basic sector borrowers. Even with a guarantee mechanism in place, financial institutions may still ration credit in favor of tried and tested borrowers.

The adjustment in the portfolio mix of financial institutions, particularly banks, will be influenced by the relative attractiveness of alternative forms of assets. Funds may be drawn away from the basic sectors as other financial investments become more attractive. Regulation may not even be able to arrest this as financial innovations intended at avoidance or circumvention emerge.

The maturity structure of loans will adjust according to the type of borrower. For borrowers in the basic sectors, the risks are perceived to be greater and therefore the maturity is expected to be shorter. At the same time, monitoring and collection systems suited for small borrowings will be designed. An example is the weekly collection and monitoring of loans.

Finally, laws and regulation can either promote or thwart savings mobilization efforts. To the extent that they are able to induce the accumulation of savings, loanable funds will be generated without having to resort to scarce government resources. A supply-led approach, on the other hand, will discourage savings and will make the provision of financial services to the basic sectors difficult to sustain.

3

Review of Financial Laws and Regulations

A. General Laws and Regulations

The erstwhile Central Bank of the Philippines (CBP) started a series of reforms in the financial market in the 80s which continued on in the 90s. Interest rate ceilings were lifted; the subsidized rediscount window was abandoned and made market-oriented; interest rates of subsidized credit programs were aligned with market rates; bank entry and branching were liberalized; and universal banks were allowed to have expanded areas of equity investments. In 1994, Republic Act (RA) 7653 changed the CBP to the Bangko Sentral ng Pilipinas (BSP). The new Charter strengthened the bank and gave it greater flexibility and independence in the conduct of monetary policy.

As can be observed from its recent policy issuances, the BSP's efforts have generally been directed at promoting greater efficiency in the financial system. This overall policy thrust, however, has often been contradicted by laws and regulations that seek to allocate financial resources to specific sectors of the economy. Oftentimes these laws create distortions in the financial market rather than promote allocative efficiency. Annex A provides a summary of these laws and regulations and their implications on financial intermediation. This section discusses the specific areas that these laws affect.

Intermediation Taxes. The liberalization of the financial system starting in 1981 has not resulted in the total elimination of intermediation taxes on the financial sector. The taxes impinging on the efficiency of financial intermediation include the credit quota schemes, the gross receipts tax, the deposit retention scheme, taxes on interest income and the reserve requirement. The general result is often higher lending rates which negatively affect real investments and the affordability of formal credit to the basic sectors.[6]

A credit quota or allocation scheme usually directs banks to set aside a certain portion of their loanable funds for targeted sectors. Because of this, banks do not have the flexibility to efficiently manage their loan portfolios since a fixed portion of loanable funds are not channelled to the relatively more profitable sectors. As a result, banks incur additional costs, which may be passed on to borrowers through higher interest rates.

The Agri-Agra Law (PD 717) and the Magna Carta for Small Enterprises (RA 6977) mandate credit allocation to targeted sectors. Both are implicit taxes on financial intermediation.[7] The Agri-Agra Law, passed in 1975, directs banks to allocate 25 percent of their loanable funds for agricultural lending. Of the 25 percent, 15 percent should be alloted to general agricultural lending while 10 percent should go to agrarian reform beneficiaries (ARBs). While banks have generally complied with the agricultural lending component, compliance with the agrarian component has largely been through the purchase of reserve eligible government securities which pay lower-than-market interest rates.[8] PD 717 does not only raise the cost of intermediation, it also penalizes the non-agriculture sector by depriving them of a fixed percentage of banks' loanable funds.

The Magna Carta for Small Enterprises was legislated in 1991. Among its provisions is a mandate to banks to set aside a portion of their loan portfolios to small enterprises according to the following schedule: at least five percent by the end of the first year of the effectivity of the law; 10 percent from the second to the fifth year, five percent on the sixth year and declining thereafter. Its effect on the cost of intermediation was somewhat softened when the Central Bank allowed equity investments by member banks in, and loans by members banks to, the BAP Credit Guaranty Corporation (BCGC), as part of compliance with the mandatory allocation (provided, the BCGC extends its loans to small enterprises). (BSP Circular 1385, 1993) This was, however, allowed only for one year (in 1993). Hence, the relative flexibility of banks to manage their portfolios arising from the alternative compliance was short-lived.

While RA 6977 directs credit to small enterprises, it does so at the expense of financial market efficiency. In the long run, the targeted sector does not really benefit due to the law's impact on the cost of intermediation. But instead of lifting the mandatory allocation, the Magna Carta for Small Enterprises was amended in July 1997, extending the provision on mandated credit allocation for another 10 years. In addition, banks were mandated to set aside at least six percent of their total loan portfolio for small enterprise credit and at least two percent for loans to medium-sized enterprises.

6 Annex A provide a summarization according to type of law/regulation in chronological fashion. In this section discussion is provided by subject area that these laws/regulations affect.

7 It should be noted however that the distribution of the burden of these taxes depends on the elasticities of supply and demand. In general, borrowers bear relatively more of the burden the more elastic is supply and the less elastic is demand.

8 There is implicit taxation because they distort the financial market without the government having to directly impose or collect taxes.

Besides mandatory credit allocations, another implicit tax is the deposit retention scheme. This scheme requires banks to invest in the same geographical region at least 75 percent of the total deposits generated from that region, net of required reserves against deposit liabilities and the total amount of cash in vault (BSP Circular No. 24, 1994). This restriction distorts the financial market since it narrows the area wherein banks can lend. It, thus, prevents banks from exploiting better investment opportunities outside a given geographical area.

Still another implicit financial intermediation tax is the reserve requirement. The tax is due to the (a) reduction in banks' loanable funds out of deposits and (b) lower-than-market earnings on the reserves that are required to be deposited with the BSP. Since banks have to pay interest on deposit liabilities, they recoup the forgone income from the reserve requirement by increasing their lending rates.[9] However, reducing reserve requirements to improve financial intermediation is not that simple since lowering the reserve requirement involves a trade-off between intermediation cost and inflation.[10]

The BSP has recently reduced the reserve requirement ratio (Table 1). The required reserves on demand and savings deposits of commercial banks (KBs) was reduced to 14 percent effective January 1997 and further to 13 percent effective July 1997 (BSP Circular No. 119, 1996). This is a significant reduction since the requirement was as high as 25 percent in 1991. Rural banks and thrift banks, on the other hand, have lower required

9 Investment in government securities as a form of compliance is allowed under PD 717. Further, RA 7900 enacted on February 23, 1995 exempts banks from PD 717 provided they lend 5% of loanable funds for the production, processing, marketing or distribution of high-value crops.

10 The penalty for non-compliance with the required reserve is stiff, - 1/10 of 1% per day on the amount of deficiency or the prevailing 91-day T-Bill rate plus three percentage points (CB Circular No. 8, 1993).

ratios due to the preferential treatment given them under the Thrift Banks' Act of 1995 (RA 7353) and the New Rural Banks' Act of 1992 (RA 7906). The reserve requirement on savings deposits for thrift banks is 12 percent effective January 1997 and 11 percent effective July 1997. For rural banks, it is six percent effective January 1997 and 5 percent effective July 1997 (BSP Circular No. 119, 1996). While the reductions will help lower the cost of intermediation and release more loanable funds for the economy, the uneven requirements for different types of banks also cause distortions. Nonetheless, the extent by which the basic sectors are able to capture the incremental funds associated with a lower reserve requirement ratio for thrift banks and rural banks depends on how the banks perceive their creditworthiness and bankability.

The gross receipts tax (GRT) is an explicit tax imposed on all receipts of a bank. Again, the increase in the cost of intermediation is passed on to borrowers in the form of higher interest rates. Under the 1981 Internal Revenue Code, the GRT for all finance companies was set at five percent. With the 1991 Local Government Code, this was changed to a rate not exceeding 50 percent of one percent of gross receipts of the preceding year.

Finally, the 20 percent withholding tax on interest earned from bank deposits weakens domestic resource mobilization (National Revenue Code, 1986). Where there is a huge domestic savings-investment gap, an economy is forced to fill the gap by tapping foreign resources such as foreign loans, grants and aid. The amounts sourced externally will have implications on the fiscal deficit and inflation as debts have to be serviced upon maturity. Savings, therefore, have to be mobilized domestically in order that there will be less pressure on the fiscal budget and more resources available for capital accumulation and economic growth.

Interest Rates. Administrative ceilings on interest rates have been around since the enactment of the Anti-Usury Law in 1916 (Act 2655). The law was virtually repealed in 1973 when the country's monetary authority was granted the power to change the interest rates "when warranted by prevailing economic conditions." In 1981, the gradual freeing of interest rates formed part of the IMF-World Bank reform package. Since 1983, interest rates on deposits and loans of various maturities and rediscounts have been largely market-determined. In the long-run, the deregulation is expected to bring about greater transparency and deepening of the financial market. There will be increased incentive to invest in financial assets and greater efficiency in the pricing and allocation of credit. Also, it will lead to a better loan portfolio since viable projects that have high rates of return are the ones financed.

While the pursuit of market interest rates has been the general thrust since the 80s, legislated interest rates have, nonetheless, been a common feature in recent laws. For instance, the Comprehensive Agrarian Reform Law or the CARL (RA 6657, 1988) specifies that small landowners, farmers and farmers' organizations should be extended concessional and collateral-free credit.[11] As the government's lending arm for the agrarian sector, the Land Bank of the Philippines (LBP) is seriously affected by this provision. The provision undermines its credit delivery program to the targeted sector since LBP's cost of credit delivery is much higher than the 12 percent ceiling imposed on its lending rate to the agrarian sector. For example, based on its foreign funds, LBP's total cost of credit ranges from a low of 21.1 percent to a high of

24.7 percent. On the other hand, the cost of credit on internal funds or deposits ranges from a low of 15 percent to a high of 28.8 percent (***Table 2 and 3***). This means that LBP has been operating below break-even. Hence, for LBP to sustain its countryside lending operation, it has to rely on its commercial banking operations and on appropriations from the national government. The latter obviously has implications on the fiscal sector, particularly on the resources that need to be mobilized to meet the requirements of small farmers. This shows that the cost of maintaining concessional rates on loans ultimately finds its way back to the government.

The adoption of legislated concessional loans to small farmers affects the quantity, quality, and productivity of agricultural investments since projects with low rates of return may be made artificially-viable by the ceiling. Over time, the concessional rate may not be sustained and the projects financed may fail. In a recent survey, it was reported that the repayment rate of LBP farmer cooperatives was no greater than 50 percent for the majority of the responses (*Dingcong, 1997*). Among the major reasons cited were project failure and low profit margin. The LBP, nonetheless, has to follow its mandate in providing concessional loans. In 1994, the LBP was further instructed to increase its loans and financial assistance to farmers at low cost as a safety net measure under the GATT Uruguay Round (AO 162). In response to this, LBP reduced its interest rates on agricultural production loans from 12 percent to 10 percent.

11 Usually there is more than one combination of reserve requirements and inflation that cover a given level of budget deficit. Unless therefore the fiscal position is stable or the deficit manageable reducing reserve requirements will likely induce higher inflation.

The Magna Carta for Small Farmers (RA 7607, 1992) further reinforces the subsidized interest rate feature in the CARL. The law mandates that the interest rate on small farmer loans should not exceed 75 percent of the prevailing market rate, inclusive of all service charges. Although this provision allows the interest rate to follow interest movements in the market, it still is a cap on the interest rate that can be charged. Still another law in the agriculture sector that legislates interest rates is RA 7900, providing for low-cost credit for the promotion, production, processing and distribution of high-value crops. It sets interest rates based on the prevailing LBP rate, which, as provided for in the CARL, should be concessional.

While major laws have been passed setting price limits on credit to specific sectors, the BSP has been moving towards allowing interest rates to move freely in the financial market. It has not subjected banks to any ceiling on lending rates for rediscounted papers covering agricultural production, cottage and small industries and financing of working capital (BSP Circular No. 52, 1994). No ceiling is likewise imposed on the amount of loans that banks can extend by various loan types (i.e., maturity structure, securitization, etc.).[12] Similarly, there is no ceiling on interest paid on savings and time deposits.[13] The direction that the BSP is taking is consistent with the current thrust of financial liberalization and will likely result in a more efficient allocation of financial resources.

Nonetheless, what is apparent in the directives of lawmakers is not to set an administrative ceiling on interest rates in general but to direct government institutions to adopt ceilings on loans for specific sectors. The effect is a decrease in the supply of credit to targeted sectors, rather than an increase (as the laws hoped to achieve). This is because at the ceiling rate, the amount that lenders are willing to provide is smaller than what they would have been willing to lend at the market rate (and less than the amount borrowers would like to avail of at that rate). With excess demand for credit, the group most discriminated against are the small borrowers, the sector the law aims to protect. The end result is that small borrowers, particularly those in the basic sectors, have less access to formal credit.

Bank Branching and Entry. Bank entry restrictions in the mid- and late-80s consisted of: (1) strict prohibition of entry into areas categorized as heavily branched and ideally-branched; (2) increased required reserves in government securities for purposes of opening branches; (3) increased required capitalization for banks of all types; and (4) an implicit rule in the Monetary Board not to allow new banks and branches to enter.[14] Towards the end of the 80s, monetary authorities instituted a new policy of liberalizing bank entry and branching. In 1988 the CB eliminated the prerequisite investment in government securities for opening branches and other bank offices (Circular No. 1188). In 1991 it deleted the requirement for banks wanting to establish branches to comply with the required loans-to-deposit ratio for four consecutive quarters (Circular No. 1290). In early 1993, it further removed the policy of bidding out franchises to establish branches. Finally, in line with RA 7721 of 1994,[15] the BSP allowed the entry of

12 RA 7906 is the Thrift Banks' Act of 1995 while RA 7353 is the New Rural Banks' Act of 1992.

13 RA 6657 provides that these collateral-free loans are to be based on social collaterals like guarantees of farmers' organizations.

14 Central Bank Manual of Regulations for Banks and Other Financial Intermediaries, 1991.

15 Ibid.

foreign banks to attract foreign investments, enhance the efficiency of the domestic financial system and make Philippine banking more globally competitive. All these reforms in bank entry and branching had led to an increased level of competition and a relative improvement in the efficiency of the banking system.

Table 4 shows the number and distribution of banks and branches, particularly those of commercial banks and specialized government banks. It is clear that the number of banks of different types (except thrift banks) increased from 1989 to 1993. The number of rural banks increased but more slowly than commercial banks. However, new banks and branches are concentrated in the Metro-Manila area. As a result, bank offices in Metro Manila comprise one-third of all the banks in the Philippines.

The liberalization of bank entry has led to improvements in the bank density ratios of all regions (***Table 5***). However, there are still regions, such as the Autonomous Region of Mindanao, the Cordillera Region, Eastern Visayas, Western Mindanao, Cagayan Valley and the Bicol Region, that are not well reached by banks. This reflects the preference of banks for Metro Manila, presumably because of the bigger market and better infrastructure compared to the lack of rural and regional development in other parts of the country. It is in those regions with low bank density ratios where the poverty situation is relatively more pronounced.

The competition arising from a more liberal bank entry and branching policy has somewhat reduced the level of concentration in the banking structure. The spread between lending rates and deposit rates, a rough indicator of bank concentration level, decreased from a high of 18 percent in 1991, to 10 percent in 1992 and further to seven percent in 1994 (***Table 6***). To a large extent, this drop in bank spreads can be attributed to the incentives provided by the BSP for bank branching. These include the lifting in 1991 of the compliance requirement with the loans-to-deposit ratio for four consecutive quarters. Also, banks were allowed in 1992 to establish one branch in an area of their choice (without having to bid) for every three branches that they were able to establish in 5th and lower class municipalities (CB Circular No. 1349). As the BSP continues to promote greater competition in the banking system, concentration levels are likely to fall further.

Prudential Regulation. Financial liberalization requires strong prudential regulation and effective bank supervision. Inadequacies in these reduce public confidence in the financial sytem as well as in the monetary authorities (*McKinnon, 1987*). As seen from the experience of Latin American countries, financial liberalization is likely to fail whenever there is macroeconomic instability and inadequate bank supervision *(Diaz-Alejandro, 1985*). The BSP, while moving towards financial liberalization, has at the same time been ensuring stability in the banking system. As early as 1980, the CB has been gradually increasing the minimum capital requirements of various types of banks. In 1996, it required a new set of minimum capital requirements (BSP Circular No. 117): ₱4.5 billion for expanded commercial banks; ₱2 billion for ordinary commercial banks; and ₱250 million for thrift banks within Metro-Manila and ₱40 million for those outside Metro-Manila. These changes are important in enabling banks to generate a greater volume of business and in improving the public's perception of their stability. Other recent regulations intended to strengthen banks and influence the provision of financial services, particularly in the countryside, are: (1) setting limits on the rediscounts of rural banks based on their credit ratings (Circular no. 76, 1995); (2) applying qualification standards for rural banks accessing loans from GFIs (Circular No. 58, 1994); (3) providing incentives for mergers and consolidation among banks and other financial intermediaries (Circular No. 1312, 1991); (4) regulating RB's capital adequacy ratio to not less than 10 percent of risk assets (Manual of Regulations, Book III, 1991); (5) setting guidelines on rediscount ceilings for rural banks that need to supplement their operating capital for loans to agrarian reform beneficiaries (Manual of Regulations, Book III, 1991); and (6) granting additional assistance to Rural banks (with satisfactory rediscounting repayment records) participating in special financing programs under supervised credit schemes (Manual of Regulations, Book III, 1991).

Deposit Insurance. The Philippine Deposit Insurance Corporation (PDIC) was created by virtue of RA 3591 in 1963, primarily to insure bank deposits. In 1992, its Charter was amended to make it more responsive to the needs of the banking system. Changes include an increase in the authorized capital to ₱3 billion; an increase in the deposit insurance to ₱100,000; an increase in the assessment premium of insured banks; and a mandatory role as receiver of closed banks. While these amendments are expected to bring more stability to the banking system, deposit insurance could also lead to the entry of banks into riskier financial markets. Like financial liberalization, it works well when banks are regulated and supervised effectively. Given these prerequisites, deposit insurance can be highly effective in maintaining financial stability.

B. Role of Specialized Financial Institutions

Over the past 50 years, financial institutions have been created and existing ones rehabilitated, strengthened or re-organized to address the perceived financing needs of specific sectors. When commercial banks made little effort to penetrate the countryside and supply financial services to its residents, a system of rural banks was set up (RA 720, 1952). When demand for medium and long-term development finance rose in the early years after World War II, development institutions such as the Development Bank of the Philippines (RA 85,1946) and a number of private development banks were created or encouraged (RA 4093, 1964). Recognition of the perceived unfulfilled credit needs of small-scale industries led to the creation of the National Cottage Industries (RA 3756, 1963). Similarly, the perceived shortage of financial services in Mindanao prompted the establishment of the Amanah Bank (PD 264, 1973). Oftentimes, new financial institutions were "customized" to fit specific sectors. Hence, the legal framework within which they operated reflected rigidly the need (as perceived by legislators) for additional financial services of specific types of clientele. This approach to the organization of the financial sector has prevailed to date.

Specialized Government Financial Institutions. The most recent financial institution organized to cater to a specific sector is the People's Credit and Finance Corporation (PCFC). Created on February 22, 1995 through Memorandum Order No. 262, PCFC became operational in June 1996. Fully-capitalized by the LBP, the objective is to use PCFC for poverty alleviation programs so that LBP can concentrate on its mandate of financing agrarian reform beneficiaries and servicing agriculture's growing demand for various financial services.

PCFC is an entity fully supervised and controlled by the LBP. It provides investment credit loans to accredited NGOs, financial institutions (FIs) and people's organizations (POs) implementing credit assistance programs for livelihood projects. It also provides credit for institution and capability building activities and other expenditures related to the lending program.

Following the establishment of the PCFC, the new charter of the LBP was signed into law on February 25, 1995 (RA 7907). The bank's authorized capital was increased from ₱3 billion to ₱9 billion, enhancing its viability to perform vital financial and development assistance to small farmers and fisherfolks. Moreover, the stronger capital base and greater operational flexibility are expected to level LBP's playing field with other players in the banking industry. Among the changes introduced in the new Charter is the strengthening of the bank's capital base via the establishment of a national marketing umbrella for farmers and fisheries cooperatives to attract massive capital formation from the savings deposits of these cooperatives. This will not only aid in the further financial strengthening of LBP but will also promote savings mobilization nationwide which is essential for sustaining the operations of farmers cooperatives.

Other amendments to the LBP Charter include the requirement for the Presidential Agrarian Reform Council (PARC)[16] to provide funds from the Agrarian Reform Fund (ARF) to pay all obligations incurred as compensation to landowners, and the allocation of at least 60 percent of the proceeds from the Asset Privatization Trust (APT) to the LBP for payment of agricultural lands.

16 Presumably because of the financial crisis experienced in the early 80s that led to the collapse of a number of banks.

These provisions, assuming sufficiently available funds from said sources, will free LBP from the enormous burden of servicing payments for its land transfer operations and allow it to concentrate on the delivery of financial services to small farmers and fishermen. However, if funds are not adequately available, LBP remains liable for the payment of bonds issued to landowners. The mismatch in the payment structure between landowners and ARBs does not augur well for the LBP. The time period of 10 years for payments to landowners is much shorter than the 30-year land amortization schedule of ARBs. Further, ARBs pay an interest rate of six percent per annum while the government pays the landowners LBP bonds at market rates. This mismatch in payment structure creates an instant financing gap that has to be sufficiently supplied by the ARF and the APT. Otherwise, additional resources will probably have to come from tax revenues.

At the forefront of LBP's re-organization under its new Charter is the Unified System Program (USP). This principally involves the merger of the branches and field office networks into a single delivery system of a whole range of bank products and services. With the comprehensive assistance offered, the LBP is expected to expand its outreach to small farmers and fisherfolks and provide banking convenience to them. Also, linkages will be formed with commercial clients, particularly in the marketing of their produce resulting in improved rural incomes. The USP is also envisioned to realize financial savings via lower operating expenses, thus strengthening LBP's financial position. Moreover, the savings in operating and capital expenditures will likely reduce the cost of credit delivery to farmers. The USP, launched in 1995, will be completed in 1997.

Part of the reforms in the 80s was the rehabilitation of DBP and PNB. On December 3, 1986, the government issued revised charters for PNB and DBP (EO 8O and EO 81, respectively). These two GFIs were accorded importance because of the size of their non-performing assets and the concomitant budgetary losses these entailed to the government. The change in charters effectively relieved them from the financial burden of servicing their non-performing assets. The objective of the financial restructuring of the DBP was to reorient it into a wholesale bank with private sector orientation so that it will be able to mobilize long-term funds and act as a market for long-term papers. This is essential because of the scarcity of term credits needed for economic development. In the case of the PNB, the objective was to retain its expanded commercial functions and privatize it with the government having a minor share after the privatization. With these reforms, DBP and PNB are still expected to perform developmental functions since their new charters mandate them to provide financing to agricultural and industrial small and medium enterprises in the countryside. They are, however, required to be financially viable and not depend on government assistance.

The new policy regime in the mid-80s also effected the transfer of special lending programs from the erstwhile Central Bank (CB) to the DBP and LBP. The rationale was to free the CB from all developmental banking functions and allow it to concentrate on monetary management, regulation and supervision. Hence, the Agricultural Loan Fund (ALF) and the Integrated Rural Financing (IRF) programs were transferred to the LBP while the Industrial Guarantee Loan Fund (IGLF) was moved to the DBP. The IGLF and the ALF are exempted from the legal reserve requirement on deposits arising from their operations (CB Circular NO. 1133, 1987). Loans granted under the ALF facility to finance both seasonal production credit and medium and long term sub-loans for fixed assets and permanent working capital were set at market-oriented levels (CB Circular no. 1151, 1987). These measures enhanced the sustainability of these special programs and released funds to the agriculture sector. Further, in 1991 the CB exempted from the reserve requirement, special time deposits of financial institutions under the special financing programs of the government and/or international financial institutions being (or previously) administered by the CB (CB Circular No. 1276, 1991). While it appears that the exemption was intended to lower the intermediation cost of special financing programs, a reserve requirement that is different from that imposed on other types of deposit is inconsistent with market-oriented monetary policy.[17]

In 1988, the CARL paved the way for the transfer and attachment of the National Livelihood Support Fund (NLSF) to the LBP.[18] The NLSF was designated as one of the institutions to provide support services to Agrarian Reform Communities (ARCs). In 1993, AO 75 directed the transfer under LBP supervision of all NLSF assets and funds. In essence, NLSF is a fund used to provide livelihood credit and institutional development services for ARCs.

The Al-Amanah Islamic Investment Bank is another specialized government bank recently provided with a new Charter. On January 26, 1990, RA 6848 was enacted into law authorizing Al-Amanah bank to perform banking, financing

17 An Act Liberalizing the Entry and Scope of Operations of Foreign Banks in the Philippines and for Other Purposes, May 18, 1994.

18 Which the LBP co-chairs.

and investment operations and to establish agricultural, commercial and industrial ventures in the Autonomous Region based on the Islamic concept of banking. Among the privileges granted to the bank are an eight-year exemption from all taxes under the National Internal Revenue Code related to its conduct of business and exemption from all customs duties for all importations. The establishment of the bank will provide increased availability of banking services to the Islamic population in the Autonomous region. Its exemption from taxes implies lower intermediation costs. However, being a highly-specialized bank, it has a less diversified portfolio and a limited geographical outreach. In the long-run, both factors may take its toll on the bank.

The period from the mid-80s to the mid-90s has been a time of reforming the specialized government financial institutions. Strengthening these institutions to better serve their targeted clientele has been the focus of charter amendments. All these efforts have not reduced the presence of the government in directly providing financial services to the basic sectors. In fact another financing agency, i.e., the PCFC, was created to handle a specific task of lending to the poor.[19]

It is important to note that there is always the danger of reverting back to the 70s when a proliferation of specialized financial institutions (particularly those of government) led to the fragmented and segmented credit markets. As a result, there was little competition among financial institutions, intermediation costs were high, and resource allocation was inefficient. What that experience taught us is that creating

19 This provision is being effected even if the special funds have been transferred to GFIs because time deposits are usually subject to reserve requirement.

specialized institutions is not a panacea for the basic problem of credit allocation.

International experience over the past 40 years suggests that specialized institutions, particularly those that have attracted foreign resources, have failed completely. These institutions have a mixed record in allocating funds to productive development projects (*Gordon, 1983*). Very few of these institutions became self-supporting, autonomous financial institutions capable of mobilizing resources entirely on commercial terms. This is partly because specialized institutions have often been required by legal mandate to grant loans at low interest rates, frequently negative in real terms (*World Bank, 1985).*

The main problem with virtually all specialized financial institutions is that they are established to lend to those that existing financial institutions - the commercial banks - have avoided. By and large, commercial banks choose not to lend when the perceived risks are too high. Hence, specialized financial institutions are deliberately set up to lend to high-risk borrowers. But instead of allowing them to charge higher rates for assuming higher risks, government subsidies and privileges are provided. As a result, the specialized financial institution set up to support a problem sector of the economy itself becomes a problem institution. In the case of the Philippines, this is true not only for specialized government banks but also for rural banks.

Specialized Non-Government Financial Institutions. Rural banks had been the primary conduits of large-scale government-sponsored credit programs. Under the so-called "supply-leading strategy" of development finance, the government provided rural banks with a host of incentives and subsidies from the early 50s to the mid-80s. This strategy turned out to be costly for the rural banking system. The availability of cheap loanable funds led rural banks to (a) neglect savings mobilization and (b) follow less rigorous credit discipline. The latter, in turn, instilled among borrowers a "dole-out" mentality. Hence, when the government pursued financial liberalization in the 80s and terminated rural banks' special previleges, many of these banks increasingly became insolvent and illiquid. Thus, years of government support only weakened the rural banking system.

The rehabilitation of distressed rural banks began in 1987 with CB Circular 1143 and 1172. The scheme was able to help some banks especially the stronger ones and those with dynamic and entrepreneurial managers (*Agabin and Lim, 1993*). The New Rural Bank Act 1992 (RA 7353) offered an even more generous scheme. The major incentives are: the conversion of past due loans into government preferred shares, the extension of concessional loans by the LBP and other government banks to rural banks; the lower reserve requirements on deposits; and the grant of tax exemption privileges. While RA 7353 seeks to address the problems of rural banks and enhance their viability, there are specific provisions that are contrary to current policy.

First, mandatory subscription by GFIs to rural bank shares contradicts the government's privatization efforts. Second, allowing an appointive or elective public official to serve in any capacity in a rural bank raises the issue of conflict of interest. Third, extending concessional loans runs counter to the avowed market-orientation of financial and credit policies. These provisions highlight the type of government support that is not likely to strengthen rural banks in the long-run. Insulating rural banks from competition through legislation and subsidies will only perpetuate their inabilities to follow sound business practices that are based on independent assessments of risks and profits.

In recognition of the role of rural banks in promoting the basic sectors, the BSP also issued specific regulations for rural banks to better serve the basic sectors. These include authorizations: to reduce interest rate by two percent as an incentive to farmer-borrowers (under supervised credit) who are able to pay their loans in full on or before maturity date; to grant clean loans to meet the health, education and subsistence needs of farmers, farm families and merchants as well as other inhabitants within their service areas; and to grant loans under the supervised credit system. (Manual of Regulations, Book III, 1991).[20]

Over the course of the 1960s, several laws were passed to strengthen other types of financial institutions and make them more responsive to the needs of the basic sectors. In particular, RA 3779 was passed in 1963 to ensure the sound, stable and efficient operation of Savings and Loan Associations (SLAs). The law came in recognition of the importance of SLAs in providing financial services to small member-borrowers.

In 1964, the Private Development Banks' Act (RA 4093) was promulgated to provide medium- and long-term loans for agriculture and industry. Among others, it allowed the DBP to subscribe to the initial capitalization of a private development

20 NLSF is wholly comprised of Kilusang Kabuhayan at Kaunlaran (KKK) accounts made available for livelihood projects during the Marcos regime.

bank. However, despite the proliferation of development banks in the countryside following RA 4093 and the huge demand for term loans, lending for longer-term projects remains minimal (*Segura, 1977; ACPC, 1993*). Banks continue to prefer short-term loans to protect themselves from adverse changes in interest rates (*ACPC, 1993; Lamberte, 1991*). The few financial institutions that have extended medium and long term loans have done so either because of their mandates or because of the availability of seed funds from multilateral organizations (*ACPC, 1993*).

In 1995, a new Thrift Banks Act was passed (RA 7906)to promote agriculture and industry and provide easy access to medium and long-term credit facilities at reasonable cost. This law encourages the mobilization of savings from the public by granting thrift banks preferential terms on reserve requirements, unrestricted branching rights within a region, and tax exemptions (with the exception of corporate income taxes and local taxes) for a period of five years. As in the case of rural banks, these privileges only promoted inefficiencies in the thrift banking system.

In support of RA 7906, the BSP has also made available potentially larger credit funds to thrift banks through its existing facilities. These include rediscounting privilege covering specific papers (such as agrarian reform credit under PD 717), access to BSP credit facilities for supervised lending operations, and rediscounts of up to 100% of networth (Manual of Regulations, Book II, 1991).

C. Guarantee and Insurance Schemes[21]

In 1986, the consolidation of special lending funds of the Department of Agriculture (DA) into the Comprehensive Agricultural Loan Fund (CALF) signalled a radical shift in the policy orientation of the government (EO 113). As part of this new policy orientation, direct lending programs were terminated. Instead, agricultural credit guarantee schemes were promoted and expanded through capital allocation from the CALF portfolio. The underlying view was that the key to integrating the rural financial market into the formal financial system is the introduction of financial innovations to reduce lending risk and administrative cost. Credit guarantee mechanisms were perceived to be less distortionary because they leave intact the decision processes and institutional relationships of the private credit market. As such, they were also perceived to be generally cost-effective since a guarantee institution, unlike direct lending programs, can leverage a given fund base by a multiple (*Bautista, 1992*).

Experience with credit guarantee schemes, however, has not been very promising. Studies reveal that guarantee programs have not resulted in the expected expansion of outreach of formal credit in the rural areas (*Llanto et al, 1991; Llanto and Magno, 1994*). Banks still prefer to lend to their regular clientele, perhaps doubting the adequacy of guarantee facilities to meet sufficiently large claims. Collateral was required despite the presence of the CALF guarantee. Thus, access to formal credit remains a problem for small borrowers even with the guarantee.

21 There are current initiatives through a pending bill in Congress to privatize PCFC.

Despite the ambiguity of credit guarantee, laws have been issued to create and re-organize guarantee institutions specifically intended to induce private banks to lend to small borrowers. LOI No. 1308 (1983) established the KKK Guarantee Fund as a special account in the CB to guarantee small- and medium-sized KKK loans released through banks. Initial funding came from the Economic Support Fund. The Fund evolved into the Guarantee Fund for Small and Medium Enterprises (GFSME) which caters to the financing needs of SMEs. In 1991, the Small Business Guarantee and Finance Corporation (SBGFC) was created to provide various alternative modes of financing for small enterprises and to guarantee loans obtained by qualified borrowers (RA 6977). The following year, the Quedan Guarantee Fund was re-organized and renamed Quedan and Rural Credit Guarantee Corporation (1992).

To strengthen the implementation of the CARP, RA 7905 was signed into law in 1995. Among others, it called for the creation of a guarantee fund for agricultural landowners that will enhance the collateral value of their lands affected by the CARP. Presumably, this provision was made in response to the non-negotiability of government-issued land instruments (such as Emancipation Patents (EPs)) used as collaterals in bank loans. That is, since EPs are non-transferrable, if the farmer defaults on his loan, the EP reverts to the farmer. This prejudices the bank's right to foreclose the property (PD 27; RA 6657). Indeed, based on a bank survey, private banks do not accept farm lands as collateral due to, among others, the uncertainties over land ownership created by the implementation of the CARP (*Llanto and Dingcong, 1994*). For banks that accept farm lands as collateral, the land is required to not exceed the five-hectare CARP retention limit. Among the different types of banks, only rural banks are allowed to foreclose lands covered by the CARL (RA 7353 1992).

Also, RA 7900 (1995) created the High Value Crops Development Fund (HVCDF) with an initial capital of ₱1 billion to be sourced from the Comprehensive Agricultural Loan Fund (CALF). Managed by the LBP and the DBP, part of the fund was to be used for low-cost credit for farmers and farmers' cooperatives and the other part for high-value crop insurance. Credit guarantee was to be provided by Quedancor. Participating banks are exempted from the Agri-Agra Law provided they lend a minimum of five percent of their loanable funds to the sector.

In 1995, RA 8175 gave the Philippine Crop Insurance Corporation (PCIC) a fresh mandate. The Act increased the capitalization of the PCIC; expanded the coverage of agricultural insurance to include other crops such as coconut, coffee and pineapple and non-crop agricultural assets such as machinery, equipment, transport facilities and othe related infrastructure; created a state reserve fund; and allowed PCIC to undertake reinsurance. The charter amendments were intended to enhance the viability of PCIC's operations and address the insurance requirements of small farmers more effectively. Moreover, the expansion of agricultural insurance coverage was envisioned to provide broader protection to small farmers and fishermen and reduce PCIC's risks through portfolio and asset diversification.

D. Role of Non-Financial Government Agencies[22]

Direct Lending. Experience over the past 20 years has shown that non-financial government agencies cannot be bankers. For one, they do not have the capacity to assess project viability and to monitor and collect loans. The resulting high level of defaults jacked up administrative costs which, in turn, ate up a large proportion of the treasury-sourced budgets of the agencies. Moreover, another problem with direct lending by non-financial government agencies is their exposure to political influence (not to mention harassment) as they make decisions related to loan approvals and collections. Lastly, non-financial government agencies have to rely on external funding to meet all the fund requirements of the intended beneficiaries. With its scarce resources, the government cannot accommodate the estimated requirements for lending to targeted beneficiaries.

With the change in government in 1986, Executive Order (EO) 113 terminated all direct lending programs of non-financial government agencies and consolidated some 20 agricultural credit programs into the CALF. However, while the policy of government has been to abandon direct lending by non-financial government agencies, the existing realities seem not to support it. In 1987, EO 158 created the *"Tulong sa Tao Fund"*. The Fund seeks to provide credit for micro entreprenuers, create employment and enhance income in rural areas, and develop and strengthen NGO capabilities for the implementation of livelihood projects. The EO mandated the Department of Trade and Industry (DTI) to administer the Fund and determine the conditions and availments of the Fund. Clearly, DTI's involvement in credit management and decision contradicts the policy of no direct lending.

22 Provisions in the Manual of Regulations apply unless amended or revoked through issuance of a BSP Circular.

Similarly in 1987, the Technology Resource Center (TRC) became the Technology and Livelihood Resource Center (TLRC). It was mandated to act not only as the technology delivery arm of the government but also to further livelihood opportunities. This new mandate opened the door for TLRC's directed credit programs, which remain operational to date.

In November 1988, Cabinet Resolution No. 29 was passed as part of the anti-poverty campaign of the Aquino government. It contained an approved set of policy guidelines for government-sponsored livelihood programs and vested the Departments of Agriculture, Trade and Industry, Labor and Employment, Agrarian Reform, Social Welfare and Development, Natural Resources, Education, Culture and Sports, and Local Government with the primary responsibility of implementing livelihood programs and projects. While only the Department of Social Welfare and Development (DSWD) was allowed to engage in direct lending activities, the resolution, nonetheless, allowed non-financial agencies to extend credit through banks and NGOs. Thus, the Cabinet Resolution, which explicitly allowed regular non-financial government departments to implement livelihood programs and projects, circumvented the normally tedious process of securing approval when using budgetary appropriations for directed credit programs (*OECF, 1995; Esguerra, 1996*). This measure opened the floodgates to various livelihood programs and projects sponsored by government agencies in the name of poverty alleviation. It directly contradicted efforts taken in 1986 to consolidate numerous programs in agriculture. It also ignored the costly experience in the 70s of direct lending by government line departments (*Esguerra, 1996*).

Following the Cabinet Resolution, there was a proliferation of livelihood programs administered by government non-financial agencies. The Overseas Workers (OWI) Fund Act (RA 7111, 1991) established a credit facility for the livelihood projects of overseas workers. An OWI Fund Board was created to administer the Fund, with loans extended at concessional rates.

Likewise, the Local Government Code (RA 7160, 1991) enabled LGUs to secure loans from banks and lending institutions for livelihood projects and other economic activities. LGUs can also access financing and guarantee facilities through the *Bagong Pagkain ng Bayan* (BPnB) for agricultural and support projects. In 1992, the BPnB was transferred to TLRC giving TLRC an additional mandate to provide financial services to LGUs. These laws, created in succession, promoted a supply-led approach to credit. They encouraged non-financial government agencies to go into direct lending, mandated funds be delivered at concessional rates, and allocated credit to specific sectors.

Still another legislation that promotes direct lending is RA 7368 (1992). The Act created the Countrywide Industrialization Fund (CIF) to finance the industrialization projects of towns and cities. The Countrywide Industrialization Office (CIO), which is attached to the DTI, was set up to manage the fund. The CIO Management Board makes the final credit decision while the conduit bank simply releases the funds.

In 1994, AO 148 created the Task Force on Credit for the Poor under the Presidential Commission to Fight Poverty (PCFP). Its main task was to review the existing government credit programs for the poor with the end in view of rationalizing these programs and formulating a Master Plan for the PCFP. While the PCFP has already been operationalized, the proliferation of subsidized livelihood and credit programs seems not to reflect the concept of rationalization.[23]

In 1995, RA 7882 was passed providing credit assistance to women engaged in micro and cottage business enterprises. Under the law, GFIs were to extend loans at the lower of banks' prime rate or at 12 percent per annum. The law mandated the Bureau of Small and Medium Business Development of the DTI to implement the Act. Further, GFIs were directed to earmark five percent of their loan portfolio for women covered under the law. Clearly, this Act has all the ingredients that distort the credit market.

It is important to note that even before the reforms in the 80s, there were already non-financial government agencies mandated to go into direct lending. Among these agencies are the DSWD (RA 5416, 1969) and the Rural Workers' Office of DOLE (PD 1365, 1978).

In recent years, the General Appropriations Act[24] has set aside large amounts of financial resources to support the government's drive against poverty. The two major fund sources are the Countrywide Development Fund (CDF) and the Poverty Alleviation Fund (PAF). While the intentions are indeed meritorious, these allocations have great potential in distorting the credit market. These resources find their way in

23 Guarantee institutions and programs are reviewed in greater detail in a separate survey. This section merely focuses on the legal basis for these schemes.

24 Refer to Annex B for a summary.

the budgets of non-financial government agencies to finance livelihood and credit programs.[25] Line agencies evaluate and select the conduit or beneficiary group, and in some cases, with the endorsement of the Congressman or Senator concerned.[26] Ceilings on interest rates are also imposed. This credit delivery approach to targeted sectors is clearly not consistent with the government's policy of promoting greater efficiency in the pricing and allocation of financial resources. It is, however, important to note that recent guidelines on the use of the PAF indicate that funds for livelihood will be used only for capability building and not for extending credit.

Coordinating Bodies. Coordinating bodies were organized in the mid-80s to put to order the various credit programs of the government. EO 113 (1986) created the Agricultural Credit Policy Council (ACPC) to synchronize all credit policies and programs in support of the DA's priority programs. The Council is mandated to review and evaluate the economic soundness of all on-going and proposed agricultural credit programs. The same EO mandated the consolidation of all existing and future agriculture and agriculture-related loan funds under the CALF.

Cabinet Resolution No. 29 (1988) designated the Social Development Council (SDC) as the coordinating body for livelihood development programs and projects. SDC is responsible for monitoring and evaluating livelihood projects. It reports to the President and the Cabinet.

25 There are at least 111 directed credit programs based on the NCC report.

26 See for example RA 8250, General Appropriations Act of 1997 and EO 363, August 23, 1996 which sets the guidelines for the allocation of the Poverty Alleviation Fund.

AO 86 (1994) created the National Credit Council composed of respresentatives from government financial and non-financial agencies and private sector organizations. The Council is tasked to rationalize the various credit and guarantee programs of the government, define the role of guarantee agencies, develop a national credit delivery system geared towards productive capability of beneficiary groups and efficiency and effectiveness of financial intermediaries, and encourage private sector participation in credit delivery in the countryside.

It is interesting to note that while these coordinating agencies were created to rationalize the various credit programs, directed credit programs have continued to proliferate. Many of these adopt subsidized interest rates and direct lending by non-financial government agencies. The problem is that none of these coordinating bodies are empowered by law to enforce the necessary penalties for non-compliance. Also, there is no clear authority vested upon them to approve, disapprove and terminate projects.

Another coordinating body recently created is the National Commission on Savings (EO 364, 1996). The Commission is directed to take the lead in accelerating capital formation, particularly through savings in banks and other financial intermediaries. The E.O. is timely in view of the absence of savings mobilization in many of the existing financial laws.

E. Role of Cooperatives and NGOs

The government's thrust towards private sector involvement in development and people empowerment at the grassroots level gave rise to non-bank financial institutions servicing the basic sectors. There are now cooperative credit unions and various self-help groups (including farmers' cooperatives) encouraging savings mobilization among small rural folks and providing lending to their members. Similarly the rise of NGOs in the rural areas has increasingly contributed to funding wholistic and integrated rural development programs. These include livelihood and rural industry projects.

Cabinet Resolution No. 29 clearly supports the role of NGOs[27] in institution building and as conduits of lending programs. This role was further articulated in the NCC Policy Guidelines for Credit Programs (1994). Since these organizations deal closely with targeted beneficiaries, they are able to gather better information about the creditworthiness of small borrowers. Hence, the problems associated with asymmetric information are not as severe as those faced by private financial institutions.

NGOs involved in credit delivery however are hampered by institutional constraints (*Llanto, Garcia and Callanta, 1996*). The General Banking Act (RA 337, 1948) does not allow them to lend through the receipt of deposits of any kind. Hence, they have to rely heavily on donors and funding agencies. Also, as non-formal financial institutions, they cannot raise sufficient equity. Furthermore, unlike banks, they are constrained not to have extensive and viable networks for delivering services to the poor. All these contraints tend to hamper NGOs' expanded outreach and long-term sustainability.

In 1990, RA 6938 was passed ordaining the Cooperative Code of the Philippines. The Act promotes the growth and

27 *A separate survey on directed credit program forms part of the CPIP set of studies and hence is not discussed in this paper.*

development of cooperatives. Specifically, it recognizes the role of cooperatives in the provision of financial facilities and non-formal education to members. It also allows cooperatives to organize among themselves a cooperative bank. Cooperatives are exempted from taxes on transactions to members.

Together with the Cooperative Code, RA 6939 was passed creating the Cooperative Development Authority (CDA). The CDA has powers to develop and conduct training programs for cooperatives, merge and dissolve cooperatives, cancel cooperatives' certificates of registration, and assist cooperatives in arranging for financial and other forms of assistance, among others.

The Magna Carta for Small Farmers (1992) is another law that highlights the role of cooperatives and NGOs. It mandates the DA, through ACPC and other concerned agencies, to give subsidies for education and training of small farmers on credit awareness, loan acquisition and loan repayment. Further, it mandates an information drive to promote the establishment of strong and viable farmer's organizations such as cooperatives, credit unions, rotating savings and credit associations and NGOs, which play a major role in increasing small farmers' access to credit. In order to have greater outreach to small farmers, the Act promotes the growth of networks of development banks.

These laws, including the CARL, brought a resurgence of interest in cooperatives from the latter part of the 80s up to the 90s. Since the enactment of the CARL in 1988, the LBP has shifted from individual lending to wholesale lending through cooperatives and rural financial intermediaries. LBP lending to cooperatives has grown dramatically a few years after the CARL was launched. In the 90s, however, lending contracted. LBP became more cautious as high past due rates were registered in cooperative lending. In 1995, the Cooperative Accreditation Program was launched to help cooperatives transform into viable and bankable community-based enterprises.

Two reasons appear to explain the non-sustainability of many cooperatives: the lack of maturity; and the wrong motivation to organize (many do so not voluntarily but because of government initiatives) (*Dingcong, 1997; Llanto, 1994*). However, with the appropriate supervisory and regulatory environment, as well as efficient management policies and practices, credit cooperatives can grow into self-reliant and self-sustaining financial institutions. They have enormous potential in providing self-sustaining financial services to small borrowers, especially if capitalization is adequate and members' share and capital are adequately protected (*Llanto, 1994*).

In 1994 the general framework for fighting poverty was spelt out in Memorandum Order (M.O.) No. 213, otherwise known as the Social Reform Agenda. The expansion of credit in all the basic sectors was identified as one of the "flagship" programs. The Agenda launched a "Credit-for-the-Poor" program with (a) a socialized credit program using the Grameen Bank Approach for the ultra poor, (b) active and sustained cooperative formation and development for the average poor, and (c) dynamic mainstreaming for the near-poor. This component of the credit flagship program seemed to promote a supply-led approach to credit delivery. It transmitted the perception that in socialized credit, large amounts of financial resources are directed to the poor at concessional rates. However, without satisfying viability and sustainability conditions, these socialized programs are not likely to succeed. In this regard, the LBP has been designated as the trustee bank for socialized credit programs with cooperatives and NGOs/POs as actual program implementors. Accreditation of these program implementors is to be carefully undertaken to ensure the effectiveness of the programs.

4
Conclusions

Existing financial laws and regulations affecting the provision of financial services to the basic sectors often conflict with the government's thrust towards financial liberalization. The transition appears to be slow because of the more than two decades of heavy regulation and subsidies that permeated the financial sector. Some of the laws that should have been abolished remain. The difficulty lies, in part, on the fact that recent legislations are still reminiscent of the supply leading strategy of the 60s and 70s.

Despite the policy reforms that started in the 80s, financial laws and regulations continue to be generally repressive. Mandatory loan allocations, the deposit retention scheme, the gross receipts tax, reserve requirements and taxes on interest income remain. Positive developments, however, can be noted in recent reductions in the reserve requirements.

While the BSP has been exerting effort to fully deregulate interest rates, legislation that mandate ceilings abound. This conflict thwarts the gains made in allocative efficiency. The implications of an administrative ceiling on interest rates are well known and documented, yet it has become, and still is, a popular course of policy action. Reversing the legislation is doubly difficult because of the tedium in amending or abolishing laws.

The BSP has been doing its part in promoting greater efficiency and competition in the banking industry. It has liberalized bank entry and branching policy. This has led to (a) an increase in the number and distribution of banks and branches, (b) improved bank density ratios for all regions and (c) reduced bank concentration levels (as seen in narrowing spreads between bank lending and deposit rates). Also, signs of financial deepening have been observed with the ratio of money supply to GDP rising since 1993 and reaching about 40 percent in 1995 (Table 7). Nonetheless, while the BSP is moving towards financial liberalization, its positive moves can be deterred by subsidy promoting legislations.

Specialized banks, specifically, Al Amanah Bank, rural banks and thrift banks, have been getting preferential treatment. These banks are exempted from the GRT and have lower reserve requirements. While these exemptions lead to lower intermediation cost for these institutions, they distort the financial system since they are selective and do not cover other institutions performing financial intermediation functions. In addition, these specialized financial institutions enjoy implicit subsidies in the form of tax exemption (e.g., customs duties)[28] from all except corporate income taxes and local taxes. Further, government banks are directed to extend loans to rural banks at concessional rates. These subsidies create inefficiencies in the financial market and the government ends up bearing a large part of the cost.

28 A case in point is DTI's assistance to micro enterprise development program (AMEDP) and sectoral livelihood program.

Despite privatization efforts, existing banking laws do not seem to reflect a diminished government presence. Government subscription in rural banks, emergence of new government financial institutions, and rehabilitation and strengthening of specialized banks through increased capitalization and transfers of assets and liabilities suggest growing government involvement in financial markets. Only the privatization of the PNB under its new charter appears to signal less government presence. But, as in the case of the DBP after its rehabilitation, the PNB is still expected to perform development functions.

The other banks with new charters are the LBP and Al-Amanah Islamic Investment Bank while the newly-organized institutions are the SBGFC and the PCFC. These specialized institutions are set up or given new charters to provide financial services to sectors that commercial banks and other private financial institutions have avoided. Because of the relatively high risks associated with these types of borrowers, these institutions must be compensated with higher loan rates for assuming higher risks. However, this does not seem to be the case as reflected in the laws on interest rate ceilings.

One of the problems associated with having too many specialized institutions is the fragmentation of credit programs resulting in higher administrative costs. This is also likely to be true for special funds. In recent years, there have been a number of special funds created by law for livelihood and credit. These are the NLSF, HVCDF, CALF, CIF, PAF, CDF, agrarian guarantee fund, TST fund, trust fund for the Credit for the Poor, ARF, etc. To the extent that they affect the fiscal budget, these funds may have to be reviewed and rationalized. Consolidation may be necessary for those funds that duplicate each other.

Greater protection has been accorded to bank depositors with the amendments to the PDIC's Charter. To the extent that there is adequate supervision, the amendments are also expected to bring more stability into the banking system.

Since the mid-80s, laws promoting guarantee schemes were passed targeting small borrowers in specific sectors. However, experience with the agriculture credit guarantee scheme has not been very positive. There was no significant expansion of access to credit among small farmers. Banks continued to cater to regular and tested clients and required collateral even in the presence of the guarantee.

Government has not veered away from direct lending by non-financial agencies. Several pieces of legislation have been passed directing non-financial government agencies to manage credit programs and make credit decisions. Many of these laws even mandate the adoption of subsidized interest rates. Administrative costs of these mandated direct lending programs usually eat up a large proportion of the treasury-sourced budget of the agencies. Given scarce government resources, financing the requirements of direct lending programs will exert pressure on the fiscal budget. Meanwhile, government has to deal with competing development concerns such as those in education, energy and infrastructure. Adequate funding from tax and non-tax sources is also needed for these sectors. If the government's revenues are not able to catch up with its expenditures, the fiscal deficit will rise. Financing the deficit through money creation will generate inflationary pressures because of substantial amounts that have to be raised over the period of program implementation. On the other hand, the flotation of government securities will put pressure on interest rates to rise. Similarly, foreign borrowing will increase the debt stock. These point to the need for reforming the direct lending approach to targeted disadvantaged groups.

Recent laws have stressed the importance of cooperatives and NGOs in the provision of financial services to the basic sectors. Their emergence has enabled groups previously unserved by private banks to access credit and savings facilities. Credit cooperatives and credit NGOs possess information technologies in screening and monitoring small borrowers that are not otherwise available to private banks. Also, they have greater outreach to the poor. A major constraint, however, in the growth and sustained development of these institutions is the absence of regulation and supervision. Like banks, they too are subject to risks that can lead to financial failures and closures. The CDA currently assumes the regulatory role for credit cooperatives. However, its mandate to promote cooperatives and regulate them at the same time seem to be conflicting objectives. The capability of the CDA to perform regulatory functions is another constraint. In the case of credit NGOs engaged in savings mobilization, there is no single agency performing the functions of regulation and supervision. It should be noted that these institutions differ in the risks they face compared to banks (*Vogel, 1997*). Their mission, organizational objectives and structure also differ. Supervision and regulation of these institutions, therefore, need not be as rigid as those applied to banks (*Llanto, 1994; Llanto, Garcia, Callanta, 1996; Vogel, 1997*).

Coordinating bodies have been created to oversee and rationalize credit programs. However, despite the presence of these bodies, fragmented credit programs continue to persist as a result of laws formulated by Congress. These programs, many of which are directed to targeted beneficiaries, mandate non-financial government agencies to perform direct lending functions and lend at a fixed interest rate. Coordinating agencies are ineffective in regulating and rationalizing these programs because they lack the power to enforce penalties for violations. These agencies have no clear authority to approve, disapprove and terminate projects.

A positive development in the formulation of laws and regulations in the post-1986 regime is the inclusion of savings mobilization and institution building. These are critical ingredients for sustaining a credit delivery system. The lack of these ingredients led to the failure of supply-led programs in the 70s. If the government is to make a significant impact on poverty alleviation, it should focus on institution building, training and savings mobilization rather than on supplying large amounts of cheap credit.

In sum, despite the overall policy framework of promoting greater efficiency in the financial market, many laws are largely characteristic of the supply leading approach of the 60s and 70s. At the program and sectoral level this disparity is even magnified. Legislation to address the financial requirements of the basic sectors has often created unintended effects. A positive note, nonetheless, is the BSP's initiatives to increase competition and efficiency in the financial market. The challenge really lies in reversing and preventing laws and regulations that are inconsistent with the government's thrust to free the market of distortions and improve the allocation of financial resources.

5
Recommendations

Based on the results of the review, this section provides some broad recommendations to improve and rationalize the credit policy environment. The necessary administrative and legislative measures are highlighted.

Review of intermediation taxes. Although a much more liberal bank entry and branching policy now exists, the continued imposition of various intermediation taxes as well as portfolio restricting measures contribute to high intermediation costs. These taxes reduce financial intermediation, which in turn, affects overall economic growth. It is therefore, important that they are eventually abolished. In view of their fiscal implications, however, a time-bound phased reduction program may be undertaken, taking into account the revenue (and monetary in the case of reserve requirements) implications of their reduction.

The Agri-Agra loan quota should be lifted. The agri requirement is redundant since the scope for profitable agricultural lending is substantial and generally complied with. On the other hand, the agra requirement is inappropriate and, in any case, does not result in increased lending for ARBs. Likewise, the mandatory requirement for small enterprises is sufficiently complied with and is unnecessary.[29] The phase-out or outright abolition of these implicit taxes requires an act of Congress. The same can be applied for the explicit GRT.

On the other hand, the abolition and/or further relaxation of the deposit retention scheme and the reduction of reserve requirement need only appropriate action by the Monetary Board.

Abandon the adoption of interest rate ceilings particularly on those programs not supported by any law. This will have the immediate impact of reducing financial losses of government-subsidized credit programs. In the long-run it will improve efficiency in the utilization of funds. Abandoning interest rate ceilings will require implementing financial institutions to lift the ceilings and non-financial institutions to transfer their program lending functions to GFIs. However, for those supported by law, an increased level of advocacy with Congress needs to be done.

Abandon direct lending by non-financial government agencies. Government line agencies do not have the capability to assess project viability, monitor loan usage, and collect loans at a level and margin adequate to cover both the administrative and high levels of default. Most of the lending programs directly implemented by government non-financial institutions are supported by laws and, therefore, would require reversal by Congress. Advocacy on the fiscal implications and the ineffectiveness of the direct lending approach are necessary.

Formulation of a legislative agenda that would define the needed reforms on financial laws and regulation affecting the

29 Information provided by Ma. Piedad Geron.

basic sectors. The agenda should identify specific legal issuances that need to be revoked and revised and propose alternative legal measures that will promote greater efficiency in the financial market. It should also review pending bills in Congress and identify those that thwart or promote the reforms. Coordination and advocacy with Congress and concerned sectors have to be undertaken to effectively push the agenda forward.

Review and rationalize various special funds earmarked for the basic sectors particularly those that source appropriations from the national budget. These fragmented special funds incur high administrative costs and, in many cases, are likely to duplicate each other. Rationalization of these funds would require a policy coordinating body such as the NCC to act as an overseer. It should be noted that many of these funds were created by law and therefore would require an act of Congress to effect their transfer, consolidation, and the like.

Rationalization of coordinating agencies created to oversee and rationalize credit programs. Currently, this is done in a sporadic fashion. What is perhaps needed is a single agency that is provided with sufficient police powers to ensure that credit programs are consistent with the government's overall policy objectives. Legislation may be needed in order to attain this goal. The transfer of the NCC secretariat to the DOF is a move in the right direction. However, further review needs to be done to rationalize the remaining coordinating bodies.

6
Recommendations for Further Study

To provide further bases for rationalization and policy formulation, the following studies are suggested:

Impact of the New Rural Bank Act. Given the relative importance of rural banks in the countryside, this study will focus on the impact of the law on the efficiency and financial performance of the rural banking system five years after its effectivity. Given that a more generous scheme was granted to ailing rural banks under the Act, the study will also look into the fiscal effects of the subsidies and assistance provided by the government. These include tax exemptions, conversion of past dues into government shares and concessional loans granted to rural banks. Government financial losses arising from these interventions will be documented. A similar study can also be done for the ***Thrift Banks Act*** and the ***Al-Amanah*** **Bank.** These banks have also received explicit and implicit subsidies, the extent of which in terms of fiscal magnitude is unclear. It would be interesting to look into the viability of the lending operations of these institutions given the privileges they enjoy from the government. Further, the viability of specialized government financial institutions is critical not only in terms of providing sustained financial services to the basic sectors, but also in terms of fiscal support. This is particularly true of the **LBP** under its new Charter, and the PCFC after two years of operation.

Regulatory environment of credit cooperatives and NGOs. A separate study for each type of institution will review and assess in detail existing regulatory environments covering these institutions. It will also develop a framework for regulation where the appropriate indicators for ensuring stability and sustainability are identified. The approriate institutional framework and regulatory approaches will also be developed in this study.

As pointed out in this review, there are still numerous direct lending programs of non-financial government agencies that were created by law. The ***cost and effectiveness*** of these programs need to be studied in greater detail. Overall, government costs and savings that may be realized through rationalization have to be determined. The programs' impact on the basic sector's access to financial services also needs to be documented. Corollarily, institutional changes required for the ***transfer of direct lending programs by non-financial agencies to financial institutions*** need to be investigated. In particular, the institutional and legal reforms associated with transferring programs have to be clearly outlined.

Subsidized interest rates are characteristic of many of the laws reviewed. Documenting the costs and inefficiencies of this policy would provide further basis for reforming the various credit programs created by law and institutions mandated to lend at concessionary rates.

Intermediation taxes repress the financial market. The extent to which these taxes distort the market needs to be documented. These taxes include mandatory allocations, deposit retention scheme, reserve requirements, gross receipts tax and the withholding tax on interest earnings. The costs and efficiency implications of these interventions have to be clearly determined.

Tables and Figures

Figure 1
General Framework

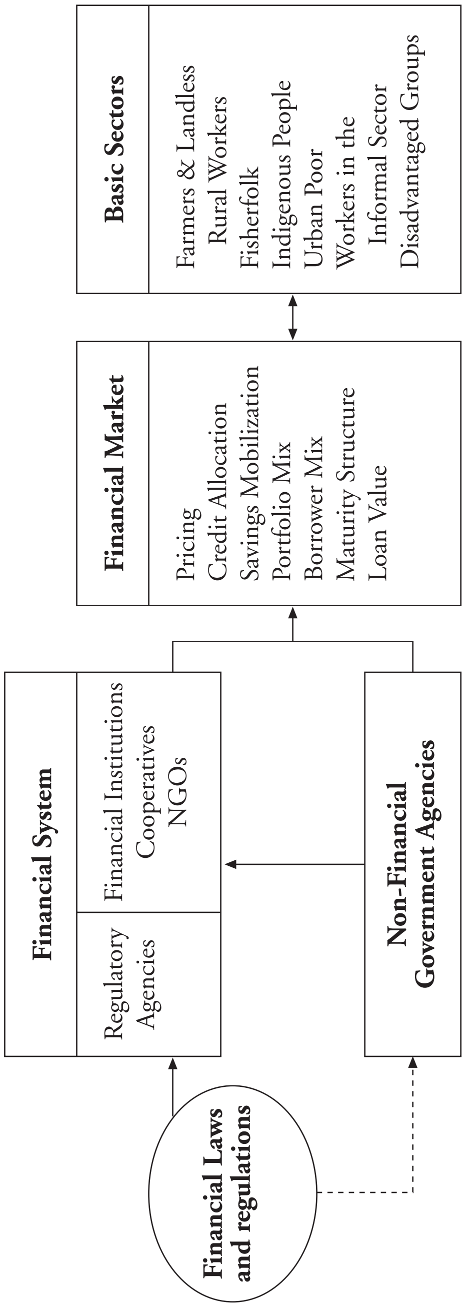

Table 1

Reserve Requirementson Deposit Liabilities, By Type of Bank

1993 to 1997 (as of End of Period Indicated)

	1993	1994	1995	1996	1997*
Commercial Banks					
Demenad Deposits	22%	19%	15%	15%	14%
Savings Deposits	22%	19%	15%	15%	14%
Time Deposits	22%	19%	15%	15%	14%
NOW Accounts	22%	19%	15%	15%	14%
Thrift Banks					
Demenad Deposits	22%	19%	15%	15%	14%
Savings Deposits	19%	16%	13%	13%	12%
Time Deposits	19%	16%	13%	13%	12%
NOW Accounts	22%	19%	15%	15%	14%
Rural Banks					
Demenad Deposits	22%	19%	15%	15%	14%
Savings Deposits	14%	11%	7%	7%	6%
Time Deposits	14%	11%	7%	7%	6%
NOW Accounts	22%	19%	15%	15%	14%

* *required reserves until June 1997, effective July 1997, required reserves will be reduced by one percentage point*
Source: CB Annual Report; CB Circulars

Table 2
Cost Of Credit Delivery on Agrarian Sector Lending of LBP Based on Internally-generated Funds

Effective Cost of Deposit (Range)	4.0	8.6	13.2	17.8
Loan Loss Provision	5.6	5.6	5.6	5.6
General Administrative Expenses	5.4	5.4	5.4	5.4
TOTAL COST (Break-even)	15.0	19.6	24.2	28.8

Source: LBP

Table 3
Cost Of Credit Delivery on Agrarian Sector Lending of LBP Foreign Funds (In Percent)

Item	On Rice And Corn Production Loans	On Other Production Loans And Other Projects
Cost of Funds	10.10 - 11.70	10.10 - 11.70
Insurance	2	
Loan Loss Provision	5.6	5.6
General and Administrative Expenses	5.4	5.4
TOTAL COST	23.1 - 24.7	21.1 - 22.7

Source: LBP

Table 4

Number and Distribution of Banking Offices in Metro Manila and Outside Manila

		Outside Metro Manila			Metro Manila			
Bank Type	**Year**	**No.**	**% Share**	**% to Total**	**No.**	**% Share**	**% to Total**	**TOTAL**
KBs	1986	903	36.2	52.1	830	76.2	47.9	1,733
	1989	901	36.7	51.7	841	75.8	48.3	1,742
	1993	1,235	42.5	52.0	1,142	79.5	48.0	2,377
TBs	1986	429	17.2	64.5	236	21.7	35.5	665
	1989	432	17.6	64.0	243	21.9	36.0	675
	1993	421	14.5	62.8	249	17.3	37.2	670
RBs	1986	1,065	42.7	98.3	18	1.7	1.7	1,083
	1989	1,025	41.8	98.3	18	1.6	1.7	1,043
	1993	1,083	37.3	98.5	16	1.1	1.5	1,099
SGBs	1986	95	3.8	95.0	5	0.5	5.0	100
	1989	97	4.0	92.4	8	0.7	7.6	105
	1993	168	5.8	85.3	29	2.0	14.7	197
ALL	1986	2,492	100.0	69.6	1,089	100.0	30.4	3,581
	1989	2,455	100.0	68.9	1,110	100.0	31.1	3,565
	1993	2,907	100.0	66.9	1,436	100.0	33.1	4,343

Source: Bangko Sentral ng Pilipinas, Factbook, various years.

Table 5
Density Ratios: Total Number of Banking Offices to Total Municipalities and Cities Per Region

	Region	1977	1980	1983	1986	1989	1993	1994
I	Ilocos Region	1.3	1.6	1.7	1.5	1.5	2.1	2.2
II	Cagayan Valley	0.7	1.0	1.0	0.9	0.9	1.4	1.6
III	Central Luzon	2.8	3.3	3.4	3.3	3.41	3.9	4.3
IV	Metro Manila	41.4	54.3	69.8	64.1	65.3	87.8	99.2
IV-A	Southern Tagalog	1.7	2.2	2.4	2.3	2.4	3.3	3.5
V	Bicol Region	1	1.4	1.4	1.3	1.2	1.4	1.4
VI	Western Visayas	1.7	2.0	2.1	2.0	1.9	2.4	2.5
VII	Central Visayas	1.2	1.6	1.8	1.6	1.6	2.3	2.5
VIII	Eastern Visayas	0.5	0.7	0.7	0.6	0.6	0.7	0.6
IX	Western Mindanao	0.6	0.8	0.7	0.7	0.7	1.1	1.1
X	Northern Mindanao	1.0	1.3	1.4	1.3	1.3	1.5	1.6
XI	Southern Mindanao	1.9	2.3	2.2	2.1	2.1	2.5	2.6
XII	Central Mindanao	0.7	0.8	0.7	0.8	0.8	1.2	1.4
	CAR						0.8	0.9
	ARMM						0.5	0.5

Source: Bangko Sentral ng Pilipinas, Factbook
Lamberte (1995)

Table 6
Flow of Loanable Funds*
1972 - 1995

	Ratio (%)
1972	26.3
1973	29.4
1974	25.6
1975	25.2
1976	26.5
1977	28.5
1978	29.2
1979	26.4
1980	25.6
1981	26.9
1982	28.0
1983	29.4
1984	22.4
1985	21.7
1986	22.5
1987	22.5
1988	24.0
1989	26.3
1990	26.6
1991	27.9
1992	28.5
1993	32.6
1994	35.9
1995	39.9
Average 1972-1980	27.0
Average 1981-1991	25.3
Average 1992-1995	34.2

** M3/Nominal GDP*
Sources: Selected Philippine Economic Indicators (June 1996)
NEDA Philippine Statistical Yearbook
Central Bank Annual Report

Table 7

Savings Deposit Rate, Loan Rate and Gross Spread, 1992 to 1994

(in % per annum)

		Savings Deposit Rate	Interest Rate on Secured Loans	Gross Spread
1992	**Jan**	5.013	23.035	18.022
	Feb	9.840	23.257	13.417
	Mar	9.879	21.694	11.815
	Apr	9.874	21.418	11.544
	May	9.456	18.931	9.475
	Jun	8.905	20.382	11.477
	Jul	8.759	19.769	11.010
	Aug	9.260	20.778	11.518
	Sep	8.809	19.386	10.577
	Oct	9.464	18.419	8.955
	Nov	9.232	16.832	7.600
	Dec	9.455	16.383	6.928
	Ave	8.996	20.024	11.028
1993	**Feb**	10.168	15.775	5.607
1994	**Feb**	8.741	14.687	5.946
	Mar	8.852	16.273	7.421
	Oct	6.302	13.902	7.600
	Dec	7.006	13.392	6.386

Source: CB Review

Annexes

Annex A
Summary of Financial Laws and Regulations Affecting the Provision of Financial Services to the Basic Sectors: Financial Institutions

Date	Law/Regulation	Description
	<u>Republic Acts</u>	
June 15, 1948	RA 265, as amended *An Act Establishing the Central Bank of the Philippines*	Provides the Central Bank with authority to oversee the entire financial and credit system.
July 14, 1948	RA 337, as amended *The General Banking Act*	Only entities authorized by the Monetary Board of the Central Bank may engage in lending through the receipt of deposits of any kind (Sec. 2).
June 22, 1963	RA 3765 *An Act to Require the Disclosure of Finance Charges in Connection with Extensions of Credit or Truth in Lending Act*	Mandates any credit institution to furnish each person to whom credit is extended the true cost of credit inclusive of all finance charges.
June 22, 1963	RA 3779, as amended *An Act to Provide for the Regulation of Organization and Operations of Savings and Loan Associations, or the Savings and Loan Association Act*	Regulates and supervises savings and loans associations for purposes of sound, stable, and efficient operation; encourages industry, frugality and accumulation of savings among the public and the members of savings and loan associations
June 22, 1963	RA 3591 *Philippine Deposit Insurance Act*	Creation of a Philippine Deposit Insurance Corporation to insure the deposits of all banks entitled to the benefits of insurance
June 19, 1964	RA 4093, as amended *Private Development Banks' Act*	Establishment of a system of private development banks which will promote agriculture and industry

Area of Financial Intermediation Affected	Targeted Sector	Impact/Implications
Supervision and regulation of the financial and credit system. Monetary and financial policy.	All sectors	Maintains internal monetary and external stability; Fosters monetary, credit and exchange conditions conducive to a balanced and sustainable growth of the economy
Savings mobilization and lending operation	Across sectors	Constrains non-formal financial institutions (e.g., NGOs) from mobilizing savings
Transparency in credit pricing	Across sectors	Greater transparency in the pricing of credit
Savings and loan facilities.	All sectors	Promotion of savings; Access to financial services for small borrowers/producers; Lower borrower transaction cost; Reduction of informational problems; Timeliness of loans
Deposit insurance	All sectors	Insures deposits and encourages more savings for economic development and the building of a more stable and progressive banking system
Availability of medium and long term credit facilities	All sectors	Increases the availability of term credit facilities to industry & agriculture

Annex A cont.

Date	Law/Regulation	Description
Aug 4, 1969	RA 5980, as amended *Financing Company Act*	Regulation of financing companies to place their operations on sound, stable and efficient basis
July 10, 1988	RA 6657 *Comprehensive Agrarian Reform Law*	Extends concessional and collateral-free credit to small landowners, farmers and farmers' organizations for agro-industrialization (Sec. 35.5) Promotes, develops and extends financial assistance to small and medium-scale industries in agrarian reform areas (Sec. 35.6) LBP to act as the financial intermediary of the CARP and prioritize the social objectives of the CARP (Sec. 64) Non-transferability of land acquired by beneficiaries except to the state or their heirs, or to other beneficiares after ten years (Sec. 27) PARC to ensure that farmer-beneficiaries are provided liberalized terms on credit facilities and production loans (Sec. 37) Transfer of the BKKK to the LBP (Sec. 37) including all existing funds
Jan. 26, 1990	RA 6848 *Charter of Al-Amanah Islamic Investment Bank*	The bank will perform banking, financing and investment operations and establish and participate in agricultural, commercial and industrial ventures based on the Islamic concept of banking in the Autonomous Region (Sec.3) Transactions related to the conduct of business of the bank are exempted from all taxes under the National Internal Revenue Code (Sec. 37)
Mar 24, 1992	RA 7279 *An Act to Provide for a Comprehensive and Continuing Urban Development and Housing*	Grant of livelihood loans by government agencies to beneficiaries of the Socialized Housing Program Launches the Community Mortgage

Area of Financial Intermediation Affected	Targeted Sector	Impact/Implications
Availability of credit facilities to consumers and to industrial, commercial or agricultural enterprises	All sectors	Provision of financing facilities
Supply and demand of countryside credit Pricing of credit Formation of farmers' organizations and cooperatives Land collateral	Small landowners, farmers and farmers' organizations Small entrepreneurs in agrarian reform areas	May promote supply-led approach to credit Subsidized/ fixed interest rate distorts the credit market Increased growth of farmers' organizations/ cooperatives Pressure on LBP's financial operation Non-acceptability to banks of land acquired due non-transferability problem
Availability of banking services in the Autonomous Region Intermediation cost	Islam population in the Autonomous Region	Increased availability of banking services in the Autonomous Region Reduction in intermediation cost due to exemption from taxes Less diversification in portfolio & limited geographical outreach
Supply of credit for livelihood Supply of funds for housing of the urban poor	Urban poor	May promote a supply-led approach to credit Enhance access to housing finance

Annex A cont.

Date	Law/Regulation	Description
	Program, Establish the Mechanism for Its Implementation, and for other Purposes	Program (CMP) of the NHMFC to assist associations of underprivileged and homeless citizens to purchase lands under the concept of community ownership; Home Insurance Guaranty Corporation (HIGC) to design appropriate guarantee scheme to encourage FIs to go into direct lending for housing
Apr. 22, 1992	RA 7353 *An Act Providing for the Creation, Organization and Operation of Rural Banks, and for Other Purposes*	To promote rural finance, additional incentives were incorporated to encourage RBs to expand their operations and strengthen their financial conditions In granting loans, preference shall be given to farmers and merchants whose cash requirements are small Unrestricted branching rights
Apr 13, 1992	RA 7393 *Reorganizing the Quedan Guarantee Fund, renaming it as Quedan and Rural Credit Guarantee Corporation, Enlarging its Powers and Resources to Support Farmers and Rural Enterprises*	The Corporation to establish a credit-support mechanism for farmers, fishermen, rural workers, coops, retailers, wholesalers and primary processors of agricultural and aquatic commodities; implement a guarantee system for agri-aqua commodities; provide uniform negotiable quedan or warehouse receipt forms for quedan financing

Area of Financial Intermediation Affected	Targeted Sector	Impact/Implications
Guarantee for housing loans of the urban poor		Expansion of credit for housing of the urban poor
Financial services in the countryside Rehabilitation of distressed rural banks Intermediation cost	Farmers, fishermen, farm families, cooperatives and merchants	Increases the flow of credit to the countryside; Strengthens rural banks' financial condition due to the conversion of all supervised past due and restructured past due loans into preferred stocks of the rural bank issued in favor of the LBP, the DBP or any government financial institution; Allows RBs to foreclose RA 6675 morgaged lands leading to the acceptability of CARL-covered lands by RBs Government subscription is inconsistent with its privatization thrust Exempts RBs from payment of all taxes, fees and charges except corporate income tax & local taxes, thereby reducing intermediation cost
Availability of credit for farmers, fishermen, rural workers, cooperatives, retailers; Risks in lending	Farmers, rural workers, fisherfolk	Increased availability of credit for farmers and fishermen Reduction in risks to lending due to guarantee

Annex A cont.

Date	Law/Regulation	Description
Apr 13, 1992	RA 7400 *Major Amendments to the PDIC Charter (RA 3591)*	Expansion of PDIC's power in the exercise of its regulatory functions: • deposit insurance coverage raised to P100,000.00; • increased authorized capital to P3.0 billion; • increased assessment premium of insured banks; • mandatory role as receiver of closed banks
May 18, 1994	RA 7721 *An Act Liberalizing the Entry and Scope of Operations of Foreign Banks in the Philippines and for Other Purposes*	Encourages greater foreign participation through increased ownership in domestic banks by foreign banks and the entry of new foreign bank branches (Sec.1); Loans extended to finance educational institutions, cooperatives, hospitals and other medical services, socialized housing, and to local government units shall be considered compliance with P.D. 717 (Sec. 9)
June 14, 1994	RA 7653 *The New Central Bank Act*	Creates an independent and accountable body known as the Central Monetary Authority responsible for money, banking and credit. This body shall enjoy fiscal and administrative autonomy The Act includes the transfer of certain assets and liabilities from the old Central bank to the BSP
Feb. 23, 1995	RA 7900 *An Act to Promote the Production, Processing, and Distribution of High-Value Crops, Providing Funds Therefor and for Other Purposes*	Creation of a High-Value Crops Development Fund (HVCDF) with an initial amount of ₱1 billion to sourced from the CALF and to be managed by the LBP and DBP. Part of the fund shall be used for the establishment of low-cost credit Participating banks exempted from PD 717 provided they lend a minimum 5% of their loanable funds

Area of Financial Intermediation Affected	Targeted Sector	Impact/Implications
Deposit insurance Stability of the banking system	All sectors	Increased deposit insurance coverage; Encourages and facilitates the strengthening of banks; Cushions the adverse effects of bank closures
Bank competition Availability of banking services	Across sectors	Increase in the efficiency and availability of banking services Reduction in interest rates
Monetary, banking and financial policy and regulation.	All sectors	Allows greater flexibility and independence in the conduct of monetary policy Strengthens BSP financially
Supply of credit fund for high-value crops Intermediation cost Pricing of credit Credit guarantee	Upland dwellers and lowland tenants, indigenous and cultural communities, CARP beneficiairies, upland farm owners, farmers, farmers' organizations/ association/ cooperatives, community associations and farmworkers	Promotes supply-led approach to credit delivery Unsustainability of concessional interest rate Higher intermediation cost due to mandatory allocation Possible reduction in lending risks due to credit guarantee

Annex A cont.

Date	Law/Regulation	Description
		Crop insurance to cover high value crops. HVCDF to be loaned to farmers' organizations/ associations/ cooperatives composed of but not limited to CARP beneficiairies. QUEDANCOR to provide credit guarantee.
Feb. 23, 1995	RA 7905 *An Act to Strengthen the Implementation of the Comprehensive Agrarian Reform Program, and for Other Purposes*	Creation of a guarantee fund for agricultural landowners that will enhance the collateral value of agricultural lands that are affected by their coverage under the agrarian reform program
Feb. 23, 1995	RA 7906 *An Act Providing for the Regulation of the Organization and Operations of Thrift Banks, and for Other Purposes*	Establishment of a thrift banking system which will promote agriculture and industry and provide easy access to medium and long-term credit facilities at reasonable cost; Encourage the accumulation of savings from the public; Equitable preferential terms on reserve requirements over those imposed on KBs; Unrestricted branching rights within the region; Exemption from payment of all taxes except corporate income taxes, fees and local taxes for a period of 5 years.
Feb. 25, 1995	RA 7907 *An Act Amending RA 3844, as amended, otherwise known as the "Code of Agrarian Reform in the Philippines"*	Amends the LBP Charter. Among others the amendents include; • strengthening the capital base of the bank by establishing a national marketing umbrella for farmers and fisheries cooperatives to attract massive capital formation from savings deposits of cooperatives nationwide; • the PARC shall provide funds from Agrarian Reform Fund or other unappropriated funds of the national

Area of Financial Intermediation Affected	Targeted Sector	Impact/Implications
Guarantee Flow of credit to agrarian reform areas	Agricultural landowners under the agrarian reform program	Guarantee will likely increase the flow of credit to agrarian reform areas Reduction in the risks involved in lending to agrarian reform beneficiaries
Savings mobilization; Medium and long term loans; Intermediation cost	Across sectors	Promotion of savings mobilization; Availability of financing for medium and long term credit needs; Reduction in intermediation cost due to exemption from taxes and preferential terms on reserve requirements; Enhances the efficiency and sustainability of thrift banking operations
Savings mobilization Financial viability of LBP	Agrarian reform beneficiaries; farmers and fisheries cooperatives	Promotion of savings mobilization nationwide Financial strengthening of LBP Expansion of outreach

Annex A cont.

Date	Law/Regulation	Description
		treasury sufficient to pay all maturing bonds, debentures and other obligations incurred as compensation to landowners; • at least 60% of proceeds from the Asset Privatization Trust shall be transferred to LBP for payment of agricultural lands
Dec. 29, 1995	RA 8175 *Amending PD 1467 or the Philippine Crop Insurance Corporation (PCIC) Charter to Make the Crop Insurance System More Stable and More Beneficial to the Farmers and for the National Economy*	Increased capitalization of PCIC Expanded coverage of agricultural insurance to include other crops such as coconut, coffee and pineapple and non-crop agricultural assets such as machineries, equipment, transport facilities and other related infrastructure Creation of a State Reserve Fund Allows PCIC to undertake reinsurance
	<u>Presidential Decrees</u>	
Jan. 29, 1973	PD 114 *Pawnshop Regulation Act*	Regulation, establishment and operation of pawnshops
May 29, 1975	PD 717 *Providing an Agrarian Reform Credit Financing System for Agrarian Reform Beneficiaries Through Banking Institutions*	Requires all banks to utilize 25% of their loanable funds for agricultural lending, i.e., 15% for agricultural credit and 10% for agrarian reform beneficiaries
Apr 3, 1980	PD 1688 Authorizing Banks to Invest in the Equity of Venture Capital Corporations Organized to *Assist Small and Medium-Scale Enterprises*	Allows banks with prior approval of the Monetary Board to acquire a majority of the equity of a venture capital corporation organized to assist small and medium scale enterprises in the form of equity financing

Area of Financial Intermediation Affected	Targeted Sector	Impact/Implications
Agricultural insurance Risks in lending	Farmers, rural workers, fisherfolk	Expands coverage of agricultural insurance beneficial to farmers, rural workers and fisherfolks An agricultural insurance which is more cost-effective and affordable to farmers Risk minimization through portfolio and asset diversification.
Credit for small borrowers	All sectors	Access to credit for small borrowers unserved by banks and other financial institutions
Credit allocation; Intermediation cost	Agrarian reform beneficiaries: tillers, tenant farmers, settlers, agricultural lessees, amortizing owners, owner-cultivators, farmers cooperatives and compact farms	Increase in intermediation Cost Penalizes the non-agriculture sector by imposing fixed allocation for agriculture on banks' loanable funds Restricts banks' efficient portfolio management Psuedo compliance among banks
Equity financing for venture capital corporations organized to assist small and medium scale enterprises	Across sectors involved in small and medium enterprises	Financial strengthening of venture capital corporations assisting small and medium scale enterprises through provision of capital funds from banks

Annex A cont.

Date	Law/Regulation	Description
	Letter of Instruction	
Apr 12, 1983	LOI No. 1308	Establishes the KKK Guarantee Fund as a special account in the CB to guarantee small and medium sized KKK loans released through duly accredited banks Initial funding to come from the Economic Support Fund The Fund evolved into the GFSME
	Executive Orders	
Dec. 3, 1986	EO 80 *Providing for the 1986 Revised Charter of the Philippine National Bank*	The bank shall give preference to loans for agriculture and small and medium-scale commercial and industrial enterprises, particularly in the countryside (Sec. 4) Transfer of assets and liabilites to the national government to rehabilitate the bank
Dec. 3, 1986	EO 81 *Providing for the 1986 Revised Charter of the Development Bank of the Philippines*	The bank shall provide banking services, principally to service the medium and long term needs of agricultural and industrial enterprises, particularly in the countryside and preferably for small- and medium-sized enterprises (Sec. 2) Rehabilitation of the bank through transfer of assets and liabilities to the national government (Sec. 30)
July 22, 1987	EO 229 *Providing the Mechanisms for the Implementation of the Comprehensive Agrarian Reform Program*	Upon transfer, each beneficiary who actually farms his land shall be eligible for a production loan to finance one crop cycle under terms and conditions to be determined by the LBP on a case to case basis, renewable upon repayment (Sec. 13)
June 9, 1988	EO 327 *Implementing Certain Provisions of EO No. 715 (1981), EO238 (1987), EO314 (1987) and for Other Purposes*	BKKK was subsumed under the National Livelihood Support Fund (NLSF). The new mandate provided for a fund delivery system and organizational machinery for the provision of socialized livelihood credit as well as the collection

Area of Financial Intermediation Affected	Targeted Sector	Impact/Implications
Guarantee	Across sectors, particularly those engaged in small and medium enterprises	Increases the flow of credit to SMEs due to the guarantee Reductions in lending risks to SMEs
Availability of credit to the countryside Financial viability of the bank	Agriculture and small and medium-scale commercial and industrial enterprises in the countryside	Increase in the availability of credit facility in the countryside. Stronger and more viable bank to service financing needs in the countryside
Availability of banking services for longer-term credit needs in the countryside.	Agricultural and industrial enterprises in the countryside, preferably small- and medium-sized enterprises	Increase in the availability of medium and long term credit facilities in the countryside Stronger and more viable Bank to service the MLT needs in the countryside
Demand for and supply of production loans	Agrarian reform beneficiaries	Expansion of loans for crop production
Credit and institution building funds for disadvantaged sectors	Disadvantaged sectors, agrarian reform beneficiaries	Provision of funds for livelihood credit and institution building May promote supply-led approach to credit

Annex A cont.

Date	Law/Regulation	Description
		and consolidation of all KKK funds Funds shall be made available on "wholesale" basis for livelihood programs of line gov't agencies, PVOs or NGOs.
	Administrative Orders	
Aug. 6, 1993	AO 75 *Directing the Transfer and Attachment of the BKKK Secretariat to the LBP, Including all its Applicable and Existing Funds, Personnel, Properties, Equipment and Record, In Accordance with Sec. 37 of RA 6675 (1988).*	Effected the final transfer of all NLSF assets, funds, personnel and equipment under LBP supervision
Dec. 7, 1994	AO 162 *Directing the LBP to Increase Its Loans/ Financial Assistance to Small Farmers and Enhance its Institutional Training Programs of Farmers cooperatives, as a Safety Net measure for the Implementation of the GATT-UR.*	LBP provided with low-cost revolving funds from the GATT-support funds for on-lending to the agriculture sector; LBP exempted from the requirement to rechannel investible funds to the Treasury and the BSP
	Memorandum Orders	
Feb. 9, 1995	M.O. 262 *Directing the Presidential Commission to Fight Poverty and the LBP to review the Legal Requirements for the Creation of the People's Credit and Finance Corporation (PCFC)*	Creation of PCFC with capitalization from the National Livelihood Support Fund (NLSF)
	Central Bank Circulars	
July 13, 1973	Circular No. 374 *Rules and Regulations for Pawnshops*	Empower pawnshops to engage in the business of lending on the security of personal property

Area of Financial Intermediation Affected	Targeted Sector	Impact/Implications
Funds for livelihood credit and institution building	Disadvantaged sectors, agrarian reform beneficiaries	Transfer of NLSF to LBP provide proper fund management for support services to farmers/agrarian reform beneficiaries
Supply of funds for the agriculture sector	Farmers, fisherfolk, agrarian reform beneficiaries	Expand LBP's fund base for farmers and fishermen Fiscal burden since LBP will source funds from the GAA and not from internally-mobilized funds
Supply of credit for the poor Funds for institution and capability building	Across sectors	Expansion of credit to the bottom poor Strengthening program partners and targeted clients
Availability of credit for small borrowers Regulation of pawnshops	All sectors	Access to credit for small borrowers unserved by banks and other institutions; Promotes the sound and stable operation of pawnshops

Annex A cont.

Date	Law/Regulation	Description
Dec. 31, 1996	BSP Circular No. 119 *Lowering Reserve Requirements for Rural Banks, Thrift Banks, Commercial Banks and Non-Bank Financial Intermediaries*	Lowers required reserves against demand deposits, NOW accounts of RBs to 14% effective 1/3/97 to 13% effective 7/4/97 and against savings and time deposits to 6% effective 1/3/97 and to 5% effective 7/4/97
Feb. 8, 1994	BSP Circular No. 12 *Mandatory Portfolio Allocation for Small Enterprises Credit*	Requires all lending institutions set aside a portion of total loan portfolio based on their consolidated Statement of Condition/Balance Sheet at the end of the previous quarter (5% by 12/31/91, 10% by 12/31/92 thru 12/31/95 and 5% by 12/31/96 to 0% by 12/31
May 18, 1994	BSP Circular No. 24 *Deposit Retention Policy for Rural Banks*	At least 75% total deposits, net of required reserves against deposit liabilities & total amount of cash in vault, accumulated by branches, agencies, extension offices, units and/or head offices of RBs, in a particular regional grouping outside NCR shall be invested to develop
Aug. 2, 1994	BSP Circular No. 38 *Lower Reserve Requirements*	Reduction of reserve requirement by 3% points on all types of deposits and deposit substitutes of commercial banks and non-banks with quasi-banking functions and certain types of deposits and deposit substitutes of thrift banks and rural banks
Oct. 14, 1994	BSP Circular No. 51 *Rules and Regulations Implementing RA 7721 "An Act Liberalizing the Entry and Scope of Operations of Foreign Banks in the Philippines"*	Liberalization of the entry of foreign banks into the Philippines to attract foreign investments, enhance the efficiency of the domestic financial system and make the Philippine banking system more globally competitive
Nov. 8, 1994	BSP Circular No. 52 *Provisions Governing the Rediscounting of Eligible Papers under the Rediscount Window of BSP*	80% of the loan value with rediscount of 1% below 91day treasury bill revised every 3 months for papers covering agricultural products, cottage & small industry credits, general purpose working capital financing & other short-term credits. No ceiling on lending rates banks charge on rediscount

Area of Financial Intermediation Affected	Targeted Sector	Impact/Implications
Intermediation cost	Across sectors	Lowers cost of intermediation; Expands/increases resources for lending
Credit allocation; Intermediation cost	Rural/small-scale entrepreneurs	Increase in cost of intermediation; Retricts banks' efficient portfolio management
Intermediation cost; Portfolio management and fund allocation	Across sectors	Portfolio management is not optimized; Retricts banks efficient portfolio management; Higher intermediation cost
Intermediation cost	Across sectors	Lower cost of intermediation, Expand/increase resources for lending
Availability of banking services; Pricing of credit	Across sectors.	Increased availability and improvement in the delivery of financial services, Reduction in interest rates
Intermediation cost; Pricing of credit	Farmers, fisherfolk, rural entrepreneurs	Increases available credit funds for the rural sector; Allows market forces to determine lending rates to end-users

Annex A cont.

Date	Law/Regulation	Description
Dec. 29, 1994	BSP Circular No. 58 *Guidelines In Connection With the Grant by Land Bank of the Philippines and the Development Bank of the Philippines or any GOCC/GFI of a Loan to a Rural Bank*	Granting of loans by LBP, DBP or any GOCC/GFI to a rural bank are subject to issuance of certification by the Monetary Board, a set of qualification standards with regards to capital to risk asset ratio, past due ratio and allowance for probable losses
June 2, 1995	BSP Circular No. 76 *Guidelines Governing Rural Bank's Application for a Rediscount or Loan*	Sets the following limit on rediscounts or loans rural banks may avail of from the BSP: P900,000 or rural banks with A or B credit rating; P700,000 for rural banks with C rating; and P400,000 for rural banks with D rating and those which are newly established
Feb. 9, 1987	CB Circular No. 1133 *Exemptions From the Reserve Requirements*	Exempts from legal reserve requirement special time deposits and deposit substitutes arising from the lending operations of IGLF and ALF
April 24, 1987	CB Circular No. 1143 *Guidelines Governing the Rehabilitation of Rural Banks*	Sets the guidelines for the rehabilitation of RBs through a CBU consisting of a prerequisite fresh capital infusion and a subsequent conversion and/or plan of payment of all arrearages with the CB which are past due and unpaid as of 12/31/86
Aug. 27, 1987	CB Circular No. 1151 *Implementing Guidelines Regarding the ALF Facilities*	Provides that ALF facility may be extended to finance both seasonal prod credit & medium & long-term sub-loans for fixed assets & permanent working capital (except for acquisition of land)
Oct. 28, 1988	CB Circular No. 1188 *Conditions for Establishment/ Opening of Branches and Other Banking Offices of All Banks*	Eliminates the prerequisite investment in government securities for purposes of establishing/opening branches and other banking offices by banks
Jan. 31, 1990	CB Circular No. 1226 *Deposit Retention Policy for KBs and TBs*	Requires at least 75% of total deposits of KBs and TBs, net of required reserves against deposit liabilities and total amount in vault accumulated in a particular regional grouping outside

Area of Financial Intermediation Affected	Targeted Sector	Impact/Implications
Viability of RBs; Fund sourcing	Rural borrowers, farmers, fisherfolk, agrarian reform beneficiaries, rural entrepreneurs	Expands fund base of RBs; Regulates loans to RBs
Viability of rural banks; Fund Sourcing	Rural borrowers: farmers, fisherfolk, agrarian reform beneficiaries and other rural workers	Regulates availment of rediscount facilities and loans to rural banks; Expands fund base of rural banks
Intermediation cost	Across sectors	Lowers cost of intermediation; Increases available funds for lending
Viability of rural banks	Rural borrowers; farmers, fisherfolk, agrarian reform beneficiaries, rural workers/entrepreneurs	Enhances viability of rural banks
Credit access; Viability of special financing programs	Farmers, fisherfolk, agrarian reform beneficiaries, rural workers/entrepreneurs	Increases available credit funds for the rural sector; Allows market forces to determine interest rates hence, enhancing lending
Availability of banking services	Across sectors	Increases available banking services for the rural sector
Intermediation cost; Portfolio management and fund allocation	Across sectors	Portfolio management is not optimized; Retricts banks efficient portfolio management;

Annex A cont.

Date	Law/Regulation	Description
		NCR, to be invested therein as a means to develop the region
June 29, 1990	CB Circular No. 1245 *Requirements for Credit Accomodation of Unsecured Loans*	Provides the following requirements for credit accomodation of unsecured loans for KBs, TBs and NBFIs: photocopy of the borrower's/co-maker's ITR and copy of the borrower's balance sheet
Oct. 12, 1990	CB Circular No. 1255 *Penalties on Past Due Loans*	Allows RBs to impose penalty on past due loans of their borrowers provided the latter's failure to pay their loans on time is due to inexcusable neglect and that the penalty shall be reasonable and unconscionable
Nov. 8, 1990	CB Circular No. 1264 *Guidelines Governing Organization of Cooperative Banks*	Sets revised guidelines for the organization of cooperative banks
March 5, 1991	CB Circular No. 1276 *Exemptions From the Reserve Requirements*	Exempts from the reserve requirements special time deposits of financial institutions under the special financing programs of the government and/or international financial institutions being or previously administered by the CB
June 17, 1991	CB Circular No. 1290 *Conditions for the Processing/ Approval of Bank Application to Qualify for Branching Privilege, Permit to Operate New Banking Offices and To Avail of CB Credit Facilities and Special Financing Programs*	Deletes the requirement of compliance with the loans to deposit ratio for 4 consecutive quarters to a) qualify for branching privilege; b) permit to operate new banking offices and to avail of CB credit facilities and special financing programs
Oct. 15, 1991	CB Circular No. 1312 *Guidelines Governing Mergers and Consolidation of Banks and Other Financial Intermediaries*	Lists the incentives for mergers and consolidations among banks and other financial intermediaries, which include condonation of liquidated damages and/ or penalties on loan arrearages to the CB
Oct. 29, 1991	CB Circular No. 1315 *Terms of Reference for the Implementation of the CFIEP*	Sets the terms of reference for the implementation of the CFIEP which aims to raise the capital base, reduce the

Area of Financial Intermediation Affected	Targeted Sector	Impact/Implications
		Higher intermediation cost
Credit access	Farmers, fisherfolk, agrarian reform beneficiaries, rural workers/entrepreneurs	Enhances access to credit of semi and non-bankable
Repayment performance of borrowers	Rural borrowers: farmers, fisherfolk, agrarian reform beneficiaries, rural workers/entrepreneurs	Discourages late payments and loan defaults
Availability of banking services	Rural borrowers: farmers, fisherfolk, agrarian reform beneficiaries, rural workers/entrepreneurs	Increases available financial services for the rural sector
Intermediation cost	Across sectors	Lowers cost of intemediation; Increases available fund for lending
Availability of banking services; Fund sourcing	Across sectors	Increases available banking services for the rural sector; Includes and increase in the volume of loans
Viability of financial institutions	Across sectors	Improves viability of financial institutions; Enhances delivery of financial services
Viability of rural financial institutions	Rural borrowers: farmers, fisherfolk, agrarian reform	Improves viability of RFIs such as rural banks and thrift banks;

Annex A cont.

Date	Law/Regulation	Description
		debt burden and improve the long-term viability of countryside financial institutions
July 24, 1992	CB Circular No. 1349 *Incentives in Bank Branching*	Allows banks to establish one branch in areas of its choice without bidding for every 3 branches that a bank has established in 5th and lower class municipalities where there are less than 4 banks.
Nov. 26, 1992	CB Circular No. 1369 *Guidelines Governing the Implementation of the Rural Banks Act of 1992.*	Covers exemption from ownership ceiling, settlement or liquidation of arrearages w/ the CB, acceptance of demand and government deposits, equity investments in allied undertakings and exemption from the 15% ceiling on deposits maintained with depositor
Feb. 26, 1993	CB Circular No. 1385 *Compliance With the Mandatory Credit Allocation to Small Enterprises*	Includes equity investments by member banks in, and loans by member banks to, the BAP Credit Guaranty Corp., provided that the same will be allowed only in 1993 and that BCGC will extend its loan facilities only to small enterprises
March 3, 1993	CB Circular No. 1386 *Liquidity Floor Requirement on Government Deposits/ Funds*	Obliges authorized government depository banks and authorized private banks including government-acquired banks with special depository privileges to maintain a 50% liquidity floor with respect to deposits of, borrowings from, and all other liabilities to the Government
Oct. 7, 1993	CB Circular No. 8 *Sanctions on Reserve Deficiencies*	Imposes a penalty on banks with reserve position below the required minimum; the penalty is equivalent to 1/10 of 1% per day or the prevailing 91-day T-Bill rate plus 3 percentage points on the amount of the deficiency
April 4, 1994	Circular-Letter: *Declaration of Period April 24 to 30 as Credit Consciousness Week per Presidential Proclamation No. 1827 Dated March 30,1979*	Requiring all banking institutions to undertake supportive publicity and promotional activities, putting up of window or counter displays, streamers and placements in observance of the Credit Consciousness Week

Area of Financial Intermediation Affected	Targeted Sector	Impact/Implications
	beneficiaries and other rural workers/ entrepreneurs	Enhances delivery of financial services
Availability of banking services	Farmers, fisherfolk, rural workers, workers in the informal sector	Increased availability and improvement in the delivery of financial services in the countryside
Viability of RBs.	Rural borrowers, farmers, fisherfolk, agrarian reform beneficiaries, rural entrepreneurs	Enhances viability of RBs
Credit allocation; Intermediation cost	Rural/small-scale entrepreneurs	Increase in cost of intermediation; Retricts banks' efficient portfolio management
Intermediation cost	Across sectors.	Increases cost of intermediation; Contacts available for lending
Intermediation cost	Across sectors	Increases cost of intermediation
Borrower bankability and creditworthiness	Across sectors	Enhances public awareness of the role of credit and creditworthiness

Annex A cont.

Date	Law/Regulation	Description
May 26, 1994	Circular-Letter: *Declaration of Period June 30 to July 6, 1994, and Every Year Thereafter as Savings Consciousness Week Per Presidential Proclamation No. 380 Dated May 15, 1994*	Requiring all banking institutions to undertake relevant publicity and attention-generating activities, such as raffles, distribution of give-aways, putting up of window displays, treamers, ads and the use of other promotional devices
	Internal Revenue Code: *Section 261 Tax on Finance Companies*	Imposes a tax of 15% on the gross receipts derived by all finance companies as well as other financial intermediaries not performing quasi-banking functions doing business in the Philippines
	Internal Revenue Code: *Section 52E Withholding of Final Tax on Interest on Bank Deposits and Yield from Deposit Subs.*	Imposes 15% withholding tax on interest earned from savings deposits and 20% on interest earned from time deposits
12:00:00 AM	Local Government Code: *Tax on Finance Companies*	Imposes tax on banks and other financial institution at a rate not exceeding 50% of 1% on the gross receipts of the preceding calendar year
12:00:00 AM	National Revenue Code: *Withholding of Final Tax on Interest on Bank Deposits and Yield from Deposit Substitutes*	Imposes 20% withholding tax on interest earned from bank deposits
Jul. 10, 1988	RA 6657 *Comprehensive Agrarian Reform Law*	Extension to small landowners, farmers and farmers' organizations the necessary credit, like (concessional and collateral-free loans) for agro-industrialization based on social collaterals (guarantees of farmers' organization) (Sec. 35) Promoting, developing and extending financial assistance to small and medium-scale industries in agrarian reform areas (Sec. 35.6) LBP shall be the financial intermediary of the CARP and shall insure that the social objectives of the CARP shall enjoy

Area of Financial Intermediation Affected	Targeted Sector	Impact/Implications
Savings/deposit mobilization	Across sectors	Promotes savings mobilization and enhances sustainability of lending operations
Intermediation cost	Across sectors	Increases cost of intermediation
Intermediation cost; Deposit/Savings mobilization	Across sectors	Increases cost of intermediation; Discourages savings among households
Intermediation cost	Across sectors	Increases cost of intermediation
Intermediation cost; Deposit/Savings mobilization	Across sectors	Increases cost of intermediation; Discourages savings among households
Supply and demand of countryside credit; Pricing of credit; Formation of farmers' organizations and cooperatives; Land collateral	Small landowners, farmers and farmers' organizations; Small entreprenuers in agrarian reform areas	May promote supply led approach to credit; Subsidized/fixed interest rate distorts the credit market; Increased growth of farmers' organizations/coops; Pressure on LBP's financial operation; Non-acceptability to banks of land acquired due non-transferable

Annex A cont.

Date	Law/Regulation	Description
		preference among its priorities (Sec. 64) Non-transferability of land acquired by beneficiaires except to the state or their heirs, or to other beneficiares after ten years (Sec. 27) PARC shall ensure that farmer-beneficiaries are provided with liberalized terms on credit facilities and production loans (Sec. 37) Transfer of the BKKK to the LBP (Sec. 37) including all existing funds
Jan. 24, 1990	RA 6846 *An Act Creating the Abot-Kaya Pabahay Fund, Otherwise Known as the Social Housing Support Fund Act, and for Other Purposes*	Creates the Abot-Kaya Pabahay Fund to be used exclusively for low-cost housing by low-income families and for other purposes The National Home Mortgage and Finance Corporation (NHMFC) and the Home Insurance Guaranty Corporation (HIGC) are administering agencies and trustees of the Fund
July 1991	Section 1116 *Networth to Risk Assets Ratio of EKBs and KBs - Central Bank Manual of Regulations for Banks and Other Financial Intermediaries - Book I*	Sets the networth of a bank at not less than an amount equal to 10% of its risk asset to regulate EKBs' and KBs' capital adequacy position vs. risk assets
July 1991	Section 1269.1 *Rediscount Ceilings for EKBs and KBs - Central Bank Manual of Regulations for Banks and Other Financial Intermediaries - Book I*	Sets the rediscount ceiling of EKBs and KBs at 100% of their networth
July 1991	Section 1273 *Rediscounting of Specific Papers - Central Bank Manual of Regulations for Banks and Other Financial Intermediaries - Book I*	Allows KBs to avail of the rediscounting privilege of the CB, covering specific papers such as those pertaining to agrarian reform credit under PD 717

Area of Financial Intermediation Affected	Targeted Sector	Impact/Implications
Supply of funds for housing	Urban poor	Expansion of credit for social housing
Viability of EKBs and KBs	Across sectors	Regulates financial performance of EKBs and KBs; Enhances delivery of financial services
Fund availability	Across sectors	Increases available credit funds
Fund availability	Farmers, fisherfolk, agrarian reform beneficiaries, rural workers, workers in the informal sector, urban poor	Increases available credit funds

Annex A cont.

Date	Law/Regulation	Description
July 1991	Section 1303 *Interest and Other Charges for EKBs and KBs - Central Bank Manual of Regulations for Banks and Other Financial Intermediaries - Book I*	Imposes no ceiling on the interest rate of (including commissions, premiums, fees and other charges) of loans extended by EKBs/KBs, or forbearance of any money, goods or credits,regardless of maturity and whether secured or unsecured
July 1991	Section 1341.3 *Required/Mandatory Allocation for Agrarian Reform and Agricultural Credit - Central Bank Manual of Regulations for Banks and Other Financial Intermediaries - Book I*	Obliges each EKB/KB to set aside an amt equivalent to 25% of its loanable funds for agri. credit in general, of which an amount equivalent to at least 10% of the loanable funds shall be made available for agrarian reform credit.

Area of Financial Intermediation Affected	Targeted Sector	Impact/Implications
Pricing of credit	Across sectors	Increased efficiency in allocation of financial resources and improvement in the delivery of financial services
Credit allocation; Intermediation cost.	Agrarian reform benficiaries: tillers, tenant farmers, settlers, agricultural lessees, amortizing owners, owner cultivators, farmers cooperatives and compact farms.	Increases cost of intermediation; Penalizes the non-agri sector by imposing fixed allocation for agri on banks loanable funds; Retricts banks' efficient portfolio management; Pseudo compliance among banks

Annex B

Summary Of Laws And Regulations Affecting The Provision Of Financial Services To The Basic Sectors: Non-financial Government Agencies

Date	Law/Regulation	Description
	<u>**Republic Acts**</u>	
June 15, 1969	RA 5416 *An Act Providing for Comprehensive Social Services for Individuals and Groups in Need of Assistance Creating for this Purpose*	Allows DSWD to provide social welfare services designed to ameliorate the living conditions of distressed Filipinos. Among others, the DSWD is authorized to undertake income-producing projects
Aug. 22, 1991	RA 7111 *Overseas Workers' (OWI) Fund Act or An Act Establishing the Overseas Workers' Investment Fund to Provide Incentives to Overseas Workers, Reduce the Foreign Debt Burden, and for Other Purposes*	Creates the OWI Fund Board to encourage the greater remittance of earning of Filipino workers overseas and to safeguard and oversee the participation of said worker's remittances and savings in the Government's debt-reduction efforts and other productive undertakings Among others, the gains from the Fund shall be used for: housing program for overseas workers; credit facility for business enterprises and/or livelihood projects at concessional rates; health/ hospitalization insurance for the family of the worker
Oct. 10, 1991	RA 7160 *An Act Providing for a Local Government Code of 1991*	A local government may secure loans from any bank and lending institution against security of real estate or other acceptable assets for livelihood projects and other economic enterprises (Sec. 297)
Sept 24, 1992	RA 7637 *Mt. Pinatubo Assistance, Resettlement and Development Fund*	Appropriates P10 billion for the aid, relief, resettlement, rehabilitation and livelihood services for victims of the Mt. Pinatubo eruption Creates the Mt. Pinatubo Assistance, Resettlement and Development Commission primarily responsible for formulating policies and plans for services and infrastructure support for victims

Area of Financial Intermediation Affected	Targeted Sector	Impact/Implications
Pricing of credit resources; Delivery mechanism	Handicapped, youth, physical and mental disability, victims of natural calamities, cultural minorities, other socially disadvantaged groups	Granting of subsidized concessional loans; Promotes direct lending by non-financial gov't agency
Availability and pricing of credit facility	Overseas contract workers and their beneficiaries	Concessional interest rate undermines the sustainability of the credit facility
Supply and price of credit	Across sectors	May promote a supply led approach to credit; Direct lending
Funds for livelihood	Mt. Pinatubo eruption victims	Provides funds for livelihood projects and other support services; May promote "dole-out" syndrome in the long-run.

Annex B cont.

Date	Law/Regulation	Description
Feb. 20, 1995	RA 7882 *An Act Providing Assistance to Women Engaging in Micro and Cottage Business Enterprises, and for Other Purposes*	Provides women who have existing micro and cottage business with loans at prime interest rate or 12% per annum, whichever is lower, from any government financing institution; Mandates the Bureau of Small and Medium Business Development of the DTI to implement the Act; All GFIs shall earmark 5% of their loan portfolio for the implementation of the Act
	<u>Presidential Decrees</u>	
May 1, 1978	PD 1365 *Creating the "Rural Workers Office" in the Department of Labor and for Other Purposes*	Creates the Rural Workers Office in the Department of Labor with, among others, the following functions and powers: general supervision and control of the social amelioration fund in the sugar industry; to engage in income and employment generating projects
	<u>Executive Orders</u>	
Apr 13, 1987	EO 158 *Creating the "Tulong sa Tao Fund" and for Other Purposes*	Mandates the Department of Trade and Industry (DTI) to administer the Fund for purposes of self-employment assistance and subcontracting financing in the rural areas. The DTI also determines the conditions or availment
Apr 19, 1992	EO 515 *Transferring the Bagong Pagkain ng Bayan Program to the Technology Resource Center and Rationalizing its Mandate and Organization*	Bagong Pagkain ng Bayan shall serve as the institutional vehicle through which LGUs shall have access to facilities, resources, technical assistance, and investment support services - such as research and development - direct loans or guarantees on loans for agricultural and support projects
	<u>Administrative Orders</u>	
Sept. 8, 1994	AO 148 *Creating the Task Force on*	Main task of the task force is to review the existing credit for the poor

Area of Financial Intermediation Affected	Targeted Sector	Impact/Implications
Pricing/cost of credit; Credit allocation	Women engaged for at least one year in any micro and cottage business with daily inventory of no more P25,000 or any business equipment with book value of no more than P50,000	Unsustainability of interest rate ceiling; Interest rate ceiling will result in credit rationing; Mandatory credit allocation taxes the GFIs and therefore increases their cost of intermediation; Direct lending by non-fonancial gov't agency
Availability of credit through a livelihood program	Landless rural workers.	Allows a non-financial agency to go into direct lending through a livelihood program May promote a supply led approach to credit
Supply of credit for rural areas	Rural entreprenuers	Promotes the supply led approach to rural finance Direct lending by non-financial government agency
Lending and guarantee funds for LGUs	Across sectors, LGUs, NGOs	Provision of credit funds for employment generation and livelihood
Review of government credit programs	Across sectors	Possible rationalization of government credit programs

Annex B cont.

Date	Law/Regulation	Description
	Credit for the Poor of the Presidential Commission to Fight Poverty	programs and mechanisms of the Government with the view of rationalizing the Credit for the Poor Program and formulating a Master Plan for PCFC
	Cabinet Resolution	
Nov. 1988	Cabinet Resolution No. 29 *Guidelines for Credit Programs*	Policy guidelines for government-sponsored livelihood programs. Only DWSD was allowed to engage in direct lending activities
	Proclamations	
Sept. 8, 1994	Proclamation No. 466 *Authorizing the Task Force for Credit for the Poor, Action Arm of the Presidential Commission to Fight Poverty, to Conduct a Fund Campaign from Date Hereof to Sept. 7, 1995*	Authorizes the Task force for Credit For the Poor to conduct a fund campaign to establish a Trust Fund

Area of Financial Intermediation Affected	Targeted Sector	Impact/Implications
Direct lending by non-financial government agencies	Across sectors	Gives way to the creation of fragmented livelihood programs
Availability of financial resources for capability building and credit for the poor	Across sectors	Expand financial resources for credit for the poor May induce a supply led approach to credit.

Annex C
Summary of Financial Laws and Regulations Affecting the Provision of Financial Services to the Basic Sectors: Across Institutions

Date	Law/Regulation	Description
	<u>Republic Acts</u>	
Jan. 24, 1991	*RA 6977* *Magna Carta for Small Enterprises*	Creates the SMED Council primarily responsible for the promotion; growth and development of small and medium enterprises in the country. One of its specific functions is directing/assisting government agencies in the provision of concessional interest rates, lower financing fees, effective substitution of government guarantee cover on loans for the borrower's lack of collateral Creates SBGFC to provide various alternative modes of financing for small enterprises and to guarantee loans obtained by qualified borrowers Mandates all lending institutions to allocate a portion of their total loan portfolio for small enterprise credit
Apr 10, 1992	*RA 7368* *Countrywide Industrialization Act of 1992*	Provides financial assistance to every town and city not exceeding P30 million and P40 million respectively for the promotion of countryside industrialization Creates the Countrywide Industrialization Fund (CIF) as a source of financial assistance to eligible countrywide industrialization projects to be sourced from the national budget and supplemented by bilateral and multilateral sources Creates the Countrywide Industrialization Office (CIO) attached to the DTI The Executive Committee of the municipal, city and provincial development councils shall serve in the Local Countrywide Industrialization

Area of Financial Intermediation Affected	Targeted Sector	Impact/Implications
Interest rate Risks in lending Intermediation cost	Across sectors particularly those engaged in small and medium enterprise	Unsustainability of concessional interest rate Reduction in risk due to credit guarantee Higher intermediation cost due to mandatory allocation on banks' loanable portfolio
Funds for countryside credit Monitoring and evaluation of loans Interest rate	Rural workers	Promotes direct lending of non-GFI Interest rate ceiling will undermine the sustainability of the credit delivery scheme Credit decision and monitoring not performed by the bank will lead to high default rates

Annex C cont.

Date	Law/Regulation	Description
		Board. Among others, the Board shall be responsible for evaluation and approval of projects for funding Projects owned by cooperatives or NGOs are qualified Financial assistance from the CIF will be provided at soft or concessional terms. Interest rate shall not be more than 11%
June 4, 1992	*RA 7607* *An Act Providing a Magna Carta of Small Farmers*	Chapter VII mandates the following: Credit to farmers shall not exceed 75% of prevailing market rate p.a. inclusive of all service charges The DA through ACPC and other concerned agencies shall give subsidies for education and training of small farmers on credit awareness, loans acquisition, and loan repayment. It shall conduct an information drive that will promote the establishment of strong and viable farmers' organizations such as cooperatives, credit unions, rotating savings and credit associations and NGOs which play a major role in increasing small farmers' access to credit Expansion of loan guarantee coverage under the CALF to cover not only rice and corn but other crops, livestock, poultry, fishery and agro-forestry as well Conduct of special projects to promote innovative credit schemes Promote the development of farmers' organizations. Government shall subsidize costs of info dissemination, monitoring, training and registration An amount shall be earmarked for lending exclusively to farmers' cooperatives at subsidized interest rates All agricultural lending programs shall

Area of Financial Intermediation Affected	Targeted Sector	Impact/Implications
Interest rate; Institution building; Credit delivery system; Risks in lending; Fund management	Farmers and rural workers; Fisherfolk	Distortion in the credit market due to interest rate ceiling Promotes capacity building of farmers' organizations and cooperatives Promotes alternative credit delivery channels such as NGOs, credit unions, savings and loan associations, etc Reduction in agri lending due to guarantee More efficient management of agri credit programs

Annex C cont.

Date	Law/Regulation	Description
		be consolidated under the administration of the LBP Promotion of cooperative banks and growth of networks of cooperative banks
Feb. 12, 1997	*RA 8250* *General Appropriations Act, 1997*	Appropriates funds for the operation of the government of the Philippines for FY 1997 Provides funds for countrywide development projects; and poverty alleviation particularly in 5th and 6th class municipalities and cities in identified SRA convergence areas
	Executive Orders	
Dec. 24, 1986	*EO 113* *Establishing the Comprehensive Agricultural Loan Fund (CALF), Creating the Agricultural Credit Policy Council*	Consolidates all existing and future loan funds that are agricultural and agriculture-related under one fund called CALF. The Fund shall be controlled, supervised and administered by the Ministry of Agriculture and Food. In no case shall any portion of the CALF be used for direct lending to end-users but shall be administered through the banking system, except in the cases of the GFSME and QGFB Creation of the Agricultural Credit Policy Council (ACPC) which shall review and evaluate the economic soundness of all on-going and proposed agricultural activities. It shall also undertake measures to increase its fund base, adopting liquidity, interest stabilization and risk cover mechanisms for its various financing program
Aug. 23, 1996	*EO 363* *Guidelines on the Allocation and Release of the 1996 Poverty Alleviation Fund (PAF)*	Provide guidelines for the allocation of the PAF (P4B) in the 1996 GAA, designating seven national agencies to oversee the implementation Preference in allocation is given to the 20 priority provinces

Area of Financial Intermediation Affected	Targeted Sector	Impact/Implications
Available funds for credit	Across sectors	May create programs that promote a supply led approach to credit.
Fund management; Credit delivery; Agricultural credit policy	Farmers, rural workers, fishermen	Termination of direct lending program on non-GFIs Lower administrative cost in managing funds for agri lending Coordination and formulation of agricultural credit policy Expansion of credit guarantee schemes Induce bank lending to agriculture
Supply of credit funds for the SRA priority provinces	Across sectors in the priority provinces	May lead to fragmented credit programs May promote a supply led approach to credit

Annex C cont.

Date	Law/Regulation	Description
Aug. 23, 1996	*EO 364* *Creating the National Commission on Savings*	The Commission shall take charge of accelerating capital formation through non-inflationary means, particularly through saving in banks and other financial intermediaries
	<u>Administrative Orders</u>	
Oct. 8, 1993	*EO 86* *Creating the National Credit Council*	Creation of a Council composed of government financial and non-financial agencies and private sector organizations The Council shall rationalize various credit programs of government; Rationalize the role of guarantee programs and guarantee agencies; Develop a national credit delivery system towards enhancing productive capability of beneficiary groups and efficiency and effectiveness of financial intermediaries; Encourage private sector participation in credit delivery in the countryside
	<u>Memorandum Orders</u>	
June 17, 1994	*M.O. No. 213* *Approving and Directing the Implementation of the Social Reform Agenda*	Launches a "Credit-for-the Poor" program; Establishes partnerships between GFIs, and coops and other NGOs, with LBP as trustee bank for socialized credit programs and coops and NGOs/POs as actual implementors; Designates specific roles for different players in the financial system

Area of Financial Intermediation Affected	Targeted Sector	Impact/Implications
Savings mobilization	Across sectors	Promotion and growth of savings nationwide
Efficiency of the rural financial markets	Across sectors	Rationalization of gov't credit and guarantee programs Greater efficiency and outreach in credit delivery to the countryside
Supply of and demand for credit for the poor Pricing of credit Delivery scheme(s) for the poor	All basic sectors: farmers and landless rural workers, fisherfolk, urban poor, indigenous cultural communities; workers in the informal sector, other disadvantaged groups	Expansion of credit for the poor; Can lead to subsidized interest rate and therefore distort the credit market Sustainability and viability of credit delivery cannot be assured

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