SPEECH BY MR LEE HSIEN LOONG, PRIME MINISTER, AT STANDARD CHARTERED 150TH ANNIVERSARY IN SINGAPORE GALA DINNER , 19 FEBRUARY 2009, 7:35 PM AT SHANGRI-LA HOTEL

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1. I am happy to join you tonight for the 150th Anniversary celebrations of Standard Chartered Bank.

2. StanChart has a rich and eventful history, and played a significant role in the early days of Singapore. It set up its first Singapore branch as part of an Asian expansion to finance the growing trade between Europe and the East. In its early years, StanChart supported the growth of the rapidly developing rubber and tin industries in Malaya, and was an active financier of commercial ventures in other key sectors. The Bank was even authorised to issue banknotes in Singapore until the end of the 19th century.

3. Over the last 150 years, StanChart has stayed committed to Singapore in good years and bad. The Bank survived the regular boom and bust cycles of the 19th Century, the Great Depression and World War II. It has been a pioneer in many areas of financial services including ATMs, online services and various innovative products. While the Bank has expanded its global footprint, it continues to have a major presence in Singa¬pore, servicing the domestic market as well as basing significant global operations here.

4. StanChart has been able to grow into an established global bank because it takes a long-term perspective of its business. The Bank maintains a strategic focus, builds lasting relationships with its customers, and holds a steady course, not whipsawed by cycles and moods.

DEVELOPMENT OF SINGAPORE'S FINANCIAL SECTOR

5. Similarly, governments must adopt a long-term perspective in supervising and developing the financial sector. We must keep abreast of industry developments, and the state of the global economy. We try to moderate excesses in booms, and stabilise things in downturns. In a crisis, we should not just focus on fire-fighting immediate problems, but should also step back, reassess our position, and prepare ourselves for the emerging landscape. We must take into account how the world has changed, and act early to reposition ourselves. Yet we must not be overly coloured by the immediate impact of the crisis or the mood of the moment.

6. Singapore started to liberalise its financial sector during the Asian financial crisis. We progressively created a more open and competitive environment. This was hardly the path of least resistance, as panic and disruption spread contagiously from one country to the next. While the natural instinct would have been to hunker down and isolate our domestic markets to protect local financial institutions from competition, Singa¬pore did the opposite. We gave foreign financial institutions more access to the domestic market, and deliberately exposed local players to greater competition so as to spur their development and upgrading.

7. We also allowed more leeway for financial innovation and market play, creating more choices for consumers with different needs. We shifted towards a disclosure-based regime, and made investors take more responsibility for their investment decisions. We required the banks to develop risk-management capabilities and have their Boards take responsibility for overseeing risk. MAS focused supervisory resources on the larger players and those who posed greater systemic risk, and monitored risk management systems instead of inspecting individual transactions.

8. There was no "big bang". We set out clearly the directions we were taking, but proceeded in careful and controlled steps, especially in the banking industry. We were very conscious that markets can get carried away, and that the process of opening up could itself create new risks, if regulators and players went too fast or too far. Hence, we always kept one foot on the ground, so that any mis-steps would be small, and could be corrected in time. Taken together, this incremental approach added up to a decisive change over several years.

Development of Banking Sector

9. The most critical liberalisation was in the banking sector. We opened up the domestic retail market to foreign banks through the Qualifying Full Bank (QFB) scheme, and broadened the scope of domestic business for the wholesale banks. But we did not take a laissez faire attitude. We believed in having strong local banks, anchored in Singapore, with a long-term stake in the well-being of the economy. But the way to strengthen local banks was to create a more competitive domestic environment, encourage them to sharpen their capabilities and set their sights beyond being domestic players. Similarly, we welcomed the leading foreign banks to broaden their domestic presence and grow a strong stake in Singapore.

10. Our concern was not just the soundness of the banking sector, but the stability of the overall economy. In normal times, it may not matter who owns the banks, or what stake they put here, because all banks will make loans based on similar commercial considerations. But in a crisis, it makes a crucial difference whether a bank has a long-term stake or a peripheral interest in Singapore. A bank with a long-term stake will consider the merits of borrowers who need financing to do business, and continue to nurture relationships with established clients, thus helping them and the economy to see through the crisis. But a bank for which Singapore is a peripheral part of its business may pull back indiscriminately to reduce its country exposure, or in response to its head office's instructions to shrink the global balance sheet. If all banks behaved that way, the economy would be in trouble.

11. Hence, while opening up banking to foreign competition, we encouraged the local banks to upgrade themselves. Eventually they consolidated from seven banks to the present three, and are now fitter and have leaner and stronger managements. Overall, the local banks have held their market share in Singapore despite the competition, and have strengthened their presence in the region.

12. The banking reforms in Singapore have led to stronger and more dynamic local banks, which act as firm anchors in the system in times of difficulty. But the leading foreign banks play an important role too. Foreign banks have grown to be active players in the wholesale banking market and in wealth management. In particular, the QFBs play an important role. They have expanded their operations, and made Singapore a regional or even global platform for important banking services. Having grown their domestic market franchise, QFBs should continue to take a long-term commercial view, stay with their clients and ride through the business cycle with them.

13. This pragmatic approach to liberalising the banking sector has proven wise in the current global crisis. Many countries have now discovered that borders and ownership do matter in banking, even between different countries in the single European market. The challenge for governments will be to nurture banks with major stakes in their economies, but while keeping their markets open to competition. This will be a difficult balance to strike.

Development of Fund and Wealth Management Sectors

14. We made good progress also with fund and wealth management. Singa¬pore has become a leading centre for managing Asian wealth globally, and managing wealth from around the world in Asia. We also liberalised rules for retail investors, to enable a better educated and more affluent population to invest in a wider range of financial products.

15. Unfortunately, this sector has been severely affected by the financial crisis. In tandem with the sharp decline in global markets, assets under management have shrunk. The collapse of Lehman Brothers had an unexpected impact here and around the world, through credit-linked structured products like the Lehman Minibond Notes, DBS High Notes and Morgan Stanley Pinnacle Notes.

16. This structured products issue has been a learning experience for financial institutions, investors and regulators. Financial institutions have been reminded that when marketing investment products they must advise customers responsibly, take full account of their needs and financial situations, and avoid mis-selling. Investors have learnt painfully that not all investments succeed and higher returns mean higher risks. Investors should not invest in products which they do not understand, or whose risks they cannot bear. MAS required financial institutions to establish a proper process for complaints handling, and to appoint independent persons to oversee this process. It urged the financial institutions not to take a narrow, legalistic view in the resolution of complaints. MAS is currently investigating whether there has been any wrongdoing by the financial institutions, and will take action where this proves to be the case.

17. MAS is also reviewing the current regulatory regime for the sale and marketing of structured products. In doing so, we must continue to emphasise investor responsibility, so that the public will not expect an automatic bailout if their investments go wrong. We will also continue to expect financial institutions to meet high standards in dealing fairly with their customers. The Government will insulate the supervisory regime from populist pressures, so that MAS can deal correctly and impartially with all parties.

18. Looking back over the last decade, controlled and phased liberalisation of the financial industry has benefited Singapore and Singaporeans. The financial sector has expanded by almost 80% over the last 10 years. We have established ourselves as a leading Asian financial centre. The industry has seen much greater use of technology, and much greater diversity of players, strategies and products. Competition and the presence of leading international financial institutions have meant more choice, better services and competitive prices for consumers and business, and for the whole economy. While financial business has contracted in the current crisis, we are well-positioned to grow again and strengthen our role as a major financial centre once the Asian economies and markets recover.

LEARNING FROM THE GLOBAL FINANCIAL STORM

19. 12 years after the Asian Financial Crisis, we face another financial crisis, this time of global scale. Fortunately, Singapore's financial sector has not been badly hit. While our equity market has suffered a big fall, an inevitable result of globalized capital flows, our financial system remains healthy. Our banks have very low non-performing loans (NPLs), minimal exposure to toxic assets, and are well-capitalised and sound. We were spared partly because our financial institutions were conservative and prudent, and did not venture too far into complex derivative products, and because our regulators were alert and proactive, and upheld high standards of supervision and risk management. But we were also lucky – we had not rushed to be right at the frontier of new techniques, and our small domestic market made some of the problematic practices of securitisation and risk transfer obviously infeasible.

20. While our banks are in good shape, there is still substantial risk in the global environment, and we expect our economy to have a very difficult year ahead. We must remain vigilant.

21. The crisis has alerted regulators all over the world to new dangers. First, excessive borrowing and leverage which multiplied the risks to individual financial institutions and the entire system. Second, complex securitisation products whose interactions can destabilise the whole financial system in unforeseeable ways, which were not fully understood even by the financial institutions selling them. Third, the limitations of mathematical models of risk and valuation, which model normal risks well but not low probability tail events or crisis behaviour of markets. Fourth, the systemic risks posed by major institutions which are too big to fail, not just commercial banks but also unregulated or lightly regulated participants. Fifth, the potentially catastrophic consequences of financial bubbles not identified, still less deflated in good time. Finally, how the globalisation of markets has made this a worldwide crisis.

22. Global regulators are now thinking hard about how to strengthen the rules. A fundamental review would have to cover many areas. Regulators should re-examine their overall stance on supervision of financial institutions. We need new rules on leveraging and gearing, including for non-bank institutions, and tighter controls on banks' proprietary operations. Regulators also need to develop procedures to ensure that financial institutions manage liquidity risk better. Accounting standard setters should develop stricter rules for treating off-balance-sheet items. In all probability, Basel II rules on capital adequacy will have to be tightened; there is growing international consensus that insufficient capital is currently required for trading book and securitisation risks. We also need measures to counter pro-cyclical behaviour, and new regulatory tool-kits, especially macro-prudential policies, to ensure financial stability.

23. In Singapore, it is unlikely for a bank to fail due to domestic problems, but problems elsewhere may affect its operations here. If it is a major financial institution, there could be large ripple effects on the health of other banks and confidence in the entire financial sector. We will therefore need to watch for contagion and deal with systemic risk. We have to ensure not just that individual banks are sound, but that the system is robust and stable, not just over normal business cycles, but in extreme swings like the one we face today. Hence we are closely monitoring developments in both foreign markets and in our own system, so that we can respond quickly with appropriate supervisory actions in the event of external failures.

24. We are also reviewing our regulations. Our basic framework has worked well, but we are scrutinising the system to minimise vulnerabilities. Where there are regulatory gaps we will close them. Where new regulatory and supervisory approaches are developed elsewhere, we will study and consider adopting them. We will do so critically, always asking ourselves whether they are relevant and useful to us, given Singapore's specific circumstances.

25. However, I believe that our basic direction in overseeing and developing the financial sector has been correct. While we take reasonable safeguards, we must stay open to the world. Walling ourselves in does not mean that we would be safe; it just means we will starve. We will continue to allow free play and competition, to operate a disclosure-based regime, to rely on the market to allocate capital productively and to intermediate funds flows efficiently, and to permit and indeed encourage creativity and innovation in the financial industry. All these must of course remain subject to sound regulation and supervision. MAS will thus maintain oversight of the stability of the financial system as a whole, and ensure that the right rules and incentives are in place.

26. Hence, even when the Government has to intervene in the workings of the market, we will try to work through the financial institutions. An example is the current shrinkage of credit and reluctance of many banks to lend. Banks have reasons to be cautious in a recession, as non-performing loans typically rise. But if each bank cuts back loans based on its own assessment, and all other banks simultaneously do the same, the result will be a sharper contraction of credit that creates a domino effect of corporate failures and a further economic contraction. Collectively, all banks will be hurt more.

27. The Government is in no position to tell banks whom to lend to. Nor is it desirable for the Government to lend directly to borrowers who cannot get loans. But the Government has a valid interest in keeping credit flowing, to avoid a negative spiral of credit and economic contractions. We do not want basically viable businesses to fail for lack of funds because lenders are too risk averse.

28. The Government has therefore stepped in to take on the bulk of risk on new loans to small and medium enterprises, to encourage the banks to lend but without supplanting their judgment. Through schemes like the Local Enterprise Finance Scheme (LEFS) and the Special Risk-Sharing Initiative (SRI), the Government shares a substantial part of the risk of the loans but still require banks to bear at least 20% of the risk. In this way, the banks have an incentive to assess loans prudently, but not too conservatively.

29. Such a regulatory approach – relying on the private sector and the profit motive, but with the government establishing the right framework within which the private sector will operate, subject to proper disclosure and safeguards – will not absolutely guarantee that things will never go wrong. But that is impossible even if governments nationalise the whole financial industry, and substitute bureaucrats for bankers. The key is to have a balance between market discipline and regulation. This calls for first-class regulators who are just as capable as the industry practitioners. They must stay abreast of developments in the field, and understand the latest financial instruments. They must be up-to-date in the game, not always lagging behind practitioners, unable to recognise the dangers or to prevent them until it is too late.

INTERNATIONAL COOPERATION

30. Singapore is taking active measures to respond to the crisis, but ultimately this is a global storm requiring coordinated global action. We will continue to contribute constructively to various international and regional forums. There are three areas where work needs to be done.

31. First, on financial reform, governments and regulators, as well as international bodies will need to strengthen the international financial architecture to prevent a crisis of this scale from happening again. We need to improve surveillance of the global financial system, to draw attention to vulnerabilities in both developing and developed countries, and to develop policy responses to address these vulnerabilities. We should tap ideas and inputs from multiple sources, and not just work out an arrangement among a few players. Singapore actively contributes to such discussions in bodies such as the Financial Stability Forum (FSF), Basel Committee on Banking Supervision, and Financial Action Task Force on Money Laundering.

32. Second, governments must cooperate to promote free trade, amidst growing pressures for nationalist and protectionist measures. We can already see in many countries banks discriminating between domestic and foreign customers, schemes to buy local products and disadvantage foreign suppliers, and emotional protests by workers and unions against foreign workers and immigrants. It is important to resist these sentiments and pressures. Yielding to them will only worsen the situation. Governments must take a strong united stand in support of free trade. Leaders are making the right statements, but they must back these up with concrete action. They must demonstrate the political will to block protectionist measures and keep international trade flowing. As Chair of APEC this year, Singapore will work with like-minded economies and international financial institutions like the IMF, World Bank and Asian Development Bank to advance free trade.

33. Third, governments must coordinate their economic policies. Right now governments need to coordinate and implement both monetary and fiscal policies on sufficient scale to cushion the global fall in economic activity. The priority must be to arrest the debilitating cycle of poor consumer sentiment, weakening economic activity and tightening credit. In the longer term, there will have to be a global re-balancing of savings and consumption. The US will have to consume less and save more, while Asian countries generally will have to consume more. The adjustment is already underway as US consumers deleverage. However, to identify and get to a more sustainable balance will require international understanding and better coordination.

34. Governments also need to discuss with one another the extraordinary measures they are individually taking to counter the crisis, and how to unwind these later in a timely and coordinated way. These extraordinary measures have dramatically increased public and market expectations of government bailouts. They have also introduced an unlevel playing field between financial institutions that receive government support from those that do not. It is critical to roll back the moral hazard and re-level the playing field as calm and stability returns to the global economy. This will require early discussion and coordination among governments to work out the exit strategies.

CONCLUSION

35. We can expect significant and permanent changes in the global financial system. Financial institutions and regulators need to be alive to these changes. In countries worst hit by this crisis, the banks will have to rebuild the trust of the communities which they serve, by cleaning up their books and strengthening their balance sheets. In Asia, we have an opportunity to build up our financial system on a sounder footing, learning the lessons from this crisis, but building on what we learnt from the earlier Asian Financial Crisis.

36. The basic role of finance in intermediating credit and capital to the economy and facilitating international trade will take centre stage. Sound financial intermediation is crucial to growth in Asia. There is a range of needs arising from industrialisation, urbanisation and infrastructure projects. Financial institutions will have to think of how best to meet these needs in straightforward, effective ways. To support this, we need robust banking systems. We also need to make further progress in building stable capital markets, focusing on well-implemented basics rather than overly complex schemes. By maintaining high regulatory standards, we can better protect ourselves against the ups and downs of the global economy.

37. Singapore’s financial sector is a major part of our success story, and forms a vital component of the economy. We must continue to foster a vibrant and reputable financial centre in Singapore, one that services a growing Asia and is trusted for its integrity and reliability. In this crisis, the Government will do its utmost to support the financial sector and co-share risks. We will maintain confidence in the economy and prepare for the future. We will continue to develop talent in key areas of finance. In tandem with our efforts, the industry must stay committed, continue to innovate and enhance the value of their businesses. In the new landscape, banks will be more careful; new rules may be introduced. But by keeping a long-term perspective, our finance industry can continue to grow and prosper.

38. I am confident that StanChart will weather this downturn, just as you have done during turbulent periods in your history, and continue to play a significant role in Singapore’s growth story. Congratulations on your 150th Anniversary, and may you enjoy enduring success in the future.