Keynote Speech by Ms Jacqueline Loh, Deputy Managing Director, MAS at the Inaugural DBS Institutional Investor Symposium on Friday, 24 June 2016 at the National Gallery, Singapore

Distinguished Guests, Ladies and Gentlemen

Introduction

1. Good afternoon. It is my pleasure to join you today for the inaugural DBS Institutional Investor Symposium at the National Gallery. The theme of this Symposium, "The Art of Seeking New Investment Value" is apt for both the investment climate we face, and the venue where we are gathered. The National Gallery is a vibrant centre bringing together the best modern artists and influences from Asia and beyond. As the financial gateway to Asia, Singapore also convenes the global investment community who are eager to explore investment opportunities in the region.

2. Before I continue, I would like to briefly address today's outcome of UK's referendum on EU membership. Following the UK's vote to leave the EU today, both the Pound and UK equities have weakened by about 5 to 10%. Risk assets globally have also fallen, with Asian currencies and equities also affected.

3. We have been prepared for the market volatility. MAS had been in close contact over the past weeks with banks in Singapore, foreign central banks and regulators to take preparatory actions to ensure the resilience of our financial system and markets in the event of Brexit.

4. Singapore's interbank money markets continue to function in an orderly manner and its banking system remains sound, following the outcome of UK's referendum.

5. The liquidity positions of the major banks in Singapore are healthy, and overall banking system liquidity remains adequate. MAS will provide additional liquidity to the banking system if needed.

6. The trade-weighted Singapore dollar remains within its policy band, notwithstanding heightened volatility in international foreign exchange markets today. MAS stands ready to curb excessive volatility in the Singapore Dollar.

7. MAS will continue to be vigilant and stay in close contact with fellow central banks and regulators, as uncertainty is likely to persist following the referendum outcome.

8. Beyond the initial turbulence, we will need to assess the wider economic implications for the region and Singapore. It is too early to make a firm call on what the referendum result would mean for prospects for a modest recovery in the global economy in the second half of this year.

9. While we need to avoid excessive pessimism, there is undoubtedly some impact to be expected on confidence and sentiments. Nevertheless, our region has continued to see relatively steady growth this year, including from resilient domestic demand.

10. Moreover, the region's underlying fundamentals remain generally healthy. There are buffers in place to cushion the impact from shocks and we should not lose sight of the medium term potential and investment opportunities that the region offers.

11. Today, I would like to share some observations on the investment landscape and how institutional investors can capitalise on these opportunities.

Global investment landscape

12. Most of us here will be familiar with the concept of peak oil – the idea that oil extraction will hit a maximum rate at some point and begin to decline. Since as early as the 1910s, there have been oil experts calling for an imminent occurrence of peak oil. Yet, more than a century has passed but it is still not evident that we have reached this peak. This has been due to a series of technological advances, including, most recently, improvements in horizontal drilling and fracking that have brought shale oil to the market.

13. My remarks today will not be on oil, but there is a parallel to the situation that confronts investors today. We are familiar with the refrain that we have passed the golden age of asset returns. In other words, we may have hit the 'peak oil' of asset returns. There are many good reasons to believe that the returns of the coming decade will be lower than the preceding two. But the investment community is not standing still. It is striving to unlock as much return as markets have to offer.

14. Let me briefly touch on three pivots that investors have been employing, to avoid the scenario of 'peak asset returns':
    - First, a pivot towards alternative strategies and assets
    - Second, a pivot towards an increasing emerging markets exposure
    - Third, a pivot towards smarter use of technology

Pivot towards alternative strategies and assets

15. First, **pivoting towards alternative strategies and assets**.

16. Alternative strategies have risen in prominence in recent years. The most visible example has been the move away from market-cap benchmarks, towards alternative-weighted benchmarks. Factor-based investing and smart-beta have been the key buzzwords of this move. MSCI estimates that more than US$500 billion is currently invested in smart beta equity strategies, compared to only US$20 billion in 2011. This represents a 25 times increase over 5 years. And this figure is likely to increase. A survey by FTSE Russell showed that global institutional investors evaluating smart beta has more than doubled to 36% in 2016, from 15% in 2014. The rise in smart-beta adoption reflects investors' attempt to reach for higher returns on the one hand, while aiming to keep implementation costs low on the other hand.

17. The search for higher returns and greater diversification has also shifted the balance from traditional assets towards alternative assets such as real estate, private equity and infrastructure. McKinsey estimated that alternative assets have grown twice as fast as traditional assets since 2005, to around US$7.5 trillion currently. Specifically on infrastructure investments, the Asia Pacific region should play a significant role, given that its capital project and infrastructure market is expected to reach nearly US$5.3 trillion, or 60% of the global share, by 2025[1].

Pivot towards an increasing emerging markets exposure

18. This leads me to the **second pivot, which is towards an increasing emerging markets exposure**.

19. Fundamentally, a gradual increase in emerging markets asset exposure over the long term would be in line with the increased weight of emerging economies in global economic activity. Emerging markets' share of global capital markets is

[1] PwC (2014), "Infrastructure development in Asia Pacific (APEC) The next 10 years"

expected to roughly double by 2030, from their current levels of around 20% of the global equity markets and 15% for bonds. Two drivers are likely to underpin the growth of the emerging markets share of capital markets. First, the process of capital market deepening. As capital markets in emerging economies mature and become increasingly open to capital flows, their size as a percentage of GDP should grow over time. For instance, the book value of equity in emerging markets is likely to narrow the gap between its current level of around 30% of GDP towards developed markets level closer to 60%. The second driver will be the extent to which GDP of emerging economies grows faster than developed economies. Although the differential between their growth rates has narrowed in recent years, emerging economies are still expected to grow at an average of 4.7% per year in the next 10 years, compared to 1.9% for developed economies.

20. Although there is clearly a long-term case for increasing emerging markets exposure, the near term outlook for emerging markets may continue to bumpy, given potential headwinds from US rate normalisation and continued uncertainty over commodity prices. However, navigating these challenges well in the short run, paired with progress in structural reforms, should provide emerging economies with a firmer macroeconomic foundation in the long run. Moreover, the silver lining to emerging markets underperformance in recent years is that their valuations are starting to look attractive relative to that of developed markets.

21. Independent of the cyclical outlook, there are also persistent opportunities to seek outperformance within the emerging markets universe, due to the relatively wide dispersion of returns across markets. For example, a study by Morgan Stanley found that the country risk factor contributed 67% of total returns in the MSCI Emerging Markets Index, versus only 35% for developed markets, with style and industry factors being the other contributing factors. Investors who make

differentiated investments on the basis of individual country analysis could benefit from this dispersion of returns.

<u>Pivot towards smarter use of technology</u>

22. This leads me to my next point – **pivoting towards smarter use of technology.**

23. Investors and analysts are starting to leverage on big data analytics in their investment processes. Use cases for data analytics in the area of macroeconomic analysis and investment are only just beginning to emerge, and there is much promise. Researchers from the Massachusetts Institute of Technology (MIT) recently produced a paper showing found that investing using data from Twitter can significantly outperform a passive strategy. Another team from MIT co-founded PriceStats, which uses online prices to provide daily inflation updates, perhaps a first step towards real-time monitoring of economic activity.

24. The use of big data tools has gained traction in developed economies due to the abundance of readily accessible data for use. However, the need to augment analyses of conventional economic data with unconventional data sources is in fact greater in emerging economies, due to the relatively smaller and less frequent set of official data releases. Digital data in emerging economies is expected to grow tremendously, with increasing smart phone penetration and usage being key drivers. In time, this growth of digital data in emerging economies may help to overcome the challenges that arise from the relatively fewer traditional economic data releases. However, headway certainly needs to be made in applying big data tools to emerging economies' datasets for that to happen.

25. I have touched briefly on three shifts that investors are making – towards alternative assets and strategies, towards emerging markets exposures and applying technology to investment. These shifts should mean that investors will naturally demand a combination of wider product diversity, deeper skills and expertise and smarter use of technology. Let me elaborate on how Singapore is developing in these areas.

Building up the asset management ecosystem

26. Over the years, Singapore has continuously built up a broad base of financial investment and risk management capabilities spanning both traditional and alternative strategies. Many of the top global fund managers are already present in Singapore. Assets under management has continued to register good growth in both traditional and alternatives. In keeping with Singapore's role of intermediating international capital flows, about 80% of total assets are sourced from investors outside Singapore and mostly invested into the region.

27. The diversity of institutional investors in Singapore has increased, with sovereign wealth funds and pension funds from Asia, Europe and North America setting up investment offices here to tap the deep Asian market expertise in Singapore and diversify their portfolio investments. Such long-term investors can play a positive role in fostering economic and financial market development. They are a source of long-term capital that can help to fund infrastructure development, and bring expertise and different market perspectives that can help to promote efficient markets in the region.

Broadening the product suite for investors

28. As institutional investors pivot to Asia, they will need a wider diversity of investible products and risk management solutions. I would like to highlight some of these opportunities in Singapore.

29. First, **Singapore's debt capital market continues to be vibrant** and features a wide range of issuers in both Singapore Dollars and foreign currencies. Investors are able to access a variety of bonds issued by corporates, denominated in G3 as well as in Asian currencies. Asian bond markets offer a useful alternative to the bank lending channel and are expected to grow, as Asian issuers including Chinese and Indian corporates continue to tap the fixed income market for their funding needs:

- RMB product offerings will broaden here in Singapore, with the expansion of cross-border RMB initiatives between Singapore and China, whereby corporates in Suzhou, Tianjin and Chongqing can issue RMB bonds in Singapore and have more flexibility to fully repatriate the proceeds onshore;

- India's immense need for funding can be financed via international capital markets. The Reserve Bank of India has announced a framework in September 2015 to allow Indian companies to tap the international capital market in Rupees, thereby removing foreign currency risk from the issuers. Singapore is a familiar destination for Indian issuers and we expect offshore Rupee-denominated bonds to be added to the pool of Indian credits available in Singapore.

- We also expect to see more covered bond issuances in Singapore as issuers develop their expertise in this fixed income instrument. DBS Bank priced the first Singapore benchmark in covered bonds in July last year, which was well-received by investors. This sets the foundation for Asian institutions with large mortgage portfolios to access a diversified and stable investor base.

30. **The second significant opportunity is in infrastructure finance**. Asia's infrastructure needs are vast. To meet demand, Asia must unlock new sources of

financing and diversify beyond government funding and bank lending. While infrastructure assets can offer long-dated and inflation-protected returns, many investors have held back due to information asymmetry and lack of access to investment opportunities.

- So to improve transparency and enhance understanding of infrastructure as an investible asset class, Singapore is working closely with the EDHEC Infrastructure Institute to develop performance benchmarks for infrastructure debt and equity. This will facilitate the progression of infrastructure into a distinct, investible asset class, which will feature more prominently in strategic asset allocation decisions;

- To improve investor access to investment opportunities, MAS is working with banks and investors to develop an infrastructure debt takeout facility that will allow the transfer of infrastructure debt from banks to institutional investors in a structured and institutionalised manner. A group of banks and investors have agreed to undertake a "proof of concept" pilot transaction this year, which will provide useful learning points for the operation of this facility.

31. Third, as they expand into the region, **institutional investors would increasingly need to access Asian foreign exchange (FX) risk management solutions in the Asian time zone**. In this respect, buy-side investors can tap on Singapore's well-developed foreign exchange market, which stands at the third largest in the world.

- In addition to the over-the-counter market in foreign exchange, Singapore offers global investors a suite of Asian currency futures contracts on the Singapore Exchange and ICE Singapore. Reflecting the healthy demand for Asian FX futures, SGX and EBS have also entered into a partnership to distribute SGX block futures on EBS' Market platform soon. This will allow institutional investors to carry out hedging using futures on a bigger scale.

- Efficient price discovery and deep market liquidity will be important factors for investors in Asia. We are building Singapore into the Asian FX electronic trading hub by working with industry players that are keen to set up key market infrastructure such as e-trading platforms and matching engines. This will significantly improve trade execution, latency and pricing for Asia-based investors, and anchor price discovery of Asian FX in Singapore.

<u>Smarter use of technology</u>

32. Let me say a few words on financial technology or FinTech. MAS has expressed the vision of a Smart Financial Centre where technology is used widely to increase efficiency, create new opportunities, manage risks better and improve people's lives. Within asset management, increasing use of technology and innovation have the potential to raise the efficiency of financial institutions in this industry, broaden their reach to new market segments in Asia, and enhance investment returns. As I mentioned earlier, investors have begun to look at more powerful computing systems that can analyse vast amounts of data to reveal new investment opportunities and improve trading performance. "Robo-advisors" employing data analytics and artificial intelligence are empowering a wider spectrum of investors to make better informed decisions based on more timely and customised advice. While the industry is still at an early stage, there is significant scope for more innovation in the asset management business over the next few years.

33. **MAS is fully committed to building up the FinTech ecosystem in Singapore**. We are collaborating with the global FinTech community to create more opportunities for innovation, and develop the skills and capabilities in Singapore to turn this

potential into reality. In November, we will host the first Singapore FinTech Festival, a week-long series of events including the FinTech Conference, FinTech Awards and Global FinTech HackCelerator. For the HackCelerator, you may know MAS has published 100 problem statements developed by the industry[2]. About 20% of the problems identified relate to portfolio management and capital markets. I would like to invite you to join in the process to source for solutions that are directly applicable to you and partner with the participating FinTech teams.

Developing deep skills and expertise

34. As Asia becomes more important as a source of return for investors, demand will grow for investment professionals with:

- Strong quantitative skills and multi-asset investment capabilities;
- Deep knowledge and expertise in Asian markets; as well as
- Information technology (IT) management skills to harness the power of technology in research, portfolio construction and implementation

35. **Developing talent must be a top priority for the asset management industry in Singapore.** MAS places great emphasis on talent development in the industry. We work closely with many of you to develop a comprehensive set of *SkillsFuture* initiatives to build talent that is deeply skilled, versatile and equipped with Asian market expertise to support the growth of the asset management industry.

Conclusion

36. In facing the possibility of having passed the peak of asset returns, institutional investors are innovating to push the returns frontier further out. As a progressive

[2] The problem statements can be downloaded at http://www.fintechfestival.sg/hackcelerator/

and innovative financial centre, Singapore has much to offer to global investors in opening the door to new markets and investment opportunities in Asia.

37. On that note, I am glad that DBS Bank has decided to launch its Institutional Investor Symposium in Singapore this year. I hope that many of you will return to Singapore for even more fruitful and useful discussions. Thank you.