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REGULATORY COMPETITION AND COMPLEMENTARITY IN AN OFFSHORE FINANCIAL CENTRE: THE ASIA DOLLAR MARKET IN SINGAPORE AND HONG KONG 1968-86

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Foreword

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Abstract

Offshore financial centres have attracted considerable critical attention over the past few decades as havens for lightly taxed funds that circulate outside the regulatory oversight of major financial centres. This paper addresses the emergence of an offshore market in US dollars in Singapore from the late 1960s using a range of archival sources to identify the motivations of the host, participant banks and regional rivals. The development of the Asia Dollar market is particularly striking because Singapore was not the most likely venue for an Asian offshore financial centre. The main regional financial centre was Hong Kong, but the Hong Kong authorities made a deliberate choice *not* to host an offshore market in Hong Kong; a decision that was initially supported both by the state and by incumbent banks, although the banks later changed their view as the Singapore market grew. This case thus opens up discussion of the influence market actors exert over regulators when they are engaged in regulatory arbitrage as well as regulatory competition between states. Evidence is also presented about the efforts of the Bank for International Settlements to encourage greater transparency in offshore financial centres in the 1980s.

Increased international capital mobility in the 1960s and 1970s created opportunities to diversify the geographical location of financial activity by separating the location of customers and services to maximise profits and minimise costs. The most dramatic example was the emergence of an offshore market in US dollar deposits and assets in London in the early 1960s that launched a new era of international finance. This example of financial innovation has been widely researched because of its lasting effects on the globalisation of international capital markets.[1] Less historical attention has been paid to the subsequent rise of a range of offshore financial centres (OFCs) in the 1970s, which sought to attract financial activity from established regulated markets to island locations with relatively little financial infrastructure ex ante. This phenomenon is usually attributed to regulatory competition (lower tax rates, less transparency, weaker supervision, lower capital requirements) that prompted regulatory arbitrage by increasingly mobile international capital.[2] This interpretation has prompted investigations of offshore centres, and efforts by the OECD and others to curb their activity.[3]

Regulatory competition exists when there are multiple agencies with overlapping competencies; the action of one agency may then have externalities for another agency that prompt a reaction.[4] As we shall see in this case the externalities can be positive as well as negative – i.e. regulatory competition is not a zero-sum game. The classic regulatory competition theory was developed in the context of the state supply of public goods and this determined that such competition can result either in enhanced regulation or a deterioration in benefits to consumers.[5] Competition between financial regulators is most often viewed as a 'race to the bottom', prompting claims that offshore centres are destabilising and undesirable, whether by facilitating money laundering (weak supervision and disclosure), undermining financial stability (lower regulatory capital, weak supervision) or reducing the tax pool for established centres (lower tax burden).[6] Thus Rose and Spiegel confirmed empirically that 'OFCs are created to facilitate bad behaviour', although they may also improve competitiveness of financial services in neighbouring centres.[7]

While these results seem well established and intuitively compelling, we still know little about the emergence of OFCs; how important were different factors (tax, time zone, secrecy, agglomeration)? What distinctive historical or institutional factors influenced the design and development of different OFCs? How did OFCs compete with, supplement or promote activity in more established IFCs? Dorry, for example, emphasizes the role of influential individuals who took advantage of opportunities provided by the

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[1] C.R. Schenk, 'The Origins of the Eurodollar Market in London, 1955-1963', *Explorations in Economic History*, 35, pp. 221-238, April 1998, G. Burn, *The re-emergence of global finance*, Palgrave, 2006. CE Altamura, *European Banks and the rise of International Finance: the post-Bretton Woods era*, Routledge, 2017.

[2] R. Bryant, *International Financial Intermediation*, Brookings Institution, 1987. E. Helleiner*, States and the Re-emergence of Global Finance*, 1994. Ethan B. Kapstein*. Governing the Global Economy: International Finance and the State*. Cambridge: Harvard University Press, 1994.

[3] In 2000 the OECD began a campaign to increase transparency in OFCs. In 2009 the G20 launched a programme to tighten up regulation and supervision in offshore centres.

[4] F. Parisi, N. Schulz, J. Klick, 'Two dimensions of regulatory competition', *International Review of Law and Economics*, 26, 2006, pp. 56-66.

[5] The classic account is C. Tiebolt, 'A pure theory of local expenditures', *Journal of Political Economy*, 64(5), 1956, pp. 416-424. For a critical review see D. Geradin and J.A. McCahery, 'Regulatory co-opetition: transcending the regulatory competition debate' in J. Jordana and D. Levi-Faur eds, *The Politics of Regulation: institutions and regulatory reforms for the Age of Governance*, Edward Elgar, 2004, pp. 90-123

[6] Financial Stability Forum, Report of the Working Group on Offshore Centres, April 2000. In 2016 the so-called 'Panama Papers' leaked details of customers of a legal firm there.

[7] A.K. Rose and M.M. Spiegel, 'Offshore financial centres: parasites or symbionts?' *Economic Journal*, 117, 2007, pp. 1310-1335. P. 1311.

macroeconomic structure in the development of the OFC in Luxembourg.[8] Christensen and Hampton argue that the OFC in Jersey 'captured' the state because of the economic power of international finance in the territory.[9] Historical enquiry based on archive records from banks and regulators promises to help answer these questions.

This paper addresses the emergence of an offshore market in US dollars in Singapore from the late 1960s. At the time, Singapore hosted several local and international banks engaged in the commercial trade and finance for Southeast Asia, particularly the rubber and tin trade of the Malaysian peninsula. The territory was also reeling from the abrupt political separation of Malaysia and Singapore in August 1965 that left Singapore estranged from its primary hinterland.[10] The development of the offshore market was part of a general re-orientation of the Singapore economy from the mid-1960s that included attracting foreign multinational corporations and developing oil refining capacity to diversify the economy. The most comprehensive study on the market's origins to date is based on interviews in 1976 and published before important regulatory changes in 1978 and 1986.[11] By extending the period under scrutiny, using the archives of participants in the market as well as contemporary accounts and oral history, we find clear evidence of deliberate regulatory competition by the Singapore state to boost local financial activity and also evidence of regulatory arbitrage by banks for tax purposes. Moreover, unlike the Eurodollar case (but similar to other offshore centres) the Asia Dollar market was deliberately created and encouraged by the Singapore government as part of its efforts to create an international financial centre (IFC) in Singapore.[12] The planners sought to use past experiences from other markets in the promotion of the Asia Dollar market, but had distinctive goals to promote interactions with the domestic capital market. The Asia Dollar market thus documents how emerging states sought to take advantage of the rapid internationalisation of global capital markets. Research on Singapore is hampered by the paucity of relevant official archives, but evidence has been collected from international agencies such as the International Monetary Fund and Bank for International Settlements as well as from oral history records and bank archives. This is the first archive based study of the Asia-dollar market.

The development of the Asia Dollar market is particularly striking because, at the time Singapore was not the most likely venue for an Asian offshore financial centre. The main regional financial centre was Hong Kong, commonly viewed as a laissez-faire paradise for international banking and commerce.[13] But the Hong Kong authorities made a deliberate choice *not* to host an offshore market in Hong Kong; a decision that was initially supported both by the Financial Secretary and by incumbent banks, although the banks

[8] S. Dorry, 'The role of elites in the co-evolution of international financial markets and financial centres: the case of Luxembourg', *Competition and Change*, 20(1), 2016, pp. 21-36.

[9] J. Christensen and M.P. Hampton, 'A legislature for hire: the capture of the state in Jersey's offshore finance centre', in M. Hampton and J. Abbott eds., *Offshore Finance Centres and Tax Havens: the rise of global capital*, Purdue University Press, 1999, pp. 166-91.

[10] Schenk, C.R. (2013) The dissolution of a monetary union: the case of Malaysia and Singapore 1963-1974*. Journal of Imperial and Commonwealth History.* Lau, A., *A Moment of Anguish; Singapore in Malaysia and the Politics of Disengagement.* Singapore: Times Academic Press, 1998.

[11] A.K. Bhattacharya, *The Asian Dollar Market: international offshore financing*, Praeger, 1977. The market is described by contemporary writers, but not analysed historically. See, e.g.Lee, Sheng-Yi, Financial Institutions and Markets in Singapore' in M.T. Skully ed., *Financial Institutions and Markets in Southeast Asia*, Macmillan, 1984. Pp. 226-295 and S.Y. Lee and Y.C. Jao, *Financial Structures and Monetary Policies in Southeast Asia*, Macmillan, 1982.

[12] In 1965 Singapore separated from Malaysia and in 1967 the British announced the withdrawal of military forces from the territory (to be completed by 1971); Singapore had to turn to new sources of economic growth (including the IFC, manufacturing, oil refining).

[13] C.R. Schenk, *Hong Kong as an International Financial Centre: emergence and development 1945-65*, Routledge, 2001.

later changed their view as the Singapore market grew. This case thus opens up discussion of the influence market actors exert over regulators when they are engaged in regulatory arbitrage as well as regulatory competition between states. The Hong Kong state proved resistant to calls from bankers to improve their competitive position for almost 20 years.

This paper examines the first fifteen years of the Asia Dollar market from three dimensions. The first section reveals new evidence on the market's origins in Singapore. The second section examines why the market was located in Singapore and not in Hong Kong and shows that this decision was contested throughout the 1970s and into the 1980s. Finally, during the 1970s a range of new offshore centres emerged and the third section shows how Singapore and Hong Kong reacted to efforts to increase transparency in these new capital markets. We shall see that official regulators and supervisors in established financial markets were preoccupied by these concerns by the early 1980s, when they began to try to achieve what Genschel and Plumper have termed a 'cooperative turnaround' to enhance cross border prudential regulation.[14] Genschel and Plumper use the negotiation of standardised capital adequacy requirements among Bank for International Settlements member banks in the 1980s as an example of a successful 'race to the top', but they neglect the BIS' failed early efforts (described in this section) to bring off-shore centres into the fold.

Early Origins

According to Yap Siong Eu, then a regional consultant with Bank of America, the Asia dollar market in Singapore was launched on a small scale by Dutch banker J. D. (Dick) van Oenen in 1963. He began with 'just a few million dollars, mainly from existing depositors of Bank of America units in Southeast Asia and I dare say most of the depositors were overseas Chinese', recalled Eu.[15] Van Oenen joined the Bank of America in the early 1960s, having trained as a foreign exchange clerk in India and Ceylon/Sri Lanka. Joseph Greene, later manager at Bank of America, described him as 'a de Gaulle figure' due to his tall stature and dynamism.[16] He quickly established Bank of America's leadership in Singapore, successfully bidding for government deposits by offering an attractive interest rate. The Bank of America's close links to the government were reinforced once van Oenen made a significant windfall on the 1967 sterling devaluation by running a sterling overdraft in London both on the bank's own account and on behalf of the government. As recalled by Greene, the 'Singapore government and ourselves made a killing in one day. This was the initial rapport with government'.[17] As well as proving the Bank of America's credentials, the devaluation of sterling by 14.3% in November 1967 encouraged the region's bankers and traders to switch to dollars instead of sterling as their preferred foreign currency. Van Oenen approached Financial Secretary Goh Keng Swee to allow the Bank of America to collect dollar deposits from Southeast Asia (for example from wealthy individuals and firms in Jakarta and Taiwan) into Singapore to fund local and regional lending.[18]

[14] P. Genschel and T. Plumper, 'Regulatory competition and international cooperation', *Journal of European Public Policy*, 4(4), 1997, pp. 626-642, p. 627.

[15] Oral History, Yap Siong Eu. Accession number 00316/11. National Archives of Singapore.

[16] National Archives of Singapore, Oral History, Cassette 001466, Reel 2, interview with Joseph H. Greene of Bank of America 21 February 1994.

[17] National Archives of Singapore, Oral History, Cassette 001466, Reel 2, interview with Joseph H. Greene of Bank of America 21 February 1994.

[18] Oral History, Joseph Greene, Oral History, 21 February 1994, Reel 2. National Archives of Singapore. J.D. van Oenen, 'The Asian Dollar', The Banker, October 1970, p. 1096-7. By this time van Oenen was Vice President and Head of the International Financial Centre, Bank of America, London.

Another key player was the Dutch economist Albert Winsemius, chief economic advisor to the Singapore government, who guided Singapore's development plan from 1961 to 1983. Prime Minister Lee Kwan Yew recalled the idea for developing Singapore as an international financial centre coming from Winsemius, who sought out van Oenen for advice.[19] In later interviews, Winsemius described how van Oenen 'took a globe and showed me a gap in the financial markets of the world' to show how Singapore could provide 24-hour banking between the closure of San Francisco and the opening of London and Zurich and thereby establish itself as a key international financial centre.[20] Whether originating with van Oenen or Winsemius, the motivations for the market were to channel regional savings into local investment and to diversify the Singapore economy to include an international financial centre.

From 1 October 1968 the Singapore government allowed banks to apply to open special departments called 'Asian Currency Units' to accept non-resident currency deposits (initially up to $50 million). This became known as the Asia Dollar Market.[21] The goal was to isolate the offshore market from the domestic market, thereby attracting regional funds inward rather than channelling domestic savings outward. In an interview with *The Banker* in 1970, Hon Sui Sen (Goh's successor as Financial Secretary) explained the government's support of the Asia Dollar market as partly ideological and partly to promote regional development:

> 'I believe that money which suffers from ill treatment should be allowed a safe refuge just as persecuted religious minorities deserve a sanctuary. Hitherto, refuge has been provided in countries such as Switzerland and to this extent the capital is lost for economic development in the region. When it remains in Singapore, it will be available when suitable investment opportunities arise'.[22]

It is clear from this evidence that the Singapore authorities planned both a distinctive off-shore market to attract international banks as part of the diversification of the economy into financial services, but also that they sought to channel regional savings into regional (or even local) investment by allowing Singapore residents to access the market. They thus expected positive spill-over effects to domestic development from attracting international banks to the OFC.

The market became one of the main focuses of the new Monetary Authority of Singapore (MAS) established in 1971 as they gradually lifted the barriers for resident individuals and companies to take part.[23] From 1972, the MAS removed the 20% reserve requirement on liabilities, along with stamp duty on certificates of deposit, and the income tax on interest receipts from offshore loans was reduced from 40% to 10%. Deposits from wealthy individuals were encouraged by the low minimum deposit of US$5000. The authorities were very ambitious for the market, encouraging the development of bond

[19] Lee Kwan Yew, *From Third World to First: the Singapore Story 1956-2000*, Harper Collins, 2000. p. 89.

[20] *UNDP and the making of Singapore's Public Service; lessons from Albert Winsemius*, United Nations Development Programme Global Centre for Public Service Excellence, 2015. P. 24-5

[21] The US followed this pattern with International Banking Facilities for offshore deposits and loans within US banks from December 1981.

[22] Interview with Hon Sui Sen, *The Banker*, October 1970, pp. 1078-83, p. 1078. Hon was Minister of Finance from August 1970 until October 1983.

[23] Resident companies were able to get approval from the Exchange Control to borrow from the market from 1972 and it was also possible to access the market for export financing. Singapore 1971 Article VIII Consultation Briefing Paper, 24 October 1972. IMF Archives [hereafter IMFA] Asian Department Immediate Office, Country Files Box 107.

markets and term loans by issuing bonds in 1972 through the Singapore Development Bank and the government.[24]

From April 1973, the MAS created a new category of 'offshore banks' that could lend funds attracted from overseas to non-residents or to local industry when explicitly approved by the MAS. Seven banks were awarded special off-shore licenses; Barclays Bank International, Bankers' Trust, Continental Illinois, First National Bank in Dallas, Marine Midland Bank, Nat West and Toronto Dominion. There was clearly a demand to take part in the new market, and not all applicants were successful. One example is Credit Lyonnais. Credit Lyonnais had a joint representative office in Singapore with Banco di Roma and Commerzbank and in March 1973 they submitted a request to the MAS on 9 March 1973 to be considered for a license either on their own or on behalf of a subsidiary the three banks.[25] Commerzbank subsequently approached the MAS separately, thereby 'creating a bad impression at the Monetary Authority' that there was a lack of coordination among the partners and permission was not granted.[26] Credit Lyonnais continued to seek a license, but soon discovered there were significant costs to taking part in this form of regulatory arbitrage.[27]

In September 1973 Henri Picq, of Credit Lyonnais' Singapore office interviewed bankers from four of the first cohort of offshore banks to get an idea of the opportunities and constraints. He found unanimous optimism about the prospects for their new offshore business, but pessimism about the prospects for lending in Singapore dollars and most did not expect to cover their costs.[28] Payne, the Director of Barclay's Bank International in Singapore, for example remarked that the start of their offshore operations exceeded their hopes due to the bank's international reputation, the quality of their exchange dealer and the embeddedness of Barclays Bank in Hong Kong and Australia. Most of the banks viewed their ACUs at this point as placing them advantageously for the future growth of demand for funds in Asia. The MAS allocated each bank a ceiling of up to S$20 million for local loans (with a minimum S$1 million for each individual loan and a minimum term of 2 years), but even more restricting was the shortage of inter-bank funds on appropriate terms and maturities. Claude Gizard at Credit Lyonnais' head office in Paris, thought this ceiling was 'paralysing', but Credit Lyonnais still renewed its efforts to gain a license for the three partners on 2 October 1973.[29] This time they were unsuccessful because the MAS considered that there was no pre-established subsidiary of the three banks to take the license as a single institution despite the joint representative office.[30] What is interesting in this archival evidence is

[24] Article VIII Consultation Briefing Paper, 24 October 1972. IMFA Asian Department Immediate Office, Country Files Box 107.

[25] Letter from Jean Saint-Geours, Director General of Credit Lyonnais to Michael Wong Pakshong, Managing Directory MAS, 9 March 1973. Credit Lyonnais Archives [hereafter CL] 332AH167.

[26] Letter from Commerzbank to Hon Sui Sen, Minister of Finance, 30 March 1973. Memo Affaires internationals, Cooperation – Reunion des Directions Generales due 9 mai 1973. CL 332AH167.

[27] Letter and Report from Credit Lyonnais Singapore, 1 October 1983 for M Deflassieux, Director of Aone Asie Pacifique. CL332AH167.

[28] Letter H. Picq, Joint Representative Office for Banco di Roma, Commerzbank and Credit Lyonnais, Singapore, 1 October 1973. CL 332AH167. The banks were Toronto Dominion, Barclay's Bank International, First National Bank in Dallas, Marine Midland. TD had no ceiling, Continental Illinois had a ceiling of S$10 million.

[29] Letter signed by Banco di Roma, Commerzbank and Credit Lyonnais to Monetary Authority of Singapore, 2 October 1973. Claude Gizard to Picq, 10 October 1973. CL 332AH167.

[30] Letter from Tew Chong Kew, Manager, Banking and Financial Institutions Department, Monetary Authority of Singapore to J Deflassieux, Manager International Affairs, Credit Lyonnais, 21 November 1973. CL332AH167. Credit Lyonnais offered to apply on its own but this was not accepted. Banco di Roma was the most reluctant to set up a special subsidiary with the required minimum capital of S$6 million.

the emphasis banks placed on local lending opportunities by the local offices as well as the offshore business per se, which could be booked in Hong Kong.

Figure 1 (log scale) shows the exponential growth of deposits in the early years, beginning to level off at the time of the international banking scandals of mid-1974, when the growth of the Eurodollar market also stumbled.[31] By March 1978 there were 79 ACUs operated by local commercial banks, 54 by foreign commercial banks, 18 by merchant banks and one by a foreign owned investment company.[32] In June 1978 all exchange controls were eliminated and the market started another phase of accelerated growth. Still, by 1983 the Asia Dollar market was only 5.1% percent of the global Eurodollar market, and never exceeded 7% in the 1980s.[33]

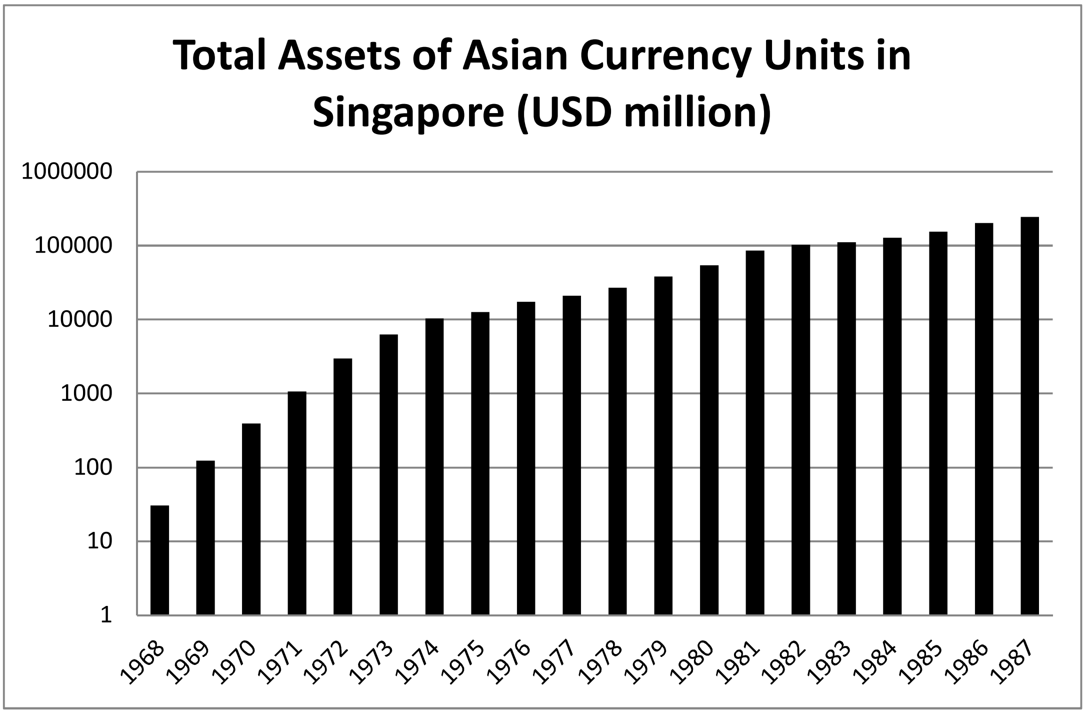

Figure 1: Source: Yearbook of Statistics Singapore, Chief Statistician, Department of Statistics, Singapore

While initially established to attract dollar deposits from Asia, which were then channelled to Euro-markets in Europe, from the early 1970s the flow reversed and the source of deposits shifted to Europe and the Middle East and assets were increasingly local. Initial deposits were mainly from residents of sterling area countries and the funds were then channelled into the Eurodollar market so the ACUs were mainly short term interbank funds, but by 1972 about 85% of funds with ACUS were used by bank and nonbank customers in Asia and Australia, compared with 43% in early 1970. In early 1971 lending rates fell relative to local rates in East Asia and the market became a more attractive source of funds for

[31] C.R. Schenk, 'Summer in the City: banking scandals of 1974 and the development of international banking supervision', *English Historical Review,* 2014, pp. 1129-1156.
[32] Memo 11 April 1974 for Technical Assistance Mission to Singapore IMFA Asian Department, Immediate Office, Country Files, Box 106, Singapore Correspondence 1971-87.
[33] Based on data of cross-country foreign currency liabilities reported by banks to the Bank for International Settlements. Stats.bis.org. Data is reported separately for Singapore only from December 1983.

regional borrowers.[34] But the share of inter-bank assets remained about 70% of total through the 1980s as is shown in Figure 2.

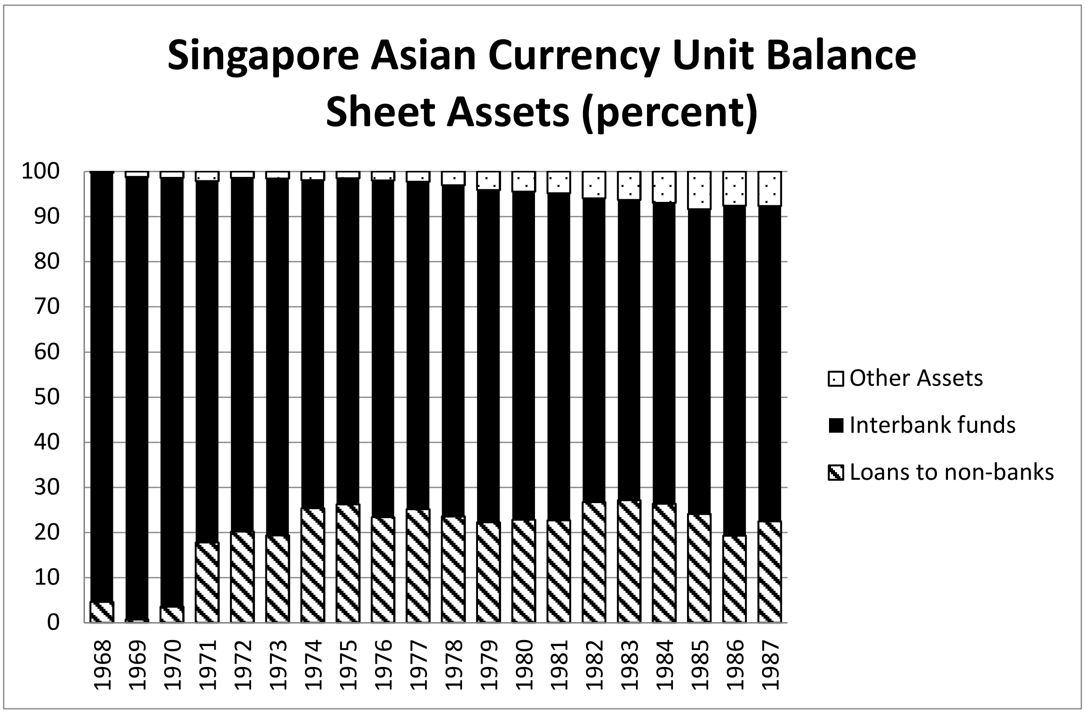

Figure 2: Yearbook of Statistics Singapore, Chief Statistician, Department of Statistics, Singapore

In common with other off-shore markets, greater global dollar liquidity from the accumulation of petrodollars in the Middle East after the first oil crisis in October 1973 was a potential boost to the Asia Dollar market. Foreign Minister S. Rajaratnam toured the Middle East in the Spring of 1974 to rebuild links with oil producing states there and to assess the supply and price situation of crude oil. By this point oil refining accounted for about a quarter of total Singapore's manufacturing output. The IMF noted that Rajaratnam 'also sounded the Arab States on possibilities of siphoning their fast-growing revenues into Singapore's burgeoning Asian dollar market (over US$6 billion in 1973) and into the local petrochemical industry'.[35] By the end of 1974 the market had reached $10.5 billion, but then began to slow from mid-1975 due to political uncertainties related to the US defeat in Vietnam, the global recession and the Hertsatt bank failure in mid-1974, so that by the end of 1975 the market had reached US$12.b billion, mainly through growth in the number of newly licensed banks building their asset portfolios.[36] Despite Rajaratnam's efforts, in mid-1975, the IMF reported that about half of liabilities and 80% of claims in the market were related to Asian business and customers. The principal net borrowers were in Hong Kong, Japan and Southeast Asian countries and most of the flow of foreign funds was reported to come from the Eurocurrency market, with very little coming directly from the Middle East oil surplus countries.[37] By

[34] R. F. Emery, 'The Asian Dollar Market', International Finance Discussion Papers, Federal Reserve Bank, 21 November 1975. P. 18.

[35] Preliminary Report: 1974 Article VIII Consultation - Singapore from A.G. Chandavarkar IMF to Managing Director, 24 April 1974. The mission visited Singapore 9-21 April 1974. IMFA Central Files, Country Files, Singapore Box 2.

[36] Report of mission to Singapore, 5 April 1976. IMFA Asian Department, Immediate Office, Country Files, Box 106, Singapore Correspondence 1971-87.

[37] IMF Staff Report 1975 Article VIII Consultation, 7 July 1975. IMFA Asian Department, Immediate Office, Country Files, Box 107, Singapore Missions 1975-83. The mission took place in the second half of May 1975.

1982, however, the IMF reported that the main non-bank borrowers continued to be Singapore's neighbouring countries and that the major net suppliers of funds were the UK, USA and countries in the Middle East and Caribbean.[38]

The market in loans and deposits soon spread to other products. At the end of 1976, US dollar denominated certificates of deposit began to be issued in Singapore. They were considered a close substitute for US$ denominated time deposits, although they were transferable through a secondary market.[39] By 1977 it was estimated that 75% of the funds were channelled into loans within Asia (Hong Kong, Japan and other Southeast Asian countries) but most of this was on short term. The bond market began in 1971 was slower to develop with only 4 issues by 1976, but changes to exchange control and tax gave it a boost and a further nine bonds were issued in 1976 (US$266m), 13 in 1977 ($368m) and 12 in 1978 (US$454m).[40] But this remained a small market, described by John F. Salmon, general manager of Bankers Trust International (Asia) as 'a non-starter' in 1981.[41]

In sum, the market grew quickly once established, and the opportunities to take part were taken up with alacrity by foreign banks, primarily from the USA. The Singapore government's strategy of creating an OFC through competitive regulation seemed to be a success in terms of the growth in nominal assets, although the effort to diversify the market was less successful.

Hong Kong and the Asia Dollar Market

Although Hong Kong was the leading Asian financial centre in the 1960s and 1970s, the authorities there did not follow Singapore down the route of encouraging offshore banking. Interest earned by depositors in Hong Kong was taxable at 15% no matter where the depositor was resident and the tax was with-held by the banks. But unlike Singapore, banks' profits arising from activity carried on outside Hong Kong was not subject to tax. The tax situation between Singapore was thus symmetrical: Hong Kong taxed depositors (15%) but not off-shore bank profits; Singapore taxed bank profits (40% until 1972, then 10%) but not offshore depositors. The result was a flow of offshore deposits into Singapore and a rise in offshore banking business undertaken by Hong Kong banks. Table 1 sets out the main changes in Singapore and Hong Kong regulations relevant to offshore financial activity from 1969-1986 culminating in the opening of an offshore market in Tokyo.

[38] Staff Report for the 1983 Article IV Consultation, draft, October 1983. IMFA Asian Department, Immediate Office, Country Files, Box 107, Singapore Missions 1975-83

[39] Memo by I. Otanlind, IMF, 4 January 1978 IMFA Asian Department, Immediate Office, Country Files, Box 106, Singapore Correspondence 1971-87.

[40] Paper on Singapore, 24 October 1979. IMFA Asian Department, Immediate Office, Country Files, Box 106, Singapore Correspondence 1971-87.

[41] Pamela Hollie, 'Singapore: banker to region', *The New York Times*, 23 January 1981.

Table 1: Key Tax and Exchange Control Changes in Singapore and Hong Kong

	Singapore	Hong Kong
1969	Elimination of withholding tax on interest earned on deposits	15% withholding tax on interest earned by residents and non-residents
	Profits on offshore and on-shore business 40%	No profits tax paid by banks on offshore business
June 1972	Elimination of preferential exchange control among sterling area countries	
1972	Elimination of 20% liquidity requirement on ACU deposits	
1973	Income tax on interest earnings from offshore loans reduced from 40% to 10%	
21 June 1973	Singapore dollar floated	
1973-March 1974	Special reserve requirements on domestic bank net foreign currency interbank liabilities	
November 1977	Floating interest rate USD negotiable certificates of deposit introduced	
1978 (or Feb. 1977)	Tax on all offshore income by ACUs reduced to 10%	Introduction of tax on banks' interest earned overseas (17%)
June 1978	Exchange control lifted – all residents can participate in ACUs without limits	
1982		Removal of withholding tax on foreign currency deposits; reduction of tax on HK$ deposits to 10%
1983		Removal of withholding tax on Hong Kong dollar deposits
1986		Introduction of tax on banks' profits earned overseas
	Japan opens offshore banking market (December 1986)	

Based on interviews, Battarchaya asserted that in 1968 'Hong Kong was the first choice' among banking circles to host the market but that the Hong Kong government resisted cutting withholding tax on deposits and was concerned that an Asia Dollar market would divert local resources to offshore business and (conversely) might put upward pressure on the Hong Kong dollar.[42] The Financial Secretary, J.J. Cowperthwaite explained his position in a somewhat frosty interview with *The Banker* magazine in July 1970.[43] He recalled that, unlike the case for Singapore, 'in our discussions with interested Hongkong [sic] banks, it became very clear that they were not concerned to attract dollars to a pool in Hongkong but dollars from Hongkong to a non-resident pool'.[44] An offshore market would therefore merely drain liquidity from the domestic market. Cowperthwaite declared that Hong Kong had 'no ambitions to be a tax haven nor to attract the kind of money that flows into tax havens. We are not fond of gimmicks'.[45] Tax on interest income was already low (at 15%), and in any case 'the use of a substantial proportion of the Asian dollar deposits in Singapore are in practice managed by the Hong Kong offices of the banks concerned'.[46] Depositors avoided paying tax on interest by locating their funds in Singapore, and banks avoided paying tax on profits from overseas lending by channelling these offshore funds through Hong Kong banks.

But the rivalry between Singapore and Hong Kong was more contested than this traditional account of cosy complementarity would suggest. The rapid growth of the Asia Dollar market in Singapore soon led to calls for Hong Kong to be more directly involved, and in his February 1973 budget speech Cowperthwaite's successor, Sir Philip Haddon Cave publicly offered to reassess the decision to put Hong Kong at a competitive disadvantage to Singapore and to investigate ways to 'encourage an international currency market in Hong Kong'.[47] He suggested that this might follow the Singapore model and take the form of special departments of Hong Kong banks that would issue Hong Kong Certificates of Deposit and engage in foreign currency borrowing for lending off-shore in ways similar to Singapore. Importantly, while there could be an exemption of tax on interest earned on offshore loans, the banks' profits from such trading would be subject to local tax.

In June 1973, as liquidity in the Hong Kong market fell due to a drain of deposits and capital overseas, the Exchange Banks' Association established a small sub-committee to explore the effects of the withholding tax, off-shore borrowings in Hong Kong, and the effect of short-term borrowing by non-bank financial companies and merchant banks.[48] It seemed that there was a danger that the relative tax advantages in Singapore were attracting funds out of Hong Kong. A joint investigation by banking commissioners and exchange controllers (Ockendon, Paterson and Giddy) however, recommended that the withholding tax should not be removed and the Financial Secretary's 'offer' was rescinded in Haddon Cave's 1974 budget speech. There were several factors that led to this outcome.

First, the investigation identified fears that eliminating tax on *all* foreign currency deposits would generate a massive switch out of Hong Kong dollars and into US$ in Hong Kong, with destabilising local monetary effects. Ockendon, Paterson and Giddy tested the possibility of following the Singapore model of special departments in banks that would be able to accept foreign currency deposits from non-residents where interest earned by depositors would not be taxed. But both the banks and the Inland Revenue believed that maintaining a distinction between resident and non-resident deposits was too difficult without the introduction of new exchange controls. Unlike Singapore, in Hong Kong there was no ex ante distinction made in exchange control between resident and non-resident depositors; a principle that had been hard fought in the early post-war years to preserve Hong Kong's traditional

[42] Battarchaya, p. 4-5.
[43] Interview with Cowperthwaite in *The Banker*, 120, July 1970, pp. 734-745.
[44] Interview with Cowperthwaite in *The Banker*, 120, July 1970, p. 744.
[45] Interview with Cowperthwaite in *The Banker*, 120, July 1970, pp. p. 739.
[46] Interview with Cowperthwaite in *The Banker*, 120, July 1970, p. 745.
[47] Haddon Cave's Budget Speech 1973.
[48] Memo from J.L. Boyer to M.G.R. Sandberg, 4 June 1973. HSBC Group Archives [hereafter HSBC] GHO 422.

entrepot role.[49] In the end, the proposals were abandoned since banks and other financial institutions were engaged in international currency markets in ways that already avoided the withholding tax, as suggested by Cowperthwaite in 1970. Thus, ironically, the free market for foreign exchange that operated in Hong Kong in contravention of the sterling area rules from the 1940s made it difficult to host an offshore dollar market. In Singapore, by contrast, the market was launched when sterling area controls distinguished between residents and non-residents of the sterling area. Even when the sterling area controls were lifted in June 1972, the apparatus for distinguishing non-resident accounts persisted in Singapore.

Bringing the profits from the Asia Dollar market on-shore in Hong Kong and therefore liable to Hong Kong profits tax was deemed an unattractive price to pay for eliminating tax on interest earnings from overseas deposits. The 1973 report concluded 'the establishment of an "official" international currencies market would not provide an extra facility but a simpler method of providing an existing facility'.[50] The Inland Revenue Ordinance specifically exempted banks from paying withholding tax on their interest earnings – instead this income was taxed as part of profits.[51] But at the same time (unlike many jurisdictions) Hong Kong did not charge tax on profits and earnings arising from activity *outside* Hong Kong, so Hong Kong financial institutions could profit tax-free from operations conducted in Singapore. This 'territorial source criterion' was a zealously guarded facet of Hong Kong's tax system, and suggestions of further narrowing the tax base were strongly resisted both by banks and by the Inland Revenue.[52]

Five years later, however, in 1978 the loophole was closed when the profits banks earned from off-shore transactions became subject to Hong Kong tax. Littlewood describes how this outcome was the by-product of a more substantial review of the entire tax system in Hong Kong begun in mid-1976.[53] The Review Committee confirmed the status quo that only profits originating in Hong Kong should be taxed, partly because business had threatened to 'migrate to other centres', but they also recommended that offshore earnings that were not generated by a corporate branch overseas should be taxed in Hong Kong.[54] The government rejected this proposal for most businesses but added a special exception for banks. Thus, from 1978 tax was charged on bank profits derived from business outside Hong Kong, unless it was attributable to an overseas branch.

This disrupted the symmetry of the tax burden between Singapore and Hong Kong and prompted the reconsideration of the withholding tax on interest earnings on local foreign currency deposits. In 1979 the reassessment was taken up by the government's Advisory Committee on Diversification of the Hong Kong economy, which signals that it was part of the reconsideration of the direction of Hong Kong's economic prospects as manufacturing wages rose. The banks and the Advisory Committee reported

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49 C.R. Schenk, 'Closing the Hong Kong Gap: Hong Kong and the free dollar market in the 1950s', *Economic History Review*, XLVII(2), pp. 335-53, 1994.

50 Quoted in Commissioner of Inland Revenue V.A. Ladd to Financial Secretary Haddon Cave, 18 December 1980. Citing Haddon-Cave's 1974 Budget Speech. HSBC GHO 421 Confidential Correspondence with Financial Secretary etc. In 1978-79 withholding tax on interest arising in or derived from Hong Kong amounted to only HK$118m or 1% of tax revenue, so fiscal concerns were not paramount.

51 In 1979-80 the yield from profits tax on interest from financial institutions in Hong Kong was about HK$500m. V.A. Ladd memorandum to Financial Secretary, 11 September 1980. HSBC GHO 421 Confidential Correspondence with Financial Secretary etc

52 V.A. Ladd memorandum to Financial Secretary, 11 September 1980. HSBC GHO 421 Confidential Correspondence with Financial Secretary etc.

53 M. Littlewood, *Taxation without Representation: the history of Hong Kong's troublingly successful tax system*, Hong Kong University Press, 2010, pp. 186-99.

54 Littlewood, p. 196.

concern about the possibility that Hong Kong savings were bleeding out of the local market to Singapore to take advantage of the lower taxes on non-resident deposits and that the withholding tax inhibited the inflow of capital to Hong Kong.[55] In 1980, the outgoing Financial Secretary, Sir Philip Haddon Cave began to reconsider the taxation of foreign currency borrowing by banks, but he met with stiff resistance from Victor Ladd, the Commissioner for Inland Revenue. Ladd expressed his fear that tax revenue would be lost, particularly if the 'tax-free' off-shore deposits could not be effectively isolated from the domestic market.[56] Ladd also noted that the growth of Hong Kong as an international financial centre 'at least matches Singapore' so he did not find a compelling reason to violate the territoriality source criterion of the tax system. But how did international banks view the relative attractions of Hong Kong and Singapore?

Hong Kong banks continued to seek relief from withholding tax and in 1981 the Committee of the Hong Kong Association of Banks established a working party to lobby the government. Chartered Banks' Assistant General Manager, William C. Brown advised the new Financial Secretary John Bremridge that most international banks believed that the withholding tax on non-resident deposits did, in fact, inhibit the financial development of Hong Kong vis-à-vis Singapore.[57] He went on to warn Bremridge that

> 'psychology is important to any market and if the international banking community <u>believes</u> that the difference in treatment in regard to foreign currency deposits, as between Hong Kong and Singapore, is preventing the former from developing to its full potential, then irrespective as to whether such belief is ill-founded or well-founded development will in fact be retarded by these banks' strategies in the region.[58]

But there is little evidence to suggest that the Singapore Asia Dollar market undermined Hong Kong's reputation. In 1980 the Bank of Scotland, which had opened a branch office in July 1979, remarked that 'Hong Kong is undoubtedly the Financial Centre in South East Asia and our decision to establish a presence there was the correct one.'[59] 'Interest and fee income from eurocurrency [syndicated] lending is and will continue to be by far the largest source of revenue' for the Hong Kong branch. In assessing where to base their first East Asian office, they noted that Singapore was complementary to Hong Kong, as a host for officially recording business for tax purposes outside Hong Kong; 'Loans written in Singapore may be officially recorded on the books in Hong Kong by means of a "Memorandum A/C". As the loans are not recorded in Singapore, and the business for tax purposes is outside Hong Kong, firms can avoid both Hong Kong and Singapore direct taxation'.[60] It didn't seem that even a small bank like Bank of Scotland was subject to erroneous sentiment about the relative advantages of Singapore.

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[55] Report of the Advisory Committee on Diversification quoted in V.A. Ladd memorandum to Financial Secretary, 11 September 1980. HSBC GHO 421 Confidential Correspondence with Financial Secretary etc.

[56] Commissioner of Inland Revenue V.A. Ladd to Financial Secretary Haddon Cave, 18 December 1980. Citing Haddon-Cave's 1974 Budget Speech. HSBC GHO 421 Confidential Correspondence with Financial Secretary etc.

[57] W.C.L. Brown, Chartered Bank, to John Bremridge, Financial Secretary, 20 July 1981. HSBC GHO 421 Confidential Correspondence with Financial Secretary etc.

[58] W.C.L. Brown, Chartered Bank, to John Bremridge, Financial Secretary, 20 July 1981. Emphasis in the original. HSBC GHO 421 Confidential Correspondence with Financial Secretary etc.

[59] Board Report, Hong Kong Branch, 12 August 1980. BoSA GB1830 BOS2-6-7-6. Within a year, the Hong Kong branch had US$97.17 million in loans of which 85% was outside Hong Kong (16% Malaysia, 13.45% South Korea, 10% Japan).

[60] Board Paper, 'Opportunity Areas', 10 January 1978 GB1830 BOS2-6-6-7. Treasurer's Papers, Banque Worms in Hong Kong.

Nevertheless, the HSBC management agreed with the Working Party's assessment that the tax regime was an obstacle to Hong Kong's development, even though Hong Kong banks were able to book substantial deposits off-shore. Thus, 'Hong Kong would appear to be exceptional in that the taxation system acts to discourage people from keeping a substantial portion of their savings within the country.' But the likelihood that tax relief would lead to a repatriation of these deposits depended also on the requirement that these deposits would be subject to the 25% prudential liquidity ratio.[61] Addressing the Hong Kong Association of Banks annual dinner in August 1981 Financial Secretary Bremridge rehearsed the obstacles to changing the policy, including shrinking the tax base and a danger of switching from Hong Kong dollar deposits to foreign currency deposits, which 'could lead to further pressure on the exchange value of the Hong Kong dollar; and in turn might eventually lead towards demonetisation of the local unit'.[62] Against these disadvantages the benefits in terms of repatriated deposits or development of the financial centre in Hong Kong were 'difficult to quantify', but he concluded that 'I promise you that I am genuinely open-minded with a predilection for freedom'.[63]

At the time of this speech, credit expansion in Hong Kong was rising quickly and Mike Sandberg of HSBC wrote to Bremridge suggesting that the government should impose new controls to contain the pressure. He argued that net overseas liabilities of banks in Hong Kong should be treated in the same way as other deposits in terms of liquidity requirements, particularly since banks with large overseas deposits were increasing their local lending faster than local banks.[64] Bremridge rejected this suggestion as 'discriminatory' against foreign banks and potentially damaging to 'the offshore business done out of Hong Kong by these banks, because of the difficulty of defining as tightly as would be necessary the assets and liabilities that related solely to on-shore business. It follows that the impact on Hong Kong's growth as a financial centre may be difficult to forecast'. Bremridge clearly put 'freedom' before control, despite the frustration of HSBC.[65] The debate over the offshore market was becoming mired in the controversy over bank liquidity and the management of the domestic money supply in Hong Kong.

In his budget speech for 1982 Bremridge removed tax on interest earned on foreign currency deposits and reduced the tax on Hong Kong dollar deposits from 15% to 10% to try to minimise customers switching out of local currency. The review of the tax on interest begun by Haddon Cave in 1981 had determined that there was no case for removing it, and that there was a risk that funds could be switched from Hong Kong dollars to foreign currency if there were differential tax rates on deposits. Nevertheless, the Hong Kong Association of Banks successfully lobbied for the removal of tax on interest of foreign currency deposits to enhance Hong Kong's position as an international financial centre.[66] In early June 1982, IMF staff visited Singapore and reported that 'the Singapore authorities did not appear overly concerned with the recent decision of the Hong Kong Government to remove the withholding tax on interest income earned by non-residents on offshore deposit. While this action did remove one

[61] Letter from HSBC to John Bremridge, 30 July 1981. Signed with initials UT? HSBC GHO 421 Confidential Correspondence with Financial Secretary etc.

[62] Speech by John Bremridge at the dinner of the Hong Kong Association of Banks, 11 August 1981. HSBC GHO 421 Confidential Correspondence with Financial Secretary etc.

[63] Speech by John Bremridge at the dinner of the Hong Kong Association of Banks, 11 August 1981. HSBC GHO 421 Confidential Correspondence with Financial Secretary etc.

[64] Letter from John Bremridge to Michael G. R. Sandberg, HSBC, 3 September 1981. Unsigned internal HSBC note rebutting this letter, 5 September 1981. HSBC GHO 421 Confidential Correspondence with Financial Secretary etc.

[65] For the shift in the government's attitude to the market see Catherine. R. Schenk, 'Negotiating Positive Non-Interventionism: Regulating Hong Kong's Finance Companies 1976-86', *China Quarterly*, 2017.

[66] Budget Speech by Bremridge, Hong Kong Legislative Council, 24 February 1982, p. 445. Bremridge referred to 'the clamourings of the interest tax abolitionist lobby', provoking laughter in the Council.

advantage of Singapore as a regional offshore foreign currency funding center, they doubted that there would be a significant movement of deposits to Hong Kong'.[67]

The year 1982 proved particularly unstable in Hong Kong, with a negative shock to the Hong Kong dollar in October partly related to negotiations for the return of sovereignty to China. Although foreign currency deposits increased by HK$69 billion while Hong Kong dollar deposits declined, Bremridge chose not to change the tax differential in his budget speech in February 1983, partly because this would reduce government revenue by about HK$620m.[68] In July 1983 Tony Latter, Hong Kong's Secretary for Monetary Affairs, was struggling with the mechanisms to exert monetary control in Hong Kong as inflation advanced and exchange rate stability deteriorated. In a paper for Bremridge, entitled 'A Personal View' he noted that while the use of the Hong Kong dollar had declined over the short term 'much of its apparent loss of popularity would probably be reversed if interest tax were removed'.[69] He thus implicitly agreed with the claim that the Hong Kong dollar suffered from competition from the US dollar market Singapore. The year 1983 proved even more difficult, including bank failures, currency and financial crises.

Despite these domestic disturbances, the international financial centre was remarkably robust. At the beginning of November 1983 Joh H. Heires of the Federal Reserve Bank of New York met with Frederick E. Schwartz, Senior Vice President of Bankers Trust, who noted that 'the Hong Kong situation has calmed down' and the restoration of the currency peg to the dollar was 'regarded positively'. Schwartz noted that 'as a financial centre, Hong Kong remains more attractive than Singapore as it has better transportation and telecommunication with the rest of the world. Bankers Trust in the last two years studied both centres to see which would have the most advantages and it chose Hong Kong'.[70] Vice Presidents of the Chemical Bank were more supportive of the advantages that Singapore gleaned from hosting the Asia Dollar market, particularly for commodities and futures trading although they had no evidence that funds had been flowing there during the Autumn market disturbances.[71] The Bank of New York Vice President remarked that 'to the extent there has been a decline in Hong Kong as a financial centre it was not overly visible but perhaps manifested itself in a subtle movement to Singapore'.[72]

At the same time as the linked exchange rate was introduced on 18 October 1983, Financial Secretary Bremridge announced that interest on Hong Kong dollar deposits with financial institutions would no longer be taxed. This removed any tax advantage in holding foreign currency deposits or holding Hong Kong dollar deposits off-shore. This was intended to support the HK dollar exchange rate at the time, although it was conceded that there might be an erosion of profits tax revenue arising from the removal of interest tax.[73] After these changes in relative tax positions Figure 3 shows that foreign currency liabilities began to increase sharply in Hong Kong and soon exceeded Singapore.

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[67] Richard C. Williams to Managing Director of IMF, Singapore 1982 Article IV Consultation Discussions, 18 June 1982. IMFA Asian Department, Immediate Office, Country Files, Box 107, Singapore Missions 1975-83.

[68] Budget Speech by Bremridge, Hong Kong Legislative Council, 23 February 1983. P. 549.

[69] A.R. Latter, 'Monetary Policy in Hong Kong: a personal view', passed to HSBC Assistant General Manager Finance J.M. Gray, 13 July 1983. HSBC Asia Pacific Archive, HKO192/101(2) Correspondence re: Monetary Control 1981-1988.

[70] Memo of meeting with Bankers Trust, 1 November 1983. Federal Reserve Bank of New York Archives [hereafter FRBNY] C260 Meetings with Commercial Banks July-December 1983.

[71] Memo of meeting with Charles Meissner and S. Waite Rawls, Vice Presidents, Chemical Bank. FRBNY C260 Meetings with Commercial Banks July-December 1983.

[72] Memo Meeting with Bank of New York, 12 October 1983, Thomas Renyi and Owen A. Brady Vice Presidents. FRBNY C260 Meetings with Commercial Banks July – December 1983.

[73] Memorandum from Mr. Wicks, circulated to Executive Board of IMF, 18 October 1983. IMFA China Box 22.

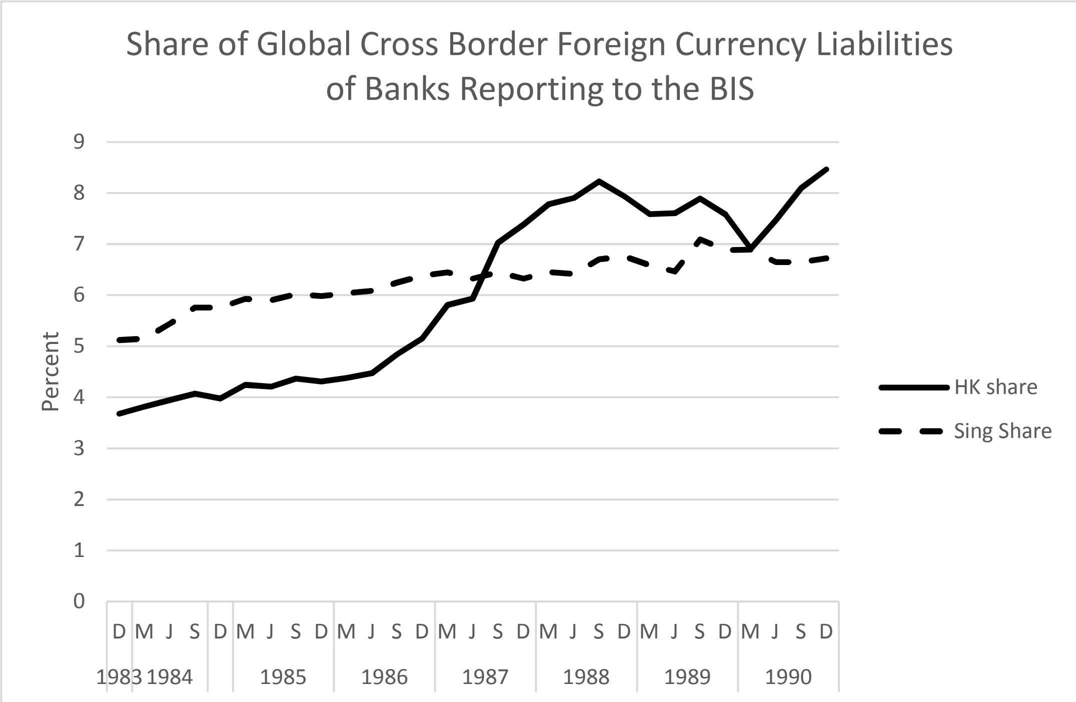

Figure 3: Source: Bank for International Settlements.

Hong Kong and Singapore Inter-Bank balances

It is difficult to identify precisely the participation of Hong Kong in the Singapore market for the early years. The Banking Commissioner in Hong Kong did collect confidential data on the geographical distribution of assets and liabilities and sent this data monthly to the Secretary of State in London, but Singapore was not reported separately from 'Rest of Sterling Area' (although Japan, Thailand and Indonesia are recorded separately).[74] This suggests that the flow was not remarkable.

Figure 4 shows the quarterly data reported from March 1979 in the Hong Kong Monthly Digest of Statistics on foreign currency inter-bank balances between Hong Kong and Singapore. About one quarter of Hong Kong banks' foreign currency liabilities to banks overseas were to Singapore from 1979 to 1982 and this share fell to about one-fifth by the end of 1986. The share of claims increased from about 13% to 24% at the end of 1981. From 1982 to 1986 both series show a gradual decline. Figure 5 shows that non-bank Deposit Taking Companies (DTCs) had a higher proportion of their overseas liabilities in Singapore, but a smaller share of claims. Banks had the largest gross claims and liabilities, although DTCs had significantly larger net liabilities to Singapore.

[74] Monthly reports for 1968-1972 are included in Hong Kong Public Record Office [hereafter HKRS] 163-3-12.

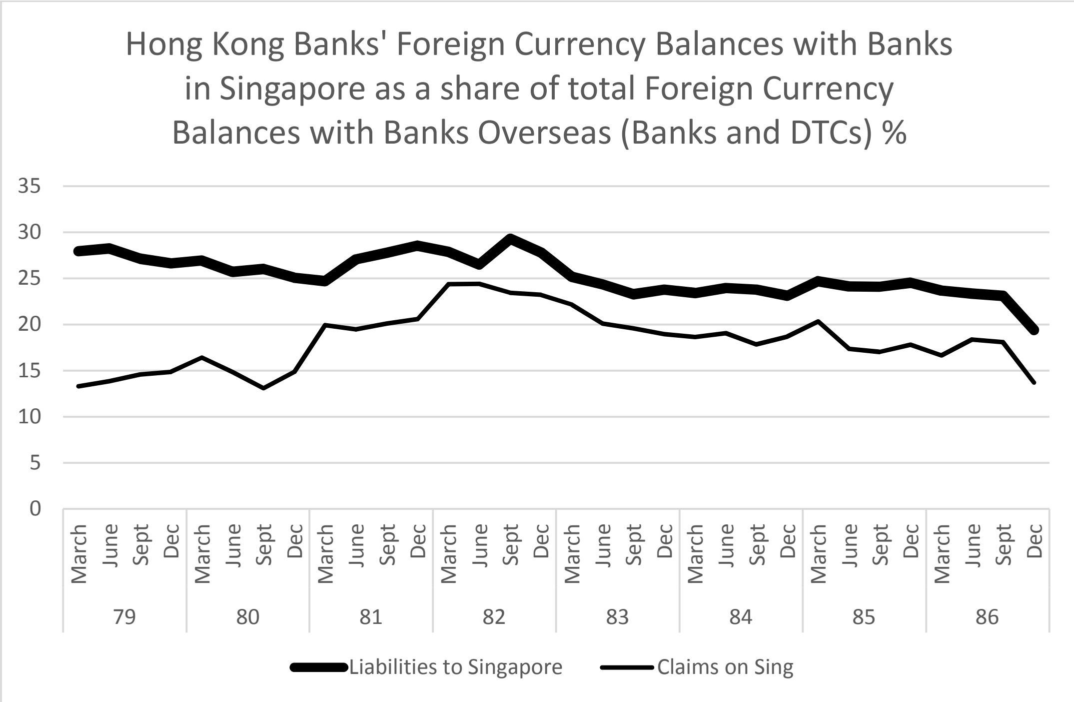

Figure 4: Source: Hong Kong Monthly Digest of Statistics

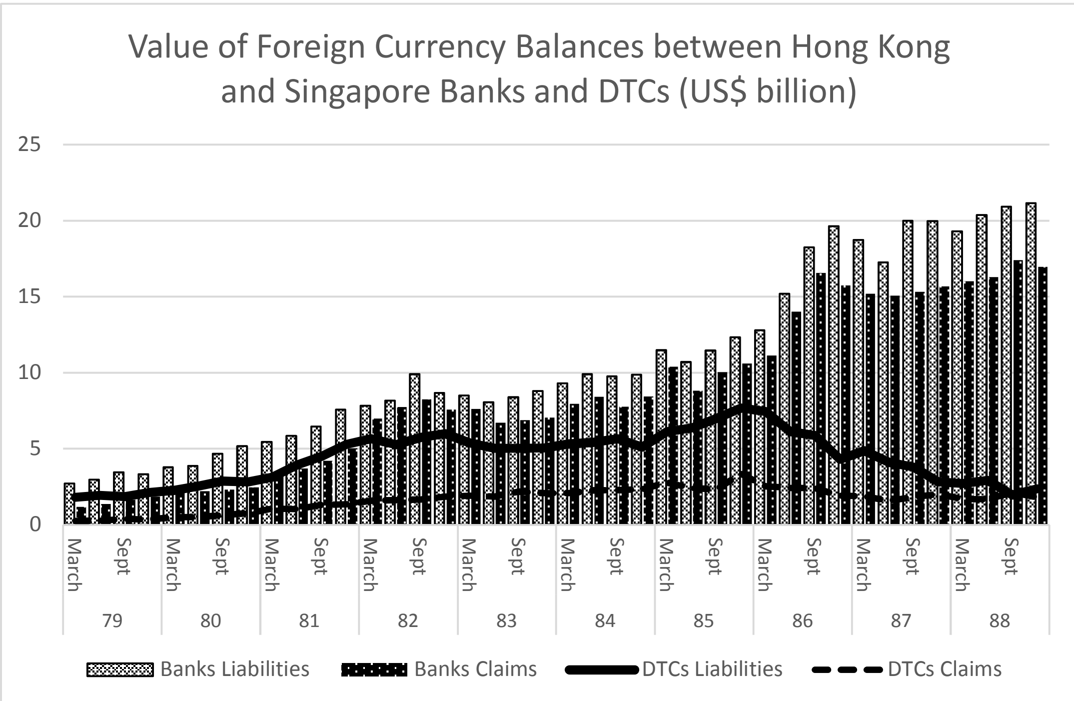

Figure 5: Source: Hong Kong Monthly Digest of Statistics

In the case of both banks and DTCs, the data show a net flow of funds from Singapore to Hong Kong (i.e. Singapore banks had net claims on Hong Kong financial firms) and indeed the net position of DTCs was about 2-3 times greater than banks, demonstrating that these more lightly regulated institutions were important players in the market.[75]

The Asia Dollar Market in the Global Market

The rapid growth of offshore markets created challenges for the monitoring of international capital and banking markets and led to a sustained campaign within the Bank for International Settlements to increase transparency. The US and UK authorities were among the first to collect the balances of branches of their banks in offshore centres. Coverage by other countries, however, was more patchy. Table 2 shows that among G10 and other European banks, Singapore was a larger target for claims by the end of 1976 than Hong Kong, and that in common with other offshore centres, most funds were deposited on short term. At this point, Singapore was approaching the size of Cayman Islands, but Bahamas remained by far the largest offshore centre for the G10, particularly for US banks.

December 1976 External Claims of G10+ Denmark, Ireland and Switzerland and of their affiliates in offshore centres

Claims on	Total	Up to 1 year	1-2 years	Over 2 years	Unallocated*	Unused Credit Commitment
Singapore	9168	8067	54	218	829	534
Bahamas	30999	27832	242	972	2253	1284
Cayman Islands	10165	8691	425	175	874	98
Hong Kong	7485	6174	150	581	580	976
TOTAL	77632	62585	1794	7166	6087	4360

*Includes all Canadian banks ($9.2 billion). First series including non-US banks. Excluding Italian banks (est. $0.3 billion). Denmark and Ireland together less than $0.2 billion. Includes only a sample of banks: Netherlands 65%, France and Swis banks 75%, USA 90%, Belgium, Canada, Luxembourg and Germany c. 95%; UK and Sweden c. 100%. French figures exclude banks' working balances and interbank money-market operations.

Source: FRBNY Archives Fed Central 260.43

However, relying on the reports branches of foreign banks alone did not capture the full data of these offshore centres. At the start of 1976 Rene Larre of the Bank for International Settlements wrote to the monetary authorities in Singapore, Panama, Bahamas and Hong Kong to ask if they would be willing to report the foreign currency positions of their commercial banks.[76] He also offered to send out a representative from the BIS to consult and Dealtry duly arrived in Hong Kong and Singapore in March 1976. He reported back to the Hong Kong banking commissioner, A.D. Ockendon that:

> 'I was also glad to learn that you feel there is a prudential case for collecting more information on the external operations of banks and other deposit-taking institutions in Hong Kong. As I think I

[75] C.R. Schenk, 'Banking Crises and the Evolution of the Regulatory Framework in Hong Kong 1945-70', *Australian Economic History Review*, 43(2), pp. 140-154, 2003. C. R. Schenk, 'Negotiating Positive Non-Interventionism: Regulating Hong Kong's Finance Companies 1976-86', *China Quarterly* 2017.

[76] Letter from Larre, 19 January 1976. BIS Historical Archive [hereafter BISA] 1/3A(3) Dec 1975-Jan 1976.

> mentioned to you the main point of our publishing every quarter a full country breakdown of the external positions of commercial banks in G10 countries is from the safety angle…I shall now wait to hear whether you are able to collect more information in this area and, if so, whether and how it might be incorporated into our reporting system'.[77]

He also found some support from the Bank of East Asia Deputy Chief Manager in Hong Kong, Michael Y.L. Kan. He wrote that 'I might add that I was interested to note that in your opinion it would be useful if more information were available in that area. Perhaps you may be able to persuade others of that view'.[78] But he was more frank in his letter to J.B. Selwyn, Hong Kong Commissioner for Securities, thanking him for a

> 'very agreeable evening at your club. What, if any, concrete results will come out of my visit to Hong Kong I've no idea. Perhaps not very much. But I had a whale of a time and shall not soon forget the impression of dynamism that I received. Singapore, while equally dynamic, I didn't like as much and shan't be too sorry if I don't go there again. If a chance to revisit Hong Kong comes up, however, I shall seize it eagerly – and shall hope to find you still there.'[79]

He played on the rivalry between Singapore and Hong Kong also in his correspondence with Mike Sandberg, Deputy Chairman of HSBC, noting

> 'after visiting Singapore, where rather more statistical information is available in this area, I was left wondering which of the two centers in fact does the greater volume of foreign currency banking'.[80]

In Singapore, Dealtry met with a range of British and US bankers to learn about the Asian Dollar Market and to make the case for disclosing more banking statistics for the BIS series.[81] Michael Wong Pakshong, Managing Director of the Monetary Authority of Singapore noted that he would be willing in principle to contribute, but he was concerned about the potential to use the data as a first step to controlling the market and also about the confidentiality of the data within the BIS. Dealtry reassured him that

> so far as 'control' of the Eurocurrency market is concerned, no such idea lay behind our decision to visit Singapore and other financial centres outside the G10 area; that we are, to say the least, skeptical about the practical possibilities of countries being able to agree on, let alone carry out, any effective control scheme; and that we do not really see how any financial centre could be 'controlled' by others against its own will. Secondly, so far as concerns the sensitive character of some of the data you receive, any information that you pass on to us would of course only be used in strict accordance with your instructions. In that connection, I would add that the full country breakdowns of their banks' external liabilities and assets that we receive from G10 monetary authorities are not circulated, either inside the BIS or among the contributing central banks, except on a consolidated basis.[82]

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[77] Letter from Dealtry to A.D. Ockenden, 30 March 1976, BISA Eurocurrency Standing Committee, 1/3A(3) Volume 22, February 1976 to March 1976.
[78] Letter from Dealtry to Michael YL Kan, 30 March 1976, BISA Eurocurrency Standing Committee, 1/3A(3) Volume 22, February 1976 to March 1976.
[79] Letter from Dealtry to J.B. Selwyn, 30 March 1976, BISA Eurocurrency Standing Committee, 1/3A(3) Volume 22, February 1976 to March 1976
[80] Letter from Dealtry to M.G.R. Sandberg, 30 March 1976, BISA Eurocurrency Standing Committee, 1/3A(3) Volume 22, February 1976 to March 1976.
[81] The banks included Chartered Bank, First National Citibank, Bank of America and HSBC.
[82] Letter from Dealtry to Wong Pakshong, 1 April 1976, BISA Eurocurrency Standing Committee, 1/3A(3) Volume 23, April 1976 to May 1976.

But neither the Singapore nor the Hong Kong authorities wanted to disclose their data. In November 1976 Wong finally responded to Larre that he preferred to wait until Hong Kong had provided their data before making Singapore's data available.[83] No offshore centre wanted to be the first to be reporting formally to the BIS. At first it seemed the Cayman Islands would disclose their annual data, but when they heard that the Bahamas authorities were hesitating, they withdrew their offer.[84] In April Larre noted that

> Mr. Wong Pakshong in Singapore is not ready to provide information until other Asian offshore centres, in particular Hong Kong, do so; and Mr. Donaldson in the Bahamas has indicated that his position is the same'…'thus the present situation is that we are unable to extend our reporting to cover any of the major offshore financial centres. We have, however, by no means given up hope of obtaining information from Hong Kong…'[85]

Much, therefore, hinged on Hong Kong's reaction, but they were slow to respond. Two years later, in 1979, Larre reported to Wong that the collection of data from Hong Kong had been delayed and that no data would be collected on Hong Kong banks' liabilities to non-resident non-banks; since there was no recognized test of residency in Hong Kong to identify these positions. On this basis Larre asked again if Singapore would participate, noting that 'you ask whether other offshore centres have agreed to provide us with statistics' but these other centres had only agreed to contribute their data if Hong Kong and Singapore did.[86]

As part of their charm offensive, in 1980 the Basel Committee on Banking Regulations and Supervisory Practices, which sought to exchange information and best practice among G-10 banking supervisors, convened a meeting of supervisors in offshore centres. The meeting was held over two days at the end of October 1980 to try to engage these centres in the sharing of data, and supervisory cooperation.[87] Beyond introducing supervisors of offshore centres to each other, there was very little tangible progress from this meeting.

In 1986 the IMF also tried to convince the Singapore authorities to disclose more banking data. The MAS participated in the Fund's international banking statistics project, providing quarterly consolidated positions of ACUs vis-à-vis most individual countries, but excluding 7 countries in Asia. The data were also not broken down into bank/nonbank positions, which needed to be estimated by the IMF on the basis of partner data.[88]

This initial evidence about official attitudes to off-shore markets reveals the tension between deregulated markets, financial globalisation and transparency during the first have of the 1980s when regulators struggled with prudential supervision in a rapidly evolving international financial market.

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[83] Letter from Wong to Larre, 30 November 1977. BISA BISA Eurocurrency Standing Committee, 1/3A(3) Volume 25, October 1976 to April 1977.

[84] Note by Dealtry 19 January 1977.BISA BISA Eurocurrency Standing Committee, 1/3A(3) Volume 25, October 1976 to April 1977.

[85] Letter Larre to Vassal Johnson, Financial Secretary, Cayman Islands, 22 April 1977. BISA Eurocurrency Standing Committee, 1/3A(3) B Volume 25, October 1976 to April 1977.

[86] Letter from Larre to Wong Pakshong, 30 March 1979. BISA Eurocurrency Standing Committee, 1/3A(3) B Volume 25, October 1976 to April 1977.

[87] Summary of 19th Meeting of the Committee on Banking Regulations and Supervisory Practices, BIS, 26-27 June 1980. BS/80/33e.

[88] Briefing Paper 1986 Article IV Consultation, 10 March 1986. IMFA Asian Department, Immediate Office, Country Files, Box 108; Singapore Missions 1984-87.

Conclusions

Over recent years there has been considerable controversy about and criticism of offshore financial centres but we know little about their emergence. How important were different factors (tax, time zone, secrecy) in their emergence? What distinctive historical or institutional factors influenced the design and development of offshore centres or were they merely a neutral and convenient space for international finance? Did they compete with, supplement or promote activity in more established international financial centres? This article has provided the first archival account of the case of Singapore and Hong Kong and demonstrates the contribution that can be made from archival evidence for explaining the emergence, motivation and operation of such financial centres.

Three conclusions emerge from this early history of the Asia-dollar market. First, the motivation for the launch of the Asia-Dollar market was two-fold: to promote an international financial centre as part of the diversification of the Singapore economy (along with a range of other initiatives), and secondly to channel regional savings into regional development projects (including in Singapore). In this sense, the market was not strictly offshore since it was hoped that part of the funds could be used locally; local residents were gradually allowed greater access to both the deposit and loan markets. Secondly, the rivalry between Hong Kong and Singapore shows some characteristics of regulatory competition, but in fact for most of the first decade, Hong Kong was able to exploit Singapore's tax concessions so the markets were more complementary than competitive. The change happened when it seemed there was a drain of liquidity from Hong Kong to Singapore in the early 1980s. Although the main motivation for Hong Kong banks to lobby for concessions in Hong Kong seems to be the challenge to the reputation of Hong Kong as an international financial centre, evidence from international banks suggests they still preferred Hong Kong over Singapore because of the agglomeration of other services there due to the longer history of the IFC. The currency instability of 1981-82 was a more important blow to Hong Kong's reputation, although the restoration of the currency board link to the US$ in 1983 resolved this issue quickly. The tax concessions in 1982 and 1983 do seem to have had an impact on inter-bank flows between Singapore and Hong Kong and the changes in tax policy in Hong Kong changed the dynamics between the two states, but the changes in Hong Kong in 1986 finally prompted the largest an increase in the colony's relative position both as a host of cross-border foreign currency deposits and the flow of funds between Hong Kong and Singapore.

We find no direct evidence for actual cooperation between jurisdictions to achieve the complementary outcome, although the banks in Hong Kong were influential in the formation of the Hong Kong government's policy stance. It seems that the underlying principle of non-territoriality in Hong Kong's tax legislation was as important as bankers' interests. Bankers had to lobby for changes once it was in their interests for the Hong Kong regulation to be changed (as it was eventually in 1986). The OFC in Singapore was not a spontaneous or neutral space for international finance; it was deliberately and strategically created and supported by the state. International banks welcomed the initiative and were keen to take part, but the advantages were mainly viewed as long term and related more to the potential benefits of a growing manufacturing and industrial region than financial or regulatory arbitrage per se. Singapore provided a supplement to the global Eurodollar market because it was able to exploit the time zone advantage through competitive tax concessions, but this owed much to the close banking integration with the established financial centre in Hong Kong. More work remains to be done on the integration of the market into global money and capital markets and comparing Singapore to other offshore centres.

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