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Understanding the politics of bailout policies in non-Western countries: The use of sovereign wealth funds

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This article examines bailout policies in non-Western states through selected case studies of financial bailouts in Hong Kong and Singapore between the 1960s and 1990s. Given their structural similarities and extreme openness, standard explanations would expect to find similar policy responses over this period. However, between the 1960s and 1990s, bailout policies differed greatly between the two countries, particularly with respect to the use of their sovereign wealth funds (SWFs). This article also shows that the differing uses of SWFs reflected the respective regulatory environments. In line with an emerging stream of studies in comparative politics, the present article finds that these differences take root in the institutional settings of the respective countries and vary across state-business relations.

Keywords: financial crises; sovereign wealth funds; bailouts; government-business relations; small open economies

1. Introduction

The use of unconventional policy instruments in the context of the unravelling financial crises of 2007/2008 were reflected in adventurous financial rescue packages. These varied from country to country. While in some, such as France, bailout packages were more balanced, with banks carrying significant parts of the burden, in others, such as the UK and Germany, bailouts were carried completely by the taxpayers (Woll 2014). Thus far, the majority of scholarship has focused on large Western economies with well-established democratic political systems (see, e.g. Grossmann and Woll [2013], Woll [2014], Culpepper and Reinke [2014], Chwieroth and Walter [2015] on this important subject). However, these studies said little about whether these claims also hold in non-Western contexts. The present paper highlights the need to go beyond the study of bailout policies in Europe and North America.

To date, little is known about the politics behind financial bailouts in non-Western countries. Yet these countries are similarly exposed to international financial crises and must respond accordingly. This paper analyses whether findings about the effects of domestic politics on bailout policies in Western countries can also explain

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the forms bailouts take in non-Western states. Especially in the contemporary situation, where a number of emerging countries – notably China – are facing financial difficulties, it becomes increasingly important to investigate the politics behind bailout policies in non-Western contexts (The Financial Times 29 April 2016, 23 April 2016). Over the last two decades, emerging economies have developed powerful financial buffers in the form of sovereign wealth funds (SWFs). As of 2016, the total volume of AUM of SWFs is estimated at around US$7tn (SWF Institute 2016). These could play a critical role in situations where economies are facing financial pressures.

Unlike their Western counterparts, non-Western countries tend to mobilise their state-owned investment funds, known as SWFs. Countries use these funds not only for diversification and for the benefit of future generations, but also for self-insurance in a globalized financial world. That became most clear during the financial crises of 2008 where a number of non-Western countries used their SWFs to support their domestic financial systems.[1] For example, in 2008 the Kuwait Investment Authority supported the Kuwait bourse and helped to bail out the Gulf Bank (Thomson Reuters 2009, January 26). In a similar fashion, the Qatar Investment Authority injected more than US$3bn into Qatar's four largest banks to keep them solvent (ESADEgeo 2013). Likewise, Abu Dhabi's SWF helped to rescue Dubai World – a major Dubai real estate investment company, and the Russian SWF helped to support the ruble during the 2015 currency cri- sis by injecting money into local banks (The New York Times 9 March 2015).

The present research looks at the use of SWFs during periods of financial pressure. Studies on the use of SWFs, particularly during periods of financial pressure, can con- tribute to the understanding of economic policy. This article links directly to a stream of economic policy literature that looks at banking crisis and policy responses (e.g. see Cardao-Pito and Baptista 2016). Within this literature few authors, notably Aizenman et al. (2016), investigate the vulnerability of non-Western countries to international financial shocks. Thus far it is not completely understood why even very similar non- Western countries adopt different SWF responses to address similar economic pressures. Studying the use of SWFs offers an opportunity to look at the circumstances under which non-Western countries mobilise their large reserves. This in itself is an important contribution to the economic policy literature, because SWFs and their behavior have become central aspects in countries' economic policy reforms.

To study the role of the underlying politics behind the use of state finance institutions during economic crises, this paper uses select case studies on the responses to financial crisis in Hong Kong and Singapore between the 1960s and 1990s. The very different uses of SWFs in Hong Kong and Singapore in this time

[1] SWFs also played a prominent role in saving Western banks, such as Citigroup and UBS (Haberly 2014).

period pose an interesting puzzle in light of standard explanations that highlight the role of the structural power of finance or the resources of financial industry (Igan, Mishra, and Tressel 2011; Culpepper and Reinke 2014).

There are a number of reasons to believe that the use of SWFs over the period 1960–1990 should have been similar in both Hong Kong and Singapore. Both are small open economies and leading financial centers. They were extremely exposed to international financial and currency crises and shocks. Similar tools in form of SWFs were available, but used differently. This presents an opportunity to investigate recent claims about the effects of state-society relations on bailout policies in non-Western economies (see Grossman and Woll 2013; Woll 2014). The combination of structural economic similarities with extreme openness, alongside the stark differences along dimensions highlighted by Woll (2014a, 2014b), makes Hong Kong and Singapore useful cases for examining the impact of state-society relations on bailout policies in non-Western countries. The independent variables posited by Woll (2014, 2014a) are at values that strongly predict dissimilar bailout policies in Hong Kong and Singapore.

The historical focus on the period between 1960s and 1990s allows to account for the influence of Chinese authorities on banking bailouts in Hong Kong. Before its return to mainland China in 1997, Hong Kong was a British Colony. Despite its colonial status Hong Kong enjoyed high levels of autonomy from the Colonial Office in London, particularly in the sphere of economic policy-making (Goodstadt 2005). It was a long-standing convention that the British government rarely issued instruction about the internal and economic affairs of Hong Kong. For example, if Hong Kong's policy-makers received policy directives from London with regard to Hong Kong's finance policy and banking regulations then they typically ignored them (Goodstadt 2005). This facilitates the comparison with Singapore – which was a British Colony until 1965 – at least with regard to economic policy.

This article discovers systematic differences in the organisation of socio-economic actors and links it to differences in public debates over the use of SWFs. It also discovers a nexus between the use of SWFs and regulation. Financial-sector regulation and bailouts are opposite sides of the same coin. The main argument is that SWF-use and regulation are not contradictory but mutually contingent. The article develops this argument in countries with broad macro-economic similarities. While Hong Kong had lax banking regulation between the 1960s and 1990s and used its Exchange Fund to bail out domestic finance companies in every banking crisis, Singapore over the same period had very strict regulation and did not use its SWFs to bail out finance companies. This paper underlines the nexus between bailout and regulation, which is driven by domestic politics.[2]

[2] Although this connection has been well established in the broader academic discourse, it still needs to be verified with regard to the use of SWFs, which are formal independent organisations.

2. Understanding bailout policies and SWFs

Studies in comparative politics underline the connection between domestic politics and financial bailout policies in Western democracies. Scholars emphasise that there is no linear relationship between the magnitude of financial crises and the magnitude of bail- outs (Grossman and Woll 2013; Culpepper and Reinke 2014; Woll 2014). To explain this, they focus on different aspects of power wielded by the finance industry. Departing from central concepts in the literature (e.g. on regulatory capture) a number of authors (e.g. Johnson 2009; Baker 2010; Hacker and Pierson 2010) highlight the connection between the regulatory capture of public agencies, the financial crisis and economic policy responses. For example, Culpepper and Reinke (2014) look at the strategic exercise of "structural power" by banks and how it affects differences in bail- out policies. Culpepper and Reinke (2014) explain the magnitude of bailouts (e.g. costs, magnitude of state intervention) in terms of the structural power of banks. To them, countries with smaller domestic markets find it more difficult to assert their preferred bailout policy vis-à-vis the financial and banking sector (Culpepper and Reinke 2014). Hence, banks found it easier to defy regulators in the UK than in the US (Culpepper and Reinke 2014). Going further, another group of scholars, such as Kwak (2013), identify the role of ideas. To Kwak (2013), bailout policies are neither the product of lobbying nor pure rational considerations. Instead, bailout policies are also shaped through a number of cognitive-social mechanisms (Kwak 2013). The regulated community can exert influence on regulators as well as policy-makers through soft power, which arises from the characteristics of the regulated sector. Status, as well as identification with groups, can have powerful effects on behaviour that goes beyond material self-interest (Kwak 2013).

A recent stream of studies within the discipline of comparative politics emphasises that, despite structural similarities and exposure to cross-sweeping diffusion pressure, countries pursue differing bailout policies. Complementing the argument based on the power of resources, the power of structures, and the power of ideas, authors, notably Grossman and Woll (2013) and Woll (2014, 2014a), emphasise the political organisation and collective-action capacity of financial actors to explain bailout policies. Economies have differing overall institutional environments in which state-society relations are embedded. State-society relationships can vary from country to country and can affect bailout policies (Woll 2014). Bailout policies are carried fully by governments in some countries, but by financial sectors in other countries (Woll 2014). Woll (2014a) is interested in the "the power exerted by doing nothing when one is needed" (428).

This inaction is a feature of government-business relations, which can vary from one country to another. Countries in which banks have close one-to-one relationships with policy-makers' bailout policies are structured around the preferences of individual banks, whereas strong organisational ties among banks, as well as

between banks and policy-makers, lead to more balanced bailout packages (Grossman and Woll 2013). Fragmented banking sectors, in which particular banks have over-proportional influence as well as differing exposures to financial pressures, impede collective action, whereas banking sectors with similar-sized banks and similar exposures to financial pressures facilitate collective action (Woll 2014). Grossman and Woll (2013) and Woll (2014) illustrate this through a number of case studies on bailout packages in France, Germany, Ireland, Denmark, the US, and Britain. However, these studies say little about the bailouts in non-Western countries with important financial sectors.

2.1. Examining bailout policies in non-Western small open economies

This article looks at the effects of state-business relations in non-Western economies during periods of economic uncertainty regarding the use of SWFs. SWFs are also known in the literature by the synonyms rainy-day funds or stabilization funds (Lee 1997; Aizenman and Glick 2009). SWFs absorb excess money supply in times of high external income (Lee 1997, 1). Without such absorption of excess liquidity (e.g. in commodity-exporting countries during boom times), capital inflows can lead to appreciation of the domestic currency, which would then undermine the international competitiveness of the domestic industry. SWFs are also described as financial buffers against capital-supply shocks (Aizenman and Lee 2007; Gilson and Milhaupt 2008). Particularly following the Asian Financial Crisis 1997/1998, many countries have created SWFs as means of self-protection in a volatile global financial economy (Aizenman and Lee 2007). SWFs experienced very fast growth in terms of number and size.[3] Within a single decade, between 2005 and 2015, assets under SWF management have increased by more than 600 percent, from US$895bn in 2005 to US$5865bn in 2014 (Rozanov 2005, 1; ESADE Annual Report 2014, 103). This makes SWFs larger than the combined size of the global hedge fund and private-equity industry (The Economist 17 January 2008).

During this century, virtually all of the non-Western small open economies have established SWFs.[4] In terms of relative size, as compared to GDP, the SWFs of small open economies are the largest worldwide (see Table 1). Their limited resource-base, combined with constrained domestic markets, makes small open economies particularly exposed to price fluctuations in the international commodity markets. Economic open- ness, measured as the ratio of international trade to GDP, render small open economies exposed to external economic conditions (Briguglio and

[3] According to some estimates, the size of global SWFs could by 2015 reach by a volume of US$12–14.4tn (Jen 2007; Aizenman and Glick 2008).

[4] There are also exceptions, notably Luxembourg and Macao, neither of which to date has created an SWF. But there have recently been debates in Macao and Luxembourg about the creation of SWFs (Macaubusiness 15 April 2015; personal communication with an official from the Luxembourg Central Bank, December 2014).

Kisanga 2004). As such, small states are especially vulnerable to capital-supply shocks, and fluctuations in prices (Briguglio and Kisanga 2004). With the aim of nurturing resilience, SWFs are created as means of self-insurance against external economic shocks (Le Borgne and Medas 2007).

Table 1, *Small open economies and their sovereign wealth funds as a part of their GDP*.

Small open Economy	**SWFs**	**Size of SWF in US$ bn**	**As part of GPD (PPP) in %**
Abu Dhabi	ADIA	773	311
	ADIC	90	36
	IPIC	68.4	28
	Mubadala	60.9	25
Dubai	Investment Corp or Dubai	70	65
Bahrain	Mumtalakat	10.5	30
Kuwait	Kuwait Investment Authority	548	330
Qatar	QIA	170	86
	Qatar Holding	n/a	n/a
	Qatar Diar	n/a	n/a
Brunei	Brunei Investment Agency	40	178
Singapore	Government Investment Corporation	320	94
	Temasek	177	52
	Monetary Authority of Singapore	273	80
Hong Kong	Hong Kong Monetary Authority	400.2	105
Equatorial Guinea	Fund for Future Generations	0.08	0.4
Kiribati	Revenue Equalization Fund	0.6	86
Trinidad & Tobago	Heritage and Stabilization Fund	5.5	20
East Timor	Timor-Leste Petroleum Fund	16.6	65
Santo Tome y Principe	Permanent Fund for Future Generation	n/a	n/a
Mauritius	Sovereign Wealth Fund	n/a	n/a
Tonga	Trust Fund	n.a	n.a
Tuvalu	Trust Fund	0.103*	300
Papua New Guinea	Mineral Resources Stabilisation Fund	Abolished in 2001	
Narau	Phosphate Royalties Trust Fund	n/a	n/a
Marshall Islands	Compact Trust Fund	0.063	55
Micronesia	Compact Trust Fund	0.087	38
Palau	Compact Trust Fund	0.153	105
Palestine	Palestine Investment Fund	0.7	10

Sources: Information compiled from the SWF Institute (2014), ESADE Annual Report (2014), Le Borgne and Medas (2007); GDP % calculated from the CIA-Factbook (2014), Trade Economics (2014), *Gulf News* (2014), *Zawya* (2014).

*Tuvalu's GDP refers to Australian $.

3. Financial systems, SWFs, and external pressures

Hong Kong and Singapore share numerous similarities. This has been acknowledged by a number of scholars. For example, Lawrence Krause described them as "kissing cousins" (Krause 1988). Hong Kong and Singapore were both products of British colonialism and were created by an immigrant population. They lack natural resources and are highly dependent on trade. In the nineteenth and twentieth century, Singapore emerged as the entrepôt for South East Asia, whereas Hong Kong became the entrepôt for South China. Between the 1960s and 1990s, both experienced rapid economic growth and each was described as an "economic miracle" (Lam 2000). Both moved from export-oriented manufacturing centers into banking and financial service hubs (Krause 1988). Both are highly integrated into world markets. In numerous rankings, such as that of the Heritage Foundation in their Index of Economic Freedom,

Hong Kong and Singapore were described as the most liberal economies in the world. As small open trading economies and financial centers, Hong Kong and Singapore share a critical interest in stable currencies. Hong Kong and Singapore both have long-established Currency Board systems with the key feature of currency-stabilization funds.[5] These funds sustained fixed exchange rates between their respective currencies (i.e. the HK$ and the S$) and both the British £ (until 1967) and the US $ (starting in 1967) (Lim 1969). They are among the oldest and largest SWFs. The Hong Kong Exchange Fund (est. 1935) and the Singapore Currency Fund (est. 1938) are the predecessors of the Hong Kong Monetary Authority (est. 1993) and the Monetary Authority of Singapore (MAS) (est. 1971). Both were originally established as government accounts (Lee 1974). Unlike SWFs in commodity- exporting countries, those of Hong Kong and Singapore arose from years of conservative fiscal policy, internal fund transfers, and foreign exchange interventions. Relative to population they were similar in size (see Table 2).

[5] A currency board sends strong signals that the government is willing to maintain strong convertible currency, which is a good protection against inflation (Goh 1992). A currency-board system refers to a system in which note issuance is fully backed by overseas reserves in order to allow a smooth conversion.

Table 2, Official foreign reserves in Hong Kong/Singapore between the 1960-1990s.

Year	Hong Kong Exchange Fund in mn HK$	Singapore Currency Fund in mn S$
1968	4,652	2,158
1970	6,196	3.075
1972	9,288	4,902
1974	2,747	6,475
1976	6,541	8,233
1978	14,113	11,436
1980	29,195	13,589
1982	47,317	17,607
1984	53,974	22,415
1986	88,591	27,733
1988	133,051	32,816
1990	196,197	48,034
1992	287,474	65,239
1994	408,485	84,559
1996	534,517	107,073

Sources: numbers drawn from: *Hong Kong Monetary Authority Quarterly Bulletin*, (May 1995, 16), Exchange Fund Balance Sheet 1936-1994; *Hong Kong Monetary Authority Annual Report* (1997,1996); Singapore Yearbooks (1965-1975); *Monetary Authority of Singapore Annual Reports* (1990 & 1991).

*including assets managed later on behalf of the MAS and the GIC.

Both the Hong Kong Exchange Fund and the Singapore Currency Fund comprised a liquid coin portfolio and an investment portfolio. Similar to the Hong Kong Exchange Fund, the majority of the Currency Fund's assets were invested in British government securities (approximately 70%) and commonwealth securities (between 20 and 30%) (Lee 1974, 17–18). Over the years, the funds have accumulated more assets than were needed for currency stabilisation. Apart from the Currency Fund (later the MAS) it should be mentioned that Singapore also has two other SWFs, the Government Investment Corporation (GIC) and Temasek (see Table 3).

Table 3, Characteristics of Singapore's and Hong Kong's sovereign wealth funds.

	Temasek	**GIC**	**Singapore Currency Fund**	**Hong Kong Exchange Fund**
Ownership and reporting structure	Owned by the government and accountable to the MinFin	Owned by the government and accountable to the MinFin	Owned by the government and accountable to the Board of Currency Commissioners	Owned by the government and accountable to the Hong Kong Monetary Authority
Nature of the fund	Investment holding company	Fund management company		
Objective	Capital appreciation, diversification and development	Wealth enhancement	Currency stabilisation	Currency and monetary stabilisation
Allocation	Domestic and foreign	Foreign	Foreign	Foreign
Time horizon of investment	Short- to long-term	Medium- to long-term	Short-term	Short- to medium-term
	Equity (in form of direct and portfolio investments), alternative assets	Equity (in form of portfolio investments), bonds, alternative assets	Bonds, currency, gold	Bonds, currency, gold

Source: Wu (2008, 104).

In the late 1960s and early 1970s, rising levels of international currency volatility as well as capital mobility confronted Hong Kong and Singapore with opportunities and challenges. Both city-state economies were exposed to Britain's currency crisis in the late 1960s. Britain's devaluation measures put pressure on Hong Kong and Singapore in terms of adjustment. Given the exchange link, any change in the anchor currency (i.e. pound sterling) translated directly to the local currency. Because of the fixed exchange rate agreement, both the devaluation of sterling in 1967 and that of the US$ in the 1970s resulted automatically in devaluation pressures on the HK$ and S$ (Teh 1988). Confronted with increasing currency volatility Hong Kong and Singapore abandoned their official peg to the US$ and embarked on a free float (Jao 1993; MAS 2011). During the time of float the Exchange Fund was quite active in selling and buying currencies in order to minimise the negative effects of an appreciating HK$ in the 1970s, and to support exports (Anonymous, personal communication, 18 March 2014). From November 1974 onwards until 1983 the

Exchange Fund was used as an intervention reserve fund.

The US interest rate shock in the early 1980s provoked an outflow of money from the real estate sector into US government bonds. This led to a stock market crash and banking crises in Asia. Many of Asia's leading property firms were publicly listed and strongly linked to the banking sector (Ngo 1996). After the reconsolidation of US interest rates, Hong Kong again experienced a wave of domestic stock market speculation, especially in real estate. This led to a bubble, which resulted in another banking crisis in Hong Kong, because many banks were overexposed to the real estate sector.

During the banking crisis of 1983, a couple of medium-sized domestic banks in Hong Kong, such as Hang Lung Bank with its 28 domestic branches, faced collapse (Ghose 1987). Likewise, Singapore's property market experienced a short run up during the mid 1980s. Banks started to lend to the stock-broking sector. At the end of 1985, they lent about S$1.1bn to the stockbrokers which was about five times the shareholder's funds (MAS 2004, 14). According to an industry professional at that time, the end of 1985, securities and equities comprised between five and 10% of banks' total assets (Anonymous, personal communication, 13 December 2014). In 1985, the Pan-Electric crisis, Singapore's largest corporate meltdown, threatened the solvency of the complete stock-broking sector in Singapore and posed risks to its creditors, the banks (Hu 2009). Pan-Electric Industries was found to owe S$450mn to more than 30 creditor banks, and, consequently, the level of loans to stockbrokers fell (MAS 2004).

The Asian Financial Crisis 1997/1998 posed another test to Hong Kong's and Singapore's financial systems. Although both city-states had strong macro-economic fundamentals (i.e. budget surpluses, excess private savings, no sovereign external debt), their position as trade and financial entrepots in the region exposed them to financial developments in neighbouring countries. Heavy losses by international investors in Thailand, Taiwan, and South Korea led international investors to sell out in other markets, notably Hong Kong and Singapore. The crisis reached Singapore in July 1997 and Hong Kong one month later (Tan 2001, 4). Singapore's stock market suffered a deflation of 47% between the 9 July 1997 and the 5 August 1998, compared with 49% in Hong Kong over the same period (Tan 2001, 5). Because of high exposure to the stock market via nonperforming loans, this downturn also affected the banking sector (Tan 2001). At the same time, the US$ started to strengthen, which put appreciation pressures on the S$ and HK$ because of their direct or indirect link to the US$ (Tan 2001).

4. Similar challenges and different responses

Over the period of the 1960s through the 1990s, Hong Kong and Singapore responded to similar international pressures with different policies in terms of SWF use. While Singapore responded with a policy of prudent regulation, avoiding use of its SWFs to bail out distressed companies, Hong Kong's administration responded

with massive financial bailouts via its SWF (see Table 4). Confronted with international currency pressures in the late 1960s and early 1970s, Hong Kong's Exchange Fund compensated domestic banks for losses incurred by Hong Kong's currency devaluation and revaluation operations during the late 1960s and the early 1970s. For example, between 1968 and 1969 alone, the Exchange Fund paid a compensation of HK$154mn to domestic banks (Hong Kong Monetary Authority Quarterly Bulletin May 1995, 6).[6] Under the Exchange Fund scheme, the Hong Kong Exchange Fund absorbed the costs and risks associated with a part of the bank's foreign exchange operations (Hong Kong Hansard 13 December 1972, 221).

Unlike Hong Kong, Singapore avoided the use of its SWF to compensate domestic banks for losses arising from foreign exchange volatility in the 1960s and 1970s. Singapore's Minister of Finance reassured a meeting of the Singapore International Chamber of Commerce that the reserves of the Currency Board and other official reserves "are not frittered away" (The Straits Times 24 March 1967, 6). However, Singapore's government highlighted its priority of supporting stable currency convertibility by maintaining the parity between S$ and the price of gold (The Straits Times 24 March 1967, 6).

Confronted with stock market and banking crises in the 1980s, Hong Kong's policy-makers used the Exchange Fund repeatedly for bailing out distressed banks. For example, in 1984, the Exchange Fund injected US$300mn into Hang Lung Bank, and it also provided a guarantee of HK$4bn to the recovery of the Ka Wah Bank to facilitate a later rescue by China International Trust and Investment Corporation (Ghose 1987; South China Morning Post 24 June 1989). The Exchange Fund rescued the Overseas Trust Bank and provided a credit-standby facility for the Hong Kong Futures Guarantee Corporation Limited (Hong Kong Monetary Authority Quarterly Bulletin, May 1995). This standby facility totalled HK$2bn and carried interest at a prime lending rate (Hong Kong Hansard 28 Oct 1987, 164). The Exchange Fund's bail- outs during the 1980s were estimated at around US$2bn, or approximately HK$16bn (Ghose 1987, 92). Another measure to stabilize Hong Kong's financial sector in the early 1980s was to re-introduce the currency peg between the HK$ and US$. The main factor for the re-introduction of the currency peg relates to the 1983 negotiations between Britain and the China about Hong Kong's future. These negotiations exacerbated existing economic problems which were affecting the HK$ value (The Wallstreet Journal, 12 July 1988).

[6] The minutes of the Hong Kong Hansard make an even higher estimate of the total costs of HK$450mn. (Hong Kong Hansard 13 December 1972, 219).

Table 4, Similar Pressures and different uses of sovereign wealth funds.

		Currency Crisis	**Stock Market Crisis**	**Banking Crisis**	**SWF used for bailout**
1960s	Hong Kong	X			Yes
	Singapore	X			No
1970s	Hong Kong	X			Yes
	Singapore	X			No
1980s	Hong Kong		X	X	Yes
	Singapore		X	X	No
1990s	Hong Kong		X		Yes
	Singapore		X		No

In stark contrast, Singapore's authorities avoided the use of its reserves to bail out financial companies. Instead, Singapore's government coordinated the setting up of a lifeboat fund, which was financed by Singapore's four large banks: the Overseas Chinese Banking Corporation, the Development Bank of Singapore, the Overseas Union Bank, and the United Overseas Bank (MAS 1986). The lifeboat fund had AUM of S$180mn and was guaranteed by the Stock Exchange of Singapore (MAS 1986). Its purpose was to hedge against a chain reaction (Hwang 2007). Brokers which had trouble meeting their obligations could draw on this lifeboat fund after fulfilling a set of strict criteria (Hwang 2007). Companies which did not meet the strict criteria, such as one of the largest coffee-trading companies, were allowed to fail (Hwang 2007).

During the Asian Financial Crisis 1997/1998, Hong Kong used the Exchange Fund for rescuing the stock market. Between 1997 and 1998 the Hang Seng Index of stock prices fell by around 50 percent. In order to avoid a collapse of the Hong Kong stock market, the Exchange Fund was used to acquire substantial parts of Hong Kong's equity market. Between the mid and late August of 1998, the Hong Kong Exchange Fund acquired around US$15bn worth of blue chip stocks (Jao 2001, 8). Although Singapore's stock market experienced a similar deflation, policy-makers did not make use of its SWF. Instead, Singapore responded by cutting the costs of doing business, including such measures as tax rebates and cuts in CPF contribution rates, as well as competitive devaluation of the S$ (Tan 2001).

5. Explaining responses

Both Hong Kong and Singapore are small open economies, but with different state traditions. While Singapore has been portrayed as illiberal democracy with a stance towards heavy state interference, Hong Kong has been frequently described as liberal autocracy with a generally laissez-faire approach towards economic policy (Krause 1988; Low 2005; Hong Kong Hansard 7 June 1985). Despite their different state traditions, they have achieved similar levels of economic success (Krause 1988). Hong Kong and Singapore have passed through similar stages of industrial development, from textiles to plastics and electronics to banking and finance.

From the 1960s through the 1990s, Hong Kong's government followed a policy of "positive nonintervention". A term coined by John Cowperthwaite and Philipp Haddon-Cave, both of whom served as Financial Secretary during this period, the notion of positive nonintervention refers to a view that any attempt at active government intervention to affect the allocation of resources frustrates the operation of market forces (Hong Kong Hansard 25 March 1966). Many basic services, such as public transport, that are provided by the state in other countries are performed by private enterprises in Hong Kong (Krause 1988). Basic public utility companies in Hong Kong, such as electricity and transport providers, are in private hands but under government regulation (Riedel 1974). Most of these companies, such as Hongkong Electric Company, China Light & Power Company, Hong Kong Telephone Company, China Motor Bus Company, Hong Kong Tramways, Star Ferry Company, and Yaumati Ferry, are controlled by large private conglomerates and listed on the Hong Kong stock exchange (Ngo 1996; Far Eastern Economic Review 20 December 1956). According to the idea of positive noninterference, financial firms operate at their own risks (Hong Kong Hansard 4 November 1987, 220). Therefore, the use of its SWF for banking bailouts would contradict the official government philosophy of nonintervention (Hong Kong Hansard 7 June 1985, 1185).

Unlike Hong Kong, Singapore's state has followed a highly interventionist approach. Numerous articles have highlighted the central role of Singapore's state in economics and have emphasised the dominant role of government-led enterprises (e.g. see Low 2005). Through its government-linked enterprises, Singapore's state has been involved in almost every sector of economic activity, notably the transport sector (e.g. Singapore Airlines, Singapore General Aviation Service), leisure industries (e.g. Jurong Bird Park, Singapore Zoo), the food industry (e.g. National Grain Elevator, Sugar Industries of Singapore), engineering (e.g. National Engineering Services), heavy industry (e.g. United Industrial Corporation, National Iron), and chemicals (e.g. Chemical Industries Far East) (The Business Times 3 September 1979). Especially in the finance sector, Singapore's state has had a strong presence via the Central Provident Fund, the Development Bank of Singapore, and the Post Office Savings Banks. Because of its strong presence, Singapore's

government has often been portrayed as intrusive (e.g. see, Lee and Low 1990). Consequently, the use of Singapore's SWFs for bailing out finance institutions during periods of financial pressure would be in line with Singapore's state tradition in economic policy.

Singapore and Hong Kong's policy responses to financial pressures during the 1960s through the 1990s should be reflections of their different state traditions. In the case of Singapore, the expectation would be for a hands-on approach toward bailing out companies, while in Hong Kong, it would be for a hands-off approach toward using public money for financial bailouts. Interestingly, the observed responses in Hong Kong and Singapore are the opposite of what would be expected according to their differing state traditions. In Hong Kong, finance has been one of very few sectors in which the government intervened heavily during the 1960s through the 1990s by spending more than HK$200bn on bailouts via its SWF.[7] In stark contrast, and despite its capability for bailing out firms via its SWFs, Singapore opted for a hands-off approach, instituting bailout policies that were carried by the entire private sector.

5.1. Hong Kong

Hong Kong's banking system was fragmented during the 1960s through the 1990s. It consisted of (a) note-issuing banks; (b) foreign banks, notably from the UK; (c) locally incorporated banks; and (d) banks from mainland China. The Hong Kong Bank and Standard Chartered were Hong Kong's most important note-issuing banks. The Hong Kong Bank's deposits made up a significant part of total deposits (Hong Kong Banking and Finance Handbook 2009). The Hong Kong Bank also acted as the banker to the government. Domestic banks, notably the Bank of East Asia, frequently opposed the privileges of the Hong Kong Bank (A. Burns, personal communication, October 25, 2013). Another group of banks was associated with foreign banks, from such countries as China, the UK, and the US. Their main purpose related to the financing of trade and commerce with their respective countries (Mc Carthy 1982). One implication of this fragmentation and of their differing exposures to different asset classes was the lack of a unified voice in the policy-making processes.

This fragmentation was reflected in their political organisation on important advisory committees, notably the Exchange Fund Advisory Committee. This committee is the major access point for socioeconomic actors to affect the operations of the Exchange Fund (Hong Kong Hansard 26 March 1969, 207). It was created under Section 3(1) of the Exchange Fund Ordinance, which "requires the Financial Secretary to consult the Committee in his exercise of control of the Exchange Fund" (Hong Kong Monetary Authority Quarterly Bulletin, May 1995, 6). It became practice to appoint leading commercial bankers to this committee (Hong

[7] Another area of public intervention referred to the provision of public housing.

Kong Monetary Authority Quarterly Bulletin, May 1995). For example, during the mid 1980s, members included only the Financial Secretary, the Secretary for Monetary Affairs, and the chief executives of the note-issuing banks, notably the Standard Chartered and the Hongkong Bank (see Table 5). Interestingly, the Financial Secretary at that time, who appointed the Exchange Fund Advisory Committee members, was himself a previous board member of the Hongkong Bank (Goodstadt 2005). The Hong Kong Bank's dominant market position was also reflected in its strong organisation on policy-making structures, which affected the operations of the Exchange Fund.

State-society relations in which few banks have strong individual connections to government led to unbalanced bailouts. The bailouts were unbalanced in the sense that the full burden was carried by the government via its SWF. This supports Woll and Grossman (2013), who highlight that bailout policies can be explained, not solely on grounds of financial stabilisation, but also as a result of state-business relations. For example, the use of the Hong Kong Exchange Fund for compensating domestic banks in the late 1960s and early 1970s was not in line with such a financial-stability explanation. Such an explanation would emphasise that the compensation payments were necessary in order to stabilise the financial market and rescue institutions, which are of systemic importance. Yet the use of the Exchange Fund to compensate Hong Kong banks created new problems. As a consequence of these compensation payments, the assets of the Exchange Fund did not meet their liabilities in the context of a transferable currency at a fixed rate with respect to another currency (Foreign and Commonwealth Office 1974). The Exchange Fund cover for the currency-note issue in 1973 was only 81.49 percent as compared to the 117 percent cover in 1972 and the 138 percent cover in 1971 (Foreign and Commonwealth Office 1974, 2). Consequently, Hong Kong failed to maintain a 100 percent currency backing in 1973 (Foreign and Commonwealth Office 1974, 2). It was noted that this shortfall in currency backing was the "most closely guarded secret in Hong Kong" and that "this could have a disastrous effect" on Hong Kong's economy (Foreign and Commonwealth Office 1974, 2).

Table 5, Members of the Hong Kong Exchange Fund Advisory Committee (1967 – 1997).

Years	Policy Maker	Banks	Others
1967-1985	Financial Secretary, Secretary of Monetary Affairs	Hong Kong Bank Standard Chartered	Accountant General
1986-1989	Financial Secretary, Secretary of Monetary Affairs	Hong Kong Bank Standard Chartered Bank of East Asia	LegCo, Accountant
1990-	Financial Secretary, Secretary of Monetary Affairs	Hong Kong Bank Standard Chartered Bank of East Asia	Academic LegCo, Accountant
1991-1992	Financial Secretary, Secretary of Monetary Affairs, Director from the Office of the Exchange Fund	Standard Chartered, Bank of East Asia, Hong Kong Bank	Academic LegCo, Accountant
1993-1997	Financial Secretary, Monetary Authority (ex officio)	Standard Chartered Bank of East Asia Hong Kong Bank Hang Seng Bank Bank of China	Academic Hong Kong Future Exchange, Accountant, Legco

Sources: Civil and Miscellaneous Lists Government between 1967 and 1997.

A situation in which the access to policy-making is heavily biased towards a few actors makes collective action in the financial sector difficult. Only a small group of actors was involved (Hong Kong Hansard, 27 March 1986, 911). Domestic banks, notably the Bank of East Asia, had been not included on the Exchange Fund Advisory Committee until 1986 (see Table 4). But even after the inclusion of the Bank of East Asia on the Exchange Fund Advisory Committee, its CEO, David Li, continued criticizing the bailouts, particularly that of the Hong Kong Future Guarantee Corporation (Hong Kong Hansard, 4 November 1987).

The Exchange Fund's capital injection to the Future Guarantee Corporation raised for David Li the question of "[w]ho are the actual winners in this recent crisis?" (Hong Kong Hansard, 4 November 1987, 220). Li indicated that the consortium of banks, which were the major shareholders of the Future Guarantee Corporation, notably the Hongkong Bank, Standard Chartered, and international banks, might have been able to keep the Future Guarantee Corporation solvent without the support of the Exchange Fund (Hong Kong Hansard, 28 October 1987, 152; 4

November 1987). However, policy-makers feared that the collapse of the Future Guarantee Corporation would affect Hong Kong's futures exchange, which had close links to Hong Kong's stock exchange. They argued that this would have a damaging effect on Hong Kong's currency and its reputation as an international financial centre (Hong Kong Hansard, 11 November 1987). As such, the use of the Exchange Fund to bail out the Future Guarantee Corporation might have been theoretically overdetermined.[8]

The use of the Exchange Fund for bailing out financial institutions was also reflected in Hong Kong's regulatory environment. Hong Kong's stock market and banking sector were weakly regulated and prone to speculation, particularly in the highly profitable real estate sector. The establishment of new financial firms in Hong Kong has been unrestricted, which has allowed all kinds of undercapitalised firms to enter the banking market (Jao 1993). After each crisis up until the 1980s, scholars, such as McCarthy (1982) and Jao (1993), highlight there was no substantive regulatory tightening in Hong Kong's financial sector.

The fact that Hong Kong's finance system did not dispose of a deposit-insurance scheme, combined with the lack of regulation, put further pressure on Hong Kong's policy-makers to bail out the banks via the Exchange Fund. Such an insurance scheme might have protected people's savings in the case of a banking crisis. This was indicated by the Financial Secretary (Hong Kong Hansard, 9 April 1986). The Financial Secretary's statement that "[i]f a system of deposit insurance existed in Hong Kong the problems might be somewhat mitigated" indicates an awareness of regulatory deficits in the banking sector (Hong Kong Hansard, 9 April 1986, 983). However, Hong Kong's banking sector heavily opposed such a deposit-insurance scheme because it would have increased the operating costs of banks.

5.2. Singapore

Singapore's banking sector is one of the most concentrated banking systems in Asia. It has been dominated by four locally incorporated banks: the Overseas China Banking Corporation, the Overseas Union Bank, the United Overseas Bank, and the Development Bank of Singapore. In contrast to other countries, the number of banks in Singapore has been controlled, and the government promoted the consolidation of the banking sector through a number of mergers. Unlike Hong Kong, the state has also been an active agent in Singapore's banking sector via its stakes in the Development Bank of Singapore and the Post Office Savings Bank. Parallel to this, Singapore's state enjoyed high levels of autonomy from the private commercial banking sector through a robust alliance between political executives and senior

[8] An outcome is overdetermined when it is determined by multiple distinct causes, where the causes are "on par" with respect to the outcome (Schaffer 2003, 23).

civil servants on key committees (Schein 1996). Particularly in the early 1980s, Singapore's policy-makers distanced themselves from commercial banks. The Minister of Finance's statement that "[the MAS] should keep a certain distance from commercial banks" and should avoid "fraternizing too much with bankers" indicates the political will toward high levels of autonomy (The Straits Times, 1 August 1982).

The Asset Management Committee was the major access point for influencing the allocation and usage of Singapore's Currency Fund. Publicly available evidence, notably reports from the International Bureau of Fiscal Documentation (International Bureau of Fiscal Documentation Bulletin, April 1985) and secondary sources, such as Hamilton-Hart (2002), suggest that no members from the private banking sector were included on this committee. Unlike in Hong Kong, the Asset Management Committee in Singapore was primarily appointed with government officials, notably from the Ministry of Finance (Hamilton Hart 2002; International Bureau of Fiscal Documentation Bulletin, April 1985). It was chaired by the Minister of Finance, and members included the Permanent Secretary for the Revenue Division from the Ministry of Finance, the Permanent Secretary of the Development Division from the Ministry of Finance, the Accountant General, and the Managing Director of the MAS (International Bureau of Fiscal Documentation Bulletin, April 1985, 156).

Singapore did not use its SWF for bailing out financial firms during periods of financial pressures but instead opted for responses that were carried by the financial sector. During the Pan Electric crisis, for example, policy-makers were determined to find an institutional mechanism which would be carried by major financial actors (Hwang 2007). This plan was quickly formed and implemented (Hwang 2007). Under the chairmanship of a senior government official, top executives of Singapore's four banks managed to set up a lifeboat fund (Far Eastern Economic Review, 8 May 1986). This fund was an external pool of funds that provided solvency to troubled firms. Stockbrokers could draw on this credit line under a set of strict conditions. Stockbrokers had to contribute a new levy based on the commissions they earned from their trades, which would flow toward the lifeboat fund. As such, the costs of this res- cue scheme were transferred to the stockbroking industry.

Parallel to this, Singapore's policy-makers tightened regulation for financial actors in Singapore's stock market. Until the Pan-El crisis in 1985, the Stock Exchange of Singapore was lacking in regulation; there were no minimum capital requirements, no limits on investments, and no systematic surveillance (MAS 2011). This made it difficult to assess the level of risk to which stockbrokers were exposed. Following the Pan-El crisis, the government revised the Securities Industry Act and the MAS took over regulation of the Stock Exchange. Under the guidance of the MAS, banks took over the fragmented brokerage system in Singapore (Hamilton Hart 2002). These measures improved the Stock Exchange position, particularly during the global stock markets of 1987 (MAS 2011).

The political organization of banks, together with high levels of state autonomy, affected Singapore's approach to regulation as well as to the use of its SWFs. During the 1960s through the 1980s, Singapore's banking system was considerably more con- trolled and regulated than Hong Kong's (Mc Carthy 1982). Excessive direct investments in any financial or other undertaking were prohibited (Ishihara and Kim 1982). As the MAS has developed its regulatory role, the banks have been held to increasingly strict standards. The MAS tightened prudential controls in the 1980s, even before the comprehensive Banking Act of 1984 (Hamilton Hart 2002, 97). It also imputes a bigger monitoring role to auditors, which are obliged to inform the MAS in any case of a breach of the Act (Business Times, 29 December 1984). The MAS requires all banks to keep and maintain credit files on customers, and encourages banks to write off or make provision for bad or doubtful loans as early as possible. Written approval is required from the MAS before any loan connected with a director of a bank or an employee can be written off the books (Far Eastern Economic Review, 4 July 1985). As a consequence of the tight regulation, banks in Singapore had a low level of nonperforming loans and high capital-adequacy ratios (Hamilton Hart 2002).

The debates about approaches toward bailing out financial firms were controversial in Hong Kong as well as in Singapore. These controversies suggest the availability of alternative options and draw attention to the linkage between the political organisation of actors and the use of SWFs. While in Singapore the debates centred around issues of overregulation, in Hong Kong the debates revolved around the use of the Exchange Fund. The prudential regulation pursued by Singapore's policy-makers during the 1980s was "highly unpopular" with the financial sector (The Straits Times, 13 April 1985). In Hong Kong, by contrast, the bank bailouts via the Exchange Fund met considerable criticism, particularly from Hong Kong's manufacturing sector (Hong Kong Hansard, 14 January 1987, 730; 4 November 1987, 237). An industrialist's statement that "too much attention is paid to [the banking sector]" suggests opposition towards the use of the SWF (Hong Kong Hansard, 14 January 1987, 730). Opponents of the bailouts questioned the real purpose of the Exchange Fund and the "real winners" (Hong Kong Hansard, 4 November 1987, 220; 7 June 1985, 1188). According to Hong Kong's manufacturers, the Exchange Fund should stimulate the economy instead of bailing out distressed banks (Hong Kong Hansard, 11 March 1970, 429.). The statement that "[i]f a similar amount has been spent in support of industrial development, the longer-term benefits to Hong Kong's industrial competi- tiveness might be equally great, if not greater" underlines the critical position of industrialists vis-à-vis the use of Exchange Fund assets (Hong Kong Hansard, 4 November 1987, 237).

6. Conclusion

The Hong Kong-Singapore comparison shows that similar exposures to financial pressures can lead to different policy responses. During the late 1960s through the 1990s, both city-states' economies disposed of similar bailout capacities via their large SWFs. But only Hong Kong used its SWF repeatedly for bailing out financial

firms; in Singapore the bailouts were carried by the private sector.

While in Hong Kong the use of the SWF was structured around the preferences of a small number of well-connected banks, in Singapore, policy responses were widely negotiated and carried by the whole sector. Hong Kong did not have a banking industry which was sufficiently homogenous and interconnected to foster collective action, whereas Singapore's banks managed a collective response under governmental leadership.

This article finds that the use of SWFs during financial pressures are the result of the political economy of a country, and not primarily related to the magnitude of the financial crises. Like central banking institutions, SWFs exhibit differing degrees of independence and autonomy. It is important to assess the type of autonomy that SWFs possess in order to understand the potential uses of SWFs in contexts of economic pressures.

However, it seems that it is not only the political organisation of banks, along with levels of state autonomy, that affects the use of SWFs, but also the broader regulatory environment. This article suggests a nexus between the use of SWFs and the regulatory environment, notably the existence of depositor-insurance schemes. The absence of such schemes during periods of financial crises put pressure on governments to bail out banks. This nexus is of critical importance for future research. The use of SWFs will be very critical in many economies that have not implemented explicit deposit- insurance schemes, such as China, Qatar, and the United Arab Emirates.

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