The crisis as a turning point for strategy

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The Financial Sector Review Group

The most important consequence of the crisis for Singapore was strategic. Paradoxically, the review of financial sector policy had begun before the crisis reached Singapore. In mid-1997 the government formed a Financial Sector Review Group to review its approach to regulating and developing the financial sector, and the overview of the MAS annual report dates its formation to August 1997. Its aim was to position Singapore as a premier financial centre in Asia and globally. MAS commissioned private sector committees on specific aspects of liberalisation and engaged McKinsey & Co for a strategic review of the sector.[1]

The crisis gave this review urgency. Lee Hsien Loong, who had succeeded Richard Hu as chairman of MAS, explained the logic in his first statement. Falling regulatory barriers, advances in information technology and a wave of mergers were transforming global finance, so that financial activity was consolidating in fewer centres.[2] A centre that stood still would lose business to those that moved. The regional crisis, which shrank the market Singapore served, made the need to compete globally more pressing.

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From regulation to supervision

The new approach had three elements. MAS shifted its emphasis from regulation to supervision. It gave better-managed institutions more freedom to take the risks they were comfortable with, concentrated on minimising systemic risk and imposed restrictions on weak institutions. It left investors to judge business risks for themselves, while raising disclosure standards so that they could make informed decisions. It promoted the financial sector actively, with the vision of developing Singapore into a world-class financial centre. Bank examinations were to focus on risk management processes and internal controls, which would allow more frequent and focused inspections.[3]

The institutional changes followed quickly. In February 1998 the government accepted most of the 55 recommendations of the Finance and Banking Sub-Committee. On 29 June 1998 Parliament passed an amendment to the MAS Act that raised the maximum size of the board from seven to ten directors and made the promotion of the financial sector one of the authority's main objectives. MAS created a dedicated Financial Sector Promotion Department and restructured its supervision group.[4] The change of direction was unusual. In the middle of the worst regional crisis in a generation, Singapore chose to deregulate its financial sector and to compete harder.

Opening the market

The liberalisation that followed is the subject of Chapter D.IV and needs only a brief outline here. On 17 May 1999 MAS announced a five-year programme to liberalise the commercial banking sector, which created a new category of Qualifying Full Banks for foreign institutions and lifted the 40 per cent limit on foreign shareholdings in local banks. The government also planned the demutualisation and merger of the stock exchange and SIMEX, which Chapter D.II describes. The chairman's statement of 1999 summed up the strategy in three prongs: a vibrant asset management industry, deep and broad capital markets and a strong and competitive banking industry.[5]

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The lessons drawn by the government

The government set out its own reading of the crisis while it was still under way. In his Tokyo speech of September 1998, Lee Hsien Loong summarised the approach in a few principles. An economy that depended on external demand could not spend its way out of the downturn and had to become more competitive internationally. Lower costs had to deliver that competitiveness, since a deliberately weaker currency would undermine confidence. Flexible wages allowed companies to keep their workers through a downturn. Restructuring and preparation for the future had to continue in the middle of the crisis. Education and retraining had to prepare the workforce for the industries that would follow, with special attention to older and less educated workers, who faced the greatest risk of losing their jobs. In the financial sector, finally, the state had to maintain high standards of integrity and sound financial management while allowing the private sector to play a larger role.[6]

These principles describe the policy of the following decade as much as the response to the crisis. Their common thread is the conviction that Singapore cannot shelter behind controls or subsidies and must make itself more useful to the world economy. The financial sector became one of the main fields in which this conviction was applied.

Asset management and the role of GIC

Asset management received particular attention. In September 1998 Lee Hsien Loong announced that the Government of Singapore Investment Corporation would place S$25 billion with private fund managers over three years. Licensing thresholds for investment advisers were lowered. Fund managers with more than S$5 billion under management in Singapore received a full tax exemption on fee income. The government also issued ten-year government securities of S$1.5 billion in July 1998 as a benchmark for a domestic bond market.[7] These measures laid the foundations for the wealth management strategy of the 2000s, which Chapter D.V examines.

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The Singapore dollar and the limits of internationalisation

The crisis also prompted a cautious review of the policy of non-internationalisation. In February 1998 the government confirmed the rationale of the policy but announced a review of specific restrictions, mainly to develop the capital markets. By 1999 MAS had adjusted the policy to allow supranational institutions and corporations of good standing to issue bonds in Singapore dollars.[8] Singapore thus kept the core protection against currency speculation that had served it during the crisis. It relaxed only the restrictions that hindered the growth of its own markets, a balance that it adjusted further in the following years.

Notes

1. MAS, *Annual Report 1997/98*, p. 29 (“A Financial Sector Review Group (FSRG) was formed in August 1997”) and p. 64 (set up “in the middle of 1997”, with the aim “to position Singapore as a premier financial centre in Asia, and globally”); MAS, *Annual Report 1997/98*, Chairman's Statement, p. 9. ↩
2. MAS, *Annual Report 1997/98*, Chairman's Statement, pp. 9–11, including the thanks to “my predecessor, Dr Richard Hu”. ↩
3. MAS, *Annual Report 1997/98*, Chairman's Statement, p. 10; MAS, *Annual Report 1997/98*, pp. 29–30. ↩
4. MAS, *Annual Report 1997/98*, calendar of events, p. 21 (18 February 1998), and p. 69 (“MAS accepted nearly all of the 55 proposals”); MAS, *Annual Report 1997/98*, calendar of events, p. 22 (29 June 1998: “increasing the maximum size of the MAS Board from 7 to 10”); MAS, *Annual Report 1997/98*, Chairman's Statement, pp. 10–11. ↩
5. MAS, *Annual Report 1998/99*, section “Liberalising Commercial Banking and Upgrading Local Banks”: programme introduced on 17 May 1999; Qualifying Full Banks; lifting of the 40 % foreign shareholding limit; MAS, *Annual Report 1998/99*, Chairman's Statement, p. 9. ↩

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6. Lee Hsien Loong, speech of 30 September 1998, paras. 10–25, in particular para. 12 (no recovery "by stimulating domestic spending"), para. 13, paras. 16–19, para. 21, paras. 23–24 and para. 25 ("we must maintain the high standards of integrity and sound financial management"; "allowing the private sector to play a larger role"). ↩
7. Lee Hsien Loong, speech of 30 September 1998, paras. 28–29 and footnote 1: full tax exemption on fee income for fund managers with more than S$5 billion managed in Singapore; GIC to place out S$25 billion to private fund managers over three years; minimum shareholders' funds for investment adviser licences reduced from S$500 million to S$100 million; Lee Hsien Loong, speech of 30 September 1998, para. 30. ↩
8. MAS, Parliamentary reply of 19 February 1998 on internationalisation: the government is "reviewing some of the specific restrictions on the use of the Singapore Dollar"; MAS, *Annual Report 1998/99*, Chairman's Statement, p. 9. ↩

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