

PART I : PAST PERFORMANCE, CHALLENGES & OPPORTUNITIES, AND SINGAPORE'S COMPETITIVE EDGE

INTRODUCTION

In April 1985, the Economic Committee was set up to review the progress of the Singapore economy and set directions for its longer-term growth. One of the committee's key recommendations was for Government to promote services as actively as the manufacturing sector, and make both the twin engines of Singapore's economic growth. The specific recommendations of the Economic Committee on the services sector are listed in Box 1.

Box 1: Recommendations of the Economic Committee on Promotion of Services

- There should be equal emphasis on both manufacturing and services, the twin engines of future growth.
- We should depend both on the growth of local companies and on an open-door policy to attract international service companies.
- Special attention should be given to helping local service companies improve their expertise. Local companies should not rely on protection to guarantee them a share of the domestic market. Nor should foreign companies be coerced to form partnerships and joint ventures with them. Instead, local companies must improve their expertise so that foreign companies will be induced to go into joint ventures with them.
- Biases in our fiscal incentives should be removed so that service companies are also eligible for existing tax incentives. New tax incentives should be introduced for the services sector.
- The (then) Business Enterprise Committee should actively review rules, regulations and legislation which could stifle the growth of certain service industries.
- Government-owned service companies should be effectively privatised.

Extracted from "The Singapore Economy: New Directions", Report of the Economic Committee, Feb 1986

2 This strategy was reaffirmed in the 1998 report of the Committee on Singapore's Competitiveness, which envisioned Singapore as the premier services hub in Asia, with a global orientation (Box 2).

Box 2: Strategy for Development of Services Sector by the Committee on Singapore's Competitiveness

“Complementing the manufacturing sector, we should build Singapore into the premier services hub in Asia with a global orientation. We must grow our existing hub services like financial and maritime services and develop new high growth areas in IT and media services. To support services as the twin engine alongside manufacturing, we need a new services paradigm in our overall policy and regulatory framework where intangible factors like creative and innovative ideas are given greater weight.”

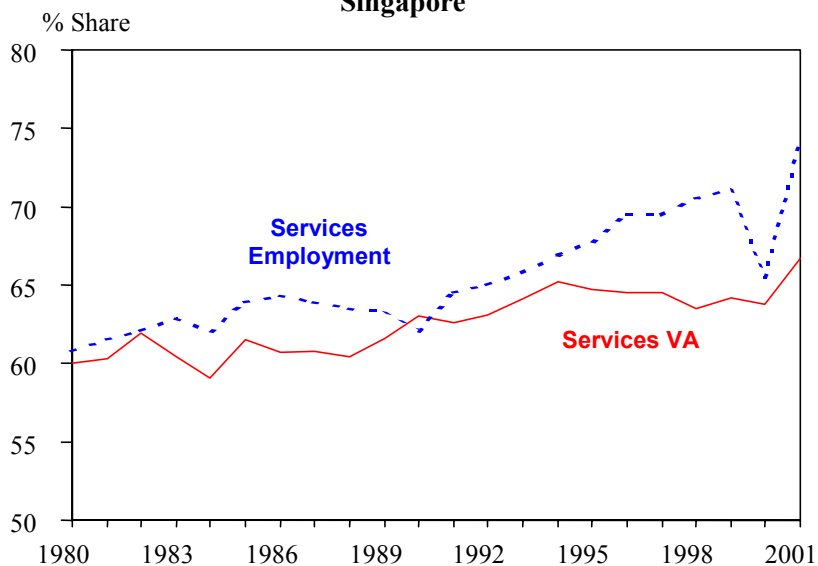
Extracted from Report of the Committee on Singapore's Competitiveness, Nov 1998

3 The work of the Economic Committee and the Committee on Singapore's Competitiveness provided the reference for the deliberations of the ERC Subcommittee on Service Industries. Building on the foundations laid, the Subcommittee looked at the new directions and strategies needed to drive our service sector forward, taking into account prevailing global trends and changes in the economic environment.

GROWING IMPORTANCE OF THE SERVICES SECTOR

4 Over the years, the services sector has assumed greater importance in our economy. The share of services in our GDP has been on the rise since the mid-1980s, from 61% in 1986 to 67% in 2001 (Fig 1). Its share of total employment has also increased from 64% to 74% over the same period.

Fig 1: Services Share of GDP and Employment in Singapore



5 This is a phenomenon that is not unique to Singapore. Many developed countries such as the US, UK, France, Germany, and Japan have also experienced a rising share of services as a proportion of GDP and employment as their economies matured (Figs 2(a) and 2(b)). Compared to the other countries, the services' share of GDP in Singapore is lower than in most developed economies, except for Japan, Finland and Korea. (Fig 3).

Fig 2a: Services' Share of GDP

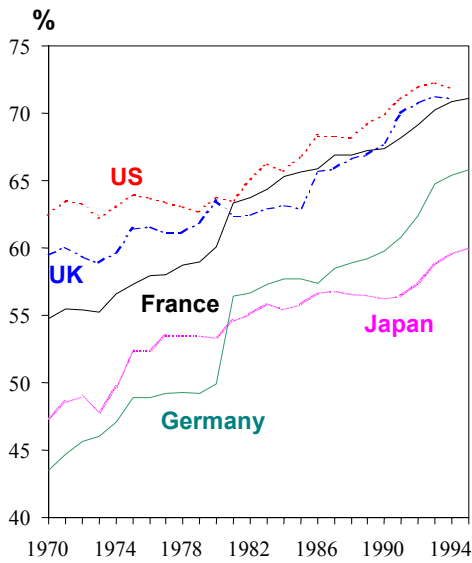
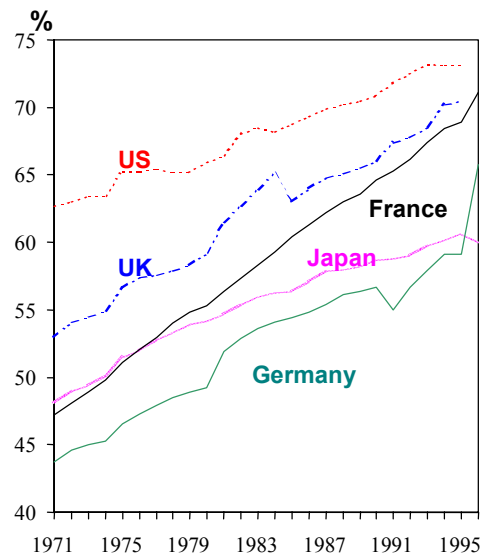
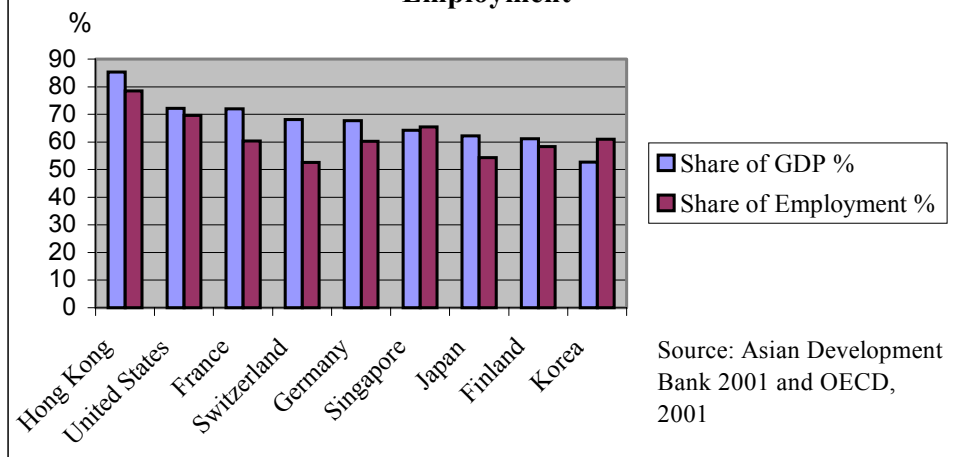


Fig 2b: Services' Share of Employment



Source: OECD Historical Statistics, 1960-1995

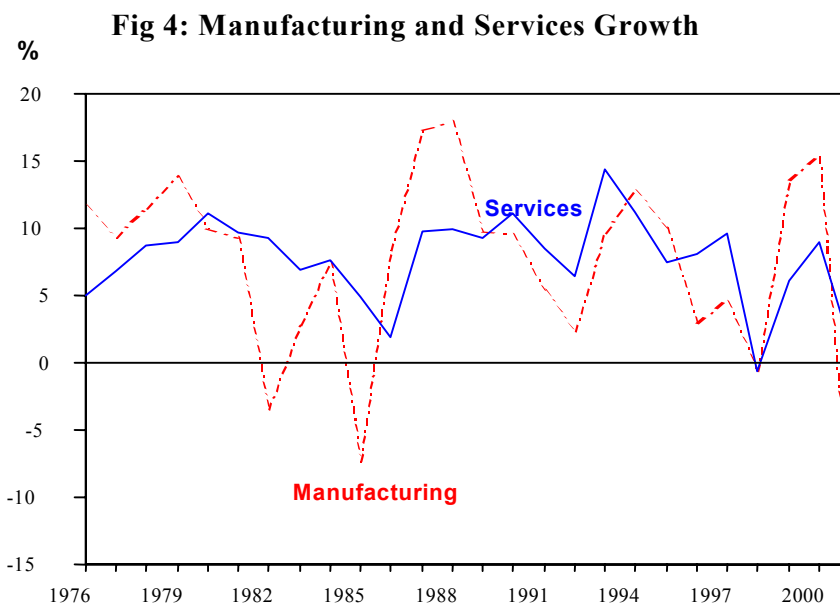
Fig 3: Services as a Percentage Share of GDP and Employment



6 The rise of services in developed economies is a natural development led by both demand and supply factors. On the demand side, the propensity to consume services increases with income. As households become more affluent, they tend to spend more on travel, education, arts & entertainment, etc. compared to manufactured goods.

7 On the supply side, the comparative advantage of an economy shifts towards services as its cost structure goes up. This is because manufacturing is very cost sensitive due to quick product commodification. Hence, except for high-end manufacturing, production tends to move towards the lower cost countries. On the other hand, services – whether medical treatment, legal or financial advice, or art performances – are much more differentiated and customised. While cost is still an important competitiveness factor for services, high cost countries can make up for their disadvantage by competing based on knowledge, skills and quality.

8 In Singapore, services growth has been more stable than manufacturing, and has helped cushion the sharp plunge in manufacturing output during the recessions in 1981-85, 1996-98 and 2001 (Fig 4). With greater uncertainty and volatility in the external environment, services' role as a buffer will become even more important – both in providing an additional source of growth, and by mitigating the large swings in the manufacturing cycle.



Source: Singapore Department of Statistics

PERFORMANCE OF THE SERVICES SECTOR

Overall Sector Performance

9 The services sector has overall performed well since the Economic Committee's report in 1986, with growth outpacing the overall economy. The sector expanded at a rapid rate of 9.6% per annum (pa) from 1986-96. However, after the Asian Financial Crisis in 1997, growth slowed considerably to 5.1% pa from 1996-2001 (Table 1). The Asian Financial Crisis has taken a heavy toll on our services market in Southeast Asia, due to the sharp fall in the exchange rate as well as the purchasing power of the regional countries.

Table 1: Performance of the Services and Manufacturing Sector

Sector	Share of GDP (%)			Employment Share (%)			VA growth (% pa)			Productivity growth (% pa)		
	1986	1996	2001	1986	1996	2001	86-96	96-01	86-01	86-96	96-01	86-01
Overall Economy	100.0	100.0	100.0	100.0	100.0	100.0	9.3	4.6	7.7	4.4	1.4	3.4
Services	60.7	64.5	66.7	64.3	69.5	74.2	9.6	5.1	8.1	4.9	0.6	3.5
Manufacturing	24.2	22.6	22.1	25.2	23.2	18.8	9.6	3.8	7.6	5.2	4.0	4.8

Source: Singapore Department of Statistics

10 Our services exports also followed the same trend. Our world ranking as an exporter of services has moved up from 18th in 1986 to 12th in 1996 before sliding to 15th in 2001 (Table 2). After the gains made in the decade since 1986, our global market share slipped from 2.3% in 1996 to 1.8% in 2001. In US\$ terms, services exports contracted by 10.8% over the period. In contrast, China's ranking rose from 16th in 1996 to 12th in 2001, with a 50.5% jump in its services exports. Korea and Hong Kong also experienced robust growths of 25.7% and 12.3% respectively in their service exports during this period (Table 3).

Table 2: Services Share of World Exports

Sector	Share of World Exports (%)			Ranking in World Exports			Growth in Exports (% pa)		
	1986	1996	2001	1986	1996	2001	86-96	96-01	86-01
Commercial Services	1.1	2.3	1.8	18	12	15	20.1	-2.3	12.2
Merchandise Exports	1.1	2.3	2.0	20	13	15	18.7	-0.5	11.9

Source: WTO Annual Report

Table 3: Services Exports Performance of Selected Asian Economies

	Ranking		Export Value (US\$b)		% Change
	1996	2001	1996	2001	
China	16	12	20.6	31.0	50.5%
Korea	15	14	22.6	28.4	25.7%
Hong Kong	9	9	38.3	43.0	12.3%
Singapore	12	15	29.6	26.4	-10.8%

Source: WTO Annual Report

11 In terms of productivity, our services sector registered a gain of 3.5% pa from 1986 to 2001, substantially lower than the 4.8% pa for the manufacturing sector (Table 1). We are ranked 23rd in services productivity in the World Competitiveness Yearbook 2002 (compared to 14th in manufacturing productivity), a fall of more than 10 places from our 11th position in the 1997 Yearbook. This shows that our services productivity growth has not kept pace with other countries.

Performance of Key Exportable Services

12 The performance of the key exportable services was in line with that of the overall services sector: rapid growth until 1996 before slowing down markedly (Table 4). Financial services and tourism were the hardest hit by the Asian Financial Crisis. Overall, the Info-Communications Technology (ICT) cluster was the fastest growing service industry (13% pa) since 1986, followed by legal and healthcare services (both 12% pa). Some of the major achievements in the various services sectors are highlighted in Box 3.

Table 4: Overall Performance of Key Service Clusters

	Value Added (VA) (\$m)			Estimated Real VA Growth (%)			Productivity VA/worker (\$000)			Estimated Real Annual Productivity Growth (%)		
	1986	1996	2000	86-96	96-00	86-00	1986	1996	2000	86-96	96-00	86-00
Financial Services ¹	4,115	13,915	16,900	10.0	0.0	7.1	102	202	245	4.3	0.0	3.0
Logistics	3,521	10,087	12,673	9.4	8.6	9.2	63	113	136	4.4	7.5	5.3
Info-Comms Technology	1,330	6,102	7,751	14.7	8.9	13.0	47	117	112	7.9	1.5	6.0
Tourism ²	1,649	5,721	6,243	9.5	2.1	7.3	16	37	42	5.2	3.1	4.6
Education	710	2,246	3,037	8.2	8.1	8.2	28	56	65	3.4	4.1	3.6
Healthcare	319	1,645	2,098	13.6	6.5	11.6	33	60	55	2.4	-1.9	1.1
Legal Services	179	577	839	13.1	8.4	11.7	44	76	82	-0.3	3.2	0.7
Total	11,823	40,293	49,541	9.3	5.2	8.1	46	94	108	3.9	3.3	3.7

Source: Survey data from Singapore Department of Statistics

¹ Includes institutions under MAS' purview

² Figures exclude overlaps with Logistics

Box 3: Examples of Key Achievements in the Services Sectors

Infocomms Technology

The liberalisation of the telecommunications sector in Apr 2000 attracted many global telecom players to Singapore, including NTT, AT&T, Reach and Belgacom. In Software & IT services, we have more than 600 local IT companies. In addition, 69 of the top 100 global software & IT companies, and 15 of the top 20 Indian IT companies, are also here. Our B2B e-commerce revenues have grown steadily, from \$40 billion in 1999 to \$109 billion in 2001. Singapore companies derived 18% of their total revenue from E-commerce in 2001, which is higher than Australia, Hong Kong, Taiwan and South Korea.

Financial Services

The debt market has grown rapidly since 1998, when measures were first implemented to develop both the government and local corporate debt market in Singapore. The corporate debt issuance in Singapore rose from S\$8 billion in 1997 to S\$72 billion in 2001. Wealth management activities have also expanded steadily. Assets managed by Singapore-based institutions grew from under S\$100 billion in 1995 to more than \$300 billion in 2001.

Logistics

In shipping, Singapore's ranking has improved 8 places from 1990 to become the 9th Most Important Maritime Nation in 2001. The Singapore Ship Registry has grown rapidly to become the largest in Asia and the 7th largest in the world. We have also attracted more than 40 shipping companies to base their regional headquarters in Singapore, including COSCO, Odjfell Tankers, Shell Tankers, IMC Shipping, and K Line. In addition, we have built up a core of homegrown transport and logistics players that are ready to take on the world, such as YCH Logistics, Sembcorp Logistics, Keppel Logistics, and Pacific International Lines.

Trading

Our offshore trade as a share of world merchandise trade has increased significantly from about 0.2% in 1990 to about 1.1% in 2000. We have also attracted about 110 leading international trading companies to base their regional trading activities here. Singapore has become the 3rd largest oil trading hub (behind London and Houston), with a good representation of players ranging from oil majors such as ExxonMobil and Shell, to Wall Street refiners such as J Aron and Morgan Stanley.

Education

To develop the post graduate segment of the industry, EDB embarked on a plan in 1998 to attract at least 10 World Class Universities to establish a significant presence in Singapore within 10 years. To date, 8 renowned educational institutions have been attracted to Singapore, including INSEAD, Wharton-SME Research Centre, Chicago Business School and Design Technology Institute.

13 Offshore trading, which is separately accounted for, has grown rapidly by 15% pa over the last decade. Growth has been resilient even after the crisis. In 2000, the major trading companies registered over \$200 billion in offshore trade, and were estimated to have contributed more than \$2 billion in value-added, or about 1.4% of our GDP.

14 In terms of productivity, ICT and logistics achieved the highest growth rate (6.0% and 5.3% pa respectively) for the period 1986-2000, while financial services registered the highest absolute productivity ([Table 4](#)). As for employment, ICT has increased its manpower by almost 2.5 times from 1986 ([Table 5](#)). Healthcare and legal services also saw their share of total employment in the economy increase significantly.

Table 5: Employment Share of Key Service Clusters

	Employment ('000)			Share of total employment (%)		
	1986	1996	2000	1986	1996	2000
Financial Services ¹	40.4	69.0	69.0	3.32	3.80	3.29
Logistics	56.2	89.6	93.3	4.63	4.94	4.45
Info-Comms Technology	28.3	52.1	69.1	2.33	2.87	3.30
Tourism	100.9	154.5	150.4	8.31	8.82	7.18
Education	25.6	40.3	46.7	2.11	2.22	2.23
Healthcare	9.6	27.6	38.1	0.79	1.52	1.82
Legal Services	4.1	7.6	10.2	0.34	0.42	0.49
Total Economy	1,214.4	1,814.4	2,094.8	100	100	100

Source: Singapore Department of Statistics

¹ Includes institutions under MAS' purview

CHALLENGES

15 The strategic thrust to develop our services sector is not new. Nevertheless, we have yet to exploit the services sector to its full potential. Our performance in recent years has also been lackluster. This is due to a few reasons:

- First, unlike manufacturing where we are globally competitive, many of our service industries are still not yet world-class, and trail behind the developed countries in productivity, capability and competitiveness.
- Second, the slowdown in the ASEAN economies after the Asian Financial Crisis has set back our exportable services sector, which is highly dependent on regional business.

- Third, competition in services is intensifying. Other countries are also rapidly developing their service industries, and closing the gap. Box 4 illustrates the aggressive promotion efforts in some countries.

Box 4: Services Development Efforts in Competing Locations

Infocomms Technology

In Hong Kong, CyberPort IT has been established to provide work-live-play environment to build a strategic cluster of companies and professional talents specialising in IT applications, information services and multimedia content creation. In China, Zhongguanchun in Beijing (dubbed China's Silicon Valley) has over 4,000 companies employing more than 100,000 workers. In fact, most of the major Chinese cities (e.g. Shanghai and Shenzhen) already have IT and technology parks in one form or another. Seoul's Digital Media City aims to provide next generation high-speed information networks to create a world-class complex for digital media industries.

Logistics

Our port has been facing rising competition from Malaysia's Port of Tanjung Pelapas (PTP). Singapore has lost two major shipping lines, Maersk and Evergreen, to PTP. Kuala Lumpur International Airport (KLIA) has waived parking and landing fees for new flights for the next 5 years in a bid to become a gateway to the region. In Taiwan, Kaoshiung International Airport plans to build a 23-ha multi-modal logistics park near its aircargo centre and Kaoshiung Harbour over the next 5 years to serve the high-tech industries. Hong Kong is making concerted efforts to become a regional aviation hub. Its Chep Lap Kok International Airport (CLKIA) has the world's largest air cargo terminal, SuperTerminal One, with air cargo handling capacity of 3 million tonnes per annum. The Philippines plans to transform the 28,000 hectares Clark International Airport (CIA) into its major international and domestic air cargo facility.

Trading

Competing locations such as Hong Kong, Dubai and Zug canton in Switzerland are offering lower and more enticing offshore taxes to attract trading enterprises. Hong Kong and Zug are also reputed for their financial, legal and physical infrastructure and supported by a strong hinterland. Hong Kong and even Shanghai are well positioned to benefit from China's WTO accession, while Dubai is emerging as an attractive trading location, especially for serving India, the African continent and the Middle East.

Healthcare

Since the Asian Financial Crisis, Malaysia and Thailand have aggressively marketed themselves as medical tourism destinations. They have improved greatly in capability and management in recent years, and are cost competitive. Some of their private hospitals have reported 200-300% annual growth in patient numbers in recent years. Bangalore has recently expressed aspirations to become the world's third largest healthcare hub after

Phoenix and Florida in the US. It has already invested in four medical colleges, three super-specialty hospitals, and attracted medical equipment manufacturers like GE Medical, Siemens and Philips to set up development bases there.

Education

India has attracted well-known universities such as Northwestern University and Carnegie Mellon to set up presence there. Hong Kong's 4 major universities have entered into collaborations with key Chinese universities to offer joint MBA programmes. Malaysia is also developing its education sector with aggressive twinning programmes between its private colleges and foreign universities, and through direct collaboration with foreign universities such as Monash University of Australia. As of May 2000, the Malaysian government has approved 86 private colleges to run twinning programmes with universities from Britain, the US, Australia and Canada.

16 Perhaps, another key factor is that we have not been as proactive and aggressive in developing the services sector as we have been in manufacturing, except for ICT (and financial services in recent years). We have allowed regulatory hurdles to get in the way of services growth, although there are indeed genuine socio-political concerns that need to be addressed. While there was no lack of trying by the various economic agencies, there was no joint effort at the national level to drive our services to become world-class. This was partly because until the Asian Financial Crisis, the ASEAN region was prospering, and our services exports had a ready market. Our strong manufacturing engine was also able to provide good growth, which made it less urgent to build a strong services sector.

17 However, we should no longer take a relaxed attitude to the development of services. We must put our whole heart and mind into growing our service industries through a concerted national effort. The need to do so has become more acute with the rapid rise of China as the manufacturing sub-contractor of the world. We are already witnessing the shift of manufacturing activities from Hong Kong, Taiwan and ASEAN to China. Although we still have comparative advantage in knowledge-intensive, high value manufacturing, we need to diversify our economy and build up services as a robust growth engine.

SINGAPORE'S COMPETITIVE EDGE

18 We have strong competitive advantages in services:

- Well-educated workforce
We have a well-educated, English speaking workforce, that has been rated by the Business Environment Risk Intelligence (BERI) as the most competitive in the world. This puts us in good stead to provide high value-added services.
- Good physical infrastructure
Singapore has an efficient, comprehensive, and integrated transport and communications infrastructure. The Political and Economic Risk Consultancy (PERC) ranked Singapore's physical infrastructure the best in the region. Singapore's overall infrastructure was also rated number one in the world in the Global Competitiveness Report 2001.
- Strategic Geographical Location:
Given our extensive transport and communications links, Singapore is well-placed to service countries within a 7-hour flight radius. This hinterland, which includes the high growth economies of China and India, covers a population of 2.8 billion people, with a burgeoning middle class.
- Conducive legal environment
We have a conducive legal environment and a good reputation for transparency in our laws, an efficient, fair, and impartial judiciary, and a strong commitment to intellectual property protection.
- Reputation for reliability, quality and trustworthiness
Singapore has built up a good reputation for reliability and trustworthiness. The Singapore name is a powerful brand to leverage and build on, especially in areas such as healthcare, education and financial services, where a high level of trust and quality is required.

19 A 2001 survey conducted by PERC ranked us first in Asia for being a preferred **business services** hub, and for having the greatest potential to be the hub five years from now. We also have strengths in **consumer services**,

such as tourism, education and healthcare. We are thus in a good position to be a major services hub in Asia, offering a wide range of quality services.

OPPORTUNITIES

20 The opportunities for services in Asia are tremendous. It is estimated that there are currently 4.8 million high-income Asian households outside of Japan with an annual income above US\$50,000¹. With a projected medium-term economic growth outlook of 3-5% pa for Southeast Asia and 5-7% for China and India, this number is set to rise steadily.

21 This growing affluence will translate into huge demand for services, especially higher-end and better quality services. For example, total healthcare expenditure in Asia is projected to grow at 10% pa, from US\$129 million in 1999 to reach US\$206 million in 2004². Those in the higher income households will increasingly be prepared to seek quality medical care overseas if they cannot find it in their home country. We should aim to tap into this market.

22 Another example is the education sector. Some 250,000 students from major Asian countries study in the US alone, contributing a massive S\$9 billion to the US economy³. A 5% share of these US-bound Asian students for tertiary and executive education would yield a significant spin-off to our economy. In particular, China is a huge potential market for us. There are 25,000 Chinese students who study abroad annually, making it the largest student exporter in the world. Singapore currently captures a significant share of this market, with a total of 13,000 to 15,000 Chinese students⁴. With rising affluence, the number is set to rise, and we should continue to capture a good slice of the market.

23 In tourism, China also offers huge promise. In the past 10 years, visitor arrivals from China to Singapore have grown at an average annual rate of 21%. Currently, only 1% of China's vast population is travelling overseas. With sustained robust economic growth and a fast rising middle class, China is predicted by the World Tourism Organisation to become the

¹ Source: Asian Demographics

² Source: Freedonia Group 2001. Figures exclude Australia, New Zealand and Japan

³ Source: Open Doors, 1999-2000.

⁴ Source: *People's Daily*, Beijing, 16 May 2002

4th largest source of tourists in the world, with an estimated 100 million Chinese travelling outside the country each year by 2020.

GROWING THE SERVICES ENGINE

24 We have what it takes to be Asia's leading services hub. Among the regional cities, only Hong Kong has an international services sector that is as well developed as ours. While Hong Kong's strength is primarily in business services, we have a competitive edge in consumer services like education and healthcare as well. Shanghai is fast emerging as a services city, but for now, it still lags considerably behind us. We must therefore build on our lead, raise our capabilities, and strengthen our position.

25 The window of opportunity is small. Other regional countries have also realised the potential of services and are embarking on vigorous development efforts. We need to act fast and strengthen our lead. Box 5 illustrates how some hub cities are able to hold on to their lead once they have established a critical mass. We must accelerate the development of our services, or risk falling behind permanently.

Box 5: Examples of Lead Services Cities

Financial Services – New York & London

New York is the undisputed financial services centre in the US, and one of the world's top international financial centres. Its lead position in the US was established as early as 1865, when it was the focal point for raising funds to build the railroad station. New York stands out for the depth and diversity of its financial markets, and is also the headquarters of the world's leading investment and commercial banks. The global market value of domestic companies listed on NYSE and NASDAQ (totalling US\$15.1 trillion) is several times larger than Tokyo (US\$3.2 trillion) and London (US\$2.6 trillion). In the debt markets, outstanding U.S. public debt exceeds the combined total for Japan, Germany, France, UK, Italy, Netherlands and Belgium.

Europe's lead financial centre is London. London's lead position was established in the late 1950s after the Second World War, when it became the focus of the euro-dollar market. Currently, London is home to 481 branches and representatives of foreign banks, considerably more than any other major financial centre. Although the introduction of the Euro has boosted the European stock markets, the capitalisation of the London Stock Exchange is still 2.5 times more than the German Stock Exchange and 3 times greater than the Paris Stock Exchange. London is also leading in the international equity

business, and has the world's largest foreign exchange market and international insurance market.

Education - Boston

In the United States, Boston has established a brand name and lead position as an education hub. The city's education cluster started with the founding of Harvard College in 1636. Nearly four centuries later, the region has one of the densest concentration of colleges in the country, with approximately 65 universities and colleges. In the for-profit learning sector, Boston is one of the key investment locations. For-profit learning centres here generated almost US\$7 billion in revenue in 2000, twice those of its runner-up, San Francisco⁵.

Healthcare Services – London

London has historically been a center for medical research. For example, the discovery of penicillin and the development of the Electro Cardio Graph (ECG) originated at the St. Mary's Hospital Medical School. Today, many of London's hospitals and medical schools are internationally known and respected as centres of scientific and clinical excellence. For example, the Royal Brompton Hospital leads the world in heart and lung medicine, while the Harefield Hospital is the largest cardiothoracic transplant centre in the world. There are 5 medical schools and 98 hospitals here, which is more than Boston, Paris, New York, Sydney, Frankfurt or Geneva. London's premier position is reflected by the presence of the European Medicines Evaluation Agency, which co-ordinates a one-stop approval process for licensing new medicines across Europe.

26 The service industries span a wide spectrum. We will have to focus on our niches. The Subcommittee has identified the following key service industries and formed 8 Working Groups to look at how we can strengthen their development: Creative Industry, Education, Healthcare, Financial Services, ICT, Legal Services, Tourism, Trading & Logistics. The recommendations on each of these service industries are contained in the respective Working Groups' reports.

⁵ Eduventures.com