The Asian Financial Crisis of 1997

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Financial centres are tested in crises. Their institutions, their banks and their currencies reveal in a few months of turmoil the strengths and weaknesses that years of growth had hidden. For Singapore, the decisive test of the post-independence period came in the second half of 1997, when a currency crisis that began in Thailand spread within weeks to Indonesia, Malaysia and the Philippines, then to Korea and Hong Kong. Within a year the economies of the region had contracted sharply, governments had fallen and the International Monetary Fund had organised the largest rescue packages in its history. Singapore sat at the centre of this region as its banker, trader and port. It could not escape the storm.

This chapter examines how the crisis reached Singapore and how the city-state responded. It looks first at the origins of the crisis in the region. It then measures Singapore's exposure through trade, bank lending, the currency and the stock market, and explains why the city proved more resilient than its neighbours. The middle sections describe the monetary and fiscal response, including the flexible management of the Singapore dollar and the cost-cutting package of November 1998, and the consequences for regional banking and trade. The final section argues

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that the crisis became a turning point for the strategy of the financial centre. Singapore emerged from it with a new approach to supervision, a programme of liberalisation and a deliberate ambition to compete with the world's leading centres.

The Geneva volume describes a comparable moment in Swiss history. The banking crisis of 1931 exposed the weaknesses of an unsupervised banking system and led, after twenty months of deliberation, to the Federal Banking Act of 8 November 1934.[1] In both cities a crisis produced institutions that shaped the financial centre for decades. In Singapore the effect of the Asian crisis was broader than any single statute, because it changed the way the state thought about its financial sector.

Essentials

The Asian financial crisis began with the floating of the Thai baht on 2 July 1997 and spread to Indonesia, Malaysia, the Philippines and Korea. Singapore had no excessive foreign borrowing and sound banks, yet its close links with the region transmitted the shock through trade, bank loans, the currency and the stock market. The Monetary Authority of Singapore (MAS) let the Singapore dollar fall against the US dollar while keeping its trade-weighted value broadly stable, and it refused both capital controls and support purchases of shares. The government added a S$2 billion off-budget package in June 1998 and a S$10.5 billion cost-cutting package in November 1998, whose centrepiece was a cut of ten percentage points in employers' CPF contributions. The crisis also became the occasion for a new strategy: risk-focused supervision, higher disclosure standards, the opening of the banking sector and an active promotion of Singapore as a world-class financial centre.

Notes

1. Ressos, *Genève, place financière internationale*, Part D, chapter “Guerre, crises et loi sur les banques (1914–1934)”, section on the crisis of 1931 and box “À retenir”: the federal banking act adopted on 8 November 1934 after twenty months of deliberation. ↩

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