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Introduction

Ladies and gentlemen. It is my pleasure to be invited to deliver the opening address at this conference on Globalisation of Financial Services.

Financial globalisation

2 The organisation of this conference is a timely one, as the globalisation of financial services has assumed greater significance in the last two decades. For one, the scope of financial globalisation has expanded tremendously, as a growing number of countries are globalising their financial markets, and as a wider range of financial activities are involved. For another, financial globalisation has resulted in fundamental changes in the structure of both domestic and international financial markets, with far-reaching implications for macro-economic management.

3 The acceleration of financial globalisation in the last few decades has been due to a number of factors. First, advances in technology has facilitated faster informational flow, which has fostered the growth in financial trading activities across different markets. Second, the greater sophistication of financial market participants has resulted

in increased demand for risk diversification, thereby fostering cross border financial transactions. Third, an increasing number of countries have liberalised their financial markets so as to mobilise domestic savings and foreign capital more effectively for economic development.

Asian Financial Markets

4 As the Asia Pacific has been growing rapidly in recent years, it is natural that globalisation of financial services has become an increasingly prescient development in this region. With the growth in regional trade and investment activities, it is not surprising that cross border trade in financial services has also grown. The globalisation of the financial sectors in Singapore and Hong Kong has followed this mould. Given their highly open, trade-based economies, financial markets in both city states were in a good position to expand through financing regional economic trade and investment.

5 The liberalisation of the Japanese financial market from the mid 1980s provided a significant boost to the globalisation of financial markets in Asia. Financial liberalisation in Japan made possible the overseas expansion of its financial institutions, resulting in the growth of international banking, foreign exchange and securities market activities in this region. In addition to this push factor, a pull factor also operated to promote financial globalisation in Asia. More Asian countries have adopted an open door policy on the financial sector, so as to facilitate

international financial flows, and foreign participation in their financial markets. The financial liberalisation measures that were undertaken included lifting of controls on interest rates, foreign exchange transactions, and revamping of domestic securities markets.

6 The experience of financial globalisation in Asia has undoubtedly been positive, as those countries which have participated have reaped considerable benefits from the process. First, financial globalisation in Asia has served to make domestic financial markets more closely interlinked with international financial markets, thereby increasing their access to international capital. One key development in this area has been the rapid growth of securities markets in developing Asian countries, which has facilitated greater foreign investment in domestic enterprises.

7 Second, financial globalisation has contributed to raising the value added per worker, and hence per capita income, of the economy. This is because the financial sector is a high value added activity, requiring professionals and workers who are well educated and possess the necessary financial skills and expertise. This has resulted in the growing importance of the financial sector in the economy.

8 Third, financial globalisation has, by exposing domestic markets to international competition, contributed to their efficiency. As result of advances in technology and greater sophistication of customers, financial institutions are now

able to provide cross border financial services more readily. If domestic financial institutions do not upgrade or improve the efficiency of their services, they would experience a loss in their share of the financial market.

Singapore's Experience In Globalisation

9 I would like to turn to Singapore's experience in the globalisation of its financial services sector. The development of our financial sector can be traced to the late 1960s. The Singapore government then decided that the sector could play a useful role in serving regional and international financial needs, over and above its role in serving the domestic economy. First, it was felt that Singapore had several natural advantages in functioning as a financial centre for the region. These included the island's strategic location, modern telecommunications infrastructure, well educated workforce and stable political system. Second, it was realised that the small size of the domestic market would severely limit the development of a modern, competitive and innovative financial market in Singapore. This meant that our financial sector had to focus on serving regional financial needs in order to develop.

10 A crucial prerequisite for the globalisation of the Singapore financial sector was the development of a c itical mass of professionals with the necessary financial skills and expertise. To facilitate the transfer of sophisticated financial skills to our market, the government implemented a number of key policies. For example, efforts were made to

encourage reputable international financial institutions to establish their regional operations in Singapore. Immigration rules were liberalised to facilitate the employment of experienced foreign expatriates in our financial market. In addition, efforts were made to provide a pool of well educated workforce for the financial sector. This has included the establishment of a specialist financial sector training institute, the Institute of Banking and Finance, to provide on-going training and skills upgrading for financial sector employees, particularly in high valued activities such as risk and fund management.

11 The success of such efforts is clearly reflected in the diversity and depth of the Singapore financial sector, which today accounts for 17% of GDP and 4% of total employment. The mainstay of the Singapore financial market is the Asian Dollar market, which is a US$350 billion deposit and loans market in international currencies. The market has its origins in the early 1970s, when a growing number of international banks established offices in Singapore to conduct regional lending and deposit taking activities, in view of Singapore's strategic location and the growing pool of liquidity in the region.

12 The development of the Asian Dollar market has played a key role in the globalisation of financial markets in Singapore and the region. About 75% of transactions in the Asian Dollar market today are interbank transactions with banks located in the major financial centres. Such a heavy international content in the market has meant that Singapore

and regional companies would have ready access to international capital. The Asian Dollar market has, by acting as a channel for international capital flows into the region, played a key role in financing regional trade and economic development.

13 The globalisation of the Singapore financial sector has also been reflected in its development as an international foreign exchange trading centre. Following the lifting of exchange controls in the 1970s, the foreign exchange market experienced strong growth as a result of buoyant economic growth in the region and Singapore's strategic time zone location. Average daily turnover in the foreign exchange market has risen to about US$80 billion, making Singapore among the top 5 foreign exchange trading centres in the world. The growth of foreign exchange trading activity in Singapore accelerated after the liberalisation of financial markets in Japan in the mid 1980s, illustrating the positive impact that financial liberalisation in one market can have for other markets.

14 The establishment of the Singapore International Monetary Exchange (SIMEX) in 1984 also marked an important milestone in the globalisation of Singapore's financial sector. SIMEX was established to provide risk management services to international investors. It is unique among international financial futures exchanges as it does not offer any domestic based contracts. Instead, SIMEX's growth, which has been spectacular, has been based entirely on international

contracts, such as Eurodollar interest rates, Euroyen interest rates, and the Nikkei stock index, which are also traded on other exchanges. SIMEX is a good example of the process of financial globalisation. The mutual offset arrangement between SIMEX and the Chicago Mercantile Exchange (CME) essentially provides for a single trading floor between the two exchanges, thereby facilitating round the clock trading by investors in the respective time zones. Through the mutual offset system, the financial markets in the US and the Asian time zone have been more closely linked. SIMEX's success in functioning as a link in the global trading chain is due to two factors, namely the efficiency and competitiveness of the exchange, and its reputation for integrity and sound regulation.

15 Another sector of the Singapore financial market that has experienced a high degree of internationalisation has been the securities broking and fund management industry. In the last several years, strong economic growth in Asia had resulted in a rise in international investor interest in Asian securities markets and companies. Given the critical mass of activity already being conducted from Singapore, international fund managers and securities dealers found it advantageous to base their regional investment and dealing activity in Singapore. The globalisation of the fund management and securities dealing markets in Singapore has also resulted in a number of benefits for regional economies. For one, regional companies could take advantage of the international placement power of the international broking companies in Singapore to tap the

international capital market more efficiently. In addition, regional companies could also increase their informational flow to the large pool of international fund managers in Singapore. Given the international links of such fund managers, this would enhance the profile of regional companies among international investors.

16 In this regard, a number of initiatives have been taken to raise the level of capital resources and professional expertise in the securities industry, in order to foster Singapore's capabilities as a centre for the trading and underwriting of regional share issues. I note that the Stock Exchange of Singapore (SES) would raise the minimum Adjusted Net Capital (ANC) requirement for member stockbroking companies from $3m to $8m. In line with this, we would relax the existing statutory limits to enable better capitalised SES member companies to take on larger underwriting commitments and act as market makers on a wholesale basis for SES and regional stocks. SES member companies are presently subject to a underwriting limit for Initial Public Offerings (IPOs) of 10% of their ANC. This limit would be raised to 100% for companies which have ANCs of below $50 million, and to 150% for companies which have ANCs of $50 million and above. In addition, the investment limit would be raised for better capitalised SES member companies to enable them to function as market makers and thereby contribute to greater liquidity. The investment limit for those member companies with ANCs of $50 million or more would be raised from the current 150% to 300% of their ANC. The investment limit would remain

unchanged at 150% for companies with ANCs of below $50 million.

17 The SES has also launched a number of other initiatives to attract sophisticated international investors to the Singapore capital market. It plans to broaden the market by introducing stock options trading by the fourth quarter of this year. In addition, to enable investors to undertake a broad range of stock options trading strategies, the SES would establish a scrip borrowing and lending market for stocks traded on the exchange.

18 Based on Singapore's experience, there are a number of benefits to countries which globalise their financial markets. First, globalisation would bring about greater access to developments in international financial technology and skills. The openness of the Singapore financial sector, for example, has helped to foster a pool of expertise in sophisticated financial risk management activities, such as financial derivatives trading. Second, globalisation has served to enhance the efficiency of the financial sector by exposing Singapore financial institutions to international competition. Third, financial globalisation in Singapore has served to raise value added and hence salaries in the financial sector. This has resulted a influx of professionals and workers from other sectors to the financial sector.

Systemic Risks

19 Although globalisation of financial services has

considerable benefits, it has also resulted in a whole new ball game for financial regulators. One consequence of financial globalisation is increased interdependence among financial markets. This means that financial shocks in one market can easily be transmitted to other markets. For example, a loss in depositor confidence in a bank in one market can easily be transmitted to a similar diminution of confidence in the branches or subsidiaries of banks in other markets. Another example is the collapse of US stock market in October 1987. Even though the Singapore economy was performing well during this period, our securities market fell much more sharply than other markets in percentage terms, reflecting the high degree of foreign investor participation in our market.

20 The dilemma which faces regulators is how to minimise the impact of international disturbances on their domestic financial markets, while continuing to maintain close links with the global financial system. In order to ensure the soundness of the domestic financial system in the face of potential international shocks, it is first necessary to ensure that domestic market is itself resilient and able to withstand external disturbances. This means that domestic financial institutions have to be financially sound, and conduct their activities prudently and professionally. In Singapore, the stock exchange and SIMEX were both able to weather the October 1987 crash without adverse consequences because of their deep financial resources and prudent risk management policies.

21 The globalisation of financial markets has had two major implications for the conduct of financial regulation. First, increased interdependence among financial markets, and the systemic implications of any collapse of one financial market for the global financial system, have made it important for national regulators to co-ordinate more closely their supervisory actions. Second, the growth of international activities of financial institutions has made it necessary for regulators to establish uniform supervisory standards. This is aimed at ensuring that financial institutions do not take advantage of jurisdictions with lax regulatory standards to conduct their international activities or to avoid effective supervision.

22 In this regard, a number of notable measures have been taken by regulators of the major industrialised countries under the auspices of the Bank for International Settlements (BIS). First, the BIS has issued minimum capital ratio guidelines of 8% to ensure that banks have sufficient capital as cushion against adverse developments. Second, BIS has emphasized the importance of consolidated supervision, ie the need for home regulatory authorities to supervise more closely the overseas subsidiaries or branches of their domestic financial institutions, as developments in such operations could have an impact on the overall well being of the domestic institution. Third, the BIS has revised its guidelines for more effective co-ordination of supervisory responsibilities of various national regulators in the light of the BCCI experience. One of the key provisions is that only banks

which are effectively supervised by a capable home regulator would be allowed to establish operations in other financial markets. The new BIS rules also specify that member regulatory authorities should not allow their banks to operate in offshore centres which do not have adequate financial supervisory framework.

23 Singapore's reputation as a well regulated and sound financial centre has been due in no small way to our stringent admission standards for financial institutions. As the financial business is an activity that is critically dependent on the confidence of investors and depositors, it is crucial for any financial centre to ensure that its financial institutions uphold high standards of professional and ethical conduct. As an international financial centre, Singapore has to ensure that its supervisory policies are in line with international standards. Hence, we would be implementing a number of adjustments in our regulatory policies to reflect international regulatory developments, and to ensure the continued soundness and integrity of our financial system. In this regard, to maintain the financial soundness of the locally-incorporated banks in Singapore, local banks would be statutorily required to maintain a minimum capital adequacy ratio of 12%. Presently, the local banks have capital ratios in excess of 13% and they therefore should not experience any difficulty in meeting the statutory minimum. In addition, in line with BIS standards, measures would also be taken to reduce the proportion of loans that can be extended by a bank to a single customer from 30% to 25% of the capital base of

the bank as recommended by BIS. Finally, Singapore would also be implementing measures to provide for more effective consolidated supervision of the overseas branches and subsidiaries of domestic financial institutions.

24 The process of financial intermediation is a constantly evolving one, and financial regulators likewise have keep up with financial innovations and developments in order to control the risks arising from new financial activities. In recent years, there has been an explosion in financial derivatives trading as a result of advances in technology. Regulators in a number of advanced economies have recently urged senior management of financial institutions to be aware of the risks involved in derivatives trading and to enforce stringent management control of such risks. The need for prudence in dealing with financial derivatives cannot be overemphasized, as given the rapid growth and global reach of such activities, any financial crisis arising in the area of derivatives trading could undermine the integrity of financial markets.

25 I would like to make one further point on the potential pitfalls of financial globalisation. The process of globalisation is often equated with the roll-back of prudential standards and controls, in addition to the lifting of restrictions on the free operation of market forces. This assumption could not be more wrong. In order to preserve the integrity of domestic financial markets, financial globalisation has to be accompanied by more effective and

stringent application of prudential standards. The reason for this is that the lifting of market restrictions, such as in the case of the thrift industry in the US or the banking sector in some Scandinavian countries, often results in greater freedom of financial institutions to undertake risk. In the highly competitive environment that often accompanies financial liberalisation, financial institutions can easily go overboard in aggressively expanding their operations and undertaking high levels of risks in order to gain market share. This build up of risk in the financial system would be exacerbated if monetary conditions were eased, as easy credit conditions could easily result in the creation of speculative bubbles. As emerging economies, countries in Asia would need to ensure that prudential and regulatory standards are strengthened and stringently enforced during financial liberalisation programmes, in order to maintain international investor confidence in their markets.

26 Thank you.

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