SEMINAR ON FINANCIAL SECTOR ASSESSMENT PROGRAMME

Presentation on the implementation of FSAP team's recommendations in respect of the banking sector by Mr B.R. Gujadhur, Managing Director of the Bank of Mauritius

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Hon. Minister of Economic Development, Financial Services and Corporate Affairs

Members of the Board of the Bank of Mauritius and the Financial Services Commission

Deputy Leader of FSAP Mission

Ms Rennie

Mr Hafez Ghanem, Country Director for the Indian Ocean of the World Bank

Chief Executive, FSC

Director FIU

Distinguished Guests

Ladies and Gentlemen

Good Morning

The FSAP process for Mauritius began in mid-2002. Agreement was reached between the Mauritian Authorities and the IMF/World Bank on the timing of the FSAP mission. Visits of the FSAP team were scheduled for the second half of 2002. Today represents the culmination of this process and I am happy to be here now as I was at the start of it all.

I should admit that there was an apprehension within the financial sector of Mauritius in the beginning that the FSAP mission would be engaged in faultfinding and that we would, after all, not get away with the impressionistic and unfounded misclassification of Mauritius by the Financial Stability Forum earlier. These fears were quickly dispelled. In the course of the introductory meeting of the FSAP team with the Chiefs of the financial sector of the country at the Bank of Mauritius, it was made abundantly clear that the purpose of the FSAP mission was to identify the soundness of the financial system of Mauritius and that, for this purpose, it was absolutely necessary that its vulnerabilities be identified. It was also established that for Mauritius' financial sector to make progress in time to come, it had to be aligned to international best practices as embedded in international financial sector standards and codes. More importantly, it was emphasized that a significant fallout from the assessment would comprise recommendations of the Mission towards improving the financial infrastructure, notably in terms of the rules, regulations, laws, institutions and markets in operation in the country.

This daunting task was undertaken by the FSAP team from October 2002 to December 2002 spilling over partly into 2003. Constant support from the industry, the Ministry of Economic Development, Financial Services and Corporate Affairs and the regulators from the Bank of Mauritius and the Financial Services Commission was available all the time. I am very impressed by the quality of output generated by the FSAP Mission and take the opportunity here to thank the FSAP team, the Head of Mission and the Deputy Head in particular, for the patience with which both sides, the Mission Members and the Mauritian Authorities, listened to the views of each other before concluding on issues. Even more, I believe that the Mission proved to be a trigger for action on several fronts, notably in the enactment of a spate of relevant legislations, for which the Hon. Minister should be congratulated, to give effect to the recommendations but also to give a boost to the regulatory and supervisory framework. We can now look forward to reinforcing the structures of the finance sector of Mauritius based on those recommendations and, hence, implement timely decisions for maintaining our competitiveness while operating on a sound and internationally accepted framework. It may be said that the Mission's work has breathed a new spurt of life in the financial sector of Mauritius. I will come to that. Let us see first how the recommendations of the Mission have been implemented.

<u>Implementation of Recommendations</u>

A number of changes have been implemented in the banking sector as a result of the FSAP. These changes should not be seen as a mere compliance factor. They involve a re-positioning of the sector with a view to drive more and better business. Let me enumerate some of the changes.

There were on-going projects already in the banking sector before the coming of the FSAP Mission. These include the draft Bank of Mauritius and Banking Bills to which a final form has now been given, thereby facilitating the enactment of these laws in the near future. The enactments will also, for the first time, provide to the Bank of Mauritius with enforcement powers for breaches of regulatory requirements by way of sanctions, in addition to existing provisions for actions on the licence in the existing legislation. The enactments will, amongst others, modernize the regulatory framework for banking and near-banking business conducted in Mauritius, establish formally the independence of the Central Bank and provide for better accountabilities as regards fit and proper criteria in the case of persons in charge of banks. They will contain a provision for the setting up of a deposit insurance scheme for banks. Another project which was in the offing was the establishment of a Credit Information Bureau, the object of which is to furnish an informed basis for decision taking to prospective lenders, derived from shared information relating to lending and other facilities already extended to enterprises and groups of borrowers intending to borrow additional funds from the market. Progress has been made in the implementation of this project which is chalked out to emerge early next year.

These changes were obviously endorsed by the FSAP Mission. From the recommendations of the Mission, the issue of Bank of Mauritius Bills for purposes of monetary policy as distinct from the issue of Treasury Bills for Public Sector Borrowing Requirements has already been implemented. This will demarcate clearly financing for budgetary purposes from debt raised for monetary management purposes. The Bank of Mauritius and the Government have started action since last year to extend the average maturity of Government debt which is too heavily tilted towards the short-term. Action to foster the development of active secondary market trading of Government securities has been implemented, notably through the primary dealing system. In this regard, medium and long-term public debt of Rs5 billion will be publicly issued in 2003-04 and it is expected that holders of Treasury Bills will have recourse to funding exercises in this context. This initiative will automatically serve to extend the maturity profile of Government debt in the desired direction.

Hopefully, current actions contemplated on the rehabilitation of enterprises by raising of their equity levels, should go along to set in motion a more lively corporate debt market as well as dynamic secondary trading of corporate debt issued by the more highly rated companies. There is an implication here that companies that go for some formal rating will benefit from the emerging market outlook. This development is expected to make a deep dent in the manner of raising funds on the financial market as also on the alternative avenues that will become available to savers in a more balanced financial risk-taking culture in the economy. It has to be expected that the profile of financial intermediation as it is undertaken now is bound to change for the better in this context.

Bank of Mauritius Guidance Notes on Anti Money Laundering/Combating the Financing of Terrorism (AML/CFT) have been revised up to the highest international standards and are in the process of being anchored in the Financial Intelligence and Anti-Money Laundering Act, as recommended by the Mission, after consultation with the industry. Without having the effect of impairing the need to protect the essential privacy of customer information, amendments have been introduced in the law to enlarge the scope of bona fide information-sharing. This step is expected to make for more efficient exchange of information between the domestic regulators and the FIU as well as participating on a level playing field in the international exchange of information with other jurisdictions. In line with the Mission's recommendations, requests have been made to other jurisdictions' regulatory authorities to enter into Memoranda of Understanding with us on the sharing of regulatory information, specially those countries in which Mauritian banks have their establishments or those parent regulatory authorities whose banks operate in Mauritius.

Rules, regulations and laws will be of limited effect in the absence of capable supervisory oversight. The Bank of Mauritius embarked some time back on the implementation of a rigorous world class supervisory system. This has involved the recruitment of additional professional staff, training of the staff, development of an in-house manual of inspection and the pursuit of an intensive on-site examination program of financial institutions to assess directly the risk management systems and controls of the financial institutions. Additional guidelines have been issued to the industry, the latest of which dealt at length on provisioning requirements of banks in the context of the adoption of IAS 39. The FSAP Mission has emphasized this aspect of the Bank's work. Further internal guidelines in respect of the supervision of financial institutions operating in conglomerate structures, the rating of banks based on the CAMEL evaluations, intervention in banks and other financial institutions in the context of early warning systems as well as the undertaking of Consolidated Supervision have been introduced. Moreover, as recommended by the FSAP mission, the Bank has improved its off-site monitoring of financial institutions with technical assistance from the IMF. The ensuing offsite framework has laid down the basis for quarterly off-site surveillance reports on each financial institution to which will be closely associated the process of rating of individual banks. The Bank of

Mauritius will soon be in a position to convey accordingly changes in individual banks' ratings in accordance with the new developed method of assessment. This process should go a long way towards risk mitigation usually associated with problem banks. Dispositions have been taken for staff to receive specialized AML/CFT training and apply a focused attention on this matter during on-site examinations.

The issue of achieving a closer integration of the so-called onshore and offshore activities has started being addressed. It is expected that this matter, which calls for policy reorientation, will be addressed with a view to increasing the scope and viability of the financial sector as a whole in an increasingly competitive global environment in which the services sector finds itself today. I will not be contradicted on this matter specially by those who have been following current WTO leveraged discussions on the provision of services.

The Mission has recognized that Mauritius is already endowed with a modern payment system infrastructure, including the Mauritius Automated Clearing and Settlement System (MACSS). The only shortcoming of this system, in the context of the application of the Core Principles for Systemically Important Payment Systems(CPSS), concerning the irrevocability of payment settlements, will be shortly addressed in the legislation relating to Insolvency. Accordingly, care will be taken to deal with what is referred to as the application of the "Zero Hour Rule" which, by reversing settlements having already taken place, has the potential to disrupt the orderly working of the payment system in the event of the bankruptcy of one or more participants in the payment system of a country.

Conclusion

In conclusion, I have to state that fine tuning of the framework of supervision and regulation of financial institutions is and has been an on-going activity in Mauritius. What it is critically important to bear in mind however is to employ those changes in approach taking place to give our financial sector a new lease of life each time, based on new and anticipated models of global financing patterns in the context of overall financial system stability. Beyond this visible stability, however, there should be forces at work at the level of the professionals operating in the sector, towards developing products and services distinct and improved as compared to customary ones. The added value and productivity factor in this context is indispensable for progress. Professionals are called upon to sell their skills and imagination in developing new products more than the sheer products themselves. This is the level at which Mauritius' financial sector can meet global competition successfully and re-position itself dynamically in the global financial economy.

The FSAP Mission has brought home more than ever before these developmental aspects to which our attention should go in the future if Mauritius is to become a significant provider of financial services to an increasingly integrating global financial services sector. More than ever before, there is need for professionals of the sector to be imaginative, technology driven and adapted to the ever-changing environment which is expected to spin off new risks and, hence, new rewards up the value chain. The FSAP should be seen as a reminder to those challenges that lie ahead rather than fixing our mind on some shortcomings which, in any event, we can easily fix. We have to thank the FSAP team leaders and their members for throwing valuable insights into how we should go about charting the future course of our financial sector.

Thank you.