MEMORANDUM ON PROPOSED CURRENCY AND BANKING ARRANGEMENTS BETWEEN SINGAPORE AND MALAYSIA

Singapore and Malaysia have been having a common currency since before the beginning of the 20th century. The existence of this common currency has greatly facilitated trade and promoted close economic ties between the two countries. The banking system of the two countries which historically has been closely linked is now operating under similar laws. Bank Negara Malaysia, with the concurrence of the Singapore Government, has continued to operate in Singapore after Singapore's independence and continues to supervise the banking system in Singapore. Although Singapore is now an independent sovereign nation, economic and financial considerations would suggest that it would be to the mutual advantage of Singapore and Malaysia to continue to have a form of common currency and an integrated banking system which would ensure the maintenance of confidence in the monetary stability of the two countries. If Singapore were to have a currency different from that of Malaysia, the existing smooth working relationship between the two countries in commercial and banking matters would be seriously affected. Every bank and most commercial firms operating in the two countries would find it advisable to keep separate their business in Singapore from that in Malaysia and considerable inconvenience would be caused to travellers moving between the two countries. Because of the physical proximity and financial links between the financial and commercial institutions in the two countries, the usual protective measures of exchange control when imposed in times of need would be unlikely to prove effective between the two countries unless both were to adopt identical policies.

2. In view of the advantages of maintaining a common currency and of the fact that the Currency Board is still the currency issuing authority in Malaysia and Singapore, it would be tempting, at first sight, to suggest that a suitable way of maintaining a common currency link between Singapore and Malaysia would be to continue the present Currency Board system with such modifications as may be found necessary.

3. The Currency Board system, which is a typical monetary system adopted in colonial territories, is a simple one and operates automatically. Currency is automatically issued in exchange for sterling at a fixed rate and is withdrawn from circulation when offered to the Currency Board in exchange for sterling. For the developing economies of Singapore and Malaysia, the Currency Board system, which is inflexible and can play only a purely passive role in the monetary situation, is no longer appropriate. It is a system which is fast disappearing, having been replaced in almost all emerging nations by the Central Bank. Moreover, the Currency Board system can do no more than look after the physical issue and redemption of currency. Bank credit is an important element in the monetary system and it is essential that the currency issuing powers and the supervision of the banking system should be concentrated in one authority, that of the Central Bank.

4. The Central Bank of Malaysia has been in operation for the last six years, and although it has yet to assume currency issuing powers, it has during this period acquired a reasonable store of expertise on banking matters in Malaysia and Singapore and on the techniques of credit control. The Central Bank of Malaysia Ordinance contains a provision which enables Bank Negara Malaysia to extend its operations to another country. It is therefore suggested that a more suitable way of maintaining the common currency and banking link between Singapore and Malaysia is for agreement to be negotiated between the two countries for Bank

Negara Malaysia to continue to operate in Singapore and to be the currency issuing authority in Singapore under the extension of jurisdiction clauses of the Central Bank of Malaysia Ordinance. Such an agreement would also provide for Bank Negara Malaysia to supervise the business of banking in Singapore and act as the agent for the Singapore Government under the Singapore Exchange Control Ordinance as well as acting as banker and financial adviser to the Singapore Government.

5. Bank Negara Malaysia would therefore be empowered to continue to operate its branch in Singapore and supervise the business of banking in Singapore. The Bank would have the sole right of issuing currency in Singapore in place of the Currency Board and of maintaining the external value of that currency. It would consequently be responsible for monetary policy in Singapore to the same extent as in Malaysia, the Governor of the Bank consulting the Singapore Minister for Finance on matters of such policy in so far as they affect Singapore in the same way as he consults the Malaysian Minister of Finance on matters affecting Malaysia. No change would be made in monetary policy on such vital matters as the exchange parity of the currency and external cover for the currency without prior consultation with the two Governments concerned so that, in the final analysis, each country would maintain its independent right of action.

6. It is proposed that the Singapore operations of the Bank should be kept separate from its Malaysian operations. The currency to be issued by Bank Negara Malaysia in Malaysia and Singapore would bear the same basic design but the currency issued in one country should have some distinguishing feature from that issued in the other to facilitate the proper separation of the operations of the Bank in each country. The currency issued in Singapore and issued in Malaysia would be legal tender in both countries and have the same external backing. Net profits on the Singapore business after provision for reasonable reserves could be paid to the Singapore Government. It is proposed that the Singapore Government should make some form of capital contribution towards the Singapore operation of the Central Bank and such contribution can take the form of a non-interest bearing deposit with the Bank. Provision could be made for Singapore's interests to be represented on the Board of Directors of the Central Bank.

7. The above proposals would enable the maintenance of a common currency in the two countries and put the supervision of the banking system in the two countries under a single authority. The maintenance of such a link should prove to the mutual advantage of both countries while, at the same time, it recognises and preserves the independence and sovereignty of each country.

Bank Negara Malaysia,
Kuala Lumpur.
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