SINGAPORE "K.I.S.S.-A.S.S."

Exactly four years ago I wrote an opinion piece about Singapore (Opinion Piece 14). That opinion piece was primarily designed to highlight the attractiveness of the Singaporean economy and one particular company in which I had invested some money.

Even though it was not the main purpose of the piece I also happened to mention that Ireland and Singapore had a number of similarities. I highlighted that we are both small open economies with a large number of multinationals.

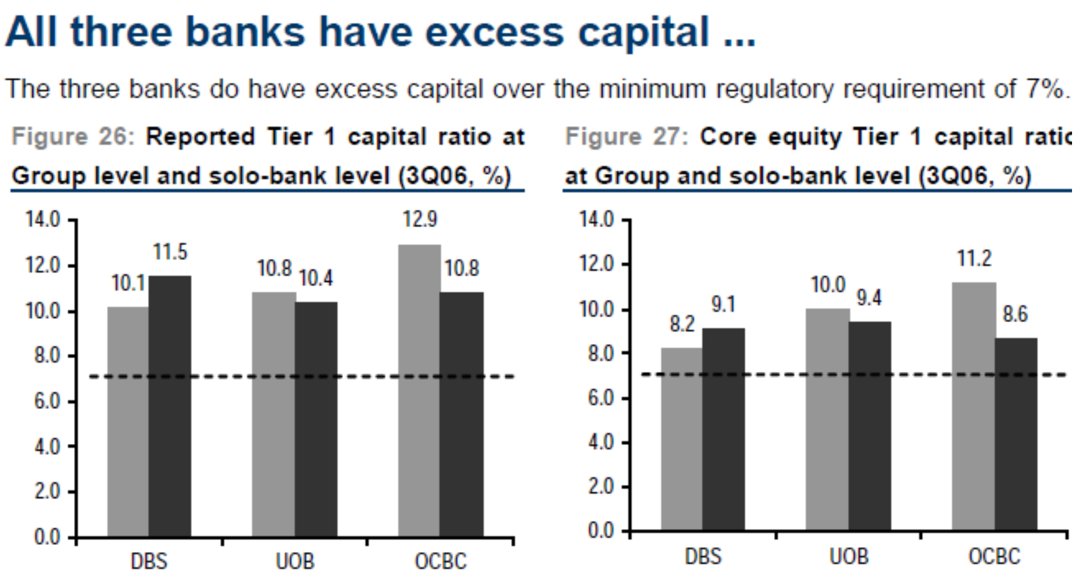
I also mentioned that Singaporean Banks were incredibly conservative. In fact I portrayed this conservatism as being a bit boring but I did not go any further to explain what I meant.

In this opinion piece I want to explore what I meant back then and go on to what I now think.

Back then I accused the three main Singaporean Banks: DBS (Development Bank of Singapore), UOB (United Overseas Bank) and OCBC (Overseas Chinese Banking Corporation) of being conservative primarily because of two things. First of all because of the amount of capital they had (capital adequacy) and second of all because of the amount of loans they had relative to their deposits (the loan / deposit ratio). I felt that they had more than enough capital and not enough loans to maximise the profits they might be able to make from their deposits.

The evidence I had to support this view is shown below:

First of all here is a section from a piece of research from 2006 that shows the amount of capital they had.



(I think that it is interesting to note that at the time it was felt that all the banks had "excess" capital. This was a different world, a world that had not experienced the sub-prime crisis!)

Second of all here is a table that shows the loan / deposit ratio at the time (with AIB added in to show the contrast with the Irish Banks)

	2006
Loan deposit ratio (x)	**%**
DBS	65.9
UOB	80.5
OCBC	79.0
AIB	160.0

When I wrote that opinion piece and when I highlighted the things that Ireland and Singapore had in common I have to admit that I thought the similarities would be far more important to our future economic performance. I thought that an educated workforce in an economy with large numbers of multinationals would be more important than the way the banks were run.
Unlike the Singaporean banks I thought that once the Irish banks stuck to the requirements set down by the regulators they would probably be ok from a capital perspective. I also thought that if deposits were not growing fast enough then there would not have been much harm using other funding. Boy was I wrong. I now know that Singapore was right, really right!

So why did Singaporean banks have more capital than most developed country banks and are there any lessons to be learned from this?
I hope I am right in my understanding of what was said to me on my visits to Singapore because I was led to believe that regional politics played a major part in bank conservatism. In fact I would go as far as saying that they gave the impression that they had a bit of a siege mentality. They felt that they were a country surrounded by neighbours that were a bit hostile and therefore they had to be prepared for the rainy day. In other words without directly naming countries they gave the impression that they were always worried that Indonesia and Malaysia could damage them and therefore it made sense to be prepared for that eventuality.
Unfortunately banks in the developed world worked on the assumption that the good times would keep on coming. When they did stress tests the worst case scenario was just too optimistic and Irish banks were major offenders.

We should therefore learn the lesson that we have to be prepared for the worst.
In other words I think that we need bankers that are a little bit paranoid about the worst case scenario. As Warren Buffett would say, we need to build in a margin of safety. We need to recognise our own failings and own limitations in forecasting the future and work on the assumption that we could be wrong and therefore we want to end up with banking institutions that survive a crisis.

It appears as if global banking regulators have partially learned this lesson. I say this because I know that new rules are being put in place but it should be worth considering that they are still not going as far as the Singaporeans. Here is an article from the Singaporean Business Times writing about these new international rules:

The Singapore banks already have common equity ratios far above the new minimum. DBS Group had a core Tier 1 ratio of 10.9 per cent at the end of June, after adjusting for a penalty capital charge imposed by the Monetary Authority of Singapore (MAS) last month for the bank's systems crash on July 5. Rival OCBC Bank's core Tier 1 ratio was 11.6 per cent, while United Overseas Bank's (UOB) was the highest, at 13 per cent.

Perhaps we should learn from Singapore and build up a bigger buffer because we never know when that rainy day will come.

In another opinion piece (opinion piece 24) I stated that I wanted bankers to keep it simple (the “KISS” principle). Well now I know that I want bankers to go a step further and stick to the “KISS-ASS” principle: Keep It Simple Stupid- And Supremely Safe”. Singapore is the best example I can think of that meets this and that is why I called this opinion piece Singapore KISS-ASS!

In conclusion I want to say that I will certainly try to make sure that any banks I own “KISS-ASS”!