Senior Minister Lee Hsien Loong delivering a lecture before taking questions in a Q&A session at Nazarbayev University in Astana, Kazakhstan, on Aug 27. A point he made was that Singapore decided to leapfrog the region and develop export markets in the developed economies in Europe, America and Japan, and adopted English as its common working language. ST PHOTO: GAVIN FOO

The turning points in Singapore's economic development

From the early 2000s to the present, Singapore has invested in enabling infrastructure, says Lee – physical infrastructure like a new integrated and automated container port (above), new airport terminals, high-quality public transport and public housing; and digital infrastructure like information technology, a nationwide fibre network for broadband internet, mobile networks and digitalised government services. PHOTO: PSA

The following is an abridged version of Senior Minister Lee Hsien Loong's lecture to Nazarbayev University in Astana, Kazakhstan, on Aug 27.

Singapore and Kazakhstan are very dissimilar countries. Singapore is a tiny island, a maritime nation surrounded by water, bereft of natural resources. Kazakhstan is a vast, landlocked country, rich in all kinds of energy and minerals in the ground. We are 6,000km apart – one in the Asia-Pacific, the other in Central Asia.

Yet, we do share certain things in common. Both have neighbours much bigger than ourselves. Both gained independence after splitting off from larger federations, and yet retain close ties with them – Kazakhstan from the former Soviet Union; Singapore from Malaysia. We both seek good relations with our neighbours, but also reach beyond our immediate regions to build links all over the world.

Between Kazakhstan and Singapore, the volume of trade and investment is still modest. And yet in an interconnected world, global developments and issues affect all of us. With multilateral frameworks under stress, countries need to develop new partnerships with like-minded countries whose interests are aligned. We also need to seek out fresh opportunities for economic cooperation beyond traditional trade and investment partners. Kazakhstan and Singapore therefore have much to gain by closer cooperation, and much to learn from each other's experiences.

SINGAPORE'S ECONOMIC DEVELOPMENT EXPERIENCE

A country's economic strategy depends on its geography, history, its culture, and its strategic situation. Singapore's experience may not be directly relevant elsewhere. We do not claim to have all the answers, not even to our own problems.

Singapore is located at the tip of the Malayan peninsula, at the southern end of the Strait of Malacca. It lay along the ancient maritime silk route between China and India. It has therefore long been a trading post, though over the centuries, Singapore's importance waxed and waned. A major turning point came 200 years ago, when the British arrived and built a free port in Singapore. Singapore swiftly grew into a thriving entrepot. It facilitated trade between Britain, India, South-east Asia and the Far East, especially after the Suez Canal opened in 1869. And this was the beginning of modern Singapore.

But after World War II, the entrepot trade began to stagnate. Communist China was closed off from the world, and very poor. Regional countries, which exported rubber, copra, tin and spices through Singapore, were increasingly looking to bypass us, and trade directly with their end markets.

And meanwhile, Singapore was experiencing a post-war baby boom. In the early 1960s, Singapore had the busiest maternity hospital in the whole world – Kandang Kerbau Hospital. I was born there, like many Singaporeans. We desperately needed to create jobs for a young and growing population.

Singapore's leaders believed that the solution was to industrialise the economy – to start labour-intensive manufacturing industries to create jobs and develop the economy; and also to join the Federation of Malaya, which later became Malaysia – to create a larger domestic market that would make our industries viable. And hence Singapore joined the Federation of Malaysia in 1963.

Unfortunately, this merger failed. The larger domestic market never materialised. There were also other deep political problems and communal tensions. Two years later, Singapore separated from Malaysia to become an independent nation.

EXPORT ORIENTATION AND INDUSTRIALISATION

This was a major turning point. As one of our founding fathers said, having previously convinced themselves that an independent Singapore could not survive, they now had to spend the rest of their lives proving themselves wrong.

The leaders decided that industrialisation and labour-intensive manufacturing was still the way forward. But now without a domestic market, import substitution no longer made sense. We had to manufacture for export – not just to the region, but to the world. And that meant we had to be internationally competitive – both the individual firms, as well as the whole economy.

We decided to leapfrog the region and develop export markets in the developed economies in Europe, America and Japan. We adopted English as our common working language. We aggressively sought investments from multinational corporations (MNCs). Only MNCs had the technology, management expertise, competitive products and market reach to make this strategy work, and generate well-paying jobs for our population. We did our best to help the first MNC projects do well. Their success attracted more investments. MNCs became a major engine of growth.

We also decided to make Singapore an international financial centre. We were in the right time zone to host an offshore Asian dollar market, inspired by the offshore Eurodollar market. We would host international financial transactions after business in the US closed, and before business in Europe opened the next day. We convinced foreign banks that we could provide the stable conditions, the good infrastructure and skilled professionals that they needed, along with strong rule of law and competent regulatory institutions. The foreign banks set up here. Our financial industry grew beyond supporting our own economy to service the region around us, which was also taking off.

Though entrepot trade was reaching its limits, we did not give up on our port. We invested in modern port infrastructure, started containerisation earlier than other ports, and aimed to become a major node in global maritime trade, which we believed would continue to grow. And fortunately, it turned out so.

To do all this, we had to abandon the old adversarial model of labour-management relations. We persuaded the trade unions and employers to instead form a tripartite partnership – three-way partnership – between the unions, employers and government. The three partners built trust in one another, adopted a win-win approach, and cooperated to enlarge the economic pie. We set up a tripartite National Wages Council to make annual wage recommendations. These set expectations for businesses and workers, guided wage negotiations and prevented wage inflation.

These strategies succeeded. Unemployment fell, incomes rose. The economy took off, creating good jobs for our people.

WAGE CORRECTION

We started in 1965. By the late 1970s, our economy had reached a transition point. Unemployment had almost disappeared. The economy was experiencing labour shortages. During the years of rapid growth, the National Wages Council had restrained wages. Now wage levels were too low. Firms had little incentive to raise productivity or invest in workers. For our economy to develop and upgrade further, we needed to change course.

So the Government launched a deliberate "corrective wage policy" to raise wages significantly. The aim was to push companies towards higher-tech, higher value-added activities. And this worked for several years, as the economy continued to boom. But the wage policy overshot.

In 1985, external conditions changed. Singapore suddenly entered a deep recession, our first since independence. We studied the problem, and concluded that we had allowed our business costs, especially wage costs, to go way out of line, and Singapore had become internationally uncompetitive. A painful correction was necessary.

The textbook answer to this situation would have been to let the Singapore dollar depreciate, and allow domestic inflation to erode the purchasing power of nominal wages, in order to restore competitiveness by stealth. We did not think this was a good solution. We felt that would undermine workers' trust in the Government, and weaken the tripartite partnership. The alternative, cutting wages directly, was politically impossible – not even in Singapore.

Fortunately, Singapore had a third option. We had a compulsory national retirement savings scheme – the Central Provident Fund. And in the years when wages were rising sharply, the Government had steadily raised contributions by workers and employers to this Central Provident Fund. By 1985, the contribution rate had reached 50 per cent of wages. Half of your salary was paid into a mandatory personal retirement savings account.

Cutting this rate would lower wage costs without reducing workers' take-home pay. It was still politically difficult, but doable. We bit the bullet and cut the CPF contribution rate significantly. The effect was an immediate 12 per cent reduction in wage costs. This drastic action, coupled with severe wage restraint, brought our labour costs back into line, and restored our competitiveness.

Singapore recovered quickly from the recession. We went back to growing at 10 per cent every year. But restored cost-competitiveness was not the only factor.

After the recession, we shifted our economic strategies. We pushed for higher value-added, tech-intensive investments. Beyond manufacturing projects, we started getting MNCs to set up their overseas and regional headquarters in Singapore. We got overseas headquarters here – operational headquarters – to manage their regional activities, and to do product development, market research, human resources and finance work out of Singapore. We also promoted the export services sector – for example, in transport and logistics, hospitality and tourism. We invested heavily in reskilling our workers, as the nature of jobs changed. We restructured our taxes, lowering personal and corporate tax rates and introducing a goods and services tax, to spur enterprise and create a light but progressive tax system.

The aim was to shift the economy towards more complex activities, which our increasingly well-educated workforce could perform, and activities that linked Singapore more closely to our region, which was also taking off. Together, these measures delivered sustained strong growth for another decade, until the Asian financial crisis in 1997.

THE ASIAN FINANCIAL CRISIS

The Asian financial crisis severely affected the Singapore economy. We were in ground zero – the crisis had started in Thailand, then spread to Malaysia and Indonesia, and beyond. Many of these countries had overborrowed in US dollars, ran into balance of payment crises, and had to call in the IMF (International Monetary Fund). But Singapore ran a healthy trade surplus and had no nett borrowings. And hence we did not experience any capital flight. Instead, there was a flight to safety – capital flowed into Singapore, and the Singapore dollar actually appreciated modestly.

In the midst of the crisis, we took advantage of this confidence in Singapore to transform our financial sector. We had grown our financial sector steadily by being very careful and cautious, taking minimal risks and keeping everything under tight control. But to take the next step forward, our regulators needed to become less risk-averse. We had to loosen up in a controlled way, in order to inject more vibrancy and create more opportunities in the financial industry. And we judged that we now had accumulated the experience and the credibility to do so. So, we carefully shifted our regulatory approach from tight regulation to a more risk-based supervisory regime.

The whole process took four to five years. It made Singapore more attractive to global financial institutions, which started moving more activities to the Republic. We became a major international financial hub, linking up with Tokyo, Hong Kong, New York and London.

THE KNOWLEDGE-BASED ECONOMY

At around the same time, we started to develop a knowledge-based economy. We built up research and development. We invested patiently and steadily in both basic and applied research. This supported advanced manufacturing industries like semiconductors and biomedical, which became important contributors to our economy. It also spawned new start-ups based on these R&D advances.

We improved our education system, to create more pathways for diverse talents and interests, and to prepare Singaporeans for jobs that required critical thinking, innovation and lifelong learning.

To support the growing economy, we allowed in a controlled, steady flow of foreign workers. We made it easy for companies to bring in skilled professionals with the talent and expertise that their businesses needed. And these foreigners complemented our own workforce, and enabled companies to create more good jobs for Singaporeans.

We invested in enabling infrastructure. Physical infrastructure – new airport terminals, a new integrated and automated container port, high-quality public transport and public housing. Digital

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