“Fostering Africa’s growth in the New Reality – From Vision to Action”

Address by Rundheersing Bheenick, Governor, Bank of Mauritius at the Opening Plenary of the SWIFT Africa Regional Conference
Mauritius, 30 May 2011

It is a pleasure to be here this morning and to address you at the Opening Plenary of the SWIFT Africa Regional Conference. Let me add my own words of welcome to the foreign delegates, especially those visiting our country for the first time. I have no doubt that you will be joining the ranks of satisfied repeat visitors as you discover for yourself how right one of our earliest publicists was when he claimed boldly that Heaven was copied after Mauritius. The name of the publicist? A certain Mark Twain. He may have been exaggerating – but just a wee bit! I thank SWIFT for giving me the opportunity to share with you some thoughts on the theme of **“Fostering Africa’s growth in the New Reality – From Vision to Action”**.

I shall focus on the need to strengthen Financial Market Infrastructure (FMI) in our region. FMIs play a key role in promoting financial stability and economic growth. When financial markets get the jitters, the world economy grinds to a halt, as we have just painfully re-learnt. It is difficult to think of a more appropriate topic for a gathering such as this at a time when we have all become acutely aware of the importance of strong financial markets for economic prosperity. It is true that much progress has been made in strengthening FMI in Africa; it is equally true that much remains to be done as African financial systems are still lagging behind and are weakly integrated with the global financial system. As policymakers in advanced economies direct their efforts towards global reforms for a more robust global financial system, it may be a suitable time for some FMI initiatives in the African region.

First, let me briefly recapitulate the scope of SWIFT’s activities and operations in the global FMI, just to give the uninitiated some idea of its systemic importance and explain why regulators take such a close interest in SWIFT. A few metrics will suffice to give you an indication of the criticality of SWIFT to the operation, safety and soundness of the global financial system. Since it was set up in the mid-1970’s, SWIFT has rapidly become an indispensable element of the global FMI. It connects over 9,000 financial institutions in more than 200 countries and territories. We learn from SWIFT’s 2009 Annual Review that 3.76 billion FIN messages – FIN is SWIFT core store-and-forward messaging service – were exchanged in that year. That means 15 million messages everyday. SWIFT has experienced exponential growth since it sent its first message in 1977. And it is extremely reliable. With 99.99 per cent availability of FIN and SWIFTNet, SWIFT truly lives up to its motto: “Failure is not an option”.

The use of SWIFT allows FMIs to support near real-time payment services using a single standard messaging platform within a private, secure and reliable environment. This leads to lower costs, lower operational risks and less operational inefficiencies. Because FMIs facilitate the clearing and settlement of monetary and financial transactions, safe and efficient FMIs are particularly important for maintaining financial stability. Their critical role comes to the fore in times of crisis when, given the interconnectedness and interlinkages of the global financial system, systemic risk is at its peak. If FMIs are not properly managed, they can pose significant risks to the financial system and be a potential source of contagion.

An efficient cross-border clearing and settlement process is a *sine qua non* for global markets to operate seamlessly and efficiently. Cross-border credit transfer services are a legitimate concern of regulators. They must be rapid, efficient, reliable, cheap, and able to cope with a rapidly-changing financial landscape. By transporting financial messages, SWIFT is at the heart of the global clearing and settlement system. If SWIFT didn’t exist, something looking like it would have had to be invented.

SWIFT is part of the plumbing of the international financial system. Plumbing plays a vital role in our homes; but it is normally hidden away, tiled over, and taken for granted. It is certainly not the subject of polite dinner table talk. Until, that is, when it springs a leak, malfunctions, or clogs up – when fixing it becomes the utmost priority, on pain of having no dinner, never mind the talk. So it is with SWIFT. And it is because of this systemic importance that the central banks of the G-10 countries agreed in 1998 that SWIFT should be under cooperative oversight by central banks. As SWIFT is established under Belgian Law, the National Bank of Belgium functions as the lead overseer.

The crisis has been a stressful time for all financial sector players and their regulators. FMIs performed quite well during the financial crisis. The severity of the crisis has brought to light important lessons regarding effective risk management. This has led international standard-setters to review and upgrade existing standards. In March this year, the Committee for Payments and Settlement System (CPSS) of the Bank for International Settlements, in collaboration with the Technical Committee of the International Organisation of Securities Commission (IOSCO), reviewed the principles for FMIs, again highlighting their critical role in fostering financial stability. This review supported the Financial Stability Board initiative to strengthen core financial infrastructures and markets. I will not bore you with the detailed list of standards for FMIs. Let me mention a few salient points. First, they are mainly expressed as broad principles that CPSS/IOSCO strongly recommend that their members should implement to the fullest extent possible. Second, they aim principally at harmonization across FMIs and countries. Third, the report also outlines the general responsibilities of central banks, market regulators, and relevant authorities responsible for FMIs, in implementing these standards. You might think that this renewed interest in beefing up standards would have got the regulatees and their lobbyists up in arms. Quite the contrary. Gottfried Leibbrandt, Head of Marketing at SWIFT, supports these moves:

"Standards underpin all hope of progress to a more efficient global financial services industry".

And I fully agree with the Chairman of SWIFT when he says that, as the world slowly emerges from the worst crisis of our generation, regulation and supervision will continue to be crucial elements for maintaining financial stability. The contrast with the reaction of global banking leaders to the proposals of the other Basel Committee, BCBS – the Basel Committee on Banking Supervision – to tighten supervisory standards and increase capital requirements for banks, especially those deemed to be systemically important, couldn't be more striking.

There are currently many market initiatives in various parts of the world. These seek to address the gaps identified during the global financial crisis in the FMIs in the leading financial centres of Europe and North America. But, interesting as it may be, it will take us too far afield to wander off in that direction. Let me turn to FMIs in the African region.

Financial Market Infrastructure in Africa

Modern attempts to build Pan-African payment systems actually started in the eighties. These sought to strengthen regional cooperation and facilitate trade between neighbouring countries. But well before that, in 1946, several decades before the Euro, the 14 countries of the West African Economic and Monetary Union (WAEMU) had already adopted a single currency and had actually set up their central bank in 1962, the *Banque Centrale de États de l'Afrique de l'Ouest* (BCEAO). 1981 saw the establishment of the Preferential Trade Area, a free trade agreement between east and southern Africa, of which Mauritius was a founder-member. This was succeeded in 1994 by the Common Market for Eastern and Southern Africa, which has emerged as one of the pillars of the proposed African Economic Community. The Southern African Development community (SADC) was launched in 1992, building on the Southern African Development Coordination Conference (SADCC), itself set up since 1980. Mauritius joined SADC in 1994. SADC has worked on the harmonisation of payments systems among its member states with the result that today all members of the SADC either have, or are in the process of implementing, a Real Time Gross Settlement (RTGS) system. There have been initiatives to integrate

African capital markets and one of these is the Regional exchange, the *Bourse Régionale des Valeurs Mobilières* (BVRM). In SADC, a number of initiatives have been launched to create a FMI by 2018 on the assumption that there will be monetary convergence and a SADC Central Bank by that date. There are parallel, if not overlapping, programs and projects at the level of COMESA, AACB – the Association of African Central Banks –, and the African Union. All of these draw their inspiration from the desire for greater integration in Africa, culminating ultimately in the distant future in the realisation of the vision of a United States of Africa, with a common currency and a common central bank.

However, despite this grand, overarching, vision – and a flurry of loosely-coordinated actions and initiatives to realize it –, the reality on the ground is that, African financial markets remain fragmented and costly. The integration of African payments systems into an FMI has a long way to go. The financial infrastructure of continental Africa can best be described in terms of adjectives of extremes. Payment systems range from the highly advanced to the underdeveloped; banking systems range from highly regulated to purely market-driven systems; and banking penetration ranges from several bank accounts per head to the highest proportion of unbanked people. Over the years, Africa has become the testbed for a number of a number of innovations in payments. Technology has made a remarkable breakthrough allowing banking services to reach the unbanked – the *M-Pesa* Mobile Banking in Kenya is a case in point.

Paradoxically, Africa is the third-fastest economic growing region in the world, behind Asia and the Middle East, with an annual average growth of around 5 per cent, driven by the rising global demand for commodities from the BRIC countries. Investments in Africa are now based on a new trade-related model. For example, as India and China become the major trading partners of Africa, and increase their dependence on the continent, they are investing more than the colonial powers did in the development of natural resources, building infrastructure such as roads and airports, and providing services such as banking. So there are now tremendous business opportunities for the African continent, as it hitches its wagon to the rising stars of the global economy. Its economic outlook can only strengthen further, driven by high commodity prices and strong external demand.

The question that arises is whether African countries will be able to put in place rapidly the FMI to support and stimulate these trade and investment flows? It is recognized that the development of a healthy financial sector is critical for countries that experience rapid growth. A recent World Bank publication, released about a week ago, 'Global Development Horizons 2011', comments on how Mauritius witnessed a further acceleration of economic growth in 2009 as private consumption rose. This new phase of growth was accompanied by the rapid expansion of domestic credit and the development of financial markets more broadly. Failure to develop the appropriate FMI can dampen growth prospects and thwart development efforts in Africa.

Regional financial integration

However, solo and unco-ordinated efforts by countries acting individually and independently may not bring the African continent to a new level of development. For me, part of the solution clearly lies in hastening the process of regional financial integration. As I mentioned earlier, there have been significant strides in the direction of regional trade integration in Africa. But, drawing from the lessons learned from the problems encountered by the European Union, I firmly believe that regional trade integration should go hand in hand with regional financial and monetary integration. And we must reckon with our African realities. We all know the PIIGS story, where some believed that pigs could actually fly! As countries in the Eurozone periphery face a severe sovereign debt crisis which threatens the foundations of the Euro, they are being bailed out by other, much-stronger, partners. It is not clear whether any African countries are either prepared, or indeed able, to bail out their peers in case they confront similar difficulties. A fiscal union and a transfer union cannot be far behind monetary union. We must therefore proceed cautiously. We should not rush into a monetary union. Financial integration can very well take place without monetary union in the first instance.

Limiting our sights to regional financial integration, does not imply any lack of ambition. It does bring many benefits for Africa. First, it would provide incentives for domestic financial reforms. Second, it would increase the scale of operations. Third, it would spur competition. Fourth, it would increase FDI inflows. And it would enable African systems to become regional, and ultimately global, players in financial markets. But, to achieve regional financial integration, there are certain conditions that must be met and a key requirement is macroeconomic stability. And this is a pretty tall order, if you take into account the fact that African economies are so vastly different on so many counts.

There are problematic asymmetries ranging from production structures to institutional effectiveness—such as democratic accountability, the incidence of corruption, and government efficiency. All these contribute to major disparities in economic performance, including public finance, and dependence, public debt, balance of payments performance, inflation, and growth. Between 2000 and 2007, annual growth in sub-Saharan Africa was around 6.5 percent – the highest rate in more than 30 years. This was accompanied by low or moderate inflation and growing macroeconomic stability. Then the region was hit by two global economic shocks, the sharp increases in food and energy prices of late 2007 and early 2008, and the onset of the recession later in 2008. The crisis came at a time when sub-Saharan Africa was in a much better shape than it had ever been before, and was resolutely heading for higher growth and faster poverty reduction. Although, at the beginning, the effects of the crisis were not felt, given the limited integration of the African financial system with the global financial system, their second round impacted negatively on macroeconomic convergence and regional financial integration efforts.

This led many to argue that the process of regional financial integration should be delayed or put on hold while awaiting better times. This view has been reinforced by the recent geopolitical tensions in the North African region, which has added grist to the mill of the confirmed Africa-skeptics who point out that Africa heads the hit-parade of failed states.

For the optimists, the crisis brings new opportunity as Ms Antoinette Sayeh, – coming herself from a failed state, and now Director, of the African Department of the International Monetary Fund – said in a speech entitled 'Sub-Saharan Africa: Challenges for 2010' at The Brooklyn Institution (November 2009) : "*…new engines to drive strong growth will be needed in the post-crisis period. Measures to improve the business environment, develop well-regulated capital markets, increase labor productivity, and enhance efficiency in the public sector will be crucial*".

Policymakers therefore face the daunting challenge of coming up with key policies aimed at reducing gaps, inequality and income differences across the region in order to transform it into regional single markets and regional production bases that are fully integrated and more competitive in the global economy. Melding the different countries into a regional bloc, with free movement of goods, services, skilled labor and free flow of capital, implies that there will be an increasing flow of funds, or payments, between economic agents in different countries and greater cross-border trading of securities. FMIs, that are harmonized, standardized, inter-operable, and inter-linkable, are fundamental requirements to achieve truly integrated markets in the region. While I am convinced that this is the way forward for Africa, I am perfectly aware of the many hurdles that that need to be overcome before this kind of ambition can become a reality. For example, the efficient functioning of a payments and settlement system, a vital component of FMIs, relies on the appropriate infrastructure being put in place i.e. telecommunications, acceptance networks, internet access etc. While many countries in the African region have made significant efforts towards implementing RTGS systems, in setting up ATMs, or effecting payments through mobiles, many still lack reliable telecommunications, good road networks, or even electricity. Another area that requires attention would be region-wide regulatory frameworks, and adequate supervision to keep pace with the expansion of cross-border banking and other financial services areas.

Financial Market Infrastructure in Mauritius

That's enough about the continent for this morning. Let me tell you a few words on our own efforts to enhance our FMI. In spite of the smallness of our economy, the FMI in Mauritius is quite developed. It has gone through a series of transformations over the years. These were made possible because we could piggy-back on state-of-the-art telecommunications infrastructure, providing global connectivity. As we welcomed global players in our jurisdiction and as our economy developed, the Mauritian financial system became increasingly integrated with international financial markets. On the downside, we also became increasingly exposed to the risk of instability, and more vulnerable to external shocks. The Bank of Mauritius has the responsibility to ensure the stability and soundness of the financial system of the country. While this financial stability role of the Bank is not a new one, it was brought into sharper focus by the legislative changes to the responsibilities of the Bank in 2004. In practice, the Bank would look at the robustness of the core financial infrastructure, which includes the payments and settlement system, and identify potential triggers, in times of stress, that could lead to a crisis. The safety of the payments and settlement system is a major concern for us not only because of the risks embedded in the system, but also because we are a fully-monetised economy where a small hiccup in the system can rapidly lead to a major economic disruption. Also, the payments and settlement system is the channel through which monetary policy is transmitted – failure of the payments and settlement system would translate into a failure of the monetary transmission mechanism and monetary policy would be ineffective.

The Bank is concerned with the efficiency and effectiveness of the payment system. As operator of the system, we have influenced its design and evolution. We directed our efforts to modernize the system, to make it more efficient, and more resilient to the risk of potential financial market instability. What distinguishes our payments and settlement system is that it is an integrated system. Our system has become a model for the region – we have been receiving a steady stream of delegations from other central banks in the region interested to look at its intricacies.

Modernisation of our payments and settlement system

The first phase of the modernization of our payments and settlement system started with the implementation of MACSS – the Mauritius Automated Clearing and Settlement System. It links electronically all banks operating in Mauritius as well as the Ministry of Finance to the Bank of Mauritius. MACSS was designed to use the SWIFT infrastructure as message carrier, instead of a private proprietary network, and was a *première* in the region at the time of its launch. MACSS processes over 2,000 transactions per day to a value of nearly Rs10 billion – or nearly 3% of our GDP. Then PLACH – the Port-Louis Clearing House – was automated, with the standardization of cheques using Magnetic Ink Character Recognition (MICR) technology and, in turn, PLACH piggy-backed on the MACSS communication network. Well before the global financial crisis had begun to unfold, I had zeroed in on the Payment Systems as a key contributor to financial stability and economic growth. I therefore decided – against quite some opposition – to create a division within the Bank, dedicated to payment system issues, as is the practice in most central banks.

The establishment of the MCIB – Mauritius Credit Information Bureau – under the aegis of the Bank of Mauritius, was a key element of our FMI. MCIB is a public registry of borrower information and provides factual information on the creditworthiness of borrowers. It improved the provision of credit information. It was also instrumental in lowering the ratio of non-performing loans in banks. In other words, it improved the quality of banks' loan portfolio. While we have been busy warding off pressing unsolicited offers to acquire it from us, we have also been constantly expanding the coverage of MCIB. In 2009, we replaced the MACSS software with a new application based on international best practice. It is built on a more resilient architecture and supports multi-currency transactions including payment of tax bills in foreign currency. Our RTGS is certified "SWIFT Gold Label" and we are the only country in the region to have a multi-currency RTGS.

There was still a missing component in our payments landscape – we did not have a proper automated clearing system for low-value payments. These make up the bulk of the payment transactions in our economy. Last December, for example, we cleared a record number of cheques: 562,000 of them in an amount of Rs29.4 billion – or a daily average of 26,800 for a daily average amount of Rs1.4 billion. We have invested in a Bulk Clearing System as the first phase in the implementation of a Cheque Truncation System. At the time that the Cheque Truncation project was envisaged in Mauritius, we wanted to be the pioneers in the region with this system which would do away with the need for physical processing of the large number of cheques which I just mentioned. Unfortunately we got entangled in board-room squabbles and procurement delays. We have been overtaken by other central banks which probably had more lee-way with respect to decisions to invest in new technology. We are making up for lost time and expect to roll out our cheque imaging system by the end of June.

Regional Payments and Settlement System (REPSS)

Let me round off this brief overview of our FMI, the part that is under the Bank's purview, with an FMI initiative for the region where the Bank is acting as the Payment and Settlement Agent, REPSS – the Regional Payments and Settlement System of COMESA. I am reminded that the last time that a SWIFT Africa Regional Conference was held in Mauritius in 2004, Arthur Cousins, Director Strategic Financial Markets Projects, Standard Bank of South Africa and Member of the SWIFT Board**,** had shared with delegates his vision of 'TARGET Africa' where he saw, as he put it:

> ***almost the entire continent running interoperable SWIFTNet-based RTGS systems by the end of 2008.***

Today, we are not quite there, but the doors of African regionalisation are slowly opening up with this FMI initiative for the COMESA region. Today, the project has made notable progress. REPSS is fully in key with the 'Target Africa Vision' and connects the 19 COMESA member-states, through the SWIFT network for cross-border payments. Low-cost linkages between the national payment systems of countries through SWIFT will no doubt reduce the cost of doing business within Africa, but requires, beyond technological capability, a real political will. And instead of duplicating similar systems in the other sub-regions, wouldn't it be far more efficient to extend the reach of REPSS beyond COMESA countries, to take on the entire continent?

Concluding remarks

We are looking at a different new world where no country is an island and none can envisage their own economic prosperity in isolation. We need to unite forces to reap the benefits of an integrated market, reduce costs and achieve greater efficiency. Regional financial integration can help to develop domestic financial markets in Africa. Recently, a fellow Central Banker, Mr Budi Mulya, Deputy Governor of the Bank of Indonesia, remarked that harmonized, standardized and interoperable market infrastructures are fundamental requirements to facilitate increased volumes of cross-border transactions within the ASEAN region. I believe his observation is very pertinent and could apply equally well to the African region. But I have one lingering concern – I am worried by the sheer multiplicity of regional initiatives in our region. The experience on the continent shows that while regional organisations may be easily formed, they can be quite difficult to take forward. Governments face difficult policy choices emanating from national, regional and international programs. Multi-regional agendas arising from multiple memberships in different regional groups can become an obstacle to broader regional integration. Is it not high time to bring all the various building blocs, like COMESA, SADC, WAEMU and others, together as part of one integrated programme to deliver on the vision of a United Africa that we have been pursuing for so long?

As for financial integration, I am an inveterate optimist. I firmly believe that we can build an integrated financial market in our part of the world. It makes economic sense – we have the know-how; we have the technology; and above all, we have the people. REPSS is a first step in the direction of financial market integration. We need to continue to concentrate our efforts and resources instead of duplicating them. The time has come for us to re-define our vision of “Target Africa”. Sometimes **Vision** has to be re-defined before it can be transformed into **Action**.