Heng Swee Keat: Financial developments in Singapore

Opening remarks by Mr Heng Swee Keat, Managing Director of the Monetary Authority of Singapore, at the press conference on the Monetary Authority of Singapore's Annual Report 2009/10, Singapore, 29 July 2010.

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Strong recovery from the recession

1. The Singapore economy has recovered strongly from the recession. Five quarters since GDP reached a trough, Singapore's output has exceeded its pre-crisis peak by 13.3%. The rapid climb from the trough can be traced to several inter-related factors. In particular, the domestic economy had been lifted by the cyclical upturn in global trade and financial market conditions since early 2009, supported by inventory restocking and unprecedented policy stimuli in the major economies. Given its openness and competitiveness, Singapore was in an especially strong position to benefit from these global forces through our externally-oriented sectors. In addition, investments made in the earlier years were completed in time to tap onto the global upturn. These investments introduced new activities in Singapore's economic landscape, including high-end manufacturing and tourism services, and strengthened the competitiveness of our existing industries.

2. Global markets also recovered strongly after March as the financial system stabilised and investor confidence recovered. Taking into account translation effects stemming from the stronger Singapore dollar, interest and dividend income, as well as gains in the valuation of assets, MAS recorded a net profit of $10.12 billion during the financial year.

3. Looking forward, considerable risks remain in the global economy and the global financial system. Singapore's financial system has, by and large, weathered the crisis well. However, we must not be complacent and we need to prepare ourselves to respond to any future challenges. There are three areas which MAS has been working on and which we will continue to focus on in the coming year: first, sustaining macroeconomic stability in the post-crisis period; second, strengthening the financial system; and third, maintaining the growth of Singapore's financial services sector.

Sustaining macroeconomic stability in the post-crisis period

4. The strong pace of growth seen in the first half of this year is not expected to be sustained. Growth is likely to have peaked at the middle of this year, and will moderate to a more sustainable rate, as external demand slows after the post-crisis bounce from stimulus measures and inventory effects wane worldwide. For 2010 as a whole, the Singapore economy is expected to expand by 13 to 15%.

5. After two quarters in negative territory, headline inflation turned positive in Q1 this year and reached 3.1% in Q2. For the rest of the year, headline CPI inflation is expected to rise, reflecting higher car and commodity prices on a year-ago basis. However, the outlook for underlying price pressures remains largely unchanged from MAS' monetary policy review in April. Despite stronger-than-expected GDP growth, the pass-through of domestic business costs to retail prices due to tightening factor markets is expected to be moderate, alongside the slowing in the economy. In part, domestic wage growth and other business costs could be temporarily tempered by the initial cyclical productivity uptick in some capital intensive sectors of the economy. For the year as a whole, headline CPI inflation is projected to average between 2.5% and 3.5%. MAS underlying inflation, which excludes the cost of accommodation and private road transport, will come in at around 2%.

6. When Singapore entered the recession in 2008, monetary policy, followed by fiscal policy, was eased to provide support to the domestic economy. As economic activity recovered swiftly in 2009, macroeconomic policy settings were recalibrated to levels which were conducive to sustainable growth and medium-term price stability. In a pre-emptive move, MAS tightened monetary policy in April 2010 by re-centring the S$NEER policy band upwards and restoring its modest and gradual appreciation path.

7. Looking ahead, the outlook of the industrialised economies remains uncertain. However, there is sufficient momentum from the Asian economies and domestic industries that will continue to support Singapore's economic activity at a high level for the rest of the year. While CPI inflation is expected to pick up towards the latter part of the year, it has evolved broadly as anticipated during the April review. At this stage, we assess that the current monetary policy stance of a modest and gradual appreciation of the S$NEER policy band remains appropriate.

Strengthening the financial system

8. Singapore's financial system remained resilient during the global crisis. In maintaining the soundness of the financial system in Singapore, MAS' approach is centred on establishing sensible rules appropriate to our circumstances, strengthening prudential and market conduct supervision, and working in partnership with the industry to develop a shared ownership of supervisory outcomes.

9. This approach has served us well. As global reforms reshape the financial landscape, we will continue to strengthen our supervisory and regulatory regimes and market infrastructure, consistent with new international standards and best practices. As we have done in the past, we will calibrate these changes to take into account our environment and regulatory objectives.

10. MAS is supportive of global reform efforts to strengthen capital and liquidity frameworks. We have always considered capital adequacy and effectiveness of a bank's risk management and capital planning processes as important parts of overall prudential management of banks. As a member of the Basel Committee on Banking Supervision, we participated actively in international discussions that helped shape the broad agreement reached earlier this week on the main design elements of the new capital and liquidity reform package. Other design details such as calibration, and phase-in arrangements as well as the framework for regulatory buffers will be determined later in the year. We would like to see a set of final proposals that can be implemented globally in a meaningful manner to promote the long term stability of the banking system. There should be a judicious balance between limiting banks' activities that are incongruent to their role as an intermediary of financial flows, and allowing them to perform their role in facilitating economic activity and sustaining the recovery. MAS will continue to be actively involved at these discussions to shape the proposals.

11. Our Singapore banks start from relatively strong capital and liquidity positions. They are generally well-capitalised and have in practice maintained capital ratios much higher than our minimum requirements. As such, on a relative basis, we do not expect the proposals to affect them in a significant manner. Nevertheless, the global reforms will set new norms for the banking sector and the Singapore banks would have to take these into consideration in their capital and liquidity plans moving forward.

12. I mentioned last year that MAS will be reviewing the Corporate Governance Regulations and Guidelines for locally-incorporated banks and significant life insurers. We have since issued a public consultation paper setting out proposed enhancements to the Corporate Governance Framework for these financial institutions. The main thrusts of the proposals emphasise the need for directors to have the relevant skills and commitment to

oversee the operations of the financial institutions, and the important role of independent directors on the Board. MAS will issue our response to the public consultation shortly.

13. On market conduct, MAS has issued two consultation papers on the sale of listed and unlisted investment products, to strengthen safeguards for retail customers and enhance MAS' regulatory powers. We will be issuing our response to the feedback received in 2H2010. Proposals which do not require legislative amendments will be implemented first. Financial institutions will be expected to adopt the remaining proposals even before legislative implementation as good practice in conducting business with their customers.

14. MAS also issued the Guidelines on Fair Dealing last year. The Guidelines stress the responsibilities of the Board and Senior Management of financial institutions to set the corporate culture and direction to deliver fair dealing outcomes to customers. Over the last year, MAS has written to CEOs and Boards of major financial institutions to emphasise our expectations. We have noted increasing awareness among financial institutions of the importance of dealing fairly with customers. Going forward, MAS will continue to engage the Board and Senior Management of financial institutions, and assess their implementation of the Guidelines through off-site and on-site supervision. Financial institutions are also expected to conduct their own mystery shopping, while MAS' mystery shopping exercise will serve as an independent check and benchmark practices across financial institutions.

15. In strengthening our regulatory and supervisory regimes, MAS will continue to maintain our balanced and consultative approach. We remain focused on achieving good regulatory outcomes that are appropriate to Singapore and seek to promote sustainable development of the financial sector.

16. Besides financial regulations, MAS is taking steps to strengthen the robustness of interbank funding markets. The financial crisis revealed the need to enhance banks' management of liquidity. As the banking system grows, demand for high quality, liquid assets will grow. To address this, MAS will do two things.

17. First, we will increase the availability of liquid securities to banks by issuing short-term MAS bills as part of money market operations. Currently, we use three instruments in our money market operations – foreign exchange swaps, borrowings and repos. MAS Bills will be our fourth instrument. These bills are negotiable, so banks needing liquidity can sell them or pledge them as collateral in interbank repo markets as well as the MAS Standing Facility. This will facilitate banks in managing their liquidity.

18. We expect to commence issuing MAS Bills in 2Q 2011. To prevent overlapping with SGS T-bills, MAS bills will have tenors of up to 3 months. We will phase MAS Bills in gradually, with up to S$20 billion initially, and then build up from there.

19. Second, we will continue to enhance the Standing Facility, which is the key liquidity facility for banks.

20. Last year, I announced that we would accept AAA-rated Singapore dollar debt securities issued by supranationals, sovereigns and sovereign-guaranteed companies. We also admitted these securities as Tier 2 liquid assets under Notice 613 with the same haircut as Singapore Government Securities. With immediate effect, we will extend the list of issuers to AAA-rated and zero risk-weighted public sector entities.

21. I also announced last year that we have established a cross-border collateral arrangement with De Nederlandsche Bank. This year, we have established such arrangements with the Banque de France, Bundesbank and Bank of England. These arrangements will allow banks in Singapore to pledge Euro and Sterling cash and eligible government securities, custodised with these central banks, as collateral when they access the MAS Standing Facility.

22. These measures will help to broaden the availability and diversity of regulatory and liquid assets for banks and allow international banks greater flexibility to tap on their global

sources of liquidity, while maintaining the high quality of eligible collateral of the Standing Facility.

Maintaining the growth of Singapore's financial services sector

23. Let me now turn to the performance of our financial sector. The sector has staged a strong rebound as global financial conditions improved. In the first quarter of this year, the financial sector grew by 3.5%, its fourth straight quarter of expansion. More recent data such as bank lending suggests that the financial sector continued to expand in Q2. Meanwhile, hiring in the financial sector has picked up from 4,000 in Q4 2009 to 5,500 in Q1 this year. The 5,500 financial sector jobs created accounted for 15% of total job creation in Q1 2010.

24. The recovery in the financial sector is broad based – banking intermediation, trading and asset management activities have all rebounded. In particular, financial assets managed by the Singapore asset management industry reached a new high in 2009. Total assets managed grew by 40% to reach S$1.2 trillion (US$861 billion), exceeding the pre-crisis peak in 2007. Average daily trading volume of foreign exchange (FX) and FX derivatives have recovered to US$290 billion in April 2010, an increase of 11% from six months ago in October 2009 and near pre-crisis levels. We are also today one of Asia's leading commodity derivatives trading centres.

25. The financial sector's strong recovery is, in part, due to our strong fundamentals, as well as action taken by the industry. We will continue to take steps to ensure that the financial industry remains vibrant. One key lesson from this financial crisis is that we need to strengthen the nexus between the financial system and the real economy, to ensure efficient intermediation of capital to support growth and development.

26. The Singapore Exchange (SGX) implemented a series of measures to facilitate fund raising by listed companies in the midst of difficult external market conditions. Earlier this year, MAS and SGX introduced a concurrent review process for initial public offerings (IPOs) and a reduction in public exposure period for prospectus review from 14 days to 7 days. These steps to shorten the time-to-market would make Singapore a more attractive listing destination.

27. To give investors a broader range of investment products, MAS will continue to enhance individual investors' access to debt capital markets, building on initiatives undertaken earlier for Singapore Government Securities. We worked with the industry to develop infrastructure for individual investors to participate in auctions of Singapore Government Securities and Treasury Bills via the ATMs of local banks, and to custodise these investments together with their equity investments in the Central Depository. To promote secondary market trading for individual investors, MAS and SGX will work towards having an SGS trading platform by the first quarter of next year.

28. To promote bilateral trade and investment between Singapore and China, MAS and the People's Bank of China announced the establishment of a S$30 billion currency swap arrangement last week. We are working with our Chinese counterparts and banks to operationalise the swap line, and will announce details in due course.

29. The completion of the Marina Bay Financial Centre is timely as it provides the physical infrastructure for financial institutions as they gear up to take part in the next phase of Asia's economic development. The industry has also continued to invest in talent even during the crisis, hiring over 800 graduates under the Finance Graduate Immersion Programme (FGIP) and the Finance Graduate Leadership Programme (FGLP). We will continue to work with the industry to invest in the development of talent and in deepening research.

Conclusion

30. Let me now conclude. While Singapore has made a strong recovery from the recession, considerable risks and policy challenges remain in the global economy and financial markets. MAS will continue to be vigilant and take appropriate steps to maintain medium-term price stability and enhance the resilience of our financial system. In strengthening our regulatory and supervisory regimes, we will do this in a manner which is consistent with international standards and best practices, but at the same time, sensitive to our environment and needs. Riding on Asia's growth, we will also continue to build on our strong fundamentals to provide for sustainable growth in the financial sector.

31. Thank you.