ENTREPRENEURSHIP AND INTERNATIONALISATION SUBCOMMITTEE ECONOMIC REVIEW COMMITTEE

RECOMMENDATIONS ON GOVERNMENT IN BUSINESS

30 MAY 2002

MAIN REPORT

Introduction

1 When Singapore became independent, the private sector was too weak to provide much needed jobs and to support economic growth. Government therefore stepped in as state entrepreneur, creating Government-Linked Companies (GLCs) and Government agencies to provide services critical to the growth of the economy, such as in development banking, aviation, telecommunications, port, and power. Singapore Airlines was created through the de-merger of Malaysia-Singapore Airlines shortly after Singapore's separation from Malaysia. SembCorp Marine was set up using naval facilities left behind by the British. GLCs are now an important part of the Singapore economy, contributing about 13% of Singapore's GDP.

2 This model was necessary in the initial stages of our economic development, and has worked well. GLCs are not like State-Owned-Enterprises found in some countries that are a drain on the nation's resources. They are professionally run. Many of them are listed on the stock exchange, have reputable brand names, and are profitable.

3 Singapore has entered a different phase of development and the challenges are different today. Unlike in the past where GLCs were put in place for economic growth and to fill market gaps, the private sector is now much more sophisticated. The market functions well in allocating most resources and responding to demand conditions. Business environment now is fast changing and competition is driven by continuous innovation. It is private enterprise, and not the Government, that is the most knowledgeable about and best able to exploit evolving market trends and technologies.

4 Our current priority must be to grow our external wing by encouraging Singapore-based enterprises to globalise their operations. We need to harness the entrepreneurial spirit in the economy to succeed. The Government's participation in the economy had certain strengths, which can be retained and leveraged upon to tackle these new challenges.

5 In line with this, the Entrepreneurship and Internatonalisation Subcommittee (EISC) recommends the following for the Government, Temasek Holdings, and individual ministries and statutory boards.

Recommendations

Government

6 The Government no longer needs to take a hands-on approach by involving itself in businesses. It should encourage the private sector to be at the frontier of developing new business ideas. Its primary role is to ensure a level playing field and provide opportunities for all enterprises to have a fair chance to succeed. It should intervene only under exceptional circumstances, such as market failure. We recommend that the Government adopt the following:

Enact a generic competition law

7 The EISC welcomes the Government's recent announcement to enact a generic competition law and set up an independent competition authority in 2-3 years.

8 Singapore does not have a generic competition law to prohibit cartel activities like price fixing and market division, and abuse of dominance by significant market players. We have enacted such rules only for specific sectors, like energy and telecommunications, which are more prone to anti-competitive behaviour. A generic competition law that covers all sectors will institutionalise and give teeth to Government's longstanding pro-competition policy. It will form part of our enabling infrastructure for entrepreneurship and ensure fair play between all enterprises, including multinational companies (MNCs), GLCs and small and medium sized enterprises (SMEs).

9 However, competition law should not impose a new layer of regulation and burdensome compliance costs to businesses. In many countries, overlapping jurisdiction between competition authorities and regulators can lead to confusion and uncertainty to businesses.

10 To prevent this, we must make clear distinctions between competition law and regulation. First, the action of a competition authority is often a one-time structural rectification of the market, such as breaking up a monopoly, or dismantling a cartel, while sectoral regulators will referee the conduct of market players continuously at the micro level. Second, regulation is often *ex ante* – meaning that regulators will require market players to seek approvals before they can act. Competition law is *ex post* – it allows market players to operate freely in the market, taking action only when they overstep the line. Competition law is therefore

regulation with a much lighter touch, and more pro-enterprise in nature. Where there is overlapping jurisdiction between competition authority and sectoral regulators, there must be a clear process to resolve them expeditiously and not burden businesses with uncertainty.

11 The EISC proposes the following key elements of the generic competition law:

a) Comprehensiveness. All sectors of the economy and all enterprises, MNCs, GLCs, SMEs, should be subject to competition law.

b) Continuous review. All laws that restrict competition will be continuously reviewed.

c) Equality of access. All companies will have equal access to critical national infrastructure, such as roads, telecommunications and power distribution network.

d) Anti-collusion. Collusion, bid rigging, price fixing, which involve co-ordinated actions by different market players, should be criminalised.

e) Abuse of dominance. Competition law should not be against dominance – as this is a legitimate motivation of all businesses – but we should prohibit abuse of dominance, e.g. such as using predatory pricing to exclude new entrants.

f) Mergers and Acquisitions. Transactions of certain thresholds either in value or resulting market share should be pre-notified to the Competition Authority. The Authority will assess the competitive implications of the merger. However, we should keep this process as simple as possible so as not to discourage industrial consolidation and restructuring.

g) Penalties. There should be a schedule of penalties for violations of competition law, including stipulations on which offences will be considered criminal offences.

h) Exemptions. Certain activities done in national interest should be exempted from the law. These could include collective wage bargaining, setting of essential charges such as public transport fares, activities to promote cluster-based development and international competitiveness.

12 Generic competition law will institutionalise a regime where GLCs do not enjoy unfair privileges, and must compete on equal footing in the market, just like any other commercial entity. The Government's approach to govern GLCs should be in line with this policy. We propose that the Government abide by the following principles in setting up and maintaining GLCs.

Establish and maintain GLCs to manage critical resource, achieve public policy objectives, or develop new growth engines

13 Businessmen have expressed concern that over the years, the number of GLCs has grown to cover many industries, encroaching into the private sector space. The government should be involved in business only where it achieves its strategic objectives. These include the following:

a) Management of critical resource – where ownership is critical to Singapore's economic prosperity, such as the airport or seaport; or where provision of a good or service is a natural monopoly, such as the distribution of power and desired outcomes may not be assured through market regulation;

b) Public policy objectives – where ownership enables the government to provide services that achieve public policy objectives for the public good, such as to ensure affordable health care, education and housing; and

c) Develop new growth engines – where private enterprises are unable or unwilling to participate because the risks are high or the gestation period is too long, but the growth potential can be enormous. One example is the life sciences.

14 Notwithstanding the above, the Government's participation in the new growth sectors should end when the private sector is ready to assume its proper role. When developing new growth engines, the Government should at the outset consider other ways of involving the private sector instead of resorting to setting up and owning GLCs. This could be done through incentives to attract private sector participation, or co-investing

with private sector parties. Even if the Government has to set up a GLC, there should be some form of private sector participation. Such an approach will ensure better commercial discipline.

<u>Ensure that GLCs are commercially run and eschew national service by GLCs</u>

15 Government should not interfere with the operations of GLCs, and should ensure that they are commercially run. In exercising its rights as a shareholder to appoint members to the board of directors, it should choose those who contribute best to the businesses of the GLCs. The Government should not accord GLCs subsidies and special privileges. Conversely, GLCs should not be asked to perform 'national service', which is defined broadly as any project or activity that they would not have done if it was evaluated purely on a commercial basis.

16 If the government needs to achieve certain national policy objectives through GLC, it should do so without undermining the commercial discipline of the GLCs. The restructured hospitals are a good example of this. They are run commercially and have to break even. This ensures that they have the incentive to be efficient and productive but at the same time their patients benefit from well-defined government subsidies.

<u>Review constantly the stable of GLCs and divest non-strategic ones</u>

17 The Government should constantly review the stable of GLCs and keep only those that serve strategic purposes.

18 As for the non-strategic GLCs, Government should divest them. However, it does not make sense to sell them if the capital market conditions are not right, or the buyer is not capable of overseeing and growing them. We should not divest for divestment's sake. Where there is no suitable buyer, it is better for Government to retain its stake to drive the growth of the GLCs.

<u>Encourage a culture of partnership</u>

19 There are certain industry clusters in Singapore where no one enterprise has all the necessary competencies to compete abroad. As a result, individual enterprise makes its own foray into the same foreign markets. The larger GLCs may be able to clinch good deals, but if they were to partner other Singapore enterprises with complementary skill sets and compete abroad as a pack, the impact could certainly be greater.

20 It is not a new concept, EDB has adopted a cluster approach in attracting MNCs to Singapore and this has served us well over the years. A similar approach for international expansion should be just as workable.

21 But left on their own, the private sector is unlikely to forge such industry clusters. There is therefore a role for agencies such as IE Singapore and SPRING to identify and catalyse the development of specific industry clusters. We can start with promising ones, such as aviation, maritime, telecommunications and media, land transport, infrastructure and engineering, technology and electronics, finance and real estate, food and resources.

22 Government agencies could bring together complementary players to work together. In particular, IE Singapore will need to build up cluster enabling capabilities, provide an information platform to help access foreign markets, and navigate foreign bureaucracy. It should identify key companies that are capable of leading the pack in overseas ventures. To do so, IE Singapore should partner Temasek closely. IE Singapore is therefore like a 'reverse EDB' – instead of attracting MNCs to Singapore to anchor the development of industry clusters, it facilitates the outward expansion of Singapore based industries.

23 In line with this, trade missions should be organised along cluster lines. There should be post-mission follow up to capitalise on the bonding fostered among the participants.

24 Permanent intra-cluster associations should be formed to promote industry development, conduct research, interact and network. These should be privately run associations, but they can qualify for Government funding if certain targets are achieved. Government Research Institutes could be roped in as members of these associations. An excellent example is SEMATECH, the semiconductor cluster which was formed this way.

<u>Raise profile of Local Industry Upgrading Programme (LIUP) and expand it to promote globalisation</u>

25 A good scheme to help foster partnership is the LIUP. The LIUP is a grant scheme to encourage MNCs to help upgrade SME vendors. The SMEs will benefit from the transfer of technical, operational and management skills, while the LIUP partners would benefit from a reliable and dependable pool of suppliers. Central to this partnership is the LIUP Manager, typically an employee of the LIUP Partner, who will plan and

execute the upgrading programme for the vendor. The Government assists by funding the cost of the LIUP Manager.

26 While the LIUP has over the years evolved to cover the statutory boards and GLCs, this is not well known by the private sector. Out of the existing 90 LIUP partners, only 12 of them are statutory boards and GLCs.

27 We recommend taking steps to raise the profile of the LIUP, and highlight the possibility of larger Singapore enterprises helping to upgrade SMEs. We should expand the LIUP to cover instances where GLCs and larger local enterprises lead a cluster of enterprises, including SMEs, to venture overseas.

28 This will encourage GLCs and larger local enterprises to provide a 'beachhead' in penetrating foreign markets and bringing other SMEs in their tailcoats. The bigger enterprises can provide various support to the SMEs and save them time and resources in conducting market research, due diligence, and corresponding with foreign government agencies. Given the overall cost savings, the Government should implement an incentive scheme to encourage larger enterprises to play this role.

Temasek Holdings

29 Temasek Holdings was formed in 1974 to hold Government investments. Although it is not involved in the daily operations of GLCs, it has oversight over key appointments, the strategic outlook and governance of GLCs. In so doing, Temasek Holdings should seek to maximise shareholder’s return in the long term. It should benchmark the performance of its GLCs against industry peers – domestically, regionally and globally. The EISC recommends the following for Temasek Holdings:

<u>Focus GLCs to internationalise their core businesses</u>

30 GLCs are natural candidates for internationalisation given their size, depth of management and competencies build up over the years. Temasek Holding’s key mission should be to grow GLCs into globally competitive enterprises that are anchored in Singapore. Temasek Holdings should compel GLCs to scale up their core competencies to build global businesses, as oppose to concentrating on the local market to build a diverse range of unrelated businesses.

31 International expansion can be done through acquisition of existing foreign companies that strengthens the core businesses. This is an

important strategic complement to organic growth. Temasek, however, must ensure that its companies can effectively manage, digest and exploit what have been acquired. A good example is Neptune Orient Lines establishing a global presence through the acquisition of American Pacific Line. There are also success stories by the private sector, such as City Development's acquisition of foreign hotel chains.

32 In cases where a dilution of its stake in GLCs is necessary for the GLCs to grow their businesses out of Singapore, Temasek should be prepared to do so. The international expansion of Singapore Telecoms and Development Bank of Singapore are cases in point. Temasek should be prepared to cede control in GLCs where it makes commercial sense. This way, GLCs can also benefit from a broader shareholding base when trying to access capital markets for future acquisitions.

Explore various ways of divestment

33 Besides initial public offering and trade sale, other methods of divestment should be given due consideration. For example, management leveraged buyouts would give the people who are already familiar with the business the opportunity to grow the company. This helps ensure that expertise in that industry is not lost but further developed.

Review constantly its stable of GLCs

34 Temasek Holdings should review its stable of GLCs constantly, and be prepared to rationalise, consolidate or divest them where it makes commercial sense and benefits shareholders.

Attract world class talent into GLCs

35 Temasek should make a conscious effort to cast a wide net to attract world class managerial talent into GLCs. This should not be confined to the appointment of Chief Executive Officers and board members but also upper management – so that best practices in management can percolate down the ranks. Conversely, under-performing board members and management staff should be removed. Temasek should carry out rigorous succession planning and leadership development across all GLCs.

Ministries and statutory boards

36 The primary role of many Government agencies is to regulate and promote certain industries in an impartial manner, and ensuring a level

playing field to all market players. In carrying out their missions, many statutory boards also set up enterprises. These are technically not GLCs, but are nonetheless fully or majority owned by statutory boards to either address certain market failures, or instill commercial discipline in some of the statutory board's functions.

37 There must however be rules governing the setting up of enterprises under statutory boards. If not done correctly, this can give rise to a conflict of interest and economic distortions. Statutory boards can also encroach into the space of the private sector and detract from Government's enabling role to provide development opportunities for the private sector. The EISC therefore proposes that statutory boards abide by the following disciplines when setting up enterprises:

<u>Do not set up enterprises to provide services that the private sector can provide</u>

38 We recommend that the Government institute a 'yellow pages' rule. This means that statutory boards should not set up enterprises when there are private sector players that are providing or able to provide the service. In fact, statutory boards should seize such opportunities to provide business opportunities to the private sector.

<u>Do not corporatise or privatise regulatory functions</u>

39 Statutory boards should as far as possible not corporatise regulatory functions because these are often monopoly functions and will lead to rent seeking by the enterprise. Further, it will not be in the enterprise's financial interest to review and trim down regulations, as this will mean loss of revenue in fees and charges. This goes against our effort towards liberalisation and deregulation. If indeed the corporate form is deemed as the best structure to carry out its regulatory functions, then it must run on a non-profit basis.

40 In a similar vein, it will be better to keep activities of statutory boards that are strategic to their missions as a public function, even if the activity can be structured to attract a commercial return. We should not corporatise for corporatisation's sake.

<u>Make a conscious effort to divest enterprises owned by statutory boards</u>

41 Even if setting up an enterprise under a statutory board is necessary, there should be proactive plans to encourage private sector to

take over the function. Criteria should be set to monitor the emergence of private sector equivalents, so as to divest the enterprise when the private sector is ready.

Conduct mandatory periodic housekeeping

42 In any case, there should be a mandatory periodic housekeeping, say every 3 to 5 years, of all enterprises set up by ministries and statutory boards to decide which to divest and which to keep.

Avoid allegations of conflict of interest

43 Statutory boards should avoid subjecting themselves to allegations of conflict of interest. They should ensure that the enterprise does not utilise the name of the statutory board in the domestic market, and that the board of directors is independent of the management of the statutory board.

Do not grant best of both worlds deal

44 Further, the enterprise should not enjoy a moratorium on its domestic business from the government while at the same time being allowed to compete with the private sector in that market segment.

Outsource more Government functions to the private sector

45 A viable alternative to setting up enterprises is to outsource functions to the private sector. Where agencies are not willing to outsource, there should be proper justifications, such as national security or confidentiality concerns. We recommend a systematic reduction of activities by each agency, and setting targets to achieve this. This way, all agencies will think of ways to develop the outsourcing industry.

Provide test beds for SMEs' products and services

46 To support the outsourcing effort, Government should have a more open mind when procuring goods and services. Nokia was a beneficiary of such a policy adopted by the Finnish government. The success of Nokia has in turn fed 300 first-tier suppliers.

47 There are some good examples in Singapore too. The Public Utilities Board, for example, contracted an SME to use ‘bioscrubbers’ which can better filter and treat sewage air at sewage facilities. This resulted in a

safer working environment and lower operating cost. The company is currently conducting research to upgrade its product. The Government has also adopted the Diagnostic Tutorial and Assessment system developed by an SME. This is a web-based system, self-learning and self-assessment system which can improve the learning process and help reduce teachers' marking time.

48 The few success stories notwithstanding, the feedback is that many SMEs often fail to qualify for Government tenders because agencies are not prepared to try them out due to the lack of track record. As a result, there have been cases of SMEs being awarded contracts by MNCs but are unable to secure contracts from government agencies.

49 We should maintain the current principles of Government procurement, which is openness, non-discrimination and value-for-money. Nevertheless, we believe there is scope for all government agencies to review their procurement practices so that products and services offered by SMEs are not automatically ruled out simply because they do not have the necessary track record. To illustrate, tender specifications should not be skewed in favour of standardised products and services such that innovative solutions from SMEs would never qualify. SMEs may well give us better value-for-money solutions.

Conclusion

50 The EISC welcomes the Ministry of Finance's recent announcement to issue a Temasek Charter. The Charter should set out clearly the principles and approach towards setting up and maintaining GLCs. It should serve to institutionalise a regime that allows GLCs to operate independently of the Government and solely on commercial considerations. This is fundamental to the profitability and value of GLCs, from which we should leverage to grow our external wing.

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