

THE MONETARY AND BANKING DEVELOPMENT OF SINGAPORE AND MALAYSIA

Second & Revised Edition
Winner of the Singapore National
Book Development Council Award 1976

The Monetary and Banking Development of Singapore and Malaysia

LEE SHENG-YI

李繩毅 著



SINGAPORE UNIVERSITY PRESS,
NATIONAL UNIVERSITY OF SINGAPORE

© 1974 Singapore University Press
Kent Ridge, Singapore 0511
Revised Edition 1986

ISBN 9971-69-098-5

Typeset by: International Typesetters
Printed by Singapore National Printers (Pte) Ltd.

**The Monetary and Banking
Development of
Singapore and Malaysia**

**To
my beloved mother,
brothers, sister and wife**

Preface

Twelve years ago, in 1974, the first edition of this book was published. It received excellent reviews both from the general public and scholars in the monetary field, and gained the National Book Development Council Book Award for non-fiction in English in 1976.

Although the book has been out of print for several years and there is demand from students, bankers, financiers and administrators for the book, I have not been able to present the second edition until now, as I have been hard pressed for time by teaching and other research work.

In this second edition, the monetary and banking development of Singapore and Malaysia has been brought up-to-date and the historical part has been condensed and shortened. The financial structures and monetary policies of the two countries have been expanded. There is much more econometric-statistical analysis in this edition, particularly in Part Five. Monetary Analysis is highlighted more in this edition.

I have been working on the subject of money, banking and finance of Singapore and Malaysia since 1965. Many bank managers and government officials have granted me interviews and provided me with data and information. In particular, Bank Negara Malaysia and the Monetary Authority of Singapore have continuously favoured me with much statistical data. Dr. Lin See Yan, Deputy-Governor of Bank Negara spent many hours of discussion with me. To all I owe a great debt of gratitude.

In the econometric analysis, I am grateful to Dr. W.K. Li of the University of Hong Kong who gave help in the sections, *Money, Income and Prices and their Lead-Lag Relationship in Singapore*, and *The Lead-Lag Relationship of Money, Income and Prices in Malaysia*. Dr. Tze Yiu Kuen, my colleague in the National University of Singapore gave me valuable statistical guidance for the analysis of the demand and supply of money in Singapore and Malaysia. My two students, Wong Sow Fook and Ong Kok Ning kindly helped me in computer work. I am further grateful to the National University of Singapore for granting me a research fund for carrying out the computer work related to the book.

I would also like to thank the editors of this book, Mrs. Rosalind Chan and Miss Lena Qua who have taken much time and effort to edit the manuscript.

Contents

List of Tables	xi
List of Graphs and Figures	xv
List of Appendix Tables	xvii
Preface	xix

Part One: Historical Development

1. Introduction	3
2. Evolution of the Currency Board System	7
<i>Silver Standard, 1786-1903</i>	7
<i>Issue of Currency Board Notes, 1899</i>	11
<i>Currency Reform, 1903-1906</i>	12
<i>Gold-Exchange Standard, 1906-1914</i>	14
<i>Currency Ordinance, 1938</i>	16
<i>Malaya, British Borneo Currency Agreement, 1950</i>	18
<i>Malaya, British Borneo Currency Agreement, 1960</i>	19
<i>Establishment of Bank Negara, 1958</i>	21
3. Appraisal of the Currency Board System	28
<i>Effect on Trade and Development</i>	28
<i>Working of the Currency Board</i>	29
<i>Merits and Demerits</i>	31
4. Development of Commercial and Merchant Banks	39
<i>Early Period, 1840-1903</i>	40
<i>Pre-War Period, 1903-1941</i>	43
<i>Post-War Period, 1946-57</i>	49
<i>Post-Independence Period, Since 1957</i>	50
<i>Similarities and Differences Between Local and Western Banks</i>	53
<i>Merging Movement of Banks</i>	57

Part Two: Monetary and Exchange Rate Issues

5. Currency Split, 1967	61
<i>Real Causes</i>	61
<i>Currency Redemption</i>	66
<i>Implications and Economic Consequences</i>	67
6. Sterling Devaluation, 1967	69
<i>Reaction in Malaysia and Singapore</i>	69
<i>Follow Devaluation?</i>	71
<i>Old and New Dollars</i>	74

7. International Monetary Crises and the Impact on Malaysia and Singapore	77
<i>The US Dollar Crisis, 1971</i>	77
<i>The Floating of Sterling since June 1972</i>	78
<i>The US Dollar Second Devaluation, 1973</i>	79

Part Three: Financial Structures

8. Financial Structure and System of Singapore	85
<i>The Monetary Authority of Singapore (MAS)</i>	85
<i>Singapore Currency Board</i>	89
<i>Commercial Banks</i>	90
<i>Finance Companies</i>	94
<i>Merchant Banks</i>	97
<i>Post Office Savings Bank (POSB)</i>	100
<i>Central Provident Fund (CPF)</i>	101
<i>Insurance Companies</i>	104
<i>Money and Discount Markets</i>	105
<i>The Stock Exchange of Singapore (SES)</i>	106
<i>Other Financial Institutions</i>	107
<i>Overall Review of the Financial System</i>	108
<i>Asian Dollar Market (ADM)</i>	110
<i>Asian Bond Market (ABM)</i>	115
9. Financial Structure and System of Malaysia	118
<i>Bank Negara Malaysia</i>	119
<i>Commercial Banks</i>	121
<i>Finance Companies</i>	129
<i>Merchant Banks</i>	133
<i>Industrial Finance Institutions</i>	136
<i>Rural Credit and Development Institutions</i>	138
<i>House Credit Institutions</i>	139
<i>Other Financial Institutions</i>	140
<i>The Capital Market: Stock Exchange of Malaysia</i>	141
<i>Overall Review of the Financial System</i>	142

Part Four: Monetary Policies

10. Monetary Policy of Singapore	149
<i>Review of Monetary Policy</i>	149
<i>Instruments of Monetary Policy</i>	152
<i>Foreign Exchange Market</i>	153
<i>Nominal Effective Exchange Rate (NEER) and</i> <i>Real Effective Exchange Rate (REER)</i>	158

11. Monetary Policy of Malaysia	166
<i>Savings, Investment and Flow of Funds</i>	166
<i>Objectives and Instruments of Monetary Policy</i>	170

Part Five: Monetary Analysis

12. Monetary Analysis of Singapore	181
<i>Demand for Money in Singapore</i>	181
<i>Statistical Analysis</i>	187
<i>Money Supply and Behaviour of Money in Singapore</i>	193
<i>Money, Income and Prices and their Lead-Lag Relationship in Singapore</i>	216
13. Monetary Analysis of Malaysia	226
<i>Demand for Money in Malaysia, 1970-81</i>	226
<i>Money Supply in Malaysia, 1968-82</i>	231
<i>Determinants of Money Supply, M_1</i>	232
<i>The Lead-Lag Relationships of Money, Income and Prices in Malaysia</i>	249
14. Problems and Prospect	259
Appendices	261
Bibliography	281
Index	293

List of Tables

8.1	Numbers of Financial Institutions in Singapore, 1965-84	86
8.2	Balance Sheet of the Monetary Authority of Singapore, 1971-84	88
8.3	Assets and Liabilities of Commercial Banks in Singapore, 1967-83	92
8.4	Assets and Liabilities of Finance Companies, 1969-83	96
8.5	Assets and Liabilities of Merchant Banks, 1974-83	99
8.6	Savings Deposits and Application of Deposit Funds of the Post Office Savings Bank, 1966-83	102
8.7	Total Assets, Deposits, Loans, Investments and Growth Rates of Financial Institutions as at End 1983	109
8.8	Consolidated Assets and Liabilities of Asian Currency Units, 1968-83	113
8.9	Asian Bond Issues, 1971-83	116
9.1	Balance Sheet of Bank Negara Malaysia, 1966-83	120
9.2	Sources and Uses of Commercial Bank Funds in Malaysia, 1966-83	123
9.3	Direction of Commercial Bank Lending in Malaysia, 1967-83	126
9.4	Sources and Uses of Finance Company Funds of Malaysia, 1969-83	131
9.5	Assets and Liabilities of Merchant Banks of Malaysia, 1973-83	135
9.6	Total Assets of the Financial System of Malaysia, 1970-83	143
10.1	Money, Income and Price, 1968-83	151
10.2	Interest Rates of Commercial Banks, Finance Companies and POSB	154

10.3	Relative Shares of Trading Partners in Singapore in the Estimation of Nominal Effective Exchange Rate (NEER) by Overseas Union Bank and Oversea-Chinese Banking Corporation	160
10.4	Trade-Weighted Exchange Rate Index for the Singapore Dollar (NEER)	161
10.5	Real Effective Exchange Rate (REER) for the Singapore Dollar	164
11.1	Money, Income and Prices of Malaysia, 1966-83	174
12.1	Demand for Money Functions, Real Term	189
12.2	Government's and CPF's Savings and Surplus in Balance of Payments	195
12.3	Determinants of Money Supply of Singapore, M_1 : Changes	198a
12.4	Relevant Variables for the Monetary Identity, 1968-82	201
12.5	Percentage Change in M_2 Attributable to Indicated Determinants	204
12.6	Means and Standard Deviations of D/R, D/C, Money Multipliers, Income and Transaction Velocities of Money	204
12.7	Directions of Predictive Causality	221
12.8	Directions of Predictive Causality	222
12.9	Directions of Predictive Causality	222
13.1	Demand for Money Function, Real Term of Malaysia, 1970-81	228
13.2	Average Annual Growth Rates of (a) Money Supply	233
13.2	Average Percentage Distribution of (b) Money Supply M_1 and Private Liquidity M_2	236
13.3	Determinants of Money Supply of Malaysia, M_1 : Changes	237

13.4	Balance of Payments and Changes in Currency, M ₁ , M ₂ and M ₃ and in External Reserves of Malaysia	239
13.5	Relevant Variables for the Monetary Identity of Malaysia, 1968–81	240
13.6	Percentage Change in M ₂ Attributable to Indicated Determinants	241
13.7	Means and Standard Deviations of H, D/R, D/C, Money Multipliers, Income and Transactions Velocities of Money	243
13.8	Lead-Lag Relationship	254

List of Graphs and Figures

2.1	Movement of Silver Price and Dollar/Sterling Exchange Rate, 1867–1938	9
10.1	Nominal and Real Effective Exchange Rates (Trade-weighted), 1972–84	156
10.2	US\$/S\$ Exchange Rate and Real Dollar Exchange Rate, 1972–84	157
10.3	Exchange Rate Indices for the Singapore Dollar, 1972–84	159
11.1	Flow of Capital Funds in the Third Malaysia Plan, 1976–80	168
11.2	Flow of Capital Funds in the Fourth Malaysia Plan, 1981–85	169
12.1	Money Supply, M_1 , M_2 , M_3 (Jan. 1966 – Mar. 1982)	188
12.2	GDP at Current and Constant (1968) Market Prices, 1966–82	190
12.3	Deposit/Reserves and Deposit/Currency Ratios of Singapore, 1966–82	203
12.4	High-power Money, Reserves, and Currency in Active Circulation, Jan. 1968–Mar. 1982	206
12.5	Money Multipliers with Respect to M_1 and M_2 , 1966–82	209
12.6	Income Velocities, V_1 , V_2 and V_3 , 1968–82	212
12.7	Transaction Velocity of Money, 1968–82	214
12.8	CPI and GDP Deflator, 1965–82	220
13.1	Deposit/Reserve and Deposit/Currency Ratios of Malaysia, 1968–82	242
13.2	High-power Money, Currency in Active Circulation and Bank Reserves of Malaysia, 1968–82	245
13.3	Money Multipliers with Respect to M_1 and M_2 of Malaysia, 1968–82	246

13.4 Income Velocities V_1 , V_2 and V_3 of Malaysia, 1971-82	248
13.5 Money Supply of Malaysia, M_1 , M_2 and M_3 , 1968-82	250
13.6 GDP at Current and Constant (1975) Prices of Malaysia	251
13.7 Consumer Price Index and GDP Deflator of Malaysia	252

List of Appendix Tables

3.A Actual Percentage Distribution of Currency Profit among the Participating Governments, 1941-68	261
3.B Liquid Portion, Investment Portion, Bullion Market Value of Coins in Circulation and Total Reserves of the Currency Fund, 1913-38	262
3.C Liquid Portion, Investment Portion, Bullion Market Value of Coins in Circulation and Total Reserves of the Currency Fund, 1941-68	263
3.D Income and Expenditure Account of the Currency Fund, 1900-1938	264
3.E Income and Expenditure Account of the Currency Fund, 1941-68	265
3.F Net Income, Annual Appropriation, Annual Transfer to Currency Surplus Fund and Distribution of Currency Profit, 1941-68	267
8.A Commercial Banks in Singapore as in February 1984	268
8.B Finance Companies in Singapore as in March 1984	270
8.C Approved Merchant Banks in Singapore as in February 1984	271
8.D Discount Houses in Singapore as in September 1978	273
8.E International Money Brokers in Singapore as in February 1984	274
9.A Commercial Banks in Malaysia as in 1984	275
9.B Finance Companies in Malaysia as in 1984	277
9.C Merchant Banks in Malaysia as in 1984	279
13.A Regression Equations on the Balance of Payments, Currency M_1 , M_2 and M_3 and External Reserves of Malaysia	280

PART ONE

HISTORICAL DEVELOPMENT

