

FINANCIAL LIBERALIZATION, INCREASED COMPETITION, AND IMPROVED BANKING SERVICES: EVIDENCE FROM SINGAPORE

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ABSTRACT

This paper examines the effect of financial liberalization on bank competition in Singapore. Specifically, the study explores whether the extensive liberalization of the once tightly protected domestic banking market in Singapore, which has paved the way for the entry of large international banking institutions has improved the availability quality of banking services and products.

INTRODUCTION

On 17 May 1999, the Monetary Authority of Singapore (MAS) announced its move to liberalize the country's "compartmentalized" commercial banking, aiming to attract foreign financial institution and hoping to turn the city-island into a world-class financial hub. Prior to the intended liberalization, Singapore banks were sheltered from foreign competition through the availability of "full service bank" licenses available only to local banks. Foreign commercial banks were allowed to practice on a more restricted basis through obtaining licenses which allowed them to operate as limited service banks, offshore banks or merchant banks.

The program, as announced, consisted of 3 key elements: the improvement of corporate governance, lifting of the 40% foreign shareholding limit and a five-year liberalization package, allowing foreign banks to enter the local banking market. The assumption of the MAS was that a more open and competitive banking environment would be the result of financial liberalization, and this in turn would lead to availability of a more diverse range of banking services, development and upgrading of local banks through competitive behavior, and eventually the flow of investment and deposit funds in to the Singapore market.

Prior research has indeed pointed to heightened competitive banking behavior following financial liberalization--Caminal et al. (1990), for example, found evidence that the slow loosening of the severe regulation environment led to the evolution of competition in banking. Increase in competition, in turn, has been found to lead to an improvement in perceived quality and range of products and services in several countries. The Organization for Economic Cooperation and Development (2001), for instance, noted that foreign bank entry "improves standards, and that open financial systems are more efficient and offer better services."

Research on the effects of liberalization in Peru identified increased competition in the banking system as one of the main impacts of liberalization, itself resulting from greater number of banks and increased presence of foreign banks (Illescas et al., 1998). Competitive behavior, in turn, improved the quality of banking services and contributed to a reduction of spread between the lending and deposit rates.

According to Zank et al. (1991), barriers to entry imposed on foreign banks in effect protected existing firms from competition and allowed them to operate inefficiently. “Through the provision of market access to new banks, competitive forces are introduced and market participants can turn to new sources for funds and financial services. Competition in banking and financial intermediation tends to limit the spread between the interest paid by borrowers and that received by depositors. Narrowing this spread is an incentive for increasing savings and will provide more and cheaper funds to investors. Competition, when combined with other liberalized financial sector reforms, enhances the efficiency with which intermediation is performed.”

Financial liberalization in Nepal, as another example, intensified competition and not only resulted in improved financial services such as longer opening hours and the provision of personalized services but also led to availability of new products through innovation as a consequence of increased competition (Pant, 2000). Chandrasekhar’s (2001) concluded similarly in the case of India--the liberalization process resulted in “dynamic” private banks, which were seen as pace setters for the rest of the banking sector. Furthermore, there was an improvement in the quality of the banking sector as these banks attracted depositors by offering better terms and better service.

Findings from International Financial Services (2002) showed foreign trade restrictions to a significant determinant of the interest rate spread for banks. Foreign trade restrictions protected domestic banks, which charged higher prices for their services and operated less efficiently. This was reflected in interest spreads that were 5-60% higher than they would have been in the absence of trade restrictions. In addition, the presence of foreign financial institutions may help in building more robust and efficient financial systems by gaining access to modern financial services that facilitate the development of a competitive export sector; improving access to foreign capital and international capital markets; and introducing international standards and practice. Other examples the strengthening of the country’s banking system as a result of successful reduction and abolishment of entry barriers include Chile, the Philippines and Turkey.

The purpose of this study is to assess the success of the financial liberalization in Singapore. As stated above, liberalization is expected to have several consequences and increased competition amongst banks is one of the main impacts (Caminal et al., 1990, discussing Spain, and Illescas et al., 1998, citing Peru). This article is modeled after Illescas et al. (1998) and hypothesizes that financial liberalization in Singapore has led to heightened competition among financial institution, and this in turn, has motivated Singaporean banks to improve product range and availability, and to provide better quality services.

The availability and quality of both core value services, and consumer-identified “important” banking services were assessed through administering a carefully designed survey questionnaire. Additionally, services offered by local banks with full banking licenses (e.g. UB and OCBC banks) were compared to those offered by foreign banks holding qualified full banking licenses (e.g. HSBC and Citibank). The results of the study not only point to the fact that liberalization has indeed improved the banking scene in Singapore through the availability of a wider range of products and better banking services, but also that foreign banks do have a competitive edge in both product availability and provision of banking services as compared to traditionally-protected

local banks. In addition, the results of the survey are important from a marketing point of view as the perception of consumers are revealed as to what services are important in their selection of banking institutions.

METHODOLOGY

To assess the availability and quality of banking services as perceived by consumers, a carefully designed survey questionnaire was administered at various locations in Singapore, including the Central Business District as well as housing estates. Potential respondents were approached and asked about their willingness to complete the survey (every 5th person was approached). Trained interns explained the purpose of the study and the affiliation of the researchers. A total of 450 questionnaires were distributed, with 414 usable responses, translating to a response rate of 92%.

The Questionnaire

Questions 1 and 2 were used to determine the target population as well as to ascertain if there was an increase in consumer banking in since liberalization started in 1999. The percentage of account holders that have opened new accounts with local and/or foreign banks is used to determine the popularity of the respective banks with the surveyed population.

(Q1): Select the banks in which you have an account. (*You may choose more than 1 bank*) and

(Q2) Select the bank or banks in which you have opened a new account during the last four years (i.e. since 1999). (*You may choose more than 1 bank*)

TABLE 1: FULL AND QUALIFYING-FULL LICENSE BANKS IN SINGAPORE

	UOB
	OCBC
	DBS
	ABN Amro Bank NV
	Banque Nationale de Paris
	Citibank NA
	Standard Chartered Bank
	HSBC
	Malayan Banking Berhad

The next two questions assessed the perception of bank customers regarding a bank services cited in the literature as having an influence in bank selection are listed in Table 2.

TABLE 2: FACTORS INFLUENCING BANK SELECTION

Category	Factors
Convenience <i>Lewis and Bingham (1991)</i>	Long Opening Hours Location of Branches Wide ATM Network
Pricing of Products and services <i>Gupta and Torkzadeh (1988);</i> <i>Leonard and Spencer (1991)</i> <i>Khazeh and Decker ((1992)</i> <i>Stafford (1996)</i>	Low Borrowing Rates High Deposit Rates Low Service Charge
Reputation <i>Yoon et al. (1993)</i> <i>Khazeh and Decker (1992);</i> <i>Boyd et al. (1994)</i> <i>Stafford (1994)</i>	Good Image Prestige
Service Quality <i>Grönroos (1990)</i> <i>Gupta and Torkzadeh (1988)</i> <i>Leonard and Spencer (1991)</i> <i>Sudin et al. (1994)</i> <i>Zineldin (1996)</i>	Efficient Staff Friendly Staff Good Credit Facilities Knowledgeable Staff Loan Repayment Flexibility Wide International Network Wide Range of Currencies Available Wide Range of Maturities for Time Deposits Wide Range of Banking Services
Perceived Risk <i>Hampton (1977)</i>	Financial Stability

There are 2 overriding dimensions of service quality (Levesque and McDougall, 1996; McDougall and Levesque, 1994).

The first dimension referred to the core aspects of the service such as reliability and the second referred to the relational or process aspects of the service such as tangibles (Jamal and Naser, 2002).

Grönroos (1987) and Storey and Easingwood (1998) defined core services as a main component of the basic service package. This result corroborated with that of the core and augmented product schema employed by Levitt (1980). TrendWatch (2002) defined value-added services as products and services outside a core product area that brings added value to the total customer relationship and which would strengthen the revenue stream for both customer and supplier.

(Q3) Which of the following factors do you consider as a “core consumer banking service?” and which do you consider only a “value-added service?”

(Q4) When selecting a bank, which of the following criteria you would be most concerned with?

TABLE 3: CONSUMERS’ PERCEPTION OF “CORE VALUE” VS. “VALUE ADDED SERVICES, AND THEIR IMPORTANCE IN BANK SELECTION

Question 4	Core Value Services				Value Added Services	
Question 5	Very Important				Not Important	
Efficient Staff	1	2	3	4	5	NA
Financial Stability	1	2	3	4	5	NA
Friendly staff	1	2	3	4	5	NA
Good credit facilities	1	2	3	4	5	NA
Good Image	1	2	3	4	5	NA
High deposit rates	1	2	3	4	5	NA
Knowledgeable staff	1	2	3	4	5	NA
Loan repayment flexibility	1	2	3	4	5	NA
Long opening hours	1	2	3	4	5	NA
Low borrowing rates	1	2	3	4	5	NA
Low service charge	1	2	3	4	5	NA
Prestige	1	2	3	4	5	NA
Wide international network	1	2	3	4	5	NA
Wide range of currencies available	1	2	3	4	5	NA
Wide range of maturities for deposits	1	2	3	4	5	NA
Wide range of services	1	2	3	4	5	NA
Wide ATM Network	1	2	3	4	5	NA
Location of Branches	1	2	3	4	5	NA
Others: (Please State)	1	2	3	4	5	NA

Questions 5 appraise the perception of consumers whether banking services have improved and question 6 asked them to list to identify which service(s) ought to be further improved.

(Q5) Which of the following services have been improved in recent years?

(Q6) Are there any banking service, which you think should be improved? Please Specify.

TABLE 4: CONSUMERS' PERCEPTION OF IMPROVED BANK SERVICES

	UOB	OCBC	DBS	ABN Amro Bank NV	Banque Nationale de Paris	Citibank NA	Standard Chartered Bank	HSBC	Malayan Banking Berhad
Efficient Staff									
Financial Stability									
Friendly staff									
Good credit facilities									
Good Image									
High deposit rates									
Knowledgeable staff									
Loan repayment flexibility									
Long opening hours									
Low borrowing rates									
Low service charge									
Prestige									
Wide international network									
Wide range of currencies available									
Wide range of maturities for deposits									
Wide range of services									
Wide ATM Network									
Location of Branches									
Others: (Please State)									

Finally, question 7 asked about the services consumers intended to use in the near future, and whether they were likely to approach local or foreign banks for such services.

(Q7): Please indicate

- (a) Bank services that you are currently using or are likely to use in future, *and*
- (b) whether you are using or would use the service provided from local Banks or foreign banks.

TABLE 5: CONSUMERS' INTENTIONS TO USE BANK SERVICES AND THEIR INTENDED SELECTION OF LOCAL OR FOREIGN BANKS

	Currently Using	Likely to use in future	Use service from Local Banks	Use service from QFBs
Advisory/ Consultancy services				
Asian currency unit (ACUs)				
ATM				
Credit cards				
Current/ Checking account				
EFTPOS cards (e.g.: NETS)				
Fixed deposit account				
Internet banking				
Investment services				
Loan facilities				
Payroll services				
Phone banking				
Safe deposit services				
Savings account				
Share brokerage				
Unit trusts				
Others: (Please State)				

Statistical Analysis

The following tests were conducted to analyze the results of the survey:

Frequency Analysis to summarize and describe the observations, such as the means and percentage of population that holds a local or QFB bank account; Factor Analysis to determine the statistically significant core value services in each category based on rotated factor matrix. A higher value of the service matrix as compared to others will implied that the service is perceived as more important and hence a core value Additionally, this technique was employed to assess which banks have made the most improvement; Chi-Square Test for Relatedness or Independence was used to analyze the relationship between the current or future usage of the banking products

and consumers' preference for the banks, and their consumers' preference for QFBs' products. In addition, results were used to determine the market penetration by the QFBs; One-way Analysis of Variance (ANOVA) was used to compare the statistical means of the consumers' perceptions on the important core value services of the different levels in each of the demographic groups (qualification, income and age). Results were used to evaluate if there were similar or different perceptions within each demographic group.

RESULTS

1. Pricing of the products and services is perceived as the highest ranked core value service; followed by perceived risk, service quality and convenience-related factors. The rotated factor matrix shows that Low Borrowing Rates, Efficient Staff, Financial Stability, Wide Range of Currencies, Location of Branches and Wide ATM Network are significantly regarded as the core value services.
2. In selecting a bank, the results show that the important categories are pricing of products and services, service quality, and convenience-related factor. Likewise, the rotated factor matrix was used to determine the significantly important services, which are Low Borrowing Rates, Wide Range of Currencies Available, Wide International Network, Efficient Staff, Wide ATM Network and Location of Branches.
3. Improved Core Value services were not perceived significant for Maybank, ABN Amro and BNP Paribas. As shown in Table 6, DBS and UOB have only perceived improvements on Wide Range of Currencies and Low Borrowing Rates, respectively. In addition, OCBC's services have not improved significantly. However, QFBs are making greater improvements as perceived by the respondents, where each QFB has improved on three important core value services.

TABLE 6: PERCEIVED IMPROVED CORE VALUE SERVICES

Improved Core Value Services	DBS	UOB	OCBC	Citi Bank	Standard Chartered	HSBC
Low borrowing rate	√			√		√
Wide Range of Currencies Available	√				√	√
Efficient Staff				√	√	√
Wide ATM Network				√		√
Location of Branches					√	

4. Table 7 depict other services perceived as improved by the respondents.

TABLE 7: PERCEIVED IMPROVED VALUE-ADDED SERVICES

Other Improved Services	DBS	UOB	OCBC	Citi Bank	Standard Chartered	HSBC
Wide Range of Deposit Maturities	√	√				√
Low Service Charge	√			√		
Friendly Staff		√	√	√		
Good Image				√		√
Long Opening Hours				√		√
Financial Stability					√	
Knowledgeable Staff						√

5. Respondents generally felt that there should be an improvement in ATM network; namely for QFBs. Inefficient staff especially during peak hours and apparent lack of staff's knowledge of products were a source of many complaints for all banks. A large number of respondents had requested for an extension of opening hours for branches and increased branches in well-located areas.
6. Most of the respondents currently use products from local banks. However, they are willing to try products from QFBs in the future. Such products include Advisory Services, Asian Currency Units, Credit Cards, Current/Checking Account, EFTPOS cards, Investment Services, Savings Account, Share Brokerage and Unit Trusts. This shows that QFBs are slowly penetrating into the consumer banking market through these products. Consumers still prefer to use basic banking products, like ATM and Fixed Deposits and Internet Banking from local banks.

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