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Explaining Sovereign Wealth Fund Variation: The Role of Domestic Politics in Small Open Economies

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Declaration

I certify that the thesis I have presented for examination for the PhD degree of the London School of Economics and Political Science is solely my own work.

I warrant that this authorisation does not, to the best of my belief, infringe the rights of any third party.

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Abstract

The emergence of sovereign wealth funds (SWFs) — large state owned investment funds – is attracting increasing attention from academics and policy makers. However, this research begins by pointing out that SWFs can differ considerably. The research question is: What accounts for the establishment of different types of SWFs across and within countries?

This research analyses the role of domestic state-society structures in policy-making processes and their effects on policy choices regarding SWFs. It empirically investigates whether and how policy networks affect decisions regarding the types and choices of SWFs. Particular emphasis is placed on SWFs with savings mandates, and SWFs with development mandates. Using process tracing on qualitative data, the research identifies key actors and interests involved in policy processes, and offers causal mechanisms that connect policy networks to decisions about the creation of different types of SWFs. Acknowledging the particular regional and historical contexts helps to account for the effects of networks within countries and across domains, and within domains across countries.

Using a case study on the 'types and choices of SWFs in Hong Kong and Singapore between the late 1960s and 1980s', this research examines whether domestic policy networks affect national decisions about SWF creation. These are hard cases for theories that emphasise the importance of domestic state-society structures. After all, over this period Hong Kong and Singapore were extremely exposed to international diffusion and economic pressures, and existing research emphasises a set of important factors (e.g. macro-economic characteristics, international economic pressures, diffusion).

The present research draws attention to four key findings between the 1960s–1980s: there were external pressures to which Hong Kong and Singapore had to respond and different policy choices were available and discussed; policy networks included and excluded actors that were making these decisions; there were systematic linkages between the type of policy networks and the type of SWFs; these had important implications for actors and created winners and losers.

Thereby this research adds to the ongoing debate on whether policy networks matter in explaining policy choices. It is doing that in four ways. To date, policy network approaches provide rather crude hypotheses on the effects of policy networks on a broad set of state strategies and forms of adjustment. These are difficult to verify because they are very broad. The present study offers a critique of policy network literature and develops policy network analysis with regard to causal mechanisms and hypotheses.

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Content

Acronyms and Abbreviations

ABS	Association of Banks in Singapore
ADIA	Abu Dhabi Investment Corporation
ADNOC	Abu Dhabi National Oil Corporation
CMA	Chinese Manufacturer Association
CPF	Central Provident Fund
DPMO	Deputy Prime Ministers Office
ExCo	Executive Council
FHKI	Federation of Hong Kong Industries
GIC	Government Investment Corporation
HKGCC	Hong Kong General Chamber of Commerce
KIA	Kuwait Investment Authority
LAC	Labour Advisory Committee
LegCo	Legislative Council
MAS	Monetary Authority of Singapore
MNCs	Multinational Corporations
PMO	Prime Ministers Office
PNs	Policy Networks
QIA	Qatar Investment Authority
SCCCI	Singapore Chinese Chamber of Commerce and Industry
SGS	Singapore Government Securities
SMA	Singapore Manufacturing Association
SWAC	Social Welfare Advisory Committee
SWF	Sovereign Wealth Fund
PAP	People's Action Party
PN	Policy Network

List of Tables

List of Figures

1. Introduction

The creation of different state finance institutions has been at the centre of an emerging literature on sovereign wealth funds (SWFs). With an estimated total size of US$7 trillion total assets under management by SWFs in 2015, SWFs surpass the combined volume of global private equity and hedge funds.[1] The average SWF size is similar to that of the world's largest pension funds, and surpasses the size of leading private-equity firms and hedge funds.[2] However, SWFs are not a homogenous group of organisations. They differ in terms of their ownership, governance structures, and mandates, which relate to different risks and strategies concerning investments (i.e. investment horizon/asset classes). These differences among SWF types and purposes of SWFs have led to much controversy about their impact and consequences.[3]

Much of the research on SWF types is informed by 'diffusion-based' and by 'efficiency-based' approaches. The latter consider efficiency in terms of what is best for a country given a set of macro-economic characteristics. For example, commodity-exporting countries create an SWF in order to avoid the Dutch Disease (Lee, 1997) or to smoothen budget volatility (IMF, 2008). Diffusion accounts consider the spread of SWFs across countries as the diffusion of financial fads or fashions (Chwieroth, 2014). The diffusion argument is based on the view that countries create certain types of SWF when other countries in their peer group also create that type of SWF in order to address similar economic policy challenges. This occurs through a process of emulation in which SWFs are considered the 'best practice' for countries with particular characteristics (Chwieroth, 2014). Central to this process are bounded actors who act in an environment of uncertainty.

While efficiency- and diffusion-based accounts offer valuable insights into SWFs, they have difficulty in explaining variations in terms of different SWF types across and within countries because they ignore the role of domestic politics. Efficiency-based accounts treat nations as unified actors that act rationally. Efficiency accounts are macro-level focused, as they implicitly incorporate the idea of the primacy of state interest. They thus impute a rationality behind the decision process of resource allocation, in terms of whether and what kind of SWF is established, which is driven by identifiable 'objective' challenges (e.g. the need to provide additional pension liabilities, stabilise fiscal revenues, or use for development purposes).

[1] See SWF Institute (2015), ESADEgeo (2015), Prequin (2015), BarclayHedge (2015).
[2] See SWF Institute (2015), ESADEgeo (2015), Towers Watson (2014).
[3] There were a number of controversial debates on their consequences (e.g. *The Financial Times,* 30 July 2007), including their role as patient long-term investors and stabilisers, as well as the revival of state capitalism, strategic investments and security issues relating to a new wave of financial protectionism (see Truman, 2010; Helleiner, 2009; Srinivasan, 2008).

Diffusion accounts emphasise the role of exogenous expert networks, perceptions, and ideas and their impacts on state interests. Although some accounts have drawn attention to institutional factors (Monk, 2010; Tranøy, 2010), little research has been done on the role of domestic politics at the meso-level and its effects on the kinds of financial institutions that are established.

This thesis examines the role of domestic politics by asking the research question, '*Do differences in domestic state-society structures influence the choice and type of state finance institutions, and, if so, how and why?'* This research question suggests a relevant link between decisions about different types of SWF and variations in state-society relations. Such variations across policy domains reflect different levels of civil society mobilisation as well as different levels of state centralisation and autonomy. According to Atkinson and Coleman (1989, p. 51) state centralisation and autonomy refers to the "degree to which ultimate decision making power is concentrated in the hands of [a small number of officials] and the degree to which these are able to act autonomously". A number of well-established studies in the discipline of comparative politics highlights that forms of state-society relations affect different policy choices in terms of financial institutions (Hall, 1986; Katzenstein, 1985; Zysman, 1983). Given that different financial institutions represent the outcomes of policy decisions and that policy decisions are influenced by state-society relations, this study can construct a direct linkage between state-society relations and the creation of different SWF types.

It finds, as is demonstrated in Chapters 4, 5, 6, and 7, that the diffusion and efficiency arguments cannot explain the variation in state finance institutions in small open economies outside the Middle East. A brief overview in Chapter 2 outlines SWF variations among small open economies in the Pacific and in small open economies of East Asia. Singapore has an SWF with a savings mandate, the Government Investment Corporation, and it is related to other state finance institutions, notably a state-run central provident fund. Despite strong demand for the creation of a state run CPF, Hong Kong's policy makers decided against the creation of such state finance institutions. Similar institutional variations can also be observed in the industrial domains of both Hong Kong and Singapore. While Singapore has an SWF with a development mandate, Temasek, and it is linked to other state finance institutions, notably a state development bank, Hong Kong decided against creating such state finance institutions. Unlike Singapore, Hong Kong's state-society structures included domestic finance and commerce organisations involved in policy-making processes which were central in affecting choices about state finance institutions. Simultaneously, Hong Kong's state-society structures excluded welfare and industrial groups, as well as international finance organisations, from these policy-making structures. Hence, variation in state finance institutions is difficult to explain without discussing domestic politics and the role of state-society structures at the meso-level..

1.1 THE PUZZLE OF DIFFERENT SWF IN SMALL OPEN ECONOMIES

Almost all of the small open economies in the Pacific, Middle East, and East Asia have created SWFs of different types. Between the 1960s and 1980s, a significant number of small open economies, such as Brunei, Singapore, Qatar, Kuwait, and Abu Dhabi, established SWFs. These decades saw dramatic changes in the global economy. Katzenstein's statement that this period was an era of "global inflation, increases in trade rivalries and protectionism, prolonged recession, volatile foreign-exchange markets, skyrocketing interest rates and debts, and structural adjustment" highlights the set of powerful economic pressures to which small open economies of that time were exposed (Katzenstein, 1985, p. 22). In an attempt to adjust to a new international economic environment and confronted with windfall revenues (e.g. from hydrocarbon exports), many small open economies started to create SWFs (Tranøy, 2010). In 1953, for example, Kuwait created the Kuwait Investment Board, a predecessor of the Kuwait Investment Authority (created in 1982), and Qatar created the Qatar Investment Board in 1972, a predecessor of the Qatar Investment Authority. Likewise, Abu Dhabi created the Abu Dhabi Investment Authority in 1976, and Singapore established Temasek in 1974. In the 1980s Singapore created the Government Investment Corporation in 1981, and Brunei established the Brunei Investment Authority in 1983.

Differences in mandate reflect different investment patterns and mirror different governance structures. For example, SWFs with development mandates are usually established under company law, or by decree (Hammer, Kunzel and Petrova, 2008). Their governance structure allows them to invest in domestic and international companies, which are sufficiently large to affect a firm's management decisions, while SWFs with savings mandates make long-term-return oriented investments by spreading risks through portfolio investments across a large spectrum of assets with a strong international focus (Al-Hassan et al., 2013). Meanwhile, SWFs with stabilisation mandates are usually established under monetary law and controlled by the central bank. Their mandate involves monetary or budget stabilisation. As such, their investment choices are confined to highly liquid assets, such as currency derivatives or bonds.

How can we explain the variation among SWFs? How was it possible that small open economies with similar macro-historical backgrounds and located in similar regions made very different choices when creating SWFs? Why do countries in similar peer groupings, such as small open economies in East Asia and the Gulf, adopt different SWF types? Answering these questions leads to answers to related questions. For example, why do countries in different peer groupings, such as China and Singapore, create similar SWF types? The answers help clarify why countries choose different kinds of financial institutions to address common challenges.

1.2 UNDERSTANDING SWF VARIATION IN SMALL OPEN ECONOMIES

Central to an understanding of what influences the creation of different SWFs across countries are analyses of efficiency (Aizenman and Lee, 2005; Aizenman and Glick, 2007; 2009; Truman, 2008, 2014; Das et al., 2009) and diffusion (Chwieroth, 2014; Helleiner, 2009; Cohen, 2009). These focus on the role of macro-economic variables and ideas, arguing that they are key to understanding the creation of SWFs. While diffusion-based studies suggest that choices are affected by sweeping cross-national movements of emulation, efficiency-based accounts highlight that a country's choice of SWF type is strongly determined by its economic position. The latter views have played a significant role in the debate. They have been developed and taken up by members of national regulatory bodies (e.g. The Committee on Foreign Investment in the United States), supranational organisations (i.e. the European Commission, the European Central Bank), international organisations (e.g. The International Monetary Fund, the Organisation for Economic Co-operation and Development), and international forums (e.g. the International Working Group on SWFs), which have drafted and implemented regulatory policies and official responses to SWF investments.

EFFICIENCY-BASED ACCOUNTS

Much of the scholarship on SWFs draws on a wider literature based on economic efficiency. It considers efficiency in terms of matching a country's macro-economic characteristics with the appropriate SWF types. As mentioned, efficiency accounts treat the state as a unified actor driven by functional imperatives. They impute a rationality behind decisions on whether and what kind of SWF to establish. These decisions are driven by identifiable 'objective' challenges (e.g. the need to cover additional pension liabilities, stabilise fiscal revenues, or for development purposes). Scientific work is dominated by economists such as Aizenman and Lee (2005), Aizenman and Glick (2007, 2009), Truman (2008), Das et al. (2009), and Blundell (2008), who focus on macroeconomic issues such as reserve and stabilisation management. Efficiency-based accounts draw on well-established models, such as on foreign exchange reserve management (Flood and Marion, 2001) or resource endowment (Lee, 2007); they use well-established concepts, such as that of the Dutch Disease (*The Economist*, 26 November 1977; Lee, 1997) and well-established hypotheses, such as the permanent income hypothesis (IMF, 2008) or the precautionary savings hypothesis (see Carroll and Jeanne, 2009). These studies have made major contributions to the understanding of macro-economic factors and SWF variation. They theorise how resource endowment (e.g. oil or mineral wealth), level of current account surpluses, economic diversification, degree of trade openness, level of economic development, and socio-demographic issues (e.g. ageing societies) contribute to the decisions of whether and what type of SWF to establish. Efficiency-based approaches analyse using large-N surveys and large-N comparative studies (e.g. Aizenman and Glick, 2009) the relationship between macro-level variables across countries and SWF variation.

The common assumption among efficiency-based approaches is that countries with similar macro-economic characteristics, that are exposed to similar external pressures, make similar choices about the creation of SWF types (Frankel, 2011; IMF, 2008; Aizenman and Glick, 2009; Lee, 2007; Das et al., 2009). In an effort to broaden the analytical scope of efficiency based accounts, some scholars – notably Blackburn et al. (2008) and Monk (2010) – introduced an institutional dimension. By building on efficiency accounts, institutional studies highlight the centrality of institutions in explaining different SWF outcomes among economies. While some (e.g. Blackburn et al., 2008) perceive SWFs as substitutes for missing market institutions, others, such as Monk (2010), argue that SWFs are instruments of domestic self-insurance in the context of globalisation.

Although different in reasoning, most of the institutional explanations rely on an efficiency-based logic to explain the relationship between resource allocation and institutions as the basis for SWF variation. As a means of self-insurance, SWFs can serve two functions that would appear to be contradictory. This explanation indicates that SWFs are structural mechanisms that support existing domestic commitments and institutions of nation-states vis-à-vis the pressures of globalisation. These include safeguarding domestic institutions and commitments (e.g., macroeconomic stability and superannuation commitments). At the same time, however, SWFs can take advantage of these forces by deploying a substantial part of savings into international financial markets in order to maximise their return and get a premium (Monk, 2010). According to Monk (2010, p. 29), in fulfilling these two functions, SWFs are "desired form[s] or instrument[s] of nation-state investment." Likewise, other authors, notably Haberly (2011), highlight the strategic use of SWFs by states in order to promote national development, for example, the UAE's use of SWFs to promote the development of the aerospace sectors. Therefore, strategically oriented SWF investment can be seen as an adaptive strategy by the state under contemporary conditions of globalisation and financialisation (Haberly, 2011).

From such an institutional perspective, SWFs can be considered as substitutes for missing or underdeveloped domestic institutions. In contrast to Monk's 'positive' reasoning, other authors, most notably Blackburn et al. (2008), use 'negative' reasoning in explaining the existence of differing SWFs. Blackburn et al. (2008) explain SWFs from the perspective of markets and hierarchy. From such a perspective, the major reason behind the establishment of SWFs with development mandates (e.g., Singapore and China) would be to recapitalize and develop an underdeveloped or nonexistent financial market. In a similar fashion, SWFs with stabilisation mandates could be seen as institutional structures with the purpose of smoothening fiscal revenues in countries such as Kuwait, Bahrain, Saudi Arabia, and the UAE that lack extractive institutions (i.e. a taxation system). Similarly, the establishment of SWFs with a saving mandate could be explained as the introduction of institutional structures enabling the transfer of current wealth to future generations. Drawing on the variety of capitalism literature (Hall and Soskice, 2001) authors, notably Haberly (2014), introduce the concept of institutional complementarity and comparative institutional advantage in order to analyse the path-dependent evolution of SWFs.

As a result, it would be expected that countries similar in their international economic exposure, economic development, demographics, culture, size of domestic market size and resource endowment would make similar choices of SWF type. However, a review of the data suggests something different: even small open economies make very different decisions about the setup of their financial institutions. As will be shown in Chapter 2 across small open economies there exist significant variation in terms the financial institutions set up. Hence, small open economies with different SWF types are puzzling to efficiency-based accounts.

DIFFUSION-BASED ACCOUNTS

Diffusion-based approaches respond to the overly narrow focus of efficiency-based accounts. Diffusion studies were largely inspired by the observation that SWFs emerged at particular times in countries that were geographically close (Chwieroth, 2014) and had specific geo-strategic characteristics (Cohen, 2009). Diffusion-based approaches offer a distinctive explanation of SWF variations by drawing on organisational sociology (Chwieroth, 2014). They argue that SWF variation is not simply the outcome of efficiency considerations but the result of contingent emulation and culturally specific contexts and strategies. Scholars such as Chwieroth (2014) highlight that even the starkest SWF variations, among oil-exporting economies, should be explained in terms of ideas, culture, and strategy. Given the lack of transparency the adoption of SWFs may not be driven by similar rational concerns but more by fad (Chwieroth, 2014).

The proliferation of SWFs as a mechanism for managing sovereign wealth may also be the outcome of perceived opportunities. By referring to sociological aspects and concepts related to the discipline of international relations, studies such as Chwieroth (2014) highlight the perceived efficacy consideration of SWFs in other countries (Chwieroth, 2014). Likewise, Helleiner and Lundblad (2008) draw attention to the subject of international capitalism and the perceived opportunities and constraints of having an SWF in the context of strategic alliances (Helleiner and Lundblad, 2008). These studies use comparative large-N frameworks (Chwieroth, 2014) or descriptive historical explanations (Helleiner and Lundblad, 2008) to elaborate on how and why ideas and perceptions affect decisions regarding the creation of

SWFs that take place across countries with specific structural characteristics in certain time periods.

The processes of emulation and the transnational emergence of SWFs are the focus of Chwieroth (2014), who argues in his systematic approach that SWFs are by-products of international wealth redistribution, both in the West and in emerging economies, as well as the outcome of contingent emulation among the latter. His account is intended to confront and contest key functional-rational assumptions about SWF creation. Chwieroth's study on the emergence of SWFs at particular times in countries with specific characteristics and geographical proximities is suggestive for analysing the role of diffusion mechanisms (i.e. contingent emulation). His work is based on a perception that stresses the role of complex transnational expert networks in the diffusion of policy ideas. From this perspective, SWFs are "fads" or "socially constructed appropriate institutional forms of policy" across countries that possess similar structural features (Chwieroth, 2010, p. 3). The observable expectation of a diffusion approach is that countries in similar peer groups confronted with similar economic policy challenges follow their peers in the creation of similar SWF types. However, it should be noted that diffusion can also happen among states which are dissimilar in terms of their structural characteristics.[5] For example, Singapore's Temasek served as a role model for a number of countries that are different in terms of their structural characteristics, such as China (*The Straits Times*, 3 October 2015; *The Wall Street Journal*, 21 March 2007). Although authors such as Bernstein et al. (2013) indicate alternative paths of SWF diffusion, notably bilateral relationships, most of the studies do not specify the causal path through which political relations play a role in SWF diffusions.

Although efficiency- and diffusion-based approaches help to understand SWFs, puzzling aspects remain that existing theories cannot explain. Even small open economies within similar peer groupings (e.g. the city states of East Asia, small open oil- and gas-exporting economies of the Middle East, small phosphate-exporting island economies of the Pacific) feature significant variation in their SWF choices in terms of whether an SWF is set up and, if so, what type. Also linked to different SWF types are other state finance institutions, such as industrial banks and public pension funds. These various state finance institutions exist not only across nations, but also across domains. Both the diffusion and efficiency approaches downplay the role of domestic politics and its influence on decisions regarding state finance institutions. As a result, they cannot explain politically driven variations. This research offers important insights into the drivers of state finance institutions in small open economies by examining domestic politics, which in turn may help to solve the initial puzzle.

[5] I would like to thank Steffen Hertog for this point.

BRINGING IN DOMESTIC POLITICS

Unlike the diffusion and efficiency accounts, this thesis emphasises the role of domestic politics. Thus far, only a few academic accounts, notably Pekkanen and Tsai (2011) and Tranøy (2010) emphasise the need to link decisions about SWFs to domestic politics. In his article 'Norway: The Accidental Role Model', Bent Sofus Tranøy (2010) took the first step by examining the historical trajectory that led to the Government Pension Fund Global (GPFG). The creation of the GPFG is a political story in terms of how it integrates oil revenues into an established institutional order (Tranøy, 2010). Using Katzenstein's terminology (1985), Tranøy suggests the GPFG as a means of flexible adjustment in a highly globalised environment and a tool to address external pressures and domestic compensation in terms of supporting Norway's welfare model. When Norway discovered oil in the late 1960s, it had a well-established corporatist polity. Tranøy's statement that "one must grasp the domestic politics of handling petro-wealth in a corporatist state" indicates the importance of understanding the political context in which the GPFG was created (Tranøy, 2010, p. 198). Although Tranøy's article illuminates important aspects of domestic politics in a corporatist resource-rich democratic country in Europe, it tells us little about the domestic politics and SWFs of other countries.

Through their work on 'The Politics of Ambiguity in Asia's Sovereign Wealth Funds', Pekkanen and Tsai (2011) make an important contribution to illustrate the effects of domestic politics on SWF choices in non-Western countries. Pekkanen and Tsai (2011) look at SWF decisions in China, Singapore, and Japan during the 2000s. Inspired by constructivist work (Best, 2005; Jabko, 2006), Pekkanen and Tsai (2011) are interested in the political possibilities of SWF ambiguity. They refer to the ambiguity of SWFs as the absence of clear-cut policy goals and directions (Pekkanen and Tsai, 2011). This frequently leads to ambiguity in terms of the lack of a coherent strategy among SWFs. In turn, this ambiguity can accelerate concerns about national security in countries that receive investments from SWFs. However, Pekkanen and Tsai (2011) remain unclear in terms of whether it is the actual or perceived ambiguity in which they are interested. Furthermore, it remains open whether their dependent variable refers to the behaviour of SWFs, the creation of SWFs, or both. This, combined with a lack of clarity concerning the independent variable, makes comparison difficult. Pekkanen and Tsai (2011), comparing debates about SWFs across countries in terms of similarities and differences, highlight that there are complex struggles among domestic public actors with different interests and tensions, combined with pressing social and economic concerns that shape the discourse and direction of SWFs. They look at the expectations and perceptions of societal groups vis-à-vis the SWFs, and look at how societal groups influence discourses about the SWFs. An analysis of debates serves as a diagnostic tool in investigating underlying conflicts. These conflicts relate to some other factor that varies and needs to be explained systematically.

To account for the unexplained variation in state finance institutions systematically, this study introduces state-society structures, which have been overlooked by existing accounts on SWFs, but whose effects on policy outcomes have been described in another body of literature, that on policy networks. This literature focuses on factors like the concentration of state power, bureaucratic arrangements, the relationship between officials and the private sector, and the organisational properties of the private sector.

A domestic politics approach focussing on state-society structures offers a complementary perspective – within established analytical frames – for analysing unexplained SWF variation across countries. Efficiency approaches would benefit from the insights of a domestic-politics perspective in two crucial ways. First, a domestic-politics perspective would assist an understanding of why similar economies confronted with similar macro challenges make different decisions about SWFs. Similarly, such an approach might help to establish a greater degree of accuracy for constructivist explanations (i.e. diffusion accounts). For ideas to be influential, they must be translated into the policy-making processes. A domestic politics perspective would help to assess why ideas – the 'fad' of having an SWF – have dissimilar impacts on economies within similar peer groups facing similar challenges. For political accounts on SWFs, the focus on state-society structures provides a mediating variable that shapes debates and links actors to policy-making processes with regard to state finance institutions.

1.3 RESEARCH DESIGN AND CASES

This thesis uses a cross-country comparison (Hong Kong and Singapore) and a cross-domain comparison (industrial and savings domain) to develop and refine its hypotheses concerning the effects of state-society relations on the set up of financial institutions, with different SWF types used as instances.[6] It uses process-tracing to identify the actors and interests involved in policy processes and offers causal mechanisms that connect SWF types to state-society relations. Cross-national comparison allows an analysis of the effects of state-society relations across countries. Cross-domain comparison allows an investigation of the effects of state-society relations across domains and within countries.

The thesis arrives at these hypotheses inductively. First, it undertakes an in-depth study of state-society relations in Singapore's savings and industrial domain and their effects on the creation

[6] Each domain relates to a distinct policy arena in which state-society actors relate to each other through a series of linkages.

of Temasek and the Government Investment Corporation. It forms an initial hypothesis based on the findings. This hypothesis is then refined with additional evidence on state-society relations and the kinds of financial institutions set up in Hong Kong's savings and industrial domain. The study verifies whether the results hold in other cases using a plausibility probe in three additional countries (i.e. Abu Dhabi, Kuwait and Qatar) located in a different area of the world.[7]

Examining Hong Kong and Singapore between the 1960s and 1980s offers hard cases for studying the effects of state-society relations on the creation of state finance institutions. They are least likely cases for the effect of domestic politics on policy choices and most likely cases for diffusion and economic efficiency arguments to have an effect on choices concerning the types of SWFs, because Hong Kong and Singapore are extremely open to international diffusion and economic pressures. Between the 1960s and 1980s, Hong Kong's and Singapore's economic domains (i.e. savings and industrial) were similarly exposed to international diffusion pressures, such as cross-national learning and emulation, and economic pressures arising from competition, currency volatility and inflation. Despite having similar issues at stake, similar policy choices available, and similar actors involved (though structured differently), Singapore and Hong Kong made different choices with regard to state finance institutions.

This research focuses on the effects of state-society structures on the creation of different state finance institutions and does not investigate why certain state-society structures have emerged or endure. Though an important question, this issue would necessitate a different research design. Moreover, this research concentrates on SWFs with savings mandates and development mandates and related state finance institutions, such as state central provident funds and state industrial banks. It does not examine SWFs with stabilisation mandates and related state finance institutions, such as monetary authorities and central banks, for three main reasons. First, these institutions deal with a rather different set of issues that concern monetary policy rather than industrial policy. As such, they are not directly linked to industrial policy. However, the literature upon which this thesis draws discusses industrial policy. Second, space constraints prevent this study from examining all kinds of state finance institutions. Third, given the limited empirical material available on the politics of monetary authorities and central banks in Hong Kong and Singapore, this research concentrates on SWFs with development and savings mandates, as well as related state finance institutions.

[7] Plausibility probes are valuable to determine whether more testing of the hypotheses is warranted (see George and Bennett, 2005).

It is also important to emphasise that this research does not focus on the management of fiscal/current account surpluses, though they are important core tasks of SWFs, for two reasons. First, there has been much written on the link between SWFs and the management of fiscal/current account surpluses (see Feldstein, 1999; Jen, 2007; Aizenman, 2008; Aizenman and Glick, 2009; Das et al., 2009; Frankel, 2011). Although fiscal/current account surpluses are important sources of sovereign wealth (e.g. from the export of oil and other products), the present study focuses on other sources. To date, little systematic is known about the linkage between the creation of different SWF types and other funding sources, which are often related to choices about other state finance institutions, such as the proceeds from privatisation, the re-organisation of government enterprises into new organisational formats and large public pension funds. Second, this thesis centers on SWF creation and their different mandates. As such it does not concentrate on management issues, which are linked to aspects of investment behaviour. Although the mandate does not explain every investment made by an SWF, it provides direction and poses structural and legal constraints upon an SWF's behaviour.

FINDINGS

This research produces four key findings: between the 1960s and 1980s, policy networks (PNs) included and excluded actors that were making these decisions; there were systematic linkages between the type of PN and the type of SWFs; and these had important implications for actors and created winners and losers. These findings are detailed below.

First, this study finds that external developments (e.g. increasing international competition, inflation, currency volatility) put pressures on socio-economic actors in Hong Kong and Singapore. By looking at domestic debates, the research finds that different choices were available and discussed between the 1960s and 1980s, and that different actors favoured different types of finance institutions. For example, in Hong Kong's welfare groups and labour organisations demanded the creation of a large state run central provident fund (CPF) and an investment organisation that invests CPF funds abroad, whereas domestic finance and commerce actors demanded the proliferation of private pensions schemes. Likewise, Singapore's domestic private finance organisations were critical of state finance institutions in the savings domain. Concerning institutional choices in the industrial domain Hong Kong as well as Singapore's manufacturers demanded the creation of state finance institutions that cater to their specific needs, while domestic finance actors supported the proliferation of private finance institutions.

Second, it discovers that variation in state finance institutions is systematically related to state-society structures. It finds cases that run counter to the observable expectations of efficiency-and diffusion-based arguments. Countries in the same peer group – in terms of structure, culture – that were confronted with similar problems responded with very different policy choices regarding state finance institutions. Both in Singapore's industrial as well as savings domain state society structures were characterised by low levels of business mobilisation, high levels of state autonomy and concentration of decision-making power. That was consistent with that of a state directed PN. Reflecting this in both domains we can observe the existence of SWFs with savings and development mandates as well as related state finance institutions, such as a public pension fund and a state run development bank. By contrast, in Hong Kong's industrial and saving domain the state society structures were characterised by high levels of business mobilisation, low levels of state autonomy and high levels of concentration of decision-making power. This is consistent with that of a clientele pluralist PN. Mirroring this PN we can observe the non-creation of SWFs with savings and development mandates as well as the non-creation of related state finance institutions, such as a public pension fund and a state run development bank.

Third, it finds evidence that state-society structures – in the form of PNs – have influenced both, the discussions about policy choices and the appointments on policy-making bodies. This research thus provides new insights into the operation of the causal mechanisms linking PNs to the kinds of financial institutions that are set up. While Hong Kong's PN included commerce and domestic finance on policy-making processes, it excluded international finance, social and welfare organisations. In contrast Singapore's PN included international finance on important advisory bodies, and excluded domestic finance and commerce. One implication of these findings is that the PN literature needs to be strengthened concerning such mechanisms of inclusion and exclusion.

Fourth, the study reveals that the types of PNs and their corresponding policy choices regarding state finance institutions involve distributional consequences. Size, combined with their specific organisational features, turn state finance institutions – specifically CPFs and SWFs – into dominant financial institutions in their respective policy domains, particularly in small open economies. For example the combined size of Temasek the CPF and the GIC is equivalent to more than 300 per cent of Singapore's GDP. Due to size and mandate these state finance institutions are highly unpopular with domestic private actors because they are rivals to existing domestic private financial institutions in their respective domain. Moreover, SWFs are frequently associated with competition and crowding out in the domestic private sector.

Overall, the study finds that countries create state finance institutions with development and savings mandates when there are state-society relations in place that are described in the literature as state-directed PN. It finds that that PNs matter empirically in hard cases (i.e. Hong Kong and Singapore between the 1970s and 1990s).

BROADER CONTRIBUTIONS

This thesis adds to the ongoing debate on whether PNs matter in explaining policy choices. Current PN approaches provide rather crude hypotheses on the effects of PNs on a broad set of state strategies and forms of adjustment (i.e. reactive and anticipatory) (Atkinson and Coleman, 1989). These arguments are difficult to verify because they are very broad. This study offers a critique of the PN literature and develops hypotheses inductively in hard cases.

Second, the thesis improves the understanding of how and why PNs influence policy choices, a heretofore underdeveloped issue. Few studies have examined systematically or comparatively the effects of PNs on policy outcomes (e.g. Howlett, 2002; Daugbjerg, 1998a; 1998b; Montpetit, 2005; Dunn and Perl, 1994), and most have linked network characteristics to policy outcomes in terms of change and stability. Few scholars have explicated the mechanisms by which PNs affect outcomes (Hindmoor, 2009). This study fills this gap by addressing the question of whether differences in domestic state-society structures influence the type of SWF, and if so, how and why. It develops the PN literature in terms of the mechanisms by which PNs might have operated to influence policy choices.

Third, this research advances the understanding of distributional consequences for domestic socio economic actors, such as private banks, which has remained underdeveloped. Understanding the distributional consequences helps clarify the role of organisational mechanisms in policy-making in terms of network effects and of who loses and who wins from particular types of SWFs.

Fourth, the present research, which uses a PN analysis as its guiding framework, alludes to a number of other well-established approaches. The underlying factors that shape PNs, including aspects of state autonomy, state centralisation, and societal mobilisation, also relate to a number of other approaches, notably the literature on the developmental state (which focuses on state autonomy) and the literature on state-business relations. PN analysis looks at similar factors in combination at the domain level. This in turn links the present thesis to other literatures. For example, PNs can be integrated into a developmental state framework in order to determine how the overall features of the developmental state play out at the sectoral level. As such, PNs can be treated as mediating factors, allowing for a more precise analysis of differences across sectors. PN analysis, however, can also benefit from the insights of other approaches. While PN approaches focus primarily on how policy outcomes are affected by structures, other approaches, such as the literature on state-business relations, look at the drivers behind these structures. This suggests that PN analyses are complementary, rather than rival, to other explanations regarding domestic structures.

The general hypothesis developed in this research is that the structure of PNs affects which kind of financial institution is set up and that different financial institutions favour different socio-economic actors. Applied to specific cases, the hypothesis is that SWFs with development and savings mandates are more likely to be created when we observe state-directed PNs.

CHAPTER OUTLINE

Following the introductory chapter, Chapter 2 shows that the creation of different state finance institutions in small open economies poses a profound puzzle for standard explanations. To distinguish among different SWFs, the chapter looks at a set of organisational features (see Hammer Kunzel and Petrova, 2008; IMF, 2008). These include ownership, legal status and investment mandate/objective. Based on the distinct characteristics, the research finds that different SWF types have different consequences with regard to the accumulation and allocation of wealth. As a result different types of SWFs favour different social actors.

Chapter 3 provides a link to the theory by showing how the empirics of SWF-type variation in small open economies can be used to understand the weaknesses of standard explanations (i.e. efficiency and diffusion) and the strengths of other explanations (i.e. PNs). The chapter sets up the theoretical framework by addressing the question of how different PNs influence the set-up of financial institutions, with SWFs as instances. It offers a critique of PN analysis, and from this, it highlights the need to develop a PN analysis in terms of causal mechanisms, and specific hypotheses. It draws on key claims in PN literature and refines them through a selected case study on 'SWF types in Hong Kong and Singapore between 1960s and 1980s'.

Chapters 4–7 constitute the empirical core of this thesis. Chapters 4–5 draw attention to the broad similarities in the industrial domains of Hong Kong and Singapore in terms of their exposure to increasing external pressure from the late 1960s onwards. In both economies, similar actors were involved in the industrial domain – but they were structured differently. Confronted with increasing levels of international competition, debates started in Hong Kong and Singapore about how to respond to these pressures, and different PNs influenced responses. Chapter 4 shows how, in the early 1970s, Singapore's state-directed PN influenced decisions in the industrial domain about state finance institutions. Controversies about alternative choices, such as the abolition of the SWF via large-scale privatisation, reveal the awareness of different choices among socio-economic actors. The chapter draws attention to the actors' organisational profile in the policy-making process. It discovers exclusion as a mechanism through which Singapore's state-directed PN operated to influence the creation of a large government linked enterprise sector with state development banks and later into Temasek. It excluded domestic finance and manufacturing, whereas it included a small group of representatives from the Ministry of Finance. The chapter finds that actors that were not a part of the PN did not benefit from the SWF. Based on these findings, the chapter is able to develop an initial hypothesis that having a state-directed PN in the industrial domain increases the likelihood of creating an SWF with a development and diversification mandate and related state finance institutions.

Chapter 5 draws upon initial findings – developed from the analysis on Singapore's industrial domain – for further refinement. It investigates how Hong Kong's clientele pluralist PN affected policy choices in the industrial domain during the 1960s and 1970s. Hong Kong's clientele pluralist PN influenced the decision to not create state finance institutions with development mandates. Hong Kong instead opted for private finance institutions. Debates about the creation of a state development bank and of a state development fund, reveal the awareness of different policy options among socio-economic actors. After outlining the organisational characteristics of the actors, the chapter looks at inclusion and exclusion as potential mechanisms through which Hong Kong's clientele pluralist PN operated to influence policy choices. It finds that the PN included domestic private finance/commerce actors on important policy bodies, whereas it excluded industrialists. The findings support the initial hypothesis developed in the previous chapter on Singapore. With regard to the overall argument, the comparative evaluation of financial institutions set up in Hong Kong's and Singapore's industrial domain provides strong evidence for the limited impact of diffusion and efficiency.

Chapters 6–7 highlight similarities in the savings domains of Hong Kong and Singapore with regard to their high levels of domestic savings and their exposure to external pressures from the 1970s onwards. Confronted with inflation and increasing international investment opportunities, discussions began in both economies about how to respond to such pressures. In Hong Kong as well as in Singapore, similar actors were involved in the savings domain – but they were structured differently. The main argument of the two chapters is that different PNs in Hong Kong and Singapore influenced different policy responses in terms of the kinds of financial institutions that were set up. Chapter 6 shows how Singapore's state-directed PN in the savings domain influenced decisions about the creation of an SWF with a savings mandate, and links it to related state finance institutions. Debates illustrate that different choices, such as the creation of large private pension funds or the expansion of private commercial banking, were discussed by socio-economic actors in Singapore's savings domain. The chapter shows that powerful actors such as large domestic private banks, had little influence in the policy-making processes. It identifies exclusion as a mechanism through which Singapore's state-directed PN operated to influence decisions about the creation of an SWF with a savings mandate. While the PN excluded domestic private finance/commerce actors, it included a small number of state officials and international finance houses. The chapter shows how and why actors, excluded by the PN, did not benefit from the creation of the Government Investment Corporation. Based on these findings, an initial hypothesis is developed, namely that having a state-directed PN in the savings domain increases the likelihood of creating an SWF with a savings and international investment mandate.

Chapter 7 draws from initial findings – developed from the analysis on Singapore's savings domain – for further refinement. It shows how Hong Kong's clientele pluralist PN affected policy choices in the savings domain during the 1970s and 1980s. These choices refer to the set-up of private finance institutions (e.g. private insurance and fund management institutions) and the decision taken against creating state finance institutions with savings mandates, notably a CPF and related to that a SWF similar to the Government Investment Corporation in Singapore. Controversies reveal the awareness of alternative choices among the socio-economic actors. The chapter examines the organisational attributes of these actors. It finds that the PN included domestic finance/commerce actors and employer organisations on important policy bodies, whereas it excluded labour and social/welfare groups. It finds that actors that were a part of the PN benefitted from the kinds of financial institutions that were set up. The findings support the initial hypothesis developed in the previous chapter on Singapore. Concerning the broader argument, the comparative analysis of financial institutional choices in Hong Kong and Singapore's savings domains indicate the limited influence of diffusion and efficiency.

Building on the in-depth analysis of the four empirical case studies, Chapter 8 offers a plausibility probe in order to see whether results of additional cases are consistent with the findings and hypotheses developed in the chapters on Hong Kong and Singapore. In the period between the 1950s and 2000s, small open economies in the Gulf region adopted different types of SWFs, and these choices are consistent with their respective PNs. Drawing on the four case studies (Chapters 4–7) and the plausibility probe in (Chapter 8), Chapter 9 takes a wider view of the empirical studies and discusses the theoretical and empirical implications of the different case studies. The aim of the present research was to show that PNs are of consequence in explaining the kind of financial institutions that are set up; hence, the question of whether differences in domestic state-society structures influence choice and type of state finance institutions, and if so, how and why.

2. The Puzzle of Different Sovereign Wealth Funds

This chapter concerns the puzzle of the differences between SWFs, which are instances of state finance institutions. State finance institutions refer to organisations that are owned by the state and that focus on dealing with financial transactions, such as investments, loans and deposits, and the management of assets.[8] There are state finance institutions that manage private wealth, such as state saving banks and public pension funds, and there are others that manage sovereign wealth. Some of the more prominent examples of the latter are the various types of SWFs.

The establishment of one particular type SWF, among the variants that exist, is related to the outcome of choices about wealth creation and wealth allocation. The latter is often associated with decisions regarding the allocation of royalties from resource extraction, current account surpluses, or surpluses from foreign exchange intervention. But the choice between the various types of SWFs is also linked to decisions about other state finance institutions, such as public pension funds. The linkage between SWFs and other state finance institutions becomes most visible in small open economies without natural resources, for example, oil and gas. These economies must create sovereign wealth in first place, and there are a number of ways of doing this.

One way relates to restructuration of state-owned enterprises into new organisational forms, together with the use of the proceeds from the listing of state-owned enterprises on the stock market. This took place, for example, in Kazakhstan, Vietnam, Malaysia, Singapore, and Bahrain, where SWFs were created in order to restructure large state enterprise sectors.[9] Another route to sovereign wealth creation involves the possibility of translating private wealth into sovereign wealth, which can then be managed by a SWF. That can be done via state finance institutions. For example, under trustee legislation, public pension funds are mandated to be invested in assets with trustee status, notably government bonds. The government can then in turn invest the proceeds from the bond issuance internationally by creating an SWF with a savings mandate.

The literature on SWFs draws on a number of established studies that distinguish among different SWFs by highlighting a set of organisational features. These include ownership, legal status, and investment mandate/objective. These organisational features can also be applied on a broader level to distinguish SWFs from other state finance institutions and their private equivalents. As such, this research suggests that SWFs have their functional private equivalents,

[8] For similar definitions of finance institutions, see Investopia (2016).
[9] These SWFs refer to Mumtalakat (Bahrain), State Capital Investment Corporation (Vietnam), Khazannah Nasional (Malaysia), and Temasek (Singapore).

which can be compared and distinguished by means of these features. For example, the functional equivalent for state finance institutions in the domestic savings domain are private finance institutions, such as private pension funds, private banks, and private insurance organisations. The case is similar for state finance institutions in the industrial domain: their functional equivalents relate to private holdings and private commercial banks (see TABLE 2.1).

TABLE 2.1. *State Finance Institutions and their Private Equivalents*

Domains	**State Finance Institutions**	**Private Finance Institutions**
Savings	SWFs with savings mandates, state savings banks, CPFs, public pension systems	Private asset managers, pension funds, commercial banks, fund managers
Industrial	SWFs with development mandates, development banks, state investment holdings	Commercial banks, private holdings

As already highlighted, these decisions have various implications on the allocation of capital, and, as such, have varying consequences for different socio-economic actors. For example, the creation of a CPF with a linked SWF that has a savings mandate implies distributional consequences for domestic private organisations in the savings domain (e.g., private pension funds, private insurers, private banks, private asset managers, and private fund managers). That is because state finance institutions can compete in the accumulation and allocation of savings with private organisations.

Likewise, the creation of state finance institutions with development mandates implies distributional consequences for private actors in the industrial domain (e.g., manufacturers and private commercial banks). Through the developmental mandate, state finance institutions can make majority investments and compete both at the international as well as the domestic level, thereby crowding out the private sector. This is particularly the case when the state finance institutions are created without an explicit mandate to cater to private companies in the respective sector. This therefore suggests that the choices made with respect to the creation of state finance institutions will have varying consequences for socio-economic actors in the respective policy domains.

The different types of sovereign wealth funds (SWFs) across and within countries pose a profound puzzle for standard explanations, which highlight a close link between the creation of SWFs and the commodity price boom and global current account imbalances. Efficiency-based explanations refer to the arguments of economic efficiency, emphasising that the creation of SWFs follows functional imperatives such as issues related to diversification, future savings, smoothening of budgets, and currency stabilisation. Efficiency accounts suggest that specific national economic factors influence the creation of particular SWF types in a highly internationalised context. Referring to national economic factors, different SWF types are means of addressing external pressures, such as from increased capital mobility, inflation, currency volatility, and international competition pressures. The sources of external pressure can relate to financial and trade integration. Governments create particular types of SWFs to address aspects of international competition, currency volatility, or capital mobility arising from these pressures. Thus, countries with similar macro-national characteristics are expected to create similar SWF types. As a result, standard explanations would lead us to expect that countries with similar macro-national characteristics and confronted with similar challenges would act in a similar manner with regard to SWF creation.

Diffusion-based accounts highlight the role of ideas and refer to the arguments of peer-based contingent emulation. It occurs when countries emulate the policies of other countries "without reflection on the evidence of the efficacy of that policy" (Chwieroth, 2010, p. 3). Diffusion-based explanations highlight that the creation of SWFs reflects a process of contingent emulation among countries in similar peer groupings (Chwieroth, 2014). In this process, the creation of a particular SWF type is constructed as an adequate response for a country with certain characteristics and exposed to a specific challenge. Particular types of SWFs are symbols that "signal conformity with a peer group's standards of behaviour" (Chwieroth, 2010, p. 3). Unlike efficiency-based explanations, diffusion-based accounts consider the creation of SWFs as fashions or fads rather than rational and efficiency-driven considerations. For several scholars, most notably Chwieroth (2010), 'fashions and fads in finance matter' in explaining the creation of different types of SWFs. The expectations of diffusion accounts are that countries that are close and similar in certain ways (e.g. in structural characteristics, especially in their export profiles) will adopt similar SWFs when confronted with similar but separate challenges. For example, if it becomes fashionable for small open economies to create SWFs with development mandates, countries with similar characteristics will be more likely to create SWFs with development mandates.

However, a cursory look at countries and their macro-economic characteristics as well as the types of SWF established suggests a more ambiguous picture. Even small open economies with similar macro-national characteristics create different types of SWFs, indicating that factors other than 'efficiency' influence the creation of different SWF types (see TABLE 2.2.). Interestingly, SWF variation even occurs across small open economies within similar peer groupings, such as in Gulf Cooperation Council (GCC) economies, as well as in the small open economies of the Pacific and in the small open economies of Asia. This also presents a puzzle for diffusion-based explanations, which emphasise the role of emulation across countries within similar peer groupings.

TABLE 2.2. *Different Sovereign Wealth Fund Types in Small Open Economies.*

		Mandate		
		Stabilisation	**Savings**	**Development**
Investment Characteristics	**Allocation**	International Bond oriented	International Primarily Equity, Alternative Investments	International & Domestic, Direct Investments, Equity, Alternatives
	Risks	Low	Medium–high	Medium–high
	Horizon	Short-term	Medium–long-term	Medium–long-term
Empirical Instances		SWFs with **stabilisation** mandates	SWFs with **savings** mandates	SWFs with **development** mandates
Funding Sources	**Commodity**	*Revenue Equalization Fund (Kiribati),* *Trust Fund (Tonga)* *Trust Fund (Tuvalu)* *Stabilisation Fund (Papua New Guinea)* *Compact Trust Fund (Marshall Islands)* *Compact Trust Fund (Micronesia)* *Compact Trust Fund (Palau)*	*The Future Generation Fund (Bahrain),* *Qatar Investment Authority,* *Brunei Investment Agency,* *Government National Oil Account (Sao Tome and Principe),* *Abu Dhabi Investment Authority,* *Heritage Fund (Trinidad),* *Kuwait Investment Authority* *Timor-Leste Petroleum Fund* *Phosphate Royalties Trust Fund (Narau)*	*Investment Corporation of Dubai,* *Qatar Holding* *Qatari Diar* *Mubadala (Abu Dhabi)* *ADIC (Abu Dhabi)*
	Reserves	*Hong Kong Monetary Authority Ex. Fund* *Monetary Authority of Singapore Currency Fund*		
	Fiscal others		*Government Investment Corporation (Singapore)*	*Temasek (Singapore),* *Mumtalakat (Bahrain)* *IPIC (Abu Dhabi)*

Sources: Information compiled from SWF websites and SWF databases (e.g. ESADEgeo, 2014, p. 102; SWF Institute, 2014).

To solve this puzzle, the present study looks at the role of domestic politics. Thus far, the role of domestic politics and the ways in which it is related to the distributional consequences of the choices made with respect to various state finance institutions have remained largely un-investigated. SWFs are regularly referred to in the literature as instances of financial organisations or financial institutions (see Clark and Monk, 2011; Clark and Monk, 2013; Clark, Dixon, and Monk, 2013). Clark, Dixon, and Monk (2013) refer to SWFs as financial organisations and conceptualise SWFs as the result of policy decisions. Clark's statement that "the SWF is the product of a political decision" suggests a political dimension behind the creation of SWFs, meaning that decisions to create an SWF are also influenced by domestic politics (Clark, Dixon and Monk, 2013, p. 31).

This thesis goes further, by asking how and why domestic politics influences policy choices, in terms of whether or not to create an SWF, and, if so, of what type. This thesis examines the effects of domestic politics on the creation of the various types of SWFs. One of the key findings is that the differences between the various types of SWFs have important implications in terms of resource allocation for different socioeconomic actors. Based on these findings, this thesis develops a domestic-politics argument regarding SWF variation.

This study elaborates on the different SWF types in two ways relevant to the domestic politics argument. First, it draws on a number of established studies that distinguish among different types of SWFs by highlighting a set of organisational features (Hammer, Kunzel and Petrova, 2008; Al-Hassan et al., 2013). These include the ownership, the legal status, and the investment mandate/objective (Hammer, Kunzel and Petrova, 2008; Al-Hassan et al., 2013). Second, the study argues that these differences in organisational characteristics have relevance for domestic politics and important implications for socio-economic actors such as domestic private finance and international finance actors, as well as domestic businesses, because different SWF types distribute and reallocate large amounts of capital in different ways. These differences are important, particularly for small open economies. Due to their size, SWFs of small open economies are powerful economic institutions, and the existence of different types of SWFs favour different interests.

Section 2.1 provides a brief overview of academic accounts and of the empirical population. Section 2.2 highlights the value of studying SWFs in small open economies. Section 2.3 outlines the different types of SWFs. It uses well-established literature as a guide to outline a threefold shorthand typology in order to distinguish among SWFs in terms of their organisational features (i.e. SWFs with development, savings, and stabilisation mandates). It outlines efficiency- and diffusion- based explanations for each of these SWF types. Furthermore, it offers a domestic politics explanation that refers to the findings of the thesis. Unlike efficiency- and diffusion-based explanations, a domestic politics explanation emphasises the implications of different SWF types for the allocation of resources and distributional struggles.

2.1 LITERATURE AND EMPIRICAL POPULATION

There is a growing literature on the creation of different SWFs.[10] Authors have introduced a number of different SWF definitions.[11] Although there is no universally accepted single definition, SWFs share a set of broad similarities (Clark, Dixon and Monk, 2013). Common to all SWFs is their (a) ownership (i.e. SWFs are owned by the government, either directly or indirectly via the appointment of a board), (b) liabilities (i.e. SWFs have no direct liabilities), and (c) beneficiaries (i.e. SWFs are managed according to the objectives of the government, and the objective and mandate drives their investment; Clark, Dixon and Monk, 2013). As a result of these broad commonalities, Clark, Dixon and Monk (2013, p. 16) have defined SWFs as "government-owned and controlled (directly or indirectly) investment funds that have no outside beneficiaries or liabilities (beyond the government or the citizenry in abstract) and invest their assets, either in the short or long term, according to the interests and objectives of the sovereign sponsor" (Clark, Dixon and Monk, 2013, p. 16). This definition allows for the integration of SWFs that invest primarily internationally, and those that invest both domestically and internationally.

SWFs have recently experienced very fast growth in terms of number and size.[12] Within a single decade, between 2005 and 2015, assets under SWF management have increased by more than 600 per cent, from US$895 bn in 2005 to US$5,865 bn in 2014 (Rozanov, 2005, p. 1; ESADEgeo Annual Report, 2014, p. 103). This makes SWFs larger than the combined size of the global hedge fund and private-equity industry (*The Economist*, 17 January 2008). During the 2007/08 financial crisis, SWFs and their variation have been one of the most widely debated topics, attracting attention from economists, such as Lawrence Summers (see *The Financial Times,* 30 July 2007) and Truman (2008), politicians, notably the German Chancellor Merkl and the former French President Sarkozy (see Raphaeli and Gersten, 2008, p. 2) and the international financial press, including *The Financial Times*, and *The Economist*. A major concern amongst observers was the investment motives – whether driven by politics or economics – of different SWFs. The combination of size and 'novelty' has led commentators to describe SWFs as potential sources of stability or instability in the international economy.[14] While there are those, most notably Summers (Summers *quoted* in *The Financial Times,* 30 July 2007) who argue that SWF investments might be politically motivated and therefore destabilising, others, such as Srinivasan (2008), highlight the stabilising effect of long-term

[10] Some of the earlier studies on SWFs including, Blundell-Wignall et al., (2008), Truman (2008, 2010), Paulson (2009), Aizenman and Glick (2009), IMF (2008), El-Katiri et al. (2011), Frankel (2011), Flood and Marion (2001).
[11] For an overview of the different definitions and conceptions of SWFs see Capapé and Guerrero-Blanco (2013).
[12] According to some estimates, the size of global SWFs could reach by 2015 a volume of between US$12–14.4 trillion (Jen, 2007; Aizenman and Glick, 2008; Lyons, 2007).
[14] Within the SWF literature it is widely agreed that SWFs have been in existence at least since the 1950s.

investments made by SWFs. These views are related to their different characteristics and investment mandates.[15] An initial empirical review of data derived from the ESADEgeo Annual Report (2014), the SWF Institute (2015), Truman (2008), the IMF (2008), and individual SWFs (i.e. SWF reports and homepages) reveals that SWFs differ in many ways, such as in their funding sources, dates of establishment, sizes, and mandates/objectives (see TABLE 2.3).

TABLE 2.3. *The 60 largest Sovereign Wealth Funds.*

	Sovereign Wealth Fund	**Estab.**	**Funding source**	**Country**	**Mandate/ Objective**	**AuM in (US$ bn)***
1	Government Pension Fund Global	1990	Commodity	Norway	Saving	897.6
2	Saudi Arabian Monetary Authority Foreign Holdings	1952	Commodity	Saudi Arabia	Stabilisation	741.8
3	Abu Dhabi Investment Authority	1976	Commodity	UAE	Saving	589.0
4	China Investment Corp.	2007	Non-commodity	China	Development	575.1
5	Kuwait Investment Authority	1980s	Commodity	Kuwait	Saving	355
6	Government Investment corporation	1981	Non-commodity	Singapore	Saving	315
7	State Administration of Foreign Exchange	1990	Non-commodity	China	Stabilization	300
8	Temasek	1974	Non-commodity	Singapore	Development	215
9	National Social Sec. Fund	2000	Non-commodity	China	Saving	179.6
10	Qatar Investment Authority	2005	Commodity	Qatar	Development	175
11	Investment Corp of Dubai	2006	Commodity	UAE	Development	160
12	Samruk-Kazyna	2008	Commodity	Kazakhstan	Development	103.3
13	Australia Future Fund	2004	Non-commodity	Australia	Saving	97.57
14	National Wealth Fund	2008	Commodity	Russia	Stabilization	87.62
15	Revenue Regulation Fund	2000	Commodity	Algeria	Stabilization	77
16	National Oil Fund	2000	Commodity	Khazakhstan	Stabilization	72.7
17	Libyan Investment Authority	2006	Commodity	Libya	n/a	66
18	Hong Kong Monetary Authority Inv	1993	Non-commodity	Hong Kong	Stabilization	65.1
19	International Petroleum Investment Corporation	2000	Commodity	UAE	Development	63.4
20	Mubadala	2002	Commodity	UAE	Development	60.9
21	National Development	2011	Commodity	Iran	Development	58.6
22	Korea Investment Corporation	2005	Non-commodity	South Korea	Stabilization	56.6
23	Alaska Permanent Fund	1976	Commodity	US	Saving	51.1
24	Khazanah Nasional Berhard	1993	Non-commodity	Malaysia	Development	40.9
25	Brunei Investment Agency	1983	Commodity	Brunei	Saving	39
26	State Oil Fund of Azerbaijan	1999	Commodity	Azerbaijan	Stabilization	36.6
27	Banque Publique d'Investissement	2008	Non-commodity	France	Development	33.6
28	Texas Permanent School Fund	1854	Non-commodity	US	Stabilisation	30.6
29	New Zealand Superannuation Fund	2001	Non-commodity	New Zealand	Saving	25.51
30	National Pensions Reserve Fund	2001	Non-commodity	Ireland	Saving	20.2

Sources: Information compiled from SWF websites and SWF databases (e.g. ESADEgeo, 2014, p. 102; SWF Institute, 2014).
*AuM refers to estimates.

[15] For an overview of different SWF characteristics see Truman (2008), the IMF (2008), Gilson and Milhaupt (2008), Aizenman and Glick (2009), Beck and Fidora (2008).

TABLE 2.3. (CONT.) *The 60 largest Sovereign Wealth Funds.*

	Sovereign Wealth Fund	Estab.	Funding source	Country	Mandate/ Objective	AuM in (US$ bn)
31	New Mexico State Investment council	1958	Non-commodity	US	Saving	19.1
32	Alberta Heritage Savings Trust Fund	1976	Commodity	Canada	Saving	17.3
33	Timor-Leste Petroleum Fund	2005	Commodity	Timor-Leste	Stabilisation	15.7
34	Fondo de Estabilidad Economica y Social	2007	Commodity	Chile	Stabilisation	15.2
35	State General Reserve Fund	1980	Commodity	Oman	Stabilisation	13
36	Russia Direct Investment Fund	2011	Commodity	Russia	Development	10
37	Fondo de Estabilization Fiscal	2011	Commodity	Peru	Stabilisation	8.5
38	Fondo de Reserva de Pensions	2006	Commodity	Chile	Saving	7.5
39	Sovereign Fund of Brazil	2008	Commodity	Brazil	n/a	7
40	Mumtalakat	2006	Non-commodity	Bahrain	Development	6.8
41	Permanent Wyoming Mineral Trust Fund	1974	Commodity	US	Stabilisation	6.7
42	Fondo Strategico Italiano	2011	Non-commodity	Italy	Development	6
43	Oman Investment Fund	2006	Commodity	Oman	Development	6
44	Public Investment Fund	2008	Commodity	Saudi Arabia	Development	5.8
45	Quebec's Generations Fund	2006	Non-Commodity	Canada	Saving	5.2
46	Pula Fund	1994	Commodity	Botswana	Stabilisation	5.1
47	Heritage and Stabilization Fund	2000	Commodity	Trinidad and Tobago	Stabilisation	5.1
48	Fundo Soberano de Angola	2012	Commodity	Angola	Development	5
49	Alabama Trust Fund	1985	Commodity	US	Stabilisation	2.2
50	Oil Revenues Stabilization Fund of Mexico	2000	Commodity	Mexico	Stabilisation	1.9
51	Fonds de Stabilisation des Recettes Budgetaires	2005	Commodity	Dem Rep Congo	Stabilisation	1.7
52	Idaho Endowment Fund	1969	Non-commodity	US	Stabilisation	1.7
53	North Dakota Legacy Fund	2011	Commodity	US	Saving	1.7
54	Fondo de Ahorro de Panama	2011	Non-commodity	Panama	Stabilisation	1.4
55	Nigerian Sovereign Investment Authority	2011	Commodity	Nigeria	Multiple	1
56	Western Australia Future Fund	2012	Commodity	Australia	Saving	1
57	Fonds souverain d'investissement strategiques	2012	Non-commodity	Senegal	Development	1
58	Fondo para la Estabilizacion Macroeconomica	1998	Commodity	Venezuela	Stabilisation	0.7
59	Palestine Investment Fund	2003	Non-commodity	Palestine	Development	0.7
60	State Capital Investment Corporation	2006	Non-commodity	Vietnam	Development	0.7

Sources: Information compiled from SWF websites and SWF databases (e.g. ESADEgeo, 2014, p.102; SWF Institute, 2014).
*AuM refers to estimates.

The academic interest in SWFs and their variants across countries was triggered in 2005 by a short article titled 'Who Holds the Wealth of Nations?' (Rozanov, 2005). The article was written in the context of trade disputes between emerging economies, most notably China, and the US. In 2005, the state-owned China National Offshore Oil Corporation attempted to acquire two strategic US oil companies, Chevron Texaco and Unocal Cooperation; and in 2006, state-owned Dubai Ports World made an offer to purchase port facilities located in the US.[16] These offers were finally withdrawn because the host country had become increasingly suspicious of high-profile state-related foreign investments (Cohen, 2009). The fear of capital account protectionism was aggravated by a sudden rise in SWFs. In his article, Rozanov (2005) described a hitherto unnoticed phenomenon, and coined the term 'sovereign wealth funds'. Rozanov's article provided an initial description of SWFs as government-related pools of capital that are not state-owned enterprises nor traditional central bank reserves and divided SWFs, according to their funding source, into commodity and non-commodity funds (Rozanov, 2005).

Most analyses on the creation of different types of SWFs have been written by economists. They use established ideas of economic theory, which suggest the investigation of key economic indicators, such as reserve levels, macro-economic openness, level of fuel exports, on-going current-account surpluses, type of resource endowment, level of development, and the levels of economic diversification. They use well-established concepts and theoretical models including: budget cycles theory (e.g. Frankel, 2011), the concept of the Dutch Disease (e.g. Lee, 1997; Frankel, 2011), the concept of enhanced lending facilities (Feldstein, 1999), the permanent income hypothesis (e.g. IMF, 2008), factor endowment theory (e.g. Lee, 2007); and foreign exchange reserve management models (e.g. Flood and Marion, 2001; Aizenman and Lee, 2005). The creation of different types of SWFs is linked to macro-economic variables and to specific socio-economic challenges such as an ageing population, the need for economic diversification, or for avoiding the 'Dutch Disease'. Many accounts link the creation of different types of SWFs to differences in surplus wealth and to different socio-economic challenges. Many are correlational studies using large-N surveys for analysing the relationship between macro-level variables across countries and SWF variation (e.g. Aizenman and Glick, 2009). In general, they suggest that SWF variation can be explained by examining a set of macro-level variables in a given socio-economic context (e.g. an ageing population or the need for economic diversification in order to create new jobs).

[16] For a detailed overview of these controversies see Hufbauer, Wong and Sheth (2006).

These studies use illustrative samples and economic as well as financial theory to bolster their explanations of different SWF types and make policy recommendations. Lee (2007), for instance, links the specific factor endowment of a country to its SWF types. Countries that are abundantly endowed with natural resources should use their surplus wealth to establish SWFs with stabilisation or savings mandates, whereas economies abundantly endowed with labour should use their surpluses for the creation of SWFs with diversification mandates (Lee, 2007). Some of these accounts, such as Das et al. (2009), are prescriptive by offering a set of operational 'roadmaps' to policy makers, which consider the establishment of an SWF. By drawing on best practice and macroeconomic and financial theory, Das et al. (2009) offer recommendations to policy makers. According to Das et al. (2009), policy makers in economies with excessive surpluses – generated either from export activities or commodity revenues – have to make choices regarding the allocation of excessive surpluses. Objectives such as return maximisation for future generations or the stabilisation of fiscal revenues, as well as development considerations, influence these choices and thereby the SWF variation.

Much attention has been paid to investigating different types of SWFs across medium to large economies. Most of these analyses are single historical case studies, such as on SWFs in South Korea (Kim, 2012), Kazakhstan (Kemme, 2012), Australia (Eccleston, 2012), Malaysia (Jikon, 2012), Vietnam (Duc-Tho et al., 2012), China (Liew and He, 2012; Wu et al., 2012) and Russia (Fortescue, 2010). Some studies describe different types of SWFs within countries such as on SWFs in the US (Rose, 2011) or SWFs in Singapore (Elson, 2008); others look at SWF differences across GCC economies (Abdelal, 2009; El-Kharouf et al., 2010). These studies aim to explain the trajectory of SWFs by embedding their emergence in their respective countries' geopolitical and domestic economic contexts. Much has been written in descriptive single case studies on different SWFs regarding different countries (in terms of resource endowment) adopting different SWFs and about similar countries with similar SWFs. Surprisingly little focus has been placed on the systematic analyses of different SWFs across small open economies.

2.2 SOVEREIGN WEALTH FUNDS IN SMALL OPEN ECONOMIES

During the 2000s, virtually all of the small open economies established SWFs.[17] What makes the study of SWFs in small open economies specifically interesting is their relative and absolute weight in their domestic economic contexts. In terms of absolute weight, SWFs of small open economies account for nearly half of the 20 largest global SWFs (see SWF Institute,

[17] There are also exceptions, notably Luxembourg and Macao, which to date have not created a SWF. But recently there have been debates in Macao and Luxembourg about the creation of SWFs (*Macaubusiness*, 15 April 2015; from a conversation with an official from the Luxembourg Central Bank, 2014, December).

ESADEgeo, 2015). In terms of relative size vis-à-vis domestic economic indicators, SWFs from small open economies surpass those of larger economies. While the Chinese Investment-Corporation – with assets of US$332 bn – is equivalent to around 6 per cent of China's GDP (2010), Temasek's and GIC's combined asset size is equivalent to 135 per cent of Singapore's GDP (see TABLE 2.4). This is similar to other cases, such as small open GCC economies or small open island economies in the Pacific (see TABLE 2.4). There are only two small open economies where the SWF is equivalent to less than 20 per cent of the domestic GDP. In 21 out of the 30 cases, SWFs are significantly larger. Their size in terms of GDP ranges from 20 per cent to more than 300 per cent.

TABLE 2.4. *Small open economies and their Sovereign Wealth Funds as a part of their GDP.*

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

Sources: Information compiled from the SWF Institute (2014), ESADEgeo (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 $.

Sovereign wealth funds are not a new phenomenon for small open economies. Between the 1960s and 1980s, a significant number of small open economies such as Brunei, Singapore, Qatar, Kuwait, and Abu Dhabi established SWFs. This period saw dramatic changes in the global economy. Katzenstein's statement that this period was an era of "global inflation, increases in trade rivalries and protectionism, prolonged recession, volatile foreign-exchange markets, skyrocketing interest rates and debts, and structural adjustment" highlights the set of powerful economic pressures to which small open economies of that time were particularly exposed (Katzenstein, 1985, p. 22). Confronted with windfall revenues, many small open economies started to create SWFs in an attempt to adjust to the new international economic environment. For example, Kuwait created the Kuwait Investment Board in the early 1950s and the London Kuwait Investment Office in the early 1960s. In the 1970s, Qatar created the Qatar Investment Board – a predecessor of the Qatar Investment Authority. Likewise, Abu Dhabi created the Abu Dhabi Investment Authority in the 1970s, and Singapore established Temasek in the same decade. In the 1980s, Singapore created the Government Investment Corporation, and Brunei established the Brunei Investment Authority.

Small open economies offer 'hard cases' for studying the role of domestic politics in the face of powerful external forces. Unlike other countries, small open economies are fully exposed to international price signals and adjustment pressures through capital flows. They also tend to have large budget surpluses or high levels of foreign exchange reserves. Despite these similarities, these economies differ in terms of their resource endowment. While a number of small open economies – specifically GCC economies and island economies of the Pacific – are abundantly endowed with natural resources (e.g. oil, gas, phosphates), others, such as Hong Kong and Singapore, own few natural resources. Consequently, among the latter group, wealth creation is confined to export-oriented activities. To create surpluses that can be channelled into an SWF, small open economies without natural resources need to follow an export-oriented strategy. Even among small open economies within similar groupings (e.g. city states of East Asia, small open oil-/gas-exporting economies of the Middle East, and small phosphate exporting island economies of the Pacific), significant SWF-type variation occurs (see TABLE 2.4).

2.3 DIFFERENT SOVEREIGN WEALTH FUND TYPES

A number of typologies have been established to distinguish among SWF types. These range from simple distinctions between oil/commodity funds and non-oil funds/non-commodity funds (Rozanov, 2005; Kimmitt, 2008) to large typologies embracing up to five cells (IMF, 2008). Although recent attempts have been made to categorise SWFs in terms of historical-geographical maps, notably Clark et al. (2013), the most established way of differentiating among different SWFs is based on their different objectives (see IMF, 2008; Gilson and Milhaupt, 2008). Using function as the main defining criteria, scholars such as Gilson and Milhaupt (2008) as well as institutions, most notably the IMF (2008) and OECD (2011), have established heuristic typologies. For example, the IMF (2008) distinguishes among Stabilisation SWFs, Reserve Investment Corporations, Savings SWFs, Contingent Pension Reserve Funds, and Development SWFs. Gilson and Milhaupt's typology instead embraces three cells: Stabilisation SWFs, Savings SWFs and Development SWFs (Gilson and Milhaupt, 2008). Most authors and commentators, such as Lyons (2007), Pascuzzo (2008), and Gilson and Milhaupt (2008) highlight that SWFs as a group can be located on a 'continuum' of other sovereign investment vehicles. The two extremes of this continuum are central banks and state owned enterprises.

The threefold typology used in this thesis is based on the view that SWFs can be systematically differentiated in terms of their organisational characteristics, relating to their official mandate, ownership, and legal status. Ownership and legal status refer to whether the SWF is organised as a separate legal entity under specialist law, or under an existing entity (e.g. central bank) and whether the SWF owns the assets that it manages or whether it manages the assets on behalf of the central government, or the ministry of finance. This is directly connected to the investment mandate/objective (i.e. stabilisation, development, savings) which influences the asset allocation in terms of geography (e.g. domestic or abroad), asset class (e.g. bonds, equity, direct investments, real estate), and investment horizon (e.g. short- or long-term oriented).

Constructing a typology that embraces all possible organisational configurations would lead to a large number of analytical dimensions and thus a very large number of cell types. Therefore, this research follows Bailey's suggestion to use a shorthand categorisation (Bailey, 1994). As in a conventional typology, the aim of a shorthand typology is to minimise within-group variance and maximise across-/between-group variance (see Bailey, 1994). Studies on SWFs, notably Clark et al. (2013), frequently introduce shorthand typologies in order to distinguish among different types of SWFs. This research focuses on three main types, which capture the most important systematic differences among SWF types: SWFs with a savings mandate, SWFs with a stabilisation mandate, and SWFs with a development mandate (see TABLE 2.5).

TABLE 2.5. *Shorthand Typology of Sovereign Wealth Funds*
'Stylised Characteristics of SWFs with development, saving and stabilisation mandates'.

SWF types	**Characteristics**				
	Organisational structure	**Legal structure**	**Investment Structure**		
MANDATE			Time horizon/risk	Control/ Ownership	Allocation
Development	Separate legal entity that owns assets that it manages; The ministry of finance is usually the major shareholder of the SWF.	Company law in combination with special law or by specified decree.	Medium to long-term; medium to high risks.	Portfolio and majority investments.	Domestic & international assets; public and private-equity, real estate, bonds, alternatives.
Savings	Separate legal entity that does not own the assets that it manages. Typically the SWF is an investment management entity owned by the ministry of finance or the central government.	Company law in combination with special law or by decree.	Long-term, medium to high risks.	Portfolio investments.	International assets, public and private-equity, bonds, real estate, alternatives.
Stabilisation	No separate legal entity that manages asset. The owner of the assets is usually the central bank or the ministry of finance.	Central bank law or via fiscal law.	Short-term, low risks.	Liquidity oriented investments.	International assets, public equity, cash, gold government bonds.

Sources: Compiled from individual SWF websites, Hammer et al. (2008), Al-Hassan et al. (2013).

Though many SWFs can be classified as SWFs with stabilisation, savings, or development mandates, this dissertation asserts that these are 'ideal' types of SWFs.[19] As such, it is important to emphasise that meaningful variation can be found within these SWF types. For instance, SWFs with stabilisation mandates can be differentiated between those that focus primarily on monetary stabilisation and those that focus on budget smoothening and fiscal stabilisation. Furthermore, SWFs with stabilisation mandates can involve investment portfolios that are not primarily used for stabilisation purposes but for return objectives, as is usually the case when the funds are larger than what is needed for stabilisation purposes. In this case, the SWF outsources parts of the funds to third-party investment managers. Alternatively, it can also create a subunit with a different investment mandate. In turn, SWFs with savings mandates can allocate a part of their portfolio in domestic assets for stabilisation purposes. Similar to SWFs with savings mandates, SWFs with development mandates can also invest minority stakes into long-term assets for the purpose of return. In addition to this, some SWFs have multiple objectives, such as stabilisation, savings, and development (e.g. Kazakhstan's SWF) or stabilisation and savings (e.g. Norway, Azerbaijan or Botswana; Al-Hassan et al., 2013). In cases where an SWF has multiple mandates, meaningful organisational variation within the SWF can also be found in terms of the existence of subunits with specific mandates.

[19] Academics, such as Gilson and Milhaupt (2009), as well as international organisations, notably the IMF (2008) have followed these classifications.

SOVEREIGN WEALTH FUNDS WITH SAVINGS MANDATES[20]

SWFs with savings mandates differ from other state finance institutions in the savings domain, notably state-run CPFs or state-owned savings banks. The most prominent differences between these institutions relate to their liability structures. While public pension funds have explicit liabilities (e.g., workers' pensions), SWFs do not. In contrast to SWFs, state-owned savings banks and CPFs manage private wealth (e.g., deposits from the population). However, there is a direct link between the creation of SWFs and public pension funds, especially in countries with limited domestic investment opportunities. Public pension funds under trustee legislation accumulate private wealth and try to get exposure into risk free and secure assets, notably government bonds.[21] However, countries with budget surpluses do not need to issue bonds in order to finance public expenditure. One way of addressing this is the creation of an SWF as an institutional means to invest the proceeds from the issuance of government bonds in international assets with higher risk-return profiles.

In organisational terms, SWFs with savings mandates differ from other SWF types, as they are commonly created as private corporations under company law in combination with constitutional law or by decree (see Hammer, Kunzel and Petrova, 2008). They are established as separate legal fund management entities, under a mandate given by the ministry of finance or the central government with full authority to act (Al-Hassan et al., 2013, p. 9). They manage assets on behalf of the central government or the ministry of finance, which are the formal owners of the assets. As such, SWFs with a savings mandate do not usually own the assets that they manage. Their organisational features are directly related to their primary function of maintaining the long-term purchasing power of national wealth. Unlike SWFs with development or stabilisation mandates, the principal objective of SWFs with savings mandates is return maximisation. This type of SWF is also known as 'reserve investment corporations' or 'future generations funds', 'contingent pension reserve funds' or 'generic sovereign wealth funds' (Blundell-Wignall, 2008; IMF, 2008; Griffith-Jones and Ocampo, 2010).

Efficiency- and Diffusion-based Explanations

Scholars explain the creation of SWFs with savings mandates by referring to a country's resource endowment and policy challenges. Efficiency-based accounts treat the state as an unified actor (IMF, 2008; Al-Hassan et al., 2013). Efficiency based accounts appear descriptive because they explain the creation of SWFs with savings mandates with reference to domestic

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[20] Examples of SWFs with savings mandates include the Australian Future Fund, the Kuwait Investment Authority, the Abu Dhabi Investment Corporation, the New Zealand Superannuation Fund and the Government Investment Corporation.

[21] It should be mentioned that some public pension funds, notably the Californian Public Employees' Retirement System, take more active investment approaches by investing internationally into variaous asset classes, such as public equity and real estate. This let them make look similar to SWFs with savings mandates (see annual ESADEgeo reports and SWF Institute, 2015).

factors. They highlight the rationality of decisions and the national interest behind the creation of SWFs with savings mandates. For example, countries with more surpluses/reserves than are needed for stabilisation purposes and with an ageing population are expected to create SWFs with savings mandates, which are “set up to meet identified outflows in the future with respect to pension-related contingent-type liabilities” (Al-Hassan et al., 2013, p. 6). Examples include the Australia Future Fund, the Irish National Pension Reserve Fund, and the New Zealand Superannuation Fund (Al-Hassan et al., 2013, p. 6). This is also the case in resource rich countries, which try to ensure that future generations can benefit from the resources after their depletion (Griffith-Jones and Ocampo, 2010, p. 6). SWFs with savings mandates share wealth across generations by “transforming nonrenewable assets into diversified financial assets” (Al-Hassan et al., 2013, p. 5). For example, the Kuwait Investment Authority and the Abu Dhabi Investment Authority refer to SWFs with a mandate of sharing wealth across generations. Similarly, reserve investment corporations such as the Korea Investment Corporation and Singapore’s GIC, aim to earn higher return on excess reserves (Al-Hassan et al., 2013). Although each of these SWFs may have different specialist objectives (e.g. saving for future generations, meeting contingent pension liabilities not covered by pension schemes, or preservation of the long-term purchasing power of reserves), they share the common goal of ensuring that a country’s savings are optimally deployed over the long term.

Unlike efficiency-based accounts, diffusion-based explanations highlight the role of peer-based contingent emulation in the creation of SWFs with savings mandates. A diffusion scholar treat the creation of an SWF with savings mandate as a socially constructed fashion and a symbol that “signal[s] conformity with a peer group’s standards of behaviour” (see Chwieroth, 2010, p. 3). The expectations of diffusion accounts would be that countries create this type of SWF when countries in their peer group have created SWFs with savings mandates when facing the question of how to preserve the future purchasing power of a country’s savings. This question is often connected to other issues ,such as demographic challenges (e.g. an ageing society) or structural socio-economic constraints (e.g. high import ratios). The process by which this is done is considered as peer-based contingent emulation. Unlike ‘learning’, emulation takes place when countries adopt a similar policy or ‘best practice’ (i.e. by creating an SWF with a savings mandate) without deliberating on the evidence of the effectiveness of that best practice (Chwieroth, 2010, p. 3). Most of the SWFs are non transparent and this makes it very difficult to assess the efficacy of SWF for other countries (Chwieroth, 2014)

When it becomes fashionable to create an SWF with a savings mandate among particular countries, countries with similar characteristics are more likely to create that type of SWF (Chwieroth, 2010). Hence, small open economies with a similar structural profile located in similar regions are expected to create SWFs with savings mandates if peers created that type of

SWF when confronted with a similar challenge. Given that emulation happens among countries with similar structural features it is difficult to dissect the effects of similar rational economic consideration from that of emulation. Furthermore, diffusion can also happen through alternative paths, such as cultural and bilateral relationships, and emulation can happen among countries with different structural profiles that are located in different regions, Indicates alternative paths to emulation.

Domestic Politics-based Explanation

The domestic politics explanation of SWFs with a savings mandate refers to the findings of this dissertation. This thesis investigates whether domestic politics (i.e. domestic structures) can explain the puzzle whereby different types of SWF exist across small open economies within the same region as well as within the same peer groupings. It uses a policy network (PN) analysis of this puzzle to develop hypotheses about why and how policy networks affect financial institutional choices.

Unlike efficiency- and diffusion-based accounts, this thesis conceptualises the creation of state finance institutions with savings mandates as the result of policy-making and policy decisions. It looks at the domestic structures and their effects on policy decisions. Decisions on the creation of state finance institutions in the savings domain, which concerns the allocation of public and private surpluses and savings. Therefore, to understand the variation among choices on SWFs with savings mandates, it is necessary to adopt a meso-level perspective. Using an established stream of PN analysis (Atkinson and Coleman, 1989) as a starting point, it investigates how the structure of state-society relations affects policy choices in the savings domain. Therefore, it looks at the potential mechanisms whereby domestic structures might have operated to affect the creation of state finance institutions with savings mandates.

The creation of state finance institutions with savings mandates has implications for the allocation and accumulation of domestic wealth and thus has direct distributional consequences for socio-economic actors. For example, it is common to observe that SWFs with savings mandates spread their risks through portfolio investments across a large spectrum of assets with an international focus. They usually have an explicit mandate to invest into international assets, notably international equity. SWFs with savings mandates often privilege international finance houses to the disadvantage of domestic private financial institutions. Similarly through their operations, state run central provident funds withdraw capital from the domestic economic system and transfer current wealth/consumption into future wealth/consumption. For private domestic finance actors (e.g. private commercial banks, pension funds), CPFs can be competitors in the quest for savings. In stark contrast, international finance actors can benefit from SWFs and CPFs with savings and international investment mandates in a number of ways, such as through investment outsourcing, wealth management, or co-investment.

SOVEREIGN WEALTH FUNDS WITH DEVELOPMENT MANDATES[22]

SWFs with development mandates differ from other state finance institutions in the industrial domain, notably development banks, statutory boards, and state holding companies. Although the line of differentiation is thin, it becomes most prominent in terms of their legal status. While state holdings, statutory boards, and development banks are often established as public law entities and invest primarily in domestic assets, SWFs with development mandates are not purely public entities under state ownership. Instead, SWFs with development mandates are often established under private company law with constitutional status. In terms of mandate and investment structure, SWFs with development mandates are similar to development banks and state holdings. Like development banks and state holdings, SWFs with development mandates may have direct holdings in companies and they may raise capital by issuing bonds. Therefore, a number of similarities in these structural characteristics make it difficult to sharply differentiate between SWFs with development mandates on the one hand and state holdings and state development banks on the other.

Sovereign wealth funds with development mandates differ from other SWF types. Unlike SWFs with stabilisation or savings mandates, SWFs with development mandates usually own the assets that they manage and follow the 'investment company model', as happens when assets are actively managed and when the SWF takes majority stakes in companies (Al-Hassan et al., 2013). They usually "take the form of state-owned corporations also with distinct legal persona" (Al-Hassan et al., 2013, p. 9). Commentators, most notably Fernandez (2008), describe these types of SWFs as government vehicles that manage government direct investments in companies. Direct investments are generally referred to as investments which are sufficiently large to affect a firm's management decisions. For conceptual reasons, this project applies a narrow view by categorising an SWF ownership stake of 51 per cent as majority/direct investment. SWFs of small open economies with between 51 and 100 per cent ownership of companies include Temasek, Mumtalakat, Qatar Holding, and the Investment Corporation of Dubai (see TABLE 2.6).[23] Unlike other SWFs, SWFs with development mandates issue bonds. Schena and Chaturvedi's statement that "[f]unds with a development or transformational mandate often have a different operating model, which requires sizeable amounts of both short and long-term operating capital to support their investment programs and the liquidity or capital needs of portfolio companies" highlights the rationale behind the bond issuance (Schena and

[22] Examples of SWFs with development/diversification mandates include Mumtalakat (Bahrain), Mubadala (Abu Dhabi), Temasek (Singapore), the China Investment Corporation; Khazanna Nasional (Malaysia) and the Vietnam State Investment Corporation.

[23] Other examples not mentioned including the International Petroleum Investment Corporation, the Abu Dhabi Investment Corporation and Qatar Diar.

Chaturvedi, 2011, p. 2). Another reason behind the issuance of bonds among SWFs with development mandates is the desire to develop and deepen domestic capital markets (Schena and Chaturvedi, 2011).

TABLE 2.6. *Asset Allocation of SWFs with Development Mandates.*

Selected SWFs	Total Holdings in			Selected Domestic Firms where the SWF holds at least 51%
	Size billion US$	**Foreign Assets**	**Domestic Assets**	
China Investment Corporation	$332.4	49%*	51%*	Central Huijin (one of the two investment arms of China Investment Corporation); China Construction Bank, Bank of China, ICBC, Agricultural Bank of China
Temasek (Singapore)	$145.3	68%	32%	Singtel, PSA International, Neptune Oriental Lines, Singapore Airlines, CapitaLand, Singapore Power
Khazanah Nasional (Malaysia)	$36.8	11%*	89%*	ACR Capital Holdings, Malaysian Agri Food Corporation, Proton Holdings, Cement Industries of Malaysia, UEM Group, Telecom Malaysia
Investment Corporation of Dubai	$19.6	n/a	n/a	Emirates NBD Bank, Noor Islamic Bank, Emirates National Oil Company, Dubai Aluminium Company, Emaar
Mubadala (Abu Dhabi)	$13.3	n/a	n/a	Abu Dhabi Aircraft Technologies, Petrofac Energy, Abu Dhabi Terminals, Emirates Aluminium, du-Emirates Integrated Communications, Zayed University,
Mumtalakat (Bahrain)	$9.1	n/a	n/a	Bahrain Aluminium, Gulf Air, Bahrain Telecommunications
State Capital Invest. Corporation(Vietnam)	$0.5	n/a	n/a	Vietcombank, Vinamilk, FPT Telecom, Vietnam National Reinsurance Corporation, Vietnam Construction Import Export , Corporation, Jetstar Pacific Airlines.

Sources: Information compiled from the SWF Institute (2011), Temasek (2011), Khazanah Nasional (2011), Reuters (2009), SCIC (2009), Mubadala (2011), CIC (2011), Mumtalakat (2007).
*Calculated on the basis of data from Truman (2008).

SWFs with a development mandate are typically set up under company law in combination with constitutional law or by decree, as a formally private company owned by the state, and often with a structure that differentiates among the owner, board, and operational management (Hammer, Kunzel and Petrova, 2008; Al-Hassan et al., 2013). Although SWFs with development mandates own the assets that they manage, they themselves are usually formally owned by the ministry of finance or the government. This makes them directly accountable to the ministry (or, in some cases, to the government or the parliament).

The ministry of finance is commonly the major shareholder and thus responsible for board appointments. Hammer, Kunzel and Petrova's statement that "[t]he Minister of Finance ensures that the Board is competent to oversee the activities of the SWF, but the government operates at arm's length and does not get involved in the business and investment decisions of the SWF" suggests strong links between the SWF and the Ministry of Finance (Hammer, Kunzel and Petrova, 2008, p. 10). The appointment of senior officials often ensures a close connection between SWFs and the political elite. The principal objective of SWFs with development mandates relates to the governments' aim of securing economic growth, socio-economic development and economic transformation (IMF, 2008; Schena and Chaturvedi, 2011). Al-Hassan et al.'s statement that "[d]evelopment funds are established to allocate resources to priority socio-economic projects" highlights that economic transformation objectives play an important role (Al-Hassan et al., 2013, p. 5). As a result, these types of SWFs are also referred to in the literature to as ‘development SWFs’, ‘development funds’, ‘industrial SWFs’, ‘productivist SWFs’ and ‘state investment holdings’ (Griffith-Jones and Ocampo, 2010; IMF, 2008; Clark et al., 2013; Kumar, 1992). Common to all is the broad aim of supporting economic diversification and transformation or diversification in other asset classes through direct investment or strategic partnerships.

Efficiency- and Diffusion-based Explanations

Efficiency-based accounts emphasise the role of a country’s identifiable development and diversification challenges as the main drivers behind the creation of SWFs with development mandates. These explanations are very functionalist and sometimes even tautological. For example, they explain the existence of SWFs with development mandates as a response to the need for economic diversification. Drawing on classical trade theory authors, such as Lee (2007), suggest that countries, which are abundantly endowed with natural resources should use these to diversify into other economic activities. In his study on ‘Sovereign Wealth in Abu Dhabi’, Abdelal (2009) explains the existence of the Mubadala development SWF through its mandate of development. According to Abdelal (2009), this mandate is shaped by Abu Dhabi’s attempt to diversify its oil-centred economic activities to other sectors (e.g. basic metals, aerospace, tourism, real estate). This is particularly the case for commodity-exporting countries. Their specific purposes can vary, ranging from restructuring the public enterprise sector, a means of facilitating government control over public assets, or a way to guide industrial development within a country’s overall development strategy (see Kumar, 1992). Others, especially Griffith-Jones and Ocampo (2010) and the IMF (2008), go further by defining them vis-à-vis the industrial policies of the respective government. They describe them in terms of their activities of funding socio-economic projects that target a country’s output growth and infrastructure development (Griffith-Jones and Ocampo, 2010; IMF, 2008).

A supporter a diffusion-based explanation would argue that the creation of SWFs with development mandates takes place through a process of emulation, in which countries create SWFs with development mandates when their peers have created that type of SWF when confronted with similar challenges, such as international competition, industrial upgrading, or industrial re-organisation. As mentioned before, an SWF with a development mandate can be conceptualised as a socially constructed best practice meant to address particular challenges. Given that the effectiveness of SWFs in responding to these challenges remain uncertain the adoption of these types of SWFs may not be driven by similar rational concerns but more by fads and fashion (see Chwieroth, 2014).

The expectations with respect to diffusion accounts are that countries with similar structural characteristics (e.g., similar export profiles) and confronted by similar challenges in industrial development and diversification will adopt their peer countries' behaviour with respect to the creation of SWFs with development mandates. Consequently, when it becomes fashionable for small open economies to create state finance institutions with development mandates, countries with similar structural characteristics will be more likely to create SWFs with development mandates. Due to the diffusion scholar's focus on analysing the effects of emulation on countries with similar structural features, it is difficult to differentiate between the effects of economic considerations and those of emulation. Emulation, furthermore, can also happen across countries with dissimilar structural features. In addition, diffusion scholars need to look at alternative paths of diffusion, including political/diplomatic relationships and policy learning.

Domestic Politics-based Explanation

As does the domestic-politics explanation of SWFs with a savings mandate, a domestic-politics explanation of SWFs with a development mandate relates to the findings of this thesis. The thesis examines whether domestic politics, especially domestic structures, can explain the puzzle whereby different SWF choices are made across small open economies exposed to similar external pressures with regard to competition and diversification. It draws on a PN analysis of this puzzle in order to develop hypotheses about why and how policy networks affect financial institutional choices in the industrial domains of small open economies.

Unlike efficiency and diffusion accounts, this research conceptualises the state finance institutions with a development mandate as the consequence of industrial policy-making and policy decisions. A politics-based explanation shows that domestic politics play an important role in influencing policy decisions concerning state finance institutions with development mandates. To demonstrate this, the thesis looks at domestic structures across countries and across policy domains. It examines how the structure of state-society relations in the industrial domain influences policy choices. It investigates the mechanisms whereby domestic structures might have operated to influence choices concerning SWFs with development mandates and related state finance institutions such as state holdings and state development banks. These institutions are characterised by specific organisational characteristics that have particular distributional implications.

Choices concerning the creation of SWFs with development mandates have important implications for the allocation of industrial capital and thus have direct consequences for socio-economic actors in the industrial domain. Their organisational characteristics allow these types of SWF to make majority direct investments in both domestic and international enterprises. The international investments of SWFs with development mandates generally have some sort of strategic connection with the domestic economy (Schena, 2012). The legal status and privileges under which an SWF with a development mandate operates are important factors affecting the degree of competition between the state and private enterprises (e.g. in terms of tax, transparency, capital access, biding for government tenders). Due to their size, their special legal status, and state backing, these types of SWFs enjoy a number of advantages vis-à-vis private sector corporations in terms of market power, political access, and in terms of credit access. There are close connections between SWFs, subsidiaries, and the banking system, as some of the SWF have banks as their subsidiaries, which may then supply preferential credit. They can assume a competitive role vis-à-vis domestic private socio-economic actors, such as in bidding for contracts, and can thus harm private businesses operating in similar sectors (e.g. real estate, retail banking, fund management, commerce and logistics)

SOVEREIGN WEALTH FUNDS WITH STABILISATION MANDATES[25]

Sovereign Wealth Funds with stabilisation mandates have organisational features that make them distinct from other SWF types. They are established under general fiscal law or central bank law, usually without a separate legal identity. Instead of creating a separate legal entity, it is common for the principal owner (e.g., either the central government or the Ministry of Finance) to use the central bank as an agent. These funds are usually owned and controlled by the Ministry of Finance and operationally managed by the central bank (Hammer, Kunzel, and Petrova, 2008; Al-Hassan et al., 2013). When the central bank acts as an agent, the principal remains accountable to the legislature (Hammer, Kunzel, and Petrova, 2008, p. 9). The fund is often a unit within the central bank. It is usually integrated in the broader framework of fiscal/monetary policy and budgetary processes. The function of SWFs with stabilisation mandates can relate to the smoothing of budget revenues and/or the smoothing of currency fluctuations, and/or hedging against capital supply shocks in an international environment of high capital mobility (Al-Hassan et al., 2013). They absorb excessive liquidity (i.e. money supply) in periods of high external income (Lee, 1997, p. 1).

Without the absorption of excessive liquidity through an SWF (e.g., in commodity-exporting countries during boom times), capital inflows can cause the appreciation of the domestic currency and thus undermine the international competitiveness of the domestic industry. These types of SWFs are also known in the literature as 'stabilisation funds', 'rainy day funds', and 'commodity stabilisation funds' (Flood and Marion, 2001; Lee, 1997; Aizenman and Glick, 2009). SWFs with stabilisation mandates have an investment mandate that is oriented towards very liquid and highly safe assets, such as currency derivatives or bonds. They have a short-

[25] Examples for SWFs with stabilisation mandates include the Hong Kong Monetary Authority, the Monetary Authority of Singapore, the Stabilisation Fund Portfolio Trinidad and the Revenue Equalisation Fund (Kiribati), the Petroleum Fund (Timor Leste), the Economic Stabilisation Fund (Chile).

term international investment horizon in order to guarantee liquidity for fiscal or monetary purposes (Hammer, Kunzel and Petrova, 2008).

It is important to emphasise that this study does not examine SWFs with stabilisation mandates, though they are an important SWF type, for two reasons. First, such SWFs deal with a rather different set of issues, particularly about monetary policy, which are not directly linked to industrial policy and domain-level policy analysis, the focus of the PN literature.[27] At the current stage of research, an investigation into monetary policy and SWFs with stabilisation mandates would go beyond the scope of PN analysis, particularly as the analytical focus of PN studies is on the meso- or domain level, whereas the analytical level of monetary policy is located at the macro-level. Monetary policy affects socio-economic actors with different characteristics across policy domains in different ways.[28] The introduction of a macro-level dimension into a meso-level centred study would introduce another layer of complexity into the analysis.[29] Second, this thesis concentrates on SWFs with savings and development mandates because of space constraints and the lack of empirical material on SWFs with stabilisation mandates.

CONCLUSION

This chapter outlines the different types of SWFs according to their organisational characteristics. Efficiency-based explanations use arguments of economic efficiency, and efficiency accounts treat the creation of different SWF types as rational responses of policy makers to policy problems – independently of any other country's policy responses. Diffusion accounts treat the creation of different SWF types as the outcome of the contingent emulation of 'best practices' among peers facing similar challenges. The creation of different SWF types across small open economies presents a puzzle for both diffusion- and efficiency-based explanations.

[27] Thus far, PN analysis has been applied on definable separate policy domains and sectors, such as the industrial domain (Atkinson and Coleman, 1989; Wright, 1990; Dunn and Perl, 1994), the finance and saving domain (McConnell, 1993; Josselin, 1995; Coleman, 1994), the health sector (Rhodes and Wistow, 1988; Proven and Milward, 2001, Kay 2006), the education sector (Raab, 1992, Homeshaw, 1995), the energy sector (MacInnes, 1991; Toke, 2000), the environment (Howlett and Rayner, 1995; Jost and Jacob, 2004) and agriculture (Daugbjerg, 1998a; 1998b; Montpetit, 2002; Botteril, 2005).

[28] For example, different socio-economic actors have different policy preferences with regard to currency stabilisation policy. Enterprises and businesses engaged in finance and export-oriented activity are assumed to be sensitive to currency volatility and to exchange risks (Broz and Frieden, 2001). As a result they want clarity and predictability with regard to their exchange rate vis-à-vis the currency of trading partner (Yam, 1998). For example, SWFs with stabilisation mandates sustain this via the buying and selling of currency. In contrast, socio-economic actors who do not carry currency risks, such as labour, social welfare or domestic retail prefer autonomous monetary policy with floating exchange rates or managed floats.

[29] The literature on Open Economic Policy is more suitable to study domestic politics at macro level and its implications (for a critical overview of the Open Economic Policy literature see Lake, 2009).

To draw a more comprehensive picture of the drivers behind different SWF types, this chapter outlines a third perspective. To account for the unexplained variation in terms of different types of SWFs across and within countries, this thesis suggests looking at domestic politics. The creation of different types of SWFs is treated as the outcome of policy decisions. As mentioned, these decisions have different implications for the allocation of capital and thus have different consequences for different socio-economic actors.

This study suggests that decisions regarding the creation of different SWF types have different consequences for socio-economic actors in different policy domains. For example, a SWF with a savings mandate accumulates domestic savings and channels significant amounts of domestic wealth into international financial assets, including equity, debt, and international real estate. This implies distributional consequences in the form of crowding out domestic private organisations in the saving domain (e.g. private pension funds, private insurers, private banks). Likewise, an SWF with a development mandate makes majority and direct investments into companies, competing on both the international and domestic fronts. As a result, the creation of a SWF that allocates capital among its subsidiaries and competes with private companies implies distributional consequences in the form of crowding out for private companies in similar sectors.

3. Bringing Domestic Politics In: Policy Networks, Differences, Variation in State Finance Institutions

This thesis investigates how and why domestic politics affects the creation of different state finance institutions. After a brief review of relevant literatures, such as on the second image reversed (Rogowski, 1989; Frieden, 1991; Milner, 1988), the developmental state (Johnson, 1982; Amsden, 1989; Wade, 1990) and state-business relations (Maxfield, 1990; Maxfield and Schneider, 1997; Schneider, 2004), it engages with a well-established literature on policy networks (Katzenstein, 1985; Atkinson and Coleman, 1989; Dunn and Perl, 1994). This literature highlights that, even in small open economies, the structures of state-society relations matter in policy making and in how these economies deal with adaptation to the international environment (Katzenstein, 1985). Several scholars, most notably Katzenstein (1985), look at how different state-society relations among small open economies affect economic policy, especially in the industrial domain. Although established academic accounts, such as Katzenstein (1985) commonly define ‘small open economies’ as smaller European states such as Austria, Sweden and Switzerland, the salient analytical features also apply to small open non-European economies. The notion of small open economies refers not to the relative or absolute GDP size but to socio-geographic factors. Small land size has important implications for wealth creation and the socio-economic structure (e.g. a weak or non-existent powerful agricultural sector and landowning class). The specificities of small open economies, such as the lack of large domestic markets and their specification towards exports orientation, makes them to ideal cases for the study of the effects of domestic structures on adjustment strategies to external pressures. Given powerful international economic pressures, policy choices of small open economies – especially in economic domains – are expected to be least likely driven by domestic structures. This research looks at small open economies in East Asia and the Middle East. Because of their high openness, small open economies in these regions are vulnerable to changes in the global economy. Despite their similarities in terms of exposure and resource endowment, they adopt different policies, reflecting different domestic politics.

This study deals with the question of how much choice small open economies have in economic policy-making, given the sweeping international pressures and domestic constraints. What is the importance of domestic politics in decisions about the kinds of finance institutions set up? Are the choices about SWF creation driven by macro-national features and external pressures or do domestic structures matter? This research uses a stream of policy network (PN) literature that offers typologies and treats state-society relations as an independent variable and policy choices as a dependent variable (Atkinson and Coleman, 1989; Dunn and Perl, 1994). A critique of this literature reveals limitations in terms of causal mechanisms and hypotheses.

Section 3.1 sets out relevant literatures, which look at how domestic structures affect policy choices. By doing that it outlines the rationale for choosing a PN approach. Section 3.2 delineates the salient features of a well-established stream of the PN literature on policy network typologies, highlighting the appropriateness of this literature for the purpose of the present research. Section 3.2 critiques this literature, uncovering its weaknesses. It responds directly to these weaknesses by outlining this thesis' research objective concerning the development of hypotheses and the provision of causal mechanisms. Section 3.3 links the research objective to the research design and cases. The findings developed from this analysis as well as the broader theoretical contribution to and implications for PN research are outlined in Chapter 9.

3.1 DOMESTIC STRUCTURES AND RELEVANT LITERATURE

There is a rich scholarly literature that treats policy outcomes as the result of domestic structures. This section does not attempt to provide a comprehensive literature review, but instead sets out some of the most influential literature streams as well as their salient features concerning domestic structures and policy outcomes. Among the most prominent are approaches that refer to studies in the tradition of the 'second image reversed' (SIR), which investigate how international events affect domestic politics and policy outcomes (Rogowski, 1989; Frieden, 1991; Milner, 1988). SIR accounts investigate how external pressures operate by influencing costs and opportunities for domestic producer groups and how these influence decisions about policy responses. Differing preferences among producer groups lead to predictable conflict lines and result in producer groups engaging in maneuvering and coalition-building. However, academic accounts vary in terms of how they expect coalition formation. For example, Milner (1988) uses neoclassical economics and trade theory to derive the interests of various socioeconomic actors vis-à-vis their preference towards free trade and protectionism, whereas Rogowski (1989) deduces domestic political alignments from factor-endowment and trade exposure. Despite this variation, all agree that policy outcomes must be traced to these struggles among socioeconomic actors that form coalitions.

However, policy outcomes are sometimes difficult to explain in purely coalitional or resource terms. Such is the case when actors with a great deal of resources exercise little influence in the policy-making process, while at the same time those with scant resources exercise greater influence. More recent SIR accounts highlight that what matter are not only maneuvering and coalition-building among actors, but also the position from which actors use their power

(Cowhey, 1993; MacIntyre, 2001; Bernhard and Leblang, 1999; Rogowski, 1999). For example, the way that institutions structure actors in Japan's policy-making process gives the very small farming sector disproportionate leverage over trade policy (see Cowhey, 1993). Scholars such as Cowhey (1993), therefore, highlight the need to bring in such institutions as electoral and party systems and legislative bodies that can serve to aggregate interests in the policy-making processes.

Political systems with a greater number of veto players face greater challenges in the face of external shocks and are less likely to initiate reforms (MacIntyre, 2001). In line with that, Rogowski (1999) argues that majoritarian systems exhibit greater flexibility in responding to challenges than proportional-representation systems. However, it is sometimes observed that patterns of inclusion and exclusion of actors from policy bodies are not necessarily based on electoral districts or party systems. Although recent SIR accounts bring in the role of institutions, they are less concerned with the independent role of the state in influencing policy outcomes.

Parallel to SIR research, another influential literature stream has emerged that emphasises the independent role of the state in explaining the success or failure of economic policy. Studies on the developmental state emerged in the 1980s and 1990s as a counter-critique of the neoclassical developmental theory (Johnson, 1982; Amsden, 1989; Wade, 1990; Öniş, 1991). In contrast to neoclassical developmental theory, developmental state theory highlights a combination of institutional and political factors that shape the pattern of state-market relations, which in turn affects the formulation and implementation of economic policies. Authors, such as Haggard (2013), investigate the historical context that influences state-market relations and the politics and institutions that are conducive to growth (Haggard, 2013). The primary interest of developmental-state scholars is not to explain the creation of different types of state institutions, but rather their contribution to successful economic development. A central analytical concept refers to the notion of state autonomy; high levels of state autonomy describe a situation in which state managers have sufficient institutional capacity to choose their own goals and realise them in the face of conflicting interests. Despite theoretical sophistication (see Evans, 1995; Yeung, 2014), a central critique of the developmental-state approach remains its "excessive focus on political institutions and its relative neglect of business" (see Haggard, 2013, p. 14).

Drawing on the insights of developmental-state theory, another stream of literature began to emerge in the 1990s and 2000s, focusing to a greater degree on the business side. This literature looks at the impact of state-business relationships on economic policy. Authors, such as Maxfield (1990) and Ross-Schneider (2004) are interested in the conditions that lead to the benevolent collaboration between state and society, which is considered to be critical for economic success (e.g., in terms of policy implementation, economic performance, or regional economic integration). Therefore these authors look at organisational features in order to unpack the relationships between state and business (Maxfield and Schneider, 1997).

The specific relationships between state and business need to be understood as outcomes of history. It is the historical context and the circumstances of this context (e.g., socioeconomic crises) in which the state grants power to business in return for political support. For example, Maxfield's study 'International Finance and Mexican Politics' investigates the patterns of state-business relations, notably coalitions between large domestic conglomerates, foreign conglomerates, and groups within the state apparatus (Maxfield, 1990). The major argument is that foreign organisations, such as the IMF, joined with domestic bankers in order to promote their common economic financial objectives. Through close consultation with the Ministry of Finance and the Central Bank, this banker alliance was able to shape fiscal and monetary policies in Mexico (Maxfield, 1990). In turn, these policies reflected the preferences of the bankers (Maxfield, 1990). However, state strength and business strength can vary across policy domains within countries, and alliances are not always formed between international and national capital.

An analysis of cross-country and cross-domain variation of state finance institutions calls for a disaggregated approach that acknowledges differences in state-business relations across policy domains. A PN analysis offers such an approach by offering a combination of factors that are applicable at the meso-level. It tells us something about the centralisation and power of state and the mobilization of civil society in a policy domain. Differences between these structural characteristics give rise to different types of PNs. In turn, PNs inform the types and power of various actors in policy-making processes and policy outcomes. As such, PNs are independent of the dependent variable, which is strategy or institutional choice.

PNs can differ from one another and are bound by the policy domain. A policy domain refers to a field of policy activity, and it is commonly given a label such as 'health' or 'environment' (Laumann and Knoke, 1987). Thus far, PN analysis has been applied in a large number of single and comparative studies on definable separate policy domains and sectors, including the industrial domain (Atkinson and Coleman, 1989; Wright, 1990; Dunn and Perl, 1994), the finance and saving domain (McConnell, 1993; Josselin, 1995; Coleman, 1994), the health sector (Rhodes and Wistow, 1988; Proven and Milward, 2001; Kay, 2006), the education sector (Raab, 1992; Homeshaw, 1995), the energy sector (MacInnes, 1991; Toke, 2000), the environment (Howlett and Rayner, 1995; Jost and Jacob, 2004), and agriculture (Daugbjerg, 1998a, 1998b; Montpetit, 2002; Botteril, 2005).

Central to all PN studies is their support for a disaggregated view of policy making and their emphasis on the existence of different subsystems across countries and across domains. They highlight organizational differences between interest groups and the state across policy domains (see Boerzel, 1998). For example, a number of comparative studies investigating industrial policy, such as Wright and Willks (1987) and Hall (1986), have illustrated that in single countries, meaningful variation can occur with regard to the role of state and society in the policy making processes and the nature and extent of state intervention. PN studies recognise that out of the entire range of actors interested in a policy issue, only a few are actually involved in the policy-making process (Montpetit, 2005). While some actors are directly involved in policy processes, other actors can merely voice their ideas and advocate policy positions in hope of influencing the policy-making process (Coleman and Skogstad, 1990; Montpetit, 2005; Howlett, 2002). PNs offer a structural analysis of civil society and state actors in the policy-making process, by which different structures create different policy logics.

By offering a combination of structural factors, a PN approach accounts for a number of those which interact in the policy making process. Through its disaggregated approach, a PN analysis allows for the investigation of both within-country and cross-country variations in domestic structures and their effects on policy choices concerning state finance institutions. A PN analysis provides a valuable framework for categorising complex formal and informal decision-making structures. Reducing this complexity by means of categories allows for the condensation and organisation of large amounts of empirical data regarding the structures of state-society relations into a small number of salient types. In addition to that, categorisations allow for the identification of similarities and differences among cases, thereby facilitating comparison.

3.2 ADOPTING A POLICY NETWORK APPROACH

Although the PN approach was a vigorously contested literature rooted in the 1970s and 1980s, this thesis has very good reasons for adopting and developing it. A PN approach gives the present thesis a framework and a clear structure with regard to a meso-level application. It allows the investigation of cross-domain and cross-national variation. It offers a valuable framework for studying the effects of state-society relations on policy outcomes regarding the kinds of financial institutions that are set up. Different types of SWFs are treated as the consequences of decisions made in policy domains. Policy domains refer to substantive areas of decision making, and are commonly divided into industrial, financial and agricultural types.

Conceptualising the creation of different SWF types as policy choices relates directly to the research question.

This research is interested in how the relationship between interest groups and the state at the sectorial/domain level affects the kinds of financial institution that are set up. Policy networks are not only descriptive maps; they also have explanatory power. Over the past 30 years, a wide range of scholars from various disciplines, including political science (Atkinson and Coleman, 1989) and sociology (Laumann and Knoke, 1987), have drawn on different methods and theoretical frameworks to contribute to PN analysis. These range from typological to interorganisational approaches and reflect differing methodological traditions (Thatcher, 1998). Börzel (1998) differentiates between quantitative and qualitative approaches. The former are process oriented and focus on the structure and the content of interactions between actors by using qualitative methods, whereas the latter analyse the relations between actors with quantitative methods.

A PN analysis offers a way to map the organisations involved in policy making, and it allows the relating of this map to policy outcomes. This facilitates the exploration of the domestic politics behind different policy outcomes within countries and across countries. Policy network theories maintain that policy outcomes, and thus institutional choices, emerge from the structure of state-society relations. The structures of these relations shape the interactions among actors, thereby influencing consultation, negotiation, and bargaining in formal and informal institutional arrangements. This makes it an excellent framework for investigating policy processes that are characterised by the involvement of peak organisations and that lead to policy choices that do not follow formal political institutional logic or reflect the underlying economic power of interest groups.

However, PN accounts differ in terms of whether they use PNs as dependent or independent variables. While some studies treat PNs a dependent variable (Van Vught, 1985; Yishai 1992; Peterson, 1993; Hay and Richardson, 2000; Kriesi and Jeger 2001), others treat PNs as intermediating or independent variables (Atkinson and Coleman, 1989; Dunn and Perl, 1994; Daugbjerg, 1998; Howlett, 2002; Fawcett and Daugbjerg, 2012). The latter group is interested in how PNs affect policy outcomes either in terms of change and stability or in terms of content and forms.

This thesis uses the PN literature as an analytical starting point. One of its fundamental claims is that different state-society relations lead to different policy outcomes across and within countries even in the face of similar external pressures. In the field of comparative politics and comparative industrial policy, PN analyses constitute legitimate approaches for studying the domestic drivers of policy outcomes. Unlike dominant frameworks in the field, notably interest group and institutional approaches, a PN framework highlights systematic differences in the relationships between state-interest groups at the meso-level. A PN perspective encourages us to take a disaggregated view of policy-making, in which PN accounts map out the different types of relationships between interest groups and the state across policy domains – specifically, the industrial policy domain. Policy network typologies were introduced to bring order to the variety of relationships between interest groups and the state in policy-making processes. They differ according to the dimensions along which state-society relations are differentiated and range from twofold to sixteen-fold typologies (see Rhodes, 1991; Waarden, 1992). Each form of PN is treated as a generic term to describe the different types of relationship between interest groups and the state; allowing a more precise analysis by considering sectoral differences in the relationship between interest groups and the state (Börzel, 1998, p. 255).

POLICY NETWORK TYPOLOGIES

This research uses a well-established PN-type literature (Atkinson and Coleman, 1989; Dunn and Perl, 1994) as an analytical starting point for two reasons. First, only a few studies, most notably Atkinson and Coleman (1985, 1989) and Dunn and Perl (1994), have tried to connect subsystem structures to policy content.[32] Atkinson and Coleman set out an initial framework for how different PNs affect the logic of the interactions between socio-economic actors and how this hampers or facilitates the access of certain actors to the policy-making process (Atkinson and Coleman, 1989). One of their fundamental claims is that different power balances among societal groups and the state – represented by different PNs – yield different policy consequences (Atkinson and Coleman, 1989). Their aim is to “elaborate […] on the organisational logic associated with these policy networks by examining them in conjunction with industrial policy” (Atkinson and Coleman, 1989, p. 47). They systematically link different types of PNs to a broader set of policy trends in the form of anticipatory and reactive policy responses.

Second, PN-type studies leave room for state autonomy. Analogising from the work on strong and weak states (Katzenstein, 1985), Atkinson and Coleman (1989) argue that state strength differs not only at the macro-level across countries but also within countries at the meso-level. Atkinson and Coleman argue that a set of structural variables gives rise to different types of

[32] Insofar as studies have developed this link, they have looked at the impact of subsystem structure on policy change versus policy continuity (Howlett, 2002; Compston, 2009). For example, Howlett (2002), Montpetit (2005) and Compston (2009) do this through analytically sophisticated explanations focussing on correlations. These studies have shown that there is strong evidence on the relationship between PN types and policy change versus policy continuity in a particular policy domain (Howlett, 2001; Compston, 2009). However, they do not provide specific hypotheses linking different PNs to policy processes and particular content of policy choices (Börzel, 1998 drawing on Bressers et al., 1994).

PNs, which reflect different state-society relations. Drawing on Katzenstein (1985), Hall (1986), and Zysman (1983), Atkinson and Coleman (1989) use the concepts of state capacity and societal mobilisation to identify a number of ideal type policy networks at the meso-level (see TABLE 3.1.). Atkinson and Coleman (1989) use structural characteristics (i.e. state centralisation, autonomy, and business mobilisation) to distinguish among different state-society relations, reflecting different types of PNs. These forms include, state-directed, concertation, corporatist, pluralist, clientele pluralist, and parentela pluralist PNs (Atkinson and Coleman, 1989; see TABLE 3.1.).

TABLE 3.1. *Atkinson and Coleman's Factors of Policy Networks.*

Mobilization of business interests	**State Structure**			
	High autonomy, high concentration	***High autonomy, low concentration***	***Low autonomy, high concentration***	***Low autonomy, low concentration***
Low	State-directed	Pressure pluralism	Pressure pluralism	Parentela pluralism
High	Concertation	Corporatism	Clientele pluralism	Industry dominant pressure pluralism

Source: Atkinson and Coleman (1989, p. 54).

The notion of state-directed PN describes a state-society structure in a policy domain where decision-making structures are highly concentrated, state officials are highly autonomous, and business mobilisation is low (see Atkinson and Coleman, 1989; Dunn and Perl, 1994). These particular characteristics shape the organisational logic of policy making. Business is divided and often "considered untrustworthy by officials" and "the political administrative style is one of managerial directive followed by a polite briefing" (Atkinson and Coleman, quoted by Dunn and Perl, 1994 p. 313). Highly mobilised and autonomous, "the state embarks upon economic projects that have serious repercussions for the investment decisions of business" (Atkinson and Coleman, 1989, p. 59). Atkinson and Coleman's statement that this takes place "with little warning, and sometimes with little explanation" highlights a policy-making logic that is strongly driven by state actors. At the other extreme are industry dominant pressure pluralist PNs, characterised by high levels of fragmentation in their decision-making structures, officials with low level of autonomy, and a high level of business mobilisation.

In between state-directed PNs and industry dominant pressure pluralist PNs, Atkinson and Coleman (1989) identify five other types of PNs: concentration, corporatism, clientele pluralism, parentela pluralism and pressure pluralism PNs. State-directed PNs, together with concentration PNs, as well as corporatist PNs, "vary significantly from the pluralist [PN] models" (Atkinson and Coleman, 1989, p. 57). Dunn and Perl (1994) build upon Atkinson and Coleman (1989) in their analysis of industrial revitalisation policies. According to Dunn and Perl, "[state directed, concertation, and corporatist] networks can be considered 'strong' policy networks, i.e. they lend themselves to effective laboration and implementation of sectoral industrial policies" (Dunn and Perl, 1994, p. 313). In state-directed, concertation, and corporatist PNs, the state possesses high levels of autonomy. This allows the adoption of a long-term view of economic policy-making, involving policies that require close-coordination and co-operation. In so-called 'anticipatory' policies, the "emphasis [is] on intrusive policy instruments, integrated with one another and aimed at structural transformation"; these are organised around comprehensive structural transformation (Atkinson and Coleman 1989, p. 60). Policies associated with state-directed, concentration, and corporatist PNs are characterised by high levels of state involvement, co-ordination and intrusion in the private sector.

A corporatist PN is a state-society structure in a policy domain where state decision-making structures are dispersed but state actors are autonomous, "seek[ing] to place the onus for decision making in the hands of conflicting [and highly mobilised] socio-economic producer groups" (Atkinson and Coleman, 1989, p. 57). Atkinson and Coleman's statement that "the parties involved are in a position of mutual deterrence" suggests that each producer group, highly mobilised, can prevent others from realising their interests (Atkinson and Coleman, 1989, p. 57). Thus, a corporatist PN "provides a means for incorporating two or more [highly mobilised socio economic producer groups] into forums where policy is formulated and implemented" (Atkinson and Coleman, 1989, p. 57). Socio-economic producer groups 'incorporated' in the policy-making process are typically highly mobilised with structures that allow them to represent their clientele's interests in the respective domain (Schmitter, 1977). This necessitates the existence of inclusive hierarchical and non-voluntary associations. At the macro-level, corporatism relates to the conflict between capital and labour whereas, at the meso-level, the conflict can emerge between other types of competing interests (Atkinson and Coleman, 1989; Dunn and Perl, 1994). In a corporatist PN, an autonomous state delegates part of the policy-making authority over a particular policy domain "to conflicting groups to permit them to resolve their differences without further state interference" (Atkinson and Coleman, 1989, p. 58).

A concertation PN is a state-society structure in a policy domain in which state decision-making structures are highly centralised and autonomous officials stand vis-à-vis a highly mobilised business sector. Similar to a corporatist PN, there are inclusive hierarchical and non-voluntary business associations; unlike corporatist PNs, "it is business, and usually just a single element or fraction of business, that shares policy-making responsibility with the state" (Atkinson and Coleman, 1989, p. 58). The features of concentration PNs facilitate "direct negotiations between a strong business association and strong state agencies at the sectoral level" (Atkinson and Coleman, 1989, p. 58). Typically, the state has its own agenda, which is broader than the business agenda in the respective domain.[33] Nevertheless, the state seeks to accommodate business interests within its broader agenda.[34]

A pressure pluralist PN describes state-society structures in a policy domain where state decision-making structures are fragmented, and public officials with low autonomy stand vis-à-vis dispersed and fragmented business producer groups with conflicting preferences. As in the business representation system, the state is also fragmented, with different agencies and departments operating in same domain. Due to this fragmentation and low autonomy, "any clear distinction between the state and society dissolves" in the respective policy domain (Atkinson and Coleman, 1989, p. 55), and "[t]he objectives of state officials emerge in the process of competition among contending interests" (Atkinson and Coleman, 1989, p. 55). Atkinson and Coleman's statement that the "intent [of government bureaus is] on organisational survival, [and therefore they] pursue narrow, short-term goals that bring them into conflict with other departments and agencies doing precisely the same thing" suggests that the consequence of a fragmented state is bureaucratic competition among different government departments within a policy domain (Atkinson and Coleman, 1989, p. 55). Atkinson and Coleman's statement that "[n]o one is discouraged from organising and no group possesses a monopoly of power" indicates the existence of many different associations in a domain with overlapping jurisdictions (Atkinson and Coleman, 1989, p. 55). As a result, no single socio-economic group is able to capture the state and the "state is little more than the distillation of societal conflicts and is, in any event, so torn by internal dissension that business would accomplish little by capturing a single part" (Atkinson and Coleman, 1989, p. 55).

A clientele pluralist PN is a state-society structure where state decision-making structures are highly concentrated and officials with low autonomy stand vis-à-vis highly organised segments of civil society. The essence of clientele pluralism is the permission of asymmetry in the representation of private interests (Atkinson and Coleman, 1989). A clientele pluralist PN involves highly mobilised segments of the private sector and a centralised state with low autonomy (Atkinson and Coleman, 1989). This facilitates interaction between both and shapes

[33] State officials "articulate objectives which are more encompassing then those of their private-sector partners and insist on standards that they alone set" (Atkinson and Coleman, 1989, p. 58). As such, there are aspects of policy making that are 'non-negotiable' (Atkinson and Coleman, 1989).

[34] At the sectoral level "state officials seek an accommodation with business that not only meets the latter's need for freedom of action and economic support, but also is in step with a set of broader political objectives" (Atkinson and Coleman, 1989, p. 59).

the content of the interactions (Atkinson and Coleman 1989). Unlike in other PNs (e.g. state-directed PN, pressure pluralist PN, corporatist PN), policymakers in a clientele pluralist PN are strongly influenced by a particular segment of society, which follows their sector-specific economic preferences (Atkinson and Coleman 1989; Dunn and Perl, 1994).

Typically, one business fraction is dominant. High levels of mobilisation allows segments of civil society to speak with one voice, which can be directed to the respective state agency. In a clientele-pluralist PN, the "state actually relinquishes some of its authority to private sector actors, who in turn, pursue objectives with which officials are in broad agreement" (Atkinson and Coleman, 1989, p. 55). In industry dominant pressure pluralist PNs, decision-making is dispersed among different state agencies with low levels of autonomy. Their goals are strongly influenced by highly mobilised sections of civil society. Likewise, in parentela pluralist PNs, decision-making is dispersed among different state agencies with low levels of autonomy. However, the system of business representation is characterised by low levels of mobilisation; consequently, a "close relationship exists between owners or managers of individual firms and the dominant political party" (Atkinson and Coleman, 1989, p. 56). Common to all pluralist PNs is that state bureaus or state agencies have low levels of autonomy, though this might be over- or underestimated if nothing is known about the level of concentration of decision making power and the mobilisation of civil society actors. It is thus important to know the network characteristics because the impact of one actors organisational characteristics depends on the organisational characteristics of other actors within the policy domain. Policy in pluralist PNs is generally organised around the immediate needs of specific societal business interests and tends to be ad-hoc and uncoordinated with previous decisions and short-term oriented (Atkinson and Coleman, 1989).

3.2 DEVELOPING POLICY NETWORK RESEARCH

Having outlined the salient features of a well-established PN research stream, this section explains how this study is developing PN analysis. It offers a critique of PN analysis and then responds to it by highlighting specific aspects that need to be addressed in order to further develop this stream of PN analysis. It thus emphasises the need to develop hypotheses and describe causal mechanisms.

CRITIQUE OF POLICY NETWORK RESEARCH

Though PN analyses offer valuable frameworks for studying the effects of state-society relations on policy choices, four major problems can be pointed out in PN analyses in general, and Atkinson and Coleman's approach in particular. The first line of criticism relates to the causal weight of PNs. Studies have been open to substantial criticism, in terms of network effects as opposed to the effects of the initial power distribution among socio-economic actors (Dowding, 1995; 2001; Mills and Saward, 1994). It is not the properties of the network but the properties of the network components that explain policy (Dowding, 1995). Much debate has occurred about whether PNs represent merely a metaphor for describing and explaining complex relations between organised interests and state agencies in policy-making processes (Börzel, 1998). According to Dowding, PNs are descriptive tools, or a sort of descriptive history, rather than models for explaining policy choices (Dowding, 1995; 2001). For Dowding (1995), it is not the PN that affects policy choices but the components of the network. For Dowding (1995), PNs merely reflect the bargaining power of agents and cannot themselves explain policy choices. Causal claims about PNs and their effect on policy choices are weak, since mechanisms are not explained in detail in most of the research. What remains to be shown is the concrete ways by which PNs operate, whilst concrete hypotheses need to be developed about the types and forms of policy choices.

The PN literature says little about the particular features of policy processes and the institutional forms they take. The research only provides frameworks for linking PNs to a very broad set of policy alternatives and lacks substantive hypotheses. As such, PN analysis is not yet sufficiently developed to explain how PNs actually influence policy processes and specific policy choices with regard to the kind of financial institutions that are set up (Börzel, 1998 drawing on Bressers et al., 1994). Many of the explanations are very specific (e.g. particular regulations in the agriculture sector such as nitrate policy-making, see Daugbjerg, 1998a). Thus, many PN studies with very narrow and specific conceptions of the dependent variables offer descriptive rather than explanatory accounts. On the other hand, many of the PN studies adopt a very broad conception of the dependent variable (e.g. reactive versus anticipatory). For example, Atkinson and Coleman (1989) link different PNs to different policy choices, in terms of whether policy responses to external pressures in a particular policy domain are reactive or anticipatory. However, they are very general in terms of the reactive and anticipatory responses, leaving it open as to whether these relate to instruments, policies, or broader strategies and indicating only the processes whereby PNs operate to influence broad policy responses. Börzel's statement that "it still remains to be systematically shown that policy networks do not only exist but are really relevant to policy-making" indicates the need for further theoretical development (Börzel, 1998, p. 253).

Policy network analysis requires the investigation of the causal mechanisms whereby PNs might have affected policy choices. Policy networks cannot themselves explain policy choices in terms of the different kinds of financial institutions that are set up. This necessitates the investigation of the mechanisms involved, which can explain the patterns of events between particular types of PNs and the kinds of financial institutions. Policy network approaches agree that PNs differ in terms of their organisational characteristics, but no study has investigated the mechanisms linking PN characteristics to policy outcomes. It needs to be shown by which mechanisms PN characteristics operate to influence policy choices. Only recently have PN accounts started to suggest causal mechanisms (Botterill, 2005; Hindmoor, 2009; Moschitz and Stolze, 2010; Wood et al., 2013). These studies focus on the investigation of socio-psychological mechanisms (e.g. priming and framing) linking PNs to policy outcomes, specifically in terms of policy change and continuity. They treat PNs as background factors rather than as explanans. They share the assumption that PNs operate directly via socio-psychological mechanisms to affect policy outcomes, thus implying that the agents (i.e. socio-economic actors) of PNs are automatically part of key policy-making bodies, through which they can influence policy outcomes via priming and framing. However, this assumption must be verified; it needs to be shown how PN characteristics affect the appointment and selection of socio-economic actors in policy-making structures and how this affects policy outcomes.

Policy network analysis pays insufficient attention to socio-economic actors, which are the agents of PNs. The relevant causality of PNs also involves socio-economic actors, and it is the selection of socio-economic actors in policy making that shapes policy choices. Socio-economic actors such as business associations and government bodies and bureaus are the agents of PNs, interlinked through network structures. Recognising the existence of different preferences among different socio-economic actors in policy-making processes is important for the evaluation of the PN effect. Showing how members of PNs benefit and non-members suffer from choices accruing from different PNs is important because PN analyses imply distributional struggles among different actors. Using occasional evidence, PN analyses emphasise that different actors benefit differently from policies accruing from the network. However, it needs to be systematically shown how socio-economic actors with different preferences matter in order to assess the impact of PNs and potential causal mechanisms. Furthermore, PN analyses need to apply a more fine-grained differentiation among the different types of socio-economic actors. Current PN accounts, notably Atkinson and Coleman (1989), treat business/civil society as a whole, ignoring the different producer groups, such as finance, manufacturing, and social-welfare groups, with different preferences, and different ways of being organised.

A number of PN analyses have been developed into over-ambitious theoretical frames (see Thatcher, 1998). Although Atkinson and Coleman's core argument is that particular PNs lead to particular forms of policy choices, they attempt to develop their framework into an all-encompassing approach consisting of three different research objectives, which would necessitate three different research designs. First, they try to link a set of structural factors to the emergence of different PNs in the context of a particular industrial cycle. Second, they try to link different PNs to a broad set of policy responses (i.e. reactive and anticipatory). Finally, they try to explain how a disjunction between the type of PN and the adopted policy responses can lead to policy failure. To illustrate their approach, they highlight that a mismatch between PN and policy choices leads to policy failure.

RESPONDING TO THE CRITIQUE

Despite some weaknesses, the assumptions and claims of PN analysis in general and Atkinson and Coleman (1989) in particular provide a useful starting point by offering a framework for linking different types of state-society relationships to broader policy choices that can be further developed into more fine-grained predictions. By developing a PN analysis in terms of hypotheses, causal mechanisms and agents, this thesis responds to the critique.

1) Developing hypotheses about the effects of policy networks on the kinds of financial institutions that are set up:

The PN research provides only a framework that lacks substantive hypotheses linking PNs to policy outcomes regarding the kinds of financial institutions that are set up. This research inductively examines the linkages between PNs and policy outcomes in respective policy domains through a systematic examination of the relationship between different organisational maps of state-society relations across policy domains, policy processes, and the kinds of financial institutions that are set up. The creation of different SWF types in a select case study is used to study the effects of state-society relations on policy outcomes.

2) Investigating causal mechanisms of policy networks:

Socio-psychological mechanisms proposed in recent academic accounts provide only part of the answer as to how PNs operate to influence policy choices regarding the kinds of institutions that are set up. There are also other factors relating to what Atkinson and Coleman (1989) identified as organisational logic. If network differences account for different policy choices – as highlighted in the PN literature – then organisational characteristics may also be important for investigating how PNs influence policy choices. Using an inductive approach, this study develops causal mechanisms. Through the systematic observation of debates, actors, and policy-making processes, the study arrives at a better understanding of the paths and causal mechanisms through which PNs affect policy outcomes.

3) *Examining the role of agents (i.e. socio-economic actors):*

The inductive approach allows the refinement of PN assumptions in terms of how parts of the PN map interact (i.e. how certain actors participate and how they are related). Socio-economic actors, representing business organisations, industries, and government bureaus, are treated as the agents of PNs. As meaningful variation can also be found within business and government, however, this research emphasises the existence of a range of different economic actors, such as domestic finance, international finance, domestic manufacturing, and multinational corporations, as well as social welfare groups, government bureaus and different ministries. Different socio-economic actors also have different preferences. To translate their preferences into policy, socio-economic actors need to be involved in the policy-making processes. Via its inductive approach, this study investigates how socio-economic actors with different preferences were structured in policy processes. It also looks at socio-economic actors who have not used their intellectual and economic resources to influence policy processes or institutional choices, producing important insights into state-society relations and their effects on the kind of financial institutions that are set up. Finally, the study looks at how different actors benefitted differently from PNs and their institutional choices.

4) Focusing on the link between policy networks and policy outcomes:

As mentioned, this thesis neither investigates the reasons why countries have particular types of PN nor evaluates the success or failure of particular policy choices. Although these are interesting and important questions, they would necessitate different research designs. Instead, the present thesis focuses on the link between state-society relations and their effects on the kinds of financial institutions that are set up, with different SWF types examined as instances.

3.3 RESEARCH DESIGN AND CASE STUDY

The present research adopts an inductive research design. This was decided upon because, prior to the detailed case studies of this research, no hypotheses had been developed regarding the effects of state-society relations on state finance institutions. The hypotheses suggested by this research emerge from one case study and are then further developed in another. The procedure adopted in generating these hypotheses involves a cross-country and cross-domain comparison employing process-tracing. These hypotheses are then subject to further testing by means of a plausibility probe.

It looks at whether domestic politics, and particularly whether PNs, can explain the puzzle whereby different types of SWFs are established across small open economies with similar macro-economic characteristics. It uses a PN analysis of the puzzle to develop hypotheses about why and how PNs affect the forms of financial institutions that are set up. Running counter to the expectations of the two dominant analyses, small open economies within similar peer groupings in similar regions have established different types of SWFs. Furthermore, different SWF types exist not only across nations but also across domains. These findings run counter to efficiency- and diffusion- based explanations because these dominant analyses neglect the role of domestic politics. This thesis adopts a PN approach to addresses this puzzle of cross-national and cross-domain SWF variation by looking at the role of domestic politics. This approach looks at how the structure of state-society relations at the domain level affects policy choices, making PN analysis a valuable approach for studying the effects of domestic politics on policy choices on cross-national and cross-domain levels.

The objective of this thesis is to examine the influence of the structures of state-society relations on the creation of different SWF types. Therefore, it applies a research design that enables an examination of the impact of different state-society relations on the kinds of financial institutions that are set up across different policy domains. Cross-country and cross-domain comparisons allows for the inductive investigation of the effects of PNs on the kind of finance institutions that are set up. Choosing small open economies with similar developmental starting points with similar exposures to diffusion and efficiency pressures enables a focus on the effects of PNs.

To evaluate the effects of PNs on the kinds of financial institutions that are set up, this thesis uses a select case study on SWF variation in Hong Kong and Singapore between the 1960s and 1980s. Hong Kong and Singapore are most likely cases for efficiency-based explanations, as they were highly exposed to international economic pressures. Efficiency accounts highlight macro-national variables, which were actually were very similar in Hong Kong and Singapore in this period. Both were regional financial centres with very high domestic private and public saving levels, and both were extremely open and exposed to international pressures such as inflation, currency volatility, and competition. Thus, an efficiency-based explanation cannot account for the different SWF types in Hong Kong and Singapore. Likewise, Hong Kong and Singapore are most likely cases for a diffusion-based explanation because they were exposed to similar but separate challenges while belonging to similar peer groupings.[35] Both were extremely open to emulation. They were both exposed to international organisations, such as the World Bank and UNCTAD, that promoted the adaptation of similar policies. Consequently, a diffusion-based explanation would lead us to expect similar choices of SWF type. Thus, a diffusion-based explanation cannot account for the SWF variation between Hong Kong and Singapore. What both explanations omit is domestic politics.

This thesis investigates the role of domestic politics in the form of state-society relations and its influence on the creation of different types of SWFs. Unlike efficiency- and diffusion-based accounts, the PN literature highlights that, even for small open economies, the domestic structure matters to policy-making and policy choices. This study focuses on economic domains

[35] This peer group refers to small open economies of East Asia. They share structural similarities in terms of their export profile and in terms of their resource endowment.

that were highly exposed to international pressures. The savings and industrial policy domains of Hong Kong and Singapore were highly open to international pressures, and domestic politics is least likely to have played a role in their economic policy-making. As such, Hong Kong and Singapore therefore represent hard cases for PNs' effect on policy-making and the kinds of finance institution that are set up.

This study uses a cross-domain and cross-country comparison to investigate the linkages among PNs, policy processes, and the kinds of financial institutions that are set up. The cross-national and cross-domain comparisons help in evaluating the processes whereby PNs had an effect on policy-making and policy choices. The study looks at how different state-society relations affected debates and the interaction of a limited set of actors in policy-making processes, leading to the type of financial institutions that were set up.

The study looks at the kinds of financial institutions discussed, the PNs in place, the kinds of financial institutions set up, as well as who benefited and who was harmed by particular choices. Through process-tracing, the research examines the policy-making processes between cases, allowing this thesis to gauge the effect of PNs on policy choices. Through detailed and systematic observations, the thesis identifies the potential causal mechanisms linking PN characteristics to policy choices. It examines whether the observations are linked in a particular way consistent with expectations. First, it looks at the policy problems and external pressures with which Hong Kong and Singapore were confronted between the 1960s and 1980s. Second, it identifies the policy choices available and discussed across policy domains in Hong Kong and Singapore. Third, it assesses the type of PNs in place and identifies the mechanisms through which they operated.

Using process-tracing on a new set of empirical material, the thesis develops hypotheses through a case study, 'SWF variation in Hong Kong and Singapore between the 1960s and 1980s'. Primary material was a major source of information for the entire project. This material comprised official state documents (e.g. statistical information, acts of parliaments, decrees, and other textual material), and publicly available official documents from the private sector, such as company documents, and annual reports. To make sense of the private sector's stance vis-à-vis the creation of different types of SWFs, it is necessary to analyse material that reveals private sector interests in relation to SWFs. An analysis of mission statements, lobbying reports and local newspapers (e.g. *South China Morning Post*, Hong Kong*; Hong Kong Economic Times; The Straits Times*, Singapore; *The Far Eastern Economic Review*) helps clarify the private sector's interests vis-à-vis different types of SWFs in Hong Kong and Singapore. Furthermore, an analysis of the academic literature, press releases, and interviews reveals how private commercial and industrial sectors have related to policy processes in Hong Kong and

Singapore in the form of business associations, such as the General Chamber of Commerce (Hong Kong), the Chinese General Chamber of Commerce (Hong Kong), the Chinese Manufacturers Association (Hong Kong), the Federation of Hong Kong Industries, the Chinese Chamber of Commerce (Singapore) and the Singapore Manufacturers' Federation.

This dataset is complemented through elite interviews. The interviews targeted people who had been directly or indirectly involved in decisions surrounding the creation of state finance institutions in Hong Kong and Singapore. The rationale behind this was to shed light on the manner in which PNs operate and the sequence in which actors are included and excluded.

The interviewees included both opponents and proponents of particular forms of financial institutions. In total, 22 elite interviews about financial institutional choices were conducted; 13 persons were interviewed in Hong Kong and 9 in Singapore. The interviewees occupied various positions in the PN and policy-making processes, which allowed for the investigation of distributional struggles. Given that it was a small number of people who were involved in the policy-making processes regarding financial institutions, the problem of selection bias is minimised. In addition to that, more than 10 academics were interviewed, all of whom, including Garry Rodan and Tak Wing Ngo, have conducted extensive research on public policy and financial institutions in Hong Kong and Singapore.

The format of the interviews was semi-structured, a type "often used in elite interviewing" (Leech, 2002, p. 665). Unlike standardised interviews, semi-structured interviews are not organised around a set of standardised questions and answers. Instead they are structured around an interviewing guide, which comprises the subject matter and the content to be covered. The interviewing guide was organised around the analytical framework of the thesis. Through their flexibility, semi-structured interviews allow the preservation of the narrative in a sequence of questions and provide a balance between structure and openness (Gillham, 2005). Semi-structured interviews employ open questions, which have the advantage of enhancing the possibility of discovery.[36]

CONCLUDING REMARKS

Policy network analysis offers a useful frame for investigating cross-domain and cross-national differences in state-society relations as well as policy-making and policy choices. The salient features of a well-established PN typology were outlined (Atkinson and Coleman, 1989), and a

[36] For a similar approach see Klingler-Vidra (2014).

critique of it revealed serious weaknesses. Based on this critique, this chapter has highlighted the need to further develop PN research concerning causal mechanisms and hypotheses.

Hong Kong and Singapore have been selected in order to develop hypotheses on the effects of different PNs on SWF-type variation. Subsequent empirical chapters identify the policy problems and challenges to which both economies had to respond by examining the PNs in place as well as the institutional choices available and discussed to address these challenges.

This analysis helps to identify the mechanisms through which PNs may have operated to influence the kind of finance institutions set up. Each of the chapters looks at which socio-economic actors benefited and which actors were harmed by particular institutional choices made. This is important for assessing potential causal mechanisms. Based on the findings, Chapters 4–7 formulate and refine the hypotheses.

4. The Effects of State-Directed Policy Networks on Financial Institutions in the Industrial Domain: The Creation of Temasek

Between the 1960s and 1980s, the characteristics of state-society relations in Singapore's industrial policy domain were consistent with that of a state-directed policy network (PN). The PN was marked by a high concentration of decision-making power within the Ministry of Finance, high levels of state autonomy and low levels of mobilisation among domestic producer groups. This structure influenced policy-making processes in Singapore's industrial domain with regard to the kind of financial institutions that were set up. While many different socio-economic actors – notably domestic finance and manufacturers – had a substantive interest in this issue, only a small group of state actors were directly involved in the policy-making process.

The current chapter shows how Singapore's state-directed PN affected the emergence of a large state owned enterprise sector and the creation of Temasek in 1974. This is achieved through an examination of the entire range of socio-economic actors in Singapore's industrial domain with a substantive interest in this issue. It then looks at how the PN operated by affecting policy-making processes in the industrial-policy domain. An investigation is undertaken of how network characteristics played out in policy-making processes through the inclusion in, and exclusion from, important policy-making bodies of socio-economic actors. The main question concerns which actors were included or excluded. The related question is who benefited, and who did not benefit from the type of financial institution that were set up. Therefore, the chapter examines the debates involving the Ministry of Finance, domestic finance actors and manufacturers.

The argument is that Singapore's state-directed PN in the industrial domain influenced an informal review, which led to the creation of Temasek. This review tackled the question of how Singapore should restructure its large state-enterprise sector. Different socio-economic actors at that time preferred different kinds of financial institutions in Singapore's industrial domain. The state-directed PN operated through inclusion and exclusion of socio-economic actors on committees and reviews. The main finding of this chapter is that the state-society structures allowed policy makers to bypass domestic private business actors, which demanded short-term oriented responses, such as state subsidies, preferential treatment and protection from multinational corporations (MNCs). Singapore's state-society structure allowed policy makers to take a long-term view on policy and institutional choices. These related to the upgrading and diversification of Singapore's industrial base into higher value-added activities. The PN included only a small group of officials consisting of representatives of the Ministry of Finance on key decision-making processes, which led to the creation of Temasek. The decision to create Temasek took place in a context of increasing international competition pressures. Given Singapore's high exposure to international market forces, policy makers came under increasing pressure to respond to rising international competition. Based on these findings, the chapter develops an initial hypothesis for sovereign wealth funds (SWFs) with development mandates: having a state-directed PN in the industrial domain increases the likelihood of creating an SWF with a development and diversification mandate. Related to this hypothesis is the broader argument that the type of PN affects which actors are included and which actors are excluded from policy-making processes, and this is the key factor in terms of the choice of finance institutions to set up.

It is also worth highlighting that the present chapter only explores the effects of Singapore's state-directed PN on the creation of Temasek and related to that the emergence of other state finance institutions. Although there are two other potential candidates, notably the Ministry of National Development Holding (MND Holding), and Sheng-Li Holding, the thesis has good reasons for its focus on the creation of Temasek. First, there is a lack of empirical material on the MND Holding and Sheng-Li Holding; furthermore, space limitations constrain the chapter's focus to Temasek. Second, from its creation onwards Temasek has remained the largest and most important state finance institution in Singapore's industrial domain. Third, during the 1980s, the majority of the assets from Sheng-Li Holding and from the MND Holding were transferred into the portfolio of Temasek.

Section 4.1 offers a brief background on Singapore's macro-economic context, and its industrial domain until the late 1960s. Section 4.2 looks at the actors in Singapore's industrial policy domain and at the PN characteristics. Section 4.3 develops the argument about state-directed PN in the industrial domain, and the creation of SWFs with development mandates. The examination of debates as well as policy processes at that time, in addition to actors' policy preferences, helps to identify potential mechanisms whereby Singapore's state-directed PN may have operated to affect the creation of Temasek in 1974.

4.1 ECONOMIC INHERITANCE AND THE MACRO ECONOMIC CONTEXT (1950s–1960s)

In the years following World War II Singapore was confronted with a variety of challenges. First, it experienced one of the highest population growth rates in the world (State of Singapore, Development Plan 1961–1964, p. 1). By the late 1950s to the mid-1960s this translated to a period of very high unemployment. For example, as of the mid-1960s, unemployment among Singapore's working age population was estimated at 9.1 per cent (Cheng, 1991 *quoted* by Chiu et al., 1997, p. 31). Among young people the unemployment rate reached about 23 per cent for men and about 35 per cent for women (Clark, 1971 *quoted* by Chiu et al., 1997, p. 31). As of 1957, the entrepôt trade was the most important sector in terms of employment. Entrepôt trade employed 71,362 persons compared to 66,754 in manufacturing (State of Singapore, Development Plan 1961–1964, p. 10). As of 1957 the estimates of the total economically active population were around 470,000 (State of Singapore, Development Plan 1961–1964, p.8). The situation was further aggravated by a decline in Singapore's entrepôt trade, since neighbouring countries increasingly tried to bypass Singapore in their endeavour in trading directly with Western countries (Nyaw, 1991). According to Bocock – by then an official in the World Bank Department for Information and Public Affairs – "[i]t was clear that the rate of growth of Singapore's traditional sources of income would be insufficient to cope with the island's economic and social needs" (1970, p. 27).

Between 1959 and 1965, Singapore's policy-makers followed an import-substitution industrialisation strategy that was structured around a common economic market with the states of Malaya. It was thought that in a Pan-Malayan economic partnership both parties would benefit from the same common market and tariff protection (Singapore Industrial Development Programme, 1959, p. 3). Through this strategy the Singapore state was to play an important role. As a consequence, immediately after independence in 1959 the government of Singapore set up the Minister for Finance Incorporated (MOF Inc.) with a government Act (i.e. the Minister for Finance Incorporation Act 1959). According to the MOF Inc. Act "[a]ll property, movable and immovable, which immediately before [independence] was vested in the Chief Secretary, Colony of Singapore, under the provisions of the Chief Secretary" was transferred to the MOF Inc. This made the Ministry of Finance the direct holder of corporate assets. The MOF Inc. served as the corporate body representing the Ministry of Finance's ownership stakes in local companies (*The Straits Times,* 25 June 1999; *The Straits Times,* 16 February 1977, p. 12). Targeting the common market, Singapore's government began establish joint ventures, such as Pan Malaysia Industries (established 1962) (see Tan, 1974). Furthermore, in an attempt to secure food supplies, Singapore's government participated in Sugar Industries of Singapore Ltd. (est. 1963), Prima Flour Ltd. (est. 1961), and National Grain Elevator Ltd. (est. 1961) (Tan, 1974). In 1961, Singapore's government created the Economic Development Board (EDB), a statutory board that made loans but also took equity positions. A statutory board refers to a government economic institution, which is established by an Act of Parliament and is charged with a specific task (Krause, 1987, p. 113).Other statutory boards addressing housing, trade and infrastructure were created during this period, including the Housing Development Board (est. 1960), the Public Utilities Board (est. 1963) and the Port of Singapore Authority (est. 1964).

Following its expulsion from the states of Malaya in 1965, Singapore embarked on an ambitious programme of export-oriented industrialisation. The strategy of export-oriented industrialisation relied on attracting MNCs and expanding Singapore's state enterprise sector. Shortly after the loss of the common market with Malaya in 1965, in 1967 the British Government announced its intention to withdraw its entire military from Singapore by 1975 (Rodan, 1989). The withdrawal was problematic because as of 1967, British forces in Singapore spent around S$450 mn, which was equivalent to 12 per cent of Singapore's total annual GDP (Rodan, 1989, p. 87). It was estimated that the withdrawal would lead to a further loss of 100,000 jobs in Singapore.[42] After the British withdrawal, Singapore's government transferred installations and assets left by the British into national assets, which were directly held by the MOF Inc. (A. Prasad, personal communication, 21 March 2014).

The period after 1965 witnessed a rapid increase in the number of statutory boards and state enterprises that were directly owned by the MOF Inc.[43] By the early 1970s, Singapore's state sector had expanded rapidly, and it was involved in almost all industries (Deyo, 1981). Chen's statement that "[d]uring the period 1960-1974, the private-consumption expenditure increased 263 per cent, whereas the Government consumption expenditure increased 532 per cent at constant prices" illustrates the rapid growth of the state enterprise sector (Chen, 1976, pp. 80–81). Singapore's government companies operated across a wider range of unrelated sectors, 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). In 1968, the EDB's rapid expansion led to the hiving-off of its industrial financing function to the newly created Development Bank of Singapore (DBS), and its industrial estates development and maintenance function to the newly created Jurong Town Corporation (EDB Annual Report, 1968). As a result, in the early 1970s Singapore's government became the "most important entrepreneur in the Singapore economy" (Chen, 1976, p. 81).

However, from the early 1970s onwards, international competition and protectionism put increasing pressure on Singapore's large state-run enterprise sector. Similar to private

[42] While in 1967 there were an estimated 42,000 local civilians employed in the British Armed Forces, this decreased to 32,000 in 1968 and dropped to 19,000 in 1970 (Seng and Chong-Yah, 1971, p. 29).

[43] Major statutory boards established in this period included the Jurong Town Corporation (established 1968), the National Productivity Board (est. 1972), the Sentosa Development Corporation (est. 1972), the Singapore Institute for Standards and Industrial Research (est. 1973), the Telecommunication Authority of Singapore (est. 1974), the Urban Redevelopment Authority (est. 1974), the Vocational and Industrial Training Board (est. 1979), the International Enterprise Institute (est. 1983) and the Construction Industry Development Board (est. 1984).

enterprises, government companies producing tradable goods were exposed to international competition and adjustment pressures. Until the late 1960s, Singapore's focus was on job creation via the expansion of the state enterprise sector and attracting MNCs.

From the 1970s onwards, Singapore's labour supply was shrinking and putting increasing pressure on wages, and in turn, increasing wages put pressure on labour intensive manufacturing.[44] In addition to this, successful international trade liberalisation rounds resulted in the entry of other countries that had the advantage of lower wages. New entries with low wages were able to offer more competitive prices for a variety of products, such as electrical machinery appliances or textiles that were also produced in Singapore (see Nyaw, 1991). Singapore's major export markets (i.e. OECD countries) began to introduce Non-Tariff Trade Barriers covering a wide range of labour intensive industries. Until the late 1960s a significant part of Singapore's industry percentage share of GDP was related to labour-intensive manufacturing including food, beverages, wood products, cork products, printing, metal products, rubber, plastic and textiles (Nyaw, 1991, p. 201). According to the United Nations Development Programme (UNDP), Singapore's overall development goal for the 1970s was "to transform Singapore within ten years, at an economic development rate of 15 per cent per annum (and a possible doubling of per capita income by 1975) into a regional centre for brain services and brain service industries" (UNDP, 1972, p. 5).

4.2 KEY ACTORS AND THE TYPE OF POLICY NETWORK

Between the 1960s and the 1980s, policy within Singapore's industrial domain was formulated in a state-directed PN. It was characterised by a weak system of business representation and a high degree of state autonomy, and also a high degree of power-concentration in decision-making structures. The latter was emphasised by Tan (1972) who highlighted that "[t]here is no local government authority in Singapore, and all activities of government are carried out by centralized government departments and Statutory Boards" (Tan, 1972, p. 2). Executive power was concentrated in the hands of the cabinet ministers (Tan, 1972). Until 1979, when the Ministry of Trade and Industry was created, the Ministry of Finance had combined responsibilities of the treasury and of economic development (Chew and Kwa, 2012). Next to the ministers were the permanent secretaries, who were responsible for large areas of government business (Ho, 2000). An important implication of high levels of hierarchical power-

[44] Another reason for the increase in wages was Singapore's high wage policy (see Low, 2005). Drawing on the US Bureau of Statistics Survey Chiu et al. (1997, p. 83) calculates that the hourly labour cost was higher in Singapore (i.e. US$2.67) than in other countries, notably South Korea (US$2.46). According to Sheng (2013) wage increases hit particularly small and medium enterprises in Singapore and not so much MNCs. MNCs were mostly in the high value added business so they did not mind the high wage (A. Sheng, personal communication, 30 October 2013).

concentration was that even when tensions emerged about policy choices, they would be solved rapidly (Chen, 1976). Arrangements were in place that encouraged the formation of close linkages between political executives and senior civil servants (Schein, 1996). A number of scholars, notably Chen (1976), highlight the strong nexus between bureaucrats and politicians in Singapore. According to Tan, one of Singapore's chief planning officers, policy was typically initiated by top political leaders and bureaucrats, not by the parliament (Tan, 1972). The initiation process was described by Gamer (1972), who highlights that after a state agency outlined a development plan, it was sent to the Ministry of Finance in the form of a proposal. After the Ministry of Finance Planning Unit checked whether the proposal was in line with the general objectives of the government, the Development Planning Committee under the chairmanship of the Minister of Finance made the decision (Gamer, 1972).

Over this period, the structures of state-society relations facilitated the easy co-operation between technocrats and high-level politicians. It provided the state apparatus with high levels of autonomy from a weakly organised domestic business community. In stark contrast to Hong Kong, "[o]nly about one-tenth of the members in [Singapore's] parliament [were] businessmen" (Lee, 1976, p. 50), and most of them were associated with the People's Action Party (PAP). Singapore's ruling elite was homogeneous in terms of educational, social and ideological background (Ho, 2000). According to Bogaars – a former senior civil servant in Singapore – when the PAP came into office in 1959, Prime Minister (PM) Lee Kuan Yew created the Political Study Centre where every senior civil servant had to take courses (Bogaars, 1981). Bogaars' stated that the "objective of the Prime Minister, Mr Lee Kuan Yew, was to make the senior reaches of the civil service more politically sensitive with the formation of the Political Study Centre", which indicates a politicisation of senior civil servants (Bogaars, 1981). From the late 1950s onwards, high-level bureaucrats were key components of Singapore's state-directed PN. To ensure loyalty, civil servants were carefully selected via the Directorship and Consultancy Appointments Council and the Public Service Commission. The Public Service Commission was a powerful agency that managed the recruitment of talent for supporting the government (Ho, 2000). The Directorship and Consultancy Appointments Council, which consisted of leading Ministers and senior civil servants, appointed officials to the boards of government-linked companies. In turn, the Directorship and Consultancy Appointments Council was responsible to a Coordinating Board, which reported to the PM (see Vennewald, 1994; Barr, 2014).

While state structures were marked by high levels of power concentration and autonomy, the private sector was characterised by a weak system of business mobilisation. The system of business representation in Singapore's industrial domain was typified by the presence of multiple chambers and associations with overlapping jurisdictions competing for members. For example, Singapore has had three ethnic chambers of commerce and industry, namely: the Singapore Chinese Chamber of Commerce and Industry (SCCCI), the Singapore Malay Chamber of Commerce and Industry (SMCCI), and the Singapore Indian Chamber of Commerce and Industry (SICCI). These chambers competed for members with the Singapore Manufacturing Association (SMA). The voice of private associations was further weakened in the late 1970s through the creation of the partially state run Singapore Federation of Chambers of Commerce and Industry (SFCCI).

Singapore's ethnic chambers were voluntary organisations and, as such, had little capacity to bind their members to agreements that could then be negotiated with the state. The system of business representation in the industrial domain was characterised by relatively low levels of organisational density. This refers to a situation in which associations represent only a fraction of the potential members. For example, the Singapore Food Manufacturing Association was the sector-specific association for food manufacturing, with an organisational ratio of 0.31, meaning that out of a potential of 100 firms, only 31 are members (see TABLE 4.1). In other areas, such as the wearing apparel and textile sector, no concrete data are available on membership. Furthermore, various umbrella associations, notably Singapore's racial chambers and the Singapore Manufacturing Association (SMA), claimed to represent these industries and were competing for members. However, many of these umbrella associations themselves had low levels of membership. For example, the SICCI had a membership of only 450 firms, which were mainly operating in textiles, trade, and the import and export of tailored garments (*The Business Times*, 6 January 1978, p. 6). It kept a low and quiet profile in terms of policy-making, and did not try to influence government decisions (*The Business Times*, 6 January 1978, p. 6). Not surprisingly, this passivity was criticised by its members. For example, one of the major complaints was that the SICCI did not conduct market surveys for its members (*The Business Times*, 6 January 1978, p. 6). Likewise, the SMCCI was described as a "not very active association" with a strong emphasis on racial reasoning in the policy process (*The Business Times,* 13 January 1978). From the late 1970s onwards, the SMCCI has placed more emphasis on representing a trade rather than a racial community, and it has remained very weak, particularly because of its small membership base (*The Business Times,* 13 January 1978, p. 6). As of 1978, the SMCCI had around 200 members, and most of them were active in general trade (*The Business Times,* 13 January 1978, p. 6).

TABLE 4.1. *Sector specific Associations and their Membership-ratio, and Coverage by different Umbrella Associations.*

Sector	No of firms	Sector Specific Associations	Year of Est.	Members*	Organ-Ratio	Umbrella Associations SCCCI	SICCI	SMC	SBF	SICC	SMA
Food, Beverages, Tobacco	832	Singapore Food Manufacturers Association	1967	260	0.31	✓	✓	✓	✓	✓	✓
		Provision & Sundries Merchants Association	n.a	n.a	n.a	✓		✓	✓		✓
		Singapore Noodles Manufacturer's Association	n.a	n.a	n.a	✓		✓	✓		✓
		The Canned Milk Traders Association of Singapore	n.a	n.a	n.a	✓		✓	✓		✓
		The Singapore Sugar Traders Association	n.a	n.a	n.a	✓		✓	✓		✓
Textile & Garments	94	Sewing Machines Traders Association	1983	50	0.53	✓		✓	✓		✓
		Singapore Canvas Commercial Association	n.a	n.a	n.a	✓		✓	✓		✓
		Singapore Malaya Chinese Textile Merchants Association	n.a	n.a	n.a	✓		✓	✓		✓
		Singapore Textile Centre Merchants' Association	1975	76	0.80	✓	✓	✓	✓		✓
		Singapore Textile Dealers Friendly Association	n.a	n.a	n.a	✓	✓	✓	✓		✓
		Singapore Textiles & General Merchants Association	n.a	n.a	n.a	✓	✓	✓	✓		✓
		Singapore Textiles Traders Association	n.a	n.a	n.a	✓	✓	✓	✓		✓
Wearing apparel And Leather goods	486	The Textile and Fashion Federation	1981	n.a	n.a	✓	✓	✓	✓		✓
Paper Production Printing and Reproduction of Recorded Media	945	Singapore Book Publisher Association	1968	22	0.02	✓	✓	✓	✓		
		Singapore Paper Merchants Association	1988 (not sure)	n.a	n.a	✓	✓	✓	✓		
Rubber, Plastic Non Metallic Mineral Products, Chemicals	487	Singapore Rubber Millers Association	n.a	n.a	n.a	✓			✓	✓	
		Singapore Plastic Industry Association	1989	116	0.24	✓			✓		✓
		Cement Manufacturers Association	n.a	n.a	n.a	✓			✓		✓
Pharmaceuticals	45	n.a	n.a	n.a	n.a	✓	✓	✓	✓	✓	✓
Chemicals	276	Singapore Chemical Industry Council	1979	169	0.61	✓	✓		✓	✓	✓
Fabricated Metal Products, Basic Metals (Engineering)	1,299	Singapore Iron Works Merchants Association	1981	72	0.06	✓	✓	✓	✓	✓	✓
		Singapore Metal and Machinery Association	1935	329	0.25	✓	✓	✓	✓	✓	✓
Computer Electronic and Optical Products and Electrical Machinery	542	The Association of Electronic Industries in Singapore	1973	176	0.32	✓	✓		✓	✓	✓
		Singapore Electrical Traders Association	1958	35	0.06	✓	✓		✓	✓	✓

TABLE 4.1. *(CONT.) Sector specific Associations and their Membership-ratio, and Coverage by different Umbrella Associations.*

Sector	No of firms	Sector Specific Associations	Year Est.	of Mem bers*	Organ-Ratio	Umbrella Associations					
						SCCCI	SICCI	SMC	SBF	SICC	SMA
Other Manufacturing	496	n.a	n.a	n.a	n.a	✓	✓	✓	✓	✓	✓
Petroleum Refining	14	n.a	n.a	n.a	n.a	✓	✓	✓	✓	✓	✓
Electrical Machinery	250	Singapore Industrial Automation Association	1982	59	0.24	✓	✓		✓	✓	✓
Motor Vehicles	77	n.a	n.a	n.a	n.a	✓			✓	✓	✓
Non Metallic Mineral	145	Cement and Concrete Association Singapore	n.a	8	0.06	✓		✓	✓		✓
Machinery and Equipment	1,704	Singapore Metal and Machinery Association	n.a	n.a	n.a	✓		✓	✓	✓	✓
Other Transport Equipment	1,057	n.a	n.a	n.a	n.a	✓	✓		✓	✓	✓
Furniture	620	Singapore Furniture Industries Council	1981	170	0.27	✓		✓	✓	✓	✓
		Singapore Furniture Association	1926	171	0.28	✓		✓	✓	✓	✓
		Singapore China Ware Merchants Association	n.a	n.a	n.a	✓		✓	✓		✓
		Singapore Rattan Industry Association	n.a	n.a	n.a	✓		✓	✓		
Wood and Woodproducts	116	Singapore Timber Trade United Friendly Association	n.a	n.a	n.a	✓	✓	✓	✓		
Technology	n.a	Singapore Infocomm Technology Federation	n.a	n.a	n.a	✓	✓	✓	✓	✓	✓
		Singapore High Technology Association	n.a	n.a	n.a	✓	✓	✓	✓	✓	✓
		Association of Aerospace Industries	n.a	n.a	n.a	✓	✓		✓	✓	
Engineering	n.a	Association of Process Industry	1996	430	n.a	✓	✓	✓	✓	✓	✓
		Singapore Precision Engineering and Tooling Association	n.a	n.a	n.a	✓	✓	✓	✓	✓	✓
		Singapore Engineering Merchants' Association	n.a	n.a	n.a	✓	✓	✓	✓	✓	✓
Construction	3239	Singapore Building Materials Suppliers' Association	1928	1300	0.40	✓		✓	✓	✓	✓
		Singapore Contractors Association Ltd	1937	2000	0.62	✓	✓	✓	✓	✓	
		Singapore Electrical Contractors and Licensed Electrical Workers	1976	1300	0.40	✓	✓	✓	✓	✓	
		Singapore Glass Association	1969	n.a	n.a	✓		✓	✓	✓	
		Singapore Paint Retailer& Wholesalers Association	n.a	n.a	n.a	✓					
		Singapore Renovation Contractors & Material Suppliers Association	1983	69	0.02	✓					

Sources: Information compiled from Singapore Economic Surveys Series (Transport & Storage; Information & Communication), database Singapore Statistics [online], and homepages and annual reports from various business associations.

Acronyms Umbrella Associations:
SCCCI: Singapore Chinese Chamber of Commerce and Industry
SICCI: Singapore Indian Chamber of Commerce and Industry
SMCC: Singapore Malay Chamber of Commerce and Industry
SBF: Singapore Business Federation
SICC: Singapore International Chamber of Commerce
SMA: Singapore Manufacturing Association

*Members as of 2011

Among Singapore's ethnic chambers, the SCCCI has been the largest and most important business association. As of the 1970s it had a wide network of about 6,730 members operating in finance, trade, commerce and manufacturing (*The Business Times*, 20 January 1978, p. 6; Visscher, 2007, p. 186). Dialect, in terms of geographical origin, was used as an organising principle within the Chamber (Hsieh, 1976). As a result, the internal organisation consisted of different groupings originating from various regions of China, including: Hokkien, Teochew, Fuzhou, Canton, Hakka and Hainan (Hsieh, 1976). An observer's statement that "[t]he SCCCI is the only trade organisation in Singapore still internally sectionalized along historical communal and dialect-group lines" highlights the organisational specificity of the SCCCI (*The Business Times*, 20 January 1978, p. 6). Reflecting this, the SCCCI had a traditional election system where members of the Chamber's committee were elected by the different community groups (Hsieh, 1976). However, this organisational specificity led to a number of internal conflicts during the 1960s and 1970s (see Visscher, 2007). The SCCCI's voice in policy-making processes was significantly weakened because of the internal fragmentation and tensions among different dialect groups (*The Business Times*, 20 January 1978, p. 6). This discouraged many Chinese entrepreneurs from becoming members. Thus, export-oriented Chinese manufacturers in particular began to join the SMA instead of the SCCCI (*The Business Times*, 20 January 1978).

The voice of a fragmented business representation system was further weakened through the creation of a state-run umbrella business organisation, the SFCCI. According to Visscher (2007) the SFCCI was a coordinating body for the four chambers under the guidance of government representatives and the SMA. The input for the formation of the SFCCI was given by the Minister of Finance, Hon Sui Sen during a 1976 speech.[52] The Ministry of Finance called for a single Chamber of Commerce to be formed in order to represent Singapore's business community regionally and internationally. Furthermore, the Minister of Finance urged the private sector to present itself more coherently to the Singaporean government (*The Straits Times,* 6 June 1976, p.6). Because the government saw the racially-based chambers as old fashioned, it advocated the SMA as the dominant force within the SFCCI (Visscher, 2007). In turn, the SMA was dominated by MNCs (Visscher, 2007).[53] The SFCCI was more of a facade for showing a united front on a national level (Visscher, 2007, p. 194). The objective of the SFCCI was to "provide a permanent forum for discussion among the five bodies, and to have a national body" (*The Business Times*, 5 May 1978, p. 7). Members of the SFCCI were the SMCCI, the SICCI, the SCCCI, the Singapore International Chamber of Commerce and the SMA (*The Business Times*, 28 March 1978, p. 12).

[52] The SFCCI replaced the former Joint Standing Committee of Commerce and Industry, which had been an informal body of Singapore's four Chambers.
[53] Internally the SMA was organised along product groups, such as food, drugs, drinks, tobacco, wood, paper and printing, chemicals and oil, metals and engineering and electronics. Each of these groups was headed by a chairman, and the problems of each group were presented to the SMA committee, which then carried out studies and presented them to the authorities (*The Business Times,* 3 February 1978, p. 6). The SMA also employed full-time staff for data collection (SMA, 2012, p. 11). The SMA collected statistics and information concerning trade, manufacturing and industry, and it organised trade exhibitions and trade missions (Lee, 1976; SMA, 2012).

4.3 POLICY- AND CHOICES- THE POLICY NETWORK IN OPERATION

From the early 1970s Singapore's industrial policy domain has been confronted with increasing external pressures, such as protectionism and competition in labour-intensive industries. Lim and Pang's statement that "[i]ndustrial growth in the 1960s and early 1970s was concentrated mainly in labour-intensive industries such as textiles, garments, food, paper and wood products" suggests Singapore's high exposure to labour-intensive industries by the early 1970s (Lim and Pang, 1986, p. 13). Increasing competition pressures from other newly industrialising economies such as South Korea, Taiwan, Malaysia and Thailand, and increasing protectionist sentiments among major export markets (e.g. European countries and the US), put pressure on labour-intensive industries in Singapore. In addition, Singapore had achieved full employment by the late 1970s (Chiu et al., 1997). A major policy need implied by this situation was for economic diversification. Thereafter, in line with this policy need, Singapore's prime goal was to upgrade and restructure its industrial base (Winsemius, 1982, p. 152). Policy makers were concerned about Singapore's ability to compete in the long term (P. Wilson, personal communication, 18 April 2014).

The structure of state-society relations in Singapore's industrial domain influenced policy-making processes, and in turn such policy-making processes help to explain the creation of Temasek. A number of studies on policy-making in Singapore suggest a link between a weakly mobilised civil society and economic policy outcomes (see Low, 2005; Visscher, 2007; Lee, 1976; Lim and Pang, 1986). For example, Lee's assertion that "[b]usinessmen as a group [were] not strong enough to decide government policy, nor [could] they exert pressure on the government" indicates the weak role of private business in policy-making processes (Lee, 1976, p. 50). This is also supported by other authors, notably Ho (2000), and Lim and Pang (1986). Lim and Pang's statement that "[b]oth local and foreign employers' associations — like the Singapore National Employers' Federation (SNEF), the Singapore International Chamber of Commerce (SICC), Singapore Chinese Chamber of Commerce (SCCC), Singapore Manufacturers' Association (SMA), American Business Council (ABS) and other nationality groupings — are only indirectly involved in the formulation of economic policy, which remains a state prerogative" highlights the weak role of private business in Singapore's economic policy making (Lim and Pang, 1986, p. 27).

High power concentration in decision-making structures, together with high levels of state autonomy made it very difficult for weakly mobilised private socio-economic actors to influence policy-making processes. The state-directed PN allowed for the bypassing of domestic socio-economic actors, with their sector-specific preferences. Due to its hierarchical and autonomous structure it was able to exclude private domestic banks that felt increasingly threatened by competition with state finance institutions (Yuan et al., 1990; Krause, 1987; Koh, 1987; 1987b; Mackie, 1995). It was also able to exclude domestic industrialists, who feared increasing competition with the state sector. In turn, it allowed for the adoption of a long-term view of policy and financial institutions in Singapore's industrial domain. This chapter finds that Singapore's state-directed PN operated via inclusion and exclusion mechanisms. In line with expert advice from the World Bank, Singapore began a policy of attracting large MNCs. According to scholars, such as Wilson (2014), the government focussed entirely on MNCs. Therefore, representatives from international Chambers of Commerce, such as the American Chamber of Commerce, the Japan Chamber of Commerce and the International Chamber of Commerce had privileged access in policy-making. For example, they were appointed as business representatives on the national industrial wage bargaining body (i.e. the National Wages Council). Singapore's state-directed PN resulted in policy choices that privileged large MNCs and state-linked enterprises.

The creation of Temasek in 1974 rose out of an informal review on how Singapore should reorganise its state enterprise sector and respond to pressures in an internationalising environment. As of the early 1970s most of Singapore's state-owned enterprises – which grew dramatically between the mid-1960s and early 1970s – were under the direct ownership of the MOF Inc. Policy makers were seeking ways to upgrade Singapore's industrial base from labour-intensive light manufacturing into higher value added and more capital-intensive sectors. Confronted with a complex international environment – characterised by increasing competition and protectionism – it became increasingly difficult for the Ministry of Finance to manage its numerous companies via the MOF Inc.. The evaluation about the kind of institution to set up took place during the first oil crises in 1973/74 (Nyaw, 1991).

Concerning the main argument of this thesis, the creation of Temasek in 1974 offers evidence on the limited impact of diffusion. The argument implies that given certain country characteristics the choice of creating an SWF with a development mandate reflects a process of emulation vis-à-vis peers with similar characteristics and organisations (see Chwieroth, 2014). A proponent of such a diffusion argument would assume that Singapore created Temasek in 1974 after other countries in its peer group created an SWF with a development mandate when faced with a similar problem of diversification. However, at the time of Temasek's creation, not one of Singapore's peers had created a similar institution. Although it was highlighted by Dhanabalan – a former chairman of Temasek – that Temasek at that time shared similarities with the Swedish Industrial Investment Holding Company AB, however, this thesis finds evidence that no emulation took place (Dhanabalan cited by *The Straits Times*, 25 June 1999 pp. 74–76). According to J.Y. Pillay, former Permanent Secretary of the Ministry of Finance and Temasek's first Chairman, there was no visit to Sweden or any specific attempt to follow the

Swedish AB model at that time (J.Y. Pillay, personal communication, 26 March 2014; Singapore Infopedia, 2015). Nothing like Temasek existed in any of Singapore's peer countries. According to J.Y. Pillay (2014), Singapore did not follow any best practice template.

According to the other competing argument, the creation of Temasek in 1974 provides evidence on the impact of efficiency. Efficiency-based arguments emphasise the role of national interest in diversification and the upgrading of a country's industrial base as one of the major drivers behind the creation of SWFs with development mandates (see Lee 2007; IMF, 2008). As such, a supporter of an efficiency argument would highlight national economic factors (e.g. factor endowment such as land, labour or capital) as important predictors of a country's SWF choice. Precisely because of the lack of land and natural resources, small open economies like Singapore are expected to use labour and capital factors for development. In the late 1960s and the early 1970s the entrance of new competitors with abundant labour, such as Malaysia and Thailand, put diversification pressures on Singapore's labour intensive industries. Consequently a supporter of an efficiency argument would suggest that it is not surprising to observe the establishment of Temasek in the 1970s, because confronted with powerful international competition pressures, and given domestic constraints (e.g. full employment, wage pressures) Singapore had to diversify its industrial base and upgrade into higher value added sectors. Hence, the creation of Temasek is in line with what efficiency-based accounts would predict.

THE PARTICIPANTS AND THEIR PREFERENCES

Preferences regarding finance institutions in Singapore's industrial domain varied among socio-economic actors. From the early 1970s onwards, Singapore's policy-makers had been increasingly concerned with industrial upgrading and feared that Singapore was caught in a low labour wage trap (EDB Annual Report, 1968). For example, Singapore's Minister for Foreign Affairs at that time highlighted that it was not sufficient "to provide the region with cheap textiles, shoes, slippers, chocolates and things of that order" (Rajaratnam cited by the UNDP, 1972, p. 6). Singapore's policy-makers identified the transformation of Singapore's economy as "the overall goal for Singapore's development" (UNDP, 1972, p. 5). Wilson (2014) emphasises that policy makers were constantly worried about Singapore's capacity to compete over the long run. Policy-makers thus attempted to restructure Singapore's industrial base to more capital and to more skill-intensive activities (Wong et al., 1997). They planned to achieve this through a high wage policy (i.e. by forcing firms to upgrade into higher value added sectors) and the creation of state finance institutions in the industrial domain, notably via the creation of an SWF.

Common to domestic manufacturers and businesses was scepticism about Singapore's state finance institutions. Under the leadership of the SCCCI, private domestic businesses were opposed to Temasek and related state finance institutions (Winsemius, 1982a; Low, 2001; *Far Eastern Economic Review*, 18 October 1977, pp. 36–37; *Far Eastern Economic Review,* 28 October 1977). To them, the government's choice to create Temasek came into direct conflict with their business. As a result, they demanded the retreat of the state from business, and they made subtle suggestions to privatise Temasek. There were explicit calls for the privileging of Singapore private enterprises over state enterprises controlled by Temasek and over foreign enterprises in public projects, as well as the reduction of regulatory restraints for small and medium enterprises (SMEs) (*The Straits Times*, 3 August & 20 October 1985). Furthermore, domestic manufacturers called for the creation of a development bank to cater 'exclusively' to small and medium private enterprises (*Sunday Times*, 8 May 1988, p. 17). The manufacturing sector highlighted that the EDB should set up a guarantee fund for small and medium enterprise (SME) loans, and the government should make it mandatory for banks to apportion a certain percentage of their loans to SMEs (*The Business Times,* 4 May 1988). According to the SCCCI, domestic commercial banks were unwilling to provide such loans because of the lack of collateral. Small manufacturers have usually operated from rented premises and as such they were lacking of collateral. As a consequence, banks were not keen on lending to them, because of the lack of guarantees (Drake, 1969). In Singapore half of bank credit went to commerce, export/import businesses, as well as to the rubber industry, whereas only a small proportion went to manufacturers (Drake, 1969).

Similarly, Singapore's private commercial banks were uncomfortable with the creation of state finance institutions, such as the DBS, which were linked to the creation of Temasek. Their critique was directed at Temasek's banking subsidiaries – notably the DBS – and their loan policy. Singapore's private banks complained about unfair competition in retail and industrial banking with state related banks, the DBS in particular. Between 1974 and 1986 rates of growth for the DBS (20.6 per cent) and the government owned Post Office Savings Bank (POSB) (36.1 per cent) were significantly higher than the average growth of private commercial banks (15.7 per cent) (Schulze, 1990, p. 54). As of 1983, the DBS and POSB alone accounted for about 20 per cent of the total financial assets in Singapore (Schulze, 1990, p. 52). Schulze highlights that "[g]rowing government market shares [provides] evidence that public sector competition had a restraining effect on private [banks]" (1990, p. 54). The domestic private finance sector felt that the DBS as well as the POSB enjoyed a number of advantages with regard to tax and reserve requirements. Occasional evidence suggests that this might have allowed the DBS and the POSB to provide industrial banking and retail banking at better rates. For example, Singapore's private banks considered the POSB loan to Singapore Airlines as unfair competition. A local banker's statement read that the loan "was on such a low margin that it could not be matched by profit-conscious banks", which draws attention to the domestic financial actors concerns (*The Straits Times*, 17 November 1979, p. 18). However, the extent to which the DBS and POSB affected private banks in terms of industrial banking in Singapore remains unknown.

Reviewing Singapore's fledging State Enterprise Sector in 1974

Although there was no particular event that triggered the concrete creation of Temasek in 1974, it was brought about in an overall context of full employment and the concern of policy-makers about the future governance of state enterprises in an international environment, characterised by increasing competition and protectionism. According to J.Y. Pillay – Temasek's founding Chairman – the context of a thriving state sector made it necessary to restructure existing governance arrangements (Pillay, 2014). The existing governance arrangement at that time referred to the MOF Inc.. The MOF Inc. Act of 1959 Section (4), required the presence of the Finance Minister for all documents that required the seal of the MOF Inc. Pillay's statement that "[it was very difficult] for the Minister for Finance Incorporated to own so many [enterprises] direct" draws attention to governance aspects behind the creation of Temasek (Pillay, 2014). That is supported by Ajith Prasad – former Director of the Budget Division in the Ministry of Finance – who highlights that the logic behind the creation of Temasek was 'better governance' of a rapidly expanding government sector in a highly international environment (Prasad, 2014). Likewise, Dhanabalan – former Cabinet Minister and a former Chairman of Temasek – emphasises the important intermediary role of Temasek in the early years. Dhanabalan's statement that "[i]t was more to find a home for monitoring activities that were necessary, to collate all the information of various government investments and to keep the Minister for Finance and the Cabinet informed about the performance of the companies" underlines the central coordination function of Temasek at its very beginning (Dhanabalan cited by *The Straits Times*, 25 June 1999, pp. 74–76).

To fully understand the decisions leading to the creation of Temasek, J.Y. Pillay highlights that it is necessary to understand previous decisions leading to the emergence of a large state enterprise sector in Singapore between the 1960s and 1970s (Pillay, 2014). Pillay's statement that "[Temasek] could have been set up at any stage" suggests a closer investigation of this period. Between 1965 and 1973 state enterprises emerged in a number of different unrelated sectors, such as food manufacturing, logistics, steel, engineering and tourism (see TABLE 4.2). As such, it is important to understand the historical trajectory, whereby the once powerful Singapore business elite were removed over time from Singapore's policy-making structure.

TABLE 4.2. *Partially and wholly Government owned companies established (1965–1973).*

Partially Government owned companies as of 1973	**estab.**	**Wholly Government owned companies as of 1973**	**estab.**
Raya Mills Pte Ltd	1965	Singmanex Pte Ltd	1966
Acma Electrical Co Ltd	1965	Chartered Industries of Singapore Pte Ltd	1967
Saber Air Pte Ltd	1966	Keppel Shipyard (former Sing. Drydock and Engineering)	1968
Ming Court Hotel Ltd	1967	Singapore Pools Pte Ltd	1968
Cerebos Pte Ltd	1968	Neptune Orient Lines	1968
INTRACO	1968	United Metal and Plant Corporation Pte Ltd	1969
Development Bank of Singapore	1968	Air Charter Enterprise Pte Ltd	1969
United Vegetable Oil Pte Ltd	1968	Hotel Premier Pte Ltd	1970
Singapore General Aviation Services Pte Ltd	1968	Interarms Asia Pte Ltd	1970
Singapore Shipbuilding and Engineering Pte Ltd	1968	Singapore Aquarama Pte Ltd	1970
Jurong Shipbuilders Pte Ltd	1968	Singapore Steel Supply Center Pte Ltd	1970
Sembawang Shipyard Ltd	1968	Jurong Bird Park Pte Ltd	1970
Insurance Corporation of Sing	1969	Primary Industries Enterprise Pte Ltd	1970
Instant Asia Pte. Ltd	1970	Singapore Automotive Engineering Pte Ltd	1971
Singapore Offshore Petroleum Serv.Pte Ltd	1970	Singapore Tourist Industry Pte Ltd	1971
Singapore Cable Car Pte Ltd	1970	Transport Services Pte Ltd	1971
Patience and Nicholson Pte Ltd	1971	International Development & Construction Co Pte Ltd	1972
Metrawood Pte Ltd	1972	Jurong Abattoir Pte Ltd	1972
Singapore Airlines	1972	Sembawang Holdings Pte Ltd	1973
Mitsubishi Singapore Heavy Industries	1973	National Engineering Services	1973
Singapore Food Industrial Pte Ltd	1973	Ordinance Development and Engineering Co of Singapore Pte Ltd	1973
		Singapore Aerospace Manufacturing and Engineering Co Pte Ltd	1973
		Singapore National Printers Pte Ltd	1973
		Allied Ordinance Company of Singapore Pte Ltd	1973

Source: Tan Chwee Huat (1974, pp. 78–80).

Following World War II, the British returned to Singapore and tried to reestablish themselves as colonial power, notably through the creation of the Legislative Council (LegCo). Like their counterparts in Hong Kong, the Singaporean business elite enjoyed institutional recognition in the policy-making structures, especially in the LegCo between 1946 and 1955 (Gamer, 1972, p. 211). During this period, three seats in the LegCo were automatically allocated to the SCCC, and the LegCo was even chaired by a representative of the SCCC (Hong and Wong, 2004). Up to the mid-1960s, local private entrepreneurs were powerful forces in Singapore's economic policy domains and economic policy was described as "laissez faire" (Chin Hock, 1976). Low's statement that "there was a dynamic, influential Chinese business community in commodities, trading, real estate and banking which had emerged during the colonial period and were among the largest Chinese enterprises in Southeast Asia" highlights the existence of politically powerful domestic entrepreneurs (Low, 2001, p. 417).

EXCLUSION OF DOMESTIC FINANCE/COMMERCE AND MANUFACTURERS

With the prospects of independence, Singapore's domestic business elite had been gradually excluded from policy-making structures. By the mid 1950s, the practice of privileging business interests, as well as the voting privileges held by the English-educated segment of Singapore's population, was increasingly criticised by the majority of Singapore's population (Gamer, 1972). In this context of discontent, in which labour and student movements started to emerge, the chambers as well as traditional associations lost appeal especially for the younger population (Liu and Wong, 2004). In response to the domestic demand for more political power, and with a view toward introducing greater popular participation in Singapore's politics, the colonial British government formed the Rendel Commission in 1954 (Liu and Wong, 2004). This commission was entrusted with the review of Singapore's constitution (Liu and Wong, 2004). In contrast with previous policy-making processes, the business community was only marginally represented on this commission. Out of the nine commission members, only one was drawn from Singapore's business community (Ng-Lin, 2009). Apart from a representative from the Overseas Bank of China Corporation, other members included representatives from the Workers Union and the Labour Party, academics, and high level bureaucrats (Ng-Lin, 2009). This commission drafted a new constitution that abolished the prerogative of institutional representation of business in Singapore's legislation process. As a consequence, Singapore's domestic business elite (i.e. the Chinese Chamber of Commerce, the Singapore Chamber of Commerce, and the Indian Chamber of Commerce) lost the privilege of appointing representatives to Singapore's legislative council (Tan, 2011). The chambers, specifically, the Chinese Chamber, protested heavily against these measures (Visscher, 2007). The new constitution transferred the administrative apparatus from the colonial secretaries to the newly elected ministries (Gamer, 1972). The introduction of elected ministries further weakened the link between business and state.

The exclusion of domestic business and finance from decision-making processes was justified on the grounds of expertise and trust. Lee's statement that "[a]lthough some businessmen [were] appointed as ambassadors, they [were] not so trusted as an inner political group to hold key position in policy matter" highlights the uneasy relationship between the state and the domestic business sector (Lee, 1976, p. 50). Especially after Singapore's independence in 1959, the actors forming the core of Singapore's PN, notably policy-makers and high-level civil servants, shared the same political ideology, interests, and objectives. The core actors of the PN were highly suspicious of the domestic private-business elite (Low, 2001). According to Low the "government saw local capital largely synonymous with unproductive rentier activities" (Low, 2001, p. 417). This was illustrated by the government's response to domestic manufacturers, which called for support in the competition against multinational enterprises (MNCs). On several occasions, the Minister of Finance highlighted that the government would offer no support for domestic manufacturers (*The Straits Times*, 2 August 1966, p. 4). The minister's main fear that "[government] hand-outs may be frittered away" indicates the government's suspicion vis-à-vis domestic capital (*The Straits Times*, 2 August 1966, p. 4). Likewise, Singapore's policy advisors from the UN had little trust in Singapore's domestic business associations, notably the Chinese Chamber (Winsemius, 1982a).[55]

INCLUSION OF STATE ACTORS AND INTERNATIONAL EXPERTS

The exclusion of domestic business and commerce was accompanied by the inclusion of international organisations, such as the International Bank for Reconstruction and Development (IBRD) and the United Nations Conference on Trade and Development (UNCTAD). This was highlighted by Garry Rodan in his seminal work, *The Political Economy of Singapore's Industrialization* (Rodan, 1989). In 1954, a team of 13 experts from the IBRD was invited to Singapore to formulate recommendations for economic development and industrialization (*The Straits Times*, 13 January 1954, p. 2). One of the proposals by the IBRD group suggested the creation of an industrial promotion board (Singapore Hansard, 9 January 1957). This suggestion was taken up by Singapore's government in 1957 with the Industrial Promotion Bill (Singapore Hansard, 9 January 1957). However, the Industrial Promotion Board was unable to achieve its purpose of attracting investment because of insufficient borrowing powers and a lack of funds (*The Straits Times*, 12 December 1956, p. 6).

According to representatives from the SMA, the SCCC, and the ICCI, the Industrial Promotion Board's S$ 1mn in funding was too little to be effective (*The Straits Times*, 12 December 1956, p. 6). To be effective, the Industrial Promotion Board needed at least ten times as much capital and more power to borrow (*The Straits Times*, 12 December 1956, p. 6). In 1958, shortly after passage of the Industrial Promotion Bill (1957), Singapore government officials approached F. J. Lyle, the Colombo Plan Industrial Development advisor, concerning a report on Singapore's future direction in economic development (Rodan, 1989). In line with the earlier IBRD proposal, the Lyle Report (1959) emphasized that Singapore and Malaya should enter an economic partnership with a common market, which would be protected by the same tariffs. This would offer the same inducements to new industries as well as incentives for existing firms to expand, thereby contributing to industrial development (Lyle Report, 1959).

After Singapore's independence (1959), a small group of international experts had been systematically integrated on policy processes, leading to Singapore's first five-year plan. International experts, notably Dr Albert Winsemius and I. F. Tang from the United Nations

[55] In an interview Albert Winsemius, head of the UN delegation in Singapore, pointed out: "Generally speaking, the members of the Chinese Chamber of Commerce have almost always been against the threat of foreign enterprise. It's our island, it's our island. We will never give in to that. But the medical doctors and the lawyers also took this stand" (Winsemius, 1982a, pp. 23–24).

(UN), were repeatedly invited by key actors of Singapore's PN to consult Singapore's policy-makers on industrial policy.[56] Winsemius described himself as an economic advisor to the Singapore government, who had free access to Singapore's key economic policy-makers, notably Minister of Finance and Deputy Prime Minister Goh Keng Swee (Winsemius, 1982b, pp. 213–214).

The arguments used by the government in the State of Singapore Development Plan (1961) for creating the Economic Development Board (EDB) reflected the arguments of an earlier report by Winsemius, who recommended the creation of such an institution to provide loans and to make equity investments (Low, 2005).[57] The first managing director of the EDB was E. J. Mayer, an international expert who had previously worked as a director of the Industrial Planning Development Board in Israel (Schein, 1996). Apart from international experts, senior civil servants were also involved in the first five-year plan and in the creation of the EDB.[58] For example, Dhanabalan, who was at this time Finance Minister Goh's assistant, prepared a draft on the EDB for the cabinet's approval of the initial S$100 mn in funding (Schein, 1996, p. 38). EDB's first chairman, Hon Sui Sen, was sent to the IBRD for a six-month training (Schein, 1996).

Singapore's expulsion from the Malayan Union in 1965, combined with hostilities with neighbouring Indonesia, led to a reconceptualisation of Singapore's first five-year plan. This reconceptualisation was again driven by international experts and was characterised by a shift from an import-substitution industrialisation strategy (based on a common market with Malaya) to an export-oriented development strategy (Winsemius, 1982c). To conquer world markets, Tang and Winsemius suggested dealing with high domestic wages and relying on government-linked enterprises (Winsemius, 1982c). In line with Tang and Winsemius, Singapore's government identified MNCs as reliable economic partners for Singapore's industrial

[56] In the early 1960s, Dr Albert Winsemius and Mr I. F. Tang were dispatched from the UN to lead the UN mission for Singapore's industrial development. Soon after the UN report was completed in 1961, I. F. Tang became a high-level civil servant in Singapore, and Winsemius became an independent economic advisor to Singapore's government (Ngiam, 2006). From the 1960s onward, Winsemius spent between two and three weeks in Singapore every year advising key civil servants, such as Ngiam Tong Dow, on economic development and institutional policy (Ngiam, 2006). Most of these civil servants have occupied later central roles in the Ministry of Finance and Temasek as well as its key enterprises, such as the DBS.
[57] During this period the government also established a number of statutory boards in order to address housing transport and infrastructure issues, such as the Housing and Development Board (est. 1960), the Public Utility Board (est. 1963) and the Port Authority of Singapore (est. 1964).
[58] They included Mr J. Y. Pillay, at that time official at the Ministry of Finance and later permanent secretary at the Ministry of Finance and founding father and chairman of Temasek; Miss Heng Hong Ngoh, Administrative Officer; Mr Hon Sui Sen, at that time senior civil servant and first EDB chairman and later finance minister and chairman of DBS; Mr Ngiam Tong Dow, at that time a civil servant who later served as permanent secretary in the PMO and in the Ministry of Finance and chairman of DBS, EDB, SingTechnologies (formerly Sheng-Li Holding); and Mr S. Dhanabalan, at that time assistant secretary at the Ministry of Finance, who later became CEO of a firm owned by Temasek and CEO of Temasek (Ngiam, 2006).

development.[59] The government's preference for MNCs was an open secret. For example, a 1967 report by the US Department of Commerce noted that Singapore's government sought to avoid collaboration with local entrepreneurs and instead chose MNCs as the preferred economic partners in the development strategy (US Department of Commerce, 1967).

Academics, notably Deyo (1981), as well as newspaper reports, such as the *Far Eastern Economic Review* (28 October 1977) and *The Straits Times* (17 August 1968), highlighted that Singapore's government privileged MNCs over domestic firms in the industrialisation process of Singapore via regulatory and financial incentives. Singapore's state formed joint ventures and took equity positions in foreign companies (Yoshihara, 1975). According to Yoshihara, Singapore's government "accounted for 9 per cent of the paid-up capital of the foreign-controlled companies" (Yoshihara, 1975, p. 161). In turn, MNCs were not particularly interested in cooperating with Singapore's domestic private enterprises, mainly because domestic entrepreneurs were unknown outside Singapore (Yoshihara, 1975). This suggests that MNCs, together with state-owned enterprises and state finance institutions linked to them, became the core economic actors in Singapore in the second half of the 1960s.[60]

A central component in the reconceptualisation of Singapore's industrial policy concerned state finance institutions, in terms of which the government followed and implemented the proposal of Tang and Winsemius to modify and expand the EDB with the purpose of reaching out to potential investors through a network of representative offices in Japan, the US, the UK, and Europe (Ngiam, 2006; Winsemius, 1982c). With the EDB's expansion, its equity function was outsourced to the newly created Jurong Town Corporation and its industrial-loan function was outsourced to the newly created Development Bank of Singapore (DBS).

In the creation process of the DBS, Singapore's government included international organisations, notably the Export Credits Guarantee Department (UK) and the West German Kreditanstalt fuer Wiederaufbau (Development Bank of Singapore Ltd. 1968-1969 OD 39/92 The National Archives Kew). The DBS was established in 1968 with S$100 mn in paid-up capital, which was borrowed from Singapore's government and the state owned POSB, and

[59] The EDB's focus was on MNCs rather than domestic enterprises. The pioneer status legislation, including concessionary tax rates and economic expansion incentives, were specifically addressed for large exporting firms (i.e. MNCs). Deyo's statement that "[w]hile government industrial policy has not explicitly favoured foreign firms over local investors, it has nevertheless had this effect" draws attention to the structural bias in favour of MNCs (Deyo, 1981, p. 65). For example, until the 1980s, promotional activities for local enterprises in the EDB (i.e. the local industries desk) were carried out by only one person (Deyo, 1981, p. 65).

[60] MNCs accounted for approximately three fifths of total private investments in Singapore in the late 1960s (UN Development Programme, 1973-1975, p. 30).

from international institutions, such as the Asian Development Bank (Yoshihara, 1975, p. 21; Lee, 1984). In addition to that, the DBS raised money from the issuance of bonds in the Asian dollar market (Lee, 1984, p. 246). It also started to take direct stakes in companies.

For example, by the 1980s, the DBS had about 20 subsidiaries operating in multiple unrelated sectors, including finance and commerce (e.g., DBS Finance, DBS Trading, DBS-Daiwa Securities International Pte Ltd, Singapore Nomura Merchant Banking Ltd, Orient Leasing Singapore Pte Ltd), industry (e.g. Singapore Factory Development Ltd, National Engineering Services, Tata Precision Industries Pte Ltd, Mitsubishi Singapore Heavy Industries, Rollei Singapore Pte Ltd), real estate (e.g., DBS Land, Raffles Centre Ltd, DBS Realty) and energy (Sing Petroleum Co Pte Ltd) (Lee, 1984, p. 249; Lee, 1978).

Apart from their equity and loan functions, state finance institutions also started operating in the commercial banking sector. From the 1970s onward, the DBS started vying for private domestic savings in Singapore. For example, the Development Bank of Singapore launched the Autosave scheme "whereby funds are automatically transferred from a current account to a savings account of a customer (Lee, 1984, p. 248)". Lee's comment that "[t]his is implicitly an indirect way for a depositor to receive interest on his current account, a practice prohibited by the Association of Banks in Singapore" draws attention to the privileged position of state finance institutions in the competition for private savings (Lee, 1984, p. 248).[61] Former DBS chairman Pillay highlights that local banks at that time "objected" that "a government bank [was] muscling into their territory" (Pillay, 2006). The DBS enjoyed a number of privileges vis-à-vis private sector banks, notably its exemption from the Banking Act 1970 (part 27). Unlike private commercial banks, the DBS was allowed to acquire a share of the capital of financial, industrial, or commercial undertakings exceeding 40 per cent of the bank's capital funds. This gave the DBS the advantage in developing the government's big property projects.

INCLUSION OF STATE ACTORS AND EXCLUSION OF DOMESTIC FINANCE AND MANUFACTURERS

The decision to create Temasek in 1974 grew out of an informal review about the reorganisation of Singapore's large state enterprise sector. It was developed through a small circle of people in the Ministry of Finance. At that time the Minister of Finance and his Permanent Secretary were looking for a better way to govern Singapore's fledging government-linked enterprise sector (Pillay, 2014). By then Singapore had full employment and its economy was growing very fast

[61] Interestingly, the "interest from POSB deposits [was] tax free and in 1976-8, the interest rate of POSB savings deposits was slightly higher than that of the commercial banks" (Lee, 1984, p. 257). Consequently, Singapore's commercial private banks and financial institutions became alarmed at the flow of deposits to the state-run POSB (Lee, 1984).

(Pillay, 2014). The execution of this review was delegated by the Ministry of Finance to the Permanent Secretary of Finance – at that time, J.Y. Pillay. The Minister of Finance, Hon Sui Sen, and Permanent Secretary of Finance, J.Y. Pillay, decided to form Temasek to create a buffer and coordination tool between the Ministry of Finance and its enterprises (Pillay, 2014).[62]

Following Temasek's creation, senior civil servants were systematically appointed to the board of Temasek. Lim Siong Guan – former Head of Singapore's Civil Service – highlighted the government's strategy of systematically placing civil servants on the boards of Temasek's companies (Lim, 2006, p. 182). This was to guarantee that the Temasek control structure was in line with the ultimate shareholder: the Ministry of Finance. Dhanabalan's testimony that "[t]he Government's main interest was to make sure the right people were in charge […] after that the management was to chart its own course" indicates a clear rationale behind the selection of key people on the board of Temasek (Dhanabalan cited by *The Straits Times*, 25 June 1999, pp. 74–76). This was very important for the government because the Ministry of Finance had no direct influence over the appointment of Temasek subsidiaries. At the beginning of Temasek's operations, six high level civil servants were appointed to build the core element of Temasek governance (*The Straits Times*, 16 February 1977, referring to 1974). Due to the specific selection of these people, which comprised one company secretary (Cheong Boon Liang) and five directors (J.Y. Pillay, Permanent Secretary from the Ministry of Finance; F.J. D'Costa, Director Revenue Division from the Ministry of Finance; Moh Siew Meng from the Ministry of Finance; Elisabeth Sam from the Monetary Authority of Singapore and Chua Kim Yeow, Accountant General), the government exerted control over the controlled companies or sub-holdings (*The Straits Times*, 16 February 1977). Directors were appointed who also held multiple chief executive positions in companies controlled by Temasek. For example, Temasek's founding chairman J.Y. Pillay was at the same time Chairman of Singapore Airlines and Deputy Chairman of the Monetary Authority of Singapore as well as Director of the DBS and board member of Sembawang Shipyards (*The Straits Times*, 16 February 1977; *The Straits Times*, 18 July 1977).

DEBATES OVER THE CREATION OF TEMASEK DURING THE 1970s

From the late 1960s onward, discussions began to take place regarding policy choices in Singapore's industrial domain. For example, in 1967, the SMA criticised the government's industrial policy and called for government assistance in the form of lower-interest loans, lower

[62] Prasad – former Director of the Budget Division in the Ministry of Finance – remembers the story concerning the name of Temasek. According to Prasad a number of names, such as Colossal Holding, Singlaboran Holdings (Singapore Safeharbrour in Malay) were suggested. Finally, Mr Pillay highlighted that Temasek Holding should be elegant enough (Prasad, 2014).

rates on power and water, and lower construction costs (*The Straits Times*, 31 May 1967, p. 7). Interestingly, domestic private business actors did not perceive other countries as their key competitors. For them, competitors were MNCs and government-linked enterprises and state finance institutions linked to Temasek, and companies of the MND Holding and Sheng-Li Holding (*The Straits Times*, 1 April 1977, p. 11).

As mentioned, between the early and late 1980s most of the companies of the MND Holding and Sheng-Li Holding were transferred into the portfolio of Temasek. According to domestic private entrepreneurs, the government entered sectors via its SWF and its subsidiaries which hitherto were reserved exclusively to private business (*The Business Times*, 8 August 1978, p. 40). For example, the SCCCI formulated a memorandum asking the government to delineate the roles of the state and private sector in industrial and commercial domains. Indeed "[t]here was widespread fear then that government would compete, and compete unfairly, with private organisations, diverting much of the business to companies with official backing", which highlights the critical stance of the domestic private business sector vis-à-vis the kinds of institutions that were set up (*The Straits Times,* 16 February 1977, p. 12). In addition to that, domestic enterprises illustrated their case by highlighting that they were already in fierce competition with MNCs, such as Lever Brothers in domestic soap products and ice cream; Japanese MNC Bata in the domestic shoe industry; Japanese Yaohan in domestic shopping centres as well as Japanese construction companies backed by Japanese banks (*Asian Wallstreet Journal*, 6 September 1977).

Domestic businesses and manufacturers identified a lack of reasonable financing as one of their key obstacles in their upgrading attempts. This is interesting because the government introduced the Small Industry Finance Scheme in 1976 (later renamed the Local Enterprise Finance Scheme) which was initially financed through the DBS — a subsidiary of Temasek (see Yeung, 1999, p. 267). However, the DBS charged high fees and had very strict lending conditions, which made borrowing from the DBS unattractive for domestic firms (see Choy, 1985). According to a DBS analyst, the minimum interest rate under the Small Industry Finance Scheme was 9.5 per cent per year and the minimum rate for hire and purchase loans was 10.5 per cent (Ho, 1977). Observers also indicated that the DBS had a particular preference for government companies (*The Straits Times,* 17 November 1979). Being unable to get cheaper finance, the domestic private business sector directed its critique to government policies in general, and Temasek's firms in particular (see *Far Eastern Economic Review*, 18 & 28 October 1977). For example, the SCCCI highlighted that companies owned by Temasek were not only duplicating and competing with private business, but also competing on unfair terms (*The Business Times*, 8 August 1978, p. 40).

THE CREATION OF TEMASEK AND ITS EARLY YEARS

Singapore's state-directed PN influenced the creation of Temasek in 1974. It enabled the smooth transfer of industrial capital accumulated between the 1960s and early 1970s into a new organisational format. At the very beginning, Temasek was an institutional means of increasing coordination among Singapore's state-owned enterprises. In 1974 Temasek was vested with the shares of the MOF Inc. in exchange for 21 mn shares, which were equivalent to the entire capital issued by Temasek (*The Straits Times*, 16 February 1977 p. 12).[63] Temasek's gross assets by board control were approximately S$3.5 bn, making it the largest conglomerate in Singapore and South East Asia in 1978 (*The Business Times*, 3 September 1979, p. 1). It controlled the largest ship-repair and building complex, the national shipping line, the third largest bank, the national airline, and held significant stakes in listed companies, whilst through its DBS it had mores stakes in other companies. This was commented upon at that time by *The Business Times* as "a daunting assortment of companies which give the impression of an all pervasive government presence in business" (*The Business Times*, 8 August 1978, p.40). Temasek has remained the largest corporate entity in Singapore and in the region (*The Straits Times*, 16 February 1977, p. 12; *Far Eastern Economic Review*, 25 April 1980 & 23 May 1991; *Business Times*, 31 July 2002). Over the years, Temasek has grown significantly. It has acquired control over monopoly firms, and sectoral leaders as well as other state holdings in Singapore, notably Sheng-Li, later known as Singapore Technologies, as well as MND Holding.[65] For example, in 1977 Temasek employed around 24,000 people via its companies (*The Straits Times*, 16 February 1977, p. 12). Most of Temasek's companies have been active in manufacturing, technology, telecommunications, financial services, utilities, logistics and real estate.[66] Although Temasek started its international equity investments in the late-1970s, its basic structure, and its governing rules have remained the same. Temasek formally owns the assets that it manages, and it has always been fully accountable to the Ministry of Finance.

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[63] Companies included Sembawang Holdings, National Engineering Services, International Development and Construction, Singmanex, Singapore General Aviation Service, Neptune Oriental Lines, Development Bank of Singapore, Singapore Airlines, Jurong Bird Parks (*The Straits Times*, 16 February 1977).

[65] Sheng-Li Holding was established in the same year as Temasek in order to reorganise the 12 defence and strategic sector companies, such as Chartered Industries of Singapore and Chartered Ammunition Industries, and to coordinate the rapid growth in Singapore's defence industry in an environment of increasing international competition (*The Straits Times*, 20 April 1989, p. 27). At the beginning, Sheng-Li Holding's investment focus was primarily concentrated on the technology and defence sector. Shortly after the creation of Temasek the Ministry of Development delegated in 1976 its equity stakes to the MND Holding. It transferred government-linked companies in the infrastructure and housing sectors, such as the Resources and Development Corporation and the Housing and Urban Development Company, to MND Holding. Its official mandate was to make direct investments into companies in order to develop domestic infrastructure.

[66] The Ministry of Finance transferred its equity stakes from government linked companies, such as Singapore Airlines, Sembawang Holdings, National Engineering Services, International Development and Construction, Singmanex, Singapore General Aviation Service, Neptune Oriental Lines, Development Bank of Singapore and Jurong Bird Park to Temasek (*The Straits Times*, 16 February 1977).

Temasek was created under the Companies Act as a private exempt company, which is any private company that is wholly owned by the Singapore government (Singapore Companies Act, Chapter 50/4). This status has allowed more flexibility, because Temasek was not subject to the same limitations as other private companies, as provided in law (*The Straits Times,* 16 February 1977, p. 12; Krause, 1987, p.114). Furthermore, Temasek enjoyed a number of operational advantages that Statutory Boards under the MOF Inc. could not provide (*The Straits Times,* 16 February 1977, p. 12). For example, as an entity under a special law, Temasek was exempted from the public budget, and was allowed to expand into new economic sectors and compete freely with the private sector.

Temasek differs fundamentally from state enterprises and from Singapore's other SWF, the Government Investment Corporation (GIC). That is particularly emphasised by Sheng (A. Sheng, personal communication, 30 October 2013). Unlike the GIC, Temasek was set up with a co-ordination, development/diversification mandate, while the GIC had a pure saving mandate with a focus on return- maximisation by investing into international financial assets. These differences in mandates were reflected in very different investment structures with regard to asset classes (i.e. to what extent the SWF makes minority and majority investments), with regard to the time horizon of the investments (i.e. to what extent the SWF makes long or short-term investments), and with regard to the allocation of investments (i.e. to what extent the SWF invests in domestic assets or foreign assets). Indeed, "[Temasek] and GIC have traditionally managed their investment operations in very distinct ways", which highlights these differences (Elson, 2008, p. 86). While Temasek has held majority/controlling stakes in firms, and has used its voting power to influence enterprise policy, the GIC has been a passive investor primarily making minority investments. The GIC has invested predominantly in international long-term assets, such as international equity and government bonds, whereas Temasek has focussed on domestic assets (until the late 1990s Temasek invested primarily in domestic equity). While Temasek owns the assets that it manages, the GIC does not. In addition to its exempt status, Temasek enjoys the constitutional status of a Fifth Schedule company. As an exempt private company under Fifth Schedule status, Temasek is released from filing reports and accounts with the Registrar of Companies, and in 1983 the Statutory Bodies and Government Companies Act further limited access to data. This status allowed more flexibility for the government (*The Straits Times*, 16 February 1977, p. 12).

Between the late-1970s and the mid-1980s Temasek became active in industrial upgrading and diversification, particularly in the electronics sector, by providing finance, co-ordination and direction, producing intermediary products for MNCs and investing into technology sectors.[67] Interestingly, competition between the 1970s-1980s was not necessarily driven by efficiency motives (e.g. improving industry standards, diversification or upgrading) but by profit and opportunism. Temasek started to compete in multiple unrelated sectors with private entrepreneurs via its directly owned subsidiaries. Although Temasek's companies were primarily involved in strategic capital-intensive sectors in which private capital was hesitant to invest, it also actively competed with domestic entrepreneurs in non-strategic sectors, such as in the food, manufacturing and retail sectors.

A number of government-linked companies – controlled by Temasek – emerged in sectors that were in direct competition with domestic private entrepreneurs. These included logistics, manufacturing, food processing, hospitality, printing, heavy industry, real estate, insurance and finance (*The Straits Times*, 13 March 1985, p. 19). Given the strong reputation of Singapore's government, Temasek's companies had a particular advantage in credit rating (Hwang, 2003, p. 214). Former high-level officials, such as Ajith Prasad – former director of the Budget Division in the Ministry of Finance – highlighted that the rapid expansion of companies controlled by Temasek was also partly opportunistic (Prasad, 2014). Prasad's statement that "[SWF subsidiaries] invested whenever there was an opportunity so you had a situation where Sembawang which was originally a shipyard, diversified and acquired many other industries including the DeliFrance chain of eateries" draws attention to the potential of opportunistic investment behaviour of SWFs (Prasad, 2014). Another example is SAFE Super Store, owned by SingTechnologies – later a subsidiary of Temasek – which became a major competitor for domestic commerce. SAFE Super Store originally started as a welfare facility for the armed forces by selling TV sets and fridges at reasonable prices, but soon it opened to the wider public (Hwang, 2003, p. 214). Other examples including the roast duck business and food manufacturing, controlled by Singapore Technologies and Singapore's International Trading Company INTRACO (Hwang, 2003).

THE CROWDING OUT DEBATE OF THE 1980s AND SINGAPORE'S RECESSION

The so-called crowding out debate took place in the 1980s, and concerned the impact of MNCs and companies owned by Temasek on the local business and finance sector.[68] Apart from practitioners, the debate also included academics, such as Koh (1987) and Yuan et al. (1990), concerning the implications of Singapore's state institutions on the private sector. It gave socio-

[67] For an overview of Temasek's subsidiaries and related enterprises see the *Directory of Subsidiaries and Related Companies of Temasek Holdings (Pte) Ltd, Sheng-Li Holdings Co Pte Ltd, and MND Holdings (Pte) Ltd* (Temasek, 1982).
[68] For an in-depth view of this debate see Koh (1987), Lee and Low (1990).

economic actors who were not part of Singapore' state-directed PN an opportunity to leverage their criticism vis-à-vis the kinds of financial institutions set up in Singapore's industrial domain. They specifically used the international public press, such as *The Economist, The Financial Times* or the *Far Eastern Economic Review*, as platforms for conveying their positions on institutional policy to a wider audience. The question that was publicly raised was whether MNCs and Singapore's SWF were crowding out the private domestic sector.

To domestic private business the major problem was the expansion of government-linked companies under the auspices of Temasek, and the large influx of MNCs. Companies under Temasek and its subsidiaries were "perceived to have unfair advantages in terms of access to funds, tenders and opportunities" (Ramirez and Tan, 2003, p. 513). For example, firms owned by Temasek or firms that were integrated into Temasek, such as Construction Development Corporation and MND Resource Development Corporation, bid for government tenders. This was seen as unfair competition by domestic private entrepreneurs (Prasad, 2014). The domestic local business sector repeatedly expressed concern about the increasing role of government in areas that it occupied (see Deyo, 1986; Low 2000). The crowding out of the local private duck roasting businesses via Temasek and its subsidiaries was another prominent case in the debate (Lee and Low, 1990).

A global downturn in the demand for electronics and petro-chemical products triggered Singapore's first recession in 1985, and put pressure on Singapore's policy-makers to review existing policy and institutions in the industrial domain. As a result of previous policy decisions to focus on electronics and petrochemicals, Singapore's SWF was specifically exposed to the 1985 worldwide downturn in electronics and a dramatic slump in oil prices (Report of the Economic Committee, 1986).

To investigate and respond to the causes of Singapore's 1985 recession, the government formed a high level Economic Committee. It was created under the chairmanship of the Minister of State, Lee Hsien Loong with the official purpose of investigating "the longer term problems and prospects of the Singapore economy, identify new growth areas, and define new strategies for promoting growth" (Report of the Economic Committee, 1986, p. 1). It delineated the future strategy of Singapore as an exporter of offshore services and a base for the regional operational headquarters of MNCs (Report of the Economic Committee, 1986).

The Economic Committee was divided into eight specialist Subcommittees.[69] The Subcommittee concerning Temasek included international bankers and senior civil servants from Temasek and its subsidiaries.[70] The committee was initially appointed with senior representatives of Temasek, notably its deputy chairman and general manager, and executives from Temasek's subsidiaries, such as the chairman of Fraser & Neave, MRT, Singapore Press Holding and the senior vice president of DBS (*The Straits Times,* 3 February 1986, p. 1). Shortly after the initial appointment round, two international bankers joined the the Public Sector Divestment Committee (PSDC). One of them was the senior vice president of Union Bank of Switzerland in Singapore, and the other was a former deputy managing director of the MAS and managing director of Banque International Asia (*The Straits Times*, 17 April 1986, p. 9). The PSDC was appointed by the Minister of Finance in January 1986. Its official task was the formulation of "a programme for the divestment of government-linked companies […] and make recommendations on the implementation of the programme" (PSDC report, letter from the PSDC to the Ministry of Finance 1987, [1]). The official objectives of the PSDC related to the deepening of Singapore's stock market through the divestment and listing of non-strategic government linked companies (PSDC report, 1987, p. 1). The existence of a well-developed stock market was considered as a prerequisite for convincing MNCs to set up their operational headquarters in Singapore (*The Straits Times*, 6 September 1986, p. 21).

The specific organisational arrangement of the review on Temasek's divestment process excluded domestic private entrepreneurs, and the PSDC was supported by the staff of Temasek. Interestingly, the Temasek headquarters at the same time served as the official secretariat of the PSDC, which had 37 internal meetings and 15 discussions with officials from other Ministries and Temasek as well as its subsidiaries. The following organisations were included on the committee: the Ministry of Communication and Information, the Ministry of Defence, the Ministry of Labour, the Ministry of National Development, Temasek, Sheng-Li Holding, the Central Provident Fund, the Civil Aviation Authority, the Commercial and Industrial Security Corporation, the Economic Development Board, Jurong Town Corporation, the MAS, the Public Utilities Board, SBC, Telecom Authority, INTRACO, the National University of Singapore and Singapore's Stock Exchange (PSDC report, 1987).

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[69] The Business Enterprise Committee was chaired by the Parliamentary Secretary and its members included the Head of Civil Service, the Permanent Secretary of Home Affairs, the Permanent Secretary of Environment, the Permanent Secretary of National Development, the Director of the Revenue Division, the Director of the Management Service Department, the Director of Planning from the Ministry of National Development and the Director of the Ministry of Trade and Industry (*The Business Times,* 19 December 1985). Further Committees included the Local Business Subcommittee (*The Straits Times,* 31 December 1985) and the Entrepreneurship Subcommittee (*The Straits Times,* 24 December 1985). The Manufacturing Subcommittee was chaired by the chairman of Hewlett Packard, General Electrics, National Iron and Steel Mills, Sembawang (MNCs and GLCs) (*The Straits Times,* 19 December 1985). The Services Subcommittee was further subdivided into 18 working groups.

[70] The Subcommittee was also concerned with Sheng-Li Holding and MND Holding.

The effect was that only a small number of people – associated with Singapore's state-directed PN – were in full control of the divestment process; they could stop and reverse this process at any time. The PSDC report influenced the particular divestment procedure and as such hampered the potential full-scale privatisation. The divestment process itself was quite complex. First, Temasek's subsidiary companies submitted proposals to Temasek (*The Straits Times,* 6 April 1985, p. 1).[73] Temasek submitted its proposals to the PSDC, which then prepared a report that was submitted to the Economic Committee (PSDC report, 1987). Then, the Economic Committee headed by the Minister of State Trade and Industry decided which recommendations to endorse before forwarding suggestions to the Cabinet (*The Straits Times,* 19 December 1985, pp. 1–12). Finally, after the Cabinet approved the divestment, Temasek placed the respective company shares of the subsidiary with DBS Securities – the stockbroking arm of DBS – which itself is owned by Temasek. DBS Securities then sold these shares to other companies, linked to other state enterprises (*The Straits Times,* 3 September 1986, p. 17).

THE GROWTH OF TEMASEK FOLLOWING SINGAPORE'S RECESSION (1985–1990s)

Partial divestment was followed by the subsequent expansion and regionalisation of Temasek. By drawing on the Interim Report of the Committee to Promote Enterprise Overseas (Teo, 1993), Henry Yeung estimates that at the end of 1990s around 60 per cent of Singapore's GDP could be traced to the public sector, in which Temasek played an important role (Yeung, 2004, p. 46). From the late 1980s onwards, Temasek experienced a considerable expansion into international, regional and domestic equity. For example, between 1990 and 1991, Temasek sold equity for S$118.4 mn and purchased equity for S$305.9 mn on the stock market (*The Straits Times,* 14 June 1991). Consequently "Temasek bought three times what it sold in the stock market" (*The Straits Times,* 14 June 1991). It used the income generated from its divestments (e.g. the sale of shares in Singapore Airlines) to buy equity in strategic sectors on both a domestic and global basis (*The Business Times,* 18 March 1988, p. 1). Up until 1989, the government yielded S$2.5 bn from its divestment programme, and Temasek started re-investing in global companies which thus far had no presence in Singapore, as well as investment funds (*The Business Times,* 19 March 1991).

Between the mid-1980s and the late-1980s, Singapore's state-directed PN enabled the smooth transfer of companies from the Ministry of National Development and the Ministry of Defence into the portfolio of Temasek. For example, in 1984 MND Holdings started to transfer parts of its assets from government-linked companies related to land and housing development to the

[73] The similar process was the case for Sheng-Li Holding.

Ministry of Finance, which in turn transferred it to Temasek.[74] According to Prasad it was originally planned to consolidate MND Holdings under Temasek (Prasad, 2014). However, in the late 1980s, it became clear that Temasek had started to invest on a global basis, including the US. Temasek also needed to acquire stakes in banks; however, US legislation at that time forbade industrial holding companies with direct interest in industries to take controlling stakes in banks. Therefore, it was necessary to separate bank-related activities from industrial-related investment activities. It was thus decided to retain MND Holdings as a vehicle for the Singapore government's investment in banks. Prasad's statement that "MND holdings is largely a shell company, to get around legal hurdles" highlights the strategy behind the decision of retaining MND holding (Prasad, 2014).

In the late 1980s, Sheng-Li Holding transferred its assets to Temasek.[76] Although Sheng-Li Holding operated under the Ministry of Defence it had been directly owned by the Minister for Finance (*The Straits Times*, 20 April 1989). As of the late 1980s, the operations of Sheng-Li Holding employed more than 11,000 people and was restructured and transferred into the portfolio of Temasek. Lee Hsien Loong, the Trade and Industry Minister of Singapore, emphasised that by diversifying Sheng-Li Holding's operations into industrial products and services, it would not "rely on the military markets alone" (Lee Hsien Loong cited by *The Straits Times*, 20 April 1989, p. 27). Sheng-Li Holding was reorganised in 1989 into five subsidiaries, including Singapore Shipbuilding & Engineering, Allied Ordinance of Singapore, Singapore Aircraft Industries, Singapore Food Industries and Singapore Technologies Industrial Corporation. The latter aimed to investments in high technology, electronics, services and communication sectors. After the restructuring in 1989, all Sheng-Li companies adopted the name of Singapore Technologies (*The Straits Times*, 20 April 1989, p. 27).

Between the 1990s and 2000s Temasek became the majority owner in former statutory boards which were corporatised: Sing Tel in 1992, Singapore Power in 1995, the Post Office Savings Bank in 1998 and the Port of Singapore International in 1997 – the second biggest global port operator. The Singapore Broadcasting Corporation was corporatised in 1994 as Television Corporation of Singapore, and it became part of the Media Corporation Group, which was again owned by Temasek. The Public Works Department was corporatised as CPG Corporation in 1999 – under Temasek – and one year later it became a part of Australia Downer EDI Group.

[74] These included the Resources and Development Corporation, the Housing and Urban Development Company, the Development and Construction Pte Ltd., the Primary Industries Enterprise Pte Ltd, the Construction Technology Pte Ltd., the International Development and Consultancy Corporation Pte Ltd., the Urban Development and Management Co Pte Ltd. (see *The Straits Times,* 20 April 1989, p. 27; 5 December 1986, p. 33; 15 January 1980, p. 11).

[76] As in the case of Singapore Technologies some of the equity stakes of MND Holding were already integrated into the portfolio of Temasek in 1984.

Likewise, the Commercial and Industrial Security Corporation, which used to be a statutory board, has been owned by Temasek since 2005.

CONCLUSION

This chapter finds that a PN analysis helps to explain why Singapore created Temasek in 1974. The creation of Temasek in 1974 is closely connected to earlier state finance institutions and policy decisions. The chapter shows that Singapore's state-directed PNs operated through mechanisms involving the exclusion of domestic finance, business and industry. High concentration of decision-making power and high levels of autonomy allowed a small group of state actors to bypass domestic finance and industry on decision-making processes. In turn, these decision-making processes led to the creation of Temasek. These findings were the outcome of a systematic analysis of external pressures, actors' preferences regarding the kinds of financial institutions set up, debates about institutions, the PN in place, and the kind of institution set up. Drawing on that, this chapter has been able to formulate an initial hypothesis, namely: having a state-directed PN in the industrial domain increases the likelihood of creating an SWF with a development and diversification mandate.

The first part (4.1) on economic inheritance outlined the broader external pressures to which Singapore's industrial domain was exposed in the 1970s. By this time, Singapore had full employment and domestic wages were increasing, thereby putting pressure on industrial upgrading. The second part (4.2) focused on key actors, and the type of PN in Singapore's industrial domain. Between the 1960s and 1980s the structural relationship among actors in Singapore's industrial domain related to a state-directed PN. It was marked by high autonomy and power concentration in the Ministry of Finance.

The final part (4.3) analysed policy-making and the state-directed PN in operation. In order to do so, it examined the entire range of socio-economic actors with an interest in the kind of financial institution set up in Singapore's industrial domain. It discovered that preferences concerning institutions differed among domestic manufacturers, domestic finance and state actors. Debates reveal that different institutional options were available, at least at a later stage in the 1980s, notably a large-scale privatisation. It found that Singapore's state-directed PN operated through exclusion and inclusion mechanisms of private socio-economic actors on policy-making processes, which were important for the policy choices made. Socio-economic actors that were excluded by the PN did not benefit from the choices made. The next chapter focuses on Hong Kong's industrial domain, and analyses the effects of pluralist PNs on the kinds of financial institutions set up.

Thanks to the structure of its state-society relations, Singapore could easily bypass domestic private business and finance actors in industrial policy-making. No representative of Singapore's private business sector was part of the review that led to the creation of Temasek in 1974. The PN allowed for the adoption of a long-term view on industrial policy and financial institutions. The emergence of Singapore's large state sector between the 1960s and 1970s was accompanied by the systematic exclusion of Singapore's business elite from policy-making and consultations. In turn this allowed for an easy exclusion of business in the 1970s and a smooth creation of Temasek.

In terms of the competing explanations, the chapter found that the 'diffusion' argument cannot explain the creation of Temasek; in contrast, the 'efficiency' argument made sense. Nevertheless, the observable expectations of the efficiency argument do not fit in countries with similar macro-economic characteristics, such as Hong Kong — as will be shown in the next chapter.

5. The Effects of Clientele Pluralist Policy Networks on Policy Choices in the Industrial Domain: Private Finance Institutions in Hong Kong (1960s–1980s)

Between the 1960s and the 1980s, the structural features of state-society relations in Hong Kong's industrial domain were consistent with that of a clientele pluralist policy network (PN). The structural characteristics of Hong Kong's clientele pluralist PN allowed one segment of civil society privileged access to policy making. Decision making in Hong Kong's industrial domain was highly concentrated within the government's Finance Branch, which had strong linkages with highly mobilised domestic finance and commerce actors. At the same time Hong Kong's state apparatus was characterised by high levels of autonomy from the Colonial Office in London and from weakly mobilised domestic industrial actors. Although Hong Kong's industrialists had a substantial interest in issues regarding the creation of a state development bank and a development fund, only finance and commerce organisations were directly involved in important policy-making processes.

The present chapter shows how the clientele pluralist PN in the industrial policy domain influenced decisions not to create state finance institutions with development and diversification mandates. This is accomplished through an examination of the entire range of socio-economic actors in Hong Kong's industrial domain that have a substantive interest in this issue. To do that, the chapter examines how the characteristics of the PN affected policy-making processes in the industrial-policy domain through the inclusion in, and exclusion from, important policy-making committees of socio-economic actors. A central concern is determining which actors were included or excluded and who benefited or did not benefit from the kinds of finance institutions that were set up. The chapter examines discussions involving the Finance Branch, domestic commercial banks, merchants, and manufacturer associations.

The argument is that the clientele pluralist PN influenced a number of policy-reviews, which informed decisions not to create state finance institutions in Hong Kong's industrial domain.[77] These reviews were on the question of how Hong Kong should address upgrading and diversification pressures between the late 1950s and late 1970s. Debates reveal that different kinds of financial institutions, differing in terms of ownership, legal status, and mandates/objectives, were proposed and discussed over this period. Different choices reflected different distributional consequences, particularly for domestic finance actors and

[77] These policy-reviews included: the review of the Industrial Bank Committee (1959–1960), the review of the Working Committee on Productivity (1963–1964), the review of the Trade and Industry Advisory Board (1968), and the review of the Advisory Committee on Diversification (1979, 1979a).

manufacturers. Hong Kong's manufacturers made repeated calls for state finance institutions. However, the creation of a state development bank and a state development fund was perceived as intrusive by Hong Kong's private commercial banks, mainly because these banks charged high rates for industrial credits and would thus find it difficult to compete with the state in the industrial credit market. The main finding of this chapter concerns the state-society structures that allowed policy makers to bypass domestic manufacturers, who demanded the creation of state finance institutions, with mandates of providing cheap sources of financing for Hong Kong's industry. Hong Kong's clientele pluralist PN operated through inclusion and exclusion mechanisms. While it included finance and commerce organisations in important policy-making processes, it excluded industrialists from it. The structure of state-society relations in Hong Kong's industrial policy domain impeded the pursuit of policies as well as institutions with a long-term horizon, high levels of co-ordination, and high levels of state involvement. Instead, the kinds of financial institutions set up in Hong Kong's industrial domain were structured around the immediate needs of finance/commerce actors, and were not in line with the needs of industrial producer groups. These findings support the initial hypothesis in Chapter 4 that having a state-directed PN in the industrial domain increases the likelihood of creating an sovereign wealth fund (SWF) with a development and diversification mandate.

The cross-national comparison with Singapore indicates the effect of Hong Kong's clientele pluralist PN. By the mid- 1960s, Hong Kong and Singapore were following a similar industrial trajectory focusing on labour-intensive industrialisation. Both countries were able to accumulate considerable surpluses and as such creating substantial reserve funds (Szepanik, 1958; Low, 2005). Up to the second half of the 1960s Hong Kong's and Singapore's industrial trajectory shared many similarities in terms of their focus on labour intensive light manufacturing and in terms of their corporate financing. In both economies the financing of industrial undertakings was largely confined to informal channels, such as family lending or retained earnings. Neither domestic market was large enough to serve as an initial base for industrialisation (Nyaw, 1991). As such, Hong Kong's and Singapore's prosperity largely relied on trade- and export- oriented industrialisation (Wong et al., 1991; Yeung, 1991). Thanks to their strategic locations as well as their abundance of industrial labour, both followed an industrialisation strategy of the export promotion of labour-intensive manufactured goods. In both Hong Kong and Singapore, labour-intensive industries accounted for more than 50 per cent of total gross manufacturing output (Nyaw, 1991, pp. 192–194). In the 1960s, Hong Kong's focus was on the production and export of textiles, plastics, toys, watches, electronic products, basic metal, machinery, and equipment, whereas Singapore's focus was on textiles, electrical machinery, petroleum products, petroleum products, transport equipment, food products, printing, and publishing (Chen and Li, 1991; Nyaw, 1991).

Starting in the early 1970s, rising domestic labour costs in a highly competitive international environment and protectionist sentiments in Western markets put diversification pressures on the labour-intensive industries in Singapore and Hong Kong. These pressures were particularly strong for Hong Kong, where manufacturers relied heavily on US and UK markets, which accounted for 67 per cent of Hong Kong's total exports of toys, 54 per cent of Hong Kong's total exports of garments, 46 per cent of Hong Kong's total exports in textiles and 86 per cent of Hong Kong's total transistor radios exports (Lo, 1991, p. 394). Protectionist policies in the US, the UK, and the EEC, such as the Short- and Long-term Arrangement Regarding International Trade in Cotton Textiles, and later the Multi-Fibre Arrangement put enormous pressures on Hong Kong's labour-intensive industries from the 1960s onwards (Chen and Li, 1991). Simultaneously, in the Asia Pacific region, a number of emerging economies started entering labour-intensive manufacturing. For example, South Korea started an export-promotion strategy in labour-intensive manufacturing in the 1960s, followed by Malaysia and Thailand in the early 1970s (Wong et al., 1991).

While Singapore created a development bank in the late 1960s, which was accompanied by an expansion in government linked companies, followed by an SWF (Temasek) in the 1970s, policy makers in Hong Kong repeatedly chose not to create state finance institutions with diversification and upgrading mandates. That was broadly in line with the preferences of Hong Kong's finance and commerce community. Private commercial banks, notably the Hang Seng Bank and the Hong Kong Bank, had begun to establish industrial financing schemes (Goodstadt, 2005).[79]

Section 5.1 outlines Hong Kong's macro-economic context, and it offers a brief background on Hong Kong's industrial domain until the early 1960s. Section 5.2 looks at the socio-economic actors in Hong Kong's industrial domain and the characteristics of the PN. Section 5.3 investigates the effects of clientele pluralist PN on policy processes and debates, which resulted in decisions against creating state finance institutions with a development mandate.

5.1 ECONOMIC INHERITANCE AND MACRO-ECONOMIC CONTEXT (1950s–1960s)

In the early 1950s Hong Kong's role as an entrepôt economy was critically affected by an increasingly hostile environment. Sparked by the Korean War (1950–1953), the United Nations

[79] Between the 1960s–1980s, the Hong Kong and Shanghai Banking Corporation was commonly referred to as the Hong Kong Bank.

imposed a trade embargo on China, Hong Kong's largest trading partner, in 1951 (Szczepanik 1958, p. 45). In subsequent years, China tried to bypass Hong Kong as a trade intermediary (see Chen and Li, 1991), causing China to drop from first place among Hong Kong's trading partners in 1950 to 73rd place by the late 1970s (Wang, 1991, p. 450). Exports to China as a percentage of total value of Hong Kong's exports dropped from 40 per cent in 1950 to 7.2 per cent in 1955 (Szczepanik, 1958, p. 158). By contrast over this period imports from China to Hong Kong remained stable, which meant that Hong Kong's balance of trade surplus with China (i.e. HK$ 600 mn in 1950) turned into a deficit of HK$715 mn in 1955 (Szczepanik, 1958, p. 158).

Over the same period, manufacturing as a part of Hong Kong's GPD became significantly more important.[81] The Chinese Civil War (1946–1949) and the Communist takeover led to a migration influx to Hong Kong, building the basis for Hong Kong's industrialisation from the 1950s onwards, particularly in the textile and cotton sectors. Hong Kong's population, around 600,000 in 1945, increased dramatically to around 2.4 mn by the late 1950s (White Paper, 1973, p. 8). By then, Hong Kong disposed of surplus labour, which ensured a comparative advantage in labour-intensive light manufacturing, such as textile and plastics. Hong Kong's initial industrialisation in the early 1950s was financed mainly by the mainland Chinese industrialists themselves (EIU, 1962a). A combination of low taxation, minimal government interference, the total absence of labour laws, and weak labour unions influenced the decisions of mainland China's industrialists to reallocate their businesses to Hong Kong in the late 1940s (*Far Eastern Economic Review*, 25 December 1958). Industrialists from Shanghai brought machinery as well as initial capital and expertise to Hong Kong (see Lau, 1991). Unfortunately, no banking statistics were published before 1964 (Wong, 1988, p. 43), but estimates of the capital inflow range between four to five bn Hong Kong dollars. According to Szczepanik (1958), between 1947 to 1948 the inflow of foreign capital, the net balance of invisible earnings, and the net balance of government and private transfers were equivalent to 44 per cent of Hong Kong's national income, equivalent to HK$700 mn. Between 1948 and 1949, Szczepanik estimates that this increased to 67 per cent of Hong Kong's national income, equivalent to HK$1,200 mn (Szczepanik, 1958, p. 183).

Between the 1950s and 1960s, Hong Kong's export of labour-intensive products increased dramatically. Hong Kong's manufacturers produced labour-intensive products for mass consumption in the US and Europe (see Chiu et al., 1997). Commonwealth Preferences allowed Hong Kong's highly competitive industries, notably textiles, to enter Commonwealth markets,

[81] Unfortunately, there are no statistics or official estimates available for Hong Kong's GDP before 1961 (see Goodstadt, 2006). However, indicators for industrial expansion, such as loans, output and number of workers employed, have been put forward by a number of academics, such as Szcepanik (1958) and Youngson (1982). For example, in the early 1950s, there were about 28,000 workers in the textile sector which nearly doubled by the 1960s (Youngson, 1982, p. 4).

(*Far Eastern Economic Review*, 25 December 1958). The volume of Hong Kong exports of textiles to the UK increased rapidly from 350,000 to 54 mn square yards of cotton goods in 1955 and to more than 120 mn square yards of cotton goods in 1958 (*Far Eastern Economic Review,* 13 August 1959; Singleton, 1991, p. 120). An observer's statement in the *Far Eastern Economic Review* that "[t]o a growing extent the Colony has become dependent for its prosperity upon the operation of Imperial Preferences" suggests that the success of Hong Kong's labour-intensive industrialisation was highly dependent on the willingness of Commonwealth countries to import from Hong Kong (*Far Eastern Economic Review,* 25 December 1958, p. 848).

As a consequence of Hong Kong's success, producer groups in major export markets started to lobby their governments for protection in labour-intensive manufacturing industries. Protectionist sentiments among Hong Kong's most important trading partners (e.g. the US, Britain and the European Economic Community) started in the late 1950s, particularly in labour-intensive sectors and notably in textiles. For example, British manufacturers found it increasingly difficult to compete against textile imports from Hong Kong. As a result, British manufacturers, notably the Lancashire textile industry, started to lobby the British government for quota negotiations or restrictions (Ngo, 1996). English hollow-ware manufacturers also started to mobilise against Hong Kong imports (*Far Eastern Economic Review*, 25 December 1958). Similar complaints against Hong Kong's labour-intensive exports were made by producer groups in other countries such as Canada (*Far Eastern Economic Review*, 25 December 1958).

Given its heavy exposure to export-oriented light manufacturing, Hong Kong was extremely vulnerable to quota restrictions and tariff barriers. Hong Kong's manufacturers made an attempt to adjust to increasing protectionism in labour-intensive manufacturing industries. For example, textile entrepreneurs entered the clothing industry in 1970s. However, clothing was covered by the Multi-Fibre trade restrictions in the late 1970s. In addition, the US applied the country-of-origin regulations on Hong Kong in the 1980s (Chen and Li, 1991, p. 30).

This pressured Hong Kong's industrialists towards industrial diversification. Additional pressures towards diversification into higher value added sectors came from rising wages and from proliferating competition with other newly industrialising economies. Although Hong Kong greatly benefited from the international trade liberalisation of the 1950s, 1960s, and 1970s offered other newly industrialising economies with large labour surpluses, such as Taiwan, South Korea, Thailand and Malaysia, the opportunity to export to Western markets (see Report of the Advisory Committee on Diversification, 1979). Trade liberalisation targeted labour-intensive manufacturing, and countries with large labour surpluses started to industrialise in labour-intensive manufacturing sectors similar to Hong Kong (reports of the Hong Kong Commerce and Industry Department from Apr/Jun 1964, Oct/Dec 1964, Jan/Mar 1965, Oct/Dec 1967). From the 1960s onwards, Hong Kong's labour abundance turned into labour scarcity and put pressure on wages.[85] Hong Kong's major labour-intensive manufacturing industries experienced a dramatic wage increase among unskilled workers.[86] For example, between 1959 and 1961, the average daily wage for general and unskilled workers in the garments sector increased by about 32.5 per cent. In some sectors, notably metal torch cases, it increased by 75.5 per cent (EIU, 1962a, pp. 12–13). Official government surveys on manufacturing from 1965 onwards have highlighted that "present demand for labor at every skill level exceeds the supply" (Riedel, 1974, p. 74). For example, an official statement from the Federation of Hong Kong Industries (FHKI) that "[p]reviously [the] ratio of output to capital was very much higher" indicates a loss of productivity (FHKI cited by the *South China Morning Post*, 25 February 1968, p. 10). Chen and Li (1991) noted a change in comparative advantages in this period because of wage pressures. For example, the years between 1959 and 1961 experienced an average daily wage increase of more than 30 per cent for general and unskilled workers in major industries in Hong Kong (see TABLE 5.1). As a result, Hong Kong's labour-intensive industries found it increasingly difficult to compete internationally (Hong Kong Hansard, 09 October 1970, p. 112.).

TABLE 5.1. *Increase of Average Daily Wages for General and unskilled Workers in major Industries in Hong Kong.*

	1959	**1961**	**% change**
Cotton Spinning	4.41	5.035	+14.0
Cotton Weaving	3.95	4.51	+14.0
Garments	3.94	5.13	+32.5
Rubber footwear	2.98	3.61	+22.0
Metal torch cases	2.77	4.94	+75.5
Assembling and packaging	2.14	3.10	+45

Source: Calculated from data provided by EIU (1962, pp. 12–13).

Despite calls for government intervention in the industrial domain, no large state-enterprise sector emerged in Hong Kong. Unlike in Singapore, the public sector in Hong Kong remained very small, with basic public utility companies, such as electricity and transport providers, in private hands but under government regulation (Riedel, 1974).[87] Most of these public-utility companies, such as Hong Kong Electric Co, China Light & Power Co, Hong Kong Telephone

[85] Riedel relates that also to a "dramatic decline in the birth rate during the decade of the 1960's" which was the result of a variety of socio-economic developments, such as decline in marriage, the introduction of contraceptives and the missing generation born between 1937and 1945 (Riedel, 1974, p. 45).
[86] For average daily wages for general and unskilled workers in Hong Kong's industries see Appendix B.
[87] However, the government provided basic infrastructure, including drainage network, sanitation, roads, public housing, education, health services, and provision of some public goods; it also exercised control over franchised public utilities, especially after Maclehose's arrival.

Co, China Motor Bus Co, Hong Kong Tramways, Star Ferry Co, and Yaumati Ferry, were controlled by Hong Kong's large private conglomerates and were listed on Hong Kong's stock exchange (Ngo, 1996; *Far Eastern Economic Review*, 20 December 1956).

5.2 KEY ACTORS AND TYPE OF POLICY NETWORK

Between the 1960s and the 1980s, policy for Hong Kong's industrial domain was formulated in a clientele pluralist PN. A typical feature of a clientele pluralist PN is that the state shares power with particular segments of society (Atkinson and Coleman, 1989). For Hong Kong's industrial domain, the state delegated authority over licensing to the Hong Kong General Chamber of Commerce (HKGCC) and to the semi-governmental FHKI. In turn, the FHKI was dominated by the commerce sector, and it included a small select group of Shanghai industrialists. Likewise most of the HKGCC chairmen and vice-chairmen came from the commerce or trade sector (see TABLE 5.2). As mentioned in Chapter 3, one of the central characteristics of a clientele pluralist PN relates to the asymmetry in the representation of different segments of civil society (see Atkinson and Coleman, 1989). It is widely accepted in the literature on Hong Kong's industrial policy that business interests were over-represented in the legislative stages of policy formulation (Harris, 1988; Rear, 1971; Chan, 1998; Chiu, 1994). A number of scholars, such as Chiu (1994), Chan (1998), and Ngo (1996), highlight the asymmetry in Hong Kong's industrial domain by emphasising the dominant role of finance and commerce in policy-making processes. They had a central position in the formulation of economic policy. This became most visible with the appointment of John Bremridge – CEO of Swire Pacific Limited and later non-executive manager of Schroeders Asset Management – as Hong Kong's Financial Secretary between 1981 and 1986. Decision-making power was concentrated in the hands of a small number of people, most notably the Financial Secretary. The Financial Secretary leads the government's Finance Branch, which had an over-proportional influence in industrial policy (*The Bulletin*, September 1986). Even when tensions emerged between the Industry Section of the Department of Commerce and Industry and the government's Finance Branch, they were quickly resolved because of the hierarchical power concentration and the dominance of the Financial Secretary.

TABLE 5.2. *Hong Kong General Chamber of Commerce Directorate and Representation on LegCo (1950–1990).*

	Chairman	Vice Chairman	Legco Representatives (*Acting)
1950	C C Roberts (Butterfield & Swire)	P S Cassidy (John D Hutchinson & Co)	P S Cassidy (Hutchinson & Co)
1951	P S Cassidy (John D Hutchinson & Co)	C Blaker (Gilman & Co)	P S Cassidy (Hutchinson & Co)
1952	H J Collar (Imperial Chemical Industries)	J A Blackwood (Butterfield & Swire)	P S Cassidy (Hutchinson & Co)
1953	C Blaker Gilman & co	J A Blackwood (Butterfield & Swire)	H J Collar (Imperial Chemical Industries), C Blaker (Gilman & Co)
1954-1955	J A Blackwood (Butterfield & Swire)	R Gordon (Jardine Matheson & Co), L B Stone (Union Insurance Society of Canton)	C Blaker (Gilman & Co), J A Blackwood* (Butterfield & Swire)
1956-1957	C Blaker (Gilman & Co)	R Gordon (Jardine Matheson & Co), L B Stone (Union Insurance Society of Canton)	J D Clague* (Hutchinson & Co), C Blaker (Gilman & Co)
1958-1959	J D Clague (John D Hutchinson & Co)	B T Flanagan (Mackenzie & Co), H D M Barton (Jardine Matheson & Co)	C Blaker (Gilman & Co), J B Clague (Hutchison & Co)
1960	G M Goldsack Dodwell & Co	W C G Knowles Butterfield & Swire	J B Clague (Hutchison & Co), GM Goldsack (Dodwell & Co (1960-1961)
1961-1962	W C G Knowles Butterfield & Swire	S S Gordon Lowe, Bingham & Matthews	W C G Knowles Butterfild & Swire
1963-1964	S S Gordon Lowe, Bingham & Matthews	G R Ross (Deacon & Co)	J D Leach* (Union Insurance Society of Canton)
1965-1966	G R Ross (Deacon & Co)	J D Leach (Union Insurance Society of Canton)	G R Ross (Deacon & Co), J D Leach* (Union Insurance Society of Canton)
1967	J D Leach (Union Insurance Society of Canton)	M A R Herries (Jardine, Matheson & Co)	M A R Herries* (Jardine, Matheson & Co), G R Ross (Deacon & Co)
1968-1969	M A R Herries Jardine, Matheson & Co	G M B Salmon Mackenzie & Co	G R Ross* (Deacon & Co), M A R Herries (Jardine, Matheson & Co), G M B Salmon* (Mackencie & Co)
1970-1971	G M B Salmon (Mackenzie & Co)	P G Williams (Dodwell & Co)	G R Ross* (Deacon & Co), T K Ann* (Winsor Industrial Corp), J D Clague* (Hutchinson & Co), G M B Salmon (Mackencie & Co)
1972-1973	P G Williams (Dodwell & Co)	P Foxon (Gilman & Co)	G R Ross* (Deacon & Co), T K Ann*(Winsor Industrial Corp), J D Clague* (Hutchinson & Co), G M B Salmon (Mackencie & Co)
1974-1975	P Foxon (Gilman & Co)	L Gordon (Lowe, Bingham& Matthews)	S Godon* (Lowe, Bingham & Matthews), P G Williams (Dodwell & Co), G R Ross* (Deacon & Co), T K Ann* (Winsor Industrial Corp), J D Clague*(Hutchinson & Co)
1976-1977	L Gordon (Lowe, Bingham& Matthews)	Nigel A Rigg (Union Insurance Society of Canton Ltd.)	S Godon* (Lowe, Bingham & Matthews), P G Williams (Dodwell & Co), G R Ross* (Deacon & Co), T K Ann* (Winsor Industrial Corp), J D Clague* (Hutchinson & Co)
1978-1979	Nigel A Rigg (Union Insurance Society of Canton Ltd)	D K Newbigging (Jardine, Matheson & Co)	D K Newbigging (Jardine, Matheson & Co), J H Bremridge* (John Swire & Sons), P G Williams* (Dodwell & Co), T K Ann* (Winsor Industrial Corp), S Gordon (Lowe, Bingham & Matthews)
1980-1981	D K Newbigging (Jardine, Matheson & Co)	J L Marden (Wheelcock Marden)	D K Newbigging* (Jardine, Matheson & Co), A Lee*(Sonca), M G R Sandberg* (Hong Kong Bank)
1982-1983	J L Marden (Wheelcock Marden)	J Tang (South Seas Textile Manufacturing Company)	D K Newbigging* (Jardine, Matheson & Co), A Lee* (Sonca), M G R Sandberg*(Hong Kong Bank)
1984-1985	J Tang (South Seas Textile Manufacturing Company)	T Clydesdale (Lowe, Bingham& Matthews)	D K Newbigging*(Jardine, Matheson & Co), A Lee*(Sonca), M G R Sandberg (Hong Kong Bank), Stephen Cheong* (Lee Wa Weaving Factory), W C L Brown*(The Chartered Bank), L Dunn* (John Swire & Sons)
1986-1987	T Clydesdale (Lowe, Bingham& Matthews)	A Lee (Sonca), H Sohmen (World Wide Shipping Agency)	T Clydesdale (Lowe, Bingham & Matthews (later Pricewaterhouse)
1988-1989	A Lee (Sonca)	H Sohmen (World Wide Shipping Agency) V H S Lo (Shui On Group)	J D Mc Gregor (Mc Gregor & Co)
1989-1991	H Sohmen (World Wide Shipping Agency)	V H S Lo (Shui On Group), Charles Mackay	J D Mc Gregor (Mc Gregor & Co)

Source: Compiled from the Hong Kong General Chamber of Commerce (2014).

The autonomy of Hong Kong's state actors was substantially circumscribed by the longstanding conventions of consultation with unofficial members of the Executive Council (ExCo) and the Legislative Council (LegCo). While the ExCo is Hong Kong's executive organ, similar to the British Cabinet, the LegCo is Hong Kong's legislative organ (Beazer, 1978). Both organs comprised unofficial and official members. Official members were the secretaries of government bureaus who represented their departments in the legislative process. The appointment of unofficial members through the Governor was intended to counterbalance the dominance of official members in Hong Kong's legislative bodies. During the British administration (1843–1997), unofficial members in the LegCo and ExCo mirrored the interests of a narrow segment of society, such as commerce, finance, and a small segment of industrial interests from the Shanghai business community. For example, in the 1980s, the chairmen of large conglomerates, such as the Hong Kong Shanghai Banking Corporation, Hutchinson Int. Ltd, Jardine, Matheson & Co., Butterfield & Swire Ltd, and Wheelcock Marden & Co., were among the unofficial members of the ExCo and LegCo (Rear, 1971). In his seminal article 'One Brand of Politics', Rear (1971) highlights the dominance of big business among the unofficial members in the ExCo and LegCo.[88] Nevertheless, some of the important business firms and leaders, such as Y.K. Pao (World Wide Shipping) and Li Ka-Shing (Cheung Kong Holdings), were not members of political bodies such as the LegCo or ExCo.[89]

In the 1970s, more than half of the unofficial members had double memberships in the ExCo and the LegCo. These primarily included primarily merchants, bankers and executives from utility companies (Rear, 1971). Although these unofficial members of the ExCo and LegCo could not determine policies, they nevertheless wielded enormous influence because the government rarely resisted their requests (Rear, 1971). The Governor was not legally bound to act according to the advice of the ExCo, but it was longstanding convention to respects the majority views of the ExCo, which was supposed to be consulted on all major policy issues.[90] The LegCo's role was defined by law. No money could be spent by the government without the LegCo's approval, and no law could be passed except by the LegCo (L. Goodstadt, personal communication, 12 February 2015). Every policy involving the spending of additional money required the examination by the Finance Branch of the government and approval for inclusion in the annual budget of the Financial Secretary (Goodstadt, 2015).[91]

[88] Official members refer specifically to the Secretaries of government bureaux, who represent their departments in the legislative process. The appointment of unofficial members was intended to counterbalance the official members in Hong Kong's legislative bodies.
[89] I am grateful to Leo Goodstadt for this observation.
[90] Goodstadt (2015) highlights that there is one important exception, namely the annual budget.
[91] However, the Financial Secretary did not have a legal veto. If the Governor ordered the inclusion of a proposal in the budget, the Financial Secretary would have to obey (Goodstadt, 2015).

Another long-standing tradition related to the prerogative of the HKGCC to nominate representatives to sit in the LegCo (Miners, 1991; Wong, 2012). Prior to the introduction of functional constituency elections in the 1980s, the HKGCC (and others) nominated representatives to sit in the legislature, and the governor then appointed each of them in individual's private capacity.[92] In effect, the chamber appointed the member; legally, though, there was room for the governor to reject a nominee (D. O'Rear, personal communication, 17 September 2015). According to O'Rear, chief economist of the HKGCC, that has never happened in Hong Kong (O'Rear, 2015). Likewise, it was convention that the justices of the peace nominated members to the LegCo (Miners, 1991). The title of justice of the peace was awarded to honour community leaders who contributed to the well-being of Hong Kong. Individuals from trade, finance, commerce, and merchant organisations comprised the majority of justices of the peace (Ngo, 1996).

The HKGCC's interaction with the government was described as very deep (see HKGCC, Minutes of the General Meetings 1861–1970). Miner's statement that "[t]he full-time officials of the General Chamber of Commerce [were] in daily contact with […] government departments, and the same is true of other leading business and professional groups" indicates the deep penetration of the business sector in Hong Kong's policy making structures (Miners, 1991, p.188). Likewise, O'Rear emphasises that anytime the government set up an advisory committee, it was very likely to ask the HKGCC for a nomination (D. O'Rear, personal communication, 23 October 2013). The HKGCC had a clear monopoly position in the representation of business between the 1960s and 1980s. It represented the view of trade/commerce and large banks. This is supported by Dr Helmut Sohmen – former chairman of the HKGCC – who claims that the HKGCC was the most powerful business association in Hong Kong at that time (H. Sohmen, personal communication, 19 September 2013). Likewise, Ho Sai Chu – former LegCo member, and lifelong honorary chairman of the Hong Kong Chinese Chamber of Commerce – emphasises that before 1997 the HKGCC dominated Hong Kong's business organisations (Ho Sai Chu, personal communication, 25 November 2013). Unlike the HKGCC, the Hong Kong Chinese Chamber of Commerce was characterised by high levels of internal fragmentation, power struggles along factions with different ideologies, and

[92] The system of functional constituencies confines the suffrage to a narrow base of umbrella organisations (e.g. the HKGCC and the Hong Kong Chinese Chamber of Commerce) or sector organisations (e.g. the Federation of Hong Kong Cotton Weavers, the Federation of Hong Kong Garment Manufacturers, and the Hong Kong Chinese Textile Mills Association). Goodstadt's polemical statement that "[functional constituencies] were presented to the Hong Kong public and the outside world as a bold innovation [and as] a major advance towards a democratic future" indicates the continuity of a policy-formulation framework, which has been dominated by bureaucrats and business interests (Goodstadt, 2006, p. 54). The proportion of functional constituency members in LegCo increased from 21 per cent in 1985 to 50 per cent in 1995. In addition to functional constituencies, geographical constituencies were introduced in 1991, with 30 per cent of the LegCo seats. This number was further increased to 33 per cent in 1995 and to 50 per cent in 2004 (Young and Law, 2006, p. 64). During the last British administration under Governor Patten (1992-1997), all 60 seats of the LegCo were opened to direct election.

low research capacity. This made it difficult for the Hong Kong Chinese Chamber of Commerce to take an unified position vis-à-vis policy makers. Small Chinese traders, which could not become members of the HKGCC usually joined the Hong Kong Chinese Chamber of Commerce. Unlike the Chinese Chamber of Commerce the HKGCC had a strong structure, deep formal and informal linkages with the state, and an extensive internal research capacity (O'Rear, 2013). For example, the HKGCC had about 20 committees dealing with functional and geographic issues (O'Rear, 2013). They generated papers and viewpoints, which were passed up the line through the Secretariat to the General Committee, the HKGCC's board of directors (O'Rear, 2013).

While Hong Kong's state apparatus had low levels of autonomy from finance and commerce, it enjoyed high levels of autonomy from the Colonial Office in London as well as from domestic manufacturers. The British rule of Hong Kong (1843–1997) was coined by long-standing conventions and official documents. The basic documents included the Royal Instructions and the Letters Patent. The Letters Patent created the ExCo and the LegCo as well as the office of the Governor, whereas the Royal Instructions, a subsidiary legislation, specified in more detail the procedures and composition of the LegCo and the ExCo. Although these documents granted the British Crown comprehensive powers over Hong Kong, it has been a long-standing convention that the British government (and to some extent after 1997 the Chinese government) rarely issued instruction about the internal and economic affairs of Hong Kong. For example, if Hong Kong's policymakers received policy directives from London with regard to Hong Kong's industrial domain then they typically ignored them. Goodstadt's statement that "[London] permitted the colony a degree of freedom […] without precedent in British imperial history" suggests high a level of autonomy from the UK (Goodstadt, 2005, p. 49). Goodstadt's statement that Hong Kong's policy makers "…were very prepared to clash with London when the colonial administration was asked to follow a course of action which might be convenient or economically advantageous to the United Kingdom, but which was unacceptable to Hong Kong" (Goodstadt, 2005, p. 50).

Hong Kong's manufacturers were weakly mobilised. The department that formally covered policy-making in the industrial domain was the Department of Commerce and Industry (established in 1950). At the very beginning of its operation the main function of the Department of Commerce and Industry's was only the collection of trade statistics (Ngo, 1996, p. 129). The structure of this department was heavily biased towards trade and commerce. This was reflected in its internal organisation, comprising a very large Commerce Section and a very small Industry Section. While the Commerce Section expanded rapidly, the Industry Section remained very small and relatively insignificant (Ngo, 1996). For example, out of the 811 staff in 1960, 20 staff members belonged to the Trade Development Branch, whereas only four belonged to the Industrial Development Branch (Ngo, 1996, p. 178). While the Commerce Section had strong links to the HKGCC, the industry section had links to the Chinese Manufacturing Association (CMA) and the FHKI (Ngo, 1996). In the 1980s, the Department of Commerce and Industry was split into three separate institutions, further weakening the Industry Section of the department, as highly specialist industry experts were transferred to other departments and replaced by administrative officers with little industrial expertise or sympathy with the industry's demands (Ngo, 1996). As a result, from the 1980s onwards, the newly created Industry Department's main focus was on the promotion of overseas industrial investment in Hong Kong (Ngo, 1996).

No single association could claim monopoly representation for Hong Kong's industrial actors. Between the 1960s and the 1980s, the CMA and the FHKI competed for members (D. Akers-Jones, personal communication, 01 November 2013; *Far Eastern Economic Review*, 6 June 1963, pp. 563–565). The CMA was Hong Kong's oldest and largest association for industrial interests.[93] Culture and longstanding traditions influenced its organisational structure. Many of the key actors who sat on important and powerful internal CMA committees were "still steeped in traditional Chinese mentality" and were "showing little awareness of the British style of governmental practice" (P.C. Lund, personal communication, 15 November 2013). As a result, the CMA invested very little in attempts to engage with governmental policies (Lund, 2013). According to a former CMA employee, the "CMA's confidence in shaping industrial policy and in fully engaging with the government was below its potential to do so" (Lund, 2013). Instead of shaping government policies, the CMA followed a practice of adjustment.

Cultural differences led to a split between Cantonese and Shanghainese manufacturers. The CMA was predominantly Cantonese, and most of its members were local Cantonese family enterprises (Lund, 2013). Members of the CMA strongly resented large Shanghainese industrialists, chiefly on grounds of tradition and language. Most Shanghainese entrepreneurs in Hong Kong had received a Western education at elite universities, such as the MIT, the University of Chicago, the LSE, and the Imperial College, and spoke English (Wong, 1988). Furthermore, Shanghainese entrepreneurs tried to adopt a Western appearance by registering their companies under English names and by appointing well-known British merchants to boards of directors (Wong, 1988). As a result, instead of joining the CMA, most of the Shanghainese manufacturers joined other associations, such as the HKGCC, which also created an industrial unit (Ngo, 1996).[94] Sir Akers-Jones – former Hong Kong Governor – noted that the Hong Kong government of the day was very sceptical of the CMA (Akers-Jones, 2013), a view

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[93] The creation of the CMA in 1934, was an outcome of Hong Kong's manufacturers attempts to organise themselves in a context of import tariffs posed by China on Hong Kong products (Ngo, 1996, p. 78).

[94] But according to O'Rear there have only been very few industrial members of the HKGCC (O'Rear, 2013).

supported by Ngo (1996), who claims the government considered the CMA as a “mahjong club”.[95] Ngo’s statement that “[i]n the view of the government, the CMA lacked professional staff to run the organisation and was not well informed on the overseas market conditions” highlights the government’s distrust (Ngo, 1996, p. 116). To weaken the CMA, the government created the FHKI in 1960. During this period, many new enterprises were created in Hong Kong, specifically textile firms, and the government was not keen for these enterprises to be organised under the CMA (Akers-Jones, 2013). Although the FHKI was considered by the government as the official representative of Hong Kong’s manufacturing sector, it had the backing of only a minority of Hong Kong’s industrialists. Membership in the FHKI was highly restricted to medium to large companies employing more than 100 full-time workers (Ngo, 1996, p. 144). The General Committee of the FHKI chiefly represented British merchants, large Shanghainese industrials, and the HKGCC (Ngo, 1996).

5.3 POLICY-MAKING AND CHOICES – THE POLICY NETWORK IN OPERATION

The decision against creating state finance institutions with development mandates in Hong Kong’s industrial domain arose out of a number of reviews between the late 1950s and the late 1970s. Over this period, Hong Kong’s clientele pluralist PN had an important influence on these reviews. Central to them was the question of how Hong Kong should address increasing external pressures, notably international competition and protectionism in labour-intensive industries. State-society relations in the industrial policy domain were characterised by an established convention that the Governor follows the advice of the ExCo (Miners, 1991). It was long-established convention to not use the majority of the official members in the LegCo to overrule concordant opposition from unofficial members (Miners, 1991). The ExCo also played an important role in the appointment of committees, whilst the Financial Secretary had to approve any new law requiring the spending of additional money.

Little-noticed by most academic accounts of Hong Kong’s industrialisation was the real potential that existed for the Hong Kong state to develop into a much more active and powerful economic player.[96] In particular, the British government in London supported the idea of ‘economic planning’ in their colonial territories as a means of achieving economic growth and development (Goodstadt, 2012, p. 119). As a result, Hong Kong even prepared a 10-year development plan (*Far Eastern Economic Review*, 19 May 1948). In the early postwar period, Hong Kong’s government was actively involved in buying up large stocks of cotton yarn with

[95] Mahjong is a traditional Chinese board game.
[96] However, there are some exceptions, notably Goodstadt (2012).

the purpose of keeping Hong Kong's local mills in operation at a time when it was difficult to obtain supply (Goodstadt, 2012). Goodstadt (2012) highlights that there was a contest with respect to the level of state intervention as well as the creation of state finance institutions. Hong Kong's manufacturers in particular demanded the creation of state finance institutions, notably a state development bank and industrial-development corporations. This could have created the possibility for a DBS or for a Temasek-like institutions to emerge in Hong Kong.

In terms of the overall argument, the case of financial institutions in Hong Kong's industrial domain provides only limited support for a diffusion argument. Between the late 1950s and 1980s, it was uncommon for an industrialising economy such as Hong Kong to rely solely on private finance institutions in the industrial domain (Goodstadt, 2005, p. 4).[97] Goodstadt's statement that "Hong Kong refused to follow the prevailing economic fashions" suggests that Hong Kong explicitly rejected best practices concerning financial choices in the industrial domain (Goodstadt, 2005, p. 3). International organisations, such as the World Bank, recommended the creation of a state-run industrial bank in Hong Kong (*Far Eastern Economic Review*, 20 May 1968; *Far Eastern Economic Review*, 30 May 1968). Even Hong Kong's administration officials had been looking at other examples, such as the Development Corporation of Malaya and the Development Finance Corporation of Ceylon (Industrial Bank Committee Proceedings, 1959–1966). By drawing on examples of newly industrialising economies in East Asia, Hong Kong's manufacturers proposed – via newspapers and LegCo debates – the state finance organisations of countries, such as Singapore, as potential templates for Hong Kong (Hong Kong Hansard, 29 October 1981, p. 120). They highlighted the experience of South Korea, Taiwan, and Singapore and recommended a more active state involvement (Hong Kong Hansard, 14 January 1987, pp. 729–730). Hong Kong shared many similarities with Singapore, which in 1974 created an SWF with a diversification and development mandate. As such, from the early 1970s onwards, Hong Kong had a peer that was confronted by a set of separate but similar pressures and ended up creating an SWF. This chapter finds that, from the late 1950s onwards, the establishment of a state-run industrial bank and the creation of a state-run development fund or development corporation were available options and were debated in Hong Kong. Although Hong Kong's policy makers looked at other countries, they decided against the creation of state finance institutions in the industrial domain (see Industrial Bank Committee, 1960). The observed outcome – the decision against creating state finance institutions with development mandates in Hong Kong's industrial domain – was contrary to what a diffusion argument would predict.

[97] It seems that Goodstadt (2005) referred to newly industrialising economies, such as Singapore, Japan, South Korea and Taiwan.

Likewise, an efficiency argument cannot explain Hong Kong's institutional choices in the industrial domain. Confronted with pressures to pursue industrial upgrading into more capital-intensive industrial activities, a supporter of an efficiency argument would have expected the creation of an SWF in Hong Kong. Pressures for upgrading and diversification were especially high between the late 1960s and late 1970s. For example, the Report of the Advisory Committee on Diversification emphasised that "[s]ome of the cost advantages that Hong Kong enjoyed at the beginning of the period have undoubtedly diminished over time" and that this was "partly because of the success of other economies in expanding their lower-cost output capacity" (Advisory Committee on Diversification Report, 1979, p. 37). It was repeatedly highlighted that Hong Kong's neighbouring countries were abundantly endowed with resources (e.g. land and labour), which made it easier for them to compete with Hong Kong in labour-intensive industries (Hong Kong Hansard 29 October 1981, pp. 119–121). Given that China did not effectively start its opening until early 1980s, Hong Kong's industrialists did not have the option of outsourcing labour-intensive production into labour-abundant mainland China in the 1970s. A supporter of an efficiency argument would expect the creation of state finance institutions with development mandates, which would have supported the structural change from labour-intensive manufacturing towards more capital-intensive manufacturing. A supporter of an efficiency argument would find that the creation of a state finance institution could make a valuable contribution by helping Hong Kong's industry to upgrade their production to higher value added industries. From the late 1960s onwards it was highlighted by observers that Hong Kong's industrial input needed more capitalisation in order to address increasing labour costs (*South China Morning Post*, 25 February 1968). Hence, the observed outcome – the decision against creating state finance institutions with development mandates in Hong Kong's industrial domain – was contrary to what a supporter of an efficiency argument would expect.

PARTICIPANTS' PREFERENCES

Different socio-economic actors in Hong Kong's industrial domain had different preferences regarding types of finance institutions. While a small section of the Hong Kong Commerce and Industry Department (i.e. the Industry Section), together with Hong Kong's industrialists, supported the creation of a state finance institution that would channel capital on a preferential basis to domestic industry, the government's Finance Branch together with finance and commerce actors supported private finance institutions in the industrial domain. The Finance Branch, led by the Financial Secretary, was highly critical of the creation of state finance institutions in Hong Kong's industrial domain (Hong Kong Hansard, 9 October 1970). The official position was that it is not the government's role to pick winners and that therefore it should let market forces decide (A. Chan, personal communication, 02 December 2013). A more unofficial position among key policy makers was to not interfere with the preferences of domestic finance interests. For example, a confidential mail exchange revealed that it was not in the government's interest to interfere with the preferences of Hong Kong's commercial banks. The Financial Secretary's statement that "[t]he general view […] was that Government should not come into a sphere which was properly that of banking" reveals the Finance Branch's support for the domestic private finance sector (correspondence between the CEO of the Chartered Bank and the Financial Secretary *quoted from* Proceedings of the Industrial Bank Committee, 1959–1966, letter from the 22 October 1959 from A.O.Small, p. 7).

Finance and commerce actors shared similar preferences with the government's Finance Branch against the creation of a state development bank or a development fund in Hong Kong. Ngo's statement that "[f]rom the outset, the dominant commercial banks, including Hongkong Bank, Hang Seng Bank (a subsidiary of Hongkong Bank), and Chartered Bank, which had extensive interlocking directorates with the British merchants houses, had been strong opponents of any form of industrial financing other than the existing practice of commercial banks" illustrates the finance and commerce sector's opposition to state finance institutions in Hong Kong's industrial domain (Ngo, 1996, p. 195). Banks especially feared competing with a state institution providing cheap credit (*Hong Kong Standard*, 24 January 1968). Because the industrial credit market was highly profitable, private commercial banks were keen to keep the state out of it. In the late 1950s Hong Kong's commercial banks realised that industrial financing was a highly profitable market niche, because it involved letters of credit, foreign exchange transactions, and packaging credits (Goodstadt, 2013). Like private commercial banks, commerce actors, notably the HKGCC, objected to the creation of state financial institutions in the industrial policy domain (O'Rear, 2013; Sohmen, 2013). According to O'Rear – former Chief Economist of the HKGCC – the HKGCC was highly supportive of a policy of non-intervention, and thus opposed the creation of state finance institutions in Hong Kong's industrial domain (O'Rear, 2013).[98] This was partly because of the strong connections between Hong Kong's merchant houses and Hong Kong's commercial banks. Hong Kong's major commerce and trade actors had strong linkages to commercial banks – notably via cross directorships and equity holdings – and weak linkages to domestic industry (see Ngo, 1996). Apart from financing industrial exports, Hong Kong's merchants had little interest in supporting Hong Kong's industrial production (Ngo, 1996). They feared that an industrial policy could compromise Hong Kong's existing trade policy (Ngo, 1996). Consequently, Ngo emphasises that "[t]he result was that industrial exporting and industrial production became two separated spheres of activities" (Ngo, 1996, p. 104).

[98] According to Ngo (1996) the merchants had little interest in supporting Hong Kong's industry or its financing. Merchants feared that an industrial policy could compromise Hong Kong's existing trade policy (Ngo, 1996). Ngo emphasised that "[t]hey were interested only in financing industrial exports, but no industrial production. The result was that industrial exporting and industrial production became two separated spheres of activities" (Ngo, 1996, p. 104).

In stark contrast to finance and commerce organisations, Hong Kong's industrialists supported the creation of a state finance institution with a mandate of facilitating industrial upgrading and diversification.[99] To industrialists, the purpose of such an institution would have been to provide medium- and long-term loans for industrial organisations at preferential rates to support industrial mergers and take-overs and to facilitate technology transfer (Hong Kong Hansard, 28 March 1979, p. 652; Hong Kong Hansard, 14 January 1987, p. 719). Hong Kong's manufacturers complained about the high interest rates charged by private commercial banks and the conditions under which industrial credit had been provided by private commercial banks (see Report of the Industrial Development, 1960). According to Hong Kong's manufacturers, this made it very difficult to finance industrial upgrading and diversification, which was seen as necessary for addressing increasing levels of international competition and protectionism. Specifically, the CMA emphasised the need to create a state industrial bank to support the diversification efforts and long-term financing needs of domestic industrialists (letter from the CMA on the 27th of July 1959, *quoted from* Industrial Bank Committee Report, 1960). The CMA "requested the government to set up a special agency responsible for industrial lending, and the CMA's chairman and vice-chairman were entrusted to pass the demand to the authorities" (Chiu, 1994, p. 77). The CMA also suggested using Hong Kong's fiscal surpluses or its currency reserves as a financing source for the creation of an 'industrial development fund' (Hong Kong Hansard, 28 March 1979, p. 652; Hong Kong Hansard, 29 October 1981, pp. 119–121; Hong Kong Hansard, 14 January, 1987, p. 719).

Advisory Committees (1950s–1970s)

Between the late 1950s and the late 1970s, decisions about the kind of finance institutions to be set up in Hong Kong's industrial domain grew out of a number of reviews, including the reviews of the Industrial Bank Committee (1959/1960), the review of the Working Committee on Productivity (1963/1964), the review of the Trade and Industry Advisory Board (1968), and the review of the Advisory Committee on Diversification (1979; 1979a). All were influenced by Hong Kong's clientele pluralist PN. Thanks to their prominent positions in legislative and executive bodies (i.e. LegCo and ExCo), banking actors and merchants had developed close links to Hong Kong's key policy makers in the industrial domain (see Rear, 1971; Chiu 1994; Brewer and MacPherson, 1997; Chan, 1998). Hong Kong's clientele pluralist PN operated via the appointment of finance and commerce actors to these committees. At the same time, high power concentration within the state apparatus, combined with low levels of autonomy from

[99] This was highlighted in a local newspaper (see *Wah Kiu Po,* 21 September 1953; 6 January 1954; 15 May 1954; 22 August 1958; 8 September 1958; 21 April 1958; 11 September 1958).

highly mobilised finance and commerce actors, allowed the bypassing of domestic industrial organisations in policy-making processes.

INCLUSION OF COMMERCIAL BANKS AND EXCLUSION OF INDUSTRIALISTS

The decision against creating a state industrial bank with the objective of channelling capital into the domestic industrial domain at competitive rates grew out of a review in 1959–1960 by the Industrial Bank Committee. On behalf of Hong Kong's Governor, the Financial Secretary appointed the Industrial Bank Committee with the aim of investigating the issue of creating an industrial bank (Report of the Industrial Bank Committee, 1960). According to Sir Akers-Jones – former Chief Secretary and Governor of Hong Kong – the Financial Secretary was 'very closely involved' in choosing the membership of the Industrial Bank Committee (Akers-Jones, 2013). The Financial Secretary's confidential comment that "[he] ensured that there was strong banking representation on it" indicates the intended over-representation of the banking sector in the review (correspondence between the CEO of the Chartered Bank and the Financial Secretary *quoted in* Industrial Bank Committee Proceedings, 1959–1966, letter from the 22 October 1959 from A.O.Small, p. 7).

Only private commercial bankers and officials with a banking background were appointed. The committee consisted of six members, including J.J. Cowperthwaite, who chaired the committee in his position as Financial Secretary, as well as five unofficial members: Y.H. Kan (Chief of the Bank of East Asia), Q. W. Lee (Director of the Hang Seng Bank), Dhun Ruttonjee (Legislative Councilor with a degree in law), and A. O. Small, and G.OW. Stewart (Manager of the Hong Kong Bank; see Industrial Bank Committee, 1960, p. 17). None had an industrial background or a direct affiliation with the industrial sector. The large-scale inclusion of banking actors had informed the operation of the Industrial Bank Committee. Neither industrialists nor representatives of the Industry Section of the Department of Commerce and Industry were appointed to the highly influential Industrial Bank Committee. Thus, industry representatives were not involved in the policy processes leading to the decision against a state-run industrial bank. Industrialist associations, notably the CMA, were merely allowed to submit a position paper. Interestingly, there was only one official meeting between the Industrial Bank Committee and representatives of the industrial sector, during which the industrial sector was represented by the CMA and written memoranda were presented by other stakeholders, including the HKGCC, the Working Party of the FHKI, and the Director of Commerce and Industry Department (see Report of the Industrial Bank Committee, 1960).

The exclusion of industrialists from the committee was justified by mistrust among Hong Kong's key policy makers. The government's attitude to the CMA was highly critical. The government's view of the CMA as inefficient and unreliable in policy processes was revealed in a confidential letter of July 12, 1960, from the Secretariat for Chinese Affairs to the Financial Secretary. The Secretary for Chinese Affairs noted: “It seems to me that the publication of the exchange of correspondence with the [CMA] could certainly do no harm, in view of their present tactics, in that it does not show them up in a particularly good light as an efficient body” (Industrial Bank Committee Proceedings, *1959–1966,* p. 67). This was carefully indicated by the Report of the Industrial Bank Committee (1960), which questioned the data forwarded by the industrial associations, notably the CMA. The Industrial Bank Committee Report (1960) continued that “[a]n appeal to individual industrialists or intending industrialists to come forward to the Committee would not, we feel, have been an appropriate course of action, as the Committee was not in a position to investigate and judge the status of individual industrial enterprises or projects” (Industrial Bank Committee Report, 1960, p. 4). As a result, it was noted that “[t]he Committee was therefore forced to rely very largely on its members’ own knowledge of the position and on their private enquiries” (Industrial Bank Committee Report, 1960, p. 14).

The Industrial Bank Committee produced a highly influential report in 1960 instructing policy makers not to create a state industrial development bank. The stance of the Industrial Bank Committee reflected the preferences of Hong Kong’s banking community. By drawing on the report of the Industrial Bank Committee, which was against the creation of an industrial bank, Hong Kong’s government decided to not create a state finance institution in the industrial domain. The report noted that developed countries created industrial banks in order to respond to the “[commercial] banker’s reluctance to borrow short and lend long” and that developing countries had created such institutions in order to respond to the “lack of capital resources” (Industrial Bank Committee Report, 1960, p. 2). Although the report outlines some of the industry’s financing problems, it claimed that there was no lack of capital resources in Hong Kong and that commercial banks did not hesitate to finance good projects. The report thus concluded that there was no need for the creation of state finance institutions with development mandates in the form of an industrial bank or a development finance corporation (Industrial Bank Committee Report, 1960).

DISCUSSIONS ON THE INDUSTRIAL BANK COMMITTEE AND CHOICES MADE

Discussions on the creation of state finance institutions with development mandates started in the late 1950s. In 1958, it became public that Hong Kong’s government allocated a significant part of its foreign reserves to foreign exchange assets, including equities. A statement in the *Far Eastern Economic Review* that “the Hong Kong Government has over [HK]$400,000,000 tucked away in sterling investments, and [HK]$20,000,000 invested in Federation of Malaya

Stock" was followed by the question of whether it would be "desirable to lend [HK]$ 50,000,000 from these reserves to a Development Corporation?" (*Far Eastern Economic Review*, 25 December 1958, p. 850). It was suggested that HK$50 mn could help the diversification of Hong Kong's economy by creating new industries of advanced types, such as by attracting British Motor Corporation to start a plant in Hong Kong (*Far Eastern Economic Review,* 25 December 1958). Attention was drawn to the role of development corporations in other countries, notably the Development Finance Corporation of Ceylon (*Far Eastern Economic Review* 25 Dec 1958, pp. 848–851). Later, the *Far Eastern Economic Review* repeatedly noted that Hong Kong could have created a development fund with part of the surplus money which was used by the Exchange Fund for Hong Kong's currency stabilisation-policies and bank bailouts of the 1960s (see *Far Eastern Economic Review,* 11 March 1960; 9 April 1964; 12 November 1964; 12 March 1965; 10 October 1966; 30 November 1967; 4 April 1968). Interestingly, the government argued that insufficient funds were available for the creation of a development bank in Hong Kong (*Hong Kong Standard*, 5 January 1968). Although the *Far Eastern Economic Review*'s reports were in the interest of Hong Kong's industrial community, and particularly the CMA, there was little coordinated interaction between the CMA and the FHKI or with individual industrialists and professionals with similar preferences (see Hong Kong Hansard, 29 October 1981, pp. 119–121; Press Release Federation of Hong Kong Industries on 03. 10. 1981, in Industry Financial Assistance 1979-1983).

Low levels of mobilisation among industrial actors was reflected in their uncoordinated and fragmented stance during the discussion on state finance institutions. Individual industrial actors, individual professionals, and individual industrial associations such as the FHKI and the CMA separately supported the creation of state finance institutions. Because of their voluntary character, as well as the lack of in-house capacity for gathering information, industrial associations, notably the CMA, struggled to collect information from its members. For example, a former CMA employee mentioned that a number of organisational factors led to the CMA's difficulties in representing its constituency's preferences in a systematic way (Lund, 2013). Industrialists criticised the CMA's inability to collect information about the financing situation of Hong Kong's manufacturers.[101] According to the CMA, the information about the financial situation of Hong Kong's manufacturers required by the Industrial Bank Committee was difficult to obtain. The CMA director's statement that "it is an extremely difficult requirement put forward by the Industrial Bank Committee for the [CMA] or others concerned to gather 'concrete examples' of the matter" draws attention to the CMA's difficulties in obtaining information (*Hong Kong Standard,* 5 August 1960).

[101] For example, a Hong Kong industrialist's statement that "[i]t should be pointed out that not all factories are members of the CMA, and therefore it is not fair to penalise our entire industry on account of the CMA's failure to supply information" highlights industrialists' critique vis-à-vis the CMA (*Star*, 20 January 1968).

In the debate, Hong Kong's private finance and commerce actors were highly sceptical of the creation of state finance institutions in the industrial domain. According to them, state finance institutions would distort the flow of capital and lead to inefficient allocation decisions (see Ngo, 1996). Instead, bankers suggested relying on existing private industrial financing schemes (*Hong Kong Standard*, 24 January 1968). The finance/commerce sector's view was shared by the government's Finance Branch. The Financial Secretary's statement that it is "still the better course to rely on the nineteenth century's 'hidden hand' than to thrust clumsy bureaucratic fingers" indicates the 'deep-seated dislike and distrust' of economic planning and planning controls among high level government officials (Hong Kong Hansard, 1962, p. 133).

Hong Kong's government was able to ignore the industrialists' requests for the creation of an industrial bank. According to Goodstadt (2015), the government refused to set up an industrial bank because the manufacturers' associations could provide no evidence of a shortage of loan financing for industry. As a consequence, industrial producer groups criticised the composition of the Industrial Bank Committee, which reflected Hong Kong's PN. Industrial associations such as the CMA regarded the report as vague as well as biased, and they demanded that the government reconsider its decision (*South China Morning Post*, 5 August 1960; *Hong Kong Standard,* 5 August 1960). A high-level CMA representative expressed "great dissatisfaction" over the Industrial Bank Committee decision, and specifically with the way the Industrial Bank Committee collected information (*Hong Kong Standard,* 5 August 1960). The Industrial Bank Committee's decision was reported as "unfair and mysterious" since it was not published publicly (*The Star*, 20 January 1968). Soon after the controversial Industrial Bank Committee Report (1960), a number of other reviews were initiated between the early 1960s and late 1970s.

INTERNATIONAL PROTECTIONISM AND ADVISORY COMMITTEES (1960s–1970s)

Between the 1960s and 1970s, an international protectionist wave in labour-intensive sectors put significant pressures on Hong Kong's industry towards diversification and upgrading. OECD countries increasingly alleged price dumping by Hong Kong manufacturers (Hong Kong Industry Department, 1989, p. 18). At this time, around 70 per cent of Hong Kong's total exports (in value terms) went to the US, the UK, West Germany, Japan, Australia, and Canada (Lee, 1976, p. 16). Protectionist policies included quotas and import restrictions, such as the Short- and Long-Term Arrangements Regarding International Trade in Cotton Textiles, which extended to 1973. These were replaced in 1973 by the Multi-Fibre Arrangement (Wong et al., 1991).[102] In addition to traditional forms of protectionism such as quotas, new forms emerged, notably free trade areas (e.g. US and Canada; Australia and New Zealand). These free-trade areas, such as 'Fortress Europe', were characterised by free trade flows within and high tariffs outside the areas (Wong et al., 1991).

The proliferation of preferential trade agreements among OECD countries and the simultaneous removal of preferential trade advantages once granted to Hong Kong (e.g. Commonwealth Preferences) put additional pressures on Hong Kong's labour-intensive export industry. Hong Kong's Most Favoured Nations rights were more restricted in the 1970s than in the 1960s (Hong Kong Industry Department, 1989). An official's statement revealed that "[b]y the end of the 1970s over 60 [per cent] by value of Hong Kong's exports of clothing and textiles were subject to restraint, compared with only 10 [per cent] at the beginning of the 1960s" (Hong Kong Hansard, 27 February 1980, p. 455). It is estimated that, at this time, the textile and garment industries earned more than 40 per cent of Hong Kong's export revenue and employed more than 40 per cent of Hong Kong's industrial workforce (The Hong Kong Management Association, 1975, p. 1). This had a massive impact on Hong Kong's industry. By 1973, the textile and clothing sector were estimated to contribute 47.3 per cent of the total the net output of manufacturing in Hong Kong (Advisory Committee on Diversification, 1979a, p. 21).

THE WORKING COMMITTEE ON PRODUCTIVITY IN 1963 AND THE TRADE INDUSTRY ADVISORY BOARD IN 1968

The Working Committee on Productivity was appointed in 1963 to conduct another review to re-address the issue of increasing international competition. Hong Kong's Governor appointed this committee with a clearly specified mandate. It referred to the investigation of Hong Kong's productivity by (a) examining methods of gaining greater productivity, with specific reference to Japan, (b) advising on the desirability of a Productivity Council, and (c) advising on the desirability of a Productivity Centre (Report of the Working Committee on Productivity, 1964). This time, the government carefully excluded topics related to industrial financing facilities. In the official mandate, there was no mention of industrial financing facilities. Instead, the focus was on policies addressing competition in labour-intensive industries that did not directly harm or interfere with the preferences of finance and commerce actors. Competition pressures were re-addressed as an issue of education, training, and research as well as information services and coordination among these issues in official bodies, most notably the Productivity Centre and the

[102] The so-called Multi-Fibre Arrangement was negotiated by about 50 countries in Geneva. Under the Multi-Fibre Arrangement, Hong Kong had restraint agreements with its major export markets (Dorward, 1976, p. 27). The Multi-Fibre Arrangements allowed EU members and the US to implement protectionist measures against textiles from Singapore and Hong Kong.

Productivity Council. This time, the industrial sector was well represented on the committee, notably via the CMA, the FHKI and the director of the Department of Commerce and Industry (Hong Kong Working Committee on Productivity, 1964). The committee recommended the setting up of a Productivity Council and a Productivity Centre, which would provide various services to improve productivity in Hong Kong. Subsequent demands by the FHKI to introduce more comprehensive support schemes such as R&D development were opposed by the Finance Branch on finance grounds (see Ngo, 1996, p. 193). Through their central position in the debate and in the policy making process finance interests managed to keep broader support for state finance institutions in the industrial domain weak.

Following the Working Committee on Productivity's review (1963–1964), the issue of finance institutions in Hong Kong's industrial domain was again under discussion in 1968. In consultation with the Trade Industry Advisory Board, the Department of Commerce and Industry undertook an informal review. During the 1960s, the Trade Industry Advisory Board was a key advisory body for advising the Secretary for Commerce and Industry on policy in the industrial domain (Trade and Industry Department, 2014). The members of the Trade Industry Advisory Board included one Shanghainese industrialist, one representative from the semi-governmental FHKI, a representative from the HKGCC, three bankers, and two merchants (Civil and Miscellaneous Lists, Hong Kong Government, 1 April 1968). Within the Trade Industry Advisory Board, the Hong Kong Bank, the Hang Seng Bank, and the Chartered Bank were strongly against the creation of any form of state finance institution in the industrial domain (Ngo, 1996). This, together with the Financial Secretary's objection, led again to the decision to not create a state finance institution in Hong Kong's industrial domain (Ngo, 1996; *Far Eastern Economic Review*, 17 April 1969).

THE ADVISORY COMMITTEE ON DIVERSIFICATION IN 1977

The global oil shock of 1973–1974, which translated into the 1974–75 recession, provoked another review of Hong Kong's diversification. The Advisory Committee on Diversification was appointed in October 1977 with the purpose of re-investigating a variety of industrial policy issues, notably existing industrial financing facilities (Advisory Committee on Diversification, 1979, 1979a). The official mission of the committee was to advise on "whether the process of diversification of the economy, with particular reference to the manufacturing sector, [could] be facilitated by the modification of existing policies or the introduction of new policies" (Advisory Committee on Diversification, 1979a, p. 2). In an attempt to address increasing protectionist sentiments, specifically in the textile and clothing sectors, the Governor highlighted the need to investigate the desirability of diversification into new industrial activities. It was also noted that the origins of the committee stemmed from earlier calls, dating back to the 1960s, to re-evaluate the government's role in the economy (Report of the Advisory

Committee on Diversification, 1979). These included the evaluation of existing financial institutions in Hong Kong's industrial domain (see Advisory Committee on Diversification, 1979a, p.iii). The structure of the Advisory Committee on Diversification reflected Hong Kong's clientele pluralist PN.

The demand for the creation of Singapore-like state finance institutions continued in Hong Kong throughout the 1970s. Along with calls for the creation of a state development bank and a development fund, there were calls for the establishment of a state-run industrial estate authority. Originally proposed by the Hong Kong Industry Department, domestic industrialists also supported the idea of creating such an authority (Tsim, 1989, p. 110; Hong Kong Hansard, 2 February 1977). A state-run industrial estate authority was perceived as a means of fostering the production of precision machines and quality products, thereby making Hong Kong the "Switzerland of the Orient" (Hong Kong Hansard, 24 March 1976, p. 677; 28 April 1976).

An initial step towards the creation of such an authority had already been made in 1974 with the establishment of a working group that was composed entirely of government officials (Hong Kong Hansard, 2 February 1977). That was possible only because of the support from Hong Kong's governor on the condition that this authority would be converted into an independent corporation (Hong Kong Hansard, 6 October 1976; 2 February 1977). The Hong Kong Industrial Estates Corporation was established in 1977 by statute as a nonprofit autonomous body funded by government loans, with the aim of operating industrial estates for high-tech firms and providing ready-made factory buildings (Sung and Lawrence, 1991). Nevertheless, an observer highlighted that it "was a tough job to get government to agree to set aside land for such [an authority]", particularly because of the Financial Secretary's opposition (Tsim, 1989, p. 110; Hong Kong Hansard, 11 February, 1976).

However, the Hong Kong Industrial Estate Corporation remained largely insignificant as a state finance institution in the industrial domain. The criteria for industrial companies to qualify for support under this authority were very strict (Tsim, 1989, p. 110). As a result, the Hong Kong Industrial Estates Corporation posed little competition in terms of industrial and estate financing to Hong Kong's banks. And, interestingly, the chairman of the Hong Kong Industrial Estate Corporation was one of Hong Kong's major local bankers (Hong Kong Hansard, 30 March 1977). In the early 1990s, the organisation operated only two estates, the Tai Po Industrial Estate with 71 hectares and the Yuen Long Industrial Estate with 67 hectares (Sung and Lawrence 1991, p. 202). Those were small compared to Singapore's Jurong Town Corporation, which by 1973 had developed more than 3,700 hectares of industrial estates comprising 506 factories and employing more than 50,000 people (Yoshihara, 1975, p. 22).

The 1977 review, initiated by the Governor, was not welcome by the government's Finance Branch. The Financial Secretary, who was against the creation of state finance institutions, insisted that a review could be undertaken only under the condition that he was the chairman of the committee (The Hong Kong Management Association, 1978). The Financial Secretary was thus able to control the scope and the agenda of the Advisory Committee on Diversification (Ngo, 1996). It included 13 unofficial members and three official members. The three official members comprised the Financial Secretary, the Director of Trade Industry and Customs, and the Secretary for Economic Services. The unofficial members comprised of three from domestic banks, two from merchant houses, one journalist, one representative of the Finance Branch, and one from the Department of Industry (Report of the Advisory Committee on Diversification, 1979, p. 5). To pre-empt criticism from manufacturing, unofficial members were also drawn from the industrial sector (three came from the FKHI and one from the CMA). These included advocates of state finance institutions, who highlighted their support for creating a development bank, or development fund, or development corporation (Hong Kong Hansard, 28 March 1978; 25 April 1979). However, the committee members were again divided into specialist subcommittees.

Industrialists were carefully allocated to subcommittees, notably the Subcommittee on Industrial Development, which were not mandated to discuss policy issues regarding the kind of finance institutions set up in Hong Kong's industrial domain (Report of the Advisory Committee on Diversification, 1979). However, industrialists in the Subcommittee on Industrial Development emphasised the need for state intervention in terms of support facilities. For example, it was highlighted that Hong Kong should follow other countries' examples, such as that of Singapore (*Report of the Advisory Committee on Diversification*, 1979, p. 272). Ngo's statement that "[b]y marginalising the CMA in the advisory bodies, or by appointing its leaders to the less important committees, the government thus created a subordinate position for the CMA vis-à-vis [other associations]" indicates that socio-economic actors can be excluded from important committees by including them on less relevant bodies (Ngo, 1996, p. 151). Proponents of state finance institutions were not included on the Working Group on Financial Facilities, the subcommittee responsible for discussing issues related to the kinds of finance institutions set up in Hong Kong's industrial domain.

The Working Group on Financial Facilities consisted of one chairman (i.e. M.G.R Sandberg), who also served as the chairman of the Hong Kong Bank, and five official members, including the Secretary of Monetary Affairs, the Commissioner of Banking, the Commissioner of Securities, and the Secretary for Economic Services (Advisory Committee on Diversification, 1979a, v.5). The Working Group on Financial Facilities highlighted that domestic industry had no difficulties in acquiring loans from private commercial banks (Report of the Advisory

Committee on Diversification, 1979). Drawing on the Working Group's suggestion, the report of the Advisory Committee on Diversification (1979) concluded that there was no need for the creation of a state finance institution with a development mandate. The Subcommittee on Industrial Development, which authored the chapter on 'Industrial Development', contradicted the view of the chapter authored by the Working Group on Financial Facilities. These tensions among different subcommittees about financial institutions reflected the structure of state-society relations in Hong Kong's industrial policy domain.

DISCUSSIONS ON FINANCE INSTITUTIONS (1960s–1980s)

Discussions on state finance institutions between the 1960s and 1980s reflected the clientele pluralist PN. Industrialists highlighted the need to develop and upgrade traditional industries through active government support (Hong Kong Hansard, 14 January 1987). Their proposals and demands were made separately and were not co-ordinated. For example, the CMA complained that existing loan schemes in Hong Kong were insufficient for small-scale enterprises representing the majority of Hong Kong firms in relative and absolute terms (see Lee, 1976). By drawing attention to Japanese commercial banks' industrial loan schemes and Britain's Finance Corporation for Industry, the CMA called for another review on finance institutions in the industrial domain (*Far Eastern Economic Review*, 12 March 1965, pp. 469–471). The CMA's chairman highlighted that the process of moving to more sophisticated manufacturing requires long-term low-interest rate loans (*South China Morning Post*, 25 February 1968, p. 10). It was argued that a state-run development bank or a development fund could channel more financial resources into the upgrading of existing industries and the establishment of new industries, such as oil refineries (Hong Kong Hansard, 31 July 1974, p. 1100; Urban Council Annual Conventional Debate, 1975). Individual manufacturers not associated with the CMA highlighted the problem of undercapitalisation (*Star*, 20 January 1968). Interestingly, even professionals not directly affiliated with manufacturing supported industrialists' demand for cheap loans and assistance. For example, LegCo member Maria Chu highlighted Hong Kong's loss of competitive advantage and the need to support domestic industry (Hong Kong Hansard, 29 October 1981). Chu illustrated this point by emphasising that garment production in the early 1980s was around one third more expensive in Hong Kong than in Taiwan or South Korea (Hong Kong Hansard, 29 October 1981).

Concrete ideas about the specific form of a state development fund were proposed quite late in the 1980s, when pressure towards diversification started to ease. It was the context in which China started its effective opening, and many of Hong Kong's manufacturers started to re-allocate labour-intensive industries to mainland China. According to Ho Sai Chu – Honorary

Chairman of the Chinese Chamber of Commerce – Hong Kong's industry moved production to mainland China to take advantage of cheap labour and land (Ho Sai Chu, personal communication, 25 November 2013). Proponents of a development fund had, by then, clearer ideas about designing and sourcing a fund with a development mandate. Interestingly, they came not from the industrial sector but from actors with a professional background. They suggested the use of part of Hong Kong's reserves and the appointment of a development fund committee consisting of government and private sector representatives (Hong Kong Hansard, 14 January 1987). The most explicit call for the creation of a state-run development fund was made in 1986 by LegCo member Chung Pui Lam (Hong Kong Hansard, 6 November 1986, p. 393). Interestingly, he had a professional background (i.e. law firm) and was a representative of Sham Shui Po district, one of Hong Kong's earliest industrial centres, with many small and medium enterprises. Chung Pui Lam proposed "setting up an industrial development fund" in order to help "medium and small- sized factories by providing low interest, long-term loans" (Hong Kong Hansard, 6 November 1986, p. 393). The major objective of such a fund was to "help to promote industrial diversification and the development of […] small and medium-sized factories" (Hong Kong Hansard, 14 January 1987, p. 719). The purpose of such a fund was the provision of preferential loans to selected industries and to support industrial mergers and takeovers as well as to facilitate technology transfer (Hong Kong Hansard, 14 January 1987). Chung's statement that the "fund could also flexibly be engaged in other types of capital investment" suggests a potentially wide investment spectrum for the development fund (Hong Kong Hansard, 14 Jan 1987, p. 719). However, these ideas were not taken up, due to heavy resistance on the part of commerce and banks, who argued that diversification pressures disappeared with the effective opening of China.

POLICY CHOICES MADE (1960s–1980s)

Between the 1960s and 1980s, Hong Kong's policy makers opted repeatedly against the creation of state finance institutions that would provide long-term industrial credit at competitive rates. Hong Kong's finance sector benefited from the decisions to not create state finance institutions. Over that period, private commercial banks increasingly started to offer industrial credits. Banks, notably the Hang Seng Bank and the Hong Kong Bank, started establishing industrial financing schemes (Goodstadt, 2005). According to Jao – an academic and banking expert – the Hong Kong Bank accounted for almost half of the loans to Hong Kong's industry (Jao, 1983). This is confirmed by Andrew Burns, personal secretary to Dr David Li, CEO of the Bank of East Asia (A. Burns, personal communication, 25 October 2013). Burns' proposition that "as dominant player in the market [the Hong Kong Bank had] a much better overview on [industrial credit] than anybody else", indicates the Hong Kong Bank's central position in Hong Kong's industrial domain (Burns, 2013). Data reveal that bank loans and advances to manufacturing was a central and growing part of banking business in the years after 1965.[103] Between 1965 and 1971, the manufacturing sector accounted for about 20 per cent of the total of bank loans and advances (see TABLE 5.3).

TABLE 5.3. *Sectoral Composition of Bank Loans and Advances in million HK$ (1965–1971).*

Sector	1965	1966	1967	1968	1969	1970	1971
Commerce	1,640	1,731	1,698	2,010	2,845	3,424	4,189
Professional and private	683	668	706	808	1,004	1,367	1,862
Building and Construction	933	957	885	832	803	649	723
Transportation	191	197	219	319	730	1,136	1,439
Manufacturing (textiles)	497	519	471	526	516	678	765
Manufacturing (others)	518	632	601	641	974	1,182	1,214
Others	721	771	821	902	1,012	1,234	1,644
Total	5,183	5,475	5,401	6,038	7,884	9,670	11,836

Source: Riedel (1974, p. 124).

The role of private commercial banks in financing Hong Kong's diversification has been controversial. While there are those, notably Goodstadt (2005), who highlight that there was no shortage of credit for industrial undertakings, others, such as Chiu (1994), emphasise the shortage of industrial financing. Interestingly, a study published in 1962 highlighted that the prime rate of leading British Banks in Hong Kong was competitive with commercial banks in the UK (EUI, 1962). For example, in 1961, the prime rate was 6 to 7 per cent in Hong Kong, somewhat lower than the 8 per cent in the UK (EUI, 1962, p. 17). However, it is misleading to compare Hong Kong commercial banks' lending rates with those in developed countries. Industrial enterprises in developed countries were to a large extent not funded by private commercial banks but by state-related development banks or industrial banks with preferential interest rates that were much lower than those of commercial banks (e.g. in the UK the Industrial and Commercial Finance Corporation and the Finance Corporation, in Canada the Canadian Industrial Development Bank, in Japan the Japanese Central Bank for Commercial and Industrial Co-operation; see Industrial Development Committee Report, 1960). Furthermore, there is no public evidence available on whether the British Banks in Hong Kong applied this prime rate to industrial creditors. If they did, it was only to well- established large firms. Most of Hong Kong's firms were small-scale enterprises that usually did not get credit from large British banks (L. Goodstadt, personal communication, 15 November 2013). Even some high-level bank officials in Hong Kong, notably W.C.L Brown, chief manager of the Chartered Bank, indicated the inappropriateness of existing industrial financing. In a speech to the FHKI luncheon meeting on February 17, 1981, he drew attention to the difficulties in

[103] In the year 1965 a new Banking Ordinance necessitated banks to publish statistics on their loans.

industrial financing at attractive terms. Brown's comment that "[t]he availability of relatively long-term funds at acceptable costs is none too promising in the very near future, in view of the prevailing high and unstable interest rates" suggests unfavourable industrial financing conditions in Hong Kong.

Hong Kong's manufacturers did not benefit from this choice, because for three reasons. First, Hong Kong's commercial banks had a preference for short term 'self-liquidating loans', in stark contrast to the needs of industrial long-term finance (*Far Eastern Economic Review*, 24 February 1966, pp. 367–370). For example, an industrialist highlighted that Hong Kong's commercial banks had an 'escape clause' in all loans, which allowed commercial banks to recall the loan at any time (*China Mail,* 20 December 1967). This meant that industrialists could use these loans only for working capital but not for large-scale investments in fixed assets (*China Mail*, 20 December 1967). Second, to get a loan from the banks, manufacturers had to provide security via complex mortgage agreements. Manufacturers had to mortgage their land in order to build the factories, mortgage their factories to buy machinery, mortgage machinery to buy raw materials, and mortgage materials to pay wages (*China Mail,* 2 June 1965). It is estimated that, in the 1960s, around 95 per cent of Hong Kong's factories operated on a very risky financing basis (*China Mail,* 2 June 1965).

Third, large private banks in Hong Kong provided credit with favourable terms only to already well-established large firms with a good reputation (EIU, 1962; 1962a; Riedel, 1974). Jao's statement that the Hong Kong Bank had "a very hard-headed, prudent and shrewd lending policy towards Hong Kong's manufacturing industries" indicates high levels of selectivity on behalf of Hong Kong's large banks (Jao, 1983, p. 553). However, most of Hong Kong's firms in absolute and relative terms were small and medium enterprises. For example, more than 90 per cent of the firms in Hong Kong employed fewer than 50 workers, and only 1.2 per cent of Hong Kong's firms employed more than 200 employees (Nyaw, 1991, p. 199). Consequently, most enterprises in Hong Kong had to rely on smaller banks or on financial intermediaries. Financial intermediaries got loans from large commercial banks and re-lent the money at higher rate to industry (Wong, 1988). These rates commonly ranged between 16 and 20 per cent and had a maturity of 12 to 18 months at a maximum (*Far Eastern Economic Review*, 11 February 1960, p. 315; Topley, 1964 p. 208). Between 1970 and 1980, the growth in industrial investment exceeded the growth rate in bank loans to manufacturing (Brown 1981, pp. 8–9, *quoted* in Industry Financial Assistance, 1979-1983). This suggests that other capital sources, notably informal private channels, were behind the growth in industrial investment. However, informal private channels charged even higher interest rates of between 20 and 30 per cent (Industrial Bank Committee Report, 1960, p. 4). Some authors, notably Monks (2010, p. 46), claim that some industries, such as Hong Kong's toy industry, were actually charged with interest rates of

40 per cent or more. This made it very difficult, especially for small and medium enterprises, to address competition in labour-intensive sectors by upgrading and diversifying into higher value added sectors.

Instead of focusing on industrial financing facilities, Hong Kong's policy makers emphasised the upgrading of education facilities and private finance institutions, especially private commercial banks. By making industrial competition and industrial upgrading to an issue of education and additional services rather than an issue of inadequate industrial financing facilities, the focus was taken off state finance institutions. The provision of additional services comprised the creation of quality support service centres, productivity enhancement services, vocational services and the promotion of quality assurance (Wong et al., 1991). For example, the Hong Kong Productivity Council was established in 1967 to support the promotion of technical change in clothing and textiles. The Plastic Technology Centre Company Limited and the Hong Kong Design and Innovation Company were created to enhance productivity and to provide design services (Chen and Li, 1991). Furthermore, the Hong Kong Quality Assurance Agency and the Product Standard Information Bureau were established to support the promotion of standards and quality (Chen and Li, 1991).

CONCLUSION

This chapter highlights that a PN analysis helps to explain the kinds of finance institutions set up in Hong Kong's industrial policy domain between the 1960s and 1980s. During this period, Hong Kong's policy makers repeatedly opted against the creation of state finance institutions with development mandates. Instead, they decided in favour of private finance institutions, notably private commercial banks. These decisions rose out of a number of reviews on how Hong Kong should address increasing international competition and protectionist pressures. The comparison with Singapore suggests that efficiency as well as diffusion arguments cannot fully explain cross-country and cross-domain variation concerning SWFs with development mandates. In both economies, similar socio-economic actors existed but they were structured differently. Policy choices in Hong Kong's industrial domain were contrary to what efficiency and diffusion arguments would have predicted. Even when confronted with powerful external competition pressures and domestic constraints, both responded with very different kinds of finance institutions (see TABLE 5.4). This chapter reflects the findings of Chapter 4, and adds to the findings by emphasising the distributional struggles among socio-economic actors in policy-making processes about the types of financial institutions set up. Concerning the overall argument, the chapter highlights that diffusion and efficiency aspects did not play a significant role in the kinds of financial institutions set up in Hong Kong's industrial domain.

The first section (5.1) on economic inheritance outlined the external pressures to which Hong Kong's industrial domain was confronted over this period. These pressures related to high levels of international competition in labour-intensive manufacturing and increasing protectionist sentiments among Hong Kong's major export markets. This was the broader context in which policy decisions were made about financial institutions. The second part (5.2) looked at key actors and the type of PN in Hong Kong's industrial domain. The structural relationships of a limited set of organisations in Hong Kong's industrial domain referred to a clientele pluralist PN. It was characterised by a high concentration of power within the government's Finance Branch and low levels of autonomy in the government apparatus stemming from a highly mobilised domestic finance/commerce sector.

The third part (5.3) investigated policy-making and looked at the clientele pluralist PN in operation. It showed the effect of a clientele pluralist PN, in which a highly mobilised domestic banking sector together with a centralised state with low autonomy, influenced discussions and policy making processes concerning the kinds of finance institution set up. It found that the preferences regarding these kinds of finance institutions differed between domestic finance/commerce and domestic manufacturers. Discussions revealed that at that time there were alternative choices available, supported by different actors. It looked at the actors who were included and excluded on policy processes, important for the choices made. The chapter found that only finance/commerce actors were appointed to important committees and sub-committees regarding industrial financing facilities, whereas industrial actors were systematically excluded. Thus, the recommendations of these committees and sub-committees reflected the preferences of finance/commerce actors. Actors who were not part of the PN were harmed by the choices made, or at least did not benefit from them.

TABLE 5.4. *Similar External Pressures and Different Responses in Hong Kong and Singapore (1960s–1997).*

Period	Similar External Pressures		Different Responses	
	Hong Kong	***Singapore***	***Hong Kong***	***Singapore***
1950s–1960s	Regional hostility (i.e. the Korea War, tensions with neighbouring China) leading to a decline in entrepôt trade.	Decline of entrepôt trade following the emancipation of Singapore's neighbours in late 1950s.	Labour intensive export-oriented industrialisation strategy; laissez-faire industrial policy (no industrial bank, non expansion of state sector).	Labour intensive import-substitution industrialisation strategy (common market with Malaya); partial laissez-faire industrial policy (no industrial bank, but expansion of state sector, creation of the MFI).
1960s–1970s	Loss of Commonwealth Preferences (i.e. loss of preferential access to Commonwealth market); tensions with neighbouring China; increasing competition pressure with NIE (Taiwan, South Korea); protectionism in OECD markets.	Expulsion of Singapore from the Malaysian Union (loss of common market); tensions with neighbouring Indonesia; increasing competition pressure with NIE (Taiwan, South Korea); protectionism in OECD markets.	Labour intensive export-oriented industrialisation strategy; laissez-faire industrial policy (e.g. no industrial bank, no development board, no expansion of state sector, no promotion of FDI by MNCs).	Labour intensive export-oriented industrialisation strategy; interventionist industrial policy (e.g. creation of DBS and EDB, expansion of state sector; promotion of FDI by MNCs).
1970s–1980s	Oil shocks, int. recession; protectionism in OECD markets (e.g. Multi-Fibre-Agreements); increasing competition pressure with other Asian countries (e.g. Malaysia, Indonesia, Thailand).	Oil shocks, int. recession; increasing competition pressure with other Asian countries (e.g. Malaysia, Indonesia, Thailand).	Labour intensive export-oriented industrialisation strategy; laissez-faire industrial policy (e.g. no industrial bank, no development board, no expansion of state sector, no promotion of FDI by MNC).	Capital intensive export-oriented development strategy; interventionist industrial policy (e.g. upgrading through the re-organisation of the state sector and creation of Temasek, Sheng-Li Holding, MND Holding).
1980s–1990s	Effective opening of China's industrial zones; partial revival of Hong Kong's role as entrepôt trade hub.	Regional liberalisation (i.e. opening of Malaysia and Indonesia); recession in the US in 1983, especially in the electronics sector; translation of the US recession into Singapore's first recession in 1985.	Outsourcing of labour intensive industries to Mainland China; laissez-faire industrial policy (e.g. no industrial bank, no development board, no expansion of state sector, no development SWF).	Capital intensive export-oriented strategy combined with regionalisation; outsourcing of labour intensive industries to Malaysia and Indonesia; interventionist industrial policy (e.g. re-organisation of Sheng-Li Holding and MND Holding into Temasek).

6. The Effects of State-Directed Policy Networks on Financial Institutions set up in the Savings Domain: The Creation of the Government Investment Corporation

In the 1970s and 1980s, the structure of state-society relations in Singapore's savings domain were consistent with that of a state-directed policy network (PN).[104] It was characterised by a high concentration of decision-making power in the Prime Minister's Office (PMO) and the Deputy Prime Minister's Office (DPMO); high levels of state autonomy and low levels of mobilisation among domestic producer groups. For example, the interest representation system of domestic finance and commerce was weak and fragmented. This structure affected policy-making processes in Singapore's savings domain concerning the kinds of finance institutions that were set up. While many different socio-economic actors – particularly within domestic finance – had a substantive interest in this issue, only a small circle of state actors and international investment houses were directly involved in the policy-making processes that led to the creation of the Government Investment Corporation (GIC).

The present chapter shows how the state-directed PN influenced the creation of the GIC in 1981. That is done through an investigation of the entire range of socio-economic actors in Singapore's savings domain with a substantive interest in this issue. It then examines how the PN operated by influencing policy-making processes in the savings domain. There is an investigation of how PN characteristics played out in policy-making processes through the mechanisms of inclusion in, and exclusion from, important policy-making bodies of socio-economic actors. One of the major questions concerns which actors were included or excluded. Connected to this is the question of who benefited, and who did not benefit from the kind of financial institutions set up. For that reason, the chapter examines the discussions involving the PMO, the DPMO, the Ministry of Finance and domestic and international finance actors.

The chapter argues that Singapore's state-directed PN in the savings domain affected the review of Singapore's reserves in 1980/1981, which led to the creation of the GIC in 1981. This review questioned how Singapore's reserve management has developed against earlier expectations (Singapore Government Press Releases, statement from the Prime Minister's Office 1980, p. 1). The choice to establish the GIC took place in the early 1980s in a context of international investment opportunities and challenges, such as inflation and currency volatility. Given Singapore's high savings levels, high import ratios and its ageing population, policy makers

[104] The saving domain relates to the policy domain which is concerned with the allocation of public and private savings.

came under increasing pressure to respond to these external challenges and opportunities. Discussions at that time reveal the availability of different institutional alternatives, such as the development of a private fund management sector. Preferences with regard to the types of finance institutions differed among socio-economic actors. The main finding of this chapter is that the state-society structures allowed policy makers to bypass domestic private finance actors, which demanded the development of the private fund management, private insurance, and the private pension fund sector (e.g. by outsourcing government funds to the private fund management sector). The state-directed PN operated through the inclusion and exclusion of socio-economic actors on important policy-making bodies. The hierarchical and autonomous structure of the PMO and DPMO allowed for the exclusion of domestic private finance actors. High levels of autonomy enabled state actors to freely choose among international investment advisors. The chapter finds that the structure of state-society relations in Singapore's savings domain facilitated the pursuit of policies and institutions with a long-term horizon and was characterised by high levels of coordination and state involvement. Based on these findings the chapter develops an initial hypothesis for sovereign wealth funds (SWFs) with savings mandates: having a state-directed PN in the savings domain increases the likelihood of creating an SWF with a savings mandate.

Section 6.1 outlines Singapore's macro-economic context, and offers a brief background on Singapore's savings domain up to the late-1970s. Section 6.2 looks at the actors and the state-society relations in Singapore's savings domain. Section 6.3 develops the argument by looking at the effects of the PN on the creation of the GIC in 1981. It investigates the policy-making processes, and identifies who benefited and who was harmed by the choices made. That helps to evaluate the impact of PNs and the mechanisms whereby Singapore's state-directed PN might have operated to influence the creation of the GIC in 1981.

6.1 ECONOMIC INHERITANCE AND MACRO-ECONOMIC CONTEXT (1960s–1970s)

The period between the 1960s and the 1980s was one of significant expansion in state finance institutions, such as the Post Office Savings Bank (POSB), the Development Bank of Singapore (DBS), the Central Provident Fund (CPF), and the Monetary Authority of Singapore (MAS). These mobilised both mandatory and discretionary private savings.[105] Specifically, the CPF, a mandatory state-run pension fund, was an important state finance vehicle that contributed to Singapore's high levels of domestic savings. Its creation reaches back to the early 1950s, when

[105] A substantial part of voluntary private savings in Singapore has been accumulated by government banks, such as the DBS and the POSB.

the International Labour Organisation issued a report that emphasised the “immediate” need to create social-security schemes in less-developed countries (*The Banker*, October 1970, pp. 1107–1109).

Before of the first elections, the colonial government set up a retirement-benefits commission to enquire into the establishment of a CPF (*Annual Report*, Colony of Singapore, 1955 and 1954). These moves were also described as an official response to local strikes and the strong domestic demand for the improvement of workers’ conditions (*Annual Report*, Colony of Singapore, 1954 and 1955). The CPF was set up in 1955 as a statutory board with the official mission of “enabl[ing] Singaporeans to have a secure retirement” (CPF, 2015).[106] Its membership size increased from 180,000 in 1955, 504,828 in 1968 to 1,518,755 in 1980, and its members’ outstanding balance increased from S$9,1 mn in 1955, S$539,7 mn in 1968 to approximately S$10 bn in 1980 and to approximately S$41 bn in 1990 (see TABLE 6.1). The mandatory contribution rates, applying to the employees’ wages as well as to employers’ incomes, increased progressively from 5 per cent in 1955, to 38.5 per cent in 1980, 42 per cent in 1981, 45 per cent in 1982, and to its highest level of 50 per cent in 1985 (Lee, 1984, p. 258; Skully, 1984; Skully and Viksnins, 1987). Over the years, the investment portfolio of the CPF has also changed dramatically. At the beginning in 1955, 50 per cent of CPF’s funds were invested in British £ assets, 9 per cent in Malayan government securities, and 41 per cent in Singapore government bonds; by 1959, about 75 per cent were invested in Singapore government bonds (Lee, 1974, p. 203).

[106] According to Sheng (2013) the CPF and in Malaysia the EPF evolved in the 1950s to provide social stability by the British government and as a ‘bulwark’ against the rise of communism.

TABLE 6.1. *Central Provident Fund (Singapore), Members and Contributions (1955–1990).*

Year	Members	Contributions	Withdrawals	Total amount due to members
		in million S$		
1955	180,000	9.1	n.a	9.1
1956	230,000	25.2	n.a	34.1
1957	265,000	27.9	n.a	61.9
1958	284,000	29,5	n.a	91.0
1959	304,000	29.8	n.a	119.6
1960	321,000	30,6	n.a	149.2
1961	338,000	32.6	n.a	181.0
1962	352,000	35.5	n.a	215.8
1963	369,868	37.6	n.a	258.2
1964	393,743	42.5	n.a	306.3
1965	417,594	46.9	n.a	359.0
1966	442,351	51.5	n.a	415.9
1967	465,029	55.8	n.a	477.3
1968	504,828	68.0	30.7	539.7
1969	560,133	106.6	42.4	632.2
1970	638,829	156.4	45.7	777.5
1971	714,657	223.6	56.4	987.9
1972	855,307	330.8	57.9	1,316.0
1973	961,991	474.7	93.5	1,770.0
1974	1,041,601	686.7	154.3	2,413.7
1975	1,104,417	886.6	216.9	3,234.9
1976	1,177,538	1,008.0	377.7	4,066.1
1977	1,251,070	1,114.7	503.5	4,954.0
1978	1,340,779	1,352.0	657.8	5,981.4
1979	1,435,592	1,753.1	629.3	7,515.5
1980	1,518,755	2,296.0	779.1	9,551.2
1981	1,649,733	3,007,2	1,067.6	12,149.8
1982	1,725,293	3,901.4	1,241.2	15,655.5
1983	1,778,879	4,491.2	1.718.1	19,504.7
1984	1,852,471	5,386.4	3.511.0	22,670.4
1985	1,891,683	5,993.4	3,559.5	26,829.5
1986	1,933,830	4,777.9	3,823.8	29,337.4
1987	n.a	4,446.8	4,297.2	30,607.8
1988	n.a	4,985.1	4,010.2	32,529.3
1989	n.a	6,107.5	3.663.3	36,051.5
1990	n.a	7,165.5	3,994.7	40,646.4

Sources: Yearbook Singapore (1985, p. 313; 1987, p. 289; 1991, p. 282; 1993, p. 318; 1998, p. 374; 2001, p. 368), CPF Board Chairman's Statement and Accounts (31 December 1970).

Public-sector wealth, as well as a significant proportion of private-sector wealth, was channelled into state finance institutions. By law, the CPF was required to deposit its members' contributions with the Monetary Authority of Singapore (MAS), which in return issued Singapore Government Securities (SGS). This made the CPF the major holder of SGS (Lee, 1987). Between 1975 and 1980, the CPF alone was holding more than 70 per cent of all government bonds issued in Singapore (Lee, 1984, p. 259). In the 1980s, the CPF used more than 89 per cent of its assets to acquire SGS (Lee, 1984, p. 259). Other state finance institutions, notably the Post Office Savings Banker (POSB) and the Development Bank of Singapore (DBS), as well as private banks, also had to translate significant portions of their assets into

SGS.[108] For example, as of 1979, the POSB had invested 70 per cent of its assets in SGS (Economic Department MAS, 1980, p. 49).[109] This was significant, given the POSB's dominance in Singapore's domestic retail-banking market.[110] For example, as of 1980, the POSB accounted for approximately 63 per cent of total national savings deposits in Singapore (Yearbook Singapore, 1981, p. 50). Like Singapore's private sector, the public sector was also a major saver. It generated structural budgetary surpluses and operating surpluses of statutory boards and government-linked companies year-on-year (Chong-Yah, 1988). Budget surpluses in Singapore increased from an average of 8 per cent of GDP in the 1970s to an average of 11 per cent of GDP in the 1980s (Carling and Oestreicher, 1995). The proceeds from the bond issuance contributed to a massive increase in sovereign wealth (Schulze, 1990; Lee, 1984, p. 259).

Between the late 1960s and the early 1970s these savings were used as a cheap financing source for domestic development projects. During this period, Singapore's policy makers pursued a deliberate policy of mobilising domestic savings as a 'cheap' source of capital in order to finance infrastructure and housing projects (D. Low, personal communication, 12 February 2014). This strategy also allowed Singapore's policy makers to remain independent from international financial institutions, such as the World Bank, in terms of borrowing (Chong-Yah, 1988). Via the CPF, the government could withdraw high levels of domestic liquidity from the system for a relatively low rate of interest. As such the CPF "was basically a moper of liquidity" (A. Sheng, personal communication, 30 October 2013). Hamilton-Hart's statement that this provided "the government with a low-cost source of noninflationary finance" draws attention to the wider fiscal and monetary impact of Singapore's saving structure (Hamilton-Hart, 2003, p. 94). Domestic savings were channelled into low yielding SGS (Lee, 1974). This worked well since there was plenty of room for investing surplus capital in domestic development and infrastructure projects (Low, 2005). As a result of the low interest paid on SGS, social and public infrastructure projects, such as telecommunication and housing, could be financed at very low costs (Lee, 1974; 1984a).

By the mid-1970s most of Singapore's large development projects were complete, and Singapore increasingly looked abroad for investment opportunities. It started to manage its savings and surpluses increasingly like traditional currency reserves. This was done in the 1970s by the Monetary Authority of Singapore (MAS) Department of Overseas Investments, which invested and managed domestic savings together with the backing of Singapore's currency in highly liquid and low yielding assets, such as gold and foreign currency deposits (Ng Kok Song,

[108] Interestingly also, private banks in Singapore had to maintain very high liquid asset ratios. They had to keep about 20 per cent of their deposit liabilities in SGS (Lee, 1974, p. 57).
[109] The statutory requirement was a minimum of 50 per cent.
[110] The number of POSB branches increased from 44 in 1971 to 105 in 1980; the number of saving accounts increased from 555,000 in 1971 to 1,898,000 in 1980; and the POSB's savings deposits increased from S$91 mn in 1971 to S$ 2,757 mn in 1980 (Lee, 1984, pp. 257–258).

personal communication, 28 February 2014; *The Straits Times*, 23 May 2001). In the late 1970s Singapore's policy makers liberalised exchange control regulation in order to develop Singapore as a financial centre. Here, international market forces were introduced into Singapore's domestic financial system facilitating the free inflow and outflow of capital. Mah-Hui and Maru's statement that this move allowed "Singapore residents and companies to invest in foreign currency deposits or equities" suggests increasing levels of capital mobility (Mah-Hui and Maru, 2010, p. 2). In turn, "[t]his made it possible for all Singapore residents, including corporations, to make payments in all currencies and to invest in any country outside Singapore without restrictions" (Economic Department MAS,1980, pp. 77–78). That was specifically critical in the inflationary period of 1979–1981, which was characterised by the second oil shock (1979–1980), followed by the Latin Debt crisis and the interest rate shock (in the early-1980s).[113] In an effort to stimulate the US economy, US policy makers reacted to the 1979 oil shock with loose monetary policy, leading to high levels of inflation. The US Federal Reserve decided to tighten monetary and fiscal policy to address hyperinflation. The Chairman of the US Federal Reserve, Paul Volcker, tightened monetary policy through an increase of the interest rate up to 20 per cent. The dramatic rise of interest rates – commonly referred to as 'interest rate shock' – had varied consequences for debtor nations and creditor nations. While for debtor nations high interest rates posed severe problems, for creditor nations such as Singapore it became very lucrative to buy US treasury bonds.

6.2 KEY ACTORS AND TYPE OF POLICY NETWORK

Between the 1960s and 1980s, a weakly mobilised domestic private finance sector was confronted with a state that had high levels of autonomy and capacity. Policy-making structures in Singapore have been described as a pyramid (Ho, 2000). Near the top were the Ministries that exercised full policy responsibility within their portfolio, only subject to the overriding authority of the PMO; which is sizeable in terms of its staff, the DPMO and the Cabinet (Ho, 2000; Mauzy and Milne 2002). Even when tensions emerge among state departments they have been quickly resolved because of the existence of hierarchical power concentration within policy-making structures. With regard to Singapore's savings domain, the Ministry of Finance

[113] In the early 1980s banks of OECD countries lent heavily to firms and governments in Latin America, which were unable to pay back (see Krugman and Obstfeld, 2006). Consequently, a number of countries were experiencing a wave of defaults that affected the solvency of international banks.

was very important, but ultimate power rested in hands of the PMO, the DPMO and the Cabinet.[114]

Singapore's state apparatus disposed of high levels of independence in terms of technical expertise and information gathering. Singapore's bureaucracy had a professional ethos that was different from the prevailing ethos within society (Schein, 1996). It was governed by the principle of meritocracy, a practice of recruiting the brightest and most talented to political leadership and the civil service (Bellows, 2009). Singapore had a unitary government and an one-party dominant state (Lim and Pang, 1986). It had not been penetrated by private interest groups, which followed their sector specific goals (Ho, 2000). On the contrary, Singapore's government had significant influence on civil society, notably local community organisations and trade unions (P. Wilson, personal communication, 18 April 2014; Sheng, 2013; Lim and Pang, 1986). Soon after the PAP came into power – with a moderate labour coalition – it began to foster the creation of the semi-governmental National Trades Union Congress (NTUC) (Rodan, 1989).[115] The creation of the NTUC was a product of the governments effort to de-politicise Singapore's labour movement and to establish the de facto control over unions (Lim and Pang, 1986; Krause, 1988; Bloodsworth, 1986). As of the 1980s unions more than 90 per cent of the total union membership was affiliated with the NTUC (Lim and Pang, 1986, p. 21). Key positions of the National Trades Union Congress were filled with government representatives and PAP members. For example, in the late 1970s and the early 1980s Lim Chee Onn — Minister without portfolio — was the Secretary General of the National Trade Unions Congress (Rodan, 1989).

While the state structure was characterised by high levels of centralisation and autonomy, the system of interest representation of private business actors in Singapore's savings domain was weak.[116] There was little co-ordination among umbrella and subsector organisations. The Association of Banks in Singapore (ABS) was only formed in 1973, which included both private as well as state-owned banks, and had a coordinative role rather than an independent

[114] Singapore has had a kind of 'Westminster System' which adheres to the principle of collective responsibility. As such the Cabinet has been very important in policy-making. Cabinet Ministers are designated by the PM and appointed by the President. "The Cabinet works essentially as a committee, and a forum for discussion and a mechanism for making decisions" (Ho Khai Leong, 2000, p. 35). Singapore's constitution outlines that the "[C]abinet has the general direction and control of the government and is collectively responsible to Parliament" (Ho Khai Leong, 2000, p. 151). The PM heads the Cabinet. The Cabinet makes major policy initiatives and has been supported by the bureaucracy. Singapore's bureaucrats play a central and powerful role in Singapore's economy because they occupy key positions in statutory boards and on state related companies (Mauzy and Milne 2002, p. 29).

[115] Lim and Pang's statement that "[f]rom the 1950s through the early 1960's, Singapore was characterized by a politically active and radical, confrontationist labour movement with left-wing leadership" indicates the existence of an active labour movement before the mid 1960s (Lim and Pang, 1986, p. 20).

[116] For an overview of the organisation of Singapore's manufacturers in policy-making structures see Chapter 4.2.

lobbying function.[117] Particularly in the 1970s and in the 1980s, the ABS's organisational profile was not very well developed and membership was voluntarily. According to Hochstadt – former Deputy Director of the MAS – during the 1970s until the early 1980s the ABS had neither a directorate nor a secretariat (Hochstadt, 29 May 1981). It disposed of little capacity to bind members to agreements negotiated with the state. In an official address at the ABS annual dinner in the early 1980s, for example, Hochstadt highlighted the need to improve ABS's profile and research capacity (Hochstadt, 29 May 1981). He urged the ABS to sharpen its organisational profile in order to have a more powerful voice in policy-making (Hochstadt, 29 May 1981). Likewise, the private insurance sector was characterised by weak mobilisation with a number of associations speaking for the whole sector. Multiple voluntary domestic associations, such as the General Insurance Association of Singapore, the Life Insurance Association and the Life Underwriters Association, competed for members (IFPAS, 2014; GIA, 2014; LIA, 2014). Associations representing the private fund management sector emerged very late in the 1990s and 2000s. Interestingly, also Singapore's large commercial chambers, notably the Singapore Chinese Chamber of Commerce and Industry (SCCCI), stressed their right to represent associations and individual finance organisations, from banking, insurance and fund management sectors (SCCCI, 2014a).

6.3 POLICY-MAKING AND CHOICES – THE POLICY NETWORK IN OPERATION

From the late 1970s, Singapore's savings domain had been confronted with rising inflation pressures, and increasing international investment opportunities. Given Singapore's high levels of domestic savings, policy makers had to decide on the set up of financial institutions. They differed in terms of ownership, legal status, mandates and objectives. The debate concerned whether state or private financial institutions should lead the flow of domestic savings, and whether this flow should be channelled into the domestic system or into international assets. These choices implied re-distributional consequences, specifically for domestic and international finance actors. For example, the creation of an SWF with a savings and international investment mandate was considered intrusive by domestic private financial actors, because savings would be channelled out of the system by the state and channeled into international assets.

Between the late-1970s and early-1980s, return considerations became louder, and policy makers came under pressure to maximise return on Singapore's large savings. According to Orchard – former director of Economics and Strategy at the GIC – inflation pressures together

[117] The ABS was the successor of the Association of Banks in Singapore and Malaysia (ABS, 2014).

with currency volatility put severe pressure on Singapore's existing financial institutions, notably the MAS (F. Orchard, personal communication, 09 April 2014). As of the late 1970s Singapore's large savings were managed conservatively via the MAS, primarily in highly liquid assets such as conventional foreign reserves (e.g. cash deposits of other currencies). Due to high inflation and currency volatility Singapore's savings suffered losses during the 1970s (*The Straits Times*, 5 October 2007).[118] Orchard's statement that "if you are in the wrong currency your reserves fall" highlights the volatility and risks of international finance in the late 1970s and early 1980s (Orchard, 2014). However, over the same period international markets and international asset classes became highly lucrative, notably public and private equities as well as real estate (*The Straits Times*, 6 October 2007).

The creation of the GIC in 1981 rose out of a 'review' on how Singapore should reorganise its financial institutions in the savings domain. This review took place in a highly turbulent international financial environment. Different proposals were made with regard to the kinds of financial institutions. They were also supported by different socio-economic actors. The question was whether to continue with existing financial institutions, or whether to create an SWF with savings and international investment mandates. The review was influenced by Singapore's state-directed PN. A high concentration in decision-making power, and high levels of state autonomy facilitated the pursuit of long-term transformative policies that were highly coordinated in Singapore's savings domain. The PN characteristics allowed for the exclusion of actors, following their own short-term sector specific preferences, from the policy-making processes.

Overall, the creation of the GIC offers evidence on the limited impact of diffusion. A supporter of a diffusion argument would argue that countries create an SWF with a savings mandate when countries in its peer group have created a similar SWF, and faced similar problems concerning wealth accumulation and long-term investment. However, at the time of GIC's creation, none of Singapore's peers had established an SWF with a savings mandate. This is particularly emphasised by GIC's former Managing Director J.Y. Pillay, indeed, "[t]he formation of GIC was actually quite a novel idea, groundbreaking because no other government that we knew of had set up such a specific agency to manage the surplus assets on a diversified portfolio basis", which suggests that Singapore did not follow any other country in the decision to create an SWF (J.Y. Pillay *quoted* by MAS Commemoration 2011, p. 95). In terms of small open economies without hydrocarbon resources, Singapore was the first small open economy to create such an

[118] MAS' large levels of reserves that were reportedly not adequately managed provoked a debate in 1980/81. A newspaper's statement that "[t]here were rumours that millions were lost on currency transactions especially with the recent dive of the deutschmark" draws attention to the critique made vis-à-vis the MAS as a reserve manager (*The Straits Times*, 13 March 1981, p. 8). The MAS was allegedly also not very successful in its earlier real estate investments (*The Business Times*, 28 February 1981, p. 6; MAS, 2011).

SWF. As of the early 1980s, only countries that were not in Singapore's peer group had created SWFs with savings mandates. Although small economies of the Middle East had already established SWFs with savings mandates, they did not count as peers, because of their very different export profile structure. Singapore's policy makers were looking at examples of the Middle East, but they explicitly pursued a different model (Ng, 2014). This is also highlighted by Orchard, a former high level GIC executive. According to Orchard the idea of creating a separate institution for managing surpluses was quite 'revolutionary', because at that time, the only examples of saving SWFs were countries of the Middle East such as Kuwait and Abu Dhabi (Orchard, 2014). These countries' SWFs at that time depended heavily on external management and used external fund managers to account for most of their money. In stark contrast, Singapore's policy makers were determined to make Singapore's GIC different from existing examples in the Middle East; Singapore started from the earliest beginnings to develop in-house investment capacity (Orchard, 2014).

The creation of the GIC provides evidence on the impact of efficiency. Given significant amounts of savings and limited domestic investment opportunities, a supporter of an efficiency argument would have predicted the creation of an SWF with a savings mandate in Singapore. Unlike other governments, Singapore enjoyed structural surpluses, and as such it did not need to issue government securities for fiscal purposes. By the early 1980s, Singapore's government continued with the issuance of large amounts of SGS, specifically for the CPF and the POSB. By law, the CPF Board has been required to invest in securities issued and guaranteed by the Singapore government. As a result, the CPF, in the 1980s, used more than 89 per cent of its assets to acquire SGS (Lee, 1984, p. 259). This made the CPF into the major holder of SGS (Lee, 1987). Between 1975 and 1980 the CPF was holding more than 70 per cent of all government bonds issued in Singapore (Lee, 1984, p. 259). Given Singapore's domestic investment constraints in the 1970s and 1980s, one way of allocating high levels of domestic savings without the creation of bubbles and without fuelling inflation was to set up an SWF channelling savings abroad into long-term financial assets. Given its small domestic markets and its large savings levels in an international environment of high return opportunities, the creation of the GIC was highly rational from a macro-national perspective.

THE PARTICIPANTS AND THEIR PREFERENCES

Preferences regarding SWFs and linked state finance institutions in Singapore's savings domain differed among socio-economic actors. From 1976 onwards, parts of the state apparatus expressed concerns on the return of Singapore's large surpluses and savings. For instance, Singapore's Public Accounts Committee drew attention to the need to take action regarding

Singapore’s large-surpluses, by investing in bonds, equities, and real estate in its 1976 report for the first time. Former Deputy Speaker and chairman of the Public Accounts Committee of the Parliament of Singapore – highlighted the need for reserve diversification. His statement that “[o]ur problem is that, [...] statutory boards can place their surplus funds in local investments or with the Government; but the Government has got to do something about its foreign assets. It just cannot bring them back here. It could invest them in bonds, equities, property and other forms as well” indicates the awareness among government officials of the need to channel Singapore’s savings into international assets (Second Report of the Public Accounts Committee presented to Parliament on 17th June, 1976, p15/B8, retrieved from Singapore Hansard [Homepage]).

Especially in the context of high inflation during the 1970s, Singapore’s government officials became increasingly concerned about the maintenance of the purchasing power of Singapore’s savings over the long term. Following the 1973 oil crisis, inflation in Singapore jumped in the first quarter of 1974 to nearly 30 per cent, and in 1980 it reached 8.5 per cent (MAS Economic Explorer, 2014). Also, Singapore’s labour sector increasingly demanded higher returns on CPF savings. For example, Encik Othman bin Haron Eusofe – at the time, the Deputy Director of the National Trade Union Congress Research Unit, and later the Minister of State of Labour – highlighted that the “the contributors to the [CPF] have been expressing their concern that their CPF savings will be eroded in time due to inflation” (Singapore Hansard, 18 February 1981, Debate on President’s Address).[119] As a consequence, a fundamental reinvestigation of the CPF Board investment strategy was proposed in order to achieve higher returns – of more than eight per cent – on behalf of the contributors (Singapore Hansard, 18 February 1981, Debate on President’s Address).

From the late-1970s, Singapore’s key government departments in the savings domain, notably the PMO and the DPMO as well as the Ministry of Finance, were engaged with the issue of finding an institutional way to enhance the returns on Singapore’s savings. However, some tensions emerged among government departments. In the late 1970s there were different views on this topic, notably between the Ministry of Finance and the PMO, together with the DPMO. These tensions referred to the question of whether to create a new financial institution (i.e. SWF) for the management of Singapore’s savings or whether to continue with the existing mode via the MAS. Until 1980, the Minister of Finance was chairman of the MAS; as such, the Ministry of Finance supported the continuation of the existing institutional arrangement at that time. According to Yeoh Lam Keong – former chief economist of the GIC – the Ministry of Finance was mainly concerned with responsibility and feasibility issues of creating a new and separate financial institution (L.K. Yeoh, personal communication, 27 February 2014).

[119] Minister of State in Singapore is equivalent to the rank of a Junior Minister in other countries.

Feasibility issues at that time related to the question of stability of the flow of surpluses that can then be channelled into an SWF. Responsibility issues were related to the risks associated with non-conventional asset classes, and a long-term investment horizon. According to Yeoh Lam Keong, the Ministry of Finance may also have been uncomfortable with the attribution of responsibility in the case of losses (Yeoh, 2014).

The Deputy Prime Minister (DPM) – supported by the Prime Minister (PM) – called for a fundamental review of Singapore's existing financial institutions in the savings domain.[120] Both were highly supportive of creating an SWF with a savings mandate leading the flow of savings abroad. They were willing to take responsibility because they thought it was a 'worthwhile endeavour' (Yeoh, 2014). They highlighted that Singapore was going to have surpluses for many years, because it operated on the principle of budget surpluses and the mobilisation of private savings via state savings vehicles (e.g. the CPF). According to Orchard – a former GIC director – the DPM highlighted that, as of the early 1980s, Singapore was still a young country in demographic terms, where savings would be high in the future (Orchard, 2014). As such, the DPM and PM believed that Singapore would have surpluses from private and public savings in the long-term (Orchard, 2014). If these were going to be accumulated over the long-term then the question arose as to whether to continue to manage them on a safe short-term liquid basis, or on a more long-term risk basis via an SWF.

Singapore's domestic private finance organisations and international finance organisations also had different preferences regarding the creation of an SWF with a savings mandate. While international finance actors supported the creation of an SWF that would channel domestic savings for long-term investments into international assets, domestic private finance actors were critical of that endeavour. International finance actors had clear incentives for co-operation, joint ventures and partnerships that focused on the management and allocation of funds into international capital channels. They could benefit from the consultations in multiple ways (e.g. placement of funds under external management, consultation fees). By contrast, private domestic finance actors did not support the creation of an SWF. The creation of an SWF with a savings and an international investment mandate means that the state drains out savings from the system. According to an independent observer, because of the international investment mandate, the creation of the GIC did not help the development of the local fund management and savings industry (Anonymous, personal communication, 19 February 2014). Private domestic finance actors emphasised that high levels of state involvement replaced private domestic finance actors in the allocation and mobilisation of domestic savings (*The Straits*

[120] These considerations took place in a context of rumours that the MAS lost mns in currency transactions caused by a dive in the Deutschmark (*The Straits Times*, 13 March 1981). DPM Goh Keng Swee was reportedly not happy with how reserves were managed in Singapore (*The Straits Times,* 13 March 1981).

Times, 18 February 1979; Pillay, 2006). This was specifically highlighted by Lee (1984) an academic and banking expert. Lee's observation that "[c]ommercial banks, finance companies, merchant banks, and other financial institutions generally have the view that capital funds are excessively mobilised by the public sector […], leaving little funds available for the private sector" suggests that segments of Singapore's private financial sector did not benefit from the creation of the GIC (Lee, 1984, p. 298). For example, the Vice President of the Overseas Union Bank (OUB) – one of Singapore's large private commercial banks – highlighted that the kind of financial institutions set up in Singapore's savings domain hampered the development of the domestic private fund management sector, since much of the investible surpluses had been soaked up by the state and managed by the government itself (*The Straits Times*, 10 November 1989, p. 13).

Singapore's domestic commercial banks' criticism was very subtle; they indicated that they wanted to manage more money, and, like banks in other countries, provide comprehensive provident fund schemes, insurance schemes and savings plans (Orchard, 2014; *The Straits Times*, 18 February 1979; *The Straits Times*, 13 April 1985). As a result, they demanded that the government should release part of these funds to the domestic private sector for management (*The Straits Times*, 10 November 1989, p. 13). The *Asian Finance* magazine stated at the time that the domestic private finance sector "would like to see [Singapore's government] free a larger chunk of its funds for non-traditional investments" (*Asian Finance*, 15 February 1984, p. 21). Similarly, Singapore's private domestic insurance sector demanded less state involvement, and highlighted that more capital needed to be channelled through private domestic finance institutions.

Public discussions suggest competition between private and state finance institutions and reveal the opposition of domestic bankers to Singapore's state saving scheme. For example, by 1964, about 31 private provident funds had been set up, and by 1977 this number had increased to only about 100, most of which were weakly funded (Lee, 1974, p. 203; *The Business Times*, 23 June 1979, p. 9). By contrast, in Hong Kong the number of approved private provident fund schemes climbed from 540 in 1970 to 4,105 in 1986 (Li, 1988, p. 71, taken from *Hong Kong Economic Journal,* 27 August 1988).

While state officials in Singapore, notably the minister of finance, pointed out on numerous occasions their preference for having CPF funds channelled through the Ministry of Finance or the MAS, domestic bankers demanded the development of a private fund-management sector (*The Business Times*, 21 July 1980, p. 12). The Association of Banks of Singapore demanded the creation of more private provident fund schemes and proposed that a proportion of the CPF money should be managed by the private sector (*The Business Times*, 23 June 1979, p. 9).

Singapore's bankers argued that "concentrating investible funds into the hands of the CPF would not, in the long term, encourage the growth of the local capital market" (*The Business Times*, 23 June 1979, p. 9). It was feared that the CPF's dominance in Singapore would instead drive a decrease in the number of private provident funds (*The Business Times*, 23 June 1979, p. 9). Consequently, bankers suggested following Japan's model, by which the government operates a pension fund and allocates a substantial part of it to domestic banks, life insurance companies, and trust companies (*The Business Times*, 23 June 1979, p. 9).

Representatives from the Life Insurance Association of Singapore complained repeatedly about competition with the CPF and about insurance schemes introduced by state enterprises (*The Business Times*, 24 February 1978; *The Business Times*, 21 October 1981; *The Business Times,* 8 April 1980; *The Straits Times,* 24 March 1980). For example, the President of the Life Insurance Association of Singapore emphasised severe competition in the insurance market with the CPF due to high mandatory contribution rates, and with the POSB because of its five per cent tax-free interest rates and its housing loans at competitive rates (*The Business Times*, 24 February 1978, p.xiv). The Life Insurance Association of Singapore highlighted that the state "should not compete unfairly with the industry" (*The Straits Times*, 24 May 1980). The Life Insurance Association's President's statement that this introduces "less incentive on the part of working population to save by way of life insurance" suggests high levels of competition between the private and state sector (*The Business Times*, 24 February 1978, p.xiv). Furthermore, private insurance companies had difficulties to make investments in alternative sectors, because the Singapore Insurance Act stipulated an investment ratio of between 20 – 25 per cent in SGS and between 50 – 55 per cent in equities of companies that were incorporated in Singapore, mortgage loans, properties and cash with banks in Singapore (*The Business Times*, 24 February 1978, p.xiv). The life insurance sector highlighted that the government is in a formidable position, because the CPF alone had 1.2 mn members (*The Straits Times*, 24 March 1980, p.16). For example, a proposed Singapore Airlines life insurance scheme had worried the Life Insurance Association of Singapore. Singapore Airlines – owned by Temasek at that time – considered entering the life insurance business in Singapore (*The Business Times*, 21 October 1981, p.1; *The Business Times*, 8 April 1980).

The Policy Network and Singapore's state finance institutions

A review in 1968 of Singapore's future as a financial centre influenced the creation of the Monetary Authority of Singapore (MAS), which played a critical role in the accumulation of sovereign wealth. The Ministry of Finance, together with the DBS and international actors, notably the IMF and the Bank of America, were dominant in influencing both this review and the Monetary Authority of Singapore Act in 1970 (Orchard, 2014a). This act transferred Singapore's reserves that had previously been managed by the Ministry of Finance to the newly created MAS, the principal objective of the MAS being "to act as banker to, and financial agent of, the Government" (Effros 1982, p. 949). Albert Winsemius, Singapore's chief economic advisor, played a critical role in triggering this process. Publicly available data suggests that no representatives from private business or domestic banking organisations were included in this review (*Bulletin*, International Bureau of Fiscal Documentation, 1985, p. 156; Hamilton Hart, 2002; MAS, 2011). This observation is confirmed by a former high-level GIC official who points out that no domestic organisation was involved in the process that led to the creation of the MAS (Orchard, 2014).

At Winsemius' request, a representative of the Bank of America prepared a plan for Singapore's future financial development (Winsemius, 1982f, 1982g).[121] This plan was sent directly to the Minister of Finance (Winsemius, 1982g, pp. 148–149). The international financial press noted that this plan was highly influential (*Institutional Investor*, April 1981). One of the major conclusions of the plan was that Singapore should take advantage of its geographical location by developing into an offshore financial centre (i.e. as an Asia dollar market) and into a major foreign-exchange trading centre. It was suggested that an agency be created to promote Singapore as an international financial centre (*Institutional Investor*, April 1981, pp. 133–144). Singapore's Finance Minister was highly supportive of the recommendations to create a monetary authority and approached the IMF for advice on the setting up of such an entity (Winsemius, 1982g, pp. 148–149). The IMF in turn submitted a draft memo on the role, objectives, and organisation of the proposed institution.[122]

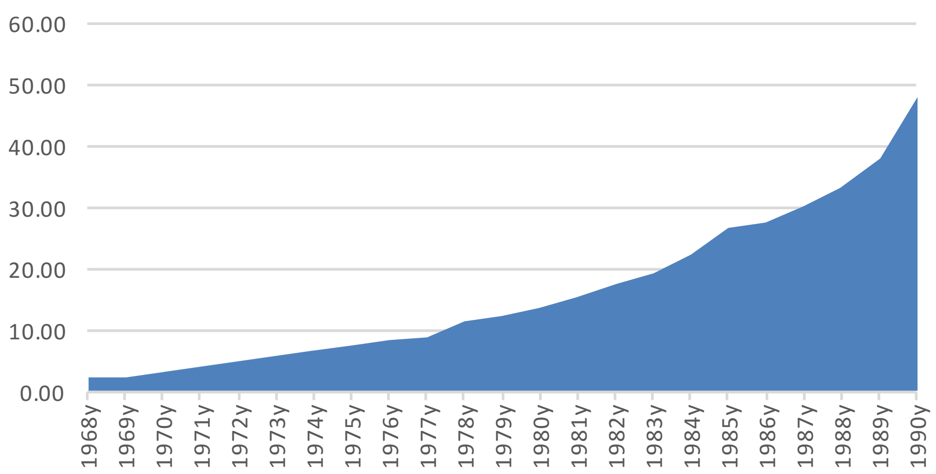
From its creation onwards, the central policy body for asset and reserve management for the MAS has been the Asset Management Committee. It gave the directions in terms of how the MAS should invest Singapore's foreign reserves (Orchard, 2014; MAS, 2011). The appointments to this committee were highly selective (Hamilton Hart, 2002). It was chaired by the minister of finance, and its members included the permanent secretary for the revenue division from the Ministry of Finance and the permanent secretary of the development division from the Ministry of Finance, the accountant general, and the managing director of the MAS (*Bulletin*, International Bureau of Fiscal Documentation, April 1985). The appointment structure was reflected in the conservative investment approach of the MAS. At that time, the MAS was primarily engaged in foreign exchange transactions, both in S$ and other currencies,

[121] Although Winsemius calls it 'plan', he means 'strategic guidelines for the future'. They are reexamined every year (Winsemius, Reel 12, 154).

[122] An IMF economist's statement that "[i]t became evident that the centralization of [different government departments] within a single organization was urgently needed to enhance the effectiveness of monetary management and to ensure a coordinated approach to financial policy and development" indicates the strong external support for the reorganisation (Ishihara and Kim, 1982, p. 916).

which were conducted in major foreign exchange centers like London, New York, and Tokyo (Orchard, 2014).

FIGURE 6.1. Reserves in billion Sing$ between 1968 and 1990.



Sources: Yearbook Singapore (1981, p.235; 1987, p.289; 1991, p.282)

The MAS' Asset Management Committee made decisions over the allocation of Singapore's increasing reserves. The International Bureau of Fiscal Documentation, as well as secondary literature, notably Hamilton-Hart (2002), suggests that no members from the private domestic banking sector be appointed to the Asset Management Committee (*Bulletin*, International Bureau of Fiscal Documentation, April 1985). However, Singapore's domestic banks were particularly keen to manage a part of the MAS' large reserves (*The Straits Times*, 9 January 1986, p. 12; Orchard, 2014). Between 1980 and 1984 Singapore's reserves increased from approximately S$13 bn to S$20 bn. But instead of sourcing reserve management out to private domestic banks, the MAS started to compete with domestic banks directly in the market for government deposits from government or government-related companies.[123] The 1984 MAS Amendment Bill allowed the MAS to pay interest on deposits from companies in which the government holds at least a 20 per cent ownership stake. A commentator's statement that this "raises the possibility of a siphoning of government funds from the private sector to the MAS" suggests increasing competition for government funds between the MAS and domestic commercial banks (*Business Times*, 2 August 1984). With the MAS starting to pay interest on

[123] Interestingly, at the end of May 1984 an estimated S$4.8 bn funds were allegedly placed by government enterprises and statutory boards with domestic commercial banks (*Business Times*, 2 August 1984).

deposits, it was expected that private domestic banks would begin losing business in the government deposit market. However, the extent to which Singapore's domestic banks were disadvantaged by the management of assets and government reserves of the MAS remains unknown.

The Policy Network and Creation of the GIC

The decision to create an SWF with a savings and international investment mandate grew out of a review in 1980/81, and concerned the reorganisation of Singapore's reserve management. The execution of the review was delegated by the PMO to the DPMO. This was done through the appointment of the DPM as Chairman of MAS (Singapore Government Press Releases, 1980). Through this appointment the Finance Minister – who was traditionally the chairman of MAS – was pushed to one side in order to allow the DPM to review Singapore's reserve management (Orchard, 2014). An official statement that "[t]he Prime Minister has charged Dr Goh Keng Swee with the responsibility of the Minister of Finance insofar as it relates to the function of the Minister under the provision of the MAS Act and the Currency Act" supports Orchard's observation (Singapore Government Press Releases, 1980). Interestingly, apart from very few humorous comments in the parliament, there is no evidence of an internal struggle between the Minster of Finance and the PMO (Singapore Hansard, 18 March 1981; Orchard, 2014). Brief internal tensions and conflicts about the review of Singapore's reserve management were quickly resolved because of the high concentration of power within the structure of state-society relations. Likewise, policy insiders, notably former MAS analyst Ng Kok Song – who later became GIC's Chief Investment Officer – highlighted that due to the high authority in the hands of PM Lee Kuan Yew and DPM Goh Keng Swee there was no internal struggle about this decision (Ng, 2014). Although the Ministry of Finance had the de jure power over savings policy, the ultimate decision-making power in the savings domain was in the hands of the PM. Together, the PM and DPM saw a need for a fundamental reconsiderations about Singapore's reserve management (*The Straits Times*, 6 October 2007).[124] The relationship between the PM and DPM at that time was very close and firm, even putting aside other Ministries' responsibilities in the Cabinet (Orchard, 2014). Hence, if the PN network had been different in terms of power concentration, this might have resulted in competition for asset management

[124] PM Lee Kuan Yew was paraphrased by the *Straits Times* on the 6 October 2007: "In the 1960s and 1970s [b]ecause of inflation, a share could be bought, and it could drop in value, and the dividends of 5 per cent, 5.5 per cent were not equal to the inflation that was taking place. So we were losing money. And that was when Dr Goh Keng Swee came to see me and said, 'We can't leave this just alone to the Minister of Finance. He's got so many other duties. We need a body that would just study asset transfers, different assets, stocks, bonds, properties, equities, commodities, steel, corn, whatever, and preserve our core value', because at that time inflation was raging 7, 8, 9, 10 per cent. […] That was when GIC was formed in 1981 and we had lost millions of dollars" (*The Straits Times*, 6 October 2007).

among different state departments (i.e. Ministry of Finance and PMO and DPMO). This in turn may have hampered the smooth creation of the GIC in 1981.

EXCLUSION OF DOMESTIC FINANCE

The mechanism whereby Singapore's state-directed PN operated to influence the kinds of financial institutions set up in the savings domain referred to exclusion. Due to the high level of power concentration and autonomy, Singapore's policy makers could bypass domestic finance actors. Reportedly no formal or informal consultation took place with private domestic finance organisations on the review (*The Business Times*, 10 March 1981; *Asian Wall Street Journal*, 11 March 1981; Singapore Government Press Release, 1980). According to J.Y. Pillay – former Managing Director of the MAS and the GIC – at that time private domestic finance organisations were not part of policy-making in the savings domain, and thus not involved in the creation of the GIC (J.Y. Pillay, personal communication, 26 March 2014). Thereby, the PN prevented domestic private banking as well as domestic private insurance actors, and later domestic fund management actors, from realising their sector-specific preferences (i.e. managing a larger part of Singapore's private and public wealth). In turn, this allowed for the pursuit of long-term transformative policies in Singapore's savings domain and enabled high levels of co-ordination with other policy domains, notably monetary.

The exclusion of domestic private finance organisations in the 1980s was justified partly on grounds of expertise. Former GIC Director Freddy Orchard and former GIC Chief Investment Officer Ng Kok Song, explain the exclusion of domestic private finance actors through the argument of 'their lack of expertise' (Orchard, 2014; Ng Kok Song, 2014; *Asian Banking*, December 1985). According to Ng Kok Song, at the time of GIC's creation Singapore's private domestic actors in the savings domain had no fund management expertise (Ng Kok Song, 2014). Consequently, the DPMO started to look for international finance actors in order to support the development of GIC's own investment capacity (*The Financial Times*, 20 July 1981).[125] International finance actors had a strong expertise in the field of international fund management, and they were keen to participate in the review of Singapore's reserve management (*Asian Wall Street Journal*, 11 March 1981). However, from the late 1970s, Singapore's domestic finance sector has started to acquire international banking skills and had begun to build expertise in modern fund management. By the early 1980s, Singapore's private banks had begun to recruit a number of experienced executives with international exposure, and

[125] For example, a former executive partner in Salomon Brothers (i.e. James D. Wolfensohn), a former real estate specialist at Prudential Insurance (i.e. Theodore M. Garhart), and a former stock specialist form College Retirement Equities Fund (i.e. Douglas C. Salmond) were recruited to train 17 Singaporeans at the GIC (*The Straits Times*, 15 March 1983).

key actors of Singapore's state-directed PN were aware of this (Lee, 1981). For example, the DPM stipulated the secondment of senior representatives of the domestic private banking sector in order to provide a 'back-up' for the GIC (*The Straits Times*, 10 March 1981, pp. 1–32). For example, the Overseas China Banking Corporation's (OCBC) Vice Chairman had to be seconded to the GIC (*The Business Times,* 10 March 1981, p. 1). Not surprisingly, these secondments were not welcomed by Singapore's domestic private finance organisations (*The Business Times*, 7 August 1982), Singapore's large private domestic banks felt that they were deprived of their best people and had to compete with state finance institutions for talent.

Although large Singapore private banks, such as the OCBC, the OUB and the United Overseas Bank (UOB) had been individually powerful economic actors, they remained very silent during the policy processes leading to the creation of the GIC.[126] None of Singapore's banks were involved in the policy and consultation processes leading to the creation of the GIC (R. Katz, personal communication, 31 April 2014). Orchard's statement that "[t]he banks leave it just to the government" draws attention to the passivity of private finance actors in the policy-making (Orchard, 2014). Although such private finance actors' passivity might have been due to their agreement with the kind of finance institutions set up, occasional public comments indicate that domestic private finance actors, notably the OUB, were critical of the kinds of finance institutions set up in Singapore's savings domain (*The Straits Times*, 10 November 1989). Private domestic finance actors wanted to see the development of private institutions in the savings domain, but the structure of state-society relations did not allow them to translate these preferences into policies (*The Straits Times*, 10 November 1989, p. 13). Singapore's commercial banks were interested in managing part of Singapore's large reserves. For example, *The Straits Times'* headline that "Singapore bankers want a slice of the MAS pie" draws attention to the banks' efforts in gaining higher exposure to the management of Singapore's reserves (*The Straits Times*, 9 January 1986, p. 12). According to Orchard, they lobbied both the MAS and the GIC for such business (Orchard, 2014).

INCLUSION OF INTERNATIONAL FINANCE

The characteristics of Singapore's PN allowed policy makers to freely choose financial consultants. The PM entrusted the DPM with the responsibility of investigating and identifying adequate international finance actors regarding advice on the creation of an SWF (Ng Kok Song, 2014). The question that was posed to international finance actors was how Singapore should reorganise its reserve management function (Ng Kok Song, 2014). Therefore, the DPM visited a number of international banks, including banks in the US, Switzerland (e.g. UBS), and the UK (i.e. Rothschild & Sons) (Orchard, 2014; Moser, 2008). According to former Rothschild

[126] Because of the oligopolistic position of large banks, it is often assumed that representatives of these firms have direct contact with policy-makers, and as such the ability to influence policy in a critical way (Coen, 1997).

& Sons Vice Chairman, Lord Claus Moser, following these visits Singapore's DPMO compiled a shortlist of four banks, of which Rothschild & Sons was included (Moser, 2008).[127] The final selection was made on a highly competitive basis, and it was overseen by key actors of Singapore's PN, notably the DPMO, the Cabinet and the PMO. During the final selection process, Rothschild produced a series of reports and had a number of interviews and meetings with the Cabinet, the DPM and the PM. Lord Moser's statement "that [this] was a very tough task [and] it was very tough competition" where Rothschild had to present and to justify its selection to all central organisations of Singapore's PN (Moser, 2008). According to Lord Moser (2008) the meetings were not characterised by 'friendship', and personal relationships did not matter in the selection process. Following the Cabinet's acceptance of Rothschild, PM Lee Kuan Yew had to give the final assent. Lord Moser's testimony that this was "certainly the most frightening hour in my life" suggests that the selection process was tough for Rothschild & Sons and was followed by formal procedures (Moser, 2008). Finally, Rothschild & Sons got an initial appointment offer for six months, which would be only renewed on the condition of them 'doing a good job' (Moser, 2008).

Rothschild & Sons was appointed as Singapore's official consultant on the 'review' that led to the creation of the GIC in 1981. According to Lord Moser the main task of Rothschild was concerned with "advising on what to do with [Singapore's] funds internationally" (Moser, 2008). Rothschild's team in Singapore was led by the Director of Rothschild's Government Advisory Division, Richard Katz, who was responsible for the international management of reserves of central banks (*The Business Times*, 10 March 1981, p. 1; Katz, 2014). Initially, Rothschild's small team in Singapore was supported by a big backup team in London (Moser, 2008). Consultations took place between Rothschild's Claus Moser, Richard Katz and Kate Mortimer and key representatives from the DPMO, notably DPM Goh Keng Swee (*The Straits Times*, 9 April 1981, p. 12). The Singapore leadership demanded the creation of an SWF with an international investment mandate, and Rothschild suggested a concrete form of institution (Katz, 2014). Rothschild formulated GIC's memorandum, which outlined the investment mandate and investment classes.[128] From the beginning, GIC's investment spectrum comprised shares, stocks, debentures, debenture stock, scrip, loans, bonds, obligations, notes, securities and

[127] For Lord Claus Moser the short-listing of Rothschild & Sons was the direct result of the personal relationship between him and Singapore's DPM Goh (Moser, 2008). Lord Moser noted in an interview: "Dr Goh had been my student as an undergraduate at LSE and he had done his PhD under me. He considered me as his great man. And he got in touch with Rothschilds formally because of me. So we got a tender to get shortlisted with the other banks" (Moser, 2008).

[128] Preceding the creation of the GIC, Rothschild & Sons had already been actively involved in the creation of the Venezuelan Investment Fund (Katz, 2014). Katz's statement that "this was what we suggested to Dr Goh and followed up with a full presentation and memorandum" highlights the important influence of Rothschild (Katz, 2014). Although this looks like diffusion, the thesis can exclude emulation as a potential explanation for the creation of the GIC, because Venezuela's structural characteristics differed significantly from that of Singapore. As such Venezuela cannot be considered as a peer of Singapore.

investments by original subscription, tender purchase, and participation in syndicates in any part of the world (Memorandum GIC, 1981). Furthermore, the GIC was allowed to invest in gold, silver, commodities, buy and sell currencies, property and land and enter arrangements with other government authorities (Memorandum GIC, 1981).

DISCUSSIONS ON THE CREATION OF THE GIC IN THE 1980s

In Singapore's savings domain, the structure of state-society relations was reflected in the discussions about the kinds of finance institutions set up. Between the 1970s and 1980s, as Singapore's large savings became increasingly exposed to external pressures, discussions began about the kinds of financial institutions in Singapore's savings domain. Criticism at that time was subtle. A number of private commercial banks in Singapore raised anonymous complaints, and the ABS had not been present or active in any of the policy debates. The political conditions at that time made it difficult to be explicitly critical vis-à-vis Singapore's government policy. Singapore has been frequently described as an illiberal democracy or a non-liberal communitarian democracy with judicial actions applied to government criticism (see Mauzy and Milne, 2002).[129] There were official responses to newspapers that criticised government policy during the 1970s and 1980s.[130] As such, debates about the kinds of financial institutions were only carried out in public to a very limited extent. Nevertheless, from subtle comments and recommendations it can be seen that domestic private finance actors, such as banking, insurance and fund management associations, were against the kinds of financial institutions set up in Singapore's savings domain. Although the debates were informal and generally not public, interviews and occasional public comments (e.g. *The Straits Times*, 13 April 1985), as well as secondary literature (e.g. Lee, 1984), suggest that the creation of the GIC was unpopular with domestic private finance, notably banks and fund managers.

In discussions, the stance of private finance actors was critical vis-à-vis the creation of the GIC. Initially domestic finance actors argued of the 'crowding out' of talent. Supported by the international press, notably *The Economist*, occasional complaints were publicised stating that the Singapore government 'raids the private sector for bankers' (*The Straits Times*, 1 August 1982). *The Economist*'s statement that "[t]he cleverest managers and workers are hired by state-

[129] The Internal Security Act had been instituted by British rule and was kept by the PAP. Originally it was used against suspected communists. The Criminal Law Temporary Provisions Act allowed the arrest without warrant and detention without trial. The Societies Act (1967 amended in 1988) demanded that organisations of more than 10 people needed to be registered. The Law of Defamation has constrained the right of free speech (Mauzy and Milne, 2002). The judicial system in Singapore has been regularly criticised for lack in independence, specifically in political sensitive areas.

[130] For example in the 1970s, the government detained the chief editor and chief editor-writer of the Nanyang Siang Pau, a Chinese daily newspaper in Singapore, which were criticising the government's policy towards Chinese language and education (Kim, 1985).

controlled companies which dominate parts of the economy" draws attention to the competition for talent between state and private sector (*The Economist*, 3 September 1983, p. 68). This was particularly the case when a number of high profile bankers were seconded to the GIC in the early years (*The Straits Times*, 1 August 1982). These secondments were initiated by the DPMO and were not welcomed by Singapore's domestic private banks and international commentators (*The Business Times*, 7 August 1982; *Asian Finance*, 15 September 1982). An observer at that time noted that it was very difficult to refuse an offer to serve in the government in Singapore (*Euromoney*, June 1981, pp. 17–31). This suggests that secondments of private senior bankers to executive positions in the GIC were not necessarily on a purely voluntary basis. A number of newspaper commentaries indicated that these appointments were largely not welcomed by the private sector (see *The Straits Times,* 13 March 1981; 1 August 1982; 10 March 1981; *The Business Times*, 7 August 1982). Reportedly, Singapore's banks feared that the government was taking some of their most experienced bankers away (*The Business Times*, 7 August 1982). The DPM's public pledge that the MAS had no plans "to raid the private sector for bankers" draws attention to the existence of tensions between the government and private sector regarding retrenchment (*The Straits Times*, 1 August 1982, p. 1). However, the extent to which GIC's recruitment of talent interfered with the private domestic banking sector's recruitment remains unknown.

Domestic finance actors emphasised the competition with state savings vehicles, which channel money out of Singapore. Funds were first channeled to the government, which then translated it into foreign assets. Even Singapore's Finance Minister admitted that government policies of the 1980s were 'highly unpopular' with the financial sector (see Hamilton-Hart, 2003, p. 98). According to Yeoh Lam Keong – a former Chief Economist of the GIC – there were quite a few critiques from the domestic private finance sector, because a substantial amount of fund flows ended up being managed by the GIC (Yeoh, 2014). Yeoh (2014) highlights that a number of private finance actors in Singapore believed that the GIC monopoly was restricting the development of the local fund management industry. Yeoh (2014) admits that "there is some truth in there" but at the same time he suggests that the extent to which the GIC crowded out domestic fund management remains unknown. Private finance organisations from the insurance and banking sector have repeatedly highlighted that they wanted to manage domestic surpluses and savings in order to 'boost' the local fund management sector or a private-run pension sector (*The Straits Times*, 10 November 1989, p. 13; *The Straits Times*, 18 February 1979; *The Straits Times,* 13 April 1985).

The Creation of the GIC in 1981 and its initial Years

High levels of power concentration in decision-making structures combined with high levels of autonomy allowed for the smooth carving out of a significant portion of assets – previously managed by the MAS – and the creation of the GIC. According to former GIC Executive, Orchard (2014), this was done in a quite 'authoritarian' way and accepted by all government departments without resistance. This involved the redundancy of former MAS employees. Although there were some critical comments from international media about MAS' restructuring – about 10 per cent of existing MAS staff had been made redundant – there was no struggle regarding the creation of the GIC. This is also confirmed by Ng Kok Song (2014) – at that time an analyst with MAS. According to Ng Kok Song there was no conflict within the MAS International Department about the restructuring and outsourcing of assets from the MAS to the GIC (Ng Kok Song, 2014).

The GIC's corporate structure evolved under the influence of Singapore's state-directed PN, which included a small circle of politicians, high level bureaucrats and international finance actors. From the very beginning onwards the DPM has selected international experts to lead GIC's different departments. For example, a former executive of the US based College Retirement Equity Fund joined GIC in 1981 to head its Pacific & European Equities Department (MAS-GIC Link, 1984; The *Business Times*, 13 November 1981). A regional vice president of real estate at Prudential Insurance Company joined in 1982 to head GIC's Real Estate Department (MAS-GIC Link, 1984). A former partner of investment management firm Hagler Mastrovita & Hewitt joined in 1983 to lead the GIC's US Equities Department (MAS-GIC Link, 1984). Members of GIC's board held simultaneous key positions in government companies and ministries. Former board members of the GIC had been drawn from Singapore's bureaucratic elite and small circle of policy makers. They included permanent secretaries and high-level civil servants (e.g. S. Dhanabalan, J.Y. Pillay, Tan Teck Chwee) and Cabinet Ministers (e.g. Goh Keng Swee, Hon Sui Sen, Lim Kim San, Goh Chok Tong) (Lee Kuan Yew, 2006, p. 2). Since the GIC's establishment in 1981, the position of the Chairman had always been occupied by the PM (Lee Kuan Yew and later Lee Hsien Loong). As such, the governance structure of GIC reflected Singapore's state-directed PN. This again facilitated policy coordination with monetary and fiscal policy and it allowed for the adaptation of a long-term horizon in Singapore's savings domain.

The GIC allocates capital into international assets. Owned by the government, the GIC was created under the Singapore Companies Act (Chapter 50) as a private exempt company. This legal status protects the GIC from revealing any loss-making investment to the public and it frees the GIC from filing audits with the public registry (see Section 4[1] of the Companies Act

Chapter 50, Statutes Singapore, 2012). In addition to its 'exempt private company' status, since late 1980s the GIC has also enjoyed a constitutional status in the form of a Fifth Schedule Company. This status has safeguarded Singapore's savings from depletion. Fifth Schedule Companies are defined in the constitution of Singapore as key statutory boards and government companies with a constitutional responsibility. In order to prevent the potential misuse of reserves and government assets by future governments, the constitution of Singapore protects past reserves of Fifth Schedule Companies that have been accumulated during previous legislative periods (Ministry of Finance, 2015). As such, the GIC has a constitutional responsibility to safeguard national reserves. It is accountable to the President regarding to GIC Board appointments. The Auditor General, appointed by the President, submits annual reports to the president and parliament on GIC audit (GIC, 2015). The GIC was established with the objective of maintaining long-term purchasing power of Singapore's savings. However, it does not own the assets that it manages. The mandate requires the GIC to invest exclusively into international assets. It started its international investment operations in 1981 with a size of about S$10 bn, which reached approximately S$110 bn – equivalent to US$82 bn – in 1997 (Lee Kuan Yew, 2006 Welcome Remarks 25 years; *The Straits Times*, 14 April 1999). Through its investments, the GIC has been channelling liquidity out of Singapore since 1981.[131]

Over time the GIC's business partners involved a select international group of financial organisations.[132] It is estimated that in the late 1990s, about 35 per cent of the GIC's assets – equivalent to about S$30 bn – were outsourced to international finance houses (*The Straits Times*, 14 April 1999). This has been well appreciated by international finance actors. For example, Rothschild & Sons was highly welcoming of its 1981 appointment to become GIC's official advisor. Lord Moser – then Deputy Chairman of Rothschild & Sons – describes this as the "biggest stroke of luck" in his career (Moser, 2008). Soon after the GIC's creation under the auspices of the DPM and the chairmanship of the PM, the GIC began to recruit external experts (Orchard, 2014). For example, the DPM travelled abroad in March 1981 to recruit talent in other financial centres (*The Straits Times*, 10 March 1981, pp.1–32). The GIC hired a number of international managers in order to start the department and to train the young people that the

[131] This had the important effect of mitigating inflation pressures (see Low, 2005).

[132] GIC's network of international business partner's has included a highly select group of individuals notably: Barton M. Biggs (Managing Director at Morgan Stanley Investment Management), Rolf E. Breuer (Chairman Deutsche Bank), Raymond T. Dalio (Chairman Bridgewater Associates), David I. Fisher (Chairman, Capital Group International), Maurice R Greenberg (Chairman American International Group), William H. Gross (Managing Director of Pacific Investment Management Company), Yoshinari Hara (President Daiwa Securities Group), David H. Komansky (Chairman Merrill Lynch & Co), Duncan M. McFarland (President Wellington Management Company), John Olcay (Vice Chair, Fischer Francis Trees and Watts), Ramon De Oliveira (Chairman, J.P. Morgan Fleming Asset Management), Marcel Ospel (President, UBS) and Henry M. Paulson (Goldman Sachs) (GIC Yearbook, 2001).

GIC was recruiting.[133] There is some evidence that the GIC outsourced funds to international fund managers in return for management expertise and staff training. For example, in 1983 GIC turned to Hagler Mastrovita & Hewitt Inc. which provided expertise and staff training in exchange for the management of discretionary funds from the GIC (*Fortune*, 21 March 1983).[134] However, the extent to which funds were placed to external managers in exchange for expertise and in-house investment capacity development at the GIC remains unknown.

Because of its explicit policy of in-house investment capacity building, the creation of the GIC did not contribute to the development of domestic private insurance and provident fund sectors. Since its creation, the GIC has followed a strategy of in-house investment capacity building via the strategic interaction and partnerships with third party managers. An official GIC statement that "[t]hese partnerships have helped [the GIC] to gain insights into high-quality investment ideas and research, as well as industry best practices in the areas of investments and operations" suggests that the GIC has greatly benefited from third party managers (GIC report, 2012, p. 20). A GIC report noted the strategic benefits of allocating funds to external managers. The statement that "[i]t diversifies the Government's portfolio, expands the investment opportunities available and deepens our understanding of financial markets" highlights the rationale behind capital outsourcing (GIC report, 2012, p. 20). The GIC partnered with international financial organisations and developed its own asset management capabilities (Ng, 2014). Ng Kok Song – a former GIC executive – highlights that the idea was to develop a reserve management institution, which was distinct from existing reserve management institutions, notably the MAS, in terms of its 'culture' (Ng, 2014). According to Ng Kok Song, the MAS had a risk averse culture, characterised by investments in highly secure and liquid international assets, whereas the GIC had a pure investment purpose, which required a more risk-based approach characterised by long term investments into riskier assets. Therefore, the GIC needed to be able to attract and retain funds and talent. Ng Kok Song's statement that "you need to compete against the private sector" indicates the tensions between the private domestic finance sector and the government (Ng, 2014). As the GIC has upgraded its internal investment capabilities over the years "the role of external managers has become more nuanced" (GIC report, 2012, p. 20). Over the years the GIC has sought co-investment deals with firms which have been operating in niche markets in which the GIC had not yet built capabilities or superior returns. GIC has built up an in-house team to manage external managers (the "external Managers Department"), responsible for appointing, and monitoring and reviewing (GIC report, 2012, p. 20).

[133] In addition, Rothschild & Sons provided long-term staff training. For example, each year two people from the GIC or the MAS were appointed to a two-year training programme. Furthermore, there was an agreement with Wharton Econometric Forecasting Associates from Wharton Business School to train 12 Singaporeans in computerised systems of modelling and forecasting at the NUS.

[134] *Fortune's* comment that "[Hagler Mastrovita's] compensation includes management of discretionary fund" suggests that the GIC placed out funds in return for staff training (*Fortune,* 21 March 1983).

Between the 1980s and 1990s the private fund management industry in Singapore was excluded to a significant extent from managing government surpluses and CPF savings. The GIC had a quasi-monopoly over fund management. Former GIC Chief Economist Yeoh Lam Keong underlines that most of Singapore's savings ended up with the GIC (Yeoh, 2014). The complete public sector, including government agencies and particularly statutory boards, relied heavily on the GIC Client Service Unit for investment consultancy and their asset management (Anonymous, personal communication, 03 March 2014). Most of the statutory board's investments are governed by the Trustees Act, which confines their investment spectrum exclusively to local stocks with a trustee status, especially fixed interest securities of other statutory boards and government securities (Koh and Kee, 1988; Economic Review Committee, 2002). The Ministry of Finance has asked the 30 statutory boards to choose between three alternatives: entrust their surplus funds to GIC, or an approved bank or an investment committee; Statutory boards with surpluses of more than S$500 mn have been traditionally required to deposit 50 per cent in treasury bills, and the remainder according to the act of incorporation (*The Straits Times*, 27 August 1981). Via the GIC, Singapore's government drained out investible surpluses and then channelled them abroad (*Asian Finance*, 15 February 1984). In the late 1990s the estimated total of assets under management by the GIC was approximately S$110 bn (*The Straits Times*, 14 April 1999). That was a very large sum if compared with the total amount of funds managed by financial institutions in Singapore, which was at the end of the end of 1997 about S$123 bn (MAS Annual Report 1998, p. 89). As of 1997, out of the GIC's S$110 bn only S$10 bn – about nine per cent of the total – was placed under management of investment houses located in Singapore (IMF, 1999, p. 9).

CONCLUSION

This chapter suggests that a PN analysis helps to explain why Singapore created an SWF with a savings and an international investment mandate. Alternative institutional choices were available at that time, such as using existing financial institutions (i.e. the MAS) or promoting private finance institutions (e.g. private funds, banks or insurance schemes) for allocating Singapore's domestic savings. These choices were supported by different socio-economic actors. Through a systematic analysis of debates, policy processes, and examining the kinds of institutions set up, the chapter finds that the state-directed PN in Singapore's savings domain operated via exclusion mechanisms of actors who followed narrow and sector-specific preferences. In turn this allowed for the pursuit of a long-term horizon with regard to the kinds of finance institutions set up. Based on these findings the chapter has been able to formulate an initial hypothesis, namely: having a state-directed PN in the savings domain increases the likelihood of creating an SWF with a savings and international investment mandate.

The first part (6.1) on economic inheritance outlined the broader macro-economic context and the external pressures to which Singapore's savings domain was confronted in the late-1970s and early-1980s. These related to rising inflation pressures and an international environment characterised by increasing investment opportunities. The second part (6.2) looked at the key actors and the type of PN in Singapore's savings domain. The structural relationship of actors in Singapore's savings domain referred to a state-directed PN characterised by a high concentration of power within a small number of state actors who enjoyed high levels of autonomy from domestic finance and business actors.

The third part (6.3) investigated the policy-making processes, and the state-directed PN in operation. Therefore, it looked at the entire range of actors in the savings domain with a substantial interest in the kinds of financial institutions set up and finds that the preferences regarding finance institutions differed between private domestic finance and international finance actors as well as between the Ministry of Finance and the Prime Minister's Office. Discussions at the time revealed that there were alternative institutional choices available that were supported by different socio-economic actors; state-society linkages in the savings domain operated via inclusion and exclusion mechanisms, and that socio-economic actors that were excluded were critical about the choices made. Singapore's state-directed PN influenced the quick resolution of internal conflicts about the kinds of financial institutions set up; indeed, the next chapter supports these findings and focuses on Hong Kong's industrial domain and analyses the effects of pluralist PNs on the choices of financial institutions.

With regard to the general argument of the thesis, the creation of the GIC in 1981 provided evidence on the limited impact of diffusion. However, its creation offered evidence in support of the efficiency argument. Though the 'efficiency' argument makes sense of the creation of GIC in 1981, the observable expectations of the efficiency argument do not fit in countries with similar macro-economic characteristics – as will be shown in the next chapter with reference to Hong Kong.

7. The Effects of Clientele Pluralist Policy Networks on Policy Choices in the Savings Domain: Private Finance Institutions in Hong Kong (1960s–1980s)

Between the 1960s and 1980s, the structural features of state-society relations in Hong Kong's savings domain were consistent with that of a clientele pluralist policy network (PN). It allowed a segment of civil society to influence policy-making. The structure of state-society relations was characterised by a high concentration of decision-making power within the government's Finance Branch, which had strong linkages to highly mobilised domestic finance and commerce organisations. While the state enjoyed low levels of state autonomy from finance and commerce, it disposed of high levels of autonomy from the Colonial Office in London, from Hong Kong's labour unions and from welfare organisations. Labour unions and welfare organisations were weakly mobilised and fragmented. This structure affected policy-making processes in Hong Kong's savings domain with regards to the types of finance institutions that were set up. It influenced the systematic over-representation of finance and business actors on important policy committees. While various socio-economic actors – notably labour and welfare organisations – had a serious interest in this issue, only finance and business actors were directly involved in policy-making.

The present chapter shows how Hong Kong's clientele pluralist PN in the savings domain influenced choices against creating state finance institutions. That is attained through an investigation of the entire range of socio-economic actors in Hong Kong's savings domain with a substantial interest in this issue. Subsequently it takes a view on how the PN operated by influencing policy-making processes in the savings domain. There is an examination of how network characteristics played out in policy-making processes through the mechanisms of inclusion in, and exclusion from, central policy-making committees of socio-economic actors. Central to this is the question of who was included or excluded. Related to that is the question of which actors benefited and which actors did not benefit from the type of finance institution that was set up. For this reason, the chapter examines the debates involving the Finance Branch, the Manpower Department, labour unions, welfare as well as business associations and finance organisations.

The chapter rests upon the argument that Hong Kong's clientele pluralist PN in the savings domain influenced a review, which led to decisions against creating state finance institutions with savings mandates. This review was based on the question of whether Hong Kong should establish a large state run Central Provident Fund (CPF) and a sovereign wealth fund (SWF) that invests CPF funds into international financial assets. Debates indicate the availability of different financial institutions and these differed in terms of ownership, legal status and mandate. Different choices implicated different re-distributional consequences for various socio-economic actors, notably labour unions, welfare/grass-roots groups as well as domestic finance and business actors. For example, private banks feared competition with state finance institutions, whereas labour unions and welfare associations highlighted their distrust of private finance institutions. The main finding of this chapter is that the state-society structures allowed policy makers to bypass domestic social and welfare organisations as well as labour unions, which demanded the creation of a CPF and an SWF that invests CPF funds. Hong Kong's clientele pluralist PN hampered the pursuit of policies and institutions with a long term horizon and characterised by high levels of coordination and state involvement. Instead, the PN influenced institutional choices – notably the promotion of private-pension and private-insurance schemes – that were structured around the immediate needs of Hong Kong's finance and business organisations. The PN included only a small group consisting of public officials and finance/business organisations, on key policy-making bodies that informed the decisions against creating state finance institutions. These findings support the initial hypothesis from Chapter 5 that having a state-directed PN in the savings domain increases the likelihood of creating an SWF with a savings and international investment mandate.

It is the cross-national comparison with Singapore that indicates the effect of Hong Kong's clientele pluralist PN. Until the 1960s Hong Kong and Singapore had similar kinds of financial institutions. In Hong Kong a number of powerful banks have emerged, such as the Hong Kong Bank, Standard Chartered and the Bank of East Asia. Likewise, Singapore saw the creation of a number of large banks, such the Overseas Chinese Banking Corporation, the Overseas Union Bank, and the United Overseas Bank. These were mainly established to serve the entrepôt trade as well as foreign investment, and to meet the banking requirements of a growing local population (Ishihara and Kim, 1982). Although in 1955 Singapore had created a state run CPF, but it remained relatively insignificant as a finance institution until the 1970s, because of its low contribution rates (P. Bowring, personal communication, 16 October 2013).[139] Hong Kong and Singapore started to establish themselves as regional financial centres (Ishihara and Kim, 1982). At that time both operated under currency board systems.

[139] Originally, in the 1950s and 1960s, mandatory contribution rates to the CPF were very low, applying to the employees' wages as well as to the employers' incomes (Lee, 1984, p. 258; Skully, 1987, p. 67; CPF Annual Reports, 1967-80; MAS Annual Report, 1980). They increased progressively from 5 per cent in 1955, to 38.5 per cent in 1980, to 42 per cent in 1981, to 45 per cent in 1982 and to its highest level of 50 per cent in 1985 (Lee, 1984, p. 258; Skully, 1987, p. 67; CPF Annual Reports, 1967–80; MAS Annual Report, 1980). Reflecting this increase was an increase in CPF's annual contributions with S$68 mn in 1968, to S$1.4 bn in 1978, to S$6 bn in 1985 (see TABLE 6.1).

Between the 1970s and 1980s Singapore as well as Hong Kong disposed of high levels of public and private savings. Thanks to their conservative fiscal policy, they both experienced concomitant levels of surpluses (see TABLE 7.1). One of core functions of an SWF with a savings mandate is the management of fiscal and current account surpluses. High surplus levels in Singapore and Hong Kong suggests that the sheer size of surpluses does not automatically lead to the creation of a SWF with a savings mandate.

TABLE 7.1. *Surpluses Singapore and Hong Kong between 1960 – 1980.*

	Singapore in mill Sing$	**Hong Kong** in mill HK$
1960	88	14
1965	136	77
1970	100	449
1975	551	488
1980	1,214	2,500

Sources: Youngson (1982, p.60), Low (2005, p.170).

NB: The Singapore figures refer to current account surpluses, whereas the Hong Kong figures refer to budget surpluses.

High levels of economic growth combined with a high propensity to save among the population also led to high levels of private savings. This situation was reflected in high savings ratios (see TABLE 7.2.). For example, in the 1980s, savings ratios in both even surpassed those of OECD economies, such as Germany, Austria and the US (Worldbank, Gross savings, 2015). Over that period similar institutional choices were available and similar socio-economic actors, which were mobilised and structured differently, participated in public debates.

TABLE 7.2. *Public and Private Savings in Hong Kong and Singapore (1980–1987).*

	Saving Ratio as a Percentage of GDP	
Year	**Singapore**	**Hong Kong**
1980	38.8	31.4
1981	41.7	30.4
1982	42.3	28.2
1983	45.0	25.1
1984	45.3	28.9
1985	40.6	27.3
1986	38.9	28.5
1987	40.5	31.6

Source: James (1991, p. 308).

It is noteworthy to highlight that the present chapter's focus is on Hong Kong's decisions to not create a state run CPF and an SWF with a savings and international investment mandate. The present thesis has good reasons for its focus on the issue of a CPF and SWF with a savings mandate, and it does not focus on the Hong Kong Monetary Authority. First, the temporal focus of this thesis is between the 1960s and 1980s and the Hong Kong Monetary Authority was created in the 1990s – a context in which Hong Kong prepared itself for its return to China. Second, before the creation of the Hong Kong Monetary Authority, surpluses and exchange reserves were managed by the Hong Kong Exchange Fund (established 1935), which was essentially an SWF with a currency stabilisation mandate. As highlighted in Chapter 2.3, for theoretical purposes and word limitations the present thesis' focus is not on the creation of SWF with stabilisation mandates.

Section 7.1 outlines Hong Kong's macroeconomic context, and it offers a brief background on Hong Kong's savings domain until the early 1970s. Section 7.2 looks at the actors in Hong Kong's savings domain and at the PN characteristics. Section 7.3 refines the argument of Chapter 6 by looking back at the effects of clientele pluralist PNs on the kinds of financial institutions set up in Hong Kong's savings domain. It thereby identifies pressures, opportunities and constraints to which Hong Kong had to respond between the 1970s and 1980s.

7.1 ECONOMIC INHERITANCE AND MACRO-ECONOMIC CONTEXT (1950s–1960s)

Between the 1950s and 1960s, economic growth combined with a fast-growing population with a high propensity to save led to a significant increase in Hong Kong's domestic savings. In the period following World War II and the Communist takeover of China (in 1949) Hong Kong had been confronted with an inflow of capital. That was accompanied by an influx of migrants. Hong Kong's population was around 600,000 people in 1945 and it increased dramatically to around 2.4 mn by the late 1950s (White Paper, 1973, p. 8). Thanks to dynamic economic growth Hong Kong experienced prosperity from the 1960s onwards. That combined with a high propensity to save – on average every person saved around 60 per cent from its income – produced a significant amount of domestic savings (Jao, 1971). Jao estimates that the per capita GNP in Hong Kong for 1966 was on average US$ 560; and the per capita bank deposit for 1966 was on average US$ 392 (Jao, 1971, pp. 139–138). Based on the assumption of an even distribution among the population this means that the average person saved more than invested.

Savings in Hong Kong were channelled into a swiftly expanding domestic private commercial banking sector. Opening a savings account with private commercial banks in Hong Kong was cheap, easy and attractive (e.g. through the exemption from interest rate tax). Even low-income groups, as well as children, were attracted by banks to open accounts (Jao, 1971). As a result, from the mid-1950s Hong Kong saw a dramatic expansion of bank deposits (Jao, 1971). The total of deposits (including demand, time and savings deposits) increased from HK$1,137 mn in 1955 to HK$2,682 mn in 1960, and to HK$10,367 mn in 1968 (see Jao, 1971, p. 27). Correspondingly, the total assets of the banking sector in Hong Kong experienced a similar increase from HK$1,331 mn in 1955, to HK$2,952 mn in 1960, and to HK$10,844 mn in 1968 (Jao, 1971, p. 29). According to Jao (1971, p. 30), between 1954 and 1968 bank deposits per head increased by 465.6 per cent. Although the total number of licensed banks shrank from 94 in 1954 to 71 in 1968, the number of total offices increased from 97 in 1954 to 349 in 1968 (Jao, 1971, p. 24).

From the 1970s, high levels of domestic savings were exposed to increasing inflation. Inflation levels in Hong Kong reached double-digits, mainly because of its high import ratios, as well as large fund inflows from neighbouring countries (*The Economist*, 19 July 1975; Tradeeconomics, 2015; Jao, 2001). Hong Kong's strong economic growth, stable currency, low taxation and openness attracted capital funds in the form of 'hot money' and foreign direct investment (FDI) (Jao, 1971). Money was flowing into Hong Kong's stock market, as well as into its property market, and credit expansion pushed inflation rates in Hong Kong to around 18 per cent in the early 1970s and around 15 per cent in the early 1980s (*The Economist*, 19 July

1975, p. 15; Li, 1999; Jao 1999, 2001; Moreno, 2012, p. 185). Hong Kong's domestic commercial banks also allocated significant funds into the burgeoning property sector and into Hong Kong's speculative stock market (Jao, 1993). Jao (1993) noted that "only two sectors, building and construction […] have consistently enjoyed growing bank credit allocation in both absolute and relative terms" (Jao, 1993, p. 133). From the 1970s onwards, Hong Kong's stock market had started to become an important source for financing property (Wong, 1991a, p. 217). This had important implications. Because of the banking sector's high exposure to the property sector and later to the stock market, this translated into a number of banking crises between the 1960s and the 1980s (Jao, 2001, pp. 23–48). Hong Kong did not dispose of a depositor insurance scheme which would have protected people's savings in the case of a banking crisis. That was because Hong Kong's banking sector has heavily opposed a deposit insurance scheme because that would have increased the commercial banks' operating costs (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 the awareness of regulatory deficits in the banking sector among Hong Kong's policy makers (Hong Kong Hansard, 9 April 1986, p. 983). According to Li Kin-Yin (1988), people who invested into private pension fund schemes at that time were directly affected by Hong Kong's stock market crash in the 1980s (Li Kin-Yin, 1988).

This situation, combined with an increasingly attractive international investment environment, put pressure on Hong Kong's policy makers. As a small open economy with high import needs, Hong Kong was faced with the question of how to sustain the purchasing power of its ageing population in a context of high inflation pressures (Hong Kong Greenpaper, 1977). In the early 1980s the scope for safe long-term investment opportunities opened up with the US interest rate shock.[141] This led to an increase in US interest rates – up to 20 per cent – and an appreciation of the US$. This made it very lucrative to invest into US$ assets, specifically government bonds. The US interest rate shock had a particularly significant effect on small open economies, which were highly exposed to the US economy (Glick and Moreno, 1994). Between 1974 and 1983, the HK$ was freely floating, and therefore Hong Kong was not forced to follow US monetary policy. As such, investors (i.e. the Hong Kong state) could take advantage of the interest rate differential, and were therefore getting a premium on investments.

[141] The second oil shock, sparked by the Iranian Revolution (1979), again increased worldwide oil prices from US$13 per barrel in 1978 to US$32 per barrel in 1980 (Krugman and Obstfeld,1997, p. 585). This initiated a second worldwide recession in 1981 and 1982 (Kenwood and Loughheed, 1993, pp. 245–248). Peak inflation in the US translated in the early 1980s into high inflation levels in Hong Kong. In contrast to the first oil shock the US responded in the 1980s with a restrictive fiscal and monetary policy. To mitigate US inflation, the US Fed started to tighten monetary policy sharply in 1981 (Li, 1999, p. 130).

7.2 KEY ACTORS AND THE TYPE OF POLICY NETWORK

Between the 1960s and 1980s, policy within Hong Kong's savings domain was formulated in a clientele pluralist PN. Over that period, decision-making power in Hong Kong's savings domain was highly concentrated. Although the Governor had the ultimate decision-making power, it was conventional that for economic matters the Financial Secretary was closely involved. The Financial Secretary was the highest-ranking official responsible for financial policies (Ngo, 1996, p. 176). There was also a Banking Advisory Committee (BAC) – established by law – that advised the Governor on any issues related to banking. This committee consisted of the Financial Secretary, who was chairperson, the Accountant General and representatives of Hong Kong's domestic banks (Mc Carthy, 1982; Schenk, 2009). The policy process was usually top-down led. If a policy issue was identified (e.g. by the Governor, the Chief Secretary or Financial Secretary) then the Governor, the Chief Secretary or the Financial Secretary could decide on whether to delegate it to a relevant government branch (L. Goodstadt, personal communication, 12 February 2015). With regard to policy issues that affected labour matters, specifically insurance and pensions, it was convention to involve the Manpower Branch of the government. According to Leo Goodstadt – former Chief of Hong Kong's Central Policy Unit – this was normally done with some kind of policy direction (Goodstadt, 2015).[142]

Hong Kong's state apparatus had strong links to the finance and commerce sector. This is supported by existing academic research. Major academic accounts, such as Ngo (1996) Chiu (1990) and Leung (1990), emphasise that Hong Kong's government enjoyed low levels of autonomy from finance and commerce.[143] Chiu's statement that "[t]here is no point of speaking of an autonomous state when its actions were found regularly consistent with the interests of a particular segment of the society but not of others" indicates the influence of finance and commerce actors (Chiu, 1994, p. 62). Some scholars, such as Endacott (1964), Crisswell (1991) and Wong (1991) refer to this phenomenon as an institutionalisation of business interests in Hong Kong's policy-making structure. A similar conclusion was made by Miners' seminal research on the political system of Hong Kong, which highlights the influence of financial and commercial interests – via the Hong Kong General Chamber of Commerce (HKGCC) – on the Executive Council (ExCo) and the Legislative Council (LegCo) (Miners, 1975).[144] While the official members were senior civil servants acting as spokespeople for their departments, most

[142] However there was also room for manoeuvre for Departments and Branches of the government with regard to the suggestions and directions coming from the top (Goodstadt, 2015).
[143] There are only a few academics, notably Lau (1982), who argue that the Hong Kong state enjoyed high levels of autonomy from Hong Kong's finance and commerce actors.
[144] The LegCo is Hong Kong's legislative chamber, whereas the ExCo can be described as Hong Kong's Cabinet. The relationship between the Governor and the ExCo would be equivalent to "the relationship between the Prime Minister and his Cabinet" in Britain (Owen, 1971, p. 348). The LegCo consisted of the Governor, four ex-officio members (i.e. the Chief Secretary, the Attorney General, the Secretary for Home Affairs, and the Financial Secretary), 17 official members, and 26 unofficial members.

of the unofficial members were mainly drawn from the finance, trade and commerce sector (Leung, 1990; Ngo, 1996). Hong Kong's government rarely opposed the views of the unofficial members in the ExCo, which were mainly chairmen of merchant houses, major local banks or directors of public utility companies (Miners, 1975; Leung, 1990; Chiu, 1994; Ngo, 1996).[145]

The literature on economic policy in Hong Kong highlights the asymmetry of interest-representation in the policy-making process. Ngo (1996) even talks about an "alliance" between the colonial state and finance and commerce. In *The East Asian anomaly revisited: the politics of laissez-faire in Hong Kong 1945-1985,* Ngo (1996) outlines the historical context in which government-business relations emerged and influenced Hong Kong's "laissez-faire" industrial policy. Hong Kong's economic success without government intervention is presented as a puzzle for developmental-state theory (Ngo, 1996). Ngo (1996) investigates why Hong Kong between 1945 and 1985 adopted specific patterns of interventions and not others. Ngo (1996) draws on a coalitional analysis in which he looks at the interest-group configuration in Hong Kong's polity and relates it to patterns of economic intervention. This makes Ngo's work highly compatible with a PN analysis. Ngo (1996) builds on a long tradition of research that looks at state-society structures in Hong Kong (Ngo, 1996; Harris, 1988; Rear, 1971; Chiu, 1994). Rear (1971) investigated LegCo and ExCo membership and describes the banking and merchant houses as a "fairly tight-knit group" (Rear 1971, p. 73) and Davies (1977) goes further by investigating overlapping membership in government councils, boards, and committees. Leung (1990) investigated whether these patterns also held in the 1980s. Miners' statement that in Hong Kong "[a]ll groups do not have equal access to government" draws attention to the representation asymmetry (Miners, 1991, p. 191). It has been widely accepted in the literature that finance and commerce interests were overrepresented in Hong Kong's policy-making structures (Ngo, 1996; Chiu, 1994; Leung, 1990).

Up to the 1980s, nearly all of the ExCo and the LegCo unofficials were successful businessmen. About 45 per cent of all LegCo and ExCo members were businessmen or had direct links to business associations, and 48 per cent of all LegCo and ExCo members were civil servants (Davies, 1977, p. 78). The remaining 7 per cent were attributable to persons with a professional background (e.g. doctors, lawyers). Interestingly, there was no member from lower income groups or the labour sector (Davies, 1977, p. 78). Until the LegCo reform in 1984 both bodies were exclusively composed of appointed unofficial members and appointed official members. The dominance of business and finance was maintained even after the LegCo reform in 1984, which introduced the a system of Functional Constituencies (Miners, 1994; Ma, 2007). Miners'

[145] The socioeconomic backgrounds of LegCo and ExCo were quite homogeneous. In the 1950s and in the 1960s most of them were directors of British merchant houses, whilst from the late 1960s onwards it has also included Chinese business leaders, notably bankers (e.g. from the Hang Seng Bank or from the Bank of East Asia) and a few Chinese with industrial backgrounds (especially large manufacturers from Shanghai) (Chiu, 1994).

statement that "[t]he composition of the Legislative Council remained substantially the same from 1985 to 1991" suggests that there were no significant changes following the 1984 reform (Miners, 1994, p. 229). Interestingly, a significant number of important business leaders, specifically from the real estate sector (e.g. K.S. Li, the Kwok brothers, and Gordon Wu) were not represented on political bodies.[148]

In turn, Hong Kong's large commercial banks had close links to Hong Kong's large merchant groups. They were not only connected via financial ties, notably cross-equity holdings, but also through cross-directorships (McCarthy, 1982). Chiu states that "[the Hong Kong Bank's] boardroom where members of the major hongs were well represented, served as an arena for the hongs to exchange ideas and coordinate their operations", which highlights strong ties between the finance and commerce sector (Chiu, 1994, p. 22).[149] For example, in 1987, out of the ten unofficial members of Hong Kong's Cabinet (i.e. the ExCo), seven were related to CEOs of organisations in trade, commerce and banking. Out of these seven, two were affiliated with the Hong Kong Bank (see TABLE 7.3). In addition, Hong Kong's banks were organised in the Hong Kong Association of Banks.[150] Membership was compulsory for commercial banks (McCarthy, 1982, p. 101). If a member ceased its membership it automatically also ceased its banking license (McCarthy, 1982). This provided the Association of Banks with a strong sanction mechanism. It had a standing committee, which managed the Association, which was comprised of three permanent members (i.e. The Bank of China, the Chartered Bank, the Hong Kong Bank) and nine elected members. Domestic commercial banks also had strong linkages to the deposit-taking sector as well as the insurance sector, as banks had established their own deposit-taking companies, or via strategic alliances (Yu, 1997; P.C. Lund, personal communication, 15 November 2013). As such, Hong Kong's banks were also affiliated with other associations that represented different segments of the finance sector, such as the Hong Kong Investment Fund Association. Many banks were also members of the Deposit Taking Companies Association (Lund, 2013). For example, as of the late 1970s there were more than 1,500 finance companies (e.g. commercial banks, deposit taking companies, merchant banks and insurance companies) registered in Hong Kong (Jao 1979, p. 675). Around one third of the members of the Hong Kong Investment Fund Association were from the banking sector, and the remaining members came from insurance and investment companies or investment banks (Thomas, 2004, p. 66).

[148] That might be due to the fact that finance and commerce were well entrenched and long established political forces, whereas real estate as an economic and political grouping emerged at a relatively late stage, specifically from the 1970s onwards.
[149] The notion of 'hongs' refers to large business houses, such as Swire, Jardine Matheson, Butterfield and Swire, Dent& Co, Wheelock Marden.
[150] The Association of Banks replaced in 1981 the long standing Exchange Banks Association (est. 1897). The Association of Banks was established with the Hong Kong Association of Banks Ordinance with the main objectives of (1) furthering the interests of licensed banks (2) regulating issues regarding the governance of banks (3) to represent the interests of member banks vis-à-vis public bodies and (4) to act as an advisory body to its members.

TABLE 7.3. *Business Background of unofficial ExCo members in 1987.*

Chung Sze-yuen	Chairman, Sonca Industries Director, China Light and Power Director, Swire Properties Director, World International (Holdings)
Lydia Dunn	Executive Director, Swire Pacific Ltd Director, John Swire and Sons (HK) Ltd Director, Cathay Pacific Airways Director, Hong Kong Bank
Lee Quo-wei	Chairman, Hang Seng Bank
Chen Shou-lum	Director, The Hong Kong Electric Co. Ltd Director, Cable and Wireless (HK) Director, Hang Seng Bank-
Allan Lee Peng-fei	President AVA International Ltd Director, Elec and Eltek Co. Inc Director, British American Tobacco (HK) Ltd Director, Playmate Holdings Ltd
Peter C. Wong	Solicitor Non-executive director, Chow Sang Sang Holding Co. Ltd Non-executive director, Commercial Bank of HK Ltd Non-executive director, Asia Insurance Co. Ltd
William Purves	Chairman, Hong Kong Bank Director, British Bank of the Middle East Director, International Commercial Bank Director, Marine Midland Bank
Maria Tam Wai-chu	Barrister-at-law
Chiu Hin-kwong	Medical Practitioner
Daniel Tse Chi-wai	President, HK Baptist College

Source: Leung (1990, p. 23).

While Hong Kong's state apparatus enjoyed low levels of autonomy from finance and commerce, it enjoyed high levels of autonomy from the Colonial Office in London, from domestic manufacturers, as well as from domestic grass-roots organisations and welfare and labour pressure groups (D. Akers-Jones, personal communication, 01 November 2013; A. Chan, personal communication, 02 December 2013). With the abolition of the Imperial Restrictions in 1958, which required the strict monitoring of colonial budgets, Hong Kong was quasi-independent in the financial/savings domain from the United Kingdom (Ngo, 1996; Goodstadt, 2007). This status gave Hong Kong autonomy in finance and savings matters, such as raising loans without the permission of the United Kingdom (Ngo, 1996). For example, in the 1970s, London's Labour government and the Minister of State at the Foreign and Commonwealth Office urged the Hong Kong's government to create a social security system (Miners, 1991). However, Hong Kong's policy makers resisted those demands (see Chapter 5.2. for an overview of the mobilisation among Hong Kong's industrial actors). According to Miners (1991) British trade unions were among the key drivers behind this, because they wanted to see rising wages in Hong Kong, which would make British products more competitive.

Domestic grassroots organisations, such as welfare and labour pressure groups, were characterised by low levels of mobilisation.[151] Numerous associations with overlapping constituencies were competing for members. The associational landscape of social-welfare organisations and labour unions was characterised by a number of conflict lines, notably in terms of political affiliation, beliefs and sectorial affiliation. While left unions were affiliated with the Hong Kong Federation of Trade Unions, right-centre unions were affiliated with the Hong Kong and Kowloon Trades Union Council (Ng and Levin, 1983). In addition, there were nonunion labour organisations, such as the Christian Industrial Committee, run by Hong Kong's Christian Council, which had been lobbying for labour rights and legislation (Li Kin-Yin, 1988, p. 54).

Trade organisations were further grouped in a number of umbrella organisations. For example, the Hong Kong Council of Social Services was the coordinating body for voluntary social and welfare groups (Li Kin-Yin, 1988, p. 54). In addition, there were numerous ad hoc coalitions, such as the Coalition of Labour and Social Workers' Organisation and the Committee on Social Security, which comprised about 40 organisations largely from the labour sector (Li Kin-Yin, 1988, p. 35). Because of their voluntary character, their capacity to bind members was low, and most of them were small in size, in both absolute and relative terms, and membership density was low. Ng and Levin's statement that "over half of all registered unions in 1979 had fewer than 251 members and nearly 80 [per cent] had 1000 or fewer members" draws attention to the fragmentation of trade unions (Ng and Levin, 1983, p. 44). The overall union density rate (ratio of union membership to total number of employees) was relatively low compared to other countries (Ng and Levin, 1983, p. 30). Hong Kong's low density of trade union membership relates to the large proportion of small enterprises. It is more difficult to organise labour in small and medium enterprises, which were often run as family firms, and the majority of establishments in Hong Kong were run as small and medium enterprises (Lee, 1976).

[151] For example, former Hong Kong Chief Secretary Chan highlighted that during the 1980s, nongovernmental social-pressure groups were weak in Hong Kong (Chan, 2013). Likewise, former Chief of Central Policy Unit Leo Goodstadt emphasised that there was no effective lobby for welfare in Hong Kong (Goodstadt, 2013). A similar statement with regard to Hong Kong's labour unions was made by Andrew Sheng, former deputy of the Hong Kong Monetary Authority (A. Sheng, personal communication, 30 October 2013).

7.3 POLICY-MAKING AND CHOICES – THE POLICY NETWORK IN OPERATION

The 1987 decision against creating state finance institutions in Hong Kong's savings domain came about as a result of a review of the establishment of a CPF. This review was concerned with the manner in which Hong Kong should address the issue of old-age security and welfare. Debates reveal that there was an opportunity to create a large CPF in Hong Kong and a related opportunity for a GIC-like SWF. The review was affected by Hong Kong's clientele pluralist PN, which operated via mechanisms of exclusion and inclusion. State actors in the savings domain were dependent on domestic finance and business for information and co-operation, which led to a systematic over-representation of business on important policy committees (Miners, 1991; Ngo, 1996). Until 1980, the government could only indirectly access information about banks and deposit taking companies. Only the Monetary and Statistics Ordinance (1980) empowered the government to collect detailed statistics from banks and deposit taking companies (McCarthy, 1982). The combination of a highly concentrated state decision-making structure with low levels of autonomy from a highly mobilised finance/commerce sector allowed the bypassing of domestic welfare and labour organisations in the policy-making process. The state-society structures in place hindered the pursuit of a long-term view of policy in Hong Kong's savings domain, which would be highly coordinated with other policy domains and imply a high degree of state involvement.

With regard to the overall argument, the case of finance institutions in Hong Kong's savings domain offers little evidence for an efficiency argument. The observed policy outcome in Hong Kong's savings domain is contrary to what a supporter of an efficiency argument would have predicted. In view of an ageing population and given that no old-age security and welfare system had been put in place, pressures were rising in Hong Kong to create state finance institutions with savings mandates in order to secure future purchasing power of the population.[153] Interestingly, at this time Hong Kong already had the capacity and 'know-how' to manage savings abroad via state finance institutions (Hong Kong Hansard, 3 February 1993). For example, the Hong Kong government already had a small state-run CPF (i.e. the Subsidised Schools Provident Fund), which mainly invested in highly secure international assets (Hong Kong Hansard, 13 March 1987).[156] Although Hong Kong developed itself into a regional finance centre, its government debt market remained underdeveloped until the 1990s. Thanks to

[153] According to Chow (2015) assistance schemes in Hong Kong were only for very poor and it was only a very small amount of money. There was nothing in place for those who retire, unless they were very old (i.e. 70 years and above) (Chow, 2015).

[156] As such, the Hong Kong government already had experience (though on a very small scale) of state finance institutions with a mandate of investing domestic savings abroad (see Li, 1988). However, it only covered only teachers (Li, 1988). Every teacher had to contribute 5 per cent of his or her salary to the *Subsidized Schools Provident Fund,* which was managed by government officials under the Education Department (see EDB Hong Kong, 2012).

reoccurring budget surpluses, and Hong Kong's conservative fiscal policy, there was no need to issue bonds to finance public projects (Tomkins, 1962).[157]

The case of financial institutions in Hong Kong's savings domain also offers little evidence for a diffusion argument. With Hong Kong's high savings and given that its peer, Singapore, had created state finance institutions with a savings and international investment mandate (i.e. CPF and SWF), a supporter of a diffusion argument might have predicted the creation of similar state finance institutions in Hong Kong. Although Hong Kong's policy makers had been actively looking at other peers from the 1960s, notably Singapore, they explicitly opted for private financial institutions (N. Chow, personal communication, 17 February 2015; OMELCO, 1986). For example, Chan (2013) highlights that during her time at the Social Services Branch she went with two other colleagues to Singapore and Malaysia to investigate their CPFs (see SBR Harbour Department of Social Services, Confidential report, 1974–1976). Similarly, in the 1980s the Manpower Panel of the Office of the Members of the Executive and Legislative Councils (OMELCO) in Hong Kong contacted local and overseas organizations for information on the running of a central provident (OMELCO, 1986). Surprisingly, official discussions about establishing a CPF in Hong Kong took place in 1986/87, a period when Singapore's CPF with its high contribution rates was no longer considered an example of best practice by policy makers in Singapore itself (Hong Kong Hansard, 13 March 1987).[160] This is surprising for a supporter of a diffusion argument, because Hong Kong's debate about the creation of a CPF took place at a time when it was 'unfashionable' to create a large CPF similar to Singapore. Singapore's case was used by CPF opponents in Hong Kong, notably by representatives from commerce and from manufacturing, to illustrate how a CPF can affect wage levels as well as consumption levels through mandatory CPF contribution rates (Hong Kong Hansard, 6 November 1986).

The creation of a large CPF in Hong Kong might have led to the creation of a GIC-like institution. A LegCo report from the 1980s reveals that the size of a state-run CPF covering Hong Kong's labour could have reached, over a period of 10 years, a size similar to Singapore's CPF (Hong Kong Hansard, 13 March 1987). Over ten years this might have led to a CPF with a volume of between HK$80 and HK$90 bn net (Hong Kong Hansard, 5 November 1986, p.

[157] Furthermore, the creation of a government bond market would have also implied the creation of a Central Bank or a Monetary Authority, which also controls interest rates, and the supply of money. But in Hong Kong these functions were fulfilled by large domestic commercial banks until the 1990s, which benefited respectively from the seigniorage of issuing bank notes and their status as clearing house and banker to the government (Sheng, 2013).
[160] It was then in 1985 when Singapore went into its first severe recession, partly because of its high mandatory CPF contribution rates (up to 50 per cent of the income).

327).[161] If interest rates were included in this calculation, this figure would have significantly increased. Given an annual addition of HK$8,500 mn and a minimum annual interest rate of 10 per cent (during the 1980s, the average prime interest rate was even higher), the CPF would have grown in a period of ten years to around HK$140 bn (calculated with data from Hong Kong Hansard, 5 November 1986, p. 327; FedPrimeRate, 2015). Compared with the total estimated government revenue in 1986 of about HK$40 bn, this would have amounted to a very large sum (Hong Kong Hansard, 5 November 1986, p. 327).

As mentioned previously, public pension funds governed by trustee legislation need to allocate their capital into highly secure asset classes. This typically requires a non-active management.[162] Such a pension fund usually translates its members' contributions into secure government bonds that are issued by a monetary authority or central bank. The proceeds from the issuance of government bonds are usually used to finance budget deficits (Hong Kong Hansard, 13 May 1987). But between the 1960s and the 1980s, Hong Kong enjoyed structural surpluses and, therefore, did not need to issue bonds. As a result, it issued only a small quantity of government bonds. Hong Kong's shallow government-debt market, combined with the lack of alternative secure asset classes in Hong Kong, inhibited flexibility in investment configurations. Between the 1960s and the 1980s, a highly volatile real estate and stock market made investments in other domestic assets highly risky (Hong Kong Hansard, 13 May 1987).

Given the lack of alternative domestic asset classes in the context of an attractive international investment environment, a supporter of an efficiency argument would have expected the creation of an SWF that channels savings into international assets.[163] It was noted that it would have been rational to allocate CPF funds into safe and long-term international assets (see Mok, 1986a). This idea was also brought up on several occasions in Hong Kong's LegCo (Hong Kong Hansard, 13 Mar 1987). It was highlighted that in the case of the creation of a large CPF, the funds need to be invested professionally, and the return on the investments should be used to pay the interest on CPF members' accounts ('Implications of Establishing a CPF in HK', Hong Kong Hansard, 13 May 1987, p. 1591). A LegCo member with strong links to international finance even suggested the creation of a state investment agency to invest domestic savings in international assets (Hong Kong Hansard, 13 May 1987). This might have led to the creation of a GIC-like SWF in Hong Kong.

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[161] This estimation was made in 1986, based on the following calculation: given 2,600,000 people in the local labour force, a 5 per cent contribution, and an average worker income of HK$ 3,000 per month, each year would mean an accumulation of between HK$ 8,000 and 9,000 mn net (excluding interest earned) (Hong Kong Hansard, 5 November 1986, p. 327).

[162] Some public pension fund schemes, such as the Californian Public Employees' Retirement System, invest part of their assets abroad. If CPFs manage their assets actively in international assets, then they are very similar, apart from their liability structure, to SWFs with a savings mandate.

[163] The risk referred to high levels of volatility in Hong Kong's domestic market (i.e. reoccurring speculation and domestic banking crises).

THE PARTICIPANTS AND THEIR PREFERENCES

Preferences with regard to the kinds of financial institutions set up in Hong Kong's savings domain differed among socio-economic actors. Domestic finance and commerce actors shared similar preferences with regard to the kinds of finance institutions set up (Ngo, 1996). Common to them was their objection against the creation of a large state-run mandatory CPF, and the creation of an SWF. Although they shared similar preferences regarding the non-creation of a CPF, the reasoning behind these preferences differed. Domestic finance framed the creation of a CPF as an issue of inefficient state intervention, which would affect the allocation of resources and Hong Kong's role as a financial centre. By collecting large 'mandatory' amounts of domestic savings, a CPF would distort free market forces in the savings sector (*The Bulletin,* June 1985, p. 54). As such, financial actors saw a large CPF as a direct competitor to their private schemes (Li, 1988). The banking sector feared that people who put their savings into domestic bank accounts would be forced to reallocate their savings into state organisations, which would then be invested in long-term secure assets, notably government bonds. Commercial actors framed their opposition against a mandatory state-run CPF as an issue of consumption.

For example, the HKGCC highlighted that the existence of large mandatory CPFs would result in less spending and lower living standards. One of the major arguments was that a CPF would "decrease […] several thousand million dollars of money in circulation" and "this would in turn inflict a heavy blow on the domestic consumer market" (see Hong Kong Hansard, 5 November 1986, p. 327). Furthermore, the HKGCC also saw the introduction of a CPF as an increase in taxation, because a CPF would increase labour costs. Consequently, commercial representatives emphasised that this would have a direct impact on Hong Kong's productivity and competitiveness. Chamber representatives highlighted that such a mandatory scheme is against the principle of 'freedom of choice' and that the creation of a mandatory CPF could be first step towards a welfare state (Hong Kong Hansard, 13 May 1987). As such the commercial community feared that a CPF could discourage new investment into the Colony because of the uncertainty over gradual contribution increases. Likewise, Clydesdale and his constituency (i.e. the Employer Association) opposed the creation of a CPF (Hong Kong Hansard, 4 November 1987). Clydesdale's statement that "government involvement in such a scheme will discourage business investors and business investment, essentially because business, which would pay directly into such a scheme yet have no control over its dimension, would see no end to potential gradual increases in cost" suggests high levels of opposition among employer groups

(Hong Kong Hansard, 13 May 1987, p. 1544). It should also be noted that the private insurance sector was well represented within the HKGCC. For example, in the late 1960s and in the late 1970s the chairman of the Union Insurance Society of Canton, was at the same time the chairman or vice-chairman of the HKGCC (see TABLE 7.3). That gave private insurance actors a powerful voice, especially given that the chairman and/or vice chairman of the HKGCC were usually appointed to LegCo. Likewise, the Chinese Chamber of Commerce opposed the creation of a mandatory state-run CPF in Hong Kong (Ho Sai Chu, personal communication, 25 November 2013). They feared that a CPF would drain liquidity out of the system and thereby depress domestic consumption.

Different sections of the government apparatus, notably the Finance Branch, the Health and Social Welfare Branch, as well as the Education and Manpower Branch supported Hong Kong's existing policy of having savings channelled on a voluntary basis through private finance institutions. The Government at the time shared the business worldview that the state ought not to get involved in the allocation of savings via the creation of a CPF (L. Goodstadt, personal communication, 15 November 2013; Akers-Jones 2013). According to Ronald Arculli – former LegCo member and later the Chairman of the LegCo Mandatory Provident Fund Committee – Hong Kong's policy makers were reluctant to the idea of insuring Hong Kong's population under the government (R. Arculli, personal communication, 30 October 2013). Arculli's statement that "if there was a financial disaster, and there was a loss in the CPF, the government would be responsible to the beneficiaries" indicates the potential risks involved in the creation of a CPF (Arculli, 2013). Between the 1960s and 1980s Hong Kong's government was not prepared to take such risks on behalf of the population (Arculli, 2013).

The government did not want to interfere with the business of Hong Kong's commercial banks. According to Joseph Yam – former Chief of the Hong Kong Monetary Authority – the Hong Kong government believed that private finance institutions manage savings more efficiently and better than state finance institutions (J. Yam, personal communication, 19 November 2013). Likewise Andrew Burns – personal assistant to David Li, the CEO of the Bank of East Asia – highlights that philosophically the government was not committed to the position of providing a state run pension scheme (A. Burns, personal communication, 25 October 2013). The government considered it an opportunity for private fund managers to make a profit and thereby to promote Hong Kong's status as an international financial centre (Yam, 2013). It did not wish to frustrate the finance and commerce actors. For example, former Hong Kong Governor Sir Akers-Jones highlights that during the volatile 1980s in particular, the government was very cautious to not 'upset the commercial community' (Akers-Jones, 2013). Also Nelson Chow – former Chairman of the Social Welfare Advisory Committee – emphasises the influence of business over politics on the kinds of financial institution set up. Chow's statement that "[the

Secretaries of that time] were very much under the pressure of commercial business sector" highlights the influential role of domestic business on the policy process regarding the CPF (Chow, 2015).

While different sections of the government, together with domestic finance and commerce, supported the option of private finance institutions, domestic grassroots/social-welfare actors and trade unions demanded the creation of a state run CPF. The director of the Hong Kong Council of Social Services Hui was highly critical of private financial institutions. Hui's testimony that "according to the suggestion of the consultation paper, their future contribution [employees] will only enrich the financial institutions or insurance and trust fund companies which are responsible for the management of the retirement funds" indicates high levels of mistrust among social service organisations vis-à-vis the introduction of privately run saving schemes (Hong Kong Hansard, 3 February 1993, p. 1715). Common to domestic grassroots/social-welfare actors and trade unions was their lack of trust in private finance institutions in the savings domain. According to them, private finance institutions such as commercial banks were mainly driven by self-interested profit maximisation, whereas a state-run CPF was believed to bring more benefits to the population (Hong Kong Hansard, 3 February 1993; *South China Morning Post*, 12 November 1987). As such, many associations, such as the Christian Industrial Committee, the Hong Kong Council of Social Services, and the Hong Kong Social Worker's General Union, supported the creation of a state run CPF. However, their actions in the pursuit of this objective were not well coordinated. Different but overlapping proposals and surveys were produced by various groups at similar times (see Li, 1988). For example, the Methodist Church released a survey showing that 90 per cent of workers in Chai Wan – a district of Hong Kong – supported the creation of a CPF (Li, 1988). In August 1986 the Christian Industrial Committee, together with labour unions, published another survey indicating that around 80 per cent of 4,000 respondents supported the formation of a CPF (*South China Morning Post*, 17 August 1986).

The Christian Industrial Committee and the Hong Kong Social Worker's General Union suggested a CPF system like in Singapore, to be managed by the Hong Kong government at a national level, which would invest in secure assets, notably bonds (Mok, 1986). According to the chairman of the Hong Kong Christian Industrial Committee the CPF would have been administered by "financial institution appointed by the Government or a public corporation set up for the purpose" (*The Bulletin*, June 1985, p. 53). Simultaneously, the Hong Kong Social Workers General Union invited unions and welfare organisations to form working committees on a CPF (Li, 1988 drawing on Annual Reports of 1985-1986, 1986-1987 of Hong Kong Social General Workers Union; and *Man Wei Daily*, 3 August 1986). Also, the Hong Kong Council of Social Services drafted a proposal, though it was not published but circulated among other unions and government departments (Li, 1988). The Hong Kong Social Workers General Union, as well as the Hong Kong Social Workers Association together with the Hong Kong Council of Social Service met in May 1987 with the Secretary for Education and Manpower to propose the creation of a CPF (Li, 1988).

The position of industrial producer groups towards a CPF was mixed and somewhere between the stances of the finance and labour/social welfare organisations. In the mid-1970s a small group of industrialists feared that private pension schemes might hamper labour mobility (Hong Kong Hansard, 27 October 1976). As a result, they supported the creation of a CPF for a short while. For example, LegCo member and industrialist Dr Chung as well as Mr Wu from the FHKI highlighted in 1974 and in 1976 the need to investigate the 'feasibility of establishing a central provident fund' administered by a government agency at a national level, like in Singapore (Hong Kong Hansard, 27 October 1976, p. 79; Hong Kong Hansard, 31 October 1974, p. 83). However, following Singapore's recession in 1985/1986, Hong Kong's industrial sector unanimously began to oppose the creation of a CPF (Hong Kong Hansard, 13 May 1987). Singapore's case was used by opponents of CPFs to illustrate how contribution rates to a CPF affect wage levels, and in turn, competition levels (Hong Kong Hansard, 6 November 1986, p. 359). In November 1986 employers started to openly oppose both a mandatory private-run as well as a mandatory state-run CPF (see Li, 1988). Among the most prominent industrialist organisations opposing mandatory savings schemes were the FHKI, the Federation of Hong Kong Garment Manufacturer and the CMA.

The industrial sector increasingly saw a mandatory insurance scheme, notably a CPF, as an additional imposition of costs on their production and therefore a factor affecting competition. Industrialist Ngai Shiu-Kit, stated in a LegCo debate the implication of a CPF for the whole economic development of Hong Kong. According to Ngai Shiu-Kit, 90 per cent of Hong Kong companies were small- and medium-sized (Hong Kong Hansard, 13 May 1987, p. 1562). Furthermore, it was highlighted that "[o]ver 90 per cent of [Hong Kong's] production is exported and [that Hong Kong's] products must remain price-competitive in world markets" (Hong Kong Hansard, 13 May 1987, p. 1545). A CPF would substantially increase operating costs and create obstacles for them which would impact upon the flexibility of Hong Kong's industry in general (Hong Kong Hansard, 13 May 1987, p. 1562). As a result, manufacturers neither supported the idea of creating a CPF nor the idea of creating a private mandatory scheme, since they feared that both would increase their production costs and thereby make them less competitive. Instead, they supported voluntary private pension schemes.

The CPF Review, the Social Welfare Advisory Committee and the Labour Advisory Committee

The Financial Secretary entrusted the realisation of the CPF review in 1986–87 to the Education and Manpower Branch, specifically because the issue of creating a large CPF involved both employers and employees.[167] By then it was well known that the Secretary of the Education and Manpower Branch was highly critical of the creation of a state-run CPF (Chow, 2015). The Education and Manpower Branch organised some research on the CPF issue, and officials in the Manpower Branch prepared a draft paper. According to Nelson Chow – former Chairman of the Social Welfare Advisory Committee (SWAC) – the officials of the Manpower Branch might have also consulted business associations, notably the HKGCC (Chow, 2015). Before the draft paper was forwarded to the relevant policy committees for further discussion and comment, it was convention in Hong Kong to discuss the draft paper with the Financial Secretary and the Star Chamber – a body of high ranking officials (Scott, 2010; Goodstadt, 2015). The Star Chamber was chaired by the Financial Secretary (Goodstadt, 2015). After a decision was reached, the Secretary of Education and Manpower appointed two policy committees (i.e. the Labour Advisory Committee and the SWAC) with the aim of discussing and commenting on the draft paper. Chow (2015) noted that the draft paper prepared by the Manpower Branch had a 'negative tone' with regard to the creation of a CPF, and indeed advised against it.

EXCLUSION OF LABOUR AND WELFARE

Out of the many consultative government committees only two, namely the SWAC and the LAC, were invited to comment on the draft paper prepared by the Education and Manpower Branch – as chosen by the government (*South China Morning Post*, 26 November 1986; 18 December 1986)**.**[168] Chow's statement that the "government made sure that only members [were] appointed who agree[d] with [the government]" indicates that a careful pre-selection took place (Chow, 2015). The actual composition of the committees in 1986 confirms that business representatives were systematically overrepresented (Civil and Miscellaneous Lists Hong Kong Government, 1 July 1986, pp. 103–111; Chow, 2015).

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[167] The question of whether it was the Financial Secretary, the Chief Secretary or Governor who delegated the issue to the Education and Manpower Branch cannot be completely clarified. However, it would have involved the Financial Secretary, because he was in the centre of any decision-making in Hong Kong's savings domain.

[168] The Government could have also chosen other policy bodies, such as the Consumer Council, District Boards, Pensions Assessment Board (see Civil and Miscellaneous Lists Hong Kong Government, 1 July 1986).

If social welfare and union representatives were appointed, then they were systematically outnumbered by representatives of the finance and employer side. For example, the Labour Advisory Committee (LAC) was a non-statutory consultative body, which was chaired by the Commissioner for Labour and it had 12 unofficial members. Out of these, six were supposed to represent employees and the other six were supposed to represent employers (Labour Department Hong Kong, 2014). On the employer's side, four representatives were elected from employer associations and two were appointed by the government, whereas on the employees' side, three representatives were elected from employee associations and two appointed by the government (Labour Advisory Board, 2000). While the employee representatives of the LAC supported the creation of a CPF, the employer representatives and business associations, such as the HKGCC, opposed (see Li, 1988, p. 39; *The Hong Kong Standard*, 14 December 1986; Annual Report Hong Kong General Chamber of Commerce, 1986). With six representatives on the employer side against a CPF and five representatives on the employee side pro-CPF, a decision was taken to set up another working group (*Ming Po Daily*, 12 December 1986 highlighted by Li, 1988, p. 56). This time, only finance associations were invited by the ExCo for comments on the consultation paper. These included the Life Insurance Council of Hong Kong, the Hong Kong Bank Association, and the Discussion Group on the Hong Kong Economy (*Hong Kong Standard*, 14 December 1986; Li, 1988, p. 144). The Discussion Group on the Hong Kong Economy was an informal body of economists from Hong Kong's universities. (Li, 1988; *Hong Kong Economic Journal,* 16 May 1987). There was no formal appointment of a labour or welfare associate (*Hong Kong Standard*, 14 December 1986).

According to commentators, social welfare associations and trade unions were not consulted in the later stages of consultation (*Hong Kong Standard*, 18 May 1987; *South China Morning Post*, 12 November 1987; *Ming Po Daily*, 28 May 1987; *Mau Chi Wang*, 1 December 1986). The broad scale exclusion of labour unions and welfare organisations was justified on the grounds that the CPF issue was highly complex (Li, 1988). To business actors and state representatives, the issue of creating a large state-run CPF was very complex and had important wider economic implications (Li, 1988). It was considered too important to allow unions and welfare organisations make decisions regarding the topic. Consequently, government officials concluded that the issue of creating a CPF should be approached from an economics perspective and should not be mixed up with the '[w]ishes of the people' (Hong Kong Hansard, 13 March 1987, p. 1540).

INCLUSION OF DOMESTIC FINANCE/BUSINESS

The second body involved with the investigation of establishing a CPF in Hong Kong was the Social Welfare Advisory Committee. There were very few SWAC members, and only one representative of the Hong Kong Council of Social Services, who considered the creation of a

CPF (Civil and Miscellaneous Lists Hong Kong Government, 1 July 1986; Chow, 2015). The majority view of the SWAC was against the creation of a CPF (Chow, 2015). It was feared by most of the SWAC members that a large single fund run by the government would disturb Hong Kong's financial sector (*South China Morning Post*, 17 August 1986).

Subsequently, a paper on the 'Consultation on the Implications of Establishing a CPF in Hong Kong' was released, reflecting the preferences of finance and business actors. Its focus was mainly on the downside, outlining eleven reasons against a CPF, and highlighting only six positive reasons, and even these were very vague (Hong Kong Hansard, 13 May 1987, p. 1592). For example, the paper suggested 'a CPF would remedy certain deficiencies' and thereby 'improve Hong Kong's international image' (Hong Kong Hansard, 13 May 1987, p. 1592). However, it was not specified what that meant. Interestingly, out of these six reasons, at least three were formulated in a way that implied negative consequences. For example, it was highlighted that a CPF offered a potential pool of funding for the government, but at the same time the report emphasised that this might encourage government overspending, increasing the risks of deficit. With regard to the risks and reasons against a CPF, the consultation paper was much more specific and detailed. The report argued that a CPF is 'economically damaging' because of the increase in labour costs that would destroy Hong Kong's competitiveness. Furthermore, the report highlighted that the creation of a state-run CPF was against the government's philosophy of non-interventionism. It would also pose a financial risk due to its 'massive size'. The paper concluded that "[t]he balance of the economic arguments is against the introduction of a CPF" (Hong Kong Hansard, 13 May 1987, p. 1605). In sum, a CPF would have a disturbing effect on financial markets in Hong Kong and investment into foreign asset could have disruptions on foreign exchange and money markets, which would affect the Exchange Fund and the value of the HK$. However, according to Yam, former CEO of the Hong Kong Monetary Authority, a large CPF would not have affected the Exchange Fund because a CPF, by definition, is managed centrally by the government. Here, the government would obviously not have done anything that would have affected monetary stability in Hong Kong (Yam, 2013).

The paper recommended 'An Alternative Way Forward'. This was then used by the government to justify the non-creation of a state-run CPF (Hong Kong Hansard, 13 March 1987). Policy makers were using it as a reference, and it informed their decision about whether to create a CPF (Hong Kong Hansard, 13 May 1987). By drawing on these recommendations, policy makers turned down the proposals for a CPF (Li, 1988). The report suggested relying on private banking and the financial sector for old-age security. It recommended the improvement of existing schemes such as long-service payment schemes, the protection of wages and improved regulation concerning the protection of contributions to private funds, as well as social security benefits. The recommendations of the consultation paper primarily reflected the preferences of the financial and commercial sectors. They supported decisions of allocating savings into deposits with licensed banks, unit trusts investing in financial assets, life assurance, credit unions, real property through mortgages and the stock market (Hong Kong Hansard, 13 May 1987).

DEBATES OVER POLICY CHOICES IN THE 1980s

During the 1980s, the structure of state-society relations in Hong Kong's savings domain was reflected in public debates. Finance and business actors have spoken with a unified voice against the creation of a CPF, whereas labour and welfare associations spoke with multiple voices for the creation of a CPF. Supporting the creation, the social service and union sector formulated a number of different proposals suggesting such a creation. However, the timing of the publications, as well as the content of the proposals and position papers, were not well coordinated. The Hong Kong Council of Social Services was among the first welfare organisations in 1984 suggesting the creation of a CPF, under the management of a financial organisation appointed by government (Li, 1988, p. 133). The Federation of Trade Unions proposed the establishment of a compulsory CPF scheme, or "a Central Provident Fund Bureau or a statutory body with participation from employees, employers and government" (Li, 1988, p. 105, referring to the HKFTU report). Other proposals came from ad-hoc coalitions between labour and social workers organisation, such as the Democracy and People's Livelihood and the Hong Kong Affairs Society and the Joint Conference for the Establishment of a Central Provident Fund (*Hong Kong Standard*, 13 May 1987; Li, 1988). The Joint Conference published an informal Green Paper where they highlighted their support for a comprehensive insurance scheme rather than a CPF (see Li, 1988, p. 107). The Christian Industrial Committee, the Federation of Trade Unions and the Hong Kong Social Worker's General Union supported the creation of a compulsory CPF for firms with at least 10 employees, and a statutory management board that is doing the monitoring (*South China Morning Post*, 18 December 1986).

Due to this fragmented approach, the government paid little attention to the demands of social welfare organisations and labour unions. In turn, social welfare organisations and labour unions criticised the structural linkages in Hong Kong's savings domain. For example, Rosanna Wong – LegCo representative for Hong Kong's social work constituency – highlighted her discomfort with the structural linkages in the policy making process. Wong's statement that the government "turned a deaf ear to the labour sector's request to have the document published and to enlarge the scope of consultation" indicates that policy makers were drawing on arguments and information which supported the preferences of Hong Kong's finance and business sector (Hong Kong Hansard, 5 November 1987, p. 358). They accused the government of a consultation bias by highlighting the government's overemphasis of the points made by finance and business associations (*Hong Kong Standard*, 18 May 1987; *Ming Po Daily*, 28 May 1987; *Mau Chi Wang,* 1 December 1986). Labour and welfare associations heavily criticised the composition of the two consultation bodies and the working group formed by the government and suggested the formation of a 'Legislative Council Select Committee', that is open to the public (Hong Kong Hansard, 13 May 1987, p. 1560).

The first large-scale public discussion with a focus on the creation of a CPF took place in the mid-1980s.[169] It started formally in September 1985 when two functional LegCo constituencies for labour demanded the creation of a CPF (Li, 1988). While the labour and welfare sector highlighted their support, domestic finance and business actors were heavily in opposition. The latter had repeatedly expressed disapproval for a state-run centralised savings scheme (see Hong Kong Hansard, 5 November 1986; 13 May 1987; 3 February 1993). They feared that a CPF could interfere with the business of private domestic finance institutions, and argued that this would have major distributional consequences. For example, the representative of the banking sector in the LegCo and chairman of the Bank of East Asia, David Li, highlighted this on several occasions. Li's statement that "the concept of a central provident fund operated by the Government is completely contrary to Hong Kong's basic economic philosophy" indicates private banks' antipathy towards a government-run CPF (Hong Kong Hansard, 13 May 1987, p. 1561). Instead, domestic finance actors highlighted their support for decentralised private mandatory savings schemes (Hong Kong Hansard, 13 May 1987, p. 1561).

Commerce, together with industry, promoted the idea that savings schemes should be private, and that the government should use tax incentives and encourage the private sector to set up provident funds (Hong Kong Hansard, 13 May 1987). According to industry and commerce the creation of a mandatory state-run CPF would have an effect on economic activity and would result in a substantial decline in consumption (Hong Kong Hansard, 5 November 1986, p. 327). It was feared that private consumption would drop by the amount of funds that would be allocated to a mandatory state CPF. Based on the assumption that employees and employers contribute 5 per cent of their wages/salaries to the CPF every month this would have accounted for approximately HK$9 bn each year given an average salary of HK$3,000 per month. This number was compared with Hong Kong's general revenue for the fiscal year of 1986, which was about HK$39 bn. It was feared that this "mammoth sum" in a CPF would have decreased the money supply in circulation, and would have affected consumption (Hong Kong Hansard, 5

[169] However it should be noted that some discussions regarding the creation of a state-run CPF took place repeatedly from the late 1960s onwards. Following large-scale domestic riots in 1967, the discussions started as a means of improving social security among the population and introducing old-age security.

November 1986, pp. 326–327). Commerce representatives, such as Ho Sai Chu, feared that huge sums of money concentrated in the hands of government would affect economic activity in Hong Kong, and that government investment decisions would interfere with the market mechanisms (Hong Kong Hansard, 13 May 1987, p. 1550).

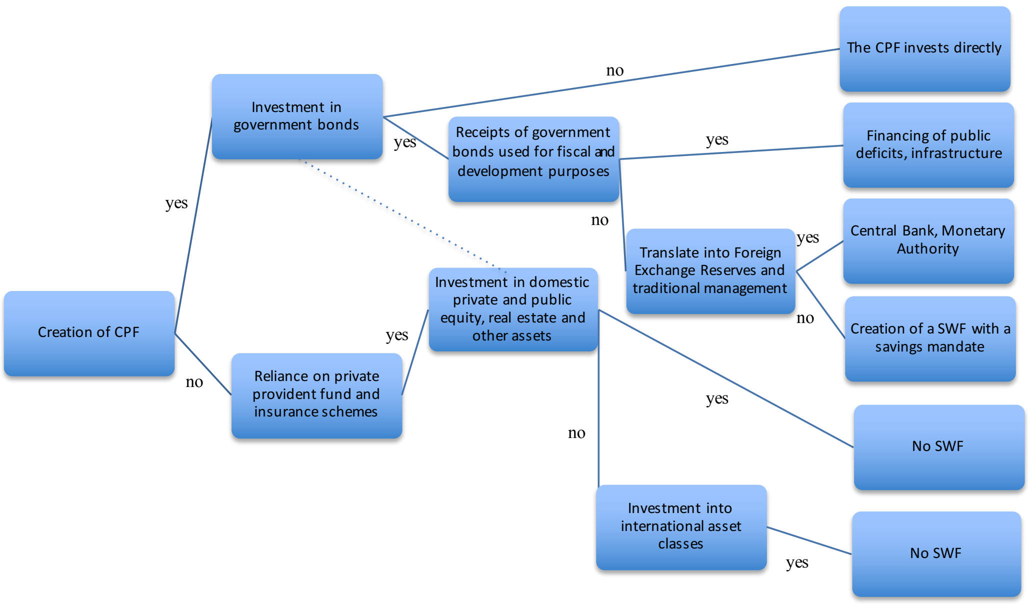
Business actors argued that there was no need for a mandatory state-run CPF because many firms had already started introducing private voluntary pension schemes (Hong Kong Hansard, 3 February 1993). Industrial representatives broadly shared a similar argument (Hong Kong Hansard, 3 February 1993, p. 1757). Hong Kong's large industrial associations, notably the FHKI and the CMA, perceived the creation of a CPF as an introduction of a new tax (Hong Kong Hansard, 13 May 1987, p. 1547). They argued that a CPF would substantially add to their production costs, rendering them uncompetitive. Industrial representatives in the LegCo repeatedly outlined their position against a CPF. They argued that the majority of Hong Kong companies – in relative and absolute terms – were small and medium sized, therefore a CPF would substantially increase operating costs and create obstacles for them, which would impact the flexibility of Hong Kong's industry in general (Hong Kong Hansard, 13 May 1987, p. 1562). For instance, industrialist Cheong Kan-Chuen's statement that a "[CPF] is no more than forcing personal savings into a pool of savings to be run and controlled by the state, thereby freezing the used of such resources until 20 to 30 years later" highlights the industrial sector's discomfort with mandatory provident fund schemes (Hong Kong Hansard, 13 May 1987, p. 1542).

The business and finance sector's broader view was shared by key policy makers, notably the Financial Secretary, the Secretary for Health and Welfare as well as the Secretary for Manpower. They problematised the potential redistributive risks associated with a state-run mandatory savings scheme. The Secretary for Health and Welfare highlighted that "the term 'Central Provident Fund' implies a centralised scheme run by a government department or a statutory authority on the lines of the Singapore provident fund" (Hong Kong Hansard, 13 May 1987, p. 1586). In the debate, Hong Kong's government was drawing on business and finance sector arguments that a CPF would create adverse market effects. For example, the Financial Secretary and the Secretary for Education and Manpower openly supported finance and business positions by highlighting the potential redistributive impact of a centralised CPF with its effects on the flows of funds among financial institutions (Hong Kong Hansard, 13 May 1987). The Financial Secretary's comment that "[a state run centralised] CPF, could also have a redistributive effect on the flows of funds between financial institutions [and] this could cause problems for the banking sector, especially for those smaller local banks which rely heavily on local deposits" draws attention to the concern of policy makers over the creation of state finance institutions in the savings domain (Hong Kong Hansard, 13 May 1987, p. 1581). In line with the preferences of domestic private finance, the Financial Secretary supported the financial sector's suggestion of creating private decentralised provident fund schemes (Hong Kong Hansard, 13 May 1987). The government thought that this would allow room for domestic business to remain competitive, while allowing Hong Kong's private finance sector to make a profit (Yam, 2013). In a similar fashion, the Secretary for Health and Welfare supported this argumentation by noting that families in Hong Kong could cope with an ageing population, and therefore would not need a CPF (Hong Kong Hansard, 13 May 1987).

POLICY CHOICES MADE IN THE 1980s

Policy makers opted against the creation of a state finance institution (i.e. CPF). The formal decision to not create a CPF was made on the 7th October 1987 in a policy speech by Hong Kong's Governor (*Hong Kong Standard*, 8 October 1987). Instead of creating a large state run CPF, and as a consequence an SWF channelling CPF funds into long-term international financial assets, the choice was made to rely on private finance institutions that invested into domestic private and public equity as well as into real estate and other assets (see FIGURE 7.1.).

FIGURE 7.1. Decision making Model on the Link between CPF and SWF.



Hong Kong's policy makers decided to support private finance institutions in the savings domain, such as domestic commercial banks, registered deposit-taking companies and private insurers (McCarthy, 1982). This included the promotion and support of private provident fund schemes and bank deposits with private commercial banks in Hong Kong. As a result, every month approximately 50 new private pension schemes were approved (Hong Kong Hansard, 13 May 1987, p. 1537). Reflecting this, the number of approved private provident fund schemes increased dramatically from 540 in 1970 to 4,105 in 1986 (Li, 1988, p. 71, taken from *Hong Kong Economic Journal,* 27 August 1988). In the 1980s these covered around 300,000 workers (Hong Kong Hansard, 13 May 1987, p. 1537).

The choice against creating a CPF favoured domestic commercial banks, which started to introduce private provident funds and life insurance schemes. Commercial banks started to enter the life insurance sector either directly or through alliances (see TABLE 7.4). For example, the Hong Kong Bank formed its own insurance subsidiary Carlingford, which also uses the Hong Kong Bank's branch network (Yeung Chak-sze, 1990). Another example is the Bank of China Group which had alliances with Ming An, China Insurance and Tai Ping. The Bank of China Group asked its mortgage customers to insure with them (Yeung Chak-sze, 1990). The Hong Kong Bank introduced a new provident fund in 1976 which was "open to all companies whether or not they [were] customers of the Bank" (*South China Morning Post*, 23 March 1976). The Hong Kong Bank and Swire formed a new partnership known as Wardley Swire Assurance, which provided services on retirement and pension schemes for Hong Kong, and managed these funds (*Hong Kong Standard*, 14 September 1976).

TABLE *7.4. Strategic Alliance of Banks and Insurance Companies of Hong Kong in the 1990s.*

Name of Banking Group	**Major Insurers**
The Hongkong & Shanghai Bank	Carlingford
Bank of China Group	Ming An, China & Tai Ping
Hang Seng Bank	Associated Bankers & Unions Ins.
Standard Chartered	AIU & Cigna
Bank of East Asia	AIU, Lombard & Ming An
Dao Heng Bank Group	Dao Heng Insurance
Overeas Trust Bank	OTB Assurance
Shanghai Commercial Bank	Paofoong Insurance
Bank of Credit & Commerce	Commercial Union
Dah Sing Bank	Tugu
Citi-Bank	Eagle Star
Liu Chong Hing	Liu Chong Hing Insurance
Kwong Chong Hing Kwong On Bank	Sumitomo Insurance
Ka Wah Bank	Ka Wa Amev Insurance
First Pacific Bank	Far East Insurance

Source: Yu (1997, p. 90).

There was, however, no formal government deposit insurance in place, which would have protected the people's savings in a banking crisis. Domestic savings were channelled via domestic finance institutions into Hong Kong's domestic system, specifically into a booming property sector, and from the 1970s, into Hong Kong's stock market (Goodstadt, 2007; McCarthy, 1982; Tomkins, 1962; Wong, 1991, p. 217). A Bank of England report in the 1960s already noted an over-exposure of Hong Kong's banks to the domestic real estate market (Tomkins, 1962, p. 8). Furthermore, more than 98 per cent of life insurance assets were allocated to domestic financial assets, as well as in cash and deposits stocks (Yu, 1997, pp. 79–80).[172] Given Hong Kong's reoccurring banking and stock market crises as well as its real estate bubbles, this was a highly risky undertaking.

CONCLUSION

The chapter argues that a PN analysis helps explain why Hong Kong choose not to create state finance institutions with savings mandates between the 1960s and 1980s. Over this period, pressure to create a large state-run mandatory CPF, and an SWF investing CPF funds into global asset classes were present. Instead, Hong Kong's policy makers chose to rely on commercial banks and to support the creation of private pension funds and insurance schemes, channelling significant parts of the savings into domestic assets. This was the result of a review that was influenced by Hong Kong's clientele pluralist PN. The cross-national and cross-domain comparison with Singapore indicates the effect of the clientele pluralist PN, in which a highly-mobilised domestic finance and business sector, together with a centralised state, influenced debates as well as policy-making processes and choices.

The case of Hong Kong adds to the findings from Chapter 6 by highlighting the distributional struggles involved in the debates and the policy-making processes. Furthermore, the case has suggested the limited role played by efficiency and diffusion in affecting the kinds of financial institutions set up in Hong Kong's savings domain. Unlike diffusion- and efficiency-based accounts, what a PN analysis highlights is that even with small open economies, domestic structures matter in terms of what occurs in policy-making processes.

The first section (7.1) on economic inheritance outlined domestic constraints and pressures to which Hong Kong was exposed between the 1960s and 1980s. Over this period Hong Kong's increasing levels of savings were exposed to a number of risks, notably inflation as well as

[172] Given an 80 per cent local asset maintenance rule, this meant that domestic finance actors had the possibility of allocating the 18 per cent differential into international assets (Yu, 1997, pp. 79–80).

domestic stock market and banking crises. A lack of welfare and social security together with questions of how to preserve future purchasing power placed pressure on Hong Kong's policy makers. The second part (7.2) looked at key socio-economic actors in Hong Kong's savings domain and the type of PN. Structural linkages among actors in that domain referred to a clientele pluralist PN. It was characterised by high concentration of power within the state apparatus and low levels of autonomy from the finance/commerce sector, which was highly mobilised.

The third part (7.3) analysed policy-making and Hong Kong's clientele pluralist PN in operation. Debates revealed that at the time there were alternatives available, notably the creation of a large state-run mandatory CPF. This choice was supported by labour unions, welfare groups and grassroots organisations. By contrast, state actors, domestic finance and business shared broadly similar views. Common to them was their support of private institutions in the savings domain. The chapter examined the actors included and excluded on the policy processes, and thereby discovered that because of the structural linkages in place, only finance and business actors were able influence the kinds of financial institutions set up.

8. The Effects of Policy Networks on Sovereign Wealth Funds in Other Small Open Economies: Kuwait, Abu Dhabi and Qatar

This chapter offers a plausibility probe for the explanations developed in the earlier chapters. It investigates whether the expectations derived from small open economies in Asia also hold in other cases. This, in turn, helps to judge whether further testing of the hypotheses developed in the previous chapters is warranted. Similar to the previous chapters, the present chapter does not investigate why some countries had particular policy networks (PNs) in place, as this would have required a different research design.

The chapter looks at additional empirical evidence from small open economies in a different part of the world. Small open Gulf economies offer further evidence on the impact of state-society relations on the kinds of financial institutions set up. Between the 1960s and the 1970s most of the small open Gulf economies became independent, and were confronted with windfall hydrocarbon revenues. They adopted different kinds of financial institutions in their industrial and savings domains. The finite nature of hydrocarbon resources has raised questions of diversification and securing future rents. Because of their high dependence on hydrocarbon exports, small open Gulf economies have been highly exposed to demand and supply shocks. Fluctuation of oil income has been translated into budget volatility.

Between the 1960s and the 2000s, small open economies in the Gulf offered interesting variation in terms of policy network (PN) types and sovereign wealth fund (SWF) types (see TABLE 8.1 and TABLE 8.2). Qatar's and Abu Dhabi's industrial domains have been characterised by SWFs with development mandates (e.g., Qatar Holding and Mubadala), corresponding to their state-directed PNs in place. Similarly, the creation of large SWFs with savings mandates (e.g., the Qatar Investment Authority and the Abu Dhabi Investment Authority) reflected the state-directed PNs in place. This thesis is aware, however, of definitional difficulties with respect to the term 'state' in GCC economies, such as those of Abu Dhabi and Qatar. In these economies, policy makers and state business entrepreneurs have often come from the same families (Herb, 2014). It is therefore difficult to differentiate between the effects of PNs and those of kinship networks. To do so would require a greater degree of in-depth investigation and process-tracing.

In contrast to Abu Dhabi and Qatar, state-society relations in Kuwait's industrial domain were characterised by highly mobilised merchant and trade organisations and a fragmented state apparatus with low levels of autonomy. This represented an industry dominant pressure pluralist PN (see Atkinson and Coleman, 1989). Reflecting this, no SWF with a development mandate was established in Kuwait. Interestingly, Kuwait created an SWF with a savings mandate (i.e. the Kuwait Investment Authority) and had a concertation PN in the savings domain. Like state-directed PNs, concertation PNs refer to state-society relations that are characterised by highly centralised decision-making structures and high levels of state autonomy from the business sector. But in contrast to state-directed PNs, in concertation PNs, segments of the business sector are highly mobilised.

TABLE 8.1. *Types of Policy Networks in Kuwait, Abu Dhabi and Qatar following their independence from Britain.*

Domains	**Kuwait** (1960s–2000s)	**Abu Dhabi** (1970s–2000s)	**Qatar** (1970s–mid-1990s)	**Qatar** (mid-1990s–early-2000s)
Industrial	Industry dominant pressure pluralism	State-directed	Pressure pluralism	State-directed
Saving	Concertation	State-directed	State-directed	State-directed

TABLE 8.2. *SWF types in Kuwait, Abu Dhabi and Qatar following their independence from Britain.*

Domains	**Kuwait** (1960s–2000s)	**Abu Dhabi** (1970s–2000s)	**Qatar** (1970s–mid-1990s)	**Qatar** (mid-1990s–early-2000s)
Industrial	n/a	Mubadala, International Petroleum Investment Corporation; Abu Dhabi Investment Corporation	n/a	Qatar Diar, Qatar Holding
Saving	Kuwait Investment Authority	Abu Dhabi Investment Authority	Qatar Investment Board	Qatar Investment Authority

This chapter finds that much of the relevant politics regarding the creation of SWFs among GCC countries happened during the pre-independence and early post-independence period. Interestingly, the issue of creating state finance institutions in Kuwait's industrial domain came up when state autonomy declined in Kuwait but remained high in Abu Dhabi and Qatar (Hertog, 2010; Herb, 2014). This draws attention to a more general focus on state autonomy and the need to widen the discussion of interest-group politics beyond state-business relations and also to include the role of popular constituencies (see Hertog, 2010). According to Herb's piece, 'A nation of bureaucrats: political participation and economic diversification in Kuwait and the United Arab Emirates', popular interests have prevented targeted industrial diversification in Kuwait (Herb, 2009). He argues that the difference between Kuwait and other GCC economies is the reduced level of policy autonomy imposed, not by business, but by parliament and the middle class (Herb, 2009). In line with Herb (2009), Hertog (2013a) describes Kuwait as a participatory rentier state where citizenry selects parliament and where the parliament has important veto powers over policy decisions. In contrast, popular interests have little influence in Abu Dhabi's and Qatar's policy-making structures (Herb, 2014). This observation is also supported by Hertog (2013a), who refers to Abu Dhabi as an authoritarian rentier state where citinzry has less influence on economic policy. This suggests the need to account for general differences in the degree of state autonomy between GCC countries when analysing the impact of state-society structures on policy making.

The chapter starts by looking at the small open GCC economies' common background in terms of their history and in terms of their macroeconomic context. This is followed by three subsections which outline Kuwait's, Abu Dhabi's and Qatar's state-society relations in the savings and industrial policy domain, and the kinds of financial institutions set up in the period from the 1960s until the 2000s.

8.1 COMMON BACKGROUND

Kuwait, Abu Dhabi and Qatar share a number of similarities in terms of their macroeconomic features, most notably, their size and dependency on oil/gas (see TABLE 8.3). With oil and gas earnings contributing on average between 60 and 70 per cent of total revenue among small open Gulf economies, government spending has fluctuated in line with energy prices. Due to their high economic openness and reliance on resource extraction, small open Gulf economies have been similarly exposed to international business and commodity cycles. A significant drop in oil prices, specifically in the mid-1980s and early-1990s, was translated into major reductions in oil revenue and led to tensions on public expenditure in 1980s and 1990.

TABLE 8.3. *Macro-characteristics Qatar, Kuwait, UAE in the years between 2008–2013.*

	Qatar (2009)	**Kuwait** (2013)	**UAE*** (2008)
GDP (in US$ bn)	95.7	148.4	222.0
GDP per head (in US$)	61,567	41,381	39,421
GDP per head (in US$ at PPP)	58,221	40,826	36,371
Consumer price inflation (average %)	15.1	11.0	14.4
Current-account balance (in US$ bn)	18.5	58.8	29.6
Current-account balance (% of GDP)	19.3	39.6	13.3
Exports of goods (fob in US$ bn)	56.9	88.2	200.4
Imports of goods (fob in US$ bn)	-24.7	-26.1	-141.1
External debt (in US$ bn)	54.3	38.6	73.7
Debt-service ratio, paid (%)	5.2	2.6	1.8

Source: Compiled from various reports, notably the EIU (2008, 2009, 2009a, 2013).
*There are no precise public data available for Abu Dhabi.

Between the 1950s and 2000s, small open Gulf economies experienced similar developmental trajectories from poverty to prosperity. Before the oil boom of the 1960s and 1970s most of the economic activity took place in the trade and pearl fishing sector (Crystal, 1990). Following the oil boom in the 1970s, most of the small open Gulf economies embarked on ambitious diversification programmes in order to address the finiteness of oil reserves and demographic pressures. High levels of welfare spending and infrastructure projects among small open Gulf economies have been financed with surging oil/gas revenues (Said Zahlan, 1989). Being among the fastest growing economies in the world Kuwait, Abu Dhabi, and Qatar have attracted a migrant inflow from the West and from Asia – resulting in large expatriate communities. With the finding and exploitation of oil/gas, small open Gulf economies were confronted with transformation. The discovery of large oil deposits took place in Kuwait from the 1930s onwards, in Abu Dhabi from the 1960s onwards and in Qatar from the 1960s onwards. Compared to its peers, Qatar can be described as a "modest producer of crude oil" (Ibrahim and Harrigan, 2012). However, Qatar has significant gas reserves, which it started to exploit from the late 1990s onwards.[173]

Kuwait, Abu Dhabi and Qatar were former British protectorates, and gained independence in the period between the 1960s and the 1970s. They share a strategic location in the Persian Gulf, one of the major energy transport routes in the world. They do not possess significant agricultural sectors. They have all been governed by strong rulers. These rulers stem from privileged and powerful domestic tribal clans, including the Al-Thani family in Qatar, the Al-

[173] The potential of the North Field discovered in 1971 – the world's largest non-associated gas reservoir – was unlocked more than 20 years later with the first liquefied natural gas shipment to Japan (Ibrahim and Harrigan, 2012, p. 2).

Sabah family in Kuwait, and the Al-Nahyan family in Abu Dhabi. In Kuwait, Abu Dhabi and Qatar, resource wealth has been controlled by the ruling families, and natural resources have been significant contributors to public finance (Said Zahlan, 1989).

Before independence, the rulers of these territories had bank accounts, specifically with private British banks, through which they channelled their oil/gas royalties. For example, Abu Dhabi held its cash reserves with the British Eastern Bank and the British Ottoman Bank (Foreign Office, 1970; Ottoman Bank, 2014).[174] Likewise, the ruler of Kuwait had a bank account with British Lloyds Bank in London through which oil revenues were channelled (Eastern Department, 1952). Also, the ruler of Qatar held accounts with the Eastern Bank, and later with the British Bank of the Middle East and the Ottoman Bank (Qatar Monetary Agency, 1985). From the late 1960s onwards the Qatar National Bank (established 1965) had started to act as the government's bank (Qatar Monetary Agency, 1985, pp. 10–11).

With the proliferation of wealth in the Middle East, other foreign banks, notably from the US, became increasingly interested in competing for domestic deposits with British banks. Private investment firms stepped up their lobbying efforts in an attempt to manage parts of the accumulated wealth in the Middle East (Eastern Department, 1952, EA1112/56; FCO 181 2215). Kuwait's, as well as Abu Dhabi's, ruling elite was willing to switch large sums to international banks offering higher returns (Foreign Office, 1970). Specifically, US banks were intensively lobbying for permission to set up domestic branches, and to get in touch with local rulers. For example, Kuwait's government opened its first dollar portfolio of equities and convertibles with the US First National City Bank (*The Financial Times*, 25 February 1976). Britain was well aware of these developments and Britain's economic advisor to the Kuwait government feared that the oil revenues could be spent on 'doubtful projects' (Arabian Department, 1960).[175]

However, with the progressive accumulation of wealth among British Middle Eastern protectorates, Britain became increasingly concerned with the allocation of royalties and the lack of differentiation between public and private wealth among the rulers (Eastern Department, 1952, EA1112/52; FCO 758 559). As a result, Britain promoted the creation of investment boards in Kuwait and Abu Dhabi. The Kuwait Investment Board (est. 1953) and the Abu Dhabi Investment Board (est. 1967) were the predecessors of Kuwait's and Abu Dhabi's SWFs.

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[174] The British Eastern Bank became known as the Standard Chartered Bank, and the British Ottoman Bank became the Grindlays Bank.

[175] Dr Shehab, attached to the University of Oxford was employed by the Kuwait Government as an economic advisor. In a dossier to the Arabian Department (1960), Shehab highlighted that "there is reliable evidence that there are many private financiers in the field only too anxious to divert some of the Kuwait's wealth to themselves and to doubtful projects and who on present form are only too likely to get a hearing in Kuwait" (Arabian Department, 1960).

However, the Kuwait Investment Board of 1953 and the Abu Dhabi Investment Board of 1967 were not yet modern SWFs (i.e. the Kuwait Investment Authority and the Abu Dhabi Investment Authority). The Kuwait Investment Board, for example, was a British run account, which was established by the British government to minimise risks linked to oil income and to efficiently manage this income. It involved five British bankers, chaired by the Director of the Middle East Department at the Bank of England (Bazoobandi, 2013, p. 37). Interestingly, the Kuwait Investment Board had no limitations regarding exclusive investment in sterling assets (Foreign Office, 1970). The Abu Dhabi Investment Board was created in 1967 under the Abu Dhabi Department of Finance and its headquarters was in London under the mandate of UBS, Robert Fleming, Morgan Guaranty Trust and Indosuez (ADIA, 2009). The appointment of the members of the board of directors of the Abu Dhabi Investment Board was made by the Emir in consultation with the Bank of England. The Abu Dhabi Investment Board's board consisted of two British citizens, one US citizen, one European and only one citizen from Abu Dhabi. Despite some similarities between the Kuwait and the Abu Dhabi Investment Board it is worthwhile to emphasise the differences with regard to the time of creation and to the structure of both entities.[176]

8.2 KUWAIT'S POLICY NETWORKS AND THE KIND OF FINANCIAL INSTITUTIONS SET UP AFTER INDEPENDENCE IN 1961

The comparative analysis of the Kuwait Investment Authority (KIA) broadens the hypothesis derived in earlier chapters (i.e. that SWFs with savings mandates are more likely to emerge in savings domains that are governed by state-directed PNs). It finds that the savings domain in Kuwait was governed by a concertation PN. Similar to a state-directed PN, a concertation PN is characterised by high levels of concentration in decision-making power and high levels of autonomy. Despite high levels of autonomy from business, Kuwait's state autonomy was reduced at a more general level by universal suffrage as well as by free and fair elections (Herb, 2009; Hertog, 2013). Herb's statement that "[i]n Kuwait the parliament challenges the political predominance of the ruling family" suggests a strong parliament (Herb, 2009, p. 375).

[176] An official statement from the British Foreign Office that "[t]he analogy with Kuwait should not be pressed too far but it may be mentioned that, whereas in Kuwait the establishment of a sterling Investment Board in 1953 was followed ten years later by the appointment of an international Advisory Committee to deal with reserve investment policy as a whole, Abu Dhabi is to have at the outset a Board with members appointed from outside the Sterling Area" indicates little evidence for a diffusion argument (Foreign Office, 1970).

The creation of the KIA offers strong support for an efficiency argument, which would expect the creation of such an SWF. Given that surpluses were large enough it would be a logical move to create such a fund in order to address intergenerational issues and the concern about the Dutch Disease. However, a diffusion argument has difficulties to explain the creation of the KIA because Kuwait was the first country, which created a SWF with a saving mandate in the Gulf. As such, there was no place for emulation or policy learning from a GCC peer.

Interestingly Kuwait decided against creating an SWF with a development mandate, which is in line with the hypothesis developed in previous chapters (i.e. that SWFs with development mandates are less likely to emerge in industrial policy domains governed by pluralist PNs). In such PNs state decision making structures are fragmented with low levels of autonomy. This combined with a highly- mobilised merchant and trade sector hampered the creation of an SWF. Both diffusion as well as efficiency-based explanations have difficulties to explain Kuwait's choice against creating an SWF with a development mandate. A supporter of an efficiency argument would expect the creation of such an SWF in Kuwait for addressing issues of diversification and development. Likewise a supporter of a diffusion argument would expect the creation of such an SWF because all of Kuwait's peers were confronted with the problem of economic diversification and responded with the creation of SWFs with development mandates.

By highlighting cross-domain differences and re-distributional conflicts among socio-economic actors, this section indicates that PNs had an independent impact on the types of financial institutions set up. Different preferences among socio-economic actors towards the types of financial institutions set up in Kuwait's savings domain indicate distributional conflicts. For example, there were conflicts of interest between Kuwait's commerce community and Kuwait's finance community. While the Kuwait Chamber of Commerce and Kuwait's merchants broadly supported the creation of an SWF, domestic private investment houses and finance firms were highly critical of the Kuwait Investment Authority (R. Al-Rabah, personal communication, 23 September 2014). They complained that Kuwait's SWF was crowding out domestic fund management and as a result they repeatedly demanded that the Kuwait Investment Authority should invest more in the Kuwait Stock Exchange in order to support or re-enforce the domestic market (Al-Rabah, 2014).[177] However, the initial analysis suggests the need to treat state autonomy at a more general level and thereby to take account of popular interests.

[177] These points were specifically highlighted by representatives from private Kuwait finance houses such as KFH Investment and the chairman of the Kuwait Economic Society (Anonymous, personal communication at the LSE Kuwait Programme Workshop in Kuwait, 22 September 2014).

CONCERTATION POLICY NETWORK IN THE SAVINGS DOMAIN AND THE KUWAIT INVESTMENT AUTHORITY

Between the 1960s and the 2000s, the characteristics of state-society relations in Kuwait's savings domain were consistent with that of a concertation PN. As mentioned in Chapter 3, this type of PN refers to a state-society structure in a policy domain in which the state decision-making structure is highly centralised and autonomous officials stand vis-à-vis a highly mobilised segment of the business sector. This facilitates direct negotiations between the state and the respective business sector, by means of which the state seeks to accommodate the interests of this group within its broader agenda (Atkinson and Coleman, 1989, p. 58). As in a state-directed PN, the state possesses high levels of policy autonomy from business, and power concentration allows the adoption of a long-term view concerning state finance institutions.

The concertation PN influenced the logic of policy-making in Kuwait's savings domain. It allowed the pursuit of long-term-oriented policies, which integrated the interests of Kuwait's merchants into its broader agenda, characterised by high levels of state involvement and coordination. The Finance Department, later renamed the Ministry of Finance, was Kuwait's dominant state agency, and it had significant autonomy from Kuwait's private sector (Moore, 2002). Nearly all banks, except the National Bank of Kuwait, were established in the period after 1960. Apart from the National Bank of Kuwait, which was established by domestic merchants with the support of the ruler, other banks were established with significant state involvement (NBK, 2015).[178] The state's dominance was reflected in the Kuwait Banking Association – formerly the Kuwait Banking Committee (est. in 1981) – which served as a coordination body. Kuwait's ruling family was directly represented on the Board of the Kuwait Banking Association. The principal objective of the Kuwait Banking Association was the coordination of members' activities "within the framework of the state's plans, and economic and monetary policies" (Kuwait Banking Association, 2014).

At the same time, leading merchant families in Kuwait had stakes in local banks through their shareholdings and board positions. Bankers, merchants and industrialists came from the same families (Herb, 2014). They held important positions within Kuwait's legislative and executive apparatus and the Kuwait Chamber (Al-Dekhayel, 2000). The Kuwait Chamber had been hierarchically organised and functioned as a lobbying, expertise, and coordination platform for private business organisations. It was formed in 1961, and it has been the only chamber in Kuwait since. It represents all private companies in Kuwait (Al-Rabah, 2014). The Chamber comprises public relations and foreign relations departments. It also monitors import licenses

[178] Out of Kuwait's five largest banks in terms of assets, the state of Kuwait holds more than 15 per cent share in three (i.e. Kuwait Finance House 32.58 per cent, Gulf Bank 17.60 per cent, Burgan Bank 60.99 per cent) (Limam, 2001, p. 6).

and conducts the public contract bidding through an executive board and it has indirect linkages to one of Kuwait's main newspapers (Moore, 2002).[179] In strong contrast to other small open Gulf economies, notably Qatar, the ruling family is absent from the Kuwait Chamber of Commerce (Crystal, 1990). The Kuwait Chamber of Commerce is represented on all major economic policy bodies via appointments to committees (Al-Rabah, 2014). These committees allow private business to interact with the state in private (Moore, 2002).

Reflecting this, Kuwait created an SWF with a savings mandate. Preparing for independence from Britain, in 1960 it established the General Reserve Fund. The General Reserve Fund was the main treasurer for the Kuwait government. It "received all revenues (including all oil revenues) from which all state budgetary expenditures were paid" (Bhagat, 2009, p.287). Immediately after independence, Kuwait established a separate investment committee in the Kuwait Department of Finance, and it created the Kuwait Investment Office in London (Bazoobandi, 2013). The Kuwait Investment Office had the purpose of replacing the British-run Kuwait Investment Board (Bazoobandi, 2013). The institutional foundations for the KIA were already laid before the period of mass political mobilization (see Herb, 2014). As such it seems that Kuwait's parliament as well as middle class politics were irrelevant in the creation process of Kuwait's savings SWF.

Since its creation in 1953, the Kuwait Investment Board had been highly unpopular with Kuwait's leadership, because of Britain's influence on Kuwait's asset allocation and 'a perceived' low return (Eastern Department, 1954). This was well known among the British leadership. An official statement that "[the Kuwait Investment Board's] investment policy is widely thought to be directed by the United Kingdom and is bound to be unpopular with the Kuwaitis, who expect at least 12 per cent [return]" draws attention to the motivation behind Kuwait's creation of SWFs (Eastern Department, 1954). Via its newly established SWF, Kuwait acquired a number of international property portfolios from the 1960s onwards. Kuwait's equity portfolio was managed by the Kuwait Investment Office and via the General Reserve Fund, which also allocated portfolios to external managers, such as the First National City, Chase Manhattan, Deutsche Bank, the Dresdner Bank (which organised the deal with Daimler AG) and the Swiss Bank Corporation (*The Financial Times*, 25 February 1976). Furthermore, Kuwait's SWF drew heavily on external organisations and management, such as Chase Manhattan, Bank of America and Morgan Guaranty to manage portfolios and investment deals (*The Financial Times*, 25 February 1976).

[179] Private organisations with strong affiliations to the Chamber started a national newspaper, 'Al-Qabas', in the 1970s (Moore, 2002). Four of five original investors of this newspaper sat on the board of the Kuwait Chamber of Commerce (Moore, 2002).

In the aftermath of Kuwait's nationalisation of oil companies in 1974/75, reserves increased substantially from about US$3 bn at the end of 1973 to about US$12 bn at the end of 1975 (*The Financial Times*, 25 February 1976, p. 21). The Crown Prince of Kuwait issued Law No.106, which was the legal basis for the creation of the Future Generations Fund. Article 2 of the law stated: "A special account shall be opened for creating a reserve that would act as an alternative to oil wealth." According to this law, 50 per cent of the assets of the General Reserve Fund were transferred to the newly created Future Generations Fund. In addition, the Future Generations Fund annually receives 10 per cent of all state revenues, and it receives the entire fund investment income (Bazoobandi, 2013, p. 35; Bahgat, 2010). The Future Generations Fund keeps all its assets outside Kuwait. Part of the Future Generations Fund is managed by the Kuwait Investment Office in London (Roberts, 2011, p.100). As of 1976, Kuwait invested in equity portfolios across France, Belgium, the Netherlands and Japan through large banks or investment companies in these respective countries (*The Financial Times*, 25 February 1976). *The Financial Times*' statement that "[Kuwait] has concentrated on developing large and powerful national financial institutions, which will handle the placing and investment of its own enormous funds abroad" draws attention to the government's effort towards international diversification (*The Financial Times*, 25 February 1976, p. 19).

Following the second oil shock in the late 1970s, and a drop in oil prices in the early 1980s, Kuwait started to consolidate separate government funds and investment entities (i.e. the Kuwait Investment Office, the General Reserve Fund and the Future Generations Fund) under the umbrella of a newly created entity (i.e. the Kuwait Investment Authority). The major aim behind this was to introduce a more sophisticated management and better co-ordination of Kuwait's reserves (Bazoobandi, 2013). The Kuwait Investment Authority took over the responsibilities of the Ministry of Finance in managing Kuwait's assets. As such, the Kuwait Investment Authority is the parent of the Kuwait Investment Office, the General Reserve Fund and the Future Generations Fund. The Kuwait Chamber of Commerce is highly supportive of the KIA and is also deeply integrated into the KIA's governance framework (Al-Rabah, 2014). For example, two members of the chamber's board of director sitting on the board of directors of the KIA (Al-Rabah, 2014).

However, the Kuwait Investment Authority does not own assets that it manages. The owner continues to be the state of Kuwait. The Kuwait Investment Authority presents annual statements of its accounts to the Cabinet and Parliament (Al Sa'ad, 2008). Over the years, it has become the practice that the Minister of Finance chairs the Kuwait Investment Authority. Roberts' statement that "[b]y the late 1980s Kuwait was earning more from its international investments than from oil" draws attention to the central role of the Kuwait Investment Authority (Roberts, 2011, p. 100). For example, in 1987 Kuwait's foreign investment by the

Kuwait Investment Authority produced US$6.3 bn compared to the US$5.4 bn received from oil export (Bazoobandi, 2013, p. 41).

INDUSTRY DOMINANT PRESSURE PLURALIST POLICY NETWORK IN THE INDUSTRIAL DOMAIN AND THE NON-CREATION OF AN SWF WITH A DEVELOPMENT MANDATE

Between the 1960s and the 2000s, the organisational configuration of state-society relations in Kuwait's industrial domain was consistent with that of an industry dominated pressure pluralist PN. As mentioned in Chapter 3 in this type of PN the decision-making processes are dispersed among different state agencies with low levels of autonomy from highly mobilised segments of the business community (Atkinson and Coleman, 1989). Policy in an industry dominated pressure pluralist PN is generally organised around the immediate needs of specific societal business interests and it tends to be ad-hoc and uncoordinated with previous decisions and short-term oriented (Atkinson and Coleman, 1989).

Kuwait's business community was highly mobilised in the industrial policy domain. Kuwait's merchants had direct presence in policy-making structures (Chrystal, 1990; Al-Dekhayel, 2000). For example, between the 1960s and 1980s, Kuwait's Cabinet comprised members of the ruling Al-Sabah family, but also members of leading Kuwait merchant families and members of the Kuwait Chamber of Commerce. Between 1962 and 1988, for example, 18 of Kuwait's leading merchant families, notably Al-Awadi, Al-Ghunaim and Al- Fulaij, occupied 68 Cabinet posts (calculated by using data from Al-Dekhayel, 2000, p. 52). This is a high number, as over the same period, out of the total of 209 Cabinet members, the ruling Al-Sabah family held only 73 cabinet posts (calculated by using data from Al-Dekhayel, 2000, p. 52). In addition to their direct membership in the Cabinet, Kuwait's private commercial organisations were also able to influence industrial policy-making via the Kuwait Chamber of Commerce.

As such, private commercial organisations have been able to influence industrial policy-making directly through their positions in state apparatus (e.g. membership on the Cabinet). Simultaneously, each of the leading merchants was represented on an average of five boards of shareholding companies (calculated by using data from Al-Dekhayel, 2000, p. 52). Together they had directorship positions in 95 of Kuwait's shareholding companies. Again this is a high number, as by 1977 there were about 109 privately-owned private shareholding companies and 40 privately-owned public shareholding companies with government participation (Khouja and Sadler 1979, p. 128).

Between the 1960s and 2000s, the state apparatus in Kuwait's industrial domain was highly fragmented. State authority in Kuwait's industrial domain was diffused, and multiple state agencies had overlapping jurisdictions. As of the late 1970s, Khouja and Sadler (1979, p. 120) estimate that Kuwait had about ten government agencies charged with the mission of industrial development. These included specialised departments, such as a joint office with the United Nations Industrial Development Organisation, the Ministry of Planning (which replaced the Kuwait Planning Board) and the Ministry of Commerce and Industry. The private domestic sector was strongly represented in these agencies (Al-Dekhayel, 2000; Al-Rabah 2014). For example, out of the Development Planning Board's 16 members, 10 were drawn from the private sector (Al-Dekhayel, 2000). Likewise, the Kuwait Chamber of Commerce had been especially influential in the Ministry of Commerce Trade and Industry (Al-Rabah, 2014). The Ministry of Commerce Trade and Industry served as an important platform for state-business interaction (Moore, 2002). As a result, the degree to which these departments could act autonomously from domestic merchants and traders was low (Khouja and Sadler, 1979). For example, a 1971 World Bank Mission report on the 'Promotion of Manufacturing in Kuwait' highlighted the lack of coordination and autonomy among these agencies (see Khouja and Sadler, 1979). These agencies did not have a clear conception of their mandate and role in order to support coherent policy (Khouja and Sadler, 1979).

The logic of policy-making and policy outcomes reflected the structure of state-society relations in Kuwait's industrial domain and the populist nature of parliamentary politics. The industry dominant pressure pluralist PN impeded the pursuit of policies as well as institutions with a long-term horizon and high levels of policy co-ordination and state involvement. With the exception of the oil sector, policy choices were structured around the immediate preferences of private producer groups (*The Financial Times*, 25 February 1976). While Kuwait's business elite had little interest in the creation of SWFs with development mandates, the populist nature of parliamentary politics in Kuwait from the 1960s onwards also did not contribute to the creation of such a fund. In his article *Defying the Resource Curse: Explaining Successful State Owned Enterprises in Rentier States*, Steffen Hertog (2013) highlights the lack of regime autonomy in economic policy making imposed by popular electoral politics from the 1960s onwards. Hertog (2013) links the absence of state autonomy in economic policy making to Kuwait's National Assembly. Unlike other Parliaments in the region Kuwait's National Assembly has important powers in policy making (e.g. power to remove confidence in individual ministers, power to override emir's veto). Its members are elected in free and fair elections, which are structured around popular politics (Herb, 2014). Popular politics, in turn, revolves around the preservation of the status quo, which is current consumption instead of long term economic-diversification. As such the outcome of the non-creation of such an SWF with a development mandate might have been over-determined.[182]

These choices were characterised by short-termism, low levels of co-ordination and low levels of intrusion for private socio-economic actors. The government only entered sectors in which private merchants had little interest (Crystal, 1990). Kuwait's merchants were heavily involved in the construction and logistics sector, such as the Kuwait Oil Tanker Company and Kuwait Airways (Crystal, 1995).[183] Al-Kandari's statement that "[m]ost industry in Kuwait other than oil and natural gas is based on simple processing and largely depends on imports of primary [and], intermediate goods and materials" indicates a link between Kuwait's merchants and manufacturers (Al-Kandari, 1982, p. 39). Organisations in the industrial domain referred mainly to light manufacturing, consumer goods such as food processing, construction, the manufacturing of building material/asbestos, the fabrication of metal windows and cement pipes (Al-Kandari, 1982).

Although the Industrial Development Board (est. 1961) was officially charged with outlining long-term anticipatory policy, most of its five year plans emphasised short-term reactive policy and institutional choices (Al-Dekhayel, 2000). They produced reports that emphasised short-term goals and the need to expand the private sector's role in manufacturing and trade, and recommended that the state should support this via tariff protection, tax exemptions, cheap loans at low subsidised interest rates and the establishment of industrial estates (Al-Dekhayel, 2000). For example, merchants were allowed to keep their monopolies in trade and services (Crystal, 1990, p. 90). The Kuwait Chamber of Commerce and Industry regulated the permits for foreigners, which were their major competitors. Another form of subsidisation of domestic entrepreneurs related to the creation of joint stock companies with preferential treatment of Kuwaitis in case of government sales. The state bought shares in order to avoid losses to Kuwaiti shareholders. Large amounts of public funds were transferred to the private sector via overpriced government land purchases (Al-Dekhayel, 2000). In addition, by law, Kuwait's private industrial sector had been given preference in government purchases. Policies and institutional choices had the objective to protect the immediate interests of local merchants (Al-Dekhayel, 2000).

Evidence suggests that PNs have played an important role in Kuwait's decisions about state finance institutions; however, there is a need to apply state autonomy at a more general level.

[182] 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, p.23).

[183] Until the mid-1970s, the Kuwait Oil Tanker Company was fully owned by Kuwait's private sector (KOTC, 2015). Kuwait National Airways was founded in 1954, but the government only took full ownership only in 1962 (Kuwait-Airport, 2015).

Kuwait's strong parliament holds important veto powers and plays a critical role in economic policy making. This becomes clearer when looking at other GCC economies, such as Abu Dhabi and Qatar, which do not have a parliament like Kuwait's.

8.3 ABU DHABI'S POLICY NETWORKS AND THE KINDS OF FINANCE INSTITUTIONS SET UP AFTER INDEPENDENCE IN 1971

The comparative analysis of the Abu Dhabi Investment Authority (ADIA), and Mubadala supports the hypotheses derived in the earlier chapters that SWFs with savings and development mandates are more likely to emerge in policy domains that are governed by state-directed PNs. Between the 1970s and the 2000s, state-society relations in Abu Dhabi's savings and industrial domain were characterised by highly-concentrated decision-making structures with high levels of autonomy from weakly-mobilised domestic private producer groups. This situation allowed the pursuit of long-term-oriented policies, characterised by high levels of coordination and state involvement. Unlike Kuwait's parliament, Abu Dhabi's appointive council has only advisory power (Herb, 2009). In the absence of parliamentary constraints, Abu Dhabi's state enjoys high levels of autonomy from popular pressures, which in turn is reflected in the type of economic policy and financial institutions it fosters.

However, the creation of the ADIA as well as Mubadala provides mixed support for major SWF explanations (i.e. efficiency and diffusion-based arguments). Given Abu Dhabi's large oil surpluses, it was a logical step for the government to create such institutions for the purpose of addressing issues related to future generations and economic diversification. As such the creation of these SWFs are in line with an efficiency-based argument. By contrast the creation of the ADIA and Mubadala offers mixed support for a diffusion argument. Although, the creation of ADIA provides support for a diffusion argument, because its creation took place after Abu Dhabi's peer Kuwait had established the KIA; the creation of Mubadala does not provide support for a diffusion argument, because Abu Dhabi was the first country, which created a SWF with a development mandate in the Gulf. Interestingly Singapore's Temasek served as a role model for Mubadala, which suggests that diffusion does not only happen between countries with similar structural profiles but also between countries that are dissimilar (*The National*, 10 August 2011). Consequently, diffusion arguments need to be further developed. An implication of this finding is that diffusion scholars, such as Chwieroth (2014), need to broaden their analytical framework to allow for emulation across countries with different macroeconomic characteristics.

ABU DHABI's STATE DIRECTED POLICY NETWORK IN THE SAVINGS DOMAIN AND THE CREATION OF ADIA

Between the 1970s and 2000s, the structure of state-society relations in Abu Dhabi's savings domain was consistent with that of a state-directed PN. It was characterised by a highly centralised and autonomous state and a weakly mobilised private finance sector. The UAE Constitution from 1971 highlighted that the resources and wealth were the property of the respective emirate (Bazoobandi, 2013). As such, from 1971 onwards, the government of Abu Dhabi has had full authority over the allocation and management of its natural resources and wealth. The Executive Council was the most central economic policy-making body and was led by the Amir (Executive Council Abu Dhabi, 2015; Davidson, 2009). It consisted of 13 members, drawn mostly from the Bani Yas Tribe, which has around 20 subsections (Sheikh Mohammed, 2014). Out of them, the Al-Nahyan family had been the most powerful tribe. Over the years, the ruling Al-Nahyan family co-opted a small number of families from these subsections into a firm political-economic network. Apart from the ruling Al-Nahyan family, important subsections of the tribe, which were on the Executive Council, were the Al-Mazrouei, the Al-Suwaidi, the Al-Romaithi and the Al-Qubaisi. As of the 2000s these five subsections of the Bani Yas Tribe were in control of the Executive Council (see TABLE 8.4.). Out of the 13 members on the Executive Council in 2014, nine were related to those five families (*Gulfnews*, 15 March 2014). According to Davidson (2009), inclusion and exclusion from the Economic Council is a barometer for influence and prestige among Abu Dhabi's tribal elite. Economic posts in the savings domain have been distributed among factions of the tribes within this network. Members of this network have occupied cross-directorships in important state bodies, such as the Executive Council, Finance Department, Development Department and banking and financial organisations. Banking organisations in Abu Dhabi's savings domain have had especially strong connections to the state. For example, the royal family has been represented in leading functions on the Board of Directors in Abu Dhabi's major banks such as the Abu Dhabi Commercial Bank, First Gulf Bank, Abu Dhabi Islamic Bank, National Bank of Abu Dhabi and the Union National Bank. Unsurprisingly, there has been no private Banking Association in Abu Dhabi, and in almost every bank the state has been a major shareholder.

TABLE 8.4. *Cross membership on Executive Council and SWF boards among the leading Bani Yas Tribes.*

Leading Bani Yas Tribes	**Members on Exec.Council**	**Membership on SWF Boards**			
		ADIA	***ADIC***	***IPIC***	***Mubadala***
Al Nahyan (part of Al Falahi)	4*	4*	5*	1*	1*
Al Mazrouei	1				
Al Suwaidi (Al Suwdan)	2	2	1		1
Al Romaithi (Al Remethat)	1				
Al Qubaisi (Al Qubaisat)	1			1	
Sub-Total (leading Bani Yas)	9	6	6	2	2
Total Membership (incl. leading Bani Yas)	13	8	8	2	7

Source: Information compiled from Sheikh Mohammed (2014), *Gulf News* (2014), Mubadala (2014), IPIC (2014), ADIA (2014), ADIC (2014).
* Chairman position hold within a particular subsection of tribe.

The state-directed PN affected the policy-making processes, and the logic of policy-making in Abu Dhabi's savings domain over this period. It facilitated the pursuit of policies with a long-term horizon, along with high levels of state involvement and co-ordination in other policy areas. Reflecting this, Abu Dhabi created an SWF with a savings mandate immediately after British independence in 1971. The Abu Dhabi Investment Administration was created as a means of managing Abu Dhabi's surpluses in parallel to the British run Abu Dhabi Investment Board, which had been in existence since 1967. The motivation behind the creation of the Abu Dhabi Investment Administration in 1971 was very similar to the move of Kuwait in 1961 with its creation of the Kuwait Investment Office. It was a means of achieving more independence (i.e. from Britain) with regard to the management of Abu Dhabi's savings, which multiplied rapidly in the 1970s due to a number of oil discoveries and high oil prices. Three years after (in 1974), the Abu Dhabi Investment Administration took over the management of all wealth – including that of the Abu Dhabi Investment Board – and in 1976 the name was changed to the Abu Dhabi Investment Authority (Bazoobandi, 2013, p. 73).

Although formally independent, the ADIA has strong links to the government. All of its senior officials and the members of its Board of Directors are senior government officials appointed by an Amiri decree. For example, half of the Board members come from the Al-Nahyan family, who occupy positions in the Executive Council at the same time. According to Davidson (2009), the chairman together with a former banker from Paribas, who joined the Investment Authority in the early 1980s, are in full control (see *The New York Times*, 28 February 2008). As of the mid-1990s, the Abu Dhabi Investment Authority reached about US$100 bn, invested internationally into equities, bonds and real estate (Davidson, 2009, p. 73; ADIA, 2009). The

Abu Dhabi Investment Authority has been receiving most of its assets under management from the Abu Dhabi National Oil Company (ADNOC) (Abdelal, 2009). With its 14 subsidiaries, the ADNOC accounts for about 80 per cent of Abu Dhabi's national income (Abdelal, 2009).

ABU DHABI'S STATE-DIRECTED POLICY NETWORK IN THE INDUSTRIAL DOMAIN AND THE CREATION OF ADIC, IPIC AND MUBADALA

Between the 1970s and 2000s, the organisational features of state-society relations in Abu Dhabi's industrial domain were consistent with that of a state-directed PN. It was characterised by weakly mobilised private producer groups and by high levels of power concentration and state autonomy. Like in Abu Dhabi's savings domain, the Executive Council was at the centre of decision-making in the industrial domain. Directly subordinated to it were the Department of Finance and the Department for Economic Development. The Department for Economic Development's as well as the Finance Department's chairmen were simultaneously members of the Executive Council. Both played a key role in formulating long-term industrial policy. The Department for Economic Development, for example, introduced the Plan Abu Dhabi 2030 infrastructure projects worth more than US$400 bn, including tramlines and metro as well as a select range of high-technology heavy industry (Davidson, 2009, p.81). The chairman of the Department of Economic Development also chaired the Abu Dhabi Council for Economic Development, which has a close relationship with the Urban Planning Council (ZonesCorp, 2010; ABCED, 2015).

Over this period, there was no independent association representing private organisations in Abu Dhabi's industrial domain. As of 2014, there were around 80,000 business entities operating in Abu Dhabi (*The National*, 12 June 2014). It has been mandatory for all commercial, industrial, vocational or professional entities with offices in Abu Dhabi to join the Abu Dhabi Chamber of Commerce and Industry. However it had weak research capacity and there were no sector specific committees within the chamber (Hertog, 2013a). Because there has been only one chamber, which comprises all businesses registered in Abu Dhabi, there has been no competition for members. However, the Chamber is a government body set up to help co-ordinate the interests of the private sector with the interests of the state (ADCCI, 2015). Its mission has been to offer coordination for the private sector with the aim of advocating policies that "contribute to Abu Dhabi's sustainable economic development (ADSG, 2015). The Chamber has had strong connections to the Department for Economic Development. Both consider each other as official partners (ADCCI, 2015a). This relationship becomes visible in terms of recruitment patterns between the two entities. Officials who started their career in the Chamber often proceed to further their career at the Department of Economic Development. Via the Chamber, the state has co-opted the private sector into the state apparatus. Until 2014, when elections were introduced, nearly one-third of the 21 members on the chamber's board were appointed by the Amir (ADCCI, 2013). This gave him the opportunity to include members with close connections to the state.. For example, the Vice-Chairman of the Chamber has been on the Board of Directors of Mubadala – one of Abu Dhabi's SWFs – and began his career in the ADNOC, whilst also having held membership positions in the state-related National Bank of Abu Dhabi (NBAD, 2015; Mubadala, 2015).

The state-directed PN influenced the policy-making processes in Abu Dhabi's industrial domain. It facilitated the pursuit of policy with high levels of state involvement and co-ordination aimed at long-term industrial transformation. This was reflected in economic policy and economic reforms with the aim of structurally transforming Abu Dhabi. During a period of low oil prices in the 1980s, Abu Dhabi made a concerted effort to diversify into the international hydrocarbon value chain. This meant the increase of Abu Dhabi's exposure to different links in the international hydrocarbon value chain, particularly midstream and downstream. From the 1990s onwards, diversification targeted other sectors besides hydro-carbon (Davidson, 2009).

Mirroring this, Abu Dhabi created a number of state finance institutions with development mandates between the 1970s and 2000s.[185] Following windfall oil revenues in the 1970s, policy decisions were made which led to the creation of the ADIC in 1977 (Davidson, 2009, p. 74). The ADIC's highest authority was the Board of Directors, and its members were appointed by the Amir. Historically, it has been under the control of the ruling family and the Al-Suwaidi section of the Bani Yas tribe (Davidson, 2009). The ADIC came under the umbrella of the 2007-established Abu Dhabi Investment Council, itself under the control of the Al-Nahyan family (InvestAD, 2015). It has invested actively in international as well as domestic assets (Abu Dhabi Council, 2015). Its domestic holdings have included stakes in the National Bank of Abu Dhabi, the Abu Dhabi National Insurance Company, and the Abu Dhabi Aviation Company (Abu Dhabi Council, 2015a).

The Abu Dhabi Investment Council created the IPIC in 1984 as a joint venture between the ADIA and the ADNOC. The IPIC was established by an Amiri decree with the mandate "to secure end markets for Abu Dhabi crude" (IPIC, 2015). As of the 2000s, the IPIC's investments spanned the entire hydrocarbon value chain at an international level. Between the 1980s and 2000, it acquired controlling stakes in the upstream companies (CEPSA, OMV and COSMO Oil) midstream companies (PARCO, Gulf Energy Maritime, ADCOP, Emirates LNG and OMV

[185] Up until 2013, Abu Dhabi disposed of at least three SWFs with development mandates including the International Petroleum Investment Corporation (est. 1984), Mubadala (est. 2002), and the Abu Dhabi Investment Council (est. 2007).

CEPSA) and downstream companies (OMV, COSMO Oil, Borealis, ChemaWEyaat, Oasis International Power, Duqm Refinery, NOVA Chemicals, Fujairah Refinery, EDP, PARCO and CEPSA) (IPIC, 2015). Although the IPIC is co-owned by the latter two it falls under the umbrella of the Supreme Petroleum Council, which is responsible for the petroleum industry of Abu Dhabi. The Petroleum Council is controlled by the ruling family. Out of its nine directors, five are from the ruling Al-Nahyan family, and three are from the Al-Suwaidi section of the Bani Yas tribe (ADNOC, 2015). The IPIC's chairman is a member of the ruling family as well as Deputy Prime Minister of the UAE, and its managing director is from the Al-Qubaisi section of the Bani Yas tribe (IPIC, 2015a).

Mubadala was established in 2002 by the government and its main objective related to the facilitation of Abu Dhabi's diversification and transformation process (Mubadala, 2015). With its asset volume of approximately US$60.8 bn, Mubadala has been involved in various economic sectors, such as aerospace, semiconductors, real estate, and healthcare. It has exposure to these sectors via its subsidiaries, international partnerships and joint ventures. Abu Dhabi's Crown Prince is the chairman of Mubadala's Board of Directors (Mubadala, 2015). The Al-Suwaidi section of the Bani Yas was also represented on Mubadala's Board of Directors. For example, as of 2014, the Al-Suwaidi member is simultaneously a member of the Abu Dhabi Executive Council and the chairman of Abu Dhabi's Department of Finance. The remaining five directors of Mubadala are successful technocrats who made careers within the state enterprise sector, and who hold important positions in the state apparatus, such as chairmanships of regulatory authorities and government departments, government enterprises, government banks, and the Abu Dhabi Executive Council.

8.4 QATAR'S POLICY NETWORKS AND THE KINDS OF FINANCE INSTITUTIONS SET UP AFTER INDEPENDENCE IN 1971 AND AFTER QATAR's POLITICAL CONSOLIDATION IN 1995

The comparative analysis on state finance institutions in Qatar, provides backing for the hypothesis that SWFs with savings and development mandates are more likely to emerge in policy domains that are governed by state-directed PNs. Between the 1970s and 2000s, Qatar's savings domain was characterised by a strong and centralised state with high levels of autonomy from the domestic private sector. Over this period Qatar's savings and industrial domains were characterised by a weakly mobilised private business sector. Unlike in Kuwait and similar to Abu Dhabi, the Chamber of Commerce in Qatar was not independent and was operating like a government agency (Moore, 2002). A representative at the Qatar Chamber of Commerce admitted that the Chamber had little influence on policy-making and that the government generally did not listen to the Chamber in economic policy making (Anonymous, personal communication, 24 September 2014).

Cross-domain comparison illustrates that changes in PNs show their independent effect on the kinds of financial institutions set up. Following the mid-1990s, the organisation of the state in Qatar's industrial domain experienced a change from a fragmented to a highly-centralised decision-making structure. This was accompanied by the creation of SWFs with development mandates in the 2000s. According to a representative of the Qatar Chamber of Commerce, the 2000s were marked by increasing competition from the state, via its SWFs, with the private domestic sector, especially in domestic construction (Anonymous, 2014). The government has been involved in almost every economic sector via the Qatar Investment Authority and its investment arms. Unlike in Kuwait and similar to Abu Dhabi, there has been no direct or indirect relationship between Qatar's SWFs and the Qatar Chamber of Commerce, which 'formally' represents the private sector. According to a Chamber official, between 1995 and 2012, the Qatar Chamber of Commerce tried 'unsuccessfully' to convince the government to consult the Chamber before major projects were commenced (Anonymous, 2014).

At the same time the creation of the QIA and other state finance institutions in Qatar provides support for an efficiency argument. Following the development of a huge liquefied natural gas sector and the commodity boom in the 2000s it was a rational step for the government to create such institutions for addressing economic development and diversification. The creation of the QIA also offers evidence, that supports a diffusion argument, because the creation of QIA, Qatar Holding and Qatar Diar came up after Qatar's peers, such as Abu Dhabi, had created such state finance institutions.

QATAR'S STATE-DIRECTED POLICY NETWORK IN THE SAVINGS DOMAIN AND THE CREATION OF THE QATAR INVESTMENT BOARD AND THE QATAR INVESTMENT AUTHORITY

Between the 1970s and the 2000s, the structure of state-society relations in Qatar's savings domain was consistent with that of a state-directed PN. Decision-making power was highly centralised in the Supreme Council of Economic Affairs, which was chaired by the Emir (Ibrahim and Harrigan, 2012). As such the Emir (i.e. Khalifa Al-Thani 1972-1995; Hamid Al-Thani 1995-2012) retained control over policy making in Qatar's finance and savings domain

(Mehran, 2013). Qatar's banking system had been controlled by the state via direct shareholdings and via appointments on the banks' Board of Directors. For example, as of the 2000s the Qatar state continued to hold a 50 per cent ownership stake in Qatar's oldest bank (i.e. the Qatar National Bank est. 1964). Its chairman is the Minister of Finance, who is appointed by the Emir. Two other members of the Qatar National Bank's Board of Directors also belong to the ruling family (QNB, 2015). The chairman of the 1975 created Commercial Bank of Qatar was from the ruling family. Although this bank is 'formally' Qatar's first private bank, the ruling family occupies central positions on the bank's Board of Directors. Likewise, the 1982-created Qatar Islamic Bank was chaired by a member of the royal family, with other royal family members sitting on the bank's Board of Directors (QIB, 2015). Among Qatar's largest banks, there had been no genuine private bank (see Qatar Monetary Agency, 1985).

Reflecting this, there was no banking association representing the private banking-finance sector. As of the 1970s and 1980s, apart from regional Arab Banks (e.g. Bank Al-Mashrek and Bank of Oman) and large foreign international banks (e.g. Standard Chartered Bank, British Bank of the Middle East, Citi Bank, Banque Paribas), there existed only smaller privately run Money Exchange Companies (e.g. Al-Fardan Exchange and Finance Co, Al-Basry Exchange) (Qatar Monetary Agency, 1985).

The state-directed PN influenced the logic of policy making in Qatar's savings domain over that period. It enabled the government to pursue long-term-oriented policies with high levels of state involvement. Reflecting this, Qatar's government created an SWF with a savings mandate. Shortly after Qatar's independence, the Emir established the Qatar Investment Board in 1972. It was created as an agency with the purpose of coordinating the 'overall investment strategy of Qatar' (El-Mallakh, 1979, p. 131). The Qatar Investment Board can be described as the predecessor of the 2004/05-created Qatar Investment Authority. From 1972 onwards, reserves were channelled via the Qatar Monetary Agency to the Qatar Investment Board, which managed and coordinated these assets. The Qatar Investment Board was led by the Minister of Finance, and its Board of Directors included an advisor to the Emir, as well as the director of the Emir's private office, the Director of Finance and a Swiss Banker. In addition, the Qatar Investment Board was also drawing on a group of international financial experts, notably representatives from Manufacturers Hanover – a bank holding company based in the US –, the First National Bank of Chicago, Morgan Grenfell, and Deutsche Bank (El-Mallakh, 1979, p. 131).

There is a direct link between the 1972-created Qatar Investment Board and the 2005-created Qatar Investment Authority. An official statement that "[the Qatar Investment Authority] builds on the heritage of Qatari investments dating back more than 3 decades" draws direct attention to the connection between these two entities (QIA, 2014). The QIA was created with the purpose of diversifying Qatar's wealth across different asset classes and regions by making return-oriented investments (QIA, 2014). Its mission, defined in Article 5 of the State of Qatar Emiri Decision No (22) of 2005 (the QIA Constitution) is to "...develop, invest and manage the state reserve funds and other property assigned to it by the Supreme Council in accordance with policies, plans and programs approved by the Supreme Council" (QIA, 2014). This means that the Supreme Council was central to QIA's funding and investment structure. Again the Supreme Council was directly subject to the Emir, and it consisted of the Minister of Energy and Industry, the Minister of Finance, the Minister of Economy and Trade, as well as the Governor of the Qatar Central Bank, the Economic Advisor of the Emir, and representatives from the Qatar Investment Authority and the Qatar Development Bank (DohaNews, 3 July 2013; GSDP, 2011). The QIA's board of directors had full control over the QIA's business and its members were appointed in accordance with the Emir's decision. It was chaired either by the Prime Minister or by the Emir himself. The Board also included members simultaneously sitting on the Supreme Council (QIA, 2014).

QATAR'S INDUSTRIAL DOMAIN: FROM A PRESSURE PLURALIST POLICY NETWORK (1972–1995) TO A STATE-DIRECTED POLICY NETWORK (1995–2000s) AND THE CREATION OF QATAR HOLDINGS, QATAR DIAR, AND THE QATAR INVESTMENT AUTHORITY

Between 1972 and 1995, the structure of state-society relations in Qatar's industrial domain was consistent with that of a pressure pluralist PN. Decision-making structures were fragmented, and officials stood vis-à-vis dispersed and fragmented business producer groups with conflicting preferences. During this period, the system of private interest representation was characterised by low levels of mobilisation. Despite the existence of a light manufacturing industry in Qatar (in 1983 there were around 1,195 establishments in the manufacturing area, such as little workshops, clothes, furniture or packaging), there existed no business association representing these organisations (Ministry of Information Qatar, 1985, p. 27). Secondary literature supports this and highlights that in contrast to other GCC economies, notably Kuwait, Qatar had a weak domestic merchant and business class (Crystal, 1990; Mehran 2013).[186] There existed no formal state agency or planning institution in Qatar's industrial domain. According to El-Mallakh (1979), this role was pursued by the Council of Ministers. But until the mid-1990s, the Council of Ministers was characterised by high levels of factionalism. Despite high levels of

[186] The lack of easily accessible ports and the collapse of the pearl fishing industry significantly weakened Qatar's merchants (Crystal, 1990). Most of the time, they played a negligent role in Qatar's economic policy-making (Crystal, 1990; Mehran, 2013). The rulers of Qatar distanced themselves very early from domestic merchants. Instead, they formed an alliance with Britain and its national population through distributive policies (Crystal, 1990).

autonomy from domestic merchants there was intensive competition among members of the ruling family over power and influence in social and industrial policy making (Crystal, 1990; Mehran, 2013).

Between the early 1970s and mid 1990s the structure of state-society relations influenced discussions about Qatar's industrialisation. Given a weakly mobilised and fragmented domestic business sector the government consulted in 1972 a British firm to make a survey on Qatar's requirement for development (El-Mallakh 1979, p. 56).[187] This survey highlighted the need for recovering fishery and agriculture, as well as import substitution, referring to products such as plastic, leather goods, cement, fertiliser and soap, and the creation of a steel petrochemical complex (El-Mallakh, 1979, pp. 56–57). Qatar followed the prescriptions of the British firm, and created a number of large joint ventures with multinational corporations in the hydrocarbon and related sectors. For example, in 1974, Qatar entered a joint venture with an international consortium which included Norsky Hydro Hambros Bank and Davy Power Gas (Ministry of Information Qatar, 1985). This resulted in the creation of the Qatar Fertiliser Company, followed in 1977 by the creation of the National Cement Company, whilst in 1980 this was followed by the establishment of the Qatar Petrochemical Company, a joint venture between Qatar General Petroleum Corporation and France state-owned CDF Chimie (Ministry of Information Qatar, 1985).

Over this period, however, oil and gas revenues were low and volatile, which was reflected in the magnitude of spending in Qatar's industrial policy domain.[188] Especially in the 1980s and the early 1990s, Qatar was highly exposed to external shocks in the energy market and the construction sector. For example, Qatar's newly established cement industry was badly affected by the early 1980s recession and intense international competition pressures (Ministry of Information, 1985). It had to make significant price cuts (reducing its prices three times) and had to reduce its original cement output to a third from 330,000 to 110,000 tonnes (Ministry of Information, 1985, p. 23). Likewise, falling steel prices and high production costs, which were three times more than in other countries, created further problems for Qatar's public sector (Moore, 2002). In addition, Qatar faced significant problems in the oil sector in the 1980s and early 1990s, as oil fields aged and oil prices dropped (Ibrahim and Harrigan, 2012). Qatar responded with austerity programs by reducing public spending and suspending public/private infrastructure projects (Moore, 2002). Furthermore, it embarked on partial privatisations in order to relieve the fiscal burden from the government (EIU, 2009).

[187] Unfortunately El-Mallakh does not provide the name of the British firm (El-Mallakh, 1979).
[188] In 1977, the state allocated around 35 per cent of its total budget to industrial development, but by 1978, the share had declined to 23 per cent (El-Mallakh, 1979, p. 69). During this same period, housing expenditures increased from 10.2 per cent in 1977 to 17.8 per cent in 1978 (El-Mallakh, 1979, p. 69).

However from the mid 1990s onwards Qatar experienced windfall gas revenues combined with a centralisation of decision-making structures in the industrial domain. The ascension of Hamad Al-Thani in 1995 – through a palace coup – triggered a process of centralisation and institutionalisation among state agencies in the industrial domain. Starting in 1995, internal factionalism in the royal family was ended through the replacement of the 'old guard' from the Council of Ministers through the appointment of like-minded members of the ruling family (Mehran, 2013).[191] Qatar's first permanent constitution in 2003 and its amendment in 2004 ascribed near absolute power to the Emir (Qatar Constitution 2004 Art 64-75). The Emir was the "supreme overseer of the whole" (Mehran, 2013, p. 117). From the mid-1990s onwards, the inner circle of top policy makers included only a handful of people, notably the Emir, the Emir's son, his second wife, the Emir's maternal and childhood friend who was the Deputy Prime Minister, and the Prime Minister (Mehran, 2013, p. 117). This circle of top policy makers under the leadership of the Emir was tied to a strong kinship network which consisted of between 50 and 60 members (Mehran, 2013). It included members from the royal family and other key families, with intimate links to the top policy makers, and technocrats occupying central positions. Their main tasks amounted to information gathering, policy-making and policy implementation via the chairmanship of specialist agencies (Mehran, 2013). Almost all specialist state agencies and bureaus in Qatar's industrial domain were created in the early 2000s. For example, the Ministry of Municipality and Urban Planning established the Central Planning Unit in order to co-ordinate national infrastructure projects in the 2000s (Ibrahim and Harrigan 2012, p. 10). In addition, the government created the General Secretariat for Development Planning in 2007, with the objective of strategic planning and the formulation of Qatar's National Vision 2030. This was followed by the formation of the Supreme Committee for Development planning in 2011, with the purpose of implementing the Qatar National Vision 2030 (GSDP, 2008).

The centralised and institutionalised decision making affected the logic of policy making in Qatar's industrial policy domain from the late 1990s onwards. Reflecting this in combination with windfall gas revenues, Qatar has created a number of state finance institutions with development mandates under the auspices of the Qatar Investment Authority. For example, the Qatar Holding was created in 2006 as a direct investment arm of the Qatar Investment Authority. Qatar Holding has been a global investment house that "invests internationally and locally in strategic private and public equity as well as in other direct investments" (Qatar Holding, 2013; Katarahospitality, 2015). Another example relates to the Qatar Investment Authority's real estate and infrastructure investment arm Qatari Diar, which was established in 2005. Among Qatari Diar's international investments there are more than 49 projects in 29

[191] Through his status of successor, Hamad Al-Thani had already started Cabinet reforms already in 1992 by reshuffling and replacing the old guard with like-minded development-oriented family members (Mehran, 2013, p. 113).

countries and among its domestic projects there are infrastructure projects such as the Qatar Railways Development Company and real estate projects, most notably Lusail City (Qatari Diar, 2014).

CONCLUSION

This chapter shows that different policy networks can be systematically linked to different types of SWFs across small open Gulf economies between the 1960s and the 2000s. The findings of the plausibility probe with three additional countries support the hypotheses developed in previous chapters.

The chapter found similarities between the configurations of state and private actors in the savings domain of Abu Dhabi and Qatar (see TABLE 8.5). Between the 1960s and the 1970s, all of these economies established SWFs with savings mandates, channelling significant proportions of domestic savings into international assets. Over this period, the savings domains of Abu Dhabi and Qatar were characterised by strong and autonomous states and by weakly mobilised domestic private-finance actors. For example, there was no banking association in Qatar and Abu Dhabi. As a result, the state was the dominant player in the banking systems across these economies, responsible for the appointment of key positions in the banking sector. Kuwait's savings domain was characterised by a centralised state with a highly mobilised segment of business. The Banking Association in Kuwait was dominated by representatives from the state-banking sector as well as from Kuwait's businesses. Unlike Qatar and Abu Dhabi, however, Kuwait had a strong parliament that was central in influencing economic policy making.

The existence of state-directed PNs in the industrial domain and the creation of SWFs with development mandates in Qatar (e.g., Qatar Holdings and Qatar Diar) and Abu Dhabi (e.g., Mubadala and IPIC) are in line with the expectations developed in earlier chapters. In both cases, a centralised and autonomous state stood vis-à-vis a weakly mobilised private sector in the industrial domain. There was no merchant elite independent from the political or royal/tribal elite in Abu Dhabi or Qatar. The ruling families were themselves the commercial elite (Herb, 2014). In Qatar, as well as in Abu Dhabi, both the chamber of commerce and industry had been quasi-government departments. The rulers of both Abu Dhabi and Qatar had strong influence over the appointment of members in the domestic business chambers. By contrast, state-society relations in Kuwait's industrial domain referred to an industry-dominant pressure pluralist PN. Short-term ad-hoc policies in Kuwait were reflected in the fact that it did not create an SWF with a development mandate.

However, small, open economies of the Gulf region with differing types of SWFs offer mixed support for efficiency- and diffusion-based arguments. The efficiency argument's expectations are widely in line with empirical observations on the creation of SWFs with savings mandates in Abu Dhabi, Qatar, and Kuwait. SWFs with savings mandates are means of addressing future uncertainty related to high dependency on single, depletable resources by channelling out liquidity and thereby translating oil wealth into financial wealth for future consumption.

Given their high dependency on hydrocarbon wealth, the small, open economies of the Gulf region would be expected by a supporter of an efficiency argument to create SWFs with savings mandates. Between the 1960s and the 2000s, all of the small, open economies of the Gulf region (i.e. Abu Dhabi, Qatar, and Kuwait) did so. However, the efficiency argument's expectations are only partially in line with empirical observations on SWFs with development mandates. Such SWFs help to diversify a country's economic base from overexposure in hydrocarbons to investment in other economic activities. A supporter of an efficiency argument would therefore expect to observe similarities between SWFs with development mandates across small, open GCC economies. However, despite their similar resource endowments in terms of gas and oil, the GCC economies made very different choices with respect to the question of creating SWFs with a development mandate.

A supporter of such a diffusion argument would expect countries to create SWFs with savings and development mandates when other countries in their peer group facing similar challenges create such institutions. The challenges may refer to issues of economic diversification or to questions of how best to translate commodity wealth into financial wealth. Timing is an important element in a diffusion argument, and, in this context, the long period between the creation of Kuwait's SWF and that of Abu Dhabi ten years later poses a problem for the diffusion argument. However, the picture looks different again if it takes into account the timing of oil and gas exploitation and independence. The creation of the Kuwait Investment Office (established in 1961), the Abu Dhabi Investment Administration (established in 1971), and the Qatar Investment Board (established in 1972) took place immediately after the countries' independence (i.e. Kuwait, 1961; Abu Dhabi, 1971; Qatar, 1971). In terms of SWFs with development mandates, however, the cases provide only limited support for a diffusion argument. While all of the small, open economies of the Gulf region were confronted with the identical problem of economic diversification, only Abu Dhabi started creating an SWF with development and diversification mandates in the 1980s, followed twenty years later by Qatar in the 2000s. Despite the availability of resources and confronted by similar challenges, Kuwait did not create a Mubadala-like SWF.

TABLE 8.5. *Policy Networks and the types of SWFs in Kuwait, Qatar and Abu Dhabi.*

	SAVING DOMAIN			***INDUSTRIAL DOMAIN***			
	Kuwait	***Abu Dhabi***	***Qatar***	***Kuwait***	***Abu Dhabi***	***Qatar***	
Period	*1960s–2000s*	*1970s–2000s*	*1970s–2000*	*1960s–2000s*	*1970s–2000s*	*1970s–mid1990s*	*mid1990s–2000s*
State ***Concentration*** ***Autonomy*** ***Private*** ***Mobilisation***	*High* *High* *High*	*High* *High* *Low*	*High* *High* *Low*	*Low* *Low* *High*	*High* *High* *Low*	*Low* *High* *Low*	*High* *High* *Low*
Policy Networks	Concertation	State-directed	State-directed	Industry dominant pressure pluralism	State-directed	Pressure Pluralism	State-directed
SWF type created	SWF with saving mandate	SWF with saving mandate	SWF with saving mandate	n/a	SWF with development mandate	n/a	SWF with development mandate
Empirical Instances	KIO KIA	ADIA	QIB QIA	n/a	Mubadala, IPIC, ADIC	n/a	Qatar Holding, Qatar Diar

9. Conclusion: Policy Networks and Variation in State Finance Institutions

The final chapter outlines the findings of the research, and its contribution to the policy network (PN) literature. It first outlines the puzzle of different types of sovereign wealth funds (SWFs) in small open economies. Then, it presents competing explanations on the drivers of different SWF types, and introduces a PN perspective, which is the adopted approach. The chapter highlights that PN analysis provides an important contribution to existing approaches on SWFs which are based on 'efficiency' and 'diffusion'. Furthermore it indicates potential avenues for integrating PN analysis with other theoretical approaches.

The research has highlighted that dominant explanations on SWFs are too limited for explaining SWF variation across and within countries, because they ignore domestic politics in the form of state-society relations. SWF variation across and within small open economies seems puzzling for standard explanations, which cannot explain this variation. What the present research has done is to draw on a different theory and show what contribution it makes. It has analysed the effects of state-society structures on the kinds of financial institutions set up in policy domains. Therefore, it posed the following research question: do differences in domestic state-society structures influence choice and type of state finance institution, and if so, how and why?

By using a selected case study on 'SWF variation in Hong Kong and Singapore between the 1960s and 1980s', the research has developed and refined hypotheses with regard to the effects of state-society relations on the kind of state finance institutions set up. It has used the cases to inductively develop hypotheses and causal mechanisms whereby PNs might have influenced the creation of different SWF types and related state finance institutions. Over this period, Hong Kong and Singapore exhibited important variations in terms of the independent variable (i.e. state-society relations) and in terms of the dependent variable (i.e. the creation of different state finance institutions). This makes both cases particularly useful for investigating mechanisms whereby state-society relations may have influenced institutional choices. The thesis has done this through a systematic observation of actors involved in debates and policy-making processes. The effects of different PNs have been compared across domains (i.e. the savings and the industrial policy domain) and across small open economies (i.e. Hong Kong and Singapore between the 1960s and 1980s). The research has compared the types of PNs with the choices made (i.e. the creation of different SWFs and other related state finance institutions, such as CPFs and development banks). It has looked at the alternative choices that were both available and discussed at the time. In addition, it has provided a plausibility probe for the hypotheses developed in earlier chapters by looking at SWF types in small open Gulf economies (i.e. Kuwait, Abu Dhabi and Qatar).

The present thesis has offered causal mechanisms whereby PNs might have operated to affect the kinds of financial institutions set up. Process tracing was used to identify potential causal mechanisms in this phenomenon, with different SWF types as instances. Different socio-economic actors were included and excluded on important policy-making processes by different types of PNs. The research has looked at the creation of SWF types and their different consequences for socio-economic actors. The major finding was the systematic variance among PNs, policy processes, causal mechanisms and policy outcomes. Out of those findings it generated hypotheses that SWFs with development mandates, as well as SWFs with savings mandates, are more likely to be created in countries where one can observe state-directed PNs. This relates to a more general hypothesis, that the structure of PNs affects which kind of financial institution is set up, and that different institutions favour different kinds of interests.

The chapter begins, first (9.1), by outlining the cases and research design. Second (9.2), it highlights the empirical findings and arguments developed, and shows how the thesis has arrived at these findings and arguments. Third (9.3), it looks at the implications of these findings and arguments for theory development with regard to PNs. It links the findings back to contemporary PN literature and also to current debates in the literature on SWFs.

9.1 RESEARCH DESIGN AND CASES

The research has used a cross-country and cross-domain comparison with process-tracing. This design has allowed the systematic examination of the effects of PNs on policy choices with regard to the creation of different SWF types. Selecting small open economies within the same peer group allows for the addressing of diffusion and efficiency arguments because small open economies are extremely exposed to international diffusion and efficiency pressures. This allows accounting for the impact of external economic pressures and emulation.

Each of the empirical chapters has looked at the policy choices discussed in the respective policy domain, the PNs in place, and the policy choices made. In order to assess the effects of different PNs on different policy choices, close attention has been paid to the debates and to the policy preferences of different socio-economic actors. Through process-tracing the present research has examined policy making processes between cases, which has allowed for the assessment of the effect of PNs on policy choices with regard to the creation of different SWF types, and with regard to the question of who benefited and who was harmed by the particular choice.

Hong Kong and Singapore were selected because they had similar values in the variables highlighted by standard explanations (i.e. efficiency- and diffusion-based explanations). Consequently, efficiency and diffusion could not have accounted for differences with regard to SWF-type variation. Efficiency-based approaches would lead us to predict that Hong Kong and Singapore would have created similar SWF types because both were very open, both were confronted with similar external pressures (e.g. competition and inflation) and both had high levels of domestic savings. Likewise, diffusion-based approaches would lead us to predict that both economies would have adopted similar types of SWFs because both belonged to the same peer group (i.e. they shared similar structural profiles) and both were highly exposed to international pressures and confronted with similar, but separate challenges. What efficiency- and diffusion-based accounts omit is domestic politics. Therefore, the present thesis has looked at domestic politics, and explored a PN approach.

CROSS-NATIONAL VARIATION IN HONG KONG AND SINGAPORE'S SAVINGS DOMAIN (1960s–1980s)

Until the early 1960s, Singapore and Hong Kong addressed low levels of external inflation in an environment of low capital mobility with similar kinds of financial institutions. The savings structures of both economies were dominated by private banks and characterised by the absence or limited presence of state financial institutions.[192] Domestic savings were primarily channeled through private savings vehicles. Their respective financial systems at that time were characterised by currency boards.[193] And from the late 1960s onwards, successive international financial deregulation rounds increased worldwide capital mobility and the scope for new investment opportunities. The period between the 1960s and 1980s saw an increase in capital mobility, caused by six interrelated factors: (1) the breakdown of the Bretton Woods system of fixed exchange rates, (2) the availability of surpluses seeking investment opportunities with higher return (3) the governments' encouragement of private financial actors to diversify their assets internationally, (4) the lowering of transaction costs through technological innovation, (5) the creation of new financial instruments, and (6) the worldwide liberalisation of capital controls (Helleiner, 2004).

[192] Although Singapore's CPF had been already created in the mid 1950s its role was negligible until the 1970s because of its low contribution rates (see TABLE 6.1).
[193] A currency board increases the credibility of an economy's commitment to maintain a fixed exchange rate. Its main focus is the maintenance of a fixed exchange rate. A classical currency board issues domestic currency liabilities only in exchange for foreign currency assets.

The 1970s witnessed unprecedented levels of commodity price hikes, translating into rising worldwide inflation. Increasing inflation, combined with heightened capital mobility put significant pressures on the high levels of domestic savings in Hong Kong and in Singapore. Through high import ratios and high levels of capital flows these pressures were directly transmitted into the domestic economy of Hong Kong and Singapore, thereby affecting purchasing power (see Krause, 1988).

Confronted with external pressures, policy choices started to diverge dramatically in Hong Kong and Singapore from the late 1960s onwards and resulted, in the 1980s, in very different kinds of finance institutions set up. While in Hong Kong savings continued to be allocated through private savings vehicles (e.g. private commercial banks, private pension funds), in Singapore a significant part of domestic savings were channelled into state finance institutions, most notably the state-run Central Provident Fund (CPF) and the state-owned banks, notably the Post Office Savings Bank. Singapore's government created an SWF – the Government Investment Corporation (GIC) – to manage these savings abroad in order to get a better return on large levels of accumulated wealth. The GIC's international investment mandate also had the effect of mitigating domestic inflation pressures.

With regard to the overall argument, the cases of Hong Kong and Singapore provide strong evidence for the effect of PNs on the kind of finance institutions set up in the savings domain. From the 1970s onwards, high levels of domestic savings in both economies were increasingly exposed to similar external pressures, notably inflation in an environment of high capital mobility. Between the 1970s and 1980s, cross-domain variation in SWFs with savings mandates combined with variations in the processes, and variation in PNs, suggest the role of PNs in influencing different policy outcomes. Hong Kong continued with private finance institutions, while Singapore embarked in the 1960s with the creation and extension of state finance institutions (i.e. CPF, POSB and DBS) and in the early 1980s on the establishment of an SWF with a mandate of allocating savings abroad. Discussions in Hong Kong and Singapore reveal that there were alternative policy choices available in both cases.

The present research has found that different PNs influenced the different policy choices made, through inclusion and exclusion. The decision to create an SWF with a savings mandate in Singapore was linked to earlier decisions on other state finance institutions and driven by a state-directed PN, which was able to exclude domestic finance and commerce organisations from policy-making processes. Due to high levels of power concentration and autonomy, Singapore's decision-makers could freely choose among international investment houses. By contrast, in Hong Kong the choice against creating state finance institutions with a savings mandate, notably a state run CPF, affected the potential of creating a SWF with a savings mandate like in Singapore. This decision was driven by a clientele pluralist PN in Hong Kong which included domestic finance and business organisations on important policy bodies and excluded weakly mobilised labour and welfare organisations.

CROSS-NATIONAL VARIATION IN HONG KONG AND SINGAPORE's INDUSTRIAL DOMAIN (1960–1980s)

By the early 1960s, Hong Kong and Singapore had embarked on labour-intensive industrialisation as a consequence of the significant decline in their role as regional entrepôts. Confronted with similar external pressures (i.e. increasing international competition and protectionism), policy choices in Singapore and Hong Kong started to diverge from the late 1960s onwards, and resulted in different types of finance institutions in their industrial domains (see TABLE 9.1). Despite similarities in terms of their high openness and their small domestic markets, Hong Kong and Singapore's policy makers made very different policy choices regarding state finance institutions. While Hong Kong's policy makers decided not to enlarge its state sector and not to create a state development bank or a state development fund, Singapore's government embarked on a comprehensive industrial upgrading programme and chose to enlarge the state sector, first creating a development bank and later a SWF with a development mandate. Through this SWF, Singapore's government took direct stakes in a variety of unrelated sectors (e.g., technology, finance, manufacturing, infrastructure) and in joint-ventures which were considered crucial for Singapore's diversification into higher value-added industries.

Between the 1960s and 1980s, industrial policy in Singapore was formulated in a state-directed PN. It was characterised by weak and fragmented manufacturing associations, a weakly mobilised and passive banking and commerce sector, as well as a centralised and autonomous state with a dominant Ministry of Finance at its centre (see TABLE 9.1). It operated via inclusion and exclusion. Only high-level bureaucrats and politicians from the Ministry of Finance, as well as a small number of external economic advisors from the World Bank, were part of the policy-making processes, leading to the emergence of a fledging state enterprise sector, the creation of the DBS and the creation of Temasek. The creation of the SWF was aimed at the structural transformation through industrial upgrading and increased co-ordination among government-linked companies. Specifically, domestic private entrepreneurs viewed the government's policies as highly intrusive, mainly because of competition and crowding out aspects. In stark contrast, MNCs did not perceive Singapore's SWFs as intrusive, because Singapore's SWF and its companies were co-operating with MNCs. They provided important infrastructure and operated in areas complementary to MNCs, creating joint-ventures with MNCs. This suggests that members of PNs benefit from institutional choices accruing from these PNs.

Over the same period, industrial policy in Hong Kong was formulated in a clientele pluralist PN. It was characterised by weakly mobilised industrial associations, and by a highly centralised state with close links to strongly mobilised finance and commerce organisations. An arrangement was in place that encouraged interaction between bureaucrats and policy makers from the Finance Branch, the Commerce and Economic Development Bureau and finance as well as commerce organisations. Because of this arrangement there was a low level of differentiation between the state apparatus and finance/commerce actors. This made finance and commerce actors influential in economic policy-making. Finance and commerce actors had diametrically opposed preferences to the manufacturing sector in terms of finance institutions in the industrial domain. They had a strong preference for low levels of state involvement in the lucrative industrial financing area. As such, they strongly opposed proposals for the creation of state finance institutions, notably a state-run development bank or a development fund. This supports the argument that clientele pluralist PNs in the industrial policy domain lead to the non-creation of state organisations leading the flow of industrial capital.

TABLE 9.1. *External Pressures and the Kind of Financial Institutions set up in Hong Kong and Singapore (1950s–1980s).*

Period	**Similar External Pressures**		**Different Responses**	
	Hong Kong	***Singapore***	***Hong Kong***	***Singapore***
1950s–early 1960s	Decline in entrepôt trade following the Korean War in the early-1950s.	Decline of entrepôt trade following the emancipation of Singapore's neighbours in the late-1950s.	Non-creation of a state industrial bank.	Establishment of the MFI and the EDB.
1960s–early 1970s	Loss of Commonwealth Preferences; tensions with neighbouring China; increasing competition with NIE (Taiwan, South Korea); protectionism in OECD markets.	Expulsion of Singapore from Malaysian Union (i.e. loss of common market); tensions with neighbouring Indonesia and Malaysia; increasing competition pressure with NIE; protectionism in OECD markets.	Expansion of private commercial banks' activities in industrial financing.	Creation of the DBS; expansion of state sector.
1970s	Increasing competition pressures with Malaysia, Thailand in labour intensive light manufacturing; 1970s oil shock; protectionism (e.g. Multi Fibre Agreement).	Increasing competition pressures with Malaysia, Thailand in labour intensive light manufacturing; 1970s oil shock; protectionism.	Non-creation of industrial bank & development fund.	Re-organisation of the state sector and the creation of Temasek.
1980s	Effective opening of China's industrial zones leading to increased outsourcing of labour intensive industries to China; Partial revival of Hong Kong's role as entrepôt trade hub.	Opening of Malaysia and Indonesia and outsourcing of labour intensive industries. Recession in US in 1983, especially in the electronics sector; translation of the US recession into Singapore's first recession in 1985.	Non-creation of a development fund for small and medium enterprises.	Restructuration of Temasek and its international expansion.

Cross-national variation in the structures of state-society relations and policy processes as well as variation in state finance institutions indicate that PNs had an impact on choices regarding SWFs and related finance institutions, such as CPFs and development banks.

Given a set of similar external macro pressures (i.e. competition), opportunities (i.e. worldwide trade liberalisation), and constraints (i.e. small domestic markets), Hong Kong decided to continue with existing institutional choices (e.g., private domestic finance organisations), whereas Singapore decided to expand and create state finance institutions with a development/transformation mandate. Public debates reveal that socioeconomic actors in Hong Kong and Singapore at least knew that different policy options were available. PN structured the voice of socioeconomic actors in the debates and affected their inclusion or exclusion from policy-making bodies.

9.2 FINDINGS

A number of findings have arisen from the thesis, which contribute to the development of PN analysis. It has shown how PNs in small open economies structured different socio-economic actors, including the state itself, in the policy making processes. The research emphasises four key findings from the case studies: there were struggles about policy choices concerning particular SWF types; there were systematic links between the type of PNs and the type of SWF; PNs included and excluded actors that influenced policy making decisions with regard to the kind of financial institutions set up; these had important implications for actors and created winners as well as losers (see TABLE 9.2.).

Between the 1960s and the 1980s, external developments (e.g. increasing international competition, inflation, currency volatility) put pressure on socio-economic actors in Hong Kong and Singapore. It has found that similar issues were discussed, similar policy choices were available and similar actors were involved in the debates, but organised differently. Different socio-economic actors favoured different policy choices, and they were aware of alternatives (see TABLE 9.2.). Second, it has discovered that different PNs lead to different strategies and to different institutional choices. There was a systematic linkage between the type of PN and the kinds of financial institutions set up. Variation concerning types of SWFs was systematically related to variation in state-society relations. In addition to this, it has found that the case outcomes show variation, which runs counter to observable expectations of the dominant explanations (i.e. efficiency- and diffusion-based explanations).

Third, it has found evidence on the processes by which PNs have influenced policy choices. This research has provided new insights into the operation of causal mechanisms linking PNs to forms of institutional policy. It has shown how these PNs were related to different choices, by examining which actors were included and excluded (see TABLE 9.2.). Fourth, it has revealed that the types of PNs and their corresponding policy choices regarding type of SWF involve distributional consequences. Different policy choices, with regard to the kinds of financial institutions set up, have an important impact on the allocation of wealth among socio-economic actors (see TABLE 9.2.). Size, combined with their specific organisational features, make state finance institutions, especially SWFs, dominant financial institutions, particularly in small open economies. SWFs and related state finance institutions, particularly CPFs, are highly unpopular with private actors in the respective policy domains, because they can be rivals to existing domestic private financial institutions. State finance institutions are frequently associated with competition and crowding out of the domestic private sector.

TABLE 9.2. *Processes, Mechanisms, Actors and Institutional Choices in Hong Kong and Singapore (1960s–1980s).*

POLICY DOMAIN ***Internat. Context*** Challenges	**Institutional choices on the table & discussed in Hong Kong and Singapore**	**Type of PN**	**Mechanisms through which PN operated**	**Institutional choice made**	**Interests helped by this choice**	**Interests harmed by this choice**
INDUSTRIAL DOMAIN ***High international competition pressures*** Development/ diversification/ upgrading	**(A)** Private finance institutions leading the flow of industrial capital with an objective of profit maximisation. **(B)** State finance institutions leading the flow of industrial capital with a mandate of supporting domestic entrepreneurs with cheap capital. **(C)** State finance institutions leading the flow of industrial capital with mandate of diversification and upgrading of the state sector (e.g. via joint ventures with MNCs)	**Clientele pluralist (Hong Kong)**	Inclusion of domestic finance and trade/commerce. Exclusion of domestic manufacturers, int. finance.	**(A)**	Domestic private commercial banks, because of profit made (through high interest rates charged).	Domestic private manufacturers seeking cheap credit.
		State-directed (Singapore)	Inclusion of state officials and bureaucrats, int. experts. Exclusion of domestic manufacturers, domestic finance and trade/commerce.	**(C)**	State enterprises, and to some extent MNCs.	Domestic private manufacturers and domestic finance because of competition.
SAVINGS DOMAIN ***High international inflation pressures, and emerging investment opportunities*** Allocating national savings/surpluses, protecting purchasing power	**(A)** Private finance institutions leading the flow of capital with the objective of profit maximisation. **(B)** State structures leading the flow of savings/finance with a mandate of channeling capital into domestic system. **(C)** State structures leading the flow of savings/finance with a mandate of channeling capital abroad (e.g. for getting highest return).	**Clientele pluralist (Hong Kong)**	Inclusion of domestic finance and trade/industry. Exclusion of MNCs, and int. finance, welfare and labour.	**(A)**	Domestic finance, commerce, and business/industry	International finance, welfare and labour.
		State-directed (Singapore)	Inclusion of state officials and int. finance. Exclusion of domestic finance, and domestic manufacturing.	**(C)**	International Finance, labour*	Domestic finance, labour intensive manufacturing.

* Labour benefited to the extent to which the CPF Board benefited from GIC's returns.

9.3 WIDER IMPLICATIONS OF FINDINGS

Through these findings the thesis adds to the ongoing debate on whether PNs matter in explaining policy choices. It does so in four ways. To date, PN approaches provide rather crude hypotheses on the effects of PNs on a broad set of state strategies, and forms of adjustment. These are difficult to verify because they are either very narrow or very broad, notably the categories of anticipatory and reactive policy (Atkinson and Coleman, 1989). As a consequence, the present study has offered a critique of PN literature, and has developed hypotheses and established causal mechanisms linking PNs to the kind of state finance institutions set up. It has done this through an inductive approach by using comparative case study and process tracing.

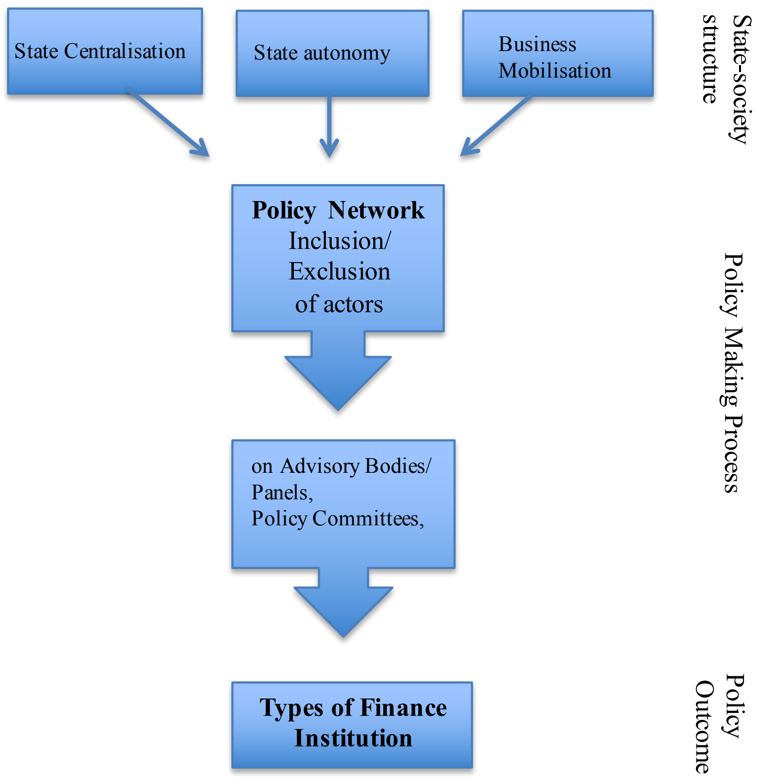
Second, the thesis improves the understanding of how and why PNs influence the form and content of policy choices, which has until now remained underdeveloped. Only a few studies have looked in a systematic way at the effects of PNs on policy outcomes (e.g., Dunn and Perl, 1994; Daugbjerg, 1998, 1998a; Howlett, 2002; Montpetit, 2005). These studies link network characteristics to policy outcomes in terms of continuity and change (Daugbjerg, 1998; Howlett, 2002). For example, Daugbjerg (1998) demonstrates the link between PN and policy types in terms of a continuum between low-cost and high-cost environmental policies. Daugbjerg (1998) finds that tight- and closed-policy communities in sectors that are subject to environmental regulation are associated with low-cost regulation, whereas loose- and open-issue networks are associated with high-cost regulation (Daugbjerg, 1998). Unlike Daugbjerg (1998), Howlett (2002) conceptualises the dependent variable in terms of policy change, and examines the manner in which policy networks affect patterns of policy change by affecting the articulation of ideas and interests in policy processes. He generates a set of hypotheses and tests them in four Canadian policy sectors (Howlett, 2002). Howlett (2002) finds that subsystem structures are correlated with the patterns of policy change and argues that structural PN characteristics are central in either inhibiting or facilitating policy change.

The present study went beyond continuity and change, to say something substantial about the content of policy outcomes. Interestingly only few studies, notably Atkinson and Coleman (1989) have tried to link network characteristics to policy form and content. Although Atkinson and Coleman (1989) offer some broad predictions (in terms of whether policy is reactive or anticipatory) they have not provided hypotheses about the effects of networks on concrete policy outcomes. This thesis addressed this looking at effect of PNs on the form and content of institutional policy choices in terms of the creation of different state finance institutions.

Common to most PN scholars is the fact that they have rarely examined and explicated the mechanisms whereby PNs affect policy outcomes. There are only few, notably Hindmoor (2009), who have tried to link PN types to policy outcomes. Most such studies treat PNs as background factors rather than as independent variables and share the assumption that PNs operate directly via sociopsychological mechanisms to affect policy outcomes (Botterill, 2005; Hindmoor, 2009; Moschitz and Stolze, 2010; Wood et al., 2013). They imply that the agents (i.e. socioeconomic actors) of PNs are automatically part of key policy-making bodies, through which they can influence policy outcomes via priming and framing. This study fills this gap by addressing the question of whether differences in domestic state-society structures influence the choice and type of state finance institutions, and, if so, how and why. By this means, the present dissertation has developed PN literature in terms of mechanisms whereby PNs may have operated to influence policy choices in terms of form and content.

It has looked at the components of PNs, namely, the mobilisation of socioeconomic actors, the concentration of decision-making power, and the levels of state autonomy. It has identified the processes whereby the PN might have operated to influence decisions about state finance institutions (see FIGURE 9.1.). The structure of PN affects policy making and the form of finance institution set up via inclusion and exclusion. An implication of these findings is that the PN literature needs to be strengthened with regard to causal mechanisms (i.e. inclusion and exclusion). Overlooking mechanisms, without establishing a link between PNs, the agents of PNs (i.e. socio economic actors) and policy choices in policy making processes, may lead scholars to underestimate the role of PNs.

FIGURE 9.1. Factors shaping Policy Networks and types of Finance Institutions.



Third, this research has advanced the understanding of the role of distributional aspects in PNs, which until now has remained underdeveloped. Understanding the distributional consequences help to clarify the role of mechanisms in policy-making in terms of network effects and in terms of who loses and who wins from particular types of SWFs. Overlooking these distributional aspects, without establishing socio-economic actors' preferences towards particular policy choices in debates and proposals may lead scholars to underestimate the role of organisational state-society linkages. In Singapore's savings domain, overlooking state-society structure could lead to the incorrect conclusion that the policy outcome of creating GIC mirrored an underdeveloped domestic private finance sector. Different socio economic actors in the debate have different preferences regarding finance institutions. Thus far PN studies have overlooked discussions about different policy choices. Neglecting the investigation of the availability of alternative policy choices may lead scholars to underestimate the role of PNs. The present thesis has illustrated how inclusion and exclusion mattered by looking at the different preferences of socio-economic actors that were part of the PN and those who were not.

Finally, the insights of the present thesis also apply to observable implications in other policy domains, such as trade policy. The variations in state finance institutions in the savings and industrial domains can also be observed in Hong Kong's and Singapore's trade-policy domains. While Hong Kong did not create state finance institutions in the trade domain between the 1960s and 1980s, Singapore created the International Trading Company (INTRACO) in 1968 with the aim of marketing Singapore in overseas markets. One of INTRACO's main purposes was to source cheaper supply overseas and to develop Singapore's export markets. INTRACO did that partly through its holdings in companies that were operating in the transport/logistics sector (e.g., INTRACO Ports Pte Ltd, Transport Services Gatx Terminals Pte Ltd) and the material supply sector (e.g., Goodwin Timbers Pte Ltd and Seasonal Garments Manufacturing Co Pte Ltd) (Lee, 1978).

Another area in which to develop the findings of this dissertation would be through their application to the monetary-policy domain, with the purpose of determining whether the meso-level insights of this thesis also hold on the macro-level. In strong contrast to other policy domains, both Hong Kong and Singapore have established similar state finance institutions in the monetary domain. As of the 1970s, both Hong Kong and Singapore had long-established SWFs with stabilisation mandates (i.e. the Hong Kong Exchange Fund and the Singapore Currency Fund). Hong Kong's Exchange Fund and Singapore's Currency Fund share many similar features. Both had their origins in the 1930s, a period of high currency volatility. Each of them had a liquid coin/notes-portfolio as well as an investment portfolio. Similarly to the Hong Kong Exchange Fund, the majority of the liquid component of the Singapore Currency Fund was held by Crown Agents as deposits in London, most notably as British treasury bills. Like the Hong Kong Exchange Fund, the Singapore Currency Fund was required to provide a 105 per cent backing of its currency in order to fully guarantee the convertibility into silver, and later into the British pound (Lee, 1974). In Singapore, the Currency Fund was managed by the Board of Currency, whilst in Hong Kong it was managed by the Exchange Fund Committee. Until the late 1960s and early 1970s, both funds were also very similar in size.

RELEVANCE OF POLICY NETWORK LITERATURE AMONG OTHER APPROACHES

The structure of state-society relations has an important influence on policy-making and policy choices. The influence arising from the structure of state-society relations in a particular policy domain depends on the centralisation of decision-making power, the autonomy of state actors and the mobilisation of civil society. Even highly mobilised private producer groups may find it very difficult to influence policy-making processes if there is a highly concentrated and autonomous state structure in place. By contrast, when the state structure is fragmented and/or characterised by low levels of autonomy, then highly mobilised domestic private groups may have more of an effect on policy-making processes and policy choices. Likewise highly mobilised producer groups may find it easier to influence policy-making processes if state structure is concentrated and characterised by low levels of autonomy. Hence, the investigation of characteristics of a single actor may not be enough in order to understand their influence on policy making processes and outcomes (see Montpetit, 2005).

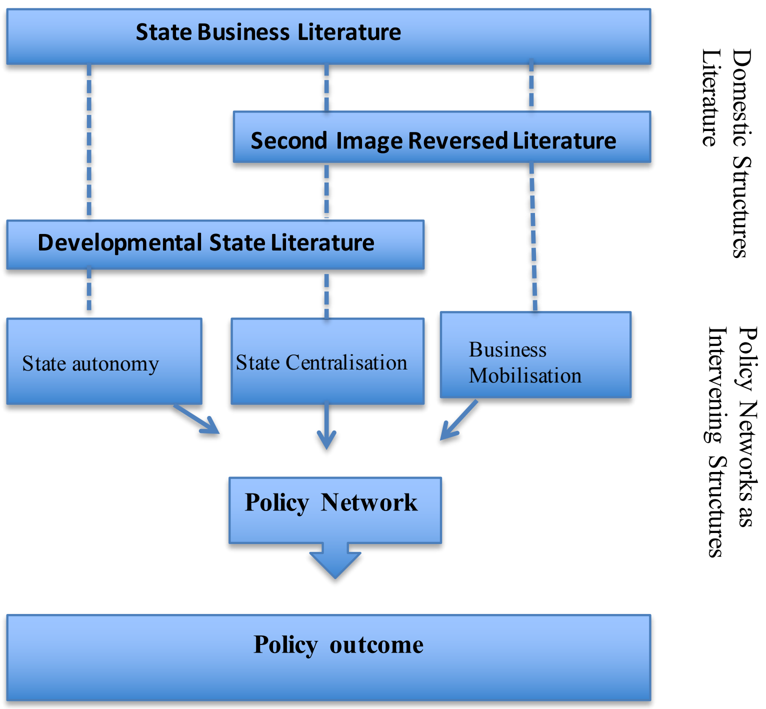
PNs remain relevant as analytical concepts with an explanatory power in contemporary comparative political science. Different types of PNs relate to different organisational maps of state-society relations across policy domains. These maps can be systematically linked to differences in policy-making processes, and as such to different policy choices. For example, between the 1960s and 1980s, Hong Kong and Singapore had similar chambers of commerce, manufacturing associations and large commercial banks, but they were organised very differently with different research capacity. While large commercial private banks had little influence on policy making in Singapore, commercial banks had a large influence on policy making and institutional choices in Hong Kong. The present research has argued and shown that this was because of different PNs. Organised interests that were not part of the particular PN were systematically excluded from policy-making and from advisory committees. This had important implications on policy-making processes and on the kinds of finance institutions set up.

State society relations constitute an important factor in the creation of state finance institutions. Efficiency and diffusion put powerful pressure on the kind of financial institutions set up. PN analysis highlights the need for integrating domestic politics, in the form of state-society relations, in the analysis of policy choices. The thesis draws on PN analysis and further develops it in terms of causal mechanisms and hypotheses regarding the effect of different PNs on the kinds of financial institutions set up. It finds that PNs operated through inclusion and exclusion of socio-economic actors on key policy bodies in policy-making processes, and that SWFs with savings mandates and SWFs with development mandates are more likely to emerge in state directed PNs.

There are important overlaps between the PN literature and other approaches in terms of specific aspects that they mutually consider important in the analysis of domestic structures and policy outcomes. One implication of this is the potential for integrating PN analysis with other theoretical frameworks. This involves drawing on the strengths of one framework in order to develop another. For example, theoretical frameworks, such as the developmental state theory, say little about the intervening structures at the subnational/domain level. However, the present thesis found that these structures are critical in affecting policy outcomes and can vary from one policy domain to another. A PN analysis is specifically interested in this domain-level variation and highlights the fact that variance in the structure of state-society relations at the domain level affects variance in policy outcomes.

The insights derived from such a PN analysis allows for the development of more precise predictions of cross-country and within-country variation in policy outcomes (see FIGURE 9.2). The present thesis treats different types of SWFs as policy outcomes. In line with this conceptualisation, SWFs can be seen as tools of state strategies in the international political economy with roots in domestic politics. In turn, this conceptualisation makes the present thesis compatible with other literatures, notably the literature on the second image reversed, which investigates how international forces influence domestic politics and policy outcomes. Likewise, other literatures, such as that on state-business relations, are interested in the conditions that lead to benevolent collaboration between state and society, which is thought to be critical for economic success. In turn, the PN analysis itself can benefit from the literature on state-business relations, because it looks at the underlying drivers behind the emergence of various state structures.

FIGURE 9.2. Integrating Policy Network Analysis with other Literature



Interviews

Hong Kong

Akers-Jones David, former Governor of Hong Kong, former Chief Secretary of Hong Kong.

Arculli Ronald, former Chairman of Hong Kong Exchange Clearing and Ltd, former LegCo and ExCo member; chairman of different committees.

Bowring Philip, Journalist, expert on Hong Kong politics and economics.

Burns Andrew, Chief Investment Strategist and Personal Secretary to Dr David Li, CEO of the Bank of East Asia.

Burns John, Professor of Political Science, Hong Kong University

Chan Anson, former Chief Secretary of Hong Kong, LegCo and ExCo member, former Director of Social Welfare.

Chow Nelson, former Chairman of the Social Welfare Advisory Committee.

Goodstadt Leo, former Chief of the Hong Kong Central Policy Unit.

Ho Lok Sang, Professor of Economics, Lingnan University

Ho Sai Chu, Vice-President of the Chinese General Chamber of Commerce Hong Kong, former LegCo member, member of the Chinese People's Political Consultative Conference.

Lam M.K. Newman, Professor of Political Science, University of Macau

Lund Pui Chong, former Secretary of Industry at the Chinese Manufacturing Association, Secretary of the Deposit Taking Companies Association Hong Kong.

Mushkat Miron, Professor of International Economics, Chinese University Hong Kong

Ngo Tak-Wing, Professor of Political Science, University of Macao

O'Rear David, Chief Economist Hong Kong General Chamber of Commerce.

Scott Ian, Professor of Political Scienc, Hong Kong University

Sheng Andrew, former Deputy CEO of the Hong Kong Monetary Authority, former Chairman of Hong Kong Futures and Securities Exchange.

Sohmen Helmut, former Chairman of the Hong Kong General Chamber of Commerce, former Chairman of World Wide Shipping, LegCo member.

Yam Joseph, former CEO of the Hong Kong Monetary Authority.

Singapore

Anonymous, expert on Singapore economic policy.

Asher Mukul, Professor of Economics, Lee Kuan Yew School of Public Policy

Katz Richard, former Head of Central Banking Rothschilds & Sons.

Lee Soon Ann, Professor of Economics, National University of Singapore

Low Donald, former Fiscal Policy Director at the Ministry of Finance.

Low Linda, Professor of Business, Lee Kuan Yew School of Public Policy

Ng Kok Song, former Chief Investment Officer of the Government Investment Corporation of Singapore.

Orchard Freddy, former Director of Economics and Strategy at the Government Investment Corporation of Singapore.

Pillay Joseph Yuvaraj, former Permanent Secretary at the Ministry of Finance, former Chairman Temasek and Development Bank of Singapore, former Managing Director of the Monetary Authority of Singapore and the Government Investment Corporation of Singapore.

Prasad Ajith, former Director of the Revenue Division at the Ministry of Finance Singapore.

Rodan Garry, Professor of Political Science, Murdoch University

Toh Mun Heng, Professor of Strategy and Policy, NUS Business School

Wilson Peter, Professor of Economics, Consultant for the Economic Policy Group Monetary Authority of Singapore.

Yeoh Lam Keong, former Chief Economist of the Government Investment Corporation of Singapore.

Qatar and Kuwait

Anonymous Interview, Official of the General Qatar Chamber of Commerce.

Anonymous Interviews at the LSE Kuwait Programme Workshop (2014) *'The International Political Economy of Sovereign Wealth Fund Investment',* Kuwait Foundation for the Advancement of Science. Kuwait, 22 September 2014.

Mr Rabah al-Rabah, Director General of the Kuwait Chamber of Commerce.

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