A Sound and Progressive Financial Sector: The Supervisory Approach of the Monetary Authority of Singapore

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Introduction

The mission of the Monetary Authority of Singapore (MAS) is "to promote sustained and non-inflationary economic growth and a sound and progressive financial services sector". To carry out this mission, MAS conducts exchange rate policy, manages the official foreign reserves, regulates and supervises the financial sector, and works with the industry to develop Singapore as an international financial centre.

In 1997, MAS launched a comprehensive review of Singapore's financial sector. We fundamentally changed our regulatory approach, from one-size-fits-all prescriptive regulation towards a more risk-focused supervisory approach. We liberalised the industry, allowing freer competition and greater risk taking by financial institutions. We actively promoted activities in which we had competitive advantages.

Singapore's financial sector held up well against the full impact of the Asian financial crisis, the SARS outbreak and other external shocks. Despite the more volatile environment, it has grown and matured. Our financial system is robust, and our legal, supervisory and institutional framework is sound. Today, over 600 local and foreign financial institutions are in Singapore. They offer a comprehensive range of world-class financial services and with 5% of our workforce, contribute 11% of Singapore's GDP.

MAS' Supervisory Approach

MAS seeks to promote a sound and progressive financial services sector through both financial supervision and developmental initiatives. We supervise the banking and insurance industries, as well as the capital markets. At the same time, we work in partnership with the private sector to identify and implement strategies for developing Singapore as an international financial centre.

Working with the boards and managers of financial institutions, MAS encourages the effective management and mitigation of risks taken by financial institutions. We aim to do so in a way that does not unnecessarily hinder the competitiveness and dynamism of financial institutions, or the efficiency of financial markets. In supervising the financial sector, MAS is guided by 12 key principles which collectively characterise our approach as **risk-focused, stakeholder reliant, disclosure-based and business-friendly**.

Risk-Focused

Principle 1: Emphasise risk-focused supervision rather than one size-fits-all regulation

In a prescriptive one-size-fits-all rules regime, a supervisor prescribes activities and risks that institutions can and cannot take. This approach is increasingly ineffective in a rapidly changing environment, and also unnecessarily restrictive for the stronger institutions. With risk-focused supervision, MAS evaluates the risk profile of an institution, taking into account the quality of the institution's internal risk management systems and processes. This allows us to give greater business latitude to well-managed institutions while retaining higher requirements or tighter restrictions for weaker ones.

Principle 2: Assess the adequacy of an institution's risk management in the context of its risk and business profiles

MAS takes a proportionate approach in assessing an institution's risks. Rather than have a fixed view of what constitutes acceptable business risks or risk management standards, MAS assesses whether risk management systems and internal controls are commensurate with the institution's risk and business profiles. Institutions engaging in complex financial businesses must demonstrate that their risk management capabilities match their risk appetite and operations, while institutions engaging in less complex or risky financial activities may find simpler risk management processes adequate.

Principle 3: Allocate scarce supervisory resources according to impact and risks

We categorise financial institutions according to the potential impact they would have on Singapore's financial system, economy and reputation in the event of a significant mishap (e.g. financial failure and prolonged disruption), and also the likelihood of these significant mishaps occurring. More resources are channeled towards supervising systemically-important institutions and institutions with higher risk profiles.

Principle 4: Ensure institutions are supervised on an integrated (across industry) and consolidated (across geography) basis

As the home supervisor of local financial groups, MAS takes an integrated supervisory approach, evaluating them on a whole-of-group basis across their banking, insurance and securities activities. We also supervise these financial groups on a consolidated basis, taking into account both their Singapore and overseas operations. For foreign banks operating in Singapore, we ensure that they are subject to consolidated supervision by their home regulators.

Insurers that are part of a wider insurance group or conglomerate are monitored on a solo and group-wide basis to assess the potential impact on the Singapore insurance operations. We also cooperate and share information with foreign supervisors for effective supervision of internationally-active insurers and insurance groups.

Principle 5: Maintain high standards in financial supervision, including observing international standards and best practices

MAS continually strives to maintain high standards in financial supervision, benchmarking itself against international standards and best practices. As an international financial centre with a strong stake in global financial stability, MAS participates actively in regional and international initiatives to enhance regulatory standards and supervisory training.

Principle 6: Seek to reduce the risk of failure rather than prevent the failure of any institution

MAS does not aim to prevent all failures. We require financial institutions to observe prudential standards, such as appropriate capitalisation, liquidity and exposure limits. We have the power to intervene if we believe that the interests of depositors, policyholders or investors are at risk. But we cannot (due to the complexity of financial activities) and should not (due to moral hazard and the undesirable consequences of excessive regulatory burden) guarantee the soundness of financial institutions.

Consumers should recognise that there are risks involved in dealing with financial institutions. Like other regulators, MAS faces the challenge of educating the public about this reality and managing their expectations. Deposit insurance and policy owners' protection schemes make explicit the level of protection available to depositors and policy owners. They also help consumers realise that risks are inherent in financial transactions.

While we cannot prevent failures, we are conscious of the systemic impact that failures can have and the damage they can do to consumers and Singapore's reputation as a financial centre. MAS will seek to reduce the risk of failure of institutions through increased supervision where it is appropriate and effective. In the case where increased supervision is ineffective, we will take measures to limit the impact of a failure.

Stakeholder-Reliant

Principle 7: Place principal responsibility for risk oversight on the institution's board and management

The primary responsibility for the prudential soundness and professional market conduct of a financial institution lies with its board of directors and senior management. By encouraging best practices by boards and management, we minimise the need to interfere with institutions' business decisions.

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Principle 8: Leverage on relevant stakeholders, professionals, industry associations and other agencies

Apart from MAS, other stakeholders such as shareholders, creditors, counterparties, depositors, policyholders and home supervisors also have an interest in the continued financial health and stability of financial institutions. Likewise, professionals such as external auditors, internal auditors and actuaries, as well as credit rating agencies, are specialists in assessing the risks inherent in the institutions and the adequacy of risk management and internal control systems. In addition, many financial institutions here are members of their respective industry associations.

MAS leverages on the relationships and work of many of these stakeholders, including the home supervisors, SGX, auditors and industry associations, to complement our own supervision of the institutions. MAS also works with other agencies, such as the Council on Corporate Disclosure and Governance, the Ministry of Finance, and the Accounting and Corporate Regulatory Authority, to strengthen corporate governance and disclosure standards.

Disclosure-Based

Principle 9: Rely on timely, accurate and adequate disclosure by institutions rather than merit-based regulation of products to protect consumers

Under a merit-based regime, the regulator assesses the suitability of a product before it is allowed to be introduced in the marketplace. Under a disclosure-based regime, the consumer makes well-informed decisions when purchasing financial products and services based on material information being made available to the consumer.

A disclosure-based regime encourages innovation and facilitates the development of a more sophisticated body of consumers. The role of MAS is to put in a place a regulatory framework that facilitates timely, accurate and meaningful disclosure of material information that consumers could reasonably rely on in making financial decisions.

Principle 10: Empower consumers to assess and assume for themselves the financial risks of their financial decisions

A disclosure-based regime is meaningless if consumers do not know how to make use of disclosed information in making financial decisions. Consumers should understand the nature of different financial products and the issues they should consider in making their financial decisions. MAS works in partnership with other public sector agencies and industry bodies on consumer education to facilitate this.

Business-Friendly

Principle 11: Give due regard to competitiveness, business efficiency and innovation

MAS seeks to undertake supervision in a way that does not unnecessarily impair the competitiveness and dynamism of individual institutions and Singapore's financial services sector. We take into account the business and operational concerns of the institutions and industry, so as not to hinder growth and innovation as long as the risks are adequately managed.

Principle 12: Adopt a consultative approach to regulating the industry

MAS actively seeks feedback from market practitioners and the public, so as to help us develop regulations that take into account market realities and industry practices. Consultation also helps to pre-empt implementation problems, minimise unintended consequences, and foster better industry understanding and support. In the end, it is the combined efforts of MAS and the industry that contribute to financial stability and resilience while promoting enterprise and innovation.

Conclusion

A sound and progressive financial services sector is a vital part of any modern economy. Apart from its direct and significant contribution to gross domestic product, the financial services sector intermediates between savers and borrowers, allocates financial resources efficiently, and thereby enhances economic growth and job creation. Promoting a sound and progressive financial services sector is an integral part of ensuring the success and resilience of the Singapore economy.

MAS is committed to the vision of Singapore as a leading global financial sector, one which is competitive, fosters enterprise and innovation, and maintains high regulatory standards. We have made steady progress toward this goal and continue to work with our stakeholders to achieve our vision. ■