Transcript of the Address of Mr Rundheersing Bheenick, Governor, Bank of Mauritius, as delivered at a Briefing Event organized by the Society of Chartered Accountants (Mauritius), Ebène, 14 September 2011[1]

It is always a pleasure to respond to an invitation from friends. I have been talking to you and to some of your colleagues from other accounting bodies fairly regularly. About two years ago, I had the opportunity of addressing a Chartered Institute of Management Accountants' gathering for the region. Before that, one of the Big 5 accounting firms organised a regional meeting and I was very pleased to be the Chief Guest there as well. Over the years, I have come to appreciate what accountants do to keep the global economy ticking. And since I have been at the Bank of Mauritius, I appreciate even more the work that you do to keep bankers on the straight and narrow path. I must tread very carefully here, as I can see some bankers present this afternoon.

Before the crisis hit, we were puzzled when we discovered that the accountancy profession was being accused of some malpractices. Since, we followed the ups and downs of the profession as you proceeded to put Enron behind, and accountants stopped committing suicide – now that kind of role is being played more by bankers. And bankers are now being taken to task for having brought the economy to the worst crisis that we have ever known. Of course, bankers repaid the courtesy by saying it is not their fault. It is the fault of the regulators they say! You should have been keeping an eye on us! You should have regulating it! The blame game is very much on.

Whither the rupee?

I was here, at Ebène, a couple of weeks ago as the Guest Speaker for the event organised by our exporters of Mauritius Export Association (MEXA). Ms Su Lin Ong[2], in her introductory remarks, mentioned the problems that our manufacturing sector, textiles in particular, is facing allegedly as a result of the strong rupee policy of the Bank of Mauritius. Essentially, the interchange with MEXA was all about where the rupee was heading. The theme of my address was "Whither the rupee?" or "Wither the rupee!" like the rupee should wither on the vine, to make a joke out of it, and reflect the thinking which I thought was at the root of inviting me to come up and address the MEXA people in the first place, maybe with some wishful thinking as well. Basically, depreciate as fast as you can. I am not macho about the value of the rupee, far from it. But I thought it is the task of a central bank Governor to defend the value of his currency and to talk it up, not talk it down. So, I was here in an audience where all the members present were basically very keen to talk down the rupee and I was probably the only taking a contrary view. I thought the best way to try to reflect that, in my presentation then, was to show two bulls locking horns, one being obviously MEXA and the other, the poor Bank of Mauritius, and I had thought one of us was likely to end up as minced meat. Luckily, we both survived, and I am sure that MEXA has very bright days ahead of it.

[1] *Transcript may be read together with the Powerpoint presentation which can be viewed at http://bom.intnet.mu/pdf/communique/PPT_20110915.pdf*

[2] *President of the Society of Chartered Accountants*

We should achieve our goals collectively as a nation and we should not try to steal a march on our fellow compatriots, especially the poor, the vulnerable and the weak. A stable rupee that contains the cost of imports, a stable rupee, that prevents inflationary pressures being passed through the exchange mechanism, is probably the best contribution that the central bank can do. Obviously, I do not expect any exporter who is concerned about his own bottom line to share that particular perspective. And I am happy we have been doing our job and we will continue to do so to maintain our economy on an even keel.

Whither Mauritius?

I thought the best thing that I could do today is to pick up from where I was, when I was here three weeks ago, although the audience is different, this time not to address the question of "Whither the rupee?" but "Whither Mauritius?". I like to believe that before we start to chart out where we want to go, it would be good to know where we are starting from. I am sure that you know the story about this tourist who was driving around in the Irish countryside, where road signs were not that good, and lost his way. So, he stopped somewhere and he found somebody in a field, called him over and asked him *"Is this the right way to Dublin?"*. Paddy removed his cap, scratched his head and said, *"If I were going to Dublin Sir, I wouldn't be starting from here"* .

It is good to situate ourselves, where we are in the current global environment, which is characterised by a high degree of uncertainty and volatility, and where fears of a double-dip recession have come back to the fore. I feel that the global outlook is vital for an economy like ours, which is very small and cannot grow its way out of its problems, like larger economies can. Our degree of openness imposes a certain discipline on us that we have to reckon with, when we recommend any kind of policies to take us forward.

The Northern Atlantic part of the world is going bad

The uncertainty was supposed to have lifted at least two years ago. When the crisis hit, we were told that it would be behind us very quickly; that the clouds may be dark but we have silver linings; that Mr Bernanke and Mr Trichet were on the job and that we would begin to see results; and that the solution to the debt problem was to flood the world with a bit more debt. Some of us were a bit puzzled by this approach; but then, when you think about it, perhaps that is the only solution left. At that time, there may have been other solutions. A few countries in Europe had tried to adopt the opposite approach. They started off on a dose of austerity before others thought that we should all go down that route.

There are two schools of thought here – the Keynesian route and the austerian school route. And when the British started down the austerity path, they got good marks from the markets. Others ended up being de-rated. I am not sure we have any precedent for the US being de-rated as Standard & Poor's did, although I am told that the first rating agency to de-rate the US recently was actually a Chinese rating agency about three or four weeks before Standard & Poor's did so. We have seen these two schools of thought in action. In the US, we have had major problems with the banks and we still have not seen their last. The US is going now after QE2, which did not have any results so far. The recovery is still not there. The unemployment rate is very high. The poverty incidence has increased. Figures came out only yesterday that it has never been as bad as it is now during the last forty years, since these particular measures have been deployed. So there is a rising incidence of unemployment, of poverty, of family breakdown, of instability. In Europe, we have seen how the sovereign debt crisis has snowballed, building up slowly from Ireland to Greece, possibly going over to

Spain, Italy and, some say, even France. We have heard about French banks, large French banks running into serious trouble. So that is basically the picture in the northern Atlantic part of the world, which was calling the shots until now. They were responsible for operating the international financial system; they were responsible for keeping open trade channels – the only way for small countries like us to hope to survive in an economy – and they were the ones who were ready to bail out other countries as the latter got into difficulties and problems of indebtedness. They are themselves having to be bailed out now. It is the first time, I think, that we in Africa can sit back and say that we are not to be blamed at all for what is going on; the blame is up in the North.

This is exactly the kind of situation which is reflected by the BRIC countries[3] offering to come to help Europe, a few days ago. Unheard of! Unprecedented! Who would have thought when the euro was being launched that the emerging world was going to have to bail out the euro zone? Who would have thought that China would have been roped in to keep propping up the US dollar? So here we have two major reserve currencies in which all of us over the world have been stocking our bonds, and both of them are in serious trouble.

The uncertainty is given for a small open economy

So, the uncertainty that we see at the level of the global economic scene, at the level of the major players, is something that we must take as being given for a very small open economy, which is not a major player and which must adapt to what goes on in the outside world. This has had major implications for volatility. Some people say that our stock exchange market is volatile, share prices have gone down – I do think that a few shares are quite volatile; and if you look at the rates at the hotel counter or at the bank counter, they have been very volatile too, because precisely the volatility from overseas seeps into our own market and we are completely overlooked. And it is not because of domestic economic concerns, nor because of domestic PE ratios being out of line. So the volatility has also reached unprecedented proportions. I think that we have to go back to eight to ten years to find the VIX or the VSTOXX having similar high levels of volatility.

The fears of a double-dip have been magnified. I have a slide showing what the recovery looked like, where it was at the bottom of the cycle, how we started picking up out of it, how we had a tiny dip where the curve almost looks like a square root and then it picked up slightly and now it is heading towards very fast. If we take that together with the meltdown in the euro zone area and the fears about the survival of the euro as a currency, we have reasons to be scared about the future. If the whole world begins to run into strong headwinds, it is next to impossible for a tiny country like ours to expect to survive in that. So, when we have so much heightened volatility, so much uncertainty from the outside world and the global environment, we should be grateful for the kind of stability that we have been able to achieve here.

Growth rates globally have been revised downwards

Let me now take you to how the global environment has performed in terms of growth rates, for example, in the wider world, in the countries that really matter globally. If you look at the World Economic Outlook which the IMF releases regularly, you find that growth forecasts for the developed markets have been revised downwards by more than one percentage point, and going down from 2.5 per cent to 1.9 per cent just over the last six months. In the

[3] *Brazil, Russia, India And China*

emerging markets, they have been revised downwards, from 6.1 per cent to 5.7 per cent, and if you go back to the beginning of the year, they have been revised by 0.2 percentage point. In the US, the largest economy in the world, growth forecast been revised by nearly 2 percentage points. For the euro area, it has declined slightly, but the prospects were not very good in the first place at the beginning of the year. In the UK, it has been revised by one and half percentage points between the beginning of the year and the last forecast. So, if we situate our own growth rate against that, I do not understand why people can claim that they are having serious trouble, that we have become all confirmed pessimists and heading downhill.

Where do we situate ourselves?

Our growth rate has been positive throughout this crisis. We have not had growth rates above 5 per cent but we have been below trend for quite some time now. A crisis is the worst time to think that we should be above trend or near trend. If you compare our own growth rates, the revision that we have brought in recently is of 0.2 percentage point, not even one percentage point. It is still a very hefty growth rate of 4.4 per cent that we expect to achieve. So, there is no reason for this creeping pessimism that seems to be getting hold of some of our economic operators if you compare what the economic situation is in some of the major countries.

The volatility/fear factor which is spreading again – I used the VIX and the VSTOXX reference earlier – you will find that it has reached the highest rates over the last ten months or so. Global growth has started going downhill and, whatever we do, we cannot correct that. There is no way for us to try to make up for the US losing traction or for even China and India beginning to revise their growth rates downwards. What we can do is to try to be more flexible and to adapt to the new emerging markets and try to position ourselves to exploit any opportunity that this kind of turmoil throws up – because there will be opportunities. So this is the global environment confronting us and it is good for us to know how we ourselves, in Mauritius, got here. And I think that I will take you back to the situation that we faced when we became an independent country.

From a GDP less than US$200 per head to a US$10 billion economy but….

We were a mono-crop economy; we depended entirely on sugar. Whatever was good for sugar was good for the rest of the country. We still have some parts of the way we conduct business which trail back to those times. We still believe we can apply some policies across the board across all sectors – what is good for one sector is equally good for the other sector. This way of thinking goes back to our sugar heritage. If you look at this slide, you will see that growth has been coming from all these red blocks that you can see on the map – the tertiary sector. And to answer the question of the Chair earlier whether our future lies with services: Yes, "services" is very much the way of the future.

The primary sector – bad news for those of us who believed that Mauritius had no future after sugar – *l'après-sucre*, or something to scare everybody, and *l'après-LOMÉ* was unimaginable. See what happened to sugar at the bottom of this chart. Sugar has been reduced to quite insignificant in the way we conduct our business. Manufacturing has become quite important – in spite of the fact that people thought Mauritius could not have any manufacturing future. But it also needs to keep adapting continually because we have no natural resources. Whatever we possess, we must sell to markets which are competitive. And we have to find these markets and fight for market share.

The next chart shows you that we have done in terms of our GDP. It shows you that overall, the GDP of our country was barely measurable, and to make it measurable, we ought to have a chart starting from the floor going up to the ceiling, so tiny was our economy. Some of you will remember that, at that time, we were an IDA country, IDA – International Development Association, the window for poor countries. We were an IDA-eligible country with GDP less than US$200 per head. See what has happened to our GDP. Total GDP of the country has risen, almost exponentially. We now are a US$10 billion economy. Our GDP growth has averaged around 5 per cent over the period. So we feel that this country has shown that by staying open, by following the right policies, it has been able to survive very tough times. We have reinvented ourselves when the sugar market collapsed; we reinvented ourselves again when the MFA agreement was dismantled and found other sources of growth to keep us going.

While we were doing that, unemployment, which was the number one problem in the country when we became independent and very high historically, at a time when many of our countrymen were actually leaving the country, in large numbers, and Government actually had a minister responsible for emigration so as to facilitate exporting people. That was the situation in the late sixties and late seventies. We moved from there to a situation where we have now 20,000 foreigners working here and our people do not want the kinds of jobs that are available. Our unemployment rate is below 8 per cent. It stayed below 8 per cent whereas in some countries on the African continent, the figure is nearer to 25 per cent. So we should count our blessings; we have been doing many more things: our policies have been the right ones; we have been able to reengineer ourselves; we have been able to create jobs; we have been able to fight poverty; we have been able to follow the Millennium Development Goals even before these goals were specified elsewhere. We have achieved higher levels of education; we have achieved longevity; we got out of the poverty trap; we have improved the health conditions in the country; we have reduced mortality rates and our current problem is probably one of a middle-income country. Our problems arise from the fact that many of us tend to believe that all these were achieved with little or no effort; that things are so good that we have just to carry on to do things the same way we are doing it. This is the complacency that comes with the middle-income trap.

So I believe that we must dispute any attempt to try to continue what we are doing; we must dispute all those who believe that we should not change. I think change is the very much the order of the day. In a world which is in turmoil, the only possible source of safety for Mauritius is to change and to change fast. Up to now, we have been able to show our resilience and to prove the truth of what Porter, for example, said of competitive advantage. We have been creating competitive advantage basically out of a situation which could make people despair.

Yet, now we have to go to the next stage; we have to go beyond competitive advantage and try to create adaptive advantage. We must adapt all our policies, all our systems, all our procedures in public sector, in private sector to be able to exploit the new markets.

I have a chart here that shows how middle-income countries are doing. Our country is second – the blue from the bottom. Unlike most other countries, our economy did not go down. Even Singapore – mighty Singapore – top of the chart wobbled before it started picking up again. Hong Kong wobbled, Ireland tumbled. Mauritius remained steadfast, stable rising. So, we should not talk down our country. We should not talk down our prospects. We have been doing many things quite well and we will continue to do that equally well. So long as we are prepared to question many of the assumptions that we have, so long as we are prepared to reengineer ourselves and not be afraid to be the first in particular areas. The chart shows that we have guaranteed rising real growth and national disposable income to our workers, to our population. But things do not look so rosy when we look at national savings.

The chart shows that national savings go down from the high rates of above 25 per cent, nearing 30 per cent, which we had about 20 years ago and have kept declining consistently. The growth of our economy is not consumption-driven. We have to increase our savings rate; otherwise there is more indebtedness staring at us in the face. The mirror image of the declining savings rate is a declining investment rate. Our Gross Domestic Fixed Capital Formation (GDFCF) has also been going down. And the distribution of our GDFCF between public and private is also a cause for concern. Normally, you would have thought that when GDFCF goes down, it is up to the public sector to try to pick up the slack and to lean against the wind with countercyclical investments. All of you know that our public infrastructure has been suffering from underinvestment over many years. We have to make up for it and there is no better time than when there is plenty of slack in the system. This can actually give an extra fillip to growth in the country.

Let me now address some emerging concerns that have come up since. Of course, we regularly gauge ourselves on some good news. We are top of the list in the *Mo Ibrahim Index*. We celebrated that. Mr Mo Ibrahim and the whole crowd came to Mauritius to crown us. In the *World Bank Ease of Doing Business*, we are top in Africa. In the *Heritage Foundation*, we are number 12; we are first in sub-Saharan Africa again. So all these make headlines here. Rightly so!

In the Global Competitiveness Report, which the World Economic Forum released a couple of days ago, Mauritius has done well in the overall ranking. We have improved by one notch, passing from 55 to 54. And there is only one country in Africa, a large one, ahead of us: South Africa. But there are other rankings there which should make us pause and reflect a little on what we are doing wrong and how we can improve our rating.

First among them – I referred to that earlier – it is this belief that we are still guided by one sector that determines everything else in the country. We must change that mind-set. If we want to adapt our country and come out as a winner tomorrow, we have to change the way we conduct our business; we show up very badly in terms of flexibility in wage determination. Do you know what our rank is? We are 107th in 138 countries. I am sure we can do better. Singapore, the country with which we compare normally is number seven on that ranking. So the gap between Singapore and us is 100. There are 100 countries between Singapore and Mauritius in terms of labour market flexibility, whicht entails hiring, firing, ease of changing jobs and rewarding people based on performance, and on what they are contributing to the enterprise. Flexibility in wage determination in our country is therefore a must.

I move to the quality of education, another sore point. With regard to the quality of education: we are number 67. And if I compare with Singapore, Singapore is top of the class – number one. The gap between Singapore and us is 66. So if you want to catch up, if you want to become this knowledge hub that we talked about, there is a lot of work to be done. This has an immediate repercussion on the innovation index. Again, this international ranking ranks us as number 89. Singapore is number 8, difference of 81 countries between Singapore and us.

In terms of our savings performance, we are number 98; Singapore is number 7. There are 91 countries between Singapore and us.

And I come to the more critical one, one which is very close to the banking sector: the interest rate spread. With regard to the interest rate spread, we are number 118: there are 50 countries between us and Singapore. Singapore does not do well on that account either: it is number 68. Let me tell you which countries we are keeping company with as number 118; you may find it enriching. They are such leading lights as Zimbabwe and Madagascar, Kyrgyz Republic, Tajikistan, Haiti and Cambodia.

I am sure we can do better in improving our global ranking and in trying to see how our banks can help us to move in that direction. I am sure, had we not had this bad rating in terms of interest rate spread, we would have had a higher raking overall. In the whole of Africa, only nine countries out of 52 in Africa have a higher spread than Mauritius. And we like to believe that we are a leader in Africa. Now if you think that it is a blame on the central bank, the regulator, it is decent to add that the central bank has been concerned about spreads and we did have long discussions with the Mauritius Bankers Association (MBA) to see how we could reduce this. The MBA had conducted a study which showed that we are doing quite well compared with the African countries. So there are two ways of interpreting the World Economic Forum data. They probably used criteria which make Mauritius appear in very poor light and make others appear even brighter, which I would discount as a remote possibility. I think the World Economic Forum is sufficiently credible to apply a consistent methodology. So I think that number 118 is something that we must go to work on seriously.

I think that we have problems, beyond the banking sector, which should be addressed by the regulators in those sectors as well. I think we have many regulators, whose job is to try to improve the performance of the sector that they are supposed to be looking at. And we, on our side, are happy to work, with whoever, to try to ensure that things are moving across a broad front to improve our own ranking.

Our banking sector is safe and resilient

Let me come to the regulatory landscape very quickly to talk about what the central bank has been doing. Basically, we have been aiming at having greater transparency, to improve efficiency in the sector and we think this is one area where the accounting profession also has a big contribution to make. Our banks are by and large very sound. They made wonderful profits, perhaps too wonderful. We will have to look into it. The capital adequacy does not give us any cause for concern. Our capital adequacy ratio is around 14-15 per cent while the minimum requirement under the Basel II framework is 8 per cent.

We have no concern about financial stability. Our concern in that area is the overwhelming concentration of banking sector assets in just two banks. We have an index called the Herfindahl–Hirschman Index (HHI), which measures the degree of concentration in the banking sector. Our HHI stands at 2024, well above the figure of 1800 which represents high concentration. The assets of our two largest banks exceed the total combined assets of the 15 other banks with domestic operations by more than 30 per cent. We believe that more competition in the banking sector will lead to a higher level of stability and will contribute to entrench our resilience. Maybe that more competition would have helped us to reduce those spreads, which led us to be number 108.

We are introducing macro-prudential supervision to assess the impact that different banks and systemically important banks have on the rest of the economy. It will also help us to ensure that the monetary transmission mechanism works properly in the country.

We have also started discussions about the advisability or otherwise of moving towards a single regulator for the entire banking and financial sector.

We have also normalised the yield curve. In the past, our yields were rising very steeply. People were very short-sighted and the horizon where there is more competition was getting shorter and shorter. We have moved basically to a straight line but there are two remaining kinks which we hope to flatten, now that we have introduced a larger measure of monetary and financial stability. A flatter yield curve will be very good for the corporate sector as well, given that we want to introduce benchmark bonds, which might serve as pointers, as anchors for the corporate sector to introduce their own bonds. We have also taken measures to develop our secondary market and we are soon to introduce single-maturity auctions of Treasury paper.

So all these measures have been taken to ensure that the banking sector is well-regulated, that there is depth in the market and the environment is conducive for the safe-keeping of assets, and that ultimately the decline in savings that we have been witnessing in the country is corrected.

We need to revisit our approach to strategic thinking and strategic planning

Where does all this take us? I believe that there is a strong case for us to revisit our approach to strategic thinking and strategic planning. We allow people who speak for particular constituencies to make the headlines and to influence the agenda. And I strongly believe that we deserve better. There is a need for a central public-private joint operation to focus on medium-term to longer-term issues in a dispassionate way. Too often, when we had debates, we cannot leave behind the official hats that we wear in our normal life. And I strongly believe that part of the reason why we are here today, why we have been able to move away from an IDA country to a country with a US$10 billion GDP is because we had that critical power to think and to reorient our strategies. And in a crisis like the one we are going through now, I think that it is more than ever vital that the public sector and the private sector pull in the same direction, that we do not seek to hang on to sectors that are losing steam, that we seek out possible sources of competitive advantage and put everything together to try to realise our vision of making this country one of the successes of tomorrow.

I believe the days when we could be a competitive primary producer are rapidly going. The days when we can be a competitive producer of undifferentiated commodity textiles are rapidly disappearing as well. But there are still bright days ahead for us in textiles where we have built up competence; we have built up confidence of our buyers. There are bright days for us but in a slightly different format: we must leave commodity textiles and go in for middle to upper range garments, we must go in part of the supply chain where we can leverage the confidence that we have in the market to still deliver and bring benefits for the entire Mauritian nation.

The same thing applies to tourism. There are people shrieking that we are losing market share. If the markets themselves are collapsing, if the markets in Europe are not growing as fast as the tourism markets in Asia, as shown for example, in the rates of growth in tourist arrivals – tourists coming from Europe are growing around 2 per cent; tourists coming from

Asia have grown at 24 per cent – probably, it is up to us to go and adapt our product and adapt our processes and adapt our seat availability to be able to tap this market instead of sitting back and saying *"Give me a new currency fix then I will be able to survive, I'll be able to compete"*.

We all have to look in the same direction whether we are from the public sector or private sector, whether we are the operator or the regulator or the policy maker. We do not have to give in to this ambient pessimism that is creeping in on us from every side. There are dark clouds on the horizon. We have been through dark clouds but all dark clouds have a silver lining. I think we should focus on the silver living and there are many of them.

Thank you for your attention.