Speech by Senior Minister Goh Chok Tong at 36th Association of Banks of Singapore Annual Dinner at Mandarin Ballroom, Level 6, Meritus Mandarin on 26 June 2009, Friday, AT 8.00 pm

"The Future of the Financial Sector in Singapore - Riding the Challenges, Emerging Stronger"

1. A very good evening to all of you. The Annual Dinner of the Association of Banks (ABS) has always been an excellent opportunity for the financial community to catch up, discuss issues impacting the financial industry and look ahead at how the Singapore financial sector will develop.

2. As we look forward tonight, we do so with a measure of optimism, as economic and financial indicators have stabilised in recent months. For example, manufacturers' Purchasing Managers' Indices (PMIs) have rebounded globally. The Chinese PMI has remained above the 50-point mark for three months in a row, and Singapore's PMI rose above 50 in May. In financial markets, interbank borrowing rates have fallen, as have interest rates on corporate debt. Markets have thus shown signs of thawing.

3. However, optimism about a recovery must be tempered with an appreciation of the risks that remain. I will just mention two briefly.

4. First, while the global financial system has stabilised relative to the dramatic events of last year, the broad-based downturn in economic activity continues to pose challenges for financial sector earnings. Losses may even be higher than expected if defaults on consumer and corporate loans mount. If banking systems in the major economies are not fully restored to health, it would reinforce the downturn as companies and consumers who are unable to access adequate credit will further weaken economic activity. The prospect of further losses cannot be ruled out. We should stay vigilant to deal with negative surprises, should they arise.

5. Second, there are incipient signs of protectionism. Following the inclusion of "Buy American" clauses in the US stimulus plan in February, we have heard in recent weeks of similar "Buy local" initiatives by economies such as China

and the Australian State of New South Wales. The commitment of governments and international bodies to combat protectionism looks set to be sorely tested. But it is important for governments everywhere to maintain their resolve, because global growth cannot return without the growth of trade and capital flows. Protectionist measures that reverse these flows will ultimately result in a lose-lose situation for all countries.

6. The present circumstances mean that we have to be on our guard as we move ahead to build a foundation for long term growth. Charting our future course involves asking two questions. First, what are the trends that shape and drive the new landscape? Second, how can we position ourselves to capitalise on these trends? Let me address these questions in turn.

Trends shaping the new landscape

7. There is growing acknowledgement that the shape of the global economy will be permanently altered. Developed economies, which have been the drivers of global demand, will experience a period of balance sheet repair and de-leveraging. After years of living on easy credit and now facing the prospect of having to rebuild their eroded retirement nest eggs, consumption in developed economies will remain depressed for a prolonged period.

8. In the global financial industry, we are witnessing a 'back to basics' movement, while regulation shifts towards stringency. In banking, risk-taking and proprietary trading will be reduced, while core activities anchored on providing services to consumers and the economy will regain its former importance. In capital markets, investors will demand less complex products and more standardisation, with trading and settlement conducted on central clearing platforms to mitigate counter-party risks.

9. Internationally, regulators are considering tighter regulation, after several decades of liberalisation. Proposals such as those laid out in the de Larosière report in Europe, the Turner review in the UK and most recently in the US Treasury's Financial Regulatory Reform document, are speeding the reform debate. The changes being discussed go beyond more capital for banks and more stringent liquidity management. It includes bringing more entities, such as near banks, under the regulatory umbrella, as well as enhancing consumer protection frameworks. Better identification and monitoring of systemic risk are also high on the agenda.

Prospects for Singapore are good

10. Although the tone of discussions about the global financial industry has been rather subdued and introspective, the outlook for Singapore's financial sector remains bright. For a start, Singapore is situated in the heart of a

growing Asia. Rapid urbanisation will bring about more infrastructure projects, which can spur the growth of project financing in Asia. Demographic trends in Asia are expected to drive the demand for greater wealth planning, including asset management, as well as life and healthcare insurance products. Also, growing trade within Asia and with the rest of the world will drive financing opportunities.

11. Moreover, the ever greater emphasis on building trust, good governance and competence plays to Singapore's advantage. We are ranked first in corporate governance standards in Asia by the World Economic Forum, and we have maintained a stable 'AAA' sovereign rating from Fitch. The City of London's Global Financial Centres Index ranked Singapore the most competitive financial centre in Asia, and third globally, after London and New York. However, it is important not to be complacent as trust, good governance and our reputation for competence require continuous reinforcement as standards change and new demands arise.

12. Nevertheless, our strong fundamentals will give us a firm footing to tap the region's growth opportunities when they come. And to better position ourselves, we need to adapt to the realities of the post-crisis landscape. In particular, I would like to highlight five strategies going forward.

<u>Sound and progressive regulatory framework</u>

13. **First, we must continue to maintain a sound and progressive regulatory regime** to provide an overarching framework for Singapore's growth as a financial centre.

14. MAS' regulatory framework has generally been regarded as stringent, and in some aspects it exceeds international standards. For example, Singapore's capital requirements were high relative to international standards, and our local banks maintained buffers in excess of the minimum. This approach of emphasising robust regulation and supervision has proven to be a prudent 'through-the-cycle' policy. It has helped our financial system remain resilient through this crisis.

15. Should the current round of discussions on regulatory reforms result in a movement towards more stringent international standards, we should be in a good position to align ourselves with these standards. But we will also be mindful of maintaining a balanced approach and not to 'over-swing' the regulatory pendulum.

16. While our financial institutions weathered the crisis well, a significant number of Singaporeans were adversely affected by losses suffered on structured products sold to them by banks and other financial institutions. Some have alleged mis-selling and misrepresentation by the financial

institutions. Others have questioned if the products were suitable for retail investors.

17. Although emotions ran high, MAS addressed investor concerns in a calm, methodical and objective manner. This is as it should be for a regulator. Apart from setting out the 3-step process for affected investors, MAS has required the relevant financial institutions to review each complaint in a serious and impartial manner.

18. Financial institutions that distributed the failed structured products have generally reviewed investors' complaints in line with MAS' recommendations not to take an overly legalistic approach, even though they are of the view that the documents signed by the customers afford them a legal basis not to offer redress in many cases. The three banks and one finance company concerned have informed MAS that as at end May, they have offered settlements on a no-admission-of-liability basis to over 3,600 investors for about $105 million. This means that of the 5,350 cases decided by these financial institutions, 67% have been offered a settlement. 25% of the cases decided received full compensation.

19. MAS has now completed its investigations into the sale of the structured notes. It will release its findings shortly. MAS has also recently consulted on proposed enhancements to the regulatory framework for the sales and marketing of structured products to retail investors. Broadly, the findings from MAS' policy review and investigations show that financial institutions will need fundamental changes in both business models and mindsets to win back the trust and confidence of consumers. This is true not only in Singapore, but across the globe.

20. This is where progress on the regulatory front can underpin the efforts by financial institutions to build strong relationships by adding real long term value to their customers. MAS has recently set out in its Fair Dealing Guidelines the roles and responsibilities of Boards and Senior Management in driving some of the fundamental changes required to deliver good customer outcomes. MAS will also fine-tune its approach to supervision of market conduct of financial institutions, including greater probing of the Boards and senior management of the steps they are taking to embed fair dealing outcomes in all their processes, from product approval to staff incentive structures.

21. I am pleased to read in recent weeks that some banks have proactively been taking steps to revamp some aspects of their sales process, such as remuneration structures for front line staff. I encourage all of you to step up these efforts in the interest of building the trust and confidence of your customers.

22. Consumers of investment products also have an important part to play as our system will remain one based fundamentally on personal responsibility for financial and investment decisions. Through the MoneySENSE programme, MAS will target consumers from all walks of life to assist them in becoming better equipped to make investment and financial planning decisions confidently.

<u>Tap growing wealth in Asia</u>

23. **Our second strategy is to tap the growing wealth in Asia.** Prior to the crisis, the asset management industry in Singapore had flourished, with growth averaging 20% per annum over the past 7 years. It has grown in diversity to include not just global traditional fund managers but also alternative investment managers. Most of the fund management firms here are from Japan, Europe and the US, reflecting the international character of our asset management industry. With the crisis and fall in global assets under management (AUM), Singapore's AUM for 2008 has fallen too. Nevertheless, the continued accumulation of Asian wealth will remain a key driver for longer-term growth.

24. What is more important is to recognise that falling asset values and wealth destruction during this crisis has created a shift in investor mindset. Investors are now also paying more attention to protecting their wealth, in addition to growing wealth. Investors are also asking for better transparency and risk management of their portfolios. The building of trust has now become a key component of the asset management industry, leading banks and wealth managers "back to basics" to restore client relationships.

25. This mindset shift plays to Singapore's advantage, as we have a reputation for a sound regulatory regime and a trusted legal and governance framework. We should build on this foundation to facilitate the growth of a trusted ecosystem for the asset management industry, encompassing high standards of risk management, transparency and industry competencies.

26. As investors shift towards demanding less complex and more transparent investment instruments, the industry should position itself to ride this shift. To this end, we are currently working to improve individual investors' access to one such investment instrument – Singapore Government Securities, or SGS. Unlike in other jurisdictions, SGS are not issued to fund government expenditures, which the Government Securities Act explicitly prohibits. Instead, SGS functions as a useful pricing benchmark for local corporations issuing bonds, and many institutional investors favour SGS as a liquid and safe investment alternative.

27. Because of rising interest among individual investors to purchase SGS, from 1st July, individuals will be able to participate in SGS auctions by submitting bids through the ATMs, similar to bidding for an equity IPO. Similar to equities, we have also moved the custody of SGS from individual banks to the Central Depository (CDP). Eventually, we hope to work with SGX to list the SGS on the exchange so that it can be traded just like other stocks. By making SGS more accessible and more liquid, we hope to enhance the array of financial instruments that financial advisors can use to match their clients' needs.

Leverage on infrastructure needs in Asia

28. **Our third strategy is to leverage on the massive infrastructure needs in Asia**. A recent ADB study showed that Asia needs to spend about US$8 trillion on transport, power and communications infrastructure over the next ten years for Asia to emerge as a viably connected, integrated and competitive region. Such infrastructure investment will spur the region's growth, and will potentially add US$1.6 trillion or 10% to developing Asia's GDP by 2020.

29. Singapore can play a significant role in regional infrastructure financing due to our developed financial markets, urban infrastructure management expertise and strong legal and regulatory framework. I know that many banks already have established project finance teams based in Singapore, and are poised to expand in this area. So I encourage ABS member banks to do more Asian infrastructure financing out of Singapore.

30. On the government's part, we are actively working with multilateral agencies to attract more private sector investments into viable infrastructure projects. The launch of the Asia Infrastructure Project Development (AIPD) last year is one positive outcome. A joint venture by the ADB, Singapore Cooperation Enterprise and three private sector participants – AIPD will assist municipal governments in sourcing for funds, from commercial banks and private investors, for commercially viable Public Private Partnership (PPP) infrastructure projects. Singapore also entered into a Memorandum of Understanding (MOU) with the World Bank last year, which would leverage on Singapore's developmental expertise to provide urban solutions for developing countries which will also have spill-over benefits to our financial sector.

Strengthen risk management capabilities and market infrastructure

31. **Our fourth strategy is to enhance our risk management capabilities and market infrastructure.** Emerging from the crisis, industry players and governments are keen to see the introduction of enhanced risk mitigation platforms for derivative products. By working on initiatives to mitigate

counter-party risks, we can enhance our lead position as a risk management hub for the region. One example is SGX's AsiaClear which will extend its current central clearing facility for OTC trades in energy derivatives and forward freight agreements to the clearing of OTC financial derivatives. This will no doubt enhance the market infrastructure for OTC clearing in Singapore.

32. Another initiative which will strengthen Singapore's market infrastructure is the ongoing industry effort to enhance the framework for the fixing of the Singapore Inter-Bank Offer Rate (SIBOR) and the Swap Offer Rate (SOR). The turmoil in the global interbank markets during the current crisis has raised questions about the robustness of the interbank rate fixing system and its reliability in representing market conditions. Banks were accused of underestimating the cost of borrowings to downplay their financial difficulties, prompting widespread calls for reviews of interbank rate fixings globally. In Singapore, the ABS has conducted a review of SIBOR and SOR fixings and found the methodologies and processes to be sound. Nevertheless, governance of the fixings can be strengthened by expanding the resources and scope of the oversight committee. These proposals will be circulated to members for comments shortly.

Build talent pool and intellectual capacity

33. **Fifth, we should take advantage of the current environment to further build our talent pool and intellectual capacity.** The economic downturn should not disrupt our efforts to look long term and strategically invest in manpower development. Doing so will prepare us for the upturn. As the global economy slows, we appreciate that managing costs has to be a priority for our financial institutions. So to ensure that our financial institutions do not lose sight of the critical need to continue to invest in developing a pool of skilled manpower, MAS announced up to 90% co-funding for training schemes supported under the Financial Sector Development Fund. MAS has also launched new schemes to spur the creation of job and industry internship opportunities for fresh graduates. This will ensure a ready pool of young talents, well-trained and ready to contribute to the growth of the financial sector when the economy recovers.

34. To contribute to enhancing Singapore's intellectual capacity in the financial sector, the AXA University Asia Pacific Campus and the SMU-Sim Kee Boon Institute for Financial Economics were established last year. Both centres will conduct research and training programmes to generate highly specialised and Asian-centric knowledge in finance.

Conclusion

35. Eleven years ago, the Asian financial crisis swept through the region. Seeing the economic wreckage that it caused, Asian governments were determined to avoid a repeat, thus spurring them to undertake the necessary reforms, and growing stronger as a result. Singapore, which was not guilty of the financial excesses then, was nevertheless affected. Pressing on with further reforms and liberalising our financial sector allowed us to emerge stronger from the Asian financial crisis. Witness the robust development of the financial sector in the last few years.

36. In the same vein, we must not waste the current crisis. Whether as financial institutions, regulators or as consumers, this downturn has not only taught us new lessons but also presented opportunities for the nimble and prepared. Today’s challenges may be different and the future environment uncertain, but with the same willingness to adapt to new realities, we can build the foundation for stronger growth. I urge us all to take advantage of the current crisis to create new opportunities for our financial sector.

37. Thank you and have an enjoyable evening ahead.

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