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March 3, 2021

**Joint Statement by Mr. Palotai, Mr. Just, Mr. Ronicle, Ms. Andreicut, Mr. Clark, and
Mr. Pucnik on Philippines
(Preliminary)
Executive Board Meeting
March 5, 2021**

We would like to thank staff for the insightful report and Ms. Mahasandana and Mr. Bautista for their instructive buff statement. We commend the authorities for the swift containment measures and policy response since the start of the pandemic. **Notwithstanding solid macro-fundamentals before the COVID-19 outbreak, the pandemic has taken a significant toll on the economy of the Philippines and could pose a threat to financial stability.** Therefore, we very much welcome this timely assessment of the financial sector. We share the thrust of staff's recommendations but would like to offer the following views.

We note that the financial sector is dominated by banks, which are well-placed to withstand a severe shock under the baseline. We understand, however, that their solvency could be impacted in a downside scenario, stemming mainly from corporate sector distress, not least given the extensive joint exposures to large mixed conglomerates. The authorities should therefore address downside risks through dividend restrictions and a gradual phase-out of existing forbearance measures, while banks should ensure the timely recognition of loan losses. We also encourage the authorities to further develop their bank resolution framework, given several recommendations are still outstanding from the 2010 FSAP. We share staff's recommendations for a broadening of the resolution toolkit and developing resolution plans for major domestic banks.

Strengthening the macroprudential framework will bolster financial stability. In line with staff's recommendation, the Philippines should develop a macroprudential strategy including additional macroprudential instruments whilst centralizing the authority for implementing and developing nationwide macroprudential policy. The authorities should also consider re-calibrating some of the existing prudential tools (currently set from a micro-prudential perspective, such as loan-to-value) for explicit macroprudential purposes. Given the countercyclical capital buffer (CCyB) is the only explicitly recognized macroprudential instrument at the moment, we encourage the authorities to put in place operational

procedures for triggering changes in the rate of the CCyB once the crisis abates. We encourage the authorities to ensure better coordination among different agencies in order to increase the effectiveness of macroprudential policy. This could involve designating a single authority for macroprudential matters. This could be the central bank, the recently created financial stability unit (the Office of Systemic Risk Management, OSRM), or a board composed of the authorities whose actions have a material impact on financial stability. *Can staff provide information on the legal basis for system-wide implementation of macroprudential instruments for the banking sector in the Philippines?*

Addressing the AML / CFT shortcomings in light of the significant risk of the Philippines being included once again on the Financial Action Task Force (FATF) list of jurisdictions with serious AML/CFT deficiencies should be an urgent priority. We note staff's concerns regarding the existing bank secrecy laws, which undermine financial integrity and stability. These have already been highlighted in previous FSAPs and we strongly encourage the authorities to make the necessary amendments.

We strongly welcome the focus on climate-related risks and the innovative tool combining climate science and catastrophe risk models to test the impact of typhoon risks on banks' solvency. We strongly support the integration of climate considerations into Fund surveillance and encourage staff to continue their efforts in future FSSAs given climate change poses risks to the financial system in the Philippines. We welcome the central bank's decision to join the Network for Greening the Financial System, as well ongoing efforts to better assess climate-related risks.

We note staff's focus on physical risks and that typhoon risks may not be systemic except for extreme tail events. However, we think transition risks are also relevant. Although the economy has been increasing its share of coal-based power generation over recent years, we understand that the government recently put forward plans to limit licenses for new coal-based power plants. We encourage staff to consider both transition risks as well as the interaction between physical and transition risks in future FSAPs. Testing both risks at the same time will provide a better overall picture of a country's exposure to the reality of climate change. We also note that the FSSA tested the impact of a one-off shock over 3 years. Given the risks and impact of climate change is likely to materialize over a much longer time horizon, we think further stress tests should take a longer-term perspective. *What are the plans to broaden the stress test to more systematically cover both physical and transition risks and expand the time horizon given the longer-term impact of climate change on the economy?* Finally, looking ahead to future bilateral surveillance with the Philippines, we encourage staff to provide policy advice that is comprehensive and consistent with getting the price of energy right, encourages the collection of climate change related data and highlights public incentives that hinder the energy transition.