The operating environment for bank Treasury dealing rooms has not been easy. Capital adequacy considerations have led to severe control of growth, if not outright reductions in the banks' balance sheets. The slow growth in the major economies has led to massive restructurings and consolidations by banks in their international operations; counterparty limits have been subject to stringent review, and have been reduced. There will, therefore, be this natural tendency for bank dealing rooms to consolidate, be defensive, and maintain the status quo.

Future Directions And Opportunities

But, looking more deeply into the developments in the international financial markets and the conditions in the regional markets, now in fact is the time for banks in Singapore to set new directions with regard to their Treasury activities.

Derivatives

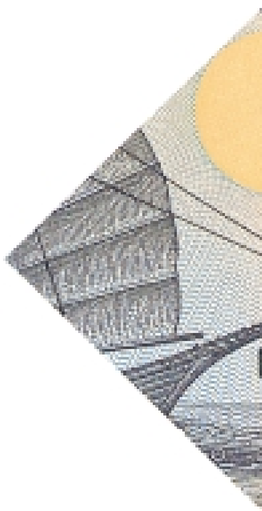
One area where bank dealing rooms should step up their involvement is in derivatives such as futures, FRAs, IRSs, and options. They offer opportunities to express interest rate and exchange rate views without severely impacting balance sheets unlike the use of cash markets. These products also tend to generate lower counterparty risks.

Banks in Singapore should be in a good position to move into derivatives as there is already a very strong foundation for risk-taking and risk management. For one, the foreign exchange cash markets have already reached international standards. This year's volume has moved above the 1991 average despite many negative factors. For another, while growth has been weak in the Eurodeposit market, the size of the Asian Currency Unit market has reached global proportions. Singapore has developed into both a major funding and loan syndication centre. In the Singapore International Monetary Exchange (SIMEX), there is a thriving futures market right in our own backyard. SIMEX offers the most successful Eurodollar interest rate futures contract outside of Chicago.

BANKS CAN BUILD ON THEIR VAST EXPERIENCE IN THE CASH MARKETS TO EXPAND INTO DERIVATIVES.

Banks can build on their vast experience in the cash markets to expand into derivatives. Given the kind of cash market products actively traded right now, it would be natural to go into futures and options in currencies, short- and long-term interest rates in the major currencies, and in some of the major stockmarket indices.

Weak market conditions in other centres such as London, New York and Sydney have created surplus skills and experienced professionals in derivatives. This situation presents an opportunity to transfer such skills and knowledge to the republic for long-lasting benefits to local professionals. As it is uncertain when, and to what extent, the developed centres currently experiencing soft market conditions will bounce back again, the move to tap the surplus skills there must be taken now. The presence of such experienced foreign professionals will immediately lift the standard and level of derivatives trading in the market and accelerate the further development of banks' derivatives activities.



The training of local staff can also be accelerated. Knowledge and understanding of theoretical concepts and market practices in derivatives can be gained from courses at the Institute of Banking and Finance (IBF). The SFEM Committee has been working closely with the IBF to include workshops and simulated modules in such courses to make them practical and effective. Local training can be supplemented by overseas exposure to active derivatives trading rooms.

Technology, another resource vital to derivatives trading, is now readily available and at increasingly lower costs. In the early days, technology had to be developed as and when the market required it. Sometimes, it took painful financial lessons before institutions realised the need for good technical systems for managing such complex products as derivatives. Today, various systems and technical applications are available to support the dealer; to assist management in tracking and controlling positions and overall risk profile; and to process, settle and account for derivative products. Competitive pressures among software developers and consistent upgrading of systems have resulted in increasingly cheaper entry to derivatives activities.

While current market conditions and availability of cheaper technical systems make it easier and quicker for banks to go into derivatives, two important pre-conditions must be met. These are that banks' senior management should have an adequate understanding of these products and an appreciation of their risks, and how they can be monitored and controlled. Expectations must likewise be realistically based on acceptable risk profile and tolerance.

Regional Financial Products

The other areas which banks should look into is the regional currencies and capital market products.

One by one, the financial markets in the region are being liberalised. The accompanying deregulation should result in capital flows not only intra-regionally but also from North America and Europe. As intra-regional trade, which has increased dramatically in the last few years, will continue to grow strongly, the market for regional currencies should therefore increase. Opportunities for foreign exchange on these currencies can only but open up.

The increasing accessibility of domestic markets and the growth in liquidity of regional currencies should also result in more use of regional markets for funding and investment purposes. International fund managers can be expected to allocate an increasing proportion of their portfolio to the region which is expected to be the fastest-growing economic block in the next decade. Securities in both bonds and equities denominated in the regional currencies should grow and with them, the secondary market.

BANKS IN SINGAPORE HAVE A DISTINCT ADVANTAGE IN TAPPING OPPORTUNITIES FROM THE LIBERALISATION AND DEREGULATION OF REGIONAL CURRENCY, DEBT AND EQUITY MARKETS.

Being in the region and in one of the most developed financial centres in the world, banks in Singapore have a distinct advantage in fully tapping opportunities that come with the liberalisation and deregulation of the regional markets in currency, debt and equities. As a centre for foreign exchange, international currency deposits and futures, their dealing rooms already have the linkages with dealers, fund managers, and investors not only regionally but also the world over. This international information and relationship infrastructure can be developed as a foundation for being the centre for foreign exchange, funding and investment in the regional currencies.

Conclusion

Market conditions and developments influence the directions which banks can take in terms of their dealing and risk management activities. In the relative pessimism that abounds in the economies of the major industrialised countries and in their financial institutions and markets, there are, in fact, very promising areas where banks in Singapore can go into. One is to extend their dealings from the cash markets to derivatives, another is to develop their dealing and sales capabilities in regional currencies and financial instruments. The opportunities are here — the commitment must be made now.