Ravi Menon: Myanmar must open up at a measured pace

Keynote address by Mr Ravi Menon, Managing Director of the Monetary Authority of Singapore, at High-Level Seminar on Financial Sector Liberalisation, Nay Pyi Taw, Myanmar, 10 January 2014.

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His Excellency U Win Shein, Union Minister, Ministry for Finance and Revenue,

His Excellency U Kyaw Kyaw Maung, Governor, Central Bank of Myanmar,

distinguished guests, ladies and gentlemen, good morning.

A defining moment

I am pleased to be here for this high-level seminar on financial liberalisation. This collaborative event is a clear testimony to two things:

- first, the commitment and resolve of the Myanmar government and central bank to modernise and develop the financial sector; and
- second, the warm relationship and close co-operation between the central banks of Myanmar and Singapore.

Myanmar is at a defining moment. There is a distinct sense of optimism, as the country rejoins the global economy. A strategic location at the intersection of China and India, a generous endowment of natural resources, and a large, youthful and literate population – Myanmar is poised to be the next economic frontier in Asia.

Finance is a handmaiden to the economy. As Myanmar opens up its economy and seeks to achieve sustained growth, it is important to liberalise and develop its financial sector in concert. But it must do this in a progressive and calibrated manner, step-by-step, making sure the fundamentals and preconditions are in place.

Let me elaborate on these two themes: why liberalise the financial sector, and why liberalise at a measured pace. In doing so, I will draw partly from Singapore's experience. Singapore and Myanmar are two very different economies and it would be unwise to apply Singapore's experience directly to Myanmar.

But I think the overall lesson is relevant: *It is critical to open up, but open up at a measured pace.*

Why financial liberalisation is important

A well-developed financial sector can be a catalyst to spur and sustain economic growth. It will lead to more effective mobilisation of domestic savings, help to harness foreign savings, and improve the efficiency of investment allocation. And opening up the financial sector to foreign participation can play a critical role in catalysing the sector's growth and development.

A basic purpose of banking is the provision of credit for economic and social development. Large segments of the Myanmese economy and population do not have access to affordable funding. Foreign financial institutions can complement the local banks in effective credit intermediation. It will deepen the financial sector, thereby helping to raise household savings and divert funds away from the shadow financial system.

Foreign financial institutions can provide a channel for Myanmar to tap into foreign savings to drive its growth, even as the country ramps up the mobilisation of domestic savings. This is particularly relevant for financing infrastructure development, which is critical to drive Myanmar's economic growth.

- A McKinsey study estimates that Myanmar will need to invest US$320 billion in infrastructure up to 2030 to achieve an annual growth of 8%.
- Foreign capital, intermediated through a well-developed banking industry and well-functioning capital markets, is a necessary complement to meeting this infrastructure need.

And it is not only financing that foreign participation brings, but critical expertise in structuring projects and managing risks.

Most important, foreign financial institutions promote competition and innovation, providing the impetus for local institutions to upgrade their capabilities. This has been Singapore's experience.

- We had protected our local banks from foreign competition in retail banking for many years.
- In 1999, MAS embarked on a programme to liberalise access to Singapore's domestic banking market.
- The aim was to strengthen our local banks through competition and provide Singaporeans with quality banking services.

The strategy worked.

- The local banks built up strong management teams and made significant infrastructural investments to expand their range of business activities and enhance operational effectiveness.
- They are now stronger and more dynamic, with much improved systems of management, risk controls, technology, and expertise.
- Liberalisation provided the spur for our local banks to raise their game and compete with some of the world's largest banks while maintaining high prudential standards.

Why liberalise at a measured pace

This leads me to my second point. The pace and sequencing of financial liberalisation are critical:

- The pace of liberalisation should proceed in accordance to the country's stage of development. Progressive liberalisation at a steady pace is better than a 'big bang' approach.
- And financial reforms must be sequenced appropriately in order to ensure the stability of the financial system.

Let me highlight three factors that must be in place for successful financial liberalisation:

- sound regulation and supervision;
- a strong core of local banks; and
- a selective admission policy.

First, regulation and supervision. Financial crises following rapid liberalisation are often caused by excessive risk-taking by financial institutions against a backdrop of weak prudential regulation and supervision. The quality of prudential oversight, risk management, and corporate governance must keep pace as the financial sector grows.

Second, a core of strong local banks. Sound banking systems need strong anchor players who are well-regulated, rigorously supervised, and able to take the long-term view, so that their interests are closely aligned with that of the domestic economy.

- This is why Singapore phased its liberalisation measures progressively, to give the local banks time to adjust so that they can compete effectively, while maintaining the stability of the financial system.
- It may be necessary to facilitate the consolidation of a fragmented local banking system to form a core group of strong local banks that are able to compete.
- In Singapore, liberalisation spurred the consolidation of Singapore banks from seven banking groups to three, a process which may otherwise have taken much longer.
- Foreign bank participation in the domestic banking system must therefore be strong enough to encourage the strengthening of the local banks but not so strong as to overwhelm them.
- It is a judicious balance that each country must find for itself.

Third, selective and stringent admission. Singapore has always had a very open policy towards foreign banks in wholesale and offshore banking activities. But when we selectively liberalised foreign bank access to retail banking, MAS considered three sets of factors:

- First, the banks' prudential strength, credit ratings, and quality of risk management. We only admitted strong, well-run banks.
- Second, we took into account the relationship we had with the home regulator, as we needed to be able to work with them on consolidated supervision of these banks and trust them to regulate the head office in a sound manner.
- Third, we evaluated the banks' long-term business plans and how they could contribute to the Singapore economy.

Liberalisation is not an end in and of itself. It must ultimately lead to a stronger, safer, and more competitive financial system that serves the needs of the economy and country.

The lessons from the development history of many economies are compelling: financial liberalisation is integral to the development process but this liberalisation must be carefully sequenced if crises are to be avoided and the benefits of liberalisation maximised. In general, domestic financial reform should precede full capital account liberalisation.

Let me conclude. Myanmar has embarked on a momentous journey to strengthen and develop its financial sector. Liberalising the financial sector is not a question of *whether* but *how*. MAS, through its growing partnership with the Central Bank of Myanmar, is happy to contribute to this effort where it can. We have been deeply engaged in many training programmes and stand ready to share our experiences where relevant. Singapore wants Myanmar to succeed and prosper, and realise its huge potential.

I wish you fruitful discussions.