Competing International Financial Centers:

A Comparative Study between Hong Kong and Singapore

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– Singapore as a Financial Centre: Development and Prospects)

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Abstract

The strong growth enjoyed by the Asian Pacific economies has given rise to the development of several financial centers in the region. Tokyo is regarded as the leading financial centre of the East while Singapore and Hong Kong are in the race to become the next largest international financial centre (IFC). The changing fortunes and developments of the East Asian and South East Asian economies have created exciting opportunities as well as potential threats for Singapore and Hong Kong as financial centres.

A review of the literature shows recent descriptive studies on financial centers that include Choi and Tschoegl (2000) and Schenk (2002). This paper presents a descriptive snap shot of the developments and performances of the two competing economies as international financial centres. Another objective of this paper is to review the policies and recommendations made by various committees and identify niche areas to further develop the financial sector in Singapore. This is in line with the government's policy to strengthen Singapore's status as a pre-eminent financial centre (Economic Review Committee 2002). Further research can be extended from studies by Schenk

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(2002), Ngiam (1996) and Ng (1998) to investigate the socio-economic, regulatory effect amongst other variables that help to attain a financial center status.

SECTION 1 - INTRODUCTION

The ongoing competition between Singapore and Hong Kong can be traced back to the days of their entrepot status. Both economies had similarly been under the British colonial rule in the past and had earned a reputation for being the trading centres of the East. There has been a shift in their focus from manufacturing and trading industries to the services sector, in particular the financial services industry.

With the onset of the Asian currency crisis since July 1997, the burst of the dot-com bubble and the devastating economic tribulations brought about by the 9/11 incident and the outbreak of the Severe Acute Respiratory Syndrome (SARS), both economies have been adversely affected since the late 90s. Coupled with the recent developments launched by the Economic Review Committee – Financial Services Working Group (FSWG) in 2002, it is appropriate to take stock of the progress and reforms made so far and re-assess the future directions for Singapore to develop as an international financial centre and its competition with Hong Kong.

As pointed by Ng (1998), most comparative studies on the two economies as financial centres do not present any conceptual framework. In Hsiao et al (1999), the study used three indicators namely Chandavarkar's monetization rate (C/M2), Shaw's

financial depth indicator (M2/GDP) and the ratio of the total capitalization of the financial industry to GDP to measure and compare the financial developments of Taiwan, Hong Kong and Singapore. However, the problem of using monetization rate lies in Singapore's monetary policy of relying on managing a trade-weighted exchange rate index instead of managing the short-term interest rates or monetary aggregates as its monetary policy instrument. Notwithstanding the limitations, this study will still employ the ratio of the total capitalization of the financial markets to GDP as an indicator of the development of the financial markets.

This paper aims to provide an overall perspective of the financial developments of Singapore and Hong Kong as international financial centres. The structure of this paper is as follows. Section two will provide the background information on the two centres, with the focus on developments from the 1960s to the present. An introduction to the financial structures and markets for Singapore and Hong Kong is presented in section three. The five different sectors of the financial industry are presented in section four with an overview, followed by their performances and reforms to date. Section five concludes this paper and provides a summary of the recommendations for future growth areas against the backdrop of the policies and recommendations proposed by various commissioned studies.

SECTION 2 - HISTORICAL BACKGROUND

This section presents the background of the two centres, tracing their developments and transformations from the 1960s to present day.

After Singapore broke away from the Federation of Malaysia and gained independence in 1965, the immediate agenda was to develop Singapore into an industrial centre as well as other trading activities. Likewise, Hong Kong had shared a similar historical course as Singapore to become a reputable commercial centre of the Far East.

The early development of financial markets in Singapore and Hong Kong was geared to meet the demand of transshipment in trade during the 1960s. In the l970s, the boom of the Euro-Dollar market and the trend of international capital flow in Asia boosted activities in the two centres.

Singapore adopted a two-pronged strategy with regards to its financial sector. (Montes 1999) First, it wanted the financial sector to play a key supporting role to the growing industries located in Singapore. Second, the financial sector itself was to become a key industry in line with the government's effort to promote manufacturing and shipping industries. Since 1968, the Singapore government has provided incentives and preferential tax treatments for the development of the Asian Currency Units (ACU) (Tan 2002) in order to cultivate an Asian Dollar Market (ADM). That helped Singapore to develop as a financial centre and a lead over Hong Kong (Hodjera 1978). The Hong Kong government at that time was unwilling to waive the 15% withholding tax on interest income from foreign currency deposits. Further a moratorium was imposed on bank licensing after the banking crisis in 1965 which further impeded the development of an ADM. The year 1978 was a turning point for Hong Kong when China decided to

embark on an ambitious open door policy that would enhance Hong Kong's status as the financial gateway to the east.

In the 1980s, uncertainties shrouded Asia as well as the rest of the developing markets. In Hong Kong, there were two important events in the financial sector, the banking failures in the early 1980s that led to a large revision of banking regulation; and the stock market crash of 1987. Singapore weathered its fair share of difficult times in 1985 when its economy underwent a severe economic downturn after enjoying buoyant economic growth since its independence. Part of the problems that plagued these two centres was underlined by their dependence on centripetal forces (Walter 1993) in the 1960s to 1980s.

Ng (1998) noted that with the trend of growing globalization in the late 1980s to the 1990s, the success of both centres as international financial centres had increasing reliance on centrifugal forces. This view is also echoed by other authors (Poon 2003 and Schenk 2002) whereby the globalization revolutionizing the finance industry had led towards the trend of concentration, with fewer large financial centres, complemented by smaller centres with specialized focuses. Given the favorable business infrastructure, Singapore and Hong Kong were the natural choices for the influx of multinational corporations' operational headquarters in the 1990s. This spun off other economic externalities which benefited the two centres in their development as financial centres. Thus, Hong Kong's growth as a financial centre can be attributed to the growing fortunes of its North Asia's neighbors such as South Korea and the China hinterland whereas

Singapore's success was owed to its status as a regional financial centre for the South East Asian region.

In 1997, the Asian Financial Crisis hit the region and economies like Indonesia, Philippines and Thailand were badly ravaged. Singapore and Hong Kong were not spared from the spillover effects of the crisis. However, due to their robust financial systems as well as prudent fiscal and monetary policies, systemic damages were kept to a manageable level in these two economies.

Following the Asian Financial Crisis was the boom and bust of the dot com era where equities valuation skyrocketed for the IT-linked companies and then plummeted when investors realized the overly optimistic expectations on such firms were mostly empty dreams. Tragedy struck on September 11 in 2001 which led to financial turmoil as businesses all over the world were severely affected. The onslaught of the Severe Acute Respiratory Syndrome (SARS) took its toll on the Asian financial markets, affecting the airlines, tourism and retail trade. Despite the turbulent environment, the financial industry in Singapore and Hong Kong had weathered through the difficult times.

SECTION 3 – FINANCIAL STRUCTURE AND MARKETS – AN OVERVIEW

After discussing the historical developments, we now present the financial structures and markets for Singapore and Hong Kong in section three. An overview of the various sectors between Singapore and Hong Kong is tabled for easy reference.

Table 1: Financial Structure in Singapore and Hong Kong

	Singapore	Hong Kong
Monetary authority	Monetary Authority of Singapore (MAS)	Hong Kong Monetary Authority (HKMA)
Currency issuer	MAS – Currency Department	HSBC, Standard Chartered Bank, Bank of China
Three-tier structure	Full licensed bank Whole Sale licensed bank Offshore licensed bank	Licensed bank Restricted bank Deposit-taking company
Non-Bank financial institutions	Merchant bank Finance company Finance holding company Money broker SGS Market Dealers Insurance company/broker Central Provident Fund (CPF)	Insurance company Pension fund Unit trust Development Loan Fund Money broker Mandatory Provident Fund (MPF)
Other	Representative office	Representative office
Exchange rate regime	Limited flexibility w.r.t. a basket (Jun 73 – Jun 83) Managed floating (Jul 87 – Sep 04)	Peg to USD (Jul 72 – Oct 74) Independently floating (Nov 74 – Oct 83) Peg to USD (Oct 83 – Sep 04)

Source: Monetary Authority of Singapore and Hong Kong Monetary Authority

There are parallels and differences in the Singapore and Hong Kong's financial structures. Both economies do not have a central bank, relying instead on the respective monetary authorities to conduct monetary policies. However Singapore's monetary policies differ from Hong Kong's policies as mentioned by Jao (2003) by way of examining the "Trilemma" of monetary economics[2] proposed by Frankel (1999).

[2] The three desirable goals of monetary policy are namely monetary independence, fixed exchange rate and full capital mobility. Monetary authorities can at most achieve two, but not all three simultaneously.

Kim and Lee (2004) discussed on the different merits of the exchange rate regimes especially since the financial crisis in 1997 with references to empirical studies by Frankel (1999), Hausman et al. (2001), Borensztein et al. (2001) and Frankel et al. (2002). The East Asian countries have faced many new challenges especially in the adoption of an appropriate exchange rate regime and monetary policy under increasing capital market liberalization. Instead of relying on short-term interest rates or monetary aggregates as its monetary policy instrument, Singapore conducts its monetary policy by managing a trade-weighted exchange rate index (TWI) on the Singapore dollar and managing it within an undisclosed band against various currencies. (MAS 2004 Staff Paper No. 31) Hong Kong on the other hand, conducts its monetary policy by pegging the Hong Kong dollar to the US dollar since 15 October 1983, after a nine year independently floating exchange rate regime from 1974.

These two differing approaches however have not impeded the developments of these two economies. Rather, the policies have worked to their own advantage given their different historical backgrounds. Singapore as an export centre would have a greater need to ensure that the Singapore dollar is not being speculated as the effect of exchange rate volatility would cause uncertainties of exports and trade. Hong Kong on the other hand, benefited from the fixed regime viz. the linked exchange rate by escaping from the possible financial collapse during the Sino-British negotiations on the territory's future. (Jao 2001) The peg means that the Hong Kong dollar carries no exchange risk vis-à-vis the US dollar and can act as a proxy for the US dollar in futures and options hedging. This however also means Hong Kong has to follow the changes made by the Federal

Reserve with respect to the US interest rates. (Borensztein et al. 2001) Notwithstanding the difference in their monetary policies, Singapore and Hong Kong are among the Top 15 economies that export capital in 2003 as reported by the IMF.[3]

Table 2: Overview of Financial Markets in Singapore and Hong Kong

	Singapore	Hong Kong
Financial Institutions (2003)		
Banks		
Full bank/licensed bank	28	136
Wholesale/Restricted	37	46
Offshore/Deposit taking	50	40
Merchant bank	52	-
Representative offices of bank	50	92
Foreign Exchange (2004)	US$ Billion	US$ Billion
Daily turnover	125	102
Position in global foreign exchange and OTC derivatives	4th	7th
Equity Market (2003)	US$ (Million)	US$ (Million)
Market capitalization	305, 354	714, 6522
Valued traded	95,266	327, 924
Listed companies	566	852
Bond Market (2003)	US$ (Million)	US$ (Million)
Total outstanding	38,853	71, 849
Insurance Market (2003)	US$ (Million)	US$ (Million)
No. of companies	134	186
Total premium	43,873	11,410

Source: Monetary Authority of Singapore, Hong Kong Monetary Authority, Office of the Commissioner of Insurance (HK), Bank of International Settlements (BIS) Triennial of Forex and OTC (over-the-counter) Derivatives Market Activity 2004

SECTION 4 – SECTORAL REVIEW OF THE FINANCIAL MARKETS

This section will present an overview of the five major financial markets of Singapore and Hong Kong. It will also highlight their performances and the reforms carried out by the respective authorities to date. The five markets are 1) banking sector, 2) equity market, 3) fund management, 4) debt market and 5) insurance sector.

[3] IMF: "Global financial stability report – market development and issues", September 2004

4.1 Banking Industry

4.1.1 An Overview

The banking sector in Singapore has a three-tier structure which comprises full banks, wholesale banks and offshore banks[4]. Likewise Hong Kong maintains a three-tier system of deposit-taking institutions, namely, licensed banks, restricted licensed banks, and deposit-taking companies. They are collectively known as authorized institutions.

The banking sector as the main pillar of the financial industry accounts for majority of the financial activities carried out as revealed by MAS annual report 2004. Total assets of financial institutions amounted to S$1.36 trillion at end 2003 of which 63.8% were banks and merchants banks (ADM) assets and the remaining 27.2% in domestic banking assets.

4.1.2 Performance

A good indication on where the banking industry stands in its developments is observed by the number of top financial institutions or banks located in the country. (Low 2000) A strong presence of top international banks/financial institutions highlights the significance of the location as part of the banks' strategic intents. Based on The Banker's

[4] For more information on full banks, wholesale banks and offshore banks, please refer to Tan Chwee Huat (2004) Financial Services in Singapore.

2004 list of Top 1000 world banks, a compiled list of the Top 100 banks that operate in Singapore and Hong Kong is shown in Table 3:

Table 3: Top 100 World Banks (2004)

Rank	1 – 50	Singapore	Hong Kong	Rank	51 – 100	Singapore	Hong Kong
1	Citigroup	√	√	51	MBNA Corp	X	X
2	Credit Agricole Groupe	√	√	52	KBC Bank	√	√
3	HSBC Holdings	√	√	53	Abbey National	X	X
4	Bank of Amercia Corp	√	√	54	Landesbank Baden-Wurttemberg	√	√
5	JP Morgan Chase Et Co	√	√	55	Danske Bank	X	X
6	Mizuho Financial Group	√	√	56	Caja De Ahorros y. Pen. De Barcelona - la Caixa	X	X
7	Mitsubishi Tokyo Financial Group	√	√	57	Canadian Imperial Bank of Commerce	√	√
8	Royal Bank of Scotland	√	√	58	Bank of Montreal	X	√
9	Sumitomo Mitsui Financial Group	√	√	59	Dresdner Bank	√	√
10	BNP Paribas	√	√	60	SunTrust Banks	X	X
11	HBOS	X	X	61	DZ Bank Deustche Zentral - Genossenschaftsbank	√	√
12	Deutsche Bank	√	√	62	Resona Group	X	X
13	Barclays Bank	√	√	63	Toronto - Dominion Bank	√	√
14	Wells Fargo Et Co	√	√	64	National City Corp	X	X
15	Rabobank Group	√	√	65	Fifth Third Bancorp	X	X
16	Bank One Corp	X	√	66	Countrywide Financial Corporation	X	X
17	ING Bank	√	√	67	HSH Nordbank	√	√
18	UBS	√	√	68	ANZ Banking Group	√	√
19	Wachovia Corporation	X	√	69	Shinkin Central Bank	X	√
20	ABN AMRO Bank	√	√	70	Capitalia Gruppo Bancario	X	X
21	China Construction Bank	√	√	71	Eurohypo	X	X
22	Santander Central Hispano	X	X	72	Sumitomo Trust Et Banking	√	√
23	Societe Generale	√	√	73	KeyCorp	X	X
24	UFJ Holdings	√	√	74	Banca Monte dei Paschi di Siena	√	√

25	Industrial and Commercial Bank of China	√	√	75	Shinsei Bank	X	X
26	Lloyds TSB Group	√	√	76	Westpac Banking Corporation	√	√
27	Credit Mutuel	X	X	77	Standard Chartered	√	√
28	Metlife	X	X	78	Commonwealth Bank Group	√	√
29	Bank of China	√	√	79	Kookmin Bank	X	√
30	Groupe Caisse d'Epargne	X	X	80	Nykredit Group	X	X
31	Banco Bilbao Vizcaya Argentaria	X	√	81	Norddeutsche Landesbank Girozentrale	√	X
32	HypoVereinsbank	√	√	82	State Bank of India	√	√
33	Credit Suisse Group	√	√	83	Svenska Handelsbanken	√	√
34	Banca Intesa	X	√	84	BB Et T Corp	X	X
35	Fleetboston Financial Corp	X	√	85	Golden West Financial Corp	X	X
36	Agricultural Bank of China	√	√	86	Shoko Chukin Bank	X	X
37	Fortis Bank	√	√	87	DnB NOR Group	√	X
38	Groupe Banques Populaires	√	√	88	Skandinaviska Enskilda Banken	√	X
39	U.S. Bancorp	X	X	89	ForeningsSparbanken (Swedbank)	X	X
40	Washington Mutual	X	X	90	United Overseas Bank	√	√
41	UniCredito Italiano	√	√	91	DBS Bank	√	√
42	Norinchukin Bank	√	X	92	Allied Irish Banks	X	X
43	DeXia	√	√	93	Bank of Ireland	X	X
44	National Australia Bank	√	√	94	PNC Financial Service Group	X	X
45	Commerzbank	√	√	95	Bank of New York	√	√
46	SanPaolo IMI	√	√	96	Mitsui Trust Holdings	√	√
47	Scotiabank	√	√	97	Comerica	X	X
48	Royal Bank of Canada	√	√	98	Caja de Ahorros y Monte de Piedad de Madrid	X	X
49	Nordea Group	√	X	99	Erste Bank	X	√
50	Bayerische Landesbank	√	√	100	Banco Popular Espanol	X	X

Source: MAS Monetary Authority of Singapore, HKMA Hong Kong Monetary Authority, The Bankers 2004 (July)

Notably, Singapore has 61% of the Top 100 banks whereas Hong Kong has 63% excluding the equivalent number of representative offices in both economies. The results

are encouraging given the fact that some of these banks (29) in The Banker's list are domestic or regional in nature and do not have an international presence. Discounting these banks from the list would raise the percentage to 86% and 88% respectively for Singapore and Hong Kong. These are impressive figures.

Hong Kong has twenty three locally registered licensed banks[5] with six of them with foreign ownership (HSBC, Bank of China, Dao Heng Bank, Industrial and Commercial Bank of China, Chekiang First Bank and DBS Bank Hong Kong). In Singapore, the seven local banking groups have consolidated into three stronger groups. The three Singapore banks, UOB, DBS Bank and OCBC are ranked 90, 91 and 110 respectively on The Banker's Top 1000. On the ranking of the Hong Kong banks, the top of the list (excluding those with foreign ownership) was Bank of East Asia ranked only 201, which paled in contrast with the Singapore banks.

Table 4 shows the contrasting fortunes of the banks in five aspects with regards to their ranking on The Banker's Top 1000 list. The five measures are 1) Tier One Capital; 2) Size on Assets; 3) Profits; 4) Return on Assets and 5) NPL to Total Loans. Overall, the total size of assets of Singapore banks vis-à-vis that of banks in Hong Kong is almost three times larger. The relatively larger asset base of Singapore banks means they are less likely to be acquisition targets compared to the banks in Hong Kong.

[5] http://www.info.gov.hk/hkma/eng/bank/three_tier/list_of_lb.xls as at 1st Oct 2004

At the Non Performing Loan (NPL) level, there might be some indications that the Singapore banks are lending to riskier profiles compared to their Hong Kong's counterparts. (Average NPL to total loan of 7.5% versus 2.83% respectively) However, according to the IMF report, Singapore has a reported lower percentage of non performing loans to total loans compared to Hong Kong. (3.2% versus 3.9% respectively) The differences could be due to the exclusion of foreign owned banks in our calculations as we only included Hong Kong incorporated banks from The Banker's Top 1000. On a ROA basis, Singapore banks seemed to fare better as they managed to achieve comparable returns of 1.26% vis-à-vis Hong Kong average ROA of 1.20%. Likewise, the IMF report on bank ROA for Singapore and Hong Kong were 0.9 and 0.8 respectively for 2003.

Looking at the credit ratings as assigned by Standard & Poor's, Singapore banks have better credit ratings with an average of an A+ grade whereas the Hong Kong banks generally fall in the BBB category, signifying the better credit quality of Singapore banks over those in Hong Kong. This is echoed by the report released by IMF[6] based on Moody's weighted average bank ratings. Singapore financial strength index was 74.7 for 2004 whereas Hong Kong index was 62.3.

Singapore's banks have also been expanding aggressively following the liberalization measures introduced in 1998 in a bid to retain their competitiveness. In his paper, Tschoegl (2001) explored the factors that explained the timing and location of

[6] IMF: "Global financial stability report – market development and issues", September 2004

their expansion. Dao Heng bank acquisition by DBS bank in mid 2001 is an example of the Singapore bank quest to expand its banking arms beyond its shores.

Table 4: Performance of Singapore and Hong Kong Banks

Rank on Banker Top 1000	Bank	Strength Tier One Capital US$M	Size Assets US$M	Profit US$M	Return on Assets %	NPL to Total Loans %	Credit Ratings (Standard & Poor's)
Singapore							
90	UOB	5754	66702	946	1.42	8.10	A+/Positive/A-1
91	DBS Bank	5659	93835	845	0.90	Na	A+/Positive/A-1
101	OCBC	4641	49681	718	1.45	6.90	A+Stable/A-1
Total		**16054**	**210218**	**2509**	**1.26**	**7.50**	
Hong Kong							
201	Bank of East Asia	2052	25567	306	1.20	2.50	BBB+/Stable/A-2
311	Shanghai Commercial Bank	1196	9636	156	1.62	2.10	BBBpi/--/--
403	Wing Lung Bank	851	8731	130	1.49	2.49	BBBpi/--/--
481	Dah Sing Financial Holdings	661	8213	145	1.76	1.55	BBBpi/--/--
484	Wing Hang Bank	656	11431	130	1.14	2.98	BBB+/Stable/A-2
499	Liu Chong Hing Bank	631	5145	47	0.92	4.80	N.A
504	CITIC Ka Wah Bank	623	9972	98	0.98	Na	N.A
965	Asia Commercial Bank	189	1680	9	0.52	3.39	N.A
Total		**6859**	**80375**	**1021**	**1.20**	**2.83**	

Source: The Banker (July 2004)

In addition to the rankings, IMF/World Bank's Financial Sector Assessment Programme (FSAP) report published in April 2004 endorsed the resilience and robustness of Singapore's financial sector despite the difficult conditions. It also commended Singapore's high degree of observance of international standards and codes. An Asian

Banker Research review in January 2004 further supported that Singapore has grown as a regional financial center with respect to economies like Thailand, Malaysia, Taiwan and Hong Kong. Supporting data from the BIS Quarterly Review in September 2004 showed the amount outstanding at offshore centers for Singapore and Hong Kong are US$245 billion and US$166 billion respectively.

4.1.3 Reforms to Date

Reforms in both economies have been on-going since the onset of the Asian crisis. Singapore. In May 1999, MAS announced a five-year programme to liberalise the domestic banking sector. The programme aims to strengthen Singapore's banking system and the local banks, and to enhance Singapore's position as an international financial centre. MAS revised regulations in line with international best practices in order to increase the competitiveness of local banks. The HKMA commissioned a consultancy study in 1998 to develop the banking sector over a five-year period. The purpose of the study was to conduct a strategic review and analyse the impact of the regime and make recommendations for necessary changes to regulations and the supervisory approach. The study suggested four strategic mandates for the HKMA in promoting future development of the banking sector. Details of the recommended reforms for Singapore can be found in Appendix 1[7] and a summary of the reforms recommended by the Hong Kong consultancy study is attached in Appendix 2.

[7] Recommendations traces the policies advocated since the 1985 Sub Committee on Banking and Financial Services to the 2002 Financial Services Working Group of the Economic Review Committee.

Singapore

The MAS has always taken a proactive approach to develop the banking industry. It is careful in balancing the need to develop the local banks as while providing the necessary incentives to attract foreign banks to operate in Singapore. In 1999, the MAS introduced a five-year program to liberalize foreign access to Singapore's domestic banking market. It worked with banks to set guidelines for best practices and give banks more room for innovation. To date, some of the reforms taken by MAS are as follows:

As the banking industry is further liberalized, local banks over the years have merged to fortify against foreign competition. With a current stable of DBS Bank, OCBC and UOB, the trend of consolidation is likely to continue until only 2 local banks are left as suggested by an interview with Business Week in 1999 where Deputy Prime Minister (DPM) Lee said that "the domestic market is big enough for two major banks." A statement released by the MAS (17 May 1999) reiterated the stance that the smallness of the domestic market and the growing economies of scale in banking, make it unlikely that Singapore can sustain more than two local banks with that critical size, although there may be other smaller players occupying niche markets.

The MAS lowered the Capital Adequacy Requirements (CAR) for local banks in May 2004[8]. The revision in the CAR would allow the local banks to be more competitive as they would have to hold less regulatory capital in reserves and deploy the freed capital more meaningfully.

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[8] For details on the changes in the Capital Adequacy Requirements for Singapore-incorporated banks, please refer to MAS Press Release on 28 May 2004.

The MAS is also moving towards a disclosure based regime, which is a shift from the supervision approach. In the new regime, banks will take the onus of monitoring their risk management practices, which is in line with the proposed new Basel Capital Accord to be implemented in 2007. This move from a one-size-fits-all approach will allow the banks to pursue their banking activities with fewer restrictions while maintaining the appropriate measures to control their credit, market, operational, business and systemic risks.

Further liberalization measures have been introduced in June 2004[9] by the MAS to drive the banking industry forward. Qualifying Full Banks (QFBs) are now permitted to establish 25 service locations up from the previous 15 (an increase of 60%). This expansion in the network allows QFBs to widen their presence in the domestic market. QFBs can negotiate with the local banks on a commercial basis to let their credit card holders obtain cash advances through the local banks' ATM networks.

A consultancy study was carried out to review the feasibility of implementing the Deposit Insurance scheme in Singapore as first mooted by DPM Lee in 2001[10]. The second consultation paper was released in April 2004 for further comments by the industry. Deposit insurance schemes have long been established in the western countries.

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[9] "Financial Sector - Liberalisation and Growth" – Address by DPM Lee Hsien Loong, Chairman MAS at the Association of Banks in Singapore's 31st Annual Dinner on 17 June 2004.
[10] "Consolidation and Liberalisation: Building World-Class Banks" – Address by DPM Lee Hsien Loong, Chairman MAS at the Association of Banks in Singapore Annual Dinner on 29 June 2001.

With the full liberalisation of the banking industry, it is timely for MAS to consider the implementation of this scheme in order to drive the banking industry forward.

A Straits Times article on 20th September 2004 reported the growing interest by the MAS to promote Islamic banking products to expand its reputation as a financial hub with collaboration with countries such as Malaysia and Brunei. According to the article, MAS would look into the value add role of Singapore in the niche area of Islamic banking given the substantial amount of funds being managed by Islamic investments institutions globally. Singapore however, will not compete with Malaysia and Brunei, which already have developed Islamic banking services.

Hong Kong

The banking industry in Hong Kong has gone through several significant reforms since the early 1960s, moving from laissez-faire to prudential supervision. Following the consultancy study conducted in 1998, the HKMA undertook several reforms to strengthen its banking sector. The consultancy study suggested four strategic mandates for the HKMA[11]. With the mandates in mind, HKMA introduced a two pronged approach to develop the banking sector which was 1) promoting competition and 2) enhancing the

[11] Extracted from Hong Kong Monetary Authority – Reforms and Development of the Banking Sector. The four strategic mandates are as follows:

1) Ensure that the regulatory and supervisory framework for Hong Kong remains appropriate.
2) Improve the competitive environment to ensure the positive benefits of global and local trends are developed in the Hong Kong markets.
3) Ensure the increasing level of risks associated with global and local trends are prudently managed.
4) Increase the level of transparency allowing the forces of market discipline to work more effectively.

infrastructure supporting bank safety and soundness. Some of the reforms that had taken place are as follows:

In May 2002, the existing market entry criteria for licensed banks were relaxed. The HKMA also evaluated simplifying the three-tier system into a two-tier system. However, it was concluded that the relaxation of the entry criteria would enable the restricted licensed banks to get a licensed bank status, thus making the two-tier system redundant.

The Hong Kong Government also considered the establishment of a Commercial Credit Reference Agency (CCRA). A CCRA would increase the lending institutions' knowledge of borrowers' credit records, expedite the loan approval process, and help to strengthen lending institutions' credit risk management. Exchanging information about borrowers among lenders also increases the incentive for borrowers to repay, thereby reducing the overall default rate. In August 2003 The Hong Kong Association of Banks (HKAB) and The DTC Association (DTCA) appointed Dun & Bradstreet (HK) Ltd. (D&B) as the Service Provider for Hong Kong's first Commercial Credit Reference Agency (CCRA), which is expected to commence operations in the third quarter of 2004.

The Deposit Protection Scheme Ordinance has been passed by the Legislative Council in May 2004. Formal introduction of Deposit Protection scheme (DPS) would provide an explicit safety net, particularly for those depositors not well equipped to protect themselves, in the event of a banking crisis. To the extent that the safety net is

able to reduce the incidence of unnecessary rumor- driven runs, it also contributes to banking stability.

4.2 Equity Market

4.2.1 An Overview

In 1998, the MAS announced a timetable for opening up access to the stock exchange and liberalizing brokerage commissions. In November 1998, DPM Lee announced that the Singapore Stock Exchange[12] (SES) and Singapore International Monetary Exchange (SIMEX) would be demutualized and merged into a single integrated privately-held stock company. Singapore Exchange (SGX) was thus formed on 1 December 1999 as a result of the merger.

Prior to 1998, Hong Kong's equity market had a relatively simple structure, similar to the SES and SIMEX in Singapore. It was comprised of two major platforms, the Stock Exchange of Hong Kong Limited (SEHK) and the Hong Kong Futures Exchange (HKFE) in addition to its associated clearing houses[13]. To increase its competitiveness and meet the challenges of the increasingly globalised capital market, the

[12] The SES now operates as the SGX-Securities Trading Division (SGX-ST) to trade in securities products such as shares and bonds. SIMEX operates as SGX Derivatives Trading Division (SGX-DT) to trade in derivatives products such as futures and options.

[13] The clearing houses are 1) Hong Kong Securities Clearing Co. Ltd (HKSCC), 2) the Stock Exchange Options Clearing House (SEOCH) and 3) the HKFE Clearing Corporation Ltd

Hong Kong securities market underwent several major changes in recent years. Under the reform, the Stock Exchange of Hong Kong Limited, Hong Kong Futures Exchange Limited demutualised and together with Hong Kong Securities Clearing Company Limited, merged into a single holding company, HKEx. Similarly, the HKEx also had its respective securities trading divisions as well as its derivative divisions. In addition, the settlement of stock was also undertaken by the Clearing Division.

Incidentally, both Singapore and Hong Kong have a secondary board in addition to the main board. The Singapore SES Dealing and Automated Quotation System (SESDAQ) is the second board of Singapore Exchange Securities Trading Limited which provides an alternative avenue for small and medium companies to raise funds. Likewise, the Growth Enterprise Market (GEM) is the Hong Kong's equivalent of the SESDAQ.

4.2.2 Performance

Singapore and Hong Kong stock markets are among the more established in Asia. The market capitalization for Singapore and Hong Kong as current data show is S$571 billion[14] (approx. US$338 billion) and HK$5,720 billion[15] (approx. US$733 billion) respectively. The total number of listed companies was 606 for SGX and 875 for HKEx as of August 2004. On the liquidity front, the turnover in both markets has been active. For the month of August 2004, the total turnover value was HK$250 billion (US$32 billion) and S$13.64 billion (US$8.1 billion) for Hong Kong and Singapore markets

[14] Monetary Authority of Singapore (MAS) data include Main Board and SESDAQ
[15] Hong Kong Exchanges and Clearing Limited (HKEx) data include Main Board and GEM

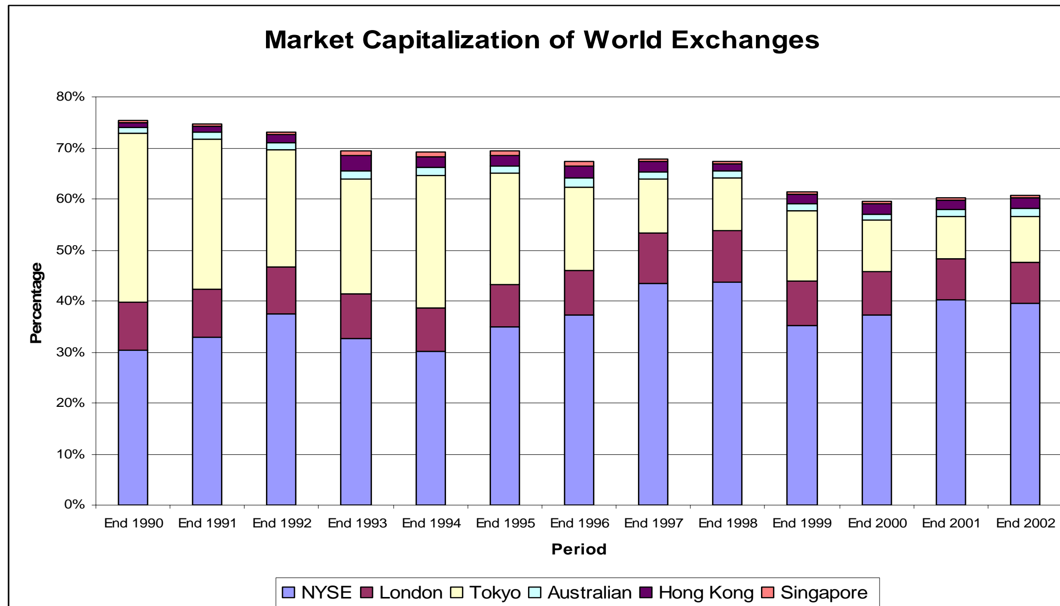
respectively. The relatively lower trading turnover for the Singapore market has been a concern as Singapore's growth as a capital market has somewhat been impeded by the low trading volume as identified by the Finance and Banking Sub-Committee in 1997. Reforms are therefore targeted at improving the liquidity of the market as well as encouraging more listings.

Notwithstanding the low trading volume and turnover compared to Hong Kong, the market capitalization of Singapore's securities market increased from US$34 billion in 1990 to US$338 billion in 2004. The increase was almost tenfold within a span of 15 years. This is a good indication that the developments and prior reforms had paid off. The influx of offshore banking activities and foreign capital spurred rapid growth in the Singapore equity markets in the mid-1980s. The use of Central Provident Fund (CPF) savings was liberalized to allow CPF members to use their savings for investment. This has fuelled the growth of the securities market. The change in the listing requirements also permitted more firms to issue equities to fund their activities.

Hong Kong's stock market is the 10th largest in the world according to the World Federation of Exchanges[16] data in 2003, maintaining its position from the previous year position. The Hong Kong securities and futures markets have been undergoing rapid changes since the Asian Financial Crisis in 1997. Reflecting the economic integration with Mainland China, numerous Mainland enterprises were listed in Hong Kong. As at August 2004, 68 and 74 firms were listed as H-shares and Red-chips respectively.

[16] The ranking was based on the market capitalization in 2003. The ranks were 1) NYSE, 2) Tokyo, 3) NASDAQ, 4) London, 5) Euronext, 6) Deutsche Borse, 7) TSX Group, 8) Swiss Exchange, 9) Hong Kong and 10) Borsa Italiana

Table 5: Percentage of the Market Capitalization of World Exchanges from 1990 – 2003



Source: World Federation of Exchanges, www.world-exchanges.org

On a global basis, these figures account for only a small percentage relative to the other exchanges such as financial market giants New York Stock Exchange (NYSE) and the London Stock Exchange (LSE). The comparisons are reflected in the above table. Whilst the market capitalization of Singapore and Hong Kong pale in comparison in absolute figures to stock markets like NYSE, LSE and the TSE, a more meaningful comparison can be drawn by the market capitalization as a percentage of GDP (a measure used in Hsiao et al 1999) to show how successful are the capital markets in their respective economies.

Table 6: Market Capitalization to GDP (2003)

Exchanges	US$ Millions		
	Market Capitalization	GDP	Ratio
AMEX / NASDAQ / NYSE	$ 14,266,023	$ 10,400,000	1.37
London	$ 2,460,064	$ 1,520,000	1.62
Tokyo	$ 2,953,098	$ 3,550,000	0.83
Hong Kong	$ 714,597	$ 186,000	3.84

Singapore	$	148,503	$	105,000	1.41
Australian	$	585,431	$	528,000	1.11
Jakarta	$	54,659	$	663,000	0.08
Korea	$	298,248	$	931,000	0.32
Kuala Lumpur	$	160,970	$	210,000	0.77
India	$	531,556	$	2,660,000	0.20
New Zealand	$	33,050	$	78,800	0.42
Philippine	$	23,190	$	356,000	0.07
Taiwan	$	379,060	$	406,000	0.94
Thailand	$	119,017	$	429,000	0.27

Source: World Federation of Exchanges, www.world-exchanges.org

Topping the list is Hong Kong where the ratio of its market capitalization to GDP was nearly 4 times its annual GDP for 2003. This was perhaps the largest amongst the other developed capital markets globally. The phenomenon attests to the growth of Hong Kong's growth as a stock market and the growing use of equity financing, which are prerequisites for financial development and increased sophistication. Singapore achieved a ratio of 1.41 over its annual GDP. While distant to Hong Kong's figure, Singapore's securities market has achieved ratios comparable to markets like New York and London and surpasses Tokyo and Australia.

The number of firms listed on Hong Kong has enjoyed almost double digit growth annually as tabulated in Table 7. The growth in successful listings to the stock exchange is also enjoyed by Singapore, though to a lesser degree. This could have been impeded by the over onerous regulations and criteria that the SGX has set for Main Board applicants prior to the reforms.

Table 7: Number of Listed Companies and Changes in Growth

	No. of Listed Companies on Exchange					% Changes in No. of Listed Companies				
	NYSE	London	Tokyo	Hong Kong	Singapore	NYSE	London	Tokyo	Hong Kong	Singapore
1990	1,774	2,559	1,752	299	172					
1991	1,989	2,572	1,764	357	182	12.12	0.51	0.68	19.40	5.81
1992	1,750	2,440	1,768	413	195	-12.02	-5.13	0.23	15.69	7.14
1993	1,945	2,412	1,775	477	216	11.14	-1.15	0.40	15.50	10.77
1994	2,128	2,416	1,782	529	251	9.41	0.17	0.39	10.90	16.20
1995	2,242	2,502	1,791	542	272	5.36	3.56	0.51	2.46	8.37
1996	2,476	2,623	1,833	583	296	10.44	4.84	2.35	7.56	8.82
1997	2,626	2,513	1,865	658	334	6.06	-4.19	1.75	12.86	12.84
1998	2,670	2,423	1,890	680	358	1.68	-3.58	1.34	3.34	7.19
1999	3,025	2,274	1,935	708	408	13.30	-6.15	2.38	4.12	13.97
2000	2,468	2,374	2,096	790	480	-18.41	4.40	8.32	11.58	17.65
2001	2,400	2,332	2,141	867	492	-2.76	-1.77	2.15	9.75	2.50
2002	2,366	2,272	2,153	978	501	-1.42	-2.57	0.56	12.80	1.83

Source: World Federation of Exchanges, www.world-exchanges.org

4.2.3 Reforms to Date

Singapore

The MAS has approved revision of the share buyback regulations to allow listed companies to re-purchase shares on the market out of distribution profits at any time within the period mandated by shareholders. This approval has given companies greater flexibility in terms of method, timing, price and volume of share buybacks. It complements existing legislation permitting share buybacks in the form of capital reduction. In 2003, the MAS also embarked on a two-phase legislative amendment process on the Securities and Futures Act (SFA) and the Financial Advisor Act (FAA). The amendments aimed to reduce the cost of raising capital in Singapore by rationalizing and simplifying the requirements in the SFA for offers of investments.

The SGX has revised regulations to allow listed companies to peg exercise prices of employee share options at deep discounts of up to 20 percent to their market prices, and to enlarge share option schemes from 5 to 15 percent of issued share capital.

Foreign currency-denominated IPOs do not attract retail interest due to foreign exchange risk aversion. Allowing a dual currency listing would solve this problem. Further, the SGX has shown strong interest in attracting foreign companies from China and India to obtain a listing on the SGX. This would add to the liquidity and vibrancy of the equity market given the strong growth enjoyed by the two powerhouse economies. The MAS has eased conditions for foreign companies to list in SG dollar on the local exchange and removed limits on investments in foreign currency denominated shares by CPF (Central Provident Fund) - Approved Unit Trusts.

The 1985 Sub Committee on Banking & Financial Services recommended that the fixed commission structure should be abolished and replaced by negotiated commission charges. Since the 1985 recommendations, the SES has yet to adopt a structure to facilitate trading. In the 1998, the Committee on Singapore's Competitiveness has revisited the issue of reducing transaction cost for trading securities in order to stay competitive. In his opening address[17], DPM Lee that by 1 Jan 2001, trading commissions will be completely freed up and access to trade on SGX will be fully liberalized.

Derivatives such as options and futures are key components of a developed equity market as they add to the breadth of the capital market. Due to the absence of security lending facilities, high regulatory capital requirements, the lack of dedicated option market makers and cumbersome settlement procedures, trading of equity options in OTC market has not taken off. There is thus an impetus to hasten the introduction of more

[17] "Financial Liberalisation – Going Global" – Opening address by DPM Lee Hsien Loong, Chairman MAS at the Singapore Work Plan Seminar, 3 April 2000

derivative products. There has been some moderate success with the launch of the MSCI Singapore Stock Index futures (1998), single stock futures, energy futures etc.

The IPS Forum on Economic Restructuring (IFER) recommendation on the establishment of independent research firms has taken off with the launch of the SGX-MAS Research Incentive Scheme. The scheme was set up to widen research coverage of stocks listed on SGX and provide investors with more information to facilitate their investment decisions. The scheme will be offered for two years and is funded from the SGX-MAS Market Development Fund. All companies listed on SGX Mainboard and SGX-Sesdaq are eligible for the scheme. A total of 122 listed companies have signed up and 9 research firms have been approved to participate in the scheme[18].

There is also a need to review the monopolistic role of the SGX and whether there could be room for competition that would facilitate greater cost efficiency, easier market access and product innovation. A Singapore Alternative Market (SAM) was proposed, which would be the alternative electronic market maker/exchange for emerging new businesses. This would attract new capital and promote entrepreneurship in the local market.

Regional governments took several initiatives to foster a regional capital market, covering both fixed income and equity. These addressed both supply and demand side issues, such as easing constraints to cross border activity, forging alliances and linkages

[18] Singapore Exchange Ltd (SGX) announced that it will launch phase two of the SGX-MAS Research Incentive Scheme from 1 December 2004. Full details of scheme can be viewed on SGX website at www.sgx.com

among the exchanges, as well as establishing a regional infrastructure. Singapore is well positioned to take advantage of these initiatives and take a lead in the cross border activities. While the SGX-ASX linkage had not seen the benefits as expected, the recent SGX-Bursa Malaysia tie up is expected to generate a higher level of liquidity. There are keen interests expressed by both Singapore and Malaysia investors to trade on the two boards.

Hong Kong

The fourth Round Table on Capital Market Reform[19] in Asia organized by the Organization for Economic Co-operation and Development (OECD) in 2002 summed up some of the efforts by the relevant authorities to further develop the capital market. The recommendations include:

The listing functions of Hong Kong Exchanges and Clearing Limited (HKEx) was recommended to be removed and transferred to a new division of the Securities and Futures Commission (SFC) to be known as the Hong Kong Listing Authority (HKLA). The HKLA would be accountable for both regulation and market development. The SFC should be the statutory regulator of listed companies and sufficient resources should be provided to enable it to perform its functions properly. As a matter of urgency, consideration should be given to raising entry levels for new listings and the SFC should have full investigative power to establish the genuineness of initial placements. The HKEx has an irreconcilable conflict of interests as both a listed company and the primary

[19] The conference and materials can be viewed at http://www.oecd.org/document/63/0,2340,en_2649_33761_2077631_1_1_1_1,00.html

regulator of companies seeking listing. Notwithstanding the efforts of the HKEx to manage this conflict, the existence of such a conflict is, in itself, not conducive to the development of Hong Kong as an international financial centre.

Hong Kong's tripartite regulatory structure involving the government, SFC and HKEx while acceptable in principle has led in practice to uncertainty, overlap and in some cases friction. The SFC should be recognized as the corporate regulator of listed companies and the HKEx should be relieved of the burden of regulation and allowed to concentrate on its commercial objectives with minimal government involvement. Given the increasing number of Mainland companies listed in Hong Kong, there should be closer and more effective regulatory cooperation between the SFC and the China Securities and Regulatory Commission.

The HKEx is also actively exploring opportunities to position itself in the global market architecture and expand its business scope. It is seeking to grow its current businesses by enhancing remote distribution. The SFC has approved rule changes proposed by the HKEx to provide overseas clients of its Futures Exchange Participant direct access to the Automated Trading System (HKATS), the trading system of its futures market.

4.3. Fund Management Industry

4.3.1 An Overview

In accordance with its government-led economic policy, the MAS has targeted the development of the fund management as a key element of the financial sector as identified by the 1997 Committee. Numerous incentives are provided by the government to encourage international fund managers to operate in Singapore. At the same time a large part of the sector can be said to be controlled by the Government in the sense that much of the funds under management are managed directly by the Central Provident Fund (CPF).

The CPF, a compulsory government-managed retirement savings scheme, was set up in 1955. Current contribution rates are very high – up to 20% of salary from the employee and 13% from the employer, subject to a cap. As at the end of September 2002, the CPF accumulated balances total S$95 billion (US$53 billion), the majority of which is invested in Government-issued bonds. Because of its size, the CPF absorbs much of the population's savings. However, in recent years CPF account holders have been permitted more flexibility in using their savings to buy a house or invest in shares.

The fund management sector was identified as a key area for development in the financial services. Numerous incentives are offered to fund managers, including tax concessions, grants, and also allocations of CPF money. Following the Asian Financial Crisis, which hit Singapore's neighbors such as Indonesia particularly hard, the MAS sped up the efforts. In 1998, the CPF Board announced that it would earmark S$35 billion (US$21 billion) as seed money to promote the development of the sector. A further round of policy recommendations were made in a report published in September

2002 by the Financial Services Working Group (FSWG). These efforts have shown some success, as many international fund management firms have set up offices in Singapore.

In contrast with Singapore, the development of the fund management industry in Hong Kong may be characterized as largely market-driven. The Hong Kong Government has generally left the growth of the industry to market forces. Although it has subjected the industry to regulation, the government has not sought to deliberately promote the industry through its policy framework. The industry is dominated by international firms.

The fund management industry in Hong Kong began developing in the late 1960s and early 1970s when British merchant banks set up operations in the territory. They managed retirement funds for their own groups but offered unit trusts to the public as well. Initially, the main customers were expatriates, since local Chinese preferred to invest directly on their own account. In the 1970s US asset management companies entered the market, and in the 1980s the Japanese. Rising wealth levels led to demand for retirement funds in the 1980s, and in the 1990s, unit trust investing gradually became more popular among the general public. A Code on Unit Trusts was first introduced in 1978 under government administration. This was replaced by a Code on Unit Trusts and Mutual Funds in 1991 administered by the SFC, and was followed by further codes and regulations on various kinds of investment-linked products. Fund managers are licensed under the securities legislation as investment advisers. A Mandatory Provident Fund (MPF) scheme was introduced in 2000, requiring employers to establish provident funds for their staff. The bulk of the fund management business in Hong Kong is done by

international firms with offices in the territory. Locally-based fund managers have only a minor role. The Hong Kong Investment Funds Association, established in 1986, represents the interests of the sector. It now has about to 50 member firms.

4.3.2 Performance

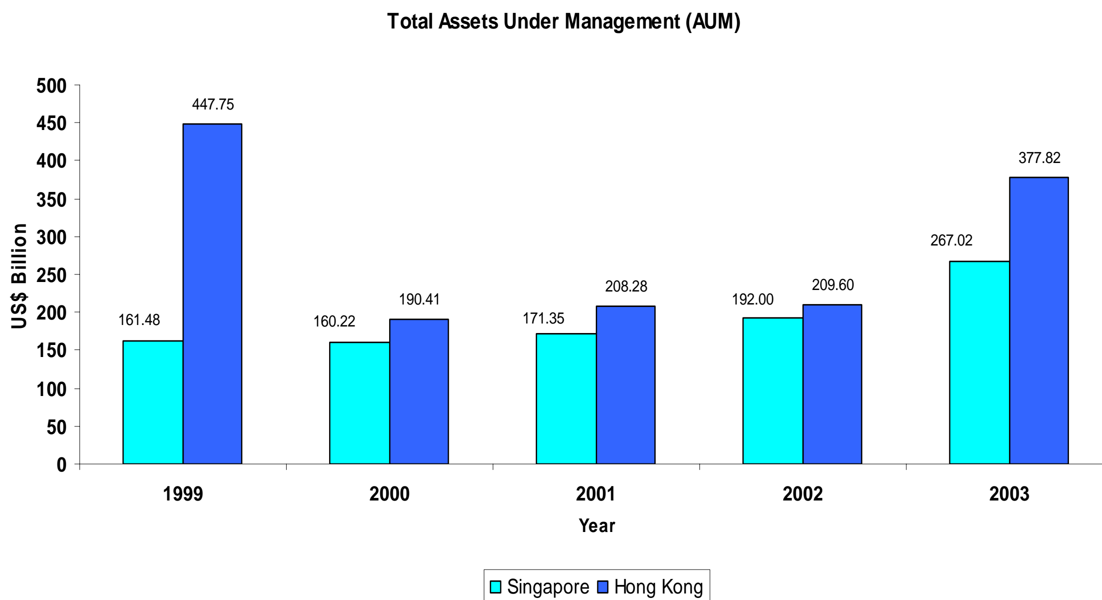
Before comparing the performance of the two fund management centres directly, it is useful to look at both in the global context. Hong Kong and Singapore are international financial centres. Both are rich economies with high GDP per capita. As they have small populations (7 and 4 million respectively), a large part of their role is to manage offshore money on behalf of investors based overseas. Nonetheless, the growth within the Asia- Pacific region, especially in Hong Kong's neighbor Mainland China, offers prospects to the industry located there. In terms of assets under management, the two centres are of course very much smaller than the global leaders London and New York. Therefore, any direct contrast against the goliaths in the industry would not be significant.

Since 1999, Singapore and Hong Kong have embarked on conducting annual survey on the fund management activities. The total assets under management figures for Singapore and Hong Kong are presented in Table 8. It should be noted that the bases for the statistics presented below differ. For example, Singapore's figure for assets under management (AUM) includes the assets of private banks whereas Hong Kong's may not. Singapore calculates discretionary AUM while Hong Kong does not. However in 2002, the survey included a new section on advisory services; Hong Kong distinguishes

between AUM managed in the territory and those managed outside while Singapore does not.

On a year-on-year growth comparison, Singapore performed significantly better than Hong Kong and grew by 15% and 39% in 2002 and 2003 respectively. The consistent upward trend in the amount of total AUM is indicative of the development of the fund management industry in Singapore. Having their total AUM shrank in 2000 with the restructuring of a very large registrant and further burdened by the general fall in asset prices, Hong Kong posted growth of less than 1% in 2002. However, it posted a growth of 50% for the year 2003, which was a huge reversal of the state of the fund management industry.

Table 8: Total Assets Under Management (1999 – 2003)



Source: MAS Survey of Singapore Asset Management Industry 1999-2003, Hong Kong Securities and Futures Commission Fund Management Activities Survey 1999-2003

Note: (Monetary values converted at HK$7.8=US$1) (Singapore monetary values converted at average value for the respective years 1999 (S$1.6949= US$1), 2000(S$1.7239=US$), 2001(S$1.7917=US$1), 2002(S$1.7906=US$1), 2003 (S$1.7422=US$1)

Other indicators such as the numbers of companies providing fund management or advisory services and the number of funds managed in the economy also provide a good quantitative comparison to the state of development of the industry. As at the end of 2003, there were 166 companies that provided fund management or advisory services in Hong Kong. The staff profile includes 2890 investment professionals in various areas of specialization as illustrated in Appendix 3. In Singapore, there were 230 asset management houses operating in Singapore in 2003 as compared to 211 in 2002. The number of investment professionals in the industry in 2003 was 986 comprising 688 portfolio managers, 275 investment analysts and 23 asset allocators/economists. The breakdown in product specialization is depicted in Appendix 3.

On the number of funds managed, for Singapore, as at end-2003, the total number of Collective Investment Schemes (CIS) increased to 401, compared to 382 CIS as at end-2002[20]. Total CIS assets increased 36% from S$14.1 billion at end-2002 to S$19.2 billion at end-2003. Capital guaranteed/protected funds and balance funds continued to be popular investment choices. Notably, the number of capital guaranteed/protected funds increased significantly from 82 funds to 119 funds, increasing its total AUM to S$7.6 billion at end-2003. Of late, funds of another nature i.e. targeted returns funds have hit the investment scene and had attracted significant following. (Straits Time 13th June

[20] MAS 2003 Survey of the Singapore Asset Management Industry

2004) This also signifies the pace of innovation by fund management companies to come up with products that fit the investors' profiles and needs.

Comparatively, the number of CIS in Hong Kong is six times larger that that of Singapore. The total was 2457 as at end 2003[21]. Majority (80%) of the CIS fell under the Unit Trusts & Mutual Funds category while investment linked assurance schemes and the Mandatory Provident Fund (MPF) Pooled Investment Funds take up 5% and 10% respectively. The total net asset values of Unit Trusts and Mutual Funds rose 20% to US$342 billion from the previous year of US$285 billion. Equity linked unit trusts continued to be the dominating type of investment although the number of such fund declined from 1,063 in 2002 to 1,030. However, there had been 150% growth rate in the number of guaranteed funds, signaling the general trend in the interest of such investment vehicles.

4.3.3 Reforms to Date

Singapore

The MAS has deliberately targeted the development of the fund management industry in its effort to expand its financial sector. The approach has been structured and deliberated. Since 1986, CPF members have been permitted to use their CPF savings to invest in approved investment products under the CPF Approved Investment Scheme. Though CPF members now have more choices in their selection of investment products (such as the introduction of approved unit trusts) with the further liberalization of the

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[21] Hong Kong Securities and Futures Commission, Table D1 – Authorized Collective Investment Schemes

CPF Investment Scheme (CPFIS)[22] in 1998, the development of a privately-managed pension plan has yet to materialize at the moment. The idea of a pension plan is not uncommon in many developed countries. The purpose of a privately-managed pension plan is to achieve economies of scale for investment of retirement funds and reduce members' investment costs as the costs of unit trust investments are relatively higher compared to an institutionalized pension plan. It also aims to increase returns on members' CPF balances. Consultations are underway with industry players as well as the relevant authorities to determine the best option to free up the excess CPF cash flow[23].

While the tax environment has been revised over the years to make it more favorable to facilitate the development of an asset management centre, the taxation treatment in other economies such as Hong Kong has also grown more competitive. Currently those on the list of Approved Fund Managers (AFMs) are accorded a concessionary tax rate of 10% on fees and commission derived from any funds managed, investment advisory services provided or loan of securities. Tax holidays will also be considered for fund managers who manage more than S$5 billion of foreign investor's funds in Singapore and are accorded the Enhanced Fund Manager (EFM) status. However boutique asset management houses are not entitled to such treatments as the criteria for qualifying under the AFM scheme is biased against start-ups and alternative investment professionals. This impedes the formation of a critical mass of asset management professionals who might otherwise base their operations here.

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[22] For further elaboration on the scheme, please visit the Central Provident Fund website at www.cpf.gov.sg A chapter on CPF has also been dedicated in Financial Services in Singapore by Tan Chwee Huat.
[23] A copy of the consultation paper can be viewed at http://www.cpf.gov.sg/cpf_info/ConsultationPaper.pdf

As fund management companies are exposed to lower risks than securities companies, they generally need less capital. The criteria for obtaining a Capital Market Services (CMS) license were too high, thus keeping smaller but well-managed fund management companies of good repute out of Singapore. The MAS has relaxed the financial requirements to qualify for a CMS license without compromising the prudential standards to safeguard investor's capital. The minimum amount of shareholder's fund required for a CMS license for a boutique fund manager has been lowered from S$500 million to S$100 million. Likewise, the minimum amount for global funds management (other than boutique fund management) has been reduced from S$5 billion to S$1 billion.

The Government has been urged by industry players to revise the Trustee Act and Insurance Act to allow for more asset classes to provide for greater flexibility for fund managers as other investment assets would be recognized within the fixed income classification. The bulk of funds available for investment in Singapore are concentrated in institutional hands. Many Singapore entities, including statutory boards are bound by the Trustees Act. The investment guidelines under the Trustees Act, intended for the protection of widows and orphans work against the growth of the asset management industry as non-retail hedge funds, foreign funds, non-Singapore equities and derivatives are not permitted investments.

Outplacement of Government Investment Corporation (GIC) funds to private fund managers would encourage the influx of professional talents into Singapore and help

nurture the finance professionals locally. Under the mandate, fund managers are expected to bring in funds of their own to manage in Singapore, which would help deepen the liquidity of the markets. The GIC has made substantial progress in placing out funds, where S$10.8bn out of the S$25bn scheduled for outplacement had been released at the end of 1999. The FSWG has also highlighted several key measures such as improving investor education as well as the professional training to boost Singapore's competitiveness as an asset management centre.

Following the collapse of the Long Term Capital Management (LTCM), the incident raised questions about the risks that large and highly leveraged hedge funds pose to systemic stability and made authorities cautious on such investment agencies. Singapore however, recognizes the value of innovation and has actively solicited the set up of hedge funds, as well as granting of mandates from the GIC to spur the influx of leading hedge fund firms to set up operations in Singapore. A robust hedge fund industry in Singapore will help to extend the range of investment products available in Singapore and also contribute to Singapore's development as a premier asset management hub. The spin-offs to ancillary service sectors such as legal, trustee and custody services are beneficial to the overall development of manpower.

The latest development in the Singapore fund management industry is the entry of Temasek Holdings into the unit trust fund arena. Temasek Holdings launched its first unit trust i.e. the Fullerton Short Term Interest Rate Fund (FSTIR Fund) in September 2004. The fund will be managed by Fullerton Fund Management Company, a newly

incorporated entity that is wholly-owned by Temasek. The move is likely to give the industry a boost for the local unit trust industry.

Hong Kong

Hong Kong's success in the fund management sector has generally relied upon the efforts of the firms rather than on government sponsorship. However, as competition heats up for more funds and expertise, the laissez-faire approach would not be overly appropriate. The government has to take on a leading role to drive the Hong Kong fund management industry.

One successful initiative was the launch of the Hong Kong' Mandatory Provident Fund (MPF) in the year 2000. Unlike Singapore where the Central Provident Fund (CPF) is largely managed by the Government, Hong Kong's MPF is managed by the private sector which helps to bring in the fund agencies and the expertise to enlarge the pool of financial professionals.

Attributing the growing importance of the Hong Kong Monetary Authority (HKMA) as a source of mandates for fund management would lead to an increase in the AUM. The increase of assets under mandates from the HKMA is likely to stimulate the industry and attract more fund management firms and professionals into Hong Kong to get a bigger slice of the market.

Relaxation on the restrictions on short selling and derivative trading would enable hedge funds and other professional firms to engage in the Hong Kong fund management industry. Current restrictions inhibit the potential boom of the industry given the investment style of hedge funds and other alternative investments agencies.

At present there are four regulators in the MPF segment: the MPF authority, the SFC, the Insurance Commission and the HKMA. The web of bureaucracy that industry participants have to sieve through impedes the efficiency in carrying out fund management activities. A proposed streamlining and simplification of the regulators leading to an improved set of regulations will encourage participants to be more active in the fund management industry.

4.4 Debt Market

4.4.1 An Overview

Debt markets are a major form of financing which has been well developed in countries like the United States and United Kingdom. They are also keys to the foundation of an international financial centre. The development of debt markets in Singapore has been one of the key components of the MAS's initiatives to enhance Singapore's role as an international financial center. (Ngiam and Loh 2002)

MAS's agenda consisted of a series of bold reforms, including the liberalization of the Singapore dollar and the development of Singapore into a hub for the primary issuance as well as secondary trading of debt securities. The debt markets in Singapore

are made up of three major segments: Singapore government securities (SGS[24]) market, the Asian dollar bond (ADB) market, and the Singapore dollar corporate bond (SDCB) market.

Hong Kong's bond market is the second largest in Asia behind Japan. According to the HKMA, Hong Kong's bond issuing bodies include the Exchange Fund, statutory organizations, multilateral development banks (MDB[25]s), non-MDB overseas banks, authorized institutions (AI[26]s) and local corporations. They are all subject to certain restrictions in their bond issuing needs. Public sector bonds are the Exchange Fund Bills and Notes issued and managed by the Hong Kong Monetary Authority (HKMA). Private sector bonds are issued by commercial banks; non-bank corporations including statutory bodies such as the MTR Corporation, Kowloon-Canton Railway Corporation and Airport Authority; and supranational issuers such as the World Bank group and Asian Development Bank.

The Hong Kong government has long been taking a prudent approach in its fiscal policies. Historical fiscal surplus in the past removes the need for issuing treasury bonds. The Exchange Fund bills and notes issued have been regarded as quasi government papers and a ten-year yield curve has been established as the benchmark for Hong Kong's bond market.

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[24] More information on SGS can be located at www.sgs.gov.sg

[25] MDBs refer to Asian Development Bank (ADB), Council of Europe Social Development Fund (CEF), European Company for the Financing of Railroad Rolling Stock (Eurofima), European Investment Bank (EIB), European Bank for Reconstruction and Development (EBRD), Inter-American Development Bank (IADB), International Bank for Reconstruction and Development (IBRD), International Finance Corporation (IFC), African Development Bank (AfDB), and Nordic Investment Bank (NIB).

[26] AIs include licensed banks, restricted licence banks (RLBs) and deposit-taking companies (DTCs).

4.4.2 Performance

Despite the fact that the Singapore Government has run budget surpluses since the 1980s and maintains huge reserves, the SGS market remains the biggest segment of the debt markets in Singapore. The Asian dollar and Asian foreign currency bond market developed in the early 1970s as part of Singapore's efforts to build up an offshore financial industry. The MAS had actively promoted the developments and encouraged such efforts before the Asian Financial Crisis. For example, the Finance and Banking Subcommittee of the Ministry of Trade and Industry's Committee on Singapore's Competitiveness observed in May 1997 that Singapore's debt market was illiquid and recommended that the market be developed. The Asian Financial Crisis gave further impetus to their policy objectives, showing clearly that countries in the region needed to develop their capital markets to diversify funding sources and rely less on commercial bank loans.

Since Singapore historically ran - and continues to run - large budget surpluses, and the government maintains huge reserves, the Singapore Government has traditionally had no need to resort to finance the budget through the issuance of bonds or Treasury notes. Thus, the rationale behind issuing SGS has been to stimulate the emergence of a debt market, and to establish benchmark rates. Five years on, the results have been encouraging. The SGS market has grown at an average rate of over 15% since 1998, with average turnover rising 360% since 1998, to over S$2.6 billion (US$1.54 billion) in

2003[27]. To encourage further liquidity, the Government has increased the size of its SGS issuances with issues generally now averaging S$2-3 billion. There are currently 11 approved primary dealers in SGS, and 23 approved secondary dealers. The MAS issues three-month T-bills weekly, while one-year T-bills, as well as two, five, seven and ten year bonds are issued regularly. As of January 31, 2004, S$64 billion (US$37.6 billion) in SGS were outstanding, comprising S$19.2 billion (US$11.3 billion) in T-bills and S$44.8 billion (US$26.3 billion) in bonds.

The other pillar of the Government's strategy has been to encourage the development of a corporate S$ bond market. The response has been impressive. The total amount of debt securities increased by an average of 140% from 1998 to 2003, from S$9.1 billion to S$67.2 billion (US$5.4 to US$39.5 billion). While non-S$ issues, i.e., Asian dollar and other foreign currency issues, account for 70% of that total, S$ debt also rose to S$19.3 billion (US$11.4 billion) in 2003, an increase of more than 5 times the amount issued in 1998 (S$3.9 billion). According to MAS 2003 survey[28], the profile of S$ issuer has diversified, where statutory boards which were previously dominant issuers formed only 3% of the market as compared to 22% in 1999. A myriad range of corporations, property companies and financial institutions makes up the rest of the debt issuers as the Singapore dollar bond market has developed beyond serving the needs of just local borrowers and attracted a diversified base of foreign issuers as an alternative venue for cost-effective funding. Large issuers, including Freddie Mac, Fannie Mae and Asian Development Bank have found cost-effective opportunities to tap Singapore’s

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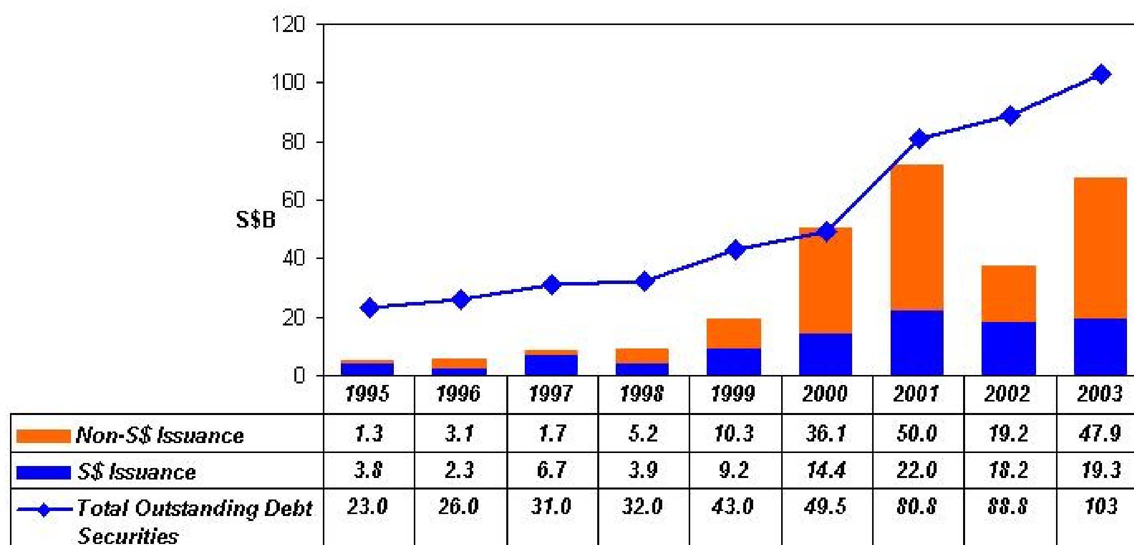
[27] www.sgs.gov.sg

[28] The findings and results can be viewed at www.mas.gov.sg

bond market. In five years, the market has grown significantly in breadth and depth. Product range has also increased significantly. Structured products now account for more than half of the Singapore dollar bond market. The asset securitization market has also gained traction, recording a fivefold increase since 1999[29].

Table 9: Size of the Corporate Bond Market



	1995	1996	1997	1998	1999	2000	2001	2002	2003
Non-S$ Issuance	1.3	3.1	1.7	5.2	10.3	36.1	50.0	19.2	47.9
S$ Issuance	3.8	2.3	6.7	3.9	9.2	14.4	22.0	18.2	19.3
Total Outstanding Debt Securities	23.0	26.0	31.0	32.0	43.0	49.5	80.8	88.8	103

Source: MAS: 2003 Survey of the Singapore Corporate Debt Market
Note: Excludes Singapore government debt securities (treasury bills and bonds)

Government-Linked Companies (GLCs) and statutory boards have responded to the call of establishing a yield curve benchmark by launching a series of progressively larger issues. As an example, in January 1998, the Jurong Town Corporation (JTC) launched a S$300 million 7-year bond offer, followed by two additional S$300 million 10-year issues in 1999, and a S$200 million 12-year issue in Q4 2000. The Housing and Development Board (HDB) has launched several issues, beginning with a S$300 million 5-year issue in 1999 and leading to the latest, S$500 million 10-year and 5-year bonds in 2004 were issued. The proactive measures taken by the government to establish a

[29] Opening remarks by Mr. Koh Yong Guan, Managing Director, at MAS' Annual Report 2003/2004 Press Conference.

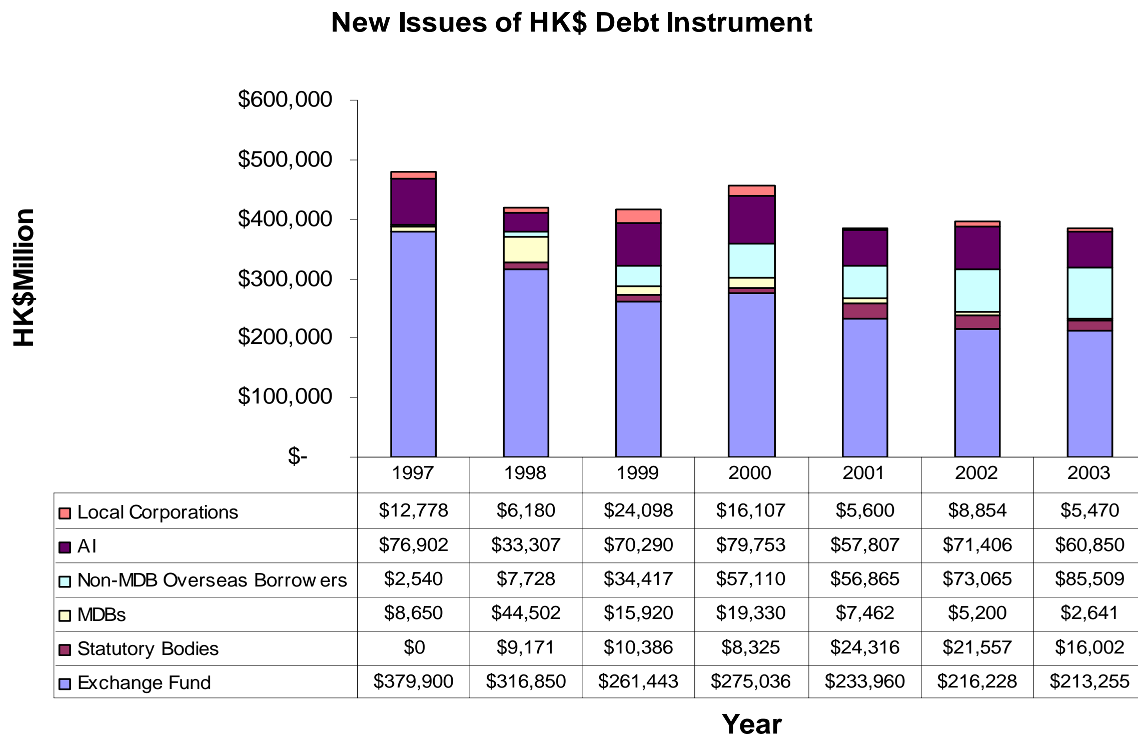
benchmark yield curve led to Singapore being the first Asian economies other than Japan to be listed on the JP Morgan bond index.

Many financial sector analysts see the S$ bond market as promising. The issuer base has diversified, from being dominated by property companies in 1998 to a better mix of GLCs, statutory boards, foreign entities, and financial institutions. In addition, the volume of derivative transactions has also increased. One key constraint is the very shallow secondary market for S$ debt. Insurance companies have been the largest buyers of S$ issues to date. With a huge appetite for fixed-income securities, especially of longer maturities, they rarely trade, adopting instead a long-term, "buy and hold" approach. As a result, the S$ bond market is mainly a primary market, with little secondary trading. The lack of liquidity and depth of the market also serve to keep foreign fund managers from putting funds into the market. The lack of depth, combined with the still-small size of the market has made foreign fund managers less interested in entering the market.

Unlike Singapore whose currency is not internationalized, Hong Kong has pegged its dollar to the US$ thus making the currency convertible. Thus, the fixed income instruments issued are commonly in Hong Kong dollar. The issuance of Hong Kong dollar debt declined by 3% to HK$384 billion in 2003. Following a sharp increase of 28% in 2002, debt issuance by overseas borrowers other than MDBs rose by 17% in 2003 to HK$86 million. This was however more than offset by the substantial decline in domestic private sector debt issuance as well as AIs and local corporations falling by 15% and 38% respectively.

New issues of fixed-rate debt, excluding Exchange Fund paper, continued to grow strongly in 2003, rising by 18% to HK$120 billion. The low interest rate environment in Hong Kong appears to be particularly attractive to foreign corporations as clearly shown by the increasing proportion of fixed-rate debt issuances in Table 10. The average maturity profiles of new debt issues have been extended by borrowers to lock in the low borrowing costs.

<u>Table 10: New Issues of Hong Kong Dollar Debt Instruments</u>



	1997	1998	1999	2000	2001	2002	2003
Local Corporations	$12,778	$6,180	$24,098	$16,107	$5,600	$8,854	$5,470
AI	$76,902	$33,307	$70,290	$79,753	$57,807	$71,406	$60,850
Non-MDB Overseas Borrowers	$2,540	$7,728	$34,417	$57,110	$56,865	$73,065	$85,509
MDBs	$8,650	$44,502	$15,920	$19,330	$7,462	$5,200	$2,641
Statutory Bodies	$0	$9,171	$10,386	$8,325	$24,316	$21,557	$16,002
Exchange Fund	$379,900	$316,850	$261,443	$275,036	$233,960	$216,228	$213,255

Source: HKMA Quarterly Bulletin March 2004
No statutory bodies' debt instrument was issued in 1997

In Hong Kong, a two-tier dealership scheme was set up when the Exchange Fund Bills and Notes Programs were implemented. A number of Recognized Dealers (RDs) and Market Makers (MMs) in Exchange Fund Bills and Notes were appointed by the HKMA. There are currently 128 approved RDs and 26 MMs in the Exchange Fund Bill, 126 RDs and 28 MMs in the Exchange Fund Notes and 107 RDs and 47 MMs dealing in Specified Instruments. Under the Exchange Fund program, bills of 91-, 182- and 364-day maturity are auctioned in form by public tender regularly. As of end 2003, HK$120,152 million (US$15,404 million) were outstanding.

4.4.3 Reforms to Date

Singapore

In 1998, the Government announced a series of actions to stimulate the market. The MAS would begin to issue more Singapore Government Securities (SGS), with larger issues and longer maturities. Statutory boards and government-linked corporations would issue more bonds. The MAS granted tax exemptions for fee income earned by financial institutions arranging debt securities in Singapore. This would apply to both S$ debt and Asian dollar and other foreign currency debt launched in Singapore. The Government also announced that interest income earned by non-residents which do not have permanent establishments in Singapore will be exempted from withholding tax. Interest income earned by financial institutions and corporations from holding debt securities would be subject to a concessionary tax rate of 10 percent.

Government officials are also taking efforts to stimulate greater liquidity. In one significant change, the Companies (Amendment) Act 2000 now allows bonds or shares that are sold to "sophisticated" (i.e., institutional) investors or professionals, and for which no prospectus is required, to be sold after six months to retail investors. Before the amendment, companies were restricted to selling bonds for which there was no prospectus to less than 50 sophisticated investors, who had to hold the shares for twelve months.

The Government allowed individual Singaporeans greater flexibility in investing part of their CPF in privately-managed mutual funds and the Supplementary Retirement Scheme (SRS). These moves are intended to stimulate the debt market from the demand side in the hope that smaller, more risk-adverse investors will find funds investing in fixed-income investments, such as corporate bonds, attractive.

The MAS has also loosened restrictions further in several areas to stimulate the S$ corporate debt market. These changes include allowing banks to lend S$ to non-residents for investment purposes in Singapore, including investments in S$ equities, bonds, and real estate; allowing banks to transact S$ financial derivatives (such as futures and options) with banks and financial institutions; and treating foreign securities intermediaries in Singapore as "residents" for the purpose of freely obtaining S$ financing in the market. In addition, with effect from 20 March 2002[30], MAS has further liberalize its S$ non-internalization policy by allowing non-resident financial entities to engage freely in S$ swap activities with non banks. The measures represent another

[30] MAS Press release 19 March 2002 – “MAS further liberalize S$ Non-Internalization Policy”

significant step in facilitating participation by international investors and financial institutions in Singapore's capital markets.

To enhance the attractiveness of Asian capital markets, MAS has over the past year, worked with various governments in the region to encourage investor demand, and to address market access and market infrastructure issues. The Asian Bond Fund or ABF is one such initiative. The MAS is also working with its ASEAN counterparts on an investors' seminar to take place later in the year to raise global awareness of the regional capital markets. There are ongoing works by leading scholars to assess the usefulness of the ABF. In Eichengreen (2004), the author questioned the effectiveness of the ABF in addressing the development of the regional bond market.

Hong Kong

Over the past years, the authorities have introduced several new measures to foster the development of the Hong Kong debt market. These included improving the debt securities clearing infrastructure, promoting Exchange Fund Notes in the retail market, expanding the profits tax concession scheme and streamlining regulations on issuing and listing debt securities.

Ever since the HKMA began implementing out-bound links from the Central Moneymarkets Unit (CMU) to other regional and international central securities depositories in 1997, the CMU has evolved as a one-stop debt securities clearing, settlement and custody platform for Asian investors. Through the CMU, Asian investors

can settle and hold domestic debt securities in Australia, Hong Kong, Korea and New Zealand, as well as international debt securities lodged with other custodians. The Euro Clearing system implemented in April 2003 enabled CMU members to settle, in addition to Hong Kong and US dollar, euro-denominated debt securities on a Delivery versus Payment (DvP) basis.

In August 2003, the HKMA launched a one year pilot scheme to facilitate retail investment in Exchange Fund Notes. Under the scheme, a portion of the 2-year and 3-year Exchange Fund Notes issued each quarter is made available for non-competitive tender by retail investors through three designated Retail Exchange Fund Notes Distributors namely 1) the Bank of East Asia, 2) DBS Bank (HK) and 3) Wing Lung Bank. In addition to providing the non-competitive tender service, the distributors agreed to adhere to a number of unified standards in the distribution of Exchange Fund Notes to retail investors in the secondary market to enhance pricing transparency and facilitate comparison by retail investors. While welcoming progress in the retail bond market, the HKMA is also concerned that the public might not be aware of the risks associated with fixed income product investments. In this regard, the HKMA has added a new section, "Exchange Fund Notes: Information for Investors", to its website to educate retail investors on bond investment.

The Hong Kong Government expanded some tax concessions to stimulate demand for debt securities. In the Budget 2003, trading profits from Qualified Debt Instruments (QDI) with a maturity period of 7 years or more, which previously were

eligible for a 50% profit tax concession, would be exempted totally from profit tax[31]. In addition, the Government relaxed the minimum maturity requirement on the current 50% tax concessions on QDI profits from 5 years to 3 years.

To further improve the regulatory framework for a robust fixed income market, the Government implemented in three phases, measures to streamline the regulations and procedures for issuing and listing debt securities. Measures under the first phase involved the issuance of various guidelines by the Securities and Futures Commission (SFC) in February 2003. These included permitting awareness advertisements, an alternative "dual prospectus" structure and allowing faxed copies of expert consent letter and bulk print proofs of prospectuses for the purpose of registration. A two-class exemption by the SFC in relation to prospectuses for offer of debentures also came into operation in May 2003. The second phase was the introduction of the Companies (Amendment) Bill 2003. It proposed to simplify procedures for registration and issue of prospectuses. In the third phase, the SFC will conduct a comprehensive review of the existing laws and procedures against international standards, with a view to facilitating the issuance and listing of securities. The SFC has started the review and aims to put forward proposals for public consultations by September 2004.

[31] Qualified debt securities (QDSs) are debt paper (a) issued to the public in Hong Kong (b) with an original maturity of not less than 5 years (c) with a minimum denomination of HK$50,000 or its equivalent in a foreign currency (d) lodged with and cleared by the CMU in its entirety and (e) for papers issued by non-statutory bodies or non-government owned corporations, they would need to have at all relevant times a credit rating from a recognized rating agency acceptable to the HKMA.

4.5 Insurance Industry

4.5.1 Overview

The Hong Kong insurance market has two major components: general insurance and long term insurance. General insurance includes accident and health, aircraft, hull, goods in transit, property damage, general damage, general liability, pecuniary loss and two statutory classes, motor vehicle and employees' compensation. Long term insurance includes non-linked and linked individual life, group life, and retirement schemes. As at 30 June 2004, there were 183 authorized insurers in Hong Kong, of which 119 were pure general insurers, 45 were pure long-term insurers and the remaining 19 were composite insurers. The industry is regulated by the Office of Commissioner of Insurance[32] which administers the Insurance Companies Ordinance.

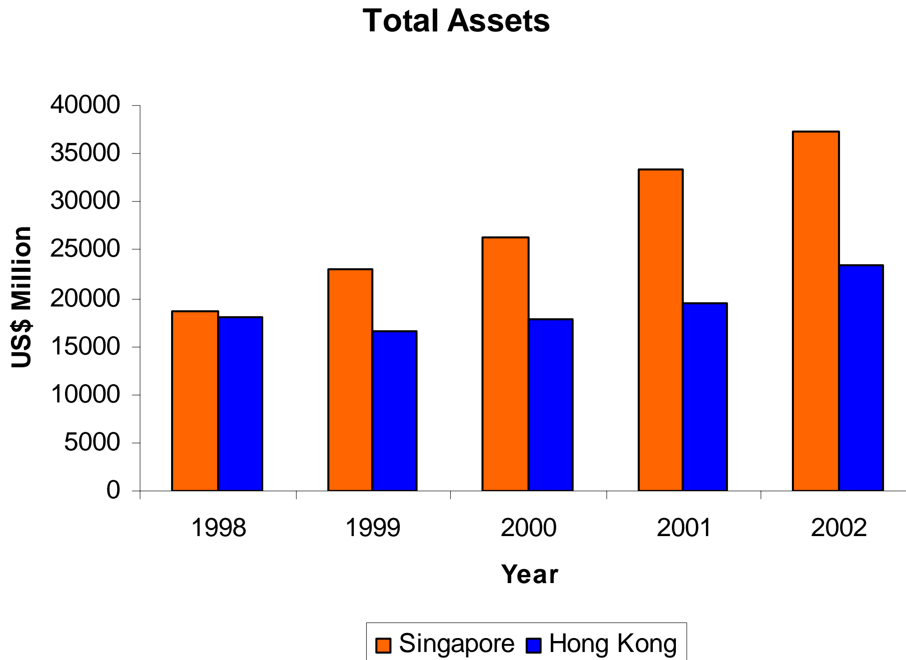
Similarly, the Singapore insurance industry comprises the general insurance and life insurance which also classifies the various businesses as in the case of Hong Kong. As of July 2004, there were 133 insurance companies of which 51 were direct insurers, 29 reinsurers and 53 captives. The MAS takes a pro-active approach in the regulation and supervision of the insurance industry and conducts periodic checks to test the robustness of the insurance companies.

[32] Office of Commissioner of Insurance, www.oci.gov.hk

4.5.2 Performance

The Hong Kong insurance industry as a whole has continued to grow in 2002. According to the latest audited statistics released by the OCI, total gross premiums[33] grew by 20.6% continuing the turnaround trend registered since 2000. Total gross premiums increased to HK$23.45 billion from HK$19.44 billion in 2001. In Singapore, the insurance industry performance report in 2002 released by MAS showed that the total premiums[34] of the insurance industry for 2002 amounted to S$16.7 billion, a decrease of 9.4% over 2001. Total assets of the industry expanded by 11.9% to S$66.8 billion. Table 11 shows total asset of the insurance industry in Singapore and Hong Kong from 1998 – 2002.

<u>Table 11: Total Assets of Insurance Industry</u>



Source: MAS Insurance Statistics, OCI Insurance Statistics

[33] Annual Statistics 2002: Table G5 - Premiums includes Direct & Reinsurance Inward Business
[34] This includes annual premiums in force and new single premiums of life business as well as gross premiums of domestic and offshore general business.

In Hong Kong, all major classes of general insurance business experienced premium growth of 20.6% in 2002. General Liability business, comprising mainly employees' compensation insurance business, showed the biggest growth of 55.3% in gross premiums, followed by property damage, motor vehicle and accident & health businesses, with growth rates ranging from 7.6% to 16.2%. Total gross premium increased to $23,448 million from $19,436 million in 2001. The overall underwriting result of general insurance business improved from a loss of $473 million in 2001 to a profit of $1,243 in 2002, turning around the loss trend experienced in the past five years.

In Singapore, the total gross premiums for the general insurance industry grew strongly by 24.5% to $4.8 billion in 2002[35]. Domestic business grew by 23.9% to $2.2 billion and offshore business grew by 25.0% to $2.5 billion. The general insurance industry is focused on returning to fundamentals and achieving positive underwriting results as forecasted by MAS.

A report compiled by Swiss Re[36] titled World Insurance Data 2003[37] ranked Hong Kong as the top economy with the highest insurance density and penetration in the emerging market in 2003 with a US$1833 premium per capita while Singapore took 2nd

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35 Insurance Report 2002, MAS

36 Swiss Re is one of the world's leading reinsurers, operating through more than 70 offices in over 30 countries. The company has been in the reinsurance business since its foundation in Zurich, Switzerland, in 1863. Through its three business groups Property & Casualty, Life & Health and Financial Services, Swiss Re offers a wide variety of products to manage capital and risk. Traditional reinsurance products, including a broad range of property and casualty as well as life and health covers and related services, are complemented by insurance-based corporate finance solutions and supplementary services for comprehensive risk management www.swissre.com

37 Swiss Re, sigma No3/2004

place with US$ 1621 amongst the 62 countries on the list which included China, Malaysia and other Asian countries. Table 12 shows the ranking of the countries in Asia in 2003 by the total premium income received. As highlighted in the table, Hong Kong position on the world ranking was 25 gaining a 18.6% in the premium volume (inflation adjusted) in 2003 while Singapore took the 29th position having seen a drop of 5.8% in its premium volume in the same year. Part of the reason could be attributed to the outbreak of SARS, which could explain the sluggish performance of life insurance industry in Singapore. Despite the non-life insurance gaining a 6.5% increase (inflation adjusted) in Singapore, it was more than off-set by an 11.9% reduction in life insurance premium in the same period.

Hong Kong had weathered through the crisis better, despite the two economies been severely affected by the outbreak. A point to note here is that the figures released by the report may not necessarily represent the official audited statistics by the regulatory authority for the insurance industry respectively. According to the Insurance Information Institute[38], the premium earned in Hong Kong and Singapore in 2003 accounted for only 0.42% and 0.30% of the world total premium respectively. The figures are still a far cry from the world's leading insurance countries as tabled in Appendix 4 of which the tenth position i.e. Spain captured 1.60% of the US$2,904 billion insurance premium market.

[38] The Insurance Information Institute (I.I.I) is recognized by the media, governments, regulatory organizations, universities and the public as a primary source of information, analysis and referral concerning insurance. www.iii.org

Table 12: Total Premium Volume in Asia 2003

Ranking	Country	Premium Volume (in millions of US$)		Changes (in %) 2003		Share of World Market 2003 (in %)
		2003	2002	Nominal (in US$)	Inflation adjusted	
2	Japan	478 865	445 940	7.4	-0.1	16.28
7	South Korea	59 758	56 720	5.4	-1.2	2.03
11	PR China	46 911	36 961	26.9	25.5	1.60
15	Taiwan	32 402	28 714	12.8	12.7	1.10
19	India	17 302	14 664	18.0	8.3	0.59
25	**Hong Kong**	**12 494**	**10 742**	**16.3**	**18.6**	**0.42**
29	**Singapore**	**8 898**	**9 146**	**-2.7**	**-5.8**	**0.30**
31	Israel	6 892	6 727	2.5	-2.2	0.23
33	Malaysia	5 609	4 881	14.9	13.6	0.19
34	Thailand	4 932	4 102	20.3	14.1	0.17
41	Indonesia	3 107	2 579	20.5	Na	0.11
46	Iran	1 484	1 134	30.9	14.8	0.05
49	Philippines	1 192	1 155	3.2	Na	0.04
51	U.A.E	971	895	8.4	Na	0.03
52	Saudi Arabia	941	905	4.0	Na	0.03
58	Vietnam	550	504	8.9	Na	0.02
59	Lebanon	520	469	10.9	9.5	0.02
65	Pakistan	434	388	11.8	Na	0.01
76	Kuwait	320	311	2.8	Na	0.01
78	Bangladesh	297	268	10.8	Na	0.01
82	Oman	257	248	3.6	Na	0.01
84	Sri Lanka	239	212	12.8	Na	0.01
87	Jordan	220	207	6.1	Na	0.01
	Other countries	1161	1 045			0.04
	Total	685 753	628 919			23.32

Source: Swiss Re, sigma No 3/2004, www.swissre.com

4.5.3 Reforms to Date

Singapore

In an article by the Asia Insurance Review[39], some of the key initiatives undertaken by the regulators were discussed. Some of the reforms are presented as follows. The MAS has moved from a 'one-size-fits-all' rule-based approach to a risk-based supervisory approach. Working closely with the industry on many of the issues for reforms, MAS has actively involved representatives such as the Singapore Actuarial Society and the Institute of Certified Public Accountants of Singapore in the

[39] Issue No. 049/10/2003

developments of frameworks to enhance Singapore's role as an insurance and reinsurance hub.

The MAS has also been working with various trade associations to set up standards for the industry. The MAS-appointed committee, CEDLI which stands for Committee for the Efficient Distribution of Life Insurance has made a series of recommendations to enhance the standards of distribution of life insurance products, including training and competency requirements. The MAS also worked with the General Insurance Association (GIA) to form CESGI, the Committee for Enhanced Standards for General Insurance. A framework for training and competence for distributors of general insurance products has been drawn up.

The MAS has put into operation in 2002 a risk-based framework in supervising insurance companies. The framework aimed at identifying areas in an insurer's operation that possess significant inherent risks and examining how such risks are being mitigated. Insurers are graded according to their risk profile and the strength of their risk-mitigating measures into 5 different "stages of health", ranging from "Normal" to "Viability-at-risk", with the most critical stage being "Winding-up or Closure". Companies that are in comparatively poorer "health" will be given more intensive supervisory attention. The implementation of the new supervisory approach would hence create incentives for insurers to strengthen their internal controls and risk management systems, where such controls and systems are currently weak or non-existent.

The Risk-based Capital (RBC) Framework for insurance industry, which was being rigorously tested in the past years and is at its final stage of development, has been launched in 2004. The MAS has been working with market practitioners and representatives of professional associations to develop risk-based capital models for life and non-life insurance businesses. The risk based capital framework aims to refine the treatment of liability risks, and set appropriate capital charges for asset risks and concentration risks. It should provide early indications of financial weaknesses, and thereby facilitate progressive intervention by insurance companies and MAS. The public consultation on the proposed RBC was launched in November 2003 with the RBC framework being implemented in August 2004. However, registered insurers in Singapore have until 1 January 2005 to comply with the new requirements. During the transition period, existing requirements will apply to insurers that have not adopted the new framework.

According to MAS[40], risk-based supervision reduces the need to rely on high minimum paid-up capital. The regulator decided to lower the minimum paid-up capital requirements for direct insurers from the existing S$25 million, to S$10 million for full-fledged insurers, and S$5 million for mono-line insurers in a move to develop the market further, and especially to attract certain niche insurance players to Singapore.

An important reform in 2002 was the full implementation Financial Advisers Act (FAA) in October. The Act provided the framework for a disclosure-based regime which maintains fair and efficient markets and sets high standards of professional conduct to

[40] Keynote Address by Deputy Prime Minister and Chairman, Monetary Authority of Singapore Lee Hsien Loong at the 10th Annual Conference of the International Association of Insurance Supervisors (IAIS)

help investors make well-informed decisions. The FAA sets the minimum entry and examination requirements for representatives. Besides being professionally qualified, representatives must also be competent, efficient, honest, and have integrity and sound financial standing. The regulatory authority has issued a set of guidelines to financial advisers to help ensure that they employ fit and proper persons.

Much work has been done over the past year to develop a regulatory framework for health insurance business as the need to finance costs of healthcare through insurance is expected to grow tremendously with the aging population and the increasingly well-informed and more affluent public who expects more. Recognizing the market's needs for long-term health insurance services, many insurers have begun introducing products with non-cancelable and pre-funding features in recent years. As these features require long-term financial commitments to be made by consumers, it is important that the information disclosed to consumers is sufficient for them to make an informed decision on the financial commitments that they are undertaking. In addition, persons employed in distribution channels should be competent and provide sound advice on health insurance. The proposed health insurance framework, which addresses the above issues, is expected to be launched in 2004.

Another development in the insurance industry was the launch of the Insurance Disputes Resolution Organization (IDRO) in March 2003. IDRO is an alternative and independent channel for resolving insurance disputes. It has replaced the Insurance Ombudsman's Bureau and the Tribunal for Third Party Property Damages. The primary concern of MAS is to protect the interest of the insuring public, without compromising on

the standards and disclosures. MAS is also facilitating the development of an integrated dispute resolution scheme for the financial sector. An integrated scheme would benefit consumers by providing the convenience of a one-stop shop and ensure that consistent processes and procedures are applied across sectors which to date do not exist.

To spur the insurance industry further, the CPF Board has announced that the Dependants Protection Scheme (DPS) will be privatized[41]. The CPF Board plans to appoint the private insurers by end 2004 and hand over the DPS to them by the first half of 2005. The selection criteria of private insurers will include their financial strength, proven operation efficiency and ability to provide good customer service. Privatization will allow for healthy competition among the private insurers.

Hong Kong

Based on the responses received from earlier consultation with the self-regulatory organizations[42] (SROs) and other stakeholders, the Insurance Authority ("IA") compiled a list of proposed improvements for further industry consultation. The IA and the industry have reached a consensus that refinements should be made to the existing self-regulatory system to improve its effectiveness and efficiency. On the basis of the industry's comments, the IA is in the process of liaising with the SROs to implement a number of proposals. Some items of the proposed improvements have been implemented. The IA keeps an open mind on the way forward and will keep on liaising with the industry and

[41] News release on CPF website 23rd June 2004 www.cpf.gov.sg
[42] Includes the Hong Kong Federation of Insurers, the Insurance Agents Registration Board, the Hong Kong Confederation of Insurance Brokers and the Professional Insurance Brokers Association Limited

parties concerned to enhance the regulatory system for insurance intermediaries and further protect the interests of the insuring public.

In December 2003, the Insurance Authority (IA) released a Public Consultation Paper on the feasibility of establishing insurance policyholders' protection funds (PPFs) in Hong Kong. PPFs aim to provide a safety net to policyholders where compensation will be paid if an insurer runs into financial difficulties and unable to make payments under its insurance policies. At present, there are no PPFs in Hong Kong, only two insolvency funds for statutory motor and employees' compensation insurance respectively. PPFs are common in many advanced economies.

The IA launched the Continuing Professional Development (CPD) Program which aimed to ensure that the insurance intermediaries continue to possess professional standard in providing advice to policyholders. The insurance intermediaries are encouraged to carry on lifelong learning, enhance professionalism and deliver excellent services through the inspiration of the CPD Program.

High on the agenda for the IA is the liberalization of the management of life insurance assets. As revealed by the Commissioner of Insurance, regulators are looking at alternative investment and management options for life insurers, including the possibility of allowing them to invest their assets overseas. The IA has engaged independent external consultants to explore the options and develop an implementation plan that will be announced in the later half of 2004.

As a trade pact between Hong Kong and China, the Closer Economic Partnership Agreement (CEPA) focusing on Trade in Goods, Trade in Services and Trade & Investment Facilitation will give insurers easier and wider accessibility to the mainland market. This will give insurance companies the opportunity to use Hong Kong as a spring board to the vast market.

SECTION 5 – CONCLUSION AND RECOMMENDATIONS

While Hong Kong and Singapore economies are small by comparison to the G7 economies, their economies have gained swift economic growth since the 1970s. Both Hong Kong and Singapore have emerged as promising economies in this new age. Their dominant positions as regional trade hubs accelerated demand for financial services in their formative years. The presence of a critical mass of foreign and domestic banks has also helped the economies to exploit opportunities for further financial development beyond the primary role of traditional trade financing to an advanced stage of financial intermediation.

The development of the two international financial centres is the result of different philosophies. Unlike Hong Kong, Singapore developed as an international financial centre mainly through active government policies. The Hong Kong government adopts a policy of non-intervention and laissez-faire that encourages entrepreneurial inflow as Ng (1998) had put it. Singapore has been successful in that the government creates and maintains Singapore's niche in the international financial market by adaptive

maintenance of internationally competitive tax structures and constant provision of a sound and stable financial system. One common policy that both government shared however is the tight regulation and corporate governance are key elements to contributing to their status as international financial centers.

Going forward, what are the possible areas of growth for Singapore? As identified by the Economic Review Committee – Financial Services Working Group (FSWG) 2002, Singapore has to play to its strengths in areas where it can develop a niche given the limited size and resources. Bermuda has built itself as a niche financial centre for risk management, Zurich and Geneva are for private banking and Dublin is for processing and fund administration activities. Singapore can build its distinctive advantages by engaging in areas such as private banking, fund management and risk management.

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Appendix 1: Recommendations by Various Committees, 1985, 1998, 2002

	Sub Committee on Banking & Financial Services Recommendations (1985)	Committee of Singapore's Competitiveness Recommendations (1998)	Economic Review Committee Financial Services Working Group Recommendations (2002)
FUND MANAGEMENT			
1	Remove tax incongruities on remitted offshore income, interest on Singapore-derived and use of Singapore-based fund managers and give clear demarcation between trading profits and capital gains.	The pace at which public sector funds (including Singapore's foreign reserves) are allocated to the private sector should be increased, with at least 20% for management in 3 years by fund managers in Singapore.	Expand Government's role in development asset management industry i. Develop start-ups and small and medium sized fund managers ii. Extend fund management mandates granted by GIC and MAS iii. Provide funds to attract private equity players.
2	CPF contributors to have part of their CPF funds managed by fund managers of their choice. Widen participation in COWEC scheme.	Fund managers should not have to guarantee principal as required by some Government agencies.	Boost competitiveness as a pre-eminent asset management centre i. Improve tax treatment ii. Review CPF structure iii. Improve investor education iv. Improve professional training.
3	Allocate Government-managed CPF funds to fund managers in Singapore.	Abolish estate duty. It no longer serves the purpose of wealth distribution. Alternatively, exemption from estate duty should be based on the gross value of the estate, regardless of asset class. The cut-off for estate duty exemption should be increased.	Increase focus on developing alternative assets clusters i. Raise development focus and regulatory responsiveness ii. Establish limited partnership structures in Singapore iii. Reform Trustees Act iv. Streamline tax incentives for private equity into one single package v. Increase tax certainty for private equity vi. Establish favorable tax environment for

			alternative investments vii. Upgrade professional skills in private equity. viii. Use private equity as an option to help GLCs spin off non-core assets.
4	Amend laws, e.g. Insurance Act to permit broader range of authorized assets	i. Rationalize unit trust regulation and administration. ii. Reduce processing time for unit trust applications to 4-6 weeks. iii. Standardize trust deeds to expedite the approval process. iv. Separate prospectuses into 2 sections: a standard section containing regulatory information and the other containing ‘investor-friendly” information relating to the investment objective and policy, fees, charges and risk factors as well as the track record of the fund manager. v. Allow for more flexibility in the promotion of unit trusts (both in respect of advertisement and in determining minimum investments) vi. Task force to be set up to identify other specifics changes to improve the competitiveness of the industry.	Develop ancillary services i. Develop Trustee and Custody services ii. Develop specialized legal, custody and other ancillary services.
5	SES to expedite establishment of OTC market.	i. Allow non-CPF funds to invest in CPF-approved unit trusts. ii. Give full discretion to (1) fund mangers of CPF-approved unit trusts and (2) managers of funds governed by the Trustees Act, to determine the geographical spread of investments, the investment instruments as well as the asset-mix, to enhance returns for the trust funds while minimizing risk. As a minimum, expand the scope of	IFER Review the fee structure under the SFA by keeping the fees unchanged under the new SFA Act.

		investment for CPF funds to all IFC developed countries. Regionally, Thailand is included in the approved lists of CPF investments. Indonesia, Philippines and China should similarly be included. Abolish the 40% cap on foreign assets and the 10% minimum liquid assets.	
6	Enlarge local capital market.	Withholding tax on distributions by unit trusts should be abolished.	<u>IFER</u> Relax procedures for offering 'restricted authorized schemes' to sophisticated investors.
7		Establish facilities for the borrowing and lending of securities quoted on the SES to provide liquidity.	<u>IFER</u> Eliminate or relax investment guidelines under the Trustee Act and Insurance Act i. Current guideline under these two Acts state the types of assets allowed for investment and set the limits allowed in different asset classes. ii. Trustee Act is narrow and too conservative iii. Guidelines to be eliminated to allow greater flexibility for fund managers.
8		Capital gains on sale of securities should not be taxed unless it is the business of the company to trade in financial instruments/assets. The authorities in reviewing the issue should examine ways in which the revenue-enhancing side of business can be promoted rather than focusing on the tax-levying side.	<u>IFER</u> Develop the depth and breadth of Singapore's fund management industry by channeling more domestic liquidity across a number of local and foreign investment management firms.
		i. Revise CPF rules and regulations relating to private pension and provident funds to encourage their development. Private pension funds can be tailored to attract, motivate and retain key personnel.	<u>IFER</u> The Government should consider developing GIC into a leading global fund management company i. GIC to consider taking on investment mandates for external clients via a

		ii. Employees should be allowed to elect to have their retirement funds placed with private pension funds rather than the CPF Board.	privatized subsidiary ii. Event privatization of GIC should be carefully considered
9		The tax treatment of funds managed by boutique fund managers should be clarified. As boutique fund managers are generally small operators, MAS should advise them of prospects for upgrading as licensed fund mangers and the criteria required.	<u>IFER</u> Create a more conducive environment i. Clients favor locations that can offer services other than financial services such a good schools, medical facilities and vibrant arts scene. ii. Development of more private schools iii. Ease travel requirements for people from Indonesia, Malaysia, Thailand, India and China to visit Singapore and arrange for reciprocal treatment for private bankers from Singapore to travel to these countries to visit their clients.
10		i. Allow approved trustee companies to establish trustee subsidiaries and holding companies in tax haven jurisdictions. The tax laws governing these subsidiaries should be reviewed. ii. Rationalize the regulation and administration of trust business to ensure flexibility and transparency. iii. Provide secrecy provisions to preserve the confidentiality of trusts, unless in criminal investigations. iv. Trust administrators should not be required to submit trust deeds and related documents executed for foreign trusts to the IRAS and Commissioner of Stamp Duties. Allow trust duty to be paid by affixing revenue stamps to the trust deeds.	

		v. Allow licensed trustee companies to set up private trust companies and any special purpose holding companies in Singapore for offshore clients. vi. Provide fiscal incentives and implement regulatory measures to encourage the development of corporate trust services. In particular, tax incentives should be provided to attract expatriate staff with knowledge of specialized trust business such as corporate trustees of infrastructure projects.	
11		Revise the Trustees Act to be more in line with the regulatory framework provided under the US Employment Income Security Act, in order to better meet the objective of prudential management of trust assets.	
		TREASURY / RISK MANAGEMENT	
1	Develop a capital market with wide range of trade-able instruments.	Abolish withholding tax on debt papers issued in Singapore. There is no withholding tax on ACU deposits. Similarly, withholding tax should not be levied on longer-dated investments.	Establish regional/global universal processing centre to support front-office and middle office activities.
2	MAS to transact more non S$ business in local market.	Provide tax incentives for targeted growth activities like project finance, cross border leasing and debt distribution.	Establish Asia Pacific risk management facility with the Asia Risk Exchange (ARX).
3	Promote fund management actively.	SIMEX should consider listing regional equity and interest rate products and their derivates to facilitate	

		fund managers' risk management and strengthen Singapore's position as a regional financial centre.	
4	Extended SDF to non-formal training overseas to develop expertise.	Expedite the listing of a Singapore Stock Index on SIMEX.	
5	Reduce telecommunication costs.		
EQUITY MARKET			
1	SES to expedite introduction of Unlisted Securities Market.	SES should review its Listing Manual to ensure that its rules and regulation remain relevant and conducive to the future development of the stock market. Steps should be taken to encourage a more active market.	IFER The SGX should accelerate the move towards open access and at a low cost to facilitate strategic decisions to be made by market incumbents on whether to use the existing SGX systems or to use alternative front and back end systems.
2	Give tax incentives for venture capital to promote growth of small companies.	Singapore's fixed brokerage should be reviewed to ensure securities transaction costs are competitive. Free brokerage rates for institutional investors and review brokerage for retail investors.	IFER SGX should compete by offering its proprietary order routing terminals or other direct access to potential market participants and investors in other countries. This will widen the reach of the SGX and provide for easier market access, thereby stimulating greater liquidity.
3	Review and loosen where possible requirements for listing on SES.	GST exemptions should be reviewed to ensure a level playing field for fund managers in Singapore managing overseas funds.	IFER MAS should review how more competition can be introduce to reduce the monopolistic role of the SGX, where such competition will facilitate greater cost efficiency, easier market access and product innovation. One area to consider is to open the securities industry value chain to competition.

4	Encourage Government owned companies and MNC subsidiaries to obtain listing.	Abolish stamp duty on all equity transactions.	IFER The convergence of some banking, securities and insurance activities can lead to greater financial product and service innovation. The SGX's regulatory role should be limited to its direct participants while broader regulatory and supervision at the wide industry level should be devolved to a separate entity such as the MAS.
5	Government to enact legislative amendments to ensure a sound securities market for the protection of the investing public and to work closely with the industry to bring about a healthy and vibrant securities industry.	Allow SES member firms to provide soft dollar commission as practiced elsewhere.	IFER Incentives should be introduced to encourage the setting up of independent research firms that can rate the instruments in the region as well as those traded on the SGX and other local exchanges.
6	Permit outside parties (local and foreign institutions) to participate in the equity of SES-member companies to strengthen their capital bases.	When promoting Singapore as a base for operations, the agenda should include encouraging foreign companies to seek a listing on the SES.	IFER Ownership structure of the CDP should be widened to include other strategic market players who can help position Singapore as the premier Asian custody and securitization centre.
7	Consider introduction of negotiated commission charges.	Allow foreign shares listed on the SES/CLOB to be traded in Singapore dollar, alternatively, allow dual currency listing	IFER Study the possibility and viability of a Singapore Alternative Market (SAM) – a separate caveat emptor, electronic, market maker driven alternative exchange for emerging new businesses.
8		Permit the use of CPF savings to buy foreign currency denominated securities listed on the SES.	
9		A committee should be set up to review the structure of the equity option market to address shortcomings.	
10		SIME should review the possibility of allowing SES members to trade stock index futures and options on SIMEX.	

11		The SES should introduce a wider range of innovative derivate products to enhance liquidity.	
12		Under the Securities Act, the definition of securities which may be traded on the SES should be broadened to include equity derivatives products.	
13		Multiple applications for IPO shares should be permitted. It is unnecessary to regulate the 'luck of the draw' provided these applications are supported by sufficient funds.	
14		Improve the Employee Stock Option Scheme (ESOP) to make it more attractive to employees to enable employers to attract and retain key personnel by implementing the following: i. Increase the maximum ESOP for companies listed on the Main Board to 10% of outstanding shares from 5% ii. Treat any gains arising out of the exercise of stock options issued under the ESOP as capital gains and therefore not subject to tax. iii. Amend the Companies Act to allow the life of the options to be extended to 10 years from 5 years. iv. Allow re-pricing of the exercise price of options, to adjust for market conditions.	
15		Rules on the 'window period" during which directors of the company as well as significant shareholders are permitted to trade in the company's shares are too restrictive. The Model Code should be removed from SES Listing Manual or amended.	
16		Amend the Companies Act to permit share buy-backs by listed companies.	

FIXED INCOME / DEBT MARKET			
1	Government bodies to issue more S$ debt instruments at market rates.	Encourage statutory boards and GLCs to borrow from the debt market to help its development.	IFER Develop a more liquid secondary bond market.
2	Expand range of debt securities and allow these to be widely held.	The Government to drive the yield curve through issuance of longer term Government bonds for benchmarking and to create depth in the market.	IFER Review the capital structure requirements for insurance and banks so that fixed income instruments such as bonds are not hoarded, but are reasonably and actively traded.
3	Amend laws governing financial sector to facilitate widespread issuance, trading and investment of debt securities.	Relax rules on the use of CPF savings for investment in approved debt instruments, including corporate bonds issued by Singapore companies.	IFER Provide more incentives to increase the number of primary and secondary dealer in the SGS market.
4	Abolish withholding tax on interest accruing from debt instruments to non-resident.	Extend tax incentives to companies to promote Singapore as the domicile for locating relevant specialists/experts, particularly in targeted growth areas like specialized project finance and debt distribution.	IFER Exempt all income earned by financial institutions derived from SGS trading in Singapore.
5	Release portion of CPF funds for management by fund managers.	Review tax laws and treaties and provide tax incentives to encourage cross border leasing activities.	IFER TO encourage individual investor participation, tax exemption should be extended to all interest income earned from investments in SGS and corporate bonds. Non residents without any Permanent Establishment in Singapore are enjoying tax exemptions on their SGS interest income.
6		A task force consisting of industry players and regulators should be set up to review ways to develop the targeted activities.	IFER Incentives should be introduced to increase non-resident investor participation in Singapore's fixed income market.

7		The Government should encourage Singapore professionals to develop research into legal, tax and accounting practices in emerging economies like Laos, Myanmar and Cambodia to enhance the information network and attract specialist finance teams to locate in Singapore.	Improve tax incentives by i. Tax exemptions be granted for domestic source investment income and foreign source income remitted to Singapore.
8		The SES should lead a consortium to establish a clearing house and regional custody facility for the trading of debt instruments issued by Asian entities and the Government should provide tax incentives.	
CORPORATE FINANCE / VENTURE CAPITAL			
1	Abolish tax on profits from third country trading transactions.	Aggressively promote Singapore as RHQ. Capital equity market professionals of investments banks are located where the regional HQs are established.	
2	Review all main costs affecting businesses.	The Government should delegate to the MAS, the authority to administer all tax incentives granted to the financial services sector.	
3	The Government should recognize concept of financial leasing and accept deferment of tax as industry norm.	Allow IPOs to be issued on a book building basis with 'green-shoe' option.	
4		The SES should allow some flexibility when determining the placement/public issue mix of IPOs. SES should give the issuer and the merchant bank the discretion and flexibility to decide on the approach for each tranche. The SES could still exercise control by prescribing a minimum size for the public tranche.	
5		Allow flexibility in share placements by allowing the company to borrow the shares from the promoters to facilitate the placement. The new shares, when	

		approved are returned to the promoters. This approach allows the issuer to take advantage of market conditions.	
6		The SES should abolish the minimum spread of investors for bond and debt issues. Since the SES has already been exercising flexibility by not insisting on the 100 holders, on a case-by-case basis, this should be reflected in the SES Listing Manual. The minimum should be flexible to be determined by negotiation between the SES and the investment bank.	
7		The SES should review the approval procedures for IPOs and rights with a view to streamlining and expediting the process.	
8		The SES should explore ways to attract an influx of foreign companies listed on established exchanges either to seek an introduction and quotation on CLOB international or listing on the SES by further simplifying procedures and documentation. Incentives should be given e.g. waiver of listing fee for the first two years.	
9		Tax relief should be considered for venture capital funds which are incorporated in Singapore but do not invest or provide seed money to Singapore companies, for example, allow gains on sale of venture capital investments carried in the company's books for, say more than 18 months, to be deemed as capital gains rather than as trading profit.	
INSURANCE / REINSURANCE			
1	Encourage local reinsurance companies to increase their capital to S$50 million or more.	To be competitive with other successful domiciles and increase the number of captive insurers, captive	

		insurer should be allowed to write second-party business.	
2	Encourage local insurance companies to merge and seek offshore reinsurance business.	Review the capitalization requirement for captive insurers and adopt a more flexible approach such as a sliding scale; perhaps lowering capital requirements to say $250k for pure captives and $500k for second-party captives.	
3	Woo new foreign or joint venture reinsurance companies to use Singapore as a base to seek international reinsurance business.	Review the current concessionary tax and adopt a flexible approach which will meet the needs of captive sponsors. Fix the corporate tax for captives at 26% but allow their sponsors to apply for a lower tax rate which could range from 0% to 25%.	
4	Set up reinsurance exchange in Singapore.	To establish reciprocal law for allowing captives to move their corporate seats and business from other domiciles to Singapore without the need to liquidate the existing captives and vice versa.	
5	To provide tax concession for income from capital investments.	Income derived from managing foreign owned captives should be taxed at the concessionary rate of 10% to encourage captive insurance managers to attract more clients to Singapore.	
6	Give tax incentives for hiring skilled expatriate staff.	Allow double tax relief on premiums paid for marine cargo and hull insured locally. A tax holiday could be considered to enable Singapore-registered insurers to build up sufficient reserve to face overseas competition.	
7	Extend SDF grants to on-the-job training overseas.	Provide tax incentives to encourage reinsurance companies to locate an enhanced level of underwriting and risk management expertise in Singapore, so as to increase the underwriting autonomy and territorial scope of their Singapore offices.	

8	Encourage small existing insurance companies to merge into larger units.	Professional reinsurers should be allowed to underwrite specialized pioneer products such as alternative risk-transfer products to promote further growth and enhance Singapore's competitiveness as a reinsurance centre.	
9	Insurance Commissioner to license brokers who are qualified.	Contingency Reserves should be totally tax-deductible as a further incentive for companies doing offshore business.	
10	CPF Board to drop proposed Dependent Protection Scheme and allow use of CPF funds for purchase of life assurance.	There is a need to review and liberalize the current investment limits for insurance funds as they are no longer appropriate in the prevailing investment environment. Investment limits as percentages of total insurance fund should be raised to 50% for equities, 50% for foreign assets and 30% for properties and property shares.	
11	Increase tax relief ceiling to encourage purchase of life assurance or exclude CPF contribution from the present limit.	Income derived from the placement of offshore risks in Singapore should be taxed at a concessionary rate of 10% as an incentive to develop reinsurance broking in Singapore and to encourage reinsurance brokers to generate business for the Singapore reinsurance market.	
12	Expand authorized assets schedule for insurance funds.	To encourage savings, premiums paid for deferred annuities should be tax-deductible up to an annual maximum limit, the annuity funds be allowed to accumulate tax free and the annuity proceeds taxed only on maturity.	
13	Give double tax deduction for marine cargo insurance purchased in Singapore.		

OTHER STRATEGIC THRUSTS AND INITIATIVES			
1	Tax The corporate and personal tax rates in the Republic should be reduced significantly to 20%-25%.	Cross Border Electronic Banking Expand NetTrust Initiative and align its development to ensure that Singapore-issued certificates are internationally accepted.	Universal Processing Centres (UPCs) Government to sponsor the establishment of UPCs
2	Tax Financial institutions should be encouraged to build up internal reserves. General provisions against doubtful debts should be allowed as a deduction against taxable income.	Cross Border Electronic Banking Continue with the deregulation of the industry and encourage innovation within the telecommunications industry to lead to more competitive pricing.	Universal Processing Centres (UPCs) UPCs to be eligible for tax incentives such as EDB's Pioneer Status etc. UPCs should also be eligible for grants on qualifying expenses under MAS's Innovation in Financial Technology & Infrastructure Grant Scheme
3	Tax A clear demarcation by the Inland Revenue Department (IRD) between 'capital gains' and 'trading profits' is urgently needed.		Financial Services Promotion Enhance Public-Private sector cooperation in promotion i. Establish the "Friends of Singapore" network ii. Establish regulatory forums and dialogue sessions iii. Use private sector endorsement
4	Tax The IRD should establish a procedure whereby tax rulings should be given in advance, given all relevant facts in writing.		Financial Services Promotion Increase the international profile of Singapore's financial sector i. Attract high profile conference to Singapore. ii. Improve Singapore's public relations and brand internationally.
5	Tax Abolish all stamp duties on securities.		Education and Training Sharpen focus and raise priority of education and training initiatives i. Establish clear national mandate and introduce accountability for progress.

			ii. Increase working-level resource. iii. Review minimum standards for financial sector professionals where appropriate. iv. Establish accreditation systems to ensure quality control amongst training providers and attract professionals to Singapore/ v. Strengthen financial services research. vi. Industry associations to play greater role in driving and supporting professional education of members and consumer education.
6	<u>Tax</u> Make capital raising expenses tax deductible.		<u>Education and Training</u> Raise international profile of Singapore's education and training environment i. Promote Singapore as a premier education hub.
7	<u>Tax</u> Remove possibility of double taxation from investment and unit trusts.		<u>Tax</u> Further enhance Singapore's tax environment i. Exempt domestic source investment income and foreign source income remitted to Singapore resident individual. ii. Enhance group relief provision for financial institutions with multiple entities. iii. Improve foreign tax credit mechanism. iv. Enhance not ordinarily resident taxpayer scheme. v. Clarify withholding tax treatment.
8	<u>Tax</u> Exempt from tax interest on deposits by individual with banks and finance companies.		<u>Business Infrastructure</u> Provide state-of-the-art building facilities for the financial sector
9	<u>Cost of Doing Business</u>		<u>IFER – Banking</u>

	Review use of profit levels as performance level as performance yardstick by Ministries and Statutory Boards.		Focus on financial activities that leverage on strengths i. Private banking where reputation and property rights protection top the list. ii. Processing, custodian and trustee centres iii. Non-geographical dependent activities such as fund management, foreign exchange, corporate finance and advisory and securitization iv. Encourage the creation of a global bank headquartered in Singapore by providing incentives for some local banks to merge and then acquire a foreign regional or global bank. v. Encourage at least one if not a few global banks to incorporate or to be headquartered globally in Singapore.
10	Regulatory Environment Further step up dialogue and teamwork between MAS and financial sector.		IFER – Regional/Global Financial Services Processing i. Study the potential and possible incentives for positioning Singapore as a Regional/Global Financial Services Processing Hub. ii. Review existing regulations to encourage outsourcing by financial institutions to locations other than Singapore. iii. Introduce incentives to entice establish foreign third party processors to bring their experience and expertise to Singapore. iv. Provide front-end incentives to alleviate the initial financial burden for companies interested in developing outsourcing businesses for back-end processing.
11	Regulatory Environment Government to consult and take into account views of		

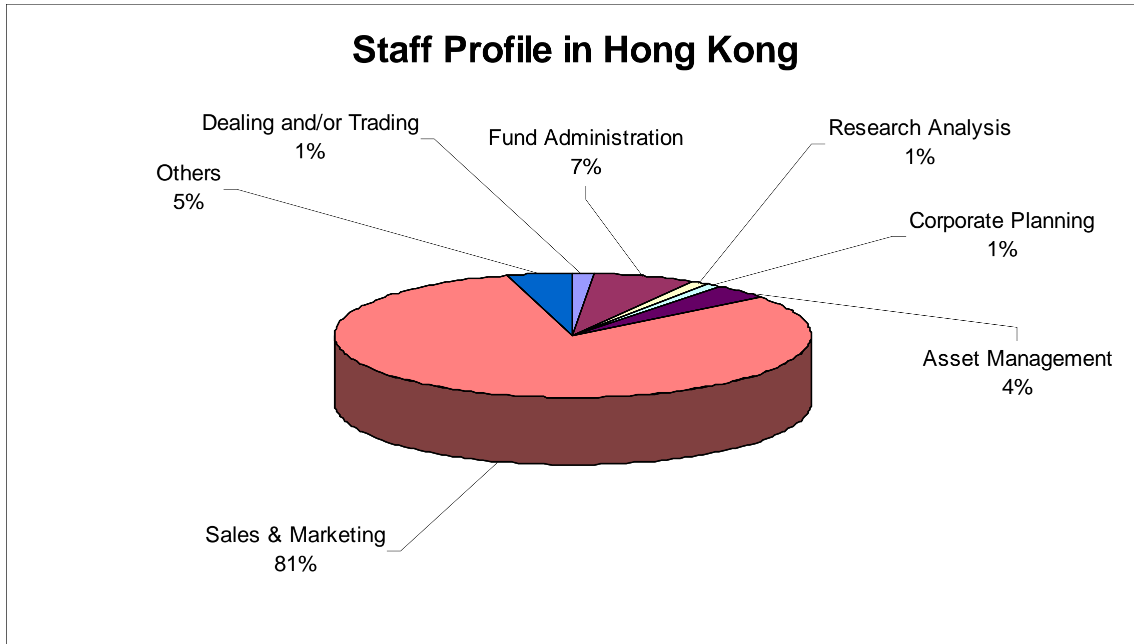
	financial sectors before introducing or amending legislation.		
12	<u>Regulatory Environment</u> Delegate to MAS the role of determining tax incentives to encourage new areas of growth.		
13	<u>Manpower</u> Liberalize SDF grants for overseas training.		
14	<u>Manpower</u> Give tax concessions to attract key expatriates to work here.		
15	<u>Manpower</u> A top flight banking school should be set up to enhance banking expertise.		
16	<u>Manpower</u> Allow double tax deduction for training and development expenses.		
17	<u>Banking</u> Government to continue to nurture local banks to enhance their competitiveness.		
18	<u>Banking</u> Given the small domestic market, encourage offshore banks to expand their offshore activities, but MAS to give incentives selectively to offshore banks which have been innovative and with proven contribution to enhancement of Singapore's financial centre status.		
19	<u>International Money Broking</u> Give substantial reduction in telecommunication rates to high volume users.		

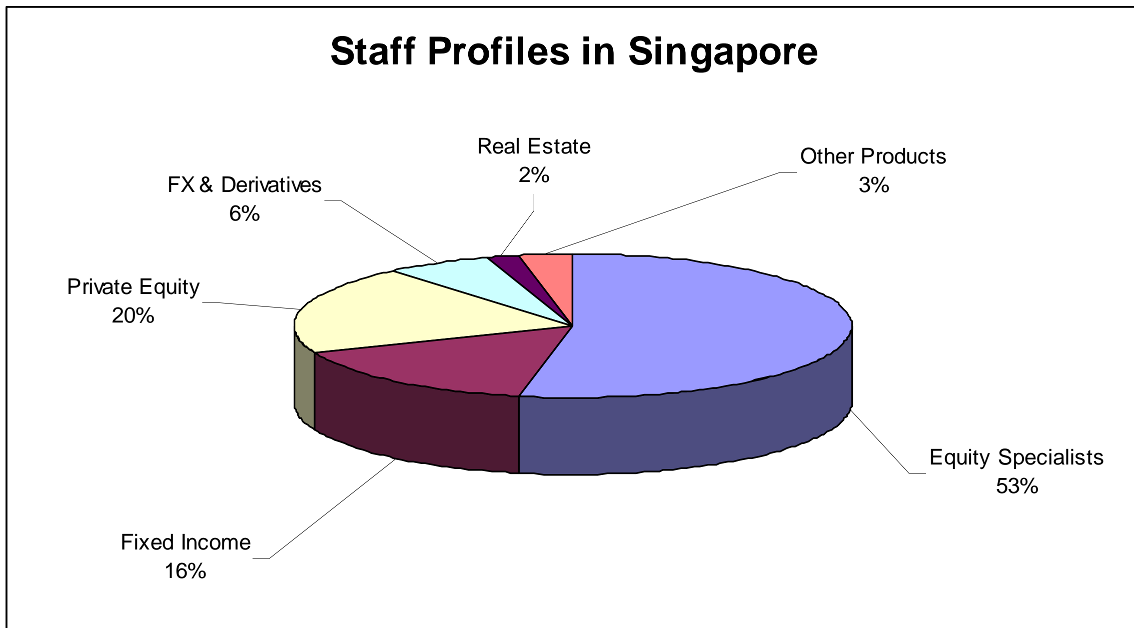
20	International Money Broking MAS to deal actively in local market whenever possible.		
21	Commercial and Merchant Banks Review the 26% reserve and liquidity requirements, in view of the deflationary state of the economy.		
22	Commercial and Merchant Banks Expedite court proceedings to enable lenders to obtain timely legal remedies.		

Appendix 2: Summary of the Hong Kong Banking Sector Reforms

Hong Kong Banking Sector Reform Program
Market reform and liberalization measure:
• Deregulate the remaining Interest Rates Rules (IRRs) in two phases, subject to the prevailing financial and economic conditions
• Relax the one branch policy to allow foreign banks to establish up to a maximum of three branches
• Allow access to Real Time Gross Settlement by restricted license banks
• Simplify the three-tier licensing system into a two-tier system
• Relax the market entry criteria for obtaining a local banking license
Safety and soundness enhancement measures:
• Conduct a detailed study to enhance deposit protection
• Clarify the HKMA's role as lender of last resort
• Improve the financial disclosure framework
• Develop a more formal risk-based supervisory regime
• Conduct a feasibility study on establishing a credit register for commercial enterprises in Hong Kong
• Promote high standards of corporate governance within the banking sector.

Appendix 3: Staff Profile of Hong Kong and Singapore Financial Professionals (2003)





Appendix 4: The World's Leading Insurance Countries, 2003
(Direct premiums written, U.S. $ billions)

				Total premiums		
Rank	Country	Nonlife Premiums (1)	Life premiums	Amount	Percent change from prior year	Percent of total world premiums
1	United States (2)	$574.6	$480.9	$1,055.5	4.9%	35.89%
2	Japan (3)	97.5	381.3	478.9	7.4	16.28
3	United Kingdom	91.9	154.8	246.7	4.2	8.39
4	Germany	94.1	76.7	170.8	25.8	5.81
5	France	58.2	105.4	163.7	30.8	5.57
6	Italy	40.1	71.7	111.8	33.0	3.80
7	South Korea	17.8	42.0	59.8	5.4	2.03
8	Canada (4)	36.3	22.8	59.1	22.1	2.01
9	Netherlands (5)	24.9	25.4	50.3	26.4	1.71
10	Spain	27.0	20.0	47.0	3.5	1.60

(1) Includes accident and health insurance.
(2) Nonlife premiums include state funds; life premiums include an estimate of group pension business.
(3) April 1, 2003 - March 31, 2004.
(4) Life business expressed in net premiums.
(5) Nonlife premiums are gross premiums including a small amount of reinsurance premiums.

Source: Swiss Re, *sigma*, No. 3/2004.