Mr Rundheersing Bheenick, Governor of the Bank of Mauritius, speaks to Mr Madhukar Ramlallah of 'Mauritius Times' newspaper, 6 July 2012

"A crisis is too good to waste"

* "Let's take the opportunity of this crisis to revisit many things that we do and the ways that we do them"

* "The monetary policy fix cannot bring a lasting solution to any problem; it cannot even add to growth in a sustainable manner"

As usual, a lot of controversy is sparked off in the media when the Central Bank does not do the bidding of interested lobbies. Rundheersing Bheenick, Governor of the Bank of Mauritius, has not yielded to this kind of short term pressure, having a duty of care towards what he has called the reverse side of policy decisions, notably the hugely negative impact of one-sided policy decisions on the rest of the population. He points out in this interview that there are other policy instruments than monetary policy measures to deal with economic restructuring to give the economy a chance to re-position itself when seeking to come out better equipped to face the current international economic crisis. Setting the macroeconomic stage for improved future economic performance is not exactly the Central Bank's kettle of fish…

Excerpts:

Mauritius Times: In the wake of Moody's upgrade of the Mauritian economy, the credibility of the rating agencies has been questioned. Opinions seem to differ depending on which side of the political fence critics stand – whether they happen to be politicians or economists. For example, we find that those who today have misgivings about Moody's kept quiet when it brought down Mauritius' rating. Tell us, Mr Bheenick: are these agencies worth their salt?

Rundheersing Bheenick: I think we should bear in mind that rating agencies play a very useful role in major markets where investors and other stockholders cannot personally evaluate each and every stock that they are being offered. Agency ratings are therefore very much a shorthand guide to the state of play within particular companies that are publicly listed. In that sense, they have a role to perform to keep the market working efficiently. But what has happened is that while rating agencies built up their own role at the core of the financial intermediation process, somehow or other they managed to escape close regulations themselves. Second, their incentives within the industry were completely wrong. The people who were paying for the rating and who had an inducement to get a very good rating were those who could call the shots and almost dictated the kinds of ratings they were getting. This created perverse incentives: many people were getting ratings that were completely out of sync with the reality.

However since the crisis hit, whereby major scandals -- having nothing to do with us in Mauritius -- connected with major money markets came to the surface, it has now become fashionable to attack rating agencies. The latter are getting their act together. They are becoming much more transparent: before it was a very opaque system; now they publish their methodology, which allows us to know how they go about rating companies and countries.

What concerns us here in Mauritius is not so much the mistakes of rating agencies as a class vis-à-vis capital markets and the financial crisis. They did not see it coming anymore than anybody else saw it coming, so let's not blame them for something that everybody else failed to do. I believe that it is not very helpful to attack rating agencies without telling us what is likely to be put in place as part of the overall financial architecture to play the role that rating agencies currently play vis-à-vis market players. There is nobody else in the offing, so all that is required is a better regulation for the rating agencies.

Admittedly, people are now more aware of what rating agencies are actually doing and not doing. Rating agencies are only giving their opinion of things, and you are not supposed to go and invest based on an opinion. You are still required to go and do your own market research. You cannot subcontract this part of your business, assuming you are a major player in the market, to a rating agency, for this is but one instrument to help you take an investment decision. Individual people have become much more prudent about that now. Likewise for countries: when small countries are being downgraded, the rating agencies are not attacked, but when major players in Europe were downgraded, the agencies started being attacked; major Prime Ministers and Presidents including Mr Obama attacked the rating agencies when the USA lost its Triple A rating, saying: "The whole world knows the USA is Triple A." But for us, small players, the ratings are critical. It so happens that Mauritius as a sovereign does not go on the debt market to borrow money, so it does not affect us directly. But market players in Mauritius, our two major banks -- the SBM and the MCB – actually borrow on the money markets due to insufficient foreign currency in the country. The rating ascribed to the country does affect them because they cannot have a higher rating than the sovereign. And as the sovereign's rating has been upgraded, theirs as well have been upgraded in the latest review. We are very happy that the SBM has for the first time ever got a C-rating, which would not have happened if the sovereign rating of Mauritius had not been going up.

All of us should be happy that we got this kind of rating. Whether we like it or not, rating agencies do matter; it is not the first time we are saying we value the ratings. We have the right to question their methodology now and then, but the fact that we are placed in a particular category as a risk speaks eloquently about the credit worthiness of the country. I think this is a thing, which markets worldwide react to. Overall I think attacking Moody's for upgrading Mauritius is ill inspired and, at the limit, this might even be antipatriotic. In my view, it is something we should applaud because at a time when countries and major banks in the US and Europe are being downgraded massively almost every week, every month there is one tiny country which is being upgraded. I think this is cause for celebration.

*** But the same logic should apply when Moody's goes for the downgrading of Mauritius, isn't it?**

I am not saying that we should be jubilating. Remember that we were put on positive watch three months ago, and since then whatever we have done here has confirmed that we are the kind of country that's going up. The outlook that we have now is stable. Now Moody's like everybody else knows that the global economy has taken a turn for the worse, and Mauritius depends a lot on the state of the global economy. There will be repercussions for Mauritius, and it's up to us to make sure that whatever happens internationally we still happen to move ahead and preserve our rating.

*** It may be politically correct to applaud or criticise Moody's ratings. But you would expect their analysis to take a comprehensive view of the economy and to delve deep into all the opportunities and risks to the economy before they come out with their opinions, won't you? Are you satisfied that that's indeed the case?**

For a start, I think it is wrong to politicize the debate about ratings. Otherwise when Moody's downgraded the rating of the US in an election year, we could jump to the conclusion that Moody's is Republican…because they are anti-Obama! This is not the case. Politics has got nothing to do with it, it's the state of finances that matter. Same way here, I think they should rise above party politics and look at the fundamentals of the Mauritian economy. These fundamentals have been examined not just by Moody's; they have been examined thoroughly by the IMF in the context of Article IV Consultations. Moody's is therefore not the exception, the IMF has also found positive things about the Mauritian economy, which can serve as a model for other economies looking up to build their resilience.

Let's depoliticize the debate, and let's focus on the economics of it. Let's try to work together to ensure that this kind of positive outlook results in a still further upgrade of the country's rating in the days ahead. Now if the world economy fares badly, as it has been the case up to now, things are going to be tough for all the players, including Mauritius which depends on the health of the international market. Let's not therefore rock the boat for politically inspired reasons by disputing a rating which we did not pay for or commission. It's a rating that came of Moody's own accord as part of its regular updating.

*** I understand that you also had misgivings earlier, in 2009, about Moody's when it went for the downgrade. You took issue with its credibility, and said then that they are playing Russian roulette. You can't be applauding their rating today, can you, especially since a few weeks back you had expressed anxiety about the economic situation?**

Obviously, ratings are things that can go up as well as go down. I took issue with Moody's in 2009 because they were proceeding to downgrade our major bank at that time when the first waves of the economic crisis were beginning to hit the world economy – and its banks. If Moody's went ahead and changed the rating of our largest bank in the country and that of the SBM for their overall financial strength, it would have meant that in an environment where bank finance were getting scarcer, the cost of borrowing for the Mauritian banks to raise funds would have been still higher.

There was nothing, in my opinion, in the state of the Mauritian economy or in the conditions of the two banks that warranted this kind of downgrading. I took issue with Moody's because at the Central Bank we do keep our finger on the pulse of the banks. Our monitoring of the local banks is so close as to enable us to ascertain precisely their strength or otherwise. There was no case for them to be downgraded at that point in time. I suspect we know more about Mauritian banks than Moody's will ever know, and that's why I then put the question: What does Moody's know that we do not know? I also put another question: Who rates the raters? Nobody rates the rating agencies, and it's only in the wake of the crisis which hit the US banks that this question has come up. I also took corrective action: since the rating downgrade of Moody's, which was likely to inflate the cost of borrowing of our banks, I offered a foreign currency line of credit to our banks for trade financing so that they need not go and borrow on foreign markets at higher cost than warranted.

*** You had expressed, a few weeks back, your concern about the health of the local economy. Statistics Mauritius has now come up with its latest National Accounts Estimates 2012. What's your reading of the economic situation today? Do the latest data add to your anxiety?**

We should look at things in their proper context. Let's not focus on the economic data flow in Mauritius without looking at what's happening to the data flow relating to major economies worldwide. The data flow elsewhere paints a very bad situation, which is darkening and is becoming even gloomier. Whether it has to do with unemployment, growth performance or the prospects of different sectors surviving, our economy is much stronger than the different economies to which we are presently exporting. The data flow here is very positive, the kind of which would have got stock markets going up in other countries…

*** Stronger, but more vulnerable, isn't it?**

The vulnerability of the Mauritian economy is not something that has arisen in the last five years. We have always been a vulnerable economy, but what I am saying is that the data flow pertaining to Mauritius, which some commentators say paint a very bad picture of our economy, is of the kind that would have got markets perking up elsewhere in the world. The reason being that in spite of the crisis we still have a very positive rate of growth: close to 4.0%, which is not bad; unemployment is around 8%, our public debt is below the 60% benchmark…

*** Many African nations are doing better than us in relation to those fundamentals, aren't they?**

Obviously. We should always be very circumspect when we make international comparisons. Some African countries are in fact doing as well as China as far as their growth rates are concerned. Now we do not have the resources of Africa, and we are not starting from a position where we have to grow fast to allow people to catch up; we have done that part already. We grew fast a long time back, and we have reached the stage of a rapidly maturing economy. Our growth drivers are not of the kind that can deliver that kind of growth anymore, so we have to adapt ourselves to a period of prolonged reduced growth compared to our premium rates unless we manage to find new drivers that can power the economy post crisis into a higher phase.

My concern that I have been sounding off relates to how to do this with precisely what kind of fundamental and structural reforms which will put Mauritius in a position to benefit from the crisis. I believe a crisis is too good to waste; let's not waste the opportunity, let's take the opportunity of this crisis to revisit many things that we do and the ways that we do them and see how we can extract more competitiveness out of them. I believe it can be done so long as we have the right policy environment and the right measures in place. We can emerge after this crisis fighting fit and able to roar ahead again in spite of being handicapped by lack of natural resources by capitalizing on the recovery in the global market whenever it's going to come. There is bound to be a recovery, because no depression has lasted for ever.

*** What if the Euro crisis stumbles from one crisis to another?**

Well, the outlook as of now is that the Euro zone will actually go from crisis to crisis. It has been doing that beautifully for quite some time now.

*** The worse, as they like to put it, is not behind us; it's yet to come?**

I don't think things are going to get particularly bad. What's going to happen, I think, is that the Euro zone must find its way to fix its problems at the political level first. If there is no political will to envisage transfers from the richer countries to the poorer ones, nothing is going to happen except for temporising solutions that are not going to work out the needed comprehensive plan. We will go from temporary fix to temporary fix, and the problems will keep shifting – which is what has been happening for some time. The way forward is well known: political and fiscal union, consolidated supervision of banks, consolidated bailout of banks at the Europe-wide level. All that means there must be somebody willing to bring out the pay check and actually pay for bankrolling all of this. Until that political commitment is there, we will go from one apparent solution to another apparent solution to a new crisis, which again will fetch another apparent solution. That will amount to 'kicking the can down the road,' as the Americans beautifully sum it up. That's exactly what the Europeans have been doing up to now.

*** And as the Europeans keep on kicking their can down the road, we in Mauritius will equally go from temporary fix to temporary fix. Right?**

No. I believe we should not depend that critically on the Euro zone, or that we should mirror every single passing problem over there in our own backyard. There was a respectable school of thought here – at very high level -- that canvassed the idea that we should put an end to our managed float and peg the rupee to the euro. I am not sure anybody in Mauritius would have appreciated the consequences of such a move. The Bank of Mauritius resisted this move, because we do not believe that what is good for the Euro zone is good for us. No need to tie our destiny to any single bloc. We think a free float regime is what serves our interests best. The IMF experts are the people who know this business, and they have given us very good marks for our regime. The Europeans can have their succession of crises in the Euro zone, but as for us we should shield our economy to the extent possible. That's the reason why we came up with the measures rolled out recently with a view to helping our economic players convert some of their exposures in the currency in which they earn their foreign earnings. This will help them remove exchange risks from their balance sheets; it will in the same breath reduce their vulnerability, which could have knock-on effects on the rest of the economy.

We have to remember that in the past it was all a one-way bet, with the rupee going only in one direction so people were very happy to borrow in rupees and earn foreign exchange because they could be helped by inflation to pay their debt. That one-way deal has gone bad now for that kind of speculators. Now the rupee has shown that it can be strong. We are trying to bail out that category of speculators, but it's going to be a once-and-for-all package. Going forward, they will have to take their own risks by hedging their exposures themselves.

*** If temporary fixes won't do for the Mauritian economy, we would then need to address the structural problems, which will not be without imposing handicaps on its immediate performance. In your post-Monetary Policy Committee press conference of 12th June, you stated that "monetary policy alone cannot make the underlying structural imbalances disappear as it is made out to appear. There was work to be done in other quarters..." What is it that needs to be done and who should be doing that?**

There is a whole lot to be done. Basically, we should be aware of the limitations of monetary policy. In the run-up to the MPC meetings, you get people here creating the impression that all that the Central Bank has to do is to lower the interest rate and everything is going to be the best in the best of all possible worlds. The monetary policy fix cannot bring a lasting solution to any problem; it cannot even add to growth in a sustainable manner. For sustainable growth you must go back to fiscal policies, to policies directed to the real sector of production, productivity, competitiveness, economic scope, etc., – not the monetary side.

*** So there is work to be done by the Minister of Finance in response to the calls for fixes from the economic operators?**

The Minister of Finance and other Ministers in the Cabinet – they've got the work cut out for them. Monetary policy can only give a temporary fix. What we are trying to do now, for example, is to combat the currency appreciation. This alone cannot give a lasting solution, because the economic history of all the countries that have tried to devalue their way out and nothing else will inform you that this has not worked. You have to have complementary policies to move up the real sectors of the economy. You must build up real competitiveness, you must increase productivity, and you must change the mindset. You must go and look for new markets and find new ways of working just as well as your competitors are doing. That is what's required, it's a "grand chantier", which is not in the line of business of the Bank of Mauritius.

What we are saying is that if you think that the monetary fix and the exchange rate fix that we offered a few weeks ago are your solution, then go and think again!

*** A "grand chantier", as you say, that requires one Minister cut for this job. Right?**

I do not wish to make comments on the political establishment -- directly or indirectly.

But to come back to the structural problems affecting our economy, the real issue is competitiveness in an economy where there is no longer any preferential access to key export markets. My feeling is that we still have this rent-seeking mentality which is still having its very pernicious effects right across the economic spectrum in Mauritius – from the top economic players right down to the workers and the job-seekers. You still have the same mindset that the world out there is theirs, waiting to be plucked; it's like somebody owes us a living and we have to get our share of it. There is no such thing: you have to fight for your market share every day, and you can only fight by being competitive. You can't fight because the Central Bank is going to give you a monetary boost – because that boost has a reverse side to the coin. The reverse side of the coin really means that you have to subsidize the big players by taxing the poor man at the bottom of the heap. It's a perverse transfer of wealth and income from the bottom to the top.

*** You have no doubt ensured that you have the support of the Prime Minister for this policy position, haven't you?**

Again, as I told you, I do not make political statements.

*** But I believe you had mentioned to a paper that you enjoy the trust of the Prime Minister. Is that right?**

Obviously, if I didn't have the trust of the Prime Minister I would not have been here in the first place. Especially given that the role of Central Bank Governors is too critical these days. If you do not have the confidence and trust of the Prime Minister, I think you should pack up and move on. And I do not believe that the enjoyment of the confidence of the Prime Minister means that you have to say everything that the Prime Minister would like to hear… The Prime Minister is also a politician. The Central Bank draws its independence from the law. That independence must be safeguarded, and the Prime Minister safeguards that independence by not instructing the Central Bank to do anything. He will never do that anyway.

*** How is it like when you sit down with the other members on the Monetary Policy Committee during its quarterly meetings? Do you feel like you are able to operate in all independence?**

The Monetary Policy Committee, as constituted, has the Governor with a casting vote, which he can have recourse to in case of a tie, to try to assert his point of view. Unfortunately, the way it is structured, that casting vote has never been used because when I was outnumbered, it was so overwhelming that there was no point to use the casting vote. The MPC has got four members, including myself, from the Central Bank, and you have got five members from outside appointed by the Minister of Finance. I have no problem with that so long as the members behave as the law expects them to behave – that is, once appointed, they must act in complete independence within the limits of their mandate and without taking instructions from anybody.

*** I would think it's not a question of numerical superiority of one side as against the other. What's the spirit like during those meetings?**

The spirit of it is that there should not be one side or the other; there should be one team of people who should focus their minds on any particular issue on the agenda and bring our resources to bear on it in order to find the best solution to it in the best interest of the country. Why is the MPC independent? It's precisely because if you leave it to the political cycle, you'll be guided by the political considerations of short term-minded politicians. We have to remember that monetary policy consequences take some time to kick in, and you do not want to change course in matters of monetary policy each time a problem crops up at Government House. Remember that the role of the Central Bank is to favour price stability – which basically means fighting inflation – in the context of balanced and orderly economic development, financial stability, payment system stability among our objectives…

*** Former BoM Governor Ramesh Basant Roi has levelled quite harsh criticisms of the Monetary Policy Committee's decisions taken over recent months. He has qualified them to be unpredictable, "erratic, inconsistent, incongruous…", and that the "rhythm and direction of changes are out of tune with the state of the economy." He adds that the BOM has focussed on controlling inflation at the expense of growth stimulation as favoured by the Ministry of Finance. How do you react to these criticisms?**

I wouldn't wish to get engaged in a polemic with my illustrious predecessor but what I can tell you is that the charge that monetary policy decisions have been unpredictable is as wrong as it could be. I am not the only one to say so; you just have to look at the PluriConseil's and other surveys published about what people have been expecting from monetary policy decisions and you will find that we have, by and large, been within the expectations of the majority on the market. So therefore they were quite predictable, the exception being the decision taken at the last but one Monetary Policy Committee meeting where obviously, as the published minutes show, I was outvoted. That was unpredictable. Otherwise our decisions had generally been within the thinking of the majority of people who take part in the surveys. So we have anchored monetary expectations in a better way that the Central Bank has ever done in the past. I reject the charge of unpredictability totally.

Same thing with regard to the "erratic, inconsistent, incongruous…" comments of Mr Basant Roi. I do not agree with these comments at all. I think that our good friend Basant Roi should ask himself why he did not set up the Monetary Policy Committee when the law was changed in 2004 until the time when he left the Bank. The Central Bank had to wait for me to assume office in February 2007 to start operations of the independent MPC in April 2007. I do not think he has the experience of working with an MPC of this kind; he was more used to working in an opaque system where the Governor and his staff would take their decisions. I do not have this latitude; I have introduced transparency and have it operationalised. And I have explained that I do not control the MPC -- for better or for worse.

I also do not think we are out of tune with the state of the economy. Quite the opposite: we have given resilience to the economy; we have built up the underlying strength of the economy, and our rupee which had been sliding consistently is now more stable. I mentioned earlier the one-way bet that people were taking -- that mindset is changing now. Our Rupee was actually in a free-float for nearly 18 months without any intervention, which is something that many currencies in the third world cannot do. We did all that. So there was something quite predictable about the economy and something reflecting a high level of confidence that the fear of floating that Central Banks of developing countries had in the past days was overcome thanks to the kind of approach that we had. We also focussed on inflation because, when I took over, we were heading towards double-digit inflation. We had to something about it, otherwise we are going to tax the poor to subsidise the rich which is completely wrong. If we had continued in that line, we would have got our own equivalent of the Arab's Spring here. This is in the domain of the hypothetical, but if we just extrapolate what was happening then without any changes there, Arab's Spring would have reached our shores. Maybe even before it happened in Tunisia.

*** To come back to the structural problems we were talking about earlier, do you think that we are perusing the right policies and addressing the right issues? When you look at the inflows of capital into Mauritius, we still seem to be privileging the real estate and the accommodation centres; permits for IRS and ERS are continuing to be delivered and these are being financed by debts and the commercial banks. Don't you think that there is any risk of implosion of the real estate bubble and/or of a drastic reduction in capital inflows?**

Obviously we have been alert to the risks in the property sector nearly five years ago when we started asking banks to be cautious in financing IRS projects. I was the first one to blow the whistle, way back in 2008, when everybody had a project on IRS. If all these projects had taken off and been financed by our banks, our banks will be left today with the overestimated collateral for which there would have been no buyers. In fact we saved our banks from going in that direction -- at tremendous cost to us --, because every bank wanted to go ahead at that time. We blew the whistle right there. Now having prevented the excesses in that sector, we have no reason to believe that currently our banks are overexposed to the sector and that they had bad debts accumulated there. I think they have been cautious and we have been monitoring the situation very closely. You must be aware there were armful of projects before, and none of them had taken off not because there was a lack of credit. The credit was available, but the risk of concentrating all that credit in one sector was too much for us to be comfortable with, so we had put some sharp limits of what banks could do in that sector.

*** But there have been allegations about a lot of hot money going into the system. Is this destabilising the rupee?**

I do not agree, I think it has become a sort of new conventional thing that we are attracting hot money. My definition of hot money basically is short-term money, which is speculative money. We do not attract speculative money, because to attract speculative money, you must offer some conditions, either some higher rates of interest or people can park their funds with no questions asked while waiting to go elsewhere. Our rates of interest, our differential is not that high vis-à-vis other centres. Second we have very tough KYC in the banking sector (Know Your Customer) so really purely speculative money which is not totally clean cannot come to our shores because we have a very tight discipline. And hot money also refers to short-term flows managed by professional speculators who move from market to market destabilising the market as they go. I said earlier that one of our roles is to have financial stability so we will never encourage speculative flows in the country because they will go against the financial stability objective of our country. Now the closest I can find hot money flowing in the country is short-term investment in official paper. We have portfolio flows in the stock exchange, we have foreign direct investment inflows, you mentioned property, that is not hot money because it comes for a long time. We have some short-term money in the government market paper and that market is very small. For those who tell us about hot money, the good thing to look at is that it has actually gone down. The flow was much higher. In December 2007, outstanding investment in GMTB's (Government of Mauritius Treasury Bills) by foreigners amounted to Rs 2.8 billion, which we could conceivably deem to be short term flows and then by extension possibly what is considered hot money. That has been reduced to Rs 557 million in May 2012. In 2007, Rs 2.8 billion and in May 2012 Rs 557 million, so where is this hot money coming. Regarding the stock exchange, I think that most people do not believe that stock exchanges attract hot money capital and even there foreigners had been investing and disinvesting depending on what is happening on their own appetite for risks in markets. So by and large, foreigners' holdings of listed stocks have been around 10%. It's moved from 9% to 10%. It moves up and down but there is no massive inflow there so we reject this charge that there is hot money flow. I understand that many people might think that in the balance of payments figures you have an item of net errors and omissions that could be conceived to be hot money. But if it is hot money, it should be parked in a bank to earn income. The residual there is likely to be offshore vehicles money that comes here and out, which is not properly captured.

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"We have always been a vulnerable economy, but what I am saying is that the data flow pertaining to Mauritius, which some commentators say paint a very bad picture of our economy, is of the kind that would have got markets perking up elsewhere in the world. The reason being that in spite of the crisis we still have a very positive rate of growth: close to 4.0%, which is not bad; unemployment is around 8%, our public debt is below the 60% benchmark…"

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economic development, financial stability, payment system stability among our objectives…"

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