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As a financial hub, Hong Kong maintains its edge over Singapore

SINGAPORE: Singapore, once so staid it banned bungee jumping, has cut taxes, opened its doors to casinos and hired fund managers to oversee billions of dollars of state funds to help attract international investment.

While the city-state has made progress toward becoming a more vibrant financial hub, it is still falling behind its perennial rival, Hong Kong. Assets held by fund managers tripled in Hong Kong to \$579 billion from 2000 to 2005, while Singapore's more than doubled to \$472 billion, according to regulators in the two cities. Hong Kong's stock market value has swelled to more than five times Singapore's.

The Singapore government's grip on the economy, which extends from the city's largest companies to its newspapers, stifles the entrepreneurialism that fuels Hong Kong's success, says one investor, Anil Thadani. While Singapore has loosened the reins, it's not moving fast enough to match Hong Kong, he says.

"Singapore has been unnecessarily restrictive," says Thadani, chairman of Singapore-based Symphony Capital Partners (Asia), which invests in Asian health care companies and luxury resorts. "People who are told from birth what to do and say aren't likely to be self-starting entrepreneurs. We need a generation to change the mind-set." With its government-driven economy, Singapore cannot rival Hong Kong in breeding private companies, says Andy Xie, a Hong Kong-based economist. Li Ka-shing, Asia's second richest man, built an empire ranging from telecommunications and property to retail after arriving in Hong Kong in 1940 as a refugee from China.

"A strong government and a strong private sector cannot coexist," says the Shanghai-born Xie, who left his previous job as Morgan Stanley's chief Asia economist in October after writing an e-mail that criticized Singapore. "In Singapore, it's all about the government taking initiatives."

The biggest threat to Hong Kong may be air pollution drifting south from factories in mainland China. Merrill Lynch cut its ratings on three Hong Kong developers in November because of concerns that educated workers would leave the city to escape the smog.

Hong Kong's gross domestic product was \$25,493 per person in 2005, and Singapore's was \$26,836. The figures ranked 23rd and 27th worldwide, according to the International Monetary Fund. The cities have also recorded comparable growth. Hong Kong's economy expanded an average of 5.3 percent annually from 2000 to 2005, compared with Singapore's 5.1 percent rate.

Singapore's expansion has been built on the foundation of government planning. Temasek Holdings, the state investment arm, owns controlling stakes in seven of Singapore's 10 largest companies, including Singapore Airlines and DBS Group Holdings, the biggest local bank.

Singapore says it wants a more diversified economy to reduce its dependence on makers of computer disk drives, mobile phones and electronic toys. The government in 2005 lifted a 40-year

ban on casinos, attracting \$6.6 billion of investment from Las Vegas Sands and Malaysia's Genting. It is also luring companies in industries such as digital media and biotechnology.

"The greatest challenge to Singapore today is to get our people to move away from the old model," Lee Kuan Yew, who founded modern Singapore and led the city-state for three decades, said in 2005. "Just being clean, green, efficient and cost-effective is not enough. You've also got to be innovative, creative, entrepreneurial."

Lee, 83, who governed from 1959 to 1990, transformed the city-state from a swampy fishing and trading town into a regional banking and technology hub and the world's biggest container port. He still holds the title of minister mentor, and his son, Lee Hsien Loong, is prime minister. After independence, Lee developed national industries such as electronics and chemical making, attracting companies including Royal Dutch Shell with cheap land and tax breaks.

"Instead of development that's entrepreneurial and bottom-up, Singapore encourages development that involves bigger investment," says Julian Jessop, chief international economist at Capital Economics in London. "A strong and interventionist government can actually be a good thing."

Singapore is the only government in Asia with AAA sovereign debt ratings — the highest — from Moody's Investors Service, Standard & Poor's and Fitch Ratings. That stability, along with government incentives, is helping the city-state attract companies such as Clariden Leu. Clariden, a private bank owned by Credit Suisse Group, chose Singapore for its first overseas branch in 2005.

"Why did we come to Singapore? Dependability, reliability, stability, predictability," says Roland Knecht, Clariden's Asia head. "These are things which are very, very important if you want to do private banking."

Jim Rogers, a New York investor who co-founded the Quantum hedge fund with George Soros in the 1970s, is weighing the pros and cons of Singapore as he prepares to move his family to Asia. Rogers, 64, says he plans to settle in Singapore or Hong Kong because he wants his 3-year-old daughter to grow up in a Chinese-speaking city and learn Mandarin, which will be the world's most important language in her lifetime. The child, Hilton Augusta, already speaks Mandarin with her full-time Chinese nanny.

"The problem for me with Hong Kong is the horrible pollution," he says. "As far as Singapore is concerned, the air is clean and everything works. It's a fantastic place if you are doing something they want you to do."

Rogers says Singapore suffers from state control. "There is no question that Hong Kong has a much more open and competitive market than Singapore," he says. "Singapore has been overprotecting its banks and citizens for decades."

Singapore has relaxed some laws as the city-state strives to soften its uptight image. The government in 2004 eased a 12-year ban on the sale of chewing gum, letting citizens buy sugarless

and tooth-whitening brands with a doctor's prescription. It ended prohibitions on bar-top dancing and bungee jumping the same year.

Other attempts to loosen up have been less successful. Crazy Horse Paris, which became the city's first topless revue in 2005, closed last month because of poor attendance. Eng Wah Organization, a local partner in the venture, blamed government restrictions on advertising.

Singapore has set its sights on becoming a center for wealth management, education and health care by exploiting its position as a link between China, India and the Middle East. About 2.5 billion people live within a seven-hour flight of the city-state.

Since the government identified biomedical science as a new growth engine in 2000, production of drugs and medical devices has quadrupled to 23 billion Singapore dollars, or \$15 billion. The government invested 500 million dollars in a seven-building science park, called Biopolis, which houses the country's top research institutes. That helped it attract drugmakers and biomedical companies, including Merck and Pfizer, according to the Economic Development Board, the state agency responsible for winning international investment.

Sixteen top U.S. and British researchers have also relocated to Singapore. They include Alan Colman, who helped create Dolly the cloned sheep; Sydney Brenner, who won the 2002 Nobel Prize for medicine; and the cancer geneticists Neal Copland and Nancy Jenkins.

Singapore this year was named one of five key locations for biotechnology research by Fierce Biotech, a U.S.-based industry journal. The four other locations are Scotland and the U.S. states of California, Florida and Washington.

The Government of Singapore Investment Corp., which manages the city's reserves, placed about 40 billion dollars with private fund managers from 1999 to 2004 to increase assets managed in Singapore.

Singapore is faced with the formidable challenge of Hong Kong's advantage as the gateway to China, the world's fastest growing major economy, and its 1.3 billion people.

"Hong Kong is China," says Mark Mobius, who oversees \$30 billion in emerging-market equities at Templeton Asset Management. "That is the market to be right now."

Hong Kong's stock-market capitalization of \$2.1 trillion dwarfs Singapore's \$393 billion. Chinese state companies such as Bank of China, which have chosen Hong Kong for international stock listings, are widening the gap.

"Singapore is not going to be the primary financial capital of the Pacific Rim," says Donald Straszheim, who is spearheading China investments for Roth Capital Partners. "That title is going to go to Hong Kong. Hong Kong already has the institutional capital that a world financial center requires."

About 19,500 new companies were formed in Singapore in 2005, a fraction of the 73,360 local companies incorporated in Hong Kong, government figures show. Singapore still relies on manufacturing for 28 percent of GDP. In Hong Kong, that share was less than 10 percent last year.

That leaves Singapore vulnerable to competition from lower-cost nations such as China and India, says Asia economist Xie. He predicts Singapore's economic growth could slow to as little as 2 percent in the next decade as electronics makers leave the city.

"I seriously doubt that Singapore will have much manufacturing in 10 years because it cannot compete on cost," Xie says.

Singapore has sought to reduce costs by cutting corporate tax rates by 6 percentage points since 2000 to 20 percent, narrowing the gap with Hong Kong's 17.5 percent rate. Singapore said in February it would drop the rate to 18 percent next year.

In Hong Kong, unfettered growth has its downside. Luxury residential rents are 54 percent higher than in Singapore, and prime office rents are more than double, says Pamela Tsui, a Hong Kong-based researcher at Knight Frank, a real estate consulting firm.

The worsening air pollution is prompting some expatriates to relocate to cleaner Singapore. Hong Kong last year dropped 12 places to 32nd in a survey of the most-attractive cities for expatriates because of poor air quality, personnel consultant ECA International said last April. Singapore topped the list, which ranked 257 cities based on factors such as climate, health care and availability of goods.

Air pollution in central Hong Kong was "very high" or "severe" on 41 days in 2006, up from 21 days in 2000, according to the city's Environmental Protection Department. At such levels the government advises people with asthma or cardiovascular disease stay indoors.

"The air quality in Hong Kong is now regularly so poor that the long-term competitiveness of this city-state is, in our minds, in some doubt," Merrill Lynch analyst Spencer White said Nov. 21 in a note to clients.

In 2001, the Economic Development Board introduced a co-financing plan for entrepreneurs, investing as much as one dollar for each dollar raised from investors to a limit of 300,000 dollars. The EDB created a pool of 110 million dollars to fund 161 companies.

Government incentives have attracted entrepreneurs such as Vikas Goel, the Indian founder of eSys Technologies, the world's largest distributor of hard disk drives for desktop computers. The company, which has \$1.7 billion in annual sales, received tax breaks for putting its headquarters in Singapore.

"We went shopping around the world, including Hong Kong, Switzerland and Dubai," says Goel, 36. "EDB offered us a lot incentives, and our overall costs are actually 40 percent less than those in China because logistics and financing costs offset labor costs."

HEALY CONSULTANTS

Pumping government cash into start-ups only perpetuates reliance on the state, says Symphony Capital's Thadani. "You can't buy or create entrepreneurialism," says Thadani, who was born in India. "You have to create an environment where entrepreneurs can fail and flourish automatically."

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