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Paper 2

Get the Boot for the Loot: How Singapore's Expulsion from Malaysia Led to Economic Success

Although Singapore and the Federation of Malaysia aimed to form a unified state in the 1960s, after conflict over how to rule and govern, "Malaysia voted to expel Singapore" and "Singapore became an independent nation" (Singapore Inc Case, 2). Recently freed from British rule, Singapore fell into a precarious situation; for Singaporean finance minister Lee Hsien Loong "it was a moment of anguish" (2). Would the tiny city-state be able to catch up economically with the west all on its own? Surprisingly enough, throughout the second half of the 20th century, Singapore not only performed well but came out on top in the region: it saw 20-fold GDP growth from 1970 to 2000 (17) and by 2002 "over 70% of all inter-ASEAN trade [moved] through Singapore" (7). I argue that the path dependent and seemingly unfortunate event of Singapore "getting the boot" was actually a key contributor to their extraordinary economic success in three main ways. As a result of being expelled from the Federation of Malaysia, Singapore could capitalize on its optimal location and history as a port for maritime trade, use its disadvantage of few domestic resources and small size as fuel for foreign direct investment, and leverage its large Chinese population for better relations with a rapidly advancing China.

Singapore's factor endowment of the perfect geography for a port city provided it an early boost in trade and a focused policy direction to head in. Located on the coast of mainland

Malaysia between the Strait of Malacca and the South China Sea, Singapore was a "port of call on the Europe-East Asia route" and had "every possible advantage, geographical and local" (2) for being a trade hub in the region. Not only did Singapore have the optimal geography to be a major port—it *was* the major port while under British occupation (2). Although Singapore suffered temporary setbacks after the British left, Singaporean officials knew to take advantage of their experience and existing infrastructure for running a sizable maritime port. The government "gradually removed almost all tariffs and invested in improving infrastructure and the efficiency of its ports", and by 1975, "Singapore was the third-busiest container port in the world" (10) with its trade volume "two to three times its GDP" (10). Compared to Singapore, Malaysia is a far larger and considerably less developed land mass consisting of fewer high-volume trade sites. Had Singapore remained a part of Malaysia, gains from its early advantage would have been distributed across other Malaysian states of lower economic productivity, and it likely would not have implemented trade-boosting policies like "removing all tariffs" (10) since this would have damaged greater Malaysia's ability to build domestic industries. The optimal location and existing infrastructure for a trading port gave Singapore an early economic boost after it separated from Malaysia.

While the small size and limited natural resources of Singapore were somewhat limiting, they forced the country towards a strategy of maximizing FDI which proved beneficial in the long run. Because Singapore's had "no capital of its own in the 1960s, the Singaporean government saw the importance of foreign direct investment as one route to growth at a time when many developing countries were suspicious of foreign investment" (8). Singapore had no choice but to prioritize FDI in order to accumulate capital, a move which Malaysia might have knocked down because of their suspicions. Furthermore, the city-state size of Singapore lent itself well to a less bureaucratic government which was more attractive to foreign investors. One of Singapore's Economic Development Board employees reminisced that the government was so easy to work with that "you could just walk into the EDB office, discuss your project, and lease a factory site or steward building on the spot" (8). Even through the 21st century, the government was such a "highly efficient system" that "a new company could incorporate online in less than 24 hours" (13). The American head of Citibank Singapore himself stated that this ease of access is what makes investing into Singapore attractive for foreigners: "if I have a problem, I have complete access to the government. There is no bureaucracy to cut through" (8). If Singapore had remained another state of Malaysia, government bureaucracy would certainly have been cumbersome, and corporations like Hewlett-Packard and Texas Instruments would have been less willing to invest. FDI ultimately allowed Singapore to attract multinational corporations and gain "employment, technology, managerial expertise, and human capital for the country" (8). That high influx of FDI was only made possible by Singapore's accessible and efficient administration and its necessity to source external capital.

Another factor distinguishing Singapore from Malaysia was its high proportion of Chinese speakers, and this proved beneficial in piggybacking on China's growth. In the late 1900s, "Shanghai threatened to jeopardize Singapore's position as the global financial services hub in the region" so Singaporeans were looking to China as a "next great market opportunity and a considerable threat" (6). Singapore's minister of Trade and Industry decided that "the only way for us to compete is to take advantage of it" by making use of cheaper Chinese inputs and facilitating the internationalization of Chinese companies (8). Singapore's demographics prepared them to build strong Chinese relations: 2002 records show that Singapore's Chinese population was a majority—77%—while Malaysia's was a mere minority (2). As a testament to how far Singapore rode China's back, in 1997 "China surpassed Malaysia as Singapore's top destination for investment abroad" (6). Singapore's high concentration of Chinese speakers helped it build solid relations with Chinese corporations and profit alongside them.

In hindsight, Malaysia made an unwise economic move by letting go of a major trading hub with a high density of Chinese speakers, and Singapore benefitted even more from its ability to independently pursue an FDI-first economic policy. Although anguished by the split at first, Minister Lee of Singapore would eventually come to appreciate the economic miracle that Singapore's independence paved the way for.