COMPARATIVE BANK STUDY: A BACKGROUND PAPER*

by

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** Research Fellow, PIDS. The author is grateful to Ms. Kristine Chua for her able research assistance and to Ms. Juanita Tolentino for patiently typing the draft.

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I. INTRODUCTION

The PIDS-OSU research project entitled: "Comparative Bank Studies in Rural Areas" will examine the performance of rural banks (RBs), branches of private commercial banks (KBs) and private development banks (PDBs) serving the same rural areas. The overall objective is to determine prospects for institutional viability in offering and expanding financial services to rural clientele in the Philippines (see Graham [1986]). Primary data will be collected from a sample of rural banks and branches of private commercial banks and private development banks.

This paper provides a general background to the abovementioned research project. The findings here could help the research team in preparing the research design for the comparative bank studies. The analysis is mainly based on secondary and more aggregative data. The main objectives are: (1) to briefly review existing banking regulations; (2) to describe the performance of the financial system in the most recent past; (3) to compare the performance of KBs, PDBs and RBs by region; (4) to test the "interest rate" and "institution elasticity" hypotheses using a combination of time series (1983-85) and cross-section data (13 regions and 3 categories of banks, namely KBs, PDBs and RBs; and (5) to examine the performance of individual commercial banks.

II. REGULATORY ENVIRONMENT

Financial institutions are operating under the framework set by the 1980 financial reforms. The main objectives of such reforms are to : (1) to increase competitive conditions among banks, and (2) to increase the availability of and access to longer term funds.

The attainment of these objectives, first of all, demands a restructuring of the banking system. Figure 1 shows the current structure of the financial system. Functional distinctions among banks have been reduced. For example, savings and mortgage banks, savings and loan associations and private development banks are not anymore legally different from each other. Services offered by one category of bank have been broadened to make banks realize economies of scope and to allow greater competition among different categories of banks. One significant feature of the 1980 financial reforms is the creation of universal banks which have expanded commercial banking functions.

Table 1 summarizes salient regulations which are relevant to our comparative bank study. The minimum capital requirement greatly varies among different types of banks. Interestingly, the current real values of these minimum capital requirements are substantially below their real values in 1980 because of the 139 percent inflation rate between 1980 and 1986.

Universal banks are allowed to offer a host of banking and non-banking services, many of which were prohibited before the

Figure 1

	Universal Banks	Commercial Banks	Private Development Banks	Rural Banks
Minimum Capital Requirement	₱500M	₱100M	a) New: Metro Manila - ₱ Other Places - ₱ b) Existing: Metro Manila - ₱10M Other Places - ₱5M	₱0.5M
II. Limits on Equity Investments	A. Financial Allied Undertakings: Comm'l banks - 30% Thrift banks & rural banks - 100% Others - 100%	A. Financial Allied Undertakings: Comm'l banks - 30% Thrift banks & rural banks - 100% Others - 100%	A. Financial Allied Undertakings: Banks - 30% Others - 40%	A. Financial Allied Undertakings: - allowed but with prior approval of the Monetary Board.
	B. Non-Financial Allied Undertakings - 100%	B. Non-Financial Allied Undertakings - 100%	B. Non-Financial Allied Undertakings - 100%	B. Non-Financial Allied Undertakings - 100%
	C. Non-Allied Enterprises - 35%	C. Non-Allied Enterprises - prohibited	C. Non-Allied Enterprises - prohibited	C. Non-Allied Enterprises - prohibited
III. Banking offices	Nationw	Nationwide	Nationwide	Limited to the region where the applicant bank is located.
IV. Reserve requirements (short-term deposit liabilities)	21%	21%	14%	14%

1980 financial reforms. For instance, they can go into investment or merchant banking which was previously restricted to investment houses only. In short, they can engage in almost all economic activities. There are however certain limitations. For instance, they may own voting shares in other commercial banks and non-allied enterprises to the extent of 30 percent and 35 percent, respectively, of the total voting shares (see Annex A for the list of financial allied and non-financial allied undertakings). Others not included in these categories may be fully owned by them.

Ordinary commercial banks and private development banks have more or less the same restrictions on equity investments as universal banks, except in two areas: they may own voting shares in financial allied undertakings but not to exceed 40 percent of the total voting shares and that they are not allowed to own shares in non-allied enterprises.

Rural banks are by far the most restricted banking system. They may invest in financial allied undertakings only upon prior approval by the Monetary Board. They cannot also own non-allied enterprises. However, they are permitted to go into non-financial allied undertakings.

The minimum networth to risk assets ratio is 8 percent for universal banks and 10 percent for other banks. The assumption here is that bigger and well-capitalized banks are more stable than smaller banks. The lower networth to risk assets ratio for universal banks is actually an invitation to banks to expand

their capital. To avoid undue concentration of wealth, universal banks are required to undertake a public offering of new shares to the extent of 10 percent of the required minimum capital.

While mergers/consolidations are being encouraged to reduce the number of banks to achieve their optimal size, branching has also been promoted. For the first time, rural banks are permitted to open branches, although still limited to the region where the main branch is located. There is, however, a regulation that might frustrate the effort to encourage branch banking. That is, the entire country is divided into five service areas, and commercial and thrift banks opening up a branch in any of these areas are required to buy five-year special government or Central Bank securities according to the following schedule:

a)	Service Area I (Heavily overbranched areas)	₱ 20M
b)	Service Area II (Overbranched areas)	₱ 15M
c)	Service Area III (Idealy branched areas)	₱ 10M
d)	Service Area IV (Underbranched areas)	₱ 5M
e)	Service Area V (Encouraged)	0

Rural banks are required to purchase special five-year government/Central Bank securities worth ₱500,000 for each branch opened. The idea that the Central Bank is able to know whether there is undercompetition or overcompetition in one area is indeed questionable. The market is in a better position to know it. However, the recent collapse of a significant number of banks has merely reinforced the Central Bank's view on this issue. In fact, it has for the time being imposed a moratorium

on the granting of license to open a new bank or branch since the onset of the financial crisis. Many of those banks collapsed due to their over-dependence on the Central Bank rediscounting facilities and poor supervision, not due to cutthroat competition.

Aside from this, the deposit retention scheme may also work against branching. Under this scheme, at least 50 percent of the total deposits mobilized by branches of banks in the area where they are given permission to operate should be lent to the same area. This limits banks to manage their portfolio across branches. While such scheme tries to ensure the flow of funds to the rural areas, which still remains a questionable fact, it reduces the profitability of banks.

The reserve requirement has already been made uniform across different types of short-term deposit liabilities (i.e., deposits with maturities of 730 days of less), but not across different types of banks. The present reserve requirement is 21 percent for universal and commercial banks and 14 percent for thrift and rural banks, even if they are subsidiaries/affiliates of universal or commercial banks. The intention of the differential reserve requirement across different types of banks is to offset the cost advantages enjoyed by bigger banks. However, the recent experience shows that bigger banks bought thrift and rural banks. Thus, they also enjoy such privilege.

The deregulation of the bank interest rates was part and parcel of the 1980 financial reforms. But while banks interest

rates were deregulated, the cheap rediscounting policy of the Central Bank which tended to favor certain economic activities continued. It was only in November 1985 that the Central Bank shifted its emphasis from credit allocation to stabilization functions. Since then, all rediscountable papers are treated uniformly in terms of rediscount rate and loan value. Since the rediscount rate has been aligned with the market rate while at the same time, ceilings on re-lending rates for rediscounting funds have been removed, credit subsidies to previously considered high priority sectors have virtually been eliminated. The experience in the past was that credit subsidies only led to misallocation of resources, disintermediation and inflation, not to mention the fact that they were highly regressive (see Lamberte and Lim [1987]).

While credit subsidies are being phased out, risk-reducing schemes are being introduced. Today, there are four guarantee schemes in addition to the crop insurance scheme for rice and corn. Their features are summarized in Table 2. CALF is the latest addition to the guarantee schemes. Its funds came from the various credit programs managed by government agencies. Unlike the previous special credit programs whose funds came directly from the government and/or Central Bank, funds for on-lending under these guarantee schemes have to come from the financial institutions. Thus, these guarantee schemes support and facilitate private initiatives in financing economic activities. Except for CALF which is just newly established, the

Table 2

SELECTED SPECIAL CREDIT PROGRAMS

Credit Program	Eligible Projects	Eligible Borrowers	Loan Purposes	Maximum Loanable Amount	Interest Rate	Maturity Period	Mode of Payment
1. Industrial Guarantee and Loan Fund (IGLF)	Those involved in the establishment or expansion of an industrial, agro-industrial or mining enterprises including manufacturing concerns and those service industries supportiv of manufacturing acti vities. for a co eligible ts.)	A. Cottage enterprise - total assets over P50,000 but not more than P500,000 before financing. B. Small-Scale Enter- se - total assets more than P5?A,000 ot exceed P5M e financ C. Medium-Scale prises - tot ts of more tha P5.0M but not e ding P20M fore financing.	A. Purchase of factory site for new and expansion projects. B. Construction of factory buildir C. Purchas machine equipme fixtures and	A. For Cottage Industries - P0.4M. B. Small-Scale	19% per annum inclusive of all charges.	A. Fixed asset acquisition - 12 years inclusive of a maximum of 3 years grace period on prinpal payment. B. Working capital 7 years inclusive of a maximum of 2 years grace period on principal payment.	Equal quarterly amortization of principapal & interest.
2. Agricultural Loan Fund (ALF)	Agri al and agro-processi g projects: A. Short-term seasonal production credit projects. B. Medium and long-term credit: poultry production, swine production, cattle production, fisheries development, plantation projects, agro-processing and post harvest facilities, and farm mechanization.	Individuals, single proprietorhips, partner ps, corporations and cooperatives.	A. ac excluding land. B. Working capital	- 18 % er annum floating interest rate)	A. Short-term not to exceed 12 months, except for sugar and banana production. B. Medium and Long-term Loans - based on project cash flow but not to exceed 15 years inclusive of a grace period not exceeding 7 years.	Monthly, quarterly, or semi- quarterly.

Credit Program	Eligible Projects	Eligible Borrowers	Loan Purposes	Maximum Loanable Amount	Interest Rate	Maturity Period	Mode of Payment
3. Guarantee Fund for Small and Medium Enterprises (GFSME)	Projects involved in the direct production and /or processing of food intended for biological consumption; those indirectly involved in food production and other agri-project; majority of its produce is intended for export. A. Small Scale - tota project assets o not less tha P62,500 but no more than P2.5 after financing. B. Medium Scale total projec assets of more tha P2.5M but not exceeding P10M after financing.	A. Small Scale Projects- i als or enter- p B. Medium Scale Projects... - Filipino stock corporations.	A. Fixed assets acquisition. B. Construction of plant facilities. C. Working capital. D. Refinancing of existing loans with other financial institutions that are current in status; not to exceed 50% of the of the total loan approved	A. Small-Scale Loan - P300,000 to P2.0M. B. Medium-Scale Loan - more than P2M to P8M.	15% per annum fixed for term of loan approved for guarantee by the GFSME.	A. Working Capital - maximum of 5 years, inclusive of the one year grace period on principal payment. B. Acquisition of fixed assets - maximum of 10 years, inclusive of the two-year grace period on principal payment.	Equal monthly or quarterly amortization.
4. DBP-SSS Financing Program	Industrial, agricultural or agro - industrial projects. (See Annex B for a partial list of eligible projects.	Individuals, single proprietorships, partnerships and corporations	Working capital.	P500,000 per borrower.	17% per annum plus service fee of 4% per annum de- ducted in advance.	Three years.	Monthly, quarterly, semi- annually.
5. Comprehensive Agricultural Loan Fund (CALF)	Any agricultural projects provided total projects assets must not exceed P500,000.	Individuals, corporations and cooperatives,	Any agricultural loan, for working capital or acquisition of fixed assets.	P500,000	Fixed term to be determined by the CALF at the beginning of the quarter.	A. Working capital - 8 years. B. Fixed Asset Acquisition 12 years.	Equal monthly or quarterly.

Table 2 (cont'd.)

track record of those schemes in terms of repayment rate has so far been quite impressive.

Recently, however, loan availments through these schemes have reached an all-time low. In the case of IGLF, the remaining unutilized funds were returned to IBRD. There are reasons for this. First, these guarantee programs are not known by other banks. Hence, only few are really pushing for this program. Second, the procedures for accessing these facilities are very cumbersome and processing usually takes about 2 to 3 months. Third, the interest rate is still fixed at a high rate despite the fact that the general interest rate has been going down. Thus, this program appears to be very expensive to borrowers. In fact, a lot of prepayments occurred recently in these programs. And lastly, the margin offered to banks under these schemes is very low, considering the fact that their transactions costs for originating such loans and processing papers are quite high.

There is therefore a need to redesign these programs in order to make them responsive to the credit needs especially of those who are currently rationed out of the credit market. Processing procedures have to be simplified and processing time shortened so that loans can be released on the time they are most needed by borrowers.

There are still a few special credit programs, however, which are primarily aimed at supplementing the funds of banking system. Examples are the DBP-SSS Financing Program and the ALF Program (see Table 2 for their features). Unlike the previous

special credit programs, these credit programs cover a wider range of economic activities and the interest rates are market oriented. The utilization rate of these funds is however very slow mainly due to their poor or unpopular design. In the case of the ALF for instance, the documentation procedure is so complex, not to mention the fact that the interest rate is way above the current market rate. Moreover, the floating rate applied during the term of the loan approved is not well understood by less sophisticated borrowers. It is also less popular to those who understand it in view of the general expectation that the interest rate is going to rise in the near future.

There are certain regulations that impinge on the intermediation cost. The currently high reserve requirement, the 25 percent agri/agra loan requirement and the 5 percent gross receipts tax (GRT) are taxes imposed on intermediation. Under a competitive environment, all these taxes are supposed to be absorbed by financial intermediaries. Unfortunately, however, such environment does not exist in the Philippine setting. So, banks fully pass on this tax burden to borrowers, who are paying a rate higher than when such intermediation taxes are absent. There seems to be a policy inconsistency here. While efforts are made to stimulate investment by keeping the interest rate low and affordable to investors, intermediation taxes are imposed that jack up the interest rate.

One of the recent changes in monetary policy was the reduction in the reserve requirement for short-term deposit

liabilities from 24 percent to 21 percent. But this ratio is still 3 percentage points above the ratio before the onset of the crisis. Thus, there is still some room for further reduction in reserve requirement. The Central Bank should not stop at 18 percent, but should aim at a much lower reserve requirement, say 10 percent. In this case, more deposit funds can be released for on-lending at relatively lower rates.

The purpose of the agri/agra loan requirement is to increase the flow of loans going to the agricultural sector. This is especially addressed to commercial banks whose loans were oriented towards the urban commercial sector. However, this policy has never accomplished its objective. Table 3 shows that the share of agricultural loans in net loanable funds as well as in total loans outstanding of banks even declined after the implementation of the agri/agra requirement policy as compared to the previous years. What did it accomplish then? Since the government securities eligible for the agri/agra requirement carried a rate much lower than the market rate most of the time, intermediaries were in effect being taxed. Since this tax were passed on to non-agricultural sector in terms of higher interest rate, the latter were in effect being penalized. This is one cross-sectoral subsidy program whose costs were borne by one sector but without clear benefits enjoyed by society as a whole. Thus, there is a need to re-examine this loan portfolio requirement.

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size of the banking system that reinvests funds in potentially new directions, from old loans as they mature (Mckinnon [1981]).

In 1965, Korea's ratio was about one-half of that of the Philippines. It means that the Philippine financial system performed better than the Korean financial system in terms of generating financial resources to support the economy. Five years later, Korea's ratio surpassed that of the Philippines by a wide margin. Since then, the Philippines was not able to catch up with Korea. One of the reasons for Korea's tremendous success was the financial reforms it initiated in 1965 which were primarily aimed at mobilizing domestic financial savings. The Philippines undertook a major financial reform only in 1980. Its effects on the ratio was positive, but more modest compared to that realized by Korea. Towards the latter part of 1983, Korea and the Philippines encountered financial difficulties. However, their impact on the ratio was more severe in the Philippines than in Korea, suggesting that the latter has a more solid financial system.

The performance of Thailand's financial system has been very impressive. The financial ratio has been steadily increasing unlike those of the Philippines and Korea which have been fluctuating.

Another indicator of the performance of the financial system is the efficiency with which it raises and allocates funds. This is determined by the interest rate it gives to deposits, the lending rate it charges to loans, and the spread between lending

and deposit rates. Indeed, one of the intentions of the 1980 financial reforms was to mobilize financial savings so that more loanable funds would be made available to industries by assuring depositors a positive real interest rate on their deposits. This was to be accomplished by improving competition among banks. The increased competition among banks was expected to result in the narrowing of the spread between lending and deposit rates, since banks would be more willing to absorb the increased deposit rate by not raising the lending rate. Thus, both depositors and borrowers stand to benefit from such development, unlike the previous repressive policy regime when only financial intermediaries benefitted.

Table 6 presents the evolution of the nominal and real interest rates and the bank spread. The latter refers to gross bank spread since intermediation cost arising from regulation, e.g., reserve requirement, and administrative cost are not yet netted out. The real deposit rates were positive for the period 1981 to 1982. However, the banks spread also widened, implying that borrowers were paying more when interest rates started to be deregulated. It seems that there is a lack of competition among banks in the credit market, and the interest rate deregulation only succeeded in hurting the borrowers more.

The financial crisis felt by the financial system in 1984 resulted in severely negative bank spread. Although, the lending rate for new loans went to as high as 45 percent, loans which were contracted in the previous period with a fixed rate could

Table 6

NOMINAL AND REAL INTEREST RATES

	INFLATION RATE (GDP)	LENDING RATE NOM	LENDING RATE REAL	DEPOSIT RATE* NOM	DEPOSIT RATE* REAL	REAL SPREAD
1981	10.98	17.119	6.14	15.60	4.62	1.519
1982	8.43	18.219	9.79	14.21	5.78	4.009
1983	11.74	19.331	7.59	14.34	2.60	4.999
1984	48.93	26.743	-22.18	32.48	-16.45	-5.737
1985	17.71	28.234	10.52	15.52	-2.19**	12.714
1986	1.49	17.348	15.86	10.46	8.96**	6.884

Note: Lending rate refers to secured loans for all maturities.
*Time Deposit - 360 Days
**Time Deposit (4th quarter) - All Maturities

not be recalled by banks (see also Remolona and Lamberte [1986] for a related study). Thus, the weighted average lending rate for secured loans increased only to 27 percent in 1984. On the other hand, many depositors pre-terminated their deposits and bought new deposit instruments which had very high nominal yields, thus, sending the nominal weighted average rate for time deposits up to 33 percent. Banks tried to recoupe their losses in the subsequent years by maintaining a wide spread even as the interest rates were going down. The worst thing in this situation is that strong and profitable firms which survived the crisis were made to pay the losses incurred by banks with the loans they gave to weak and unprofitable firms. Today, the interest rate on time deposit hovers around 6 percent while the prime rate is about 12 percent. The spread, which is about 100 percent of the deposit rate, is still very high.

It is noteworthy that while the nominal lending rate has been coming down starting in 1985, the real lending rate has been moving in the opposite direction. In fact, the current real lending rates are unusually high by any standard. Even today when the inflation rate is practically zero, the 12 percent prime rate is considered abnormally high. This is one factor that could weaken the ability of the economy to recover itself from the slump. But this is not all. Learning from their experience in 1984, banks are now charging floating or adjustable rates on almost all their loans. Indeed, this only adds more uncertainty in the market, a development most unwelcomed by businessmen.

The total resources of the banking system could give us more or less an indication of its capability to finance the economic recovery. Between 1981 to 1983, the real resources of the banking system had been increasing quite moderately (see Table 7). But the crisis which took place towards the latter part of 1983 reversed this trend. Several medium-size commercial banks, thrift banks and rural banks became insolvent and were later on closed. In two years time, the real resources of the banking system shrunk by 34 percent. There was a sharper drop in the real loans outstanding since banks substantially reduced their lending in favor of risk-free, high yielding Central Bank/government securities.

Banks have historically been focusing on short-term loans. The 1980 financial reforms that encouraged banks, particularly commercial banks, to lend long made some headway as the share of medium- and long-term loans in the total loan portfolio of commercial banks increased quite significantly (see Table 8). But the recent financial crisis have made banks more cautious. In fact, they have already started reducing the share of their long-term loans in their total portfolio. Development banks which are supposed to take care of the long-term requirements of industries could not meet the large demand for long-term funds, not to mention the fact that many of them, including DBP, are presently in financial distress. In fact, recently the biggest private development with substantial exposure to foreign multilateral loans folded up.

Table 7

RESOURCES OF THE BANKING SYSTEM, NOMINAL (In Billion Pesos

	RESOURCES	NDC OF MON SYS	TOTAL LOANS OUTSTANDING	M3 (NOM)	GDP (NOM)	M3/GDP
1981	298.36	115.77	86.51	82.09	305.26	.2689233
1982	339.17	141.49	98.24	95.27	340.60	.2797118
1983	430.93	171.40	111.39	112.96	384.69	.2936458
1984	487.24	167.01	116.38	121.22	539.41	.2247182
1985	502.50	156.75	87.57	132.88	609.52	.2180125
1986	528.00	140.47	87.60*	149.22	619.70	.2408019

*SECOND QUARTER

RESOURCES OF THE BANKING SYSTEM, REAL (In Billion Pesos)

	RESOURCES	NDC OF MON SYS	TOTAL LOANS OUTSTANDING	M3	GDP	M3/GDP
1981	94.03	36.49	27.26	25.87	96.21	.2689233
1982	98.58	41.13	28.55	27.69	99.00	.2797118
1983	112.10	44.58	28.97	29.38	100.07	.2936458
1984	85.10	29.17	20.33	21.17	94.22	.2247182
1985	74.56	23.26	12.99	19.72	90.44	.2180125
1986	77.20	20.54	12.81	21.82	90.61	.2408019

Table 8

COMMERCIAL BANK DEPOSITS AND LOANS
(₱B, 1978 PRICES*)

	1980	1981	1982	1983	1984	1985
Total Deposits	30.4	34.4	38	40.1	30.8	28.4
Share demand	29	22	16	17	13	12
Share time & savings	71	78	84	83	87	88
Loan Outstanding	55.6	55.1	56.7	58.7	40.6	27.1
Share short term	78	73	69	70	61	61
Share medium & long term	22	27	31	39	39	39

* Deflated by the CPI

Source: World Bank Report (1986).

The movements of key economic and financial indicators in 1986 seemed to be encouraging. GNP growth rate turned positive after a negative growth rate for two successive years. Inflation was practically negligible. The flow of loanable funds and the financial resources of the banking system (in real terms) started to pick up. Outstanding loans of banks and Central Bank rediscounting to banks improved moderately. The M3/GDP ratio rose slightly to 24 percent from 21 percent the previous year. With these bright prospects for the economy in the near future, the financial system is expected to play a more positive role.

IV. COMPARATIVE PERFORMANCE OF KBs, PDBs, AND RBs AT THE REGIONAL LEVEL

This section compares the performance of KBs (including both universal and ordinary commercial banks), PDBs and RBs at the regional level. All head offices of KBs are located in the National Capital Region (i.e. Region IV), but their branches are spread all over the other 12 regions (see Table 9). Although most of their branches are situated in provincial capitals and/or prime cities and towns, however, their banking operations extend to all over the province and region. With regard to PDBs, a significant number of their head offices are located outside the National Capital Region (NCR). Specifically, 20 out of 45 head offices of PDBs operate outside NCR as of December 1985. They have very few branches compared to commercial banks. Usually, their branches are located in provinces or regions close to the province or region where their head offices are situated.

Originally, RBs were supposed to be unit banks only. But after the 1980 financial reforms they are already allowed to open up branches in other towns/cities within a certain region subject to the branching regulations discussed in Section II. Even then, very few of them have opened up branches. Lately, quite a number of them became subsidiaries of commercial banks.

Essentially, we will be comparing the performance of branches of KBs with either head offices or branches of PDBs and head offices of rural banks operating at a certain region. The reason why the comparison is done at the regional level is that

Table 9

Table 9 (cont'd.)

Table 9 (cont'd.)

Table 9 (cont'd.)

the most disaggregative data published by the Central Bank regarding the financial performance of branches of banks stop at the regional level. Specifically, balance sheets and income statements of branches and/or head offices of banks belonging to the same type of bank are aggregated at the regional level. Note, however, that there are no PDBs operating in Regions II, IX and XII. In some regions, very few PDBs are operating.

The performance of branches of KBs, PDBs and RBs will be evaluated on the basis of the following indicators: (a) strength in deposit mobilization; (b) bank stability; and (c) profitability. The volume of deposits per branch and the ratio of deposits to total resources are used as measures of the strength in deposit mobilization. For bank stability the ratio of loan portfolio to deposit liabilities is utilized. Liquidity ratio could not be used here since data on liquid assets are not available. A single measure of profitability is used here, i.e., the ratio of net operating income to operating income. The rate of return on equity could have been another good measure of bank profitability. However, it is very difficult to derive such measure because of the problem involved in determining the equity of branches of banks. Indeed, the number of performance indicators we are using for this study is very limited because of the unavailability of some data.

The comparison will be done over a 3-year period, i.e., from 1983 to 1985 to see if the relative performance of the three types of banks is consistent over these years. Incidentally, the recent economic crisis started towards the second semester of

1983, and the economic downswing continued for two consecutive years. The economic conditions of the 13 regions also followed this trend, as may be gleaned from the movements of the respective regional gross domestic products (GDPs) in real terms (see Table 9). Both the commercial and rural banks seemed to be adversely affected by the crisis as may be gathered from the declining number of banking offices over the period 1983 to 1985. The number of offices of PDBs have either remained the same or have slightly increased during the same period.

Strength in Deposit Mobilization

KBs' deposit mobilization is more extensive than PDBs and RBs'. The average deposit per branch of KBs in 1985 ranged from ₱28M to ₱52M in regions outside the NCR (see Table 10). This is about 3 to 5 times the average deposit per branch of PDBs.

Except for one region, rural banks rank the last among the three groups of banks in terms of the volume of deposits per branch. It should however be noted that branches of KBs and PDBs tend to locate in cities and towns where bigger deposit accounts can be found, whereas rural banks are spread all over the countryside, including smaller towns. The ranking of the three groups of banks over the 3-year period has been fairly consistent.

The ratio of deposit liabilities to total resource indicates where most of the resources of banks come from. The higher the ratio, the more successful the banks are in mobilizing deposits.

Table 10

Table 10 (cont'd.)

Table 10 (cont'd.)

Table 10 (cont'd.)

KBs have the highest ratio among the three groups of banks in all the regions. Except for two regions, the ratios are quite high at between 75 to 91 percent in 1985.

One notable feature here is that the ratio of deposit liabilities to total resources of KBs in the NCR has been very low at about 34 to 37 percent during the period 1983 to 1985. There are reasons for this. One is that the head offices of KBs bear most of the physical resources such as, buildings, office equipment, etc. for the entire bank including branches. The other reason is that the head offices have ready access to the rediscount windows of the Central Bank which augment their resources. Still another reason is that they are the main users of funds mobilized by their branches outside the NCR.

With regard to the low ratio of deposit liabilities to total resources in Region VI, we surmise that this is due to the KBs' inability to mobilize deposits.

The PDBs rank second in terms of the ratio of deposit liabilities to total resources, although very much far behind the KBs. However, they were outperformed by RBs in at least three regions. It is noteworthy that in regions close to the NCR, specifically Region III and Region IV-A, the ratios are more than twice the ratios in other regions. Here, both supply and demand could have worked together. From the demand side, the two regions have incomes relatively higher than the other regions, except the NCR as may be gathered from their GDP values. This is translated into higher demand for deposit instruments. On the

supply side, PDBs head offices and/or branches close to Metro Manila are professionally managed and therefore tend to be more competitive. The same finding can be observed with regard to the rural banks located near the NCR.

It is noteworthy that the ratios of deposit liabilities to total resources of KBs, PDBs and RBs had been increasing in almost all the regions during the period 1983-1985. In some regions, like Region X, the increase in the ratio of KBs has been phenomenal. During this period, monetary policy was contractionary and the Central Bank practically closed its rediscounting window, except for export papers. With cheap money already unavailable, and the interest rates on CB bills and Treasury bills very high, banks responded by offering high-yielding deposit instruments in order to stay competitive.

Stability

The loan to deposit ratio "indicates the extent which a bank overstretches its resources to provide loans" (World Bank Report [1986]). The higher the ratio, the more unstable the bank is. Normally, the ratio should not exceed 100 percent because banks have still to provide reserves for their deposits. In addition, a portion of the deposits is usually invested in equities and/or securities as part of the portfolio diversification of banks. Accordingly, Japanese banks are required to keep the ratio below 80 percent.

In 1985, KBs' loan to deposit ratios ranged between 20 to 45 percent in almost all regions, except in the NCR and Region VI.

While below 100 percent, these ratios are surprisingly low. It should be pointed out that branches of KBs are covered by the deposit retention scheme and therefore, the ratios should have not gone below 50 percent. However, with the results, it appears that this regulation is not being strictly followed and enforced. Most of the deposit funds of branches of commercial banks could have gone to the NCR since the loan to deposit ratio in this region exceeds 100 percent. This tends to show that KBs regard their branches located in areas outside Metro Manila as mainly deposit taking institutions. It is highly possible then that their branches have greater discretionary power with regard to raising deposits but have very limited decision making power with regard to originating loans. Moreover, head offices may have regarded commercial and industrial loans in the NCR more profitable and less risky than agricultural loans in the countryside. This is an issue worthwhile watching in the forthcoming survey.

PDBs' and RBs' loan to deposit ratios greatly exceed 100 percent in almost all regions and in almost all the years. Indeed, a significant proportion of their loans were supported not by deposits but by borrowings from the Central Bank and other government agencies having special credit programs. As such, they acted merely as conduits or brokers of Central Bank and government funds, rather than real banks. They are more exposed to risk since a sudden change in policy could immediately put them in a difficult situation. Indeed, this happened in the

recent past when the Central Bank tightened its rediscounting policy.

It is interesting to note that PDBs located near Metro Manila have loan to deposit ratios lower than 100 percent. In the case of Region III-A, the ratio more or less falls within the normal range except in the last year. It seems that these PDBs in this region operate like a real bank whose loans mostly come from deposits they have mobilized. In Region III, however, PDBs behave like branches of KBs. They have lower loan to deposit ratio, suggesting that most of their deposits were transferred to their respective head offices in the NCR.

Note that the loan to deposit ratio of all groups of banks had been declining in almost all regions during the period 1983-1984. This was the result of two factors. One is that loans outstanding of banks declined due to general economic crisis. A significant proportion of their funds were instead invested in government securities. The other factor is that they were able to raise more deposits by offering higher interest rates. As already pointed out above, banks offered very high interest on deposits to compete with government securities.

The overall picture that can be drawn from the findings is that in regions outside Metro Manila, KBs are specializing in deposit mobilization to support the lending activity of their head offices located in Metro Manila, whereas PDBs and RBs are specializing in lending with most of the funds coming from special credit programs of the government. The implications of

this to our study comparing the performance of KBs, PDBs and RBs is clear. It means that we have to exercise extra care in comparing the performance of different types of banks using standard ratios. A branch may be pursuing an objective different from that of a unit bank. This has to be sorted out first before drawing any conclusion. For example, we found that the loan to deposit ratios of branches of commercial banks are below 100 percent, but the very low ratio made us to suspect that they are only performing one function of banking. However, it should be noted that their function is dictated by the overall objective of the mother bank.

Profitability

As mentioned above, our measure of profitability is the ratio of net operating income to total operating income. It indicates to what extent banks were able to control their operational costs. The higher these ratio, the more profitable the bank is due to mangement's ability to control costs.

There is a peculiar pattern that we observe here regarding the profits realized by banks. Branches of commercial banks in almost all regions incurred negative net profits (see Table 9). This could be the result of two factors. One is that branches of PNB which have been incurring huge losses have dominated the branches of KBs. In 1985 alone, total losses of the government-owned Philippine National Bank (PNB) amounted to ₱7.2 billion. Unfortunately, however, we could not find a way of segregating PNB branches away from the rest of the branches of KBs given the

data available on hand. The other is that their volume of deposits was much larger than their loans, hence, their interest expense on deposits greatly exceeded their interest income on loans. As we have pointed out earlier, branches of commercial banks in the regions are mainly deposit taking institutions. Note that it is only in the NCR and Region VI where KBs realized positive net profits. These are the only areas where KBs lending activity was concentrated as indicated by their loan to deposit ratios that exceeded 100 percent. Consequently, their interest income was more than their interest expense in these two regions.

The case of PDBs is somewhat similar to that of KBs. For instance, PDBs in Region III incurred negative net profits mainly due to the fact that their interest expense exceeded their interest income. In other words, they have lower volume of loans as compared to their volume of deposits. However, in regions where PDBs lending activity is quite substantial, positive net profits were realized.

Among the three groups of banks, only RBs in all regions have consistently earned positive profits during the period 1983-85. This seems to be surprising considering the fact that RBs suffered most from the recent economic crisis. It should, however, be noted that the data we are using are based on the unaudited reports of the RBs submitted to the Central Bank. Most banks did not incorporate in their reports the valuation reserves required by the CB examiners.

On the basis of these findings, it is then very hard to compare profitability of branches of KBs and PDBs with that of unit banks using the ratio of net operating income to operating income as the measure of profitability. In the first place, branches of commercial banks could afford losses so long as the consolidated profits of the bank as a whole are positive (see Section VI for an analysis of individual bank's profits). Secondly, the data available on hand cannot be used for the said purpose. The true picture of the financial statements especially RBs must be obtained in the first place. Secondly, other measures of profitability that would take into account the varying characteristics of the three groups of banks can be devised. For example, the contribution of branches of KBs to the overall profits of the bank even if they are not the ones directly lending providing that the funds come from them must be estimated. We suspect that the data on which our present analysis is based do not reflect this simply because they were compiled by branches of banks using the standard accounting procedure. This should be taken into consideration in the forthcoming comparative bank study.

V. THE INTEREST RATE ELASTICITY AND INSTITUTION ELASTICITY HYPOTHESES

The potential for mobilizing savings has long been recognized. But it is only recently when the country is facing severe foreign exchange crisis that policies are finetuned to tap the saving potentials of the domestic economy.

The project: "Comparative Bank Study" will address the extent of banks' success in mobilizing financial savings. In looking at the issue of savings mobilization, two variables are always given more importance. One is interest rate, and it is hypothesized that financial savings respond positively to interest rate. The other is the availability of financial institutions, and the hypothesis here is that savers are induced to save in financial forms if they have easy access to financial institutions. Lamberte (1987) reviewed the studies which directly or indirectly tested these hypotheses. The results were found to be mixed and no definitive conclusion could be reached.

In view of the importance of the issues involved, this background paper attempts to examine again the interest rate elasticity and the institution elasticity hypotheses. It does not, of course, intend to settle the debate, but we merely want to provide an alternative way of verifying the hypotheses that could perhaps be useful to the comparative bank study.

The model is as follows:

$$FD = f(i_D, BANKS, GDP) \qquad (1)$$

FD stands for financial deposits with banks. Data are obtained not from the households but from the banks. Bank deposits then are used as the proxy for household financial savings. The weakenes of this proxy is, of course, obvious. First of all, it excludes cash, insurance claims, bonds as instruments of financial savings. Cash is one of the most important forms of financial savings in the rural areas. Secondly, it includes corporate, institutional households and government deposits.

The variable, i_D, refers to the effective interest on deposits. This is derived by dividing the actual interest expense on deposits by the outstanding deposits of banks. This is one aspect that makes our study different from the previous studies which used either the statutory or reported actual interest rates on savings or time deposits or the weighted average of both.

BANKS refers to the number of bank offices of each type of banks in a region, while GDP stands for gross domestic product of a region.

This study makes use of a combination of cross-section and time series data. This is another aspect that makes our study different from the previous ones. Data on deposits, effective interest rates, number of branches for KBs, PDBs and RBs are available for the 13 regions. The study covers the period 1983-85. Note that the interest rate policy regime is the same in all these years. Some of the previous studies tested the two

hypotheses mentioned above not knowing that the data utilized included different interest rate policy regimes.

Equation (1) was estimated using OLS. The time dummy variables (i.e., DUM83 for 1983 and DUM84 for 1984) did not yield significant coefficients. So, they were dropped in the final runs. The results are summarized in Table 11. Model I includes all the identified independent variables. All have the expected signs. However, the coefficient of GDP is not statistically significant. The equation seems reasonable on the basis of the R^2 and F-statistic. The elasticities computed at the means are also shown in the same table. It appears that the presence of more banking institutions in the regions has greater impact on deposits than high interest rate in the regions. This seems reasonable since high interest rate does not mean anything to people in the provinces if financial institutions are not accessible to them.

Previous studies encountered severe collinearity problem between GDP and BANKS. Specifically, increase in bank network was found to be strongly correlated with income. Thus, BANKS was found to have no significant effect in previous studies. We have tried to check whether this problem appears in our case. Model II reestimated equation (1) without GDP. The estimated cofficients and elasticities of i_D have virtually remained the same. In Model III, we dropped BANKS from the equation. The result is that GDP has a significant effect on deposits while i_D does not have. However, the R^2 considerably drops to a very

Table 11

RESULTS OF TESTING THE INTEREST RATE ELASTICITY AND INSTITUTION ELASTICITY HYPOTHESES

	MODEL I	Model II	Model III
	Coefficients		
Constant	-7423.300 (-7.72)*	-7143.9 (-8.55)*	-4911.0 (-2.01)*
iD	6348.100 (2.20)*	6405.4 (2.22)*	-370.88 (-0.05)
BANKS	111.0300 (24.08)*	112.42 (28.34)*	-
GDP	0.00998 (0.59)	-	.21444 (5.79)*
R^2	.88	.88	.23
F	266.168*	401.55*	16.77*
	Elasticities		
iD	0.277	0.280	-0.016
BANKS	2.540	2.572	
GDP	0.106		2.289

Note: Figures in parentheses are t-values.

* - significant at 5 percent.

low level, suggesting that Model III is a model inferior compared to Models I and II.

The inescapable conclusion drawn from the results is that the interest and institution elasticity hypotheses cannot be rejected using the approach and data of this study.

We proceed further by examining the demand for deposit instruments of KBs, PDBs and RBs. Equation (1) was run separately for KBs, PDBs and RBs. The results are presented in Table 12.

Deposits with KBs are found to increase with an increase in the interest rate on deposits. This is not however the case with PDBs and RBs. In fact, the sign of the coefficients of interest rate is negative for both groups of banks. It should be noted that during this period, there was a general nervousness in the financial system. Many depositors shifted their deposits from small to bigger banks and from thrift and rural banks to branches of commercial banks which were perceived to be relatively more stable.

The number of offices has a significant positive effect on deposits with KBs, PDBs and RBs. In the case of KBs, an additional branch openend brings about additional deposits of ₱127 million. In contrast, an additional branch or head office of KBs and PDBs attracts only ₱6 million and ₱4 million, respectively.

Table 12

DEMAND FOR DEPOSIT INSTRUMENTS OF KBs, PDBs and RBs

	KBs	PDBs	RBs
Constant	-16904.00 (-6.33)*	-119.44 (-3.68)*	-105.70 (-1.99)**
iD	108640.00 (3.96)*	-16.447 (-0.30)	-520.11 (-1.64)
BANKS	127.00 (19.14)*	6.167 (6.55)*	3.967 (16.16)*
GDP	-0.0695 (-1.70)**	51.6321 (7.98)*	15.422 (4.19)*
R^2	0.98	0.93	0.88
F	596.81*	134.23*	97.45*

Note: * Significant at 5 percent level.
** Significant at 10 percent level.

The effect of regional income on deposits with KBs is negative and statistically significant at 10 percent level. This is indeed surprising and difficult to explain. Perhaps, more analysis is needed in this regard.

With regard to PDBs and RBs, regional income is found to have a significant positive effect on deposits. It means that improvement in regional income is important to PDBs and RBs in raising deposits.

VI. FOCUS ON INDIVIDUAL COMMERCIAL BANKS

In Section IV, we have observed that branches of KBs obtained negative profits. We have pointed out that this is not necessarily the case if the bank in its entirety is examined. This section focuses on the performance of individual commercial banks using their consolidated financial statements. This should give us idea regarding commercial banks to be included in the comparative bank study and at the same time, help us analyze the primary data to be gathered later on from sample branches of commercial banks.

Presently, there are 30 operating commercial banks. Nine of them are authorized to operate as universal banks. Ten banks have more than 50 branches (see Table 13). It can however be observed that majority of the branches are concentrated in the National Capital Region.

The financial system underwent two crises since 1981. Both crises exposed the weaknesses of several commercial banks. In the first crisis, six commercial banks encountered severe financial difficulties. For fear of a global bank run, the government attempted to rehabilitate all of them. The assistance came in the form of equity infusion, CB advances and government deposits (see Table 14). The government eventually took over these banks in view of its huge exposures. Recently, InterBank was able to sell 40 percent of government equity to a foreign financial institution.

REGIONAL DISTRIBUTION OF COMMERCIAL BANKS, 1985

	I	II	III	IV	IV-A	V	VI
1. ALLIED	8	3	6	28	4	3	8
2. AB	1	-	4	22	-	-	-
3. BA	-	-	-	1	-	-	-
4. BPI	7	-	9	58	6	3	6
5. CHINA	1	-	2	13	-	1	1
6. CITIBANK	-	-	-	1	-	-	-
7. CITYTRUST	1	-	-	19	5	2	-
8. COMBANK	-	-	-	7	1	7	-
9. CONSOLIDATED	-	-	2	24	3	3	2
10. EQUITABLE		2		26	-	-	-
11. FAR EAST	5	1		30	3	3	3
12. HONGKONG	-	-	-	1	-	-	-
13. INTERBANK	-	-		15	-	1	1
14. MANILABANK	4		5	46	3	2	8
METROBANK	6	6	10	54	14	3	6
16. PBCOM	1	-	-	17	-	-	1
17. PHILBANKING	3	-	1	25	3	-	1
18. PCIB	9	1	8	61	4	3	11
19. PNB	16	10	18	35	20	11	9
20. PHILTRUST	1	-	1	16	-	-	-
21. PILIPINAS	-	-	-	-	-	-	-
22. PRODUCERS	5	3	2	22	-	1	3
23. PRUDENTIAL	3	-	7	26	4	1	1
24. REPUBLIC	4	1	5	8	5	2	6
25. RCBC	2	1	2	18	2	1	2
26. SECURITY	4	1	1	23	5	-	4
27. STANDARD	-	-	-	-	-	-	-
28. TRADERS	5	-	5	19	2	1	7
29. UNION	-	-	1	11	-	-	2
30. UCPB	2	1	7	38	6	4	4

Table 13 (cont'd)

VII	VIII	IX	X	XI	XII	FOREIGN	TOTAL
9	3	7	4	5	3	4	95
1	-	1	1		1	-	33
-	-	-	-		-	-	1
4	2	1	5	6	-	-	107
1	-	1	1	1	-	-	22
1	-	-	-	-	-	-	2
2	-	-	2	1	-	-	32
1	-	-	-	-	-	-	16
6	1	1	3	3	1	-	52
1	1	-	1	1	-	-	33
5	-	1	1	3	1	-	59
-	-	-	-	-	1	-	1
3	-	-	1	1	-	1	29
3	2	1	2	3	3	-	83
7	3	6	5	5	2	2	129
1	-	-	1	1	-	-	22
2	-	-	1	3	-	-	39
8	4	4	10	8	7	-	138
10	8	6	9	7	6	4	169
1	-	-	-	2	-	-	21
-	-	-	-	-	-	-	-
4	1	2	3	3	2	-	51
3	1	1	-	1	-	-	48
2	1	-	1	1	-	-	36
2	2	-	1	6	1	-	49
1	-	1	1	2	-	-	43
1	-	-	-	-	-	-	1
4	1	1	1	2	-	-	42
3	1	1	1	3	-	-	23
5	2	1	3	4	2	-	79

Table 14

GOVERNMENT'S FINANCIAL ASSISTANCE TO ACQUIRED BANKS
(As of December 1984)
(₱ Million)

Bank	Government Equity	Government Deposits	Parent Advances	CB Advances
Associated	407.0	16	24.9	297.4
COMBANK	322.0	97	174.0	154.8
Inter Bank	530.0	3	-	43.9
Pilipinas	240.0	92	150.4	241.3
Republic	-	25	-	1666.9
Union	309.0	987.6	850.0	24.4

Source: Financial Reports of Individual Banks.

The second financial crisis further brought down a number of badly managed banks. This time, the government made a big change with regard to its policy towards ailing banks. It allowed the closure of two commercial banks, namely Pacific Banking Corporation and the Philippine Veterans Bank. The same policy has been applied to other types of banks encountering the same problems.

As already mentioned above, the 1980 financial reforms encourage mergers/consolidation to reduce the number of commercial banks in the system and at the same time broaden the ownership of the remaining big banks. This policy thrust has hardly produced any positive result. What happened instead was that bigger banks completely bought out other banks. For instance, Bank of the Philippine Islands bought Family Bank and Trust Co., a universal bank, and converted it into a thrift bank. The Philippine Commercial International Bank completely absorbed Insular Bank of Asia and America.

To examine the performance of individual banks, it is useful to group them into four groups: private domestic commercial banks (29), branches of foreign commercial banks (4), government-acquired commercial banks (6), and government-owned commercial bank (1).

Of the 29 private commercial banks, only 8 are listed in the two stock exchanges. The rest are still closed, family-owned corporations (see Patrick and Moreno [1984] for a related study).

The size of commercial banks vastly varies (see Table 15). Eight out of thirty banks have assets above ₱10 billion. PNB remains the biggest commercial bank even if its current size is reduced to about one-half of its previous size as outlined in its rehabilitation scheme. Citibank, a foreign-owned bank, is the second biggest commercial bank with assets amounting to ₱27 billion. Bank of America (BA) and Bank of the Philippine Islands (BPI) rank the third biggest banks, while Metro Bank and PCIB are the fourth biggest banks, followed closely by UCPB and Far East Bank in that order. COMBANK and Pilipinas Bank are the smallest commercial banks with assets less than ₱2 billion.

The growth in assets of banks over the period 1980-85 had been widely uneven. Bigger banks achieved phenomenal growth in assets well in excess of 100 percent during this six-year period. Thus, they were able to maintain their relative position in the banking system. In contrast, most small banks realized very slow growth. Hence, the size difference between big and small banks has widened since the 1980 financial reforms.

The eight big banks, that is, those whose assets exceeded ₱10 billion as of December 1985, have a fairly wide deposit base. They controlled 62.4 percent of the total deposits in the commercial banking system. Except for PNB, the growth in their deposits over the period 1980-85 had been very high, way above 100 percent. In contrast, the growth in deposits of small banks had been low, mostly below 100 percent over the same period. It is noteworthy that in almost all banks, the growth in deposits

Table 15

SELECTED FINANCIAL INDICATORS

	(1) Assets (PB, 1985)	(2) Growth in Assets (%)	(3) Deposits (PB, 1985)	(4) Growth in Deposits (%)	(5) Net Income (PM, 1985)	(6) Loans Deposits (%)	(7) Net Income Gross Income (%)	(8) Net Income Equity (%)
A. Private Commercial Banks								
1. Allied*	8.9	26	6.3	36	214	46.3	13.7	27.0
2. BPI*	16.5	157	12.3	211	262	47.8	10.0	22.6
3. China	4.4	23	3.2	90	11	63.2	1.5	2.2
4. City Trust*	5.1	238	2.5	369	153	65.9	16.9	23.7
5. Consolidated	5.4	80	3.9	86	25	50.1	3.1	5.8
6. Equitable	4.1	39	3.0	63	44	48.8	9.1	8.2
7. Far East*	2.4	186	8.3	182	290	50.2	15.5	24.5
8. Manil		152	3.7	71	46	121.5	4.8	7.3
9. Metro Bank*	15.4	202	11.5	223	136	58.4	6.8	14.1
10. Communications	3.2	16	2.0	46	18	59.2	3.1	4.8
11. Phil. Banking	2.7	22	1.8	34	(41)	80.2	(9.0)	(18.5)
12. PCIB*	16.4	260	10.8	293	120	58.9	8.0	12.2
13. Phil. Trust	2.3	155	1.8	236	32	43.5	12.1	10.6
14. Producers	2.6	88	1.0	69	NA	NA	NA	NA
15. Prudential	4.9	125	3.2	137	77	50.2	10.1	20.6
16. RCBC	5.6	50	3.3	37	56	72.2	5.5	12.3
17. Security	6.0	139	4.5	168	43	31.2	4.3	12.4
18. Traders	4.9	31	3.6	37	14	55.4	1.7	3.6
19. UCPB*	13.9	200	9.4	195	147	70.5	6.7	7.5
B. Foreign Bank								
20. BA	16.	154	2.0	178	8	NA	NA	NA
21. Citibank	27.1	443	12.2	243	568	100.9	12.8	409.3
22. Hongkong	3.3	107	0.7	30	(21)	349.3	(3.7)	(9.6)
23. Chartered	2.4	323	0.7	90	32	215.4	8.0	7.4
C. Government-Acquired								
24. A iated	2.6	27	1.4	48	(19)	81.8	(5.9)	(7.8)
25. C nk	1.8	259	0.7	1374	30	104.9	9.5	8.6
26. I bank	5.4	230	1.6	176	90	189.2	15.8	12.1
27. P inas	1.7	61	0.8	109	20	115.7	9.4	7.1
28. R lic	5.8	19	1.7	10	46	210.2	3.6	9.3
29. Union	4.0	104	3.0	1120	30	78.7	4.3	7.2
D. Government-Owned Bank								
30. PNB*	76.2	97	23.5	19	(7000)	154.8	(139.4)	(575.7)

NA - not available.

Source: Business Day, 100 Top Corporations (various years)

* Universal ba

outstripped the growth in assets over the period 1980-85. It means that banks have been increasingly relying on deposits for their lending and investment operations. The interest rate deregulation and the change in the rediscounting policy of the Central Bank seemed to produce favorable results on deposits. The branches of foreign-owned commercial banks are however the obvious exemptions in this regard. They mainly rely on resources of their head offices, not to mention the fact that they are not allowed to have branches anywhere in the country.

The year 1985 was bad for the economy as GNP plunged by 3.8 percent, but not necessarily for banks. The hefty profits realized by them were partly due to the high yields on risk-free government and CB securities. There were however four banks, one for each bank group, which incurred losses. PNB's staggering loss of ₱7 billion in 1985 was extremely high.

Table 15 also shows the loan to deposit ratio of each bank for the year 1985. Almost all of the private domestic banks had ratios below 80 percent, the level considered as normal. However, the ratios were extraordinarily low for most banks. The unstable situation in 1985 coupled with the sharp drop in demand for credit compelled banks to switch a substantial portion of their resources to government and CB securities. The only exception to this case is Manila Bank whose loan to deposit ratio reached 121 percent. Its financial situation has recently reached crisis proportion, and the CB has already stepped in to prevent further dissipation of its assets.

For foreign banks, a high loan to deposit ratio is not surprising. As already pointed out earlier, these banks depend more on the resources of their head offices.

PNB and four government-acquired commercial banks obtained loan to deposit ratios well in excess of 100 percent. This indicates that these banks are financially unstable because they are overstreching their resources to provide loans. It is indeed surprising to know that after taking over the four commercial banks for quite some time already, the government is still unable to restore financial stability to these banks.

The ratio of net income to gross income substantially varies across banks. The average ratio for the five big private commercial banks was 9.4 percent compared to only 5.9 percent for small private commercial banks. The average ratio for the six government-acquired banks which was 6.9 percent was at least comparable to that obtained by small private commercial banks.

The rate of return on equity realized by individual banks also varies considerably. The average rate of return on equity for the five big banks was quite high at 16.2 percent. Although, average rate of return on equity of small banks was only 9.2 percent, it was still well above the 6.1 percent average rate of return on equity realized by the six government-acquired commercial banks.

Some patterns have clearly emerged in our analysis. Big private commercial banks' performance had been quite impressive even during the crisis period. In contrast, government-owned and

acquired commercial banks performed miserably. Its overall performance was not even at par with the performance of small private commercial bank. But among private commercial banks, the performance varies considerably, with bigger banks performing better than smaller banks.

VII. CONCLUDING REMARKS

The general objective of this paper is to provide a general background to the forthcoming comparative bank studies which will primarily make use of primary data to be collected from a sample of rural banks (RBs), branches of commercial banks (KBs) and branches or head offices of private development banks (PDBs). The findings here could aid in formulating the research design for the comparative bank studies.

The results here indeed pose some challenge to the researchers in comparing performance of RBs, KBs and the PDBs. We have observed that the performance of these financial institutions is in some way conditioned by the operating policy framework. For example, RBs and PDBs did little savings mobilization because of the financial support they got from the government and Central Bank. In contrast, KBs' branches did intensive savings mobilization drive in regions outside the NCR. One notable finding, however, is that RBs and PDBs operating near NCR operate like branches of KBs. The strong competitive environment could have compelled them to operate as efficiently as branches of KBs. Thus, performance of the three financial institutions is also conditioned by the structure of the market in a certain region.

The findings also provide warning in using standard financial indicators to compare performance of the three banking institutions. For example, the three financial picture of the RBs has to be obtained first. Perhaps, the Central Bank method

of providing valuation reserves will be applied. Another example is that the real profits realized by branches of KBs have to be obtained. Here, their contribution to the overall profits of the entire banks has to be estimated.