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**OPENING ADDRESS BY MR LEE SUAN HIANG, CHIEF EXECUTIVE,
PRODUCTIVITY AND STANDARDS BOARD, AT THE SEMINAR ON
ECONOMIC VALUE ADDED FOR LOCAL ENTERPRISES ON 7 SEP
2000 (THU) IN PSB AUDITORIUM, BUKIT MERAH AT 9.00 AM**

Good morning
Distinguished guests
Ladies and gentlemen

On behalf of the Productivity and Standards Board, I am pleased to welcome you this morning to the seminar on Economic Value Added for Local Enterprises.

Open Economy: Competition for Investments

Singapore has one of the most open economies in the world, which, together with our small size, renders us highly vulnerable to external developments beyond our control. This was clearly evident when Singapore's economic growth slowed down sharply in 1998 as a result of the fallout from the financial crisis that hit our neighbouring countries. Not only were investments curtailed and funds withdrawn from the region, prices in our property market contracted, with commercial property prices declining at double-digit rates. The stock market's performance also hit a low. Our external trade for 1998 shrank by 7.5% to \$354 billion, sharply lower than the 5.7% growth registered in 1997. This was the first decline since 1986.

As you know, our small and medium-sized enterprises (SMEs) felt the full impact of the recession. Reduced asset values, bad debts, low demand and cash flow problems seriously hurt SMEs. Fortunately, the economic crisis also brought out the best in everyone. National consensus was achieved on implementing a series of painful, but necessary, cost cutting measures that boosted our economic competitiveness last year. One lesson we have learnt from the crisis is that our local enterprises must put an end to sub-optimal utilisation of their capital resources.

Importance of Cost of Capital

During the 1998 recession, some SMEs found that the big factories they had built were under-utilised and the sales they had made became bad debts. Others diversified into non-core areas but returns were not good. All these were the result of the companies not taking into consideration the cost of capital before they made their investment decisions. The message is clear - companies should not treat capital as abundant and free. They have to account for the way capital is used. They have to ask themselves if they are creating value because if they are not, they are actually destroying value. There is a management tool that will enable companies to measure their financial performance taking into consideration the cost of capital. It's Economic Value Added or EVA.

A study conducted by KPMG Consulting in 1998 showed that about half of the Singapore mainboard-listed manufacturing companies have 'destroyed' shareholder value over the long term. For the 1997 fiscal year alone, 56% reported negative EVA. The study pointed out that the argument "big is good" is a fallacy. Many companies classified as large in terms of sales and assets had low EVA ranking. Asset intensive companies also did not perform well. Hence, the message is clear - to perform well, companies need to make efficient use of their capital investments, and not just accumulate assets for the sake of doing so. Companies obviously do not intend to consume resources and destroy wealth. The fact is that many may not even realise they are doing so, simply because conventional performance measures often do not present the true result. Often the first thing an SME does the moment it is successful is to buy a big building. My message to such SMEs this morning is before you do that, think of EVA.

The Impact of EVA on Companies

EVA encourages a mindset change from treating capital as free to attaching a cost to the capital invested. A business creates value only when the profit it makes is greater than the total cost of its capital. Companies, both large and small, can implement EVA. The application of EVA encourages managers to use resources more effectively by focusing their attention directly on the costs associated with such items as inventories, receivables and capital equipment

Improving EVA helps ensure that sources of funds will be available when required. Companies also become more conscious of getting optimal returns for their investments. EVA is easy to understand and apply as only key data in the income statement and balance sheet are needed.

At the national level, the application of EVA brings about better 'resource

reallocation' between different industries and raises our Total Factor Productivity. PSB, therefore, aims to promote EVA widely to the companies, particularly the small and medium-sized enterprises (SMEs). Under the SME 21 Plan, EVA has been identified as a proven tool to bring about more effective use of capital.

EVA in practice

EVA has been practised widely in the United States and Europe. It is gaining importance in the Asia Pacific region. *Fortune* magazine reported that firms which use EVA to guide their business operations, have increased the value of their companies. Investors with knowledge of EVA have grown richer.

In Singapore, organisations like the Temasek Group, the Singapore Technologies Group and the PSA Corporation, have successfully applied EVA and reported improved performance. For instance, as part of the EVA implementation, Singapore Food Industries saved over \$250,000 in annual repair and maintenance costs through skills upgrading of its maintenance team and reduction in outsourcing; while SAFE Superstore managed to reduce its manpower cost by 25% through streamlining its operations.

Promoting EVA to Local Enterprises

Three of the promising small and medium-sized enterprises which PSB has helped to implement EVA are Krislite Pte Ltd, Magnificent Seven Corporation Pte Ltd and Tru-Marine Pte Ltd. They have benefited from the EVA implementation and will share their experiences and insights later at this seminar. Singapore Food Industries Ltd, an early adopter of EVA, will share how the concept has worked for them. PSB has developed an EVA package comprising a primer, implementation guide, VCD, posters and jogger cards to facilitate the adoption of EVA by more local enterprises. With this audio-visual package, our SMEs will be able to better understand and implement EVA.

Conclusion

I hope the success stories of the three pilot companies will inspire you to adopt EVA as part of your company's performance measures. The overwhelming response and support for this event is a good indication that there are many enterprises interested. I wish all of you a fruitful morning.

Thank you.

For more information, please contact :

- **Ms Ho Chow Pheng, Corporate Communications, PSB**
Tel: 279 3770, Fax : 278 5414 or e-mail: hcpheng@psb.gov.sg
- **Ms Kalaivani Ramu, Corporate Communications, PSB**
Tel: 279 3913, Fax : 278 5414 or e-mail: kalai@psb.gov.sg

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