The Financial Sector Review Group

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A review begun before the storm

The review that transformed the financial sector began as a response to global trends and only later became a response to a regional crisis. According to the Monetary Authority of Singapore, the financial sector review began in August 1997. It arose from the recognition that the rapid growth of the sector over the previous thirty years could not be taken for granted.[1] The previous chapter describes how the Thai devaluation of July 1997 and the contagion that followed gave the review an urgency that its authors had not anticipated.

The public case for the review was made by Deputy Prime Minister Lee Hsien Loong at the tenth anniversary of SESDAQ, the second board of the stock exchange, on 4 November 1997. He noted that financial services had consistently grown faster than the rest of the economy and accounted for 12 per cent of GDP. Incremental improvements to established policies, he argued, would no longer suffice. Two forces drove the change, the first being technology and the second what he called "fierce borderless competition", in which the competitors of a financial centre were now to be found "across the globe".[2]

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Committees, consultants and the private sector

The Financial Sector Review Group was a government body chaired by Lee Hsien Loong, who also signed the MAS annual report of 1997/98 as chairman of the Authority. Its method was to commission work from others, so that MAS set up private sector committees to study specific aspects of liberalisation and engaged McKinsey & Co to conduct a strategic review of the sector and identify opportunities for development. When Lee paid tribute to the contribution of the private sector in November 1998, he named five committees and their chairmen. Peter Seah chaired the Finance and Banking Competitiveness Sub-Committee, Elizabeth Sam the Committee on Banking Disclosure, Lim Yong Wah the Corporate Finance Committee and Lim Hua Min the Stock Exchange of Singapore Review Committee. The Committee on Governance of Exchanges was chaired by Tharman Shanmugaratnam, then an official of MAS and later Minister for Finance.[3]

The use of private sector committees was deliberate. Lee explained that they had helped the authorities "to tap industry expertise, and to develop the industry consensus and common purpose" that the reforms required. The committees allowed bankers, brokers and lawyers to shape proposals that would affect their own businesses. They also committed the industry in advance to reforms that would expose many of its members to competition. In February 1998 the government accepted most of the recommendations of the Finance and Banking Sub-Committee of the Competitiveness Study Committee.[4]

The new philosophy of regulation

The Review Group produced more than a list of measures, since it changed the philosophy of the regulator itself. In his first statement as chairman of MAS, Lee set out three elements. MAS would shift its emphasis from regulation to supervision and give better-managed institutions more leeway to assume the risk profiles they were comfortable with. It would leave investors to judge business risks while raising disclosure standards. It would also promote the financial sector more actively. The statement added that the changes did not signal any slackening of vigilance, since restrictions would be placed on weak or poorly managed institutions.[5]

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The legislature confirmed the promotional mandate within a few months. On 29 June 1998 Parliament passed an amendment to the MAS Act that enlarged the board from seven to ten members and made financial sector promotion one of the Authority's main objectives.[6] MAS also created a Financial Sector Promotion Department and reconfigured its Financial Supervision Group to support the new risk-focused approach. A regulator that had been known for saying no was now charged with building an industry.

Early measures of 1998

The first measures came while the crisis was at its height. MAS required banks to raise their disclosure standards, which meant that they had to stop maintaining hidden reserves and disclose details of their loan loss provisions, off-balance-sheet items and significant exposures. It lowered the minimum cash balance of banks from 6 per cent to 3 per cent, which released liquidity at a moment of regional stress.[7]

The capital requirement for local banks, by contrast, remained demanding. Local banks had been required to hold capital equal to 12 per cent of risk-weighted assets, entirely in Tier 1 capital. From 1 December 1998 MAS maintained the 12 per cent ratio but required only 10 per cent in Tier 1 capital, with the remainder allowed in Upper Tier 2 capital. The international minimum under the Basel Accord was 8 per cent, of which 4 per cent had to be Tier 1. The high ratio was a deliberate cushion that allowed the government to open the market to foreign competition while keeping the local banks among the best capitalised in Asia.[8]

The early measures also reached beyond banking. In February 1998 the Government of Singapore Investment Corporation announced that it would place an additional S$25 billion with external fund managers with offices in Singapore over three years. In November 1998 MAS announced that it would place out S$10 billion of its own over the same period.[9] The mandates were intended to attract asset managers to the city, a strategy whose results Chapter V of this part and Chapter V of Part E examine.

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Notes

1. Monetary Authority of Singapore, *Annual Report 1998/99*, section "Financial Sector Reforms", p. 52: "The financial sector review, which began in August 1997, arose from the recognition that the dramatic pace at which Singapore's financial sector had been growing over the last 30 years could not be taken for granted." ↩
2. Lee Hsien Loong, "New Approach to Regulating and Developing Singapore's Financial Sector", speech at the SESDAQ 10th anniversary, 4 November 1997, mas.gov.sg, paras. 3–4: "Incremental improvements to established policies will not suffice"; financial services "now account for 12% of GDP" – Lee Hsien Loong, speech of 4 November 1997, paras. 8, 10 and 13: "The first driving force behind this revolution is technology"; "The second driving force for change is fierce borderless competition"; competitors "not across the street, but across the globe". ↩
3. MAS, *Annual Report 1997/98*, Chairman's Statement, p. 9: "We set up the Financial Sector Review Group, and commissioned private sector committees to study specific aspects of financial sector liberalisation. We also engaged McKinsey & Co to do a strategic review of the sector" – MAS, media release, "DPM Pays Tribute to Private Sector Contribution to Financial Sector Reform", 27 November 1998, mas.gov.sg: list of the five committees and their chairmen; Lee Hsien Loong identified as "the chairman of the FSRG". The release names Tharman Shanmugaratnam without a title – Wikipedia, "Tharman Shanmugaratnam" (accessed November 2026): he "resigned as managing director of the MAS to contest in the 2001 general election". ↩
4. MAS, media release of 27 November 1998: the committees "helped to tap industry expertise, and to develop the industry consensus and common purpose" – MAS, *Annual Report 1997/98*, calendar of monetary and financial events, p. 21: on 18 February 1998 "The government accepts most of the recommendations of the Finance & Banking Sub-Committee of the Competitiveness Study Committee to liberalise the financial sector.". ↩

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5. MAS, *Annual Report 1997/98*, Chairman's Statement, p. 10: "First, MAS is shifting its emphasis from regulation to supervision … Second, MAS will leave it to investors to judge business risks … Third, MAS is promoting the financial sector more actively." – MAS, *Annual Report 1997/98*, Chairman's Statement, p. 10: "These changes do not signal any slackening of supervisory vigilance … Restrictions will be placed on weak or poorly managed institutions". ↩

6. MAS, *Annual Report 1997/98*, calendar of monetary and financial events, p. 22 (29 June 1998): the MAS (Amendment) Bill 1998 increased "the maximum size of the MAS Board from 7 to 10" and included "financial sector promotion as one of MAS's main objectives". ↩

7. MAS, media release, "Financial Sector Remains Resilient Despite Slowdown; MAS' Efforts to Reform the Sector on Track and Reaping Results", 24 August 1998, mas.gov.sg: "Raised Bank Disclosure Standards" (no hidden reserves, disclosure of provisions, off-balance-sheet items and significant exposures); "Lowered Minimum Cash Balance (MCB) from 6% to 3%". ↩

8. MAS, *Annual Report 1998/99*, p. 54: "Previously, local banks had to maintain a CAR of 12%, comprising entirely Tier 1 or equity capital … with effect from December 1998, local banks are required to have at least 10% Tier 1 capital, while the remaining 2% may consist of Upper Tier 2 capital." – MAS, media release of 27 November 1998: CAR of 12 per cent with at least 10 per cent Tier 1 effective 1 December 1998, compared with the BIS standard of 8 per cent CAR and 4 per cent Tier 1. ↩

9. MAS, *Annual Report 1998/99*, p. 55: in February 1998 GIC announced it would place out "an additional $25 billion over the following three years to external fund managers who have offices in Singapore"; in November 1998 MAS announced it would place out "$10 billion over the following three years". ↩

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