Rundheersing Bheenick: Unlocking our potential in these uncertain times...

Letter by Mr Rundheersing Bheenick, Governor of the Bank of Mauritius, to stakeholders, Bank of Mauritius, Port Louis, 28 February 2014.

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The original speech, which contains various links to the documents mentioned, can be found on the Bank of Mauritius' website

1. The year 2013 saw the Bank scoring many "firsts," reaching new "highs," and establishing new records. We sharpened our focus on financial stability and macroprudential policy. It was also the year that marked the start of my third mandate as Governor, this time without any hullabaloo. I view this mandate as a vote of confidence in my stewardship of the Bank and would wish to take this opportunity to lay out the platform for taking the Central Bank and, by implication, the economy to still greater heights. Successfully tackling the challenges ahead does not rest on my shoulders alone, but depends crucially on the support of public policy-makers, Bank staff, and private stakeholders.

2. My personal experience at the helm of the Bank has been filled with ups and downs and I expect the third mandate to be no different on this score. Anybody hankering for a quiet nine-to-five life, five days a week, would be well-advised to stay well-clear of the shoes of a Central Bank Governor. Faced with the continual global economic uncertainty, I had to focus my efforts on maintaining domestic macroeconomic stability. Our achievements speak for themselves. Our failures generated substantial public scrutiny and media coverage. However, out of every failure comes a lesson and we have learnt our lessons over time.

3. The ***Letter to Stakeholders*** now forms part of our regular calendar and its release is eagerly awaited. We see it as part of our communication strategy to inform, enlighten, and explain.[1] We share our successes and failures *sans états d'âme* or chest-beating. At the start of my new mandate, I would also like to extend the traditional ***Letter to Stakeholders*** by sharing my personal strategic vision for the Bank and the economy. I hope that this provides food for thought for our public policy-makers, private sector operators, and decision-makers to better extend our footprints in the region and to better position the country globally.

4. The letter is structured as follows: Part I provides the context of domestic and global developments and gives a brief overview of trends in monetary policy. Part II focuses on some areas of concern, listed in the text below, and readers seeing this on the website can navigate to the issues of interest to them. Part III highlights the main developments of the past year. Keeping in line with past practice, issues are discussed in greater detail in the links at the end of the relevant paragraphs. As a departure from my previous Letters, details on operational developments are provided in the Annex and a Box is devoted to the Ponzi outbreak that threatened to rock the financial sector in the early part of the year. Part IV presents some other highlights of the year, not captured elsewhere, such as regional cooperation and the close association of the Bank in the work of the Financial Stability Board. Part V concludes.

[1] This letter was finalised on Sunday, 26 January. Its publication was, however, delayed on account of the rescheduling of the December 2013 meeting of the Monetary Policy Committee (MPC) to 3 February 2014, and the need for members to observe the silence period of two weeks before and after MPC Meetings in accordance with the MPC Code of Conduct.

I. Context

5. ***Domestic developments.*** National accounts data over the last few years provide abundant evidence that our economy has gradually lost steam. Targeting the high GDP growth rates achieved in the 1970's is mere wishful thinking today – unless complex structural adjustments are first made to very many areas of our economic life. Back in the 1970's, our country had a reservoir of labour, together with access to preferential export markets, and high saving and investment rates culminating in high growth rates. Long gone are those days of sustained GDP growth rates above 5 per cent. Excluding the sugar boom of the early 1970's, our natural rate of growth hovers around 4 per cent, which is a more realistic benchmark in the absence of deep structural reforms. Our sources of growth are qualitatively different from the growth drivers of most African countries; our human capital still remains key to our progress. We have to live up to the fact that drastic changes are needed and that we need to go beyond business-as-usual, undertake structural reforms, re-skill our labour, raise more capital, step up our saving effort, enhance productivity and competitiveness and accelerate diversification efforts.

6. A critical subject that I would like to highlight is the persistent rise of domestic credit as a share of GDP in our economy. Over the last ten years, we have constantly surpassed the credit growth rate of Sub-Saharan African countries and of small states generally. Credit to households and the private sector topped Rs300 billion for the first time in December 2013, representing over 83 per cent of GDP. While we have not reached the notorious credit growth peaks of Spain and Ireland, we are almost replicating the credit growth pattern of Singapore, without, however, the decisive steps which Singapore initiated to curb excessive leverage and cool property demand. This sustained increase in credit has gone hand-in-hand with rising indebtedness, in the household as well as the corporate sector, and increasing concentration of credit risk. As regulator, we had to take prudential measures to protect the financial sector and the economy at large. We deemed it advisable to introduce a series of macroprudential measures on loan-to-value ratio, debt-to-income ratio, sectoral limits and additional provision for certain sectors to manage the budding risks.

7. One of my goals in my third mandate is to reinforce the resilience of the banking sector and to foster its sustained growth. Regulators have learnt many lessons from the global financial crisis, chief among which is the need to improve the monitoring, surveillance and governance of financial institutions to guard against current risk as well as to prepare them for potential future shocks. In 2013, we took determined steps to improve the regulatory and supervisory landscape facing financial institutions and give it a more forward-looking approach. We addressed a number of both micro- and macro-level issues. We issued several new guidelines, and brought improvements to existing ones, to adapt the regulatory framework to the evolving needs of the financial sector, and to bring it closer to international best practice. As detailed elsewhere, we also enhanced our approach to off-site surveillance and on-site inspection of individual institutions. There was considerable interest from new players in gaining entry to the local banking sector; we received seven applications for a banking licence in 2013. ***(More on this issue)***

8. I must concede that we still have to cover some ground to de-risk our financial system and add depth to the financial market. The *Deposit Insurance Scheme*, a special bank resolution regime, an Ombudsperson for the sector, a National Payment Switch (NPS), the introduction of *Sukuks* and cross-border resolution are some of the areas where we are trailing well behind. Not because we at the Bank have been sleeping at the wheel, but mainly because of lingering difficulties in securing the enabling legislation – except in one case, where despite the appropriate legislative amendments, a key player has not modified its behaviour to facilitate the objective which these amendments seek to further. I am mystified by such foot-dragging on initiatives designed to increase the safety of our banking and financial system. ***(More on this issue)***

9. ***Global backdrop.*** At the global level, there was increasing evidence in the second half of the year, of the recovery taking hold in some key economies, but little sign of a take-off as "escape velocity" continued to prove elusive. Lingering recession plagued the euro area for much of the year with, however, a significant improvement in the major Eurozone countries in Q4. Major emerging markets such as China and India slowed down. The deeper recession in the euro area has had a particular impact on global growth: the downward draft from weak balance sheets, depressed confidence, and low demand, worsened prospects for export-led recovery for trade partners such as Mauritius. Tight fiscal and financial conditions prevailed, with the spectre of a possible US debt-default arising from fiscal brinkmanship adding to the uncertainty. Mid-year speculation about possible "tapering" by the US Federal Reserve sparked increased volatility of capital flows which abated when "tapering" was actually launched – a clear sign of market nervousness in conditions of extreme uncertainty.

10. Regulators are still striving to reform the regulatory framework to minimise the likelihood of future financial crises and if they occur – as they surely will – to ensure that their systemic impact is contained. The sheer amount of public money pumped into ailing banks during the recent global financial crisis – either to bail them out, to avert collapse, or to provide liquidity support – has compelled policymakers to find ways and means to limit reliance on such recourse in future. Good progress has been made on rules on capital, leverage, and liquidity for banks. But there is still much ground to cover on the reform agenda. The implementation of new reforms has been uneven across countries worldwide and remains a challenge, especially as the pressure to reform has abated as the crisis has receded further in the past.

11. Financial institutions guilty of delinquency during and after the financial crisis are being pinned down by regulators. Banks have had to dig deep into their pockets to pay hefty fines for such offences as manipulation of the London interbank offered rate, Libor, rigging foreign exchange markets, and collusion among banks to undermine a government programme as in Hungary. Bank executives, directors, and traders have been fired or jailed. Regulators are becoming unyielding in bringing offenders to justice. Over time, it is expected that banks and other financial institutions will have to improve their internal controls to prevent irregularities and improper behaviour.

12. ***Trends in global and domestic monetary policy***. The recent years of global economic mayhem have put monetary policy to a severe test. Central bankers everywhere have been scratching their head, reflecting on the ideal approaches to monetary policy formulation in the post-Global-Financial-crisis era. Faced with tough monetary policy dilemmas, many large central banks, grappling with the zero lower bound, resorted to "forward guidance" as an additional tool in their arsenal, with a focus on signalling their monetary policy intentions through an enhanced communication strategy. The prolonged period of ultra-loose monetary policies around the world brought to the forefront issues such as asset price bubbles, volatile capital flows, dollarization, and imported instability. The twists and turns of monetary policy in major economies have rocked the boat for smaller central banks, pushing them in uncharted waters, and forcing them to intervene to combat currency appreciation that threatened to throw their economies out of kilter if left unchecked.

13. Such has indeed been the case for Mauritius, where the situation is further complicated by two idiosyncratic factors. First is the entrenched divergence of opinion among Monetary Policy Committee (MPC) members, which surfaced during the year, pitting Bank executives against "external" members. Unlike the situation in most developing economies, our MPC comprises a majority of external members who outnumber the Bank members 5–3. A second issue is the raging controversy around growth versus inflation, with the Bank resolutely sticking to its last and not allowing itself to stray from its core mandate of price stability. Mercifully, the vociferous calls from some policy quarters and interested exporters' lobbies for currency depreciation, which engulfed the Bank in the first half of 2012, were no longer heard. The voting pattern in the MPC inevitably weighs on the overall credibility of the monetary policy decision-making process. The time is ripe for a review of legislation to give

the Bank operational independence in the formulation and implementation of monetary policy as is the case not just in most developing economies, but also in a number of major central banks, including the US Federal Reserve, the European Central Bank, the South African Reserve Bank and even the Bank of Japan.

14. An acid test for a central bank is the management of inflation expectations. Despite the tussle at the level of the MPC, I am pleased to report that both inflation and inflation expectations have stayed at low levels, giving the country a stable macro-economic environment which has led, in turn, to a higher level of support for the Bank and its policies among the wider population, notwithstanding much negative coverage in some parts of the mainstream press and in business publications. A sustained communication strategy, with increasing reliance on Open Mouth Operations, facilitated this outcome. However, the fight against inflation is a continuing one. At 4 per cent year-on-year in December 2013, inflation is far below the double-digit levels greeting me on arrival at the Bank in early 2007. We should not lose sight of the fact that many of our peers, in the various regional groupings on the continent to which we belong, are doing better on this score. The Association of African Central Banks (AACB) had a target of 3 per cent meant to be achieved by 2012. SADC has an inflation target of 3 per cent by 2013–2018 – which goes to say that we must step up our efforts to bring domestic inflation even lower.

II. Areas of concern

15. ***Beyond Vision 2020 Vision 2020*** was a futures exercise with a difference. It was conducted in the mid-1990's. It sketched out a coherent view of likely future outcomes for our society and our economy. Wide participation in the exercise led to broad ownership, which facilitated our transition from an agricultural economy to a service-oriented and knowledge-based economy. I believe that we must explore all avenues to enable the Mauritian economy to avoid the middle income trap. Strategic planning is vital. We find ourselves in dire need of long-term vision – just as we did in the early-1990's. ***Vision 2020*** was led by the public sector and drew on the support of academia, business leaders, opinion-makers, non-governmental organisations, and other stakeholders. Now, when the public sector is suffering from limited planning capacity and expenditure constraints while, in parallel, the private sector has burgeoned, I would encourage private sector organisations to take centre stage, set up a think-tank and take the lead in fashioning a strategy and a vision for the country. This will mark a new stage in our much-vaunted public / private sector partnership, that lies at the root of our economic success, and will signal that the private sector has come of age and is ready to look beyond self-interest to focus on the common good.

16. ***An adult approach to understanding monetary and fiscal policy.*** There has been an open debate between the Bank and the Ministry of Finance and Economic Development (MOFED) on several economic issues this year. Although I appreciate these vivid discussions, I fear that there is a discernible tendency in the press and among other economic commentators to blow some issues out of proportion, to fan dissension, and to spread misunderstanding, raising misguided questions about the independence of the Central Bank and the effrontery of an "unelected" Governor not heeding the wishes of elected officials. The incontrovertible international evidence of superior outcomes from independent central banks, with governors immune to short-term political pressures, is occulted. There is a failure to appreciate what "coordination" between monetary and fiscal policy means. In an ideal world, coordination would entail both parties working together for a common goal. However, if all adjustments have to be borne by one side, then this can hardly qualify as "coordination". Regrettably, much of the time, this has been the case for monetary policy, where compromises were expected from the Bank.

17. Unfortunately – or fortunately, depending on where you stand on the issue – our hands are bound by the statute setting up the Bank, with the result that adjustments cannot come from the monetary policy side; and the Bank gets blamed unfairly for actually doing the job for which it was set up in the first place! I would make an appeal for a better-informed and

more adult approach to understand the differing perspectives where coordination between monetary and fiscal issues is needed. The Bank's monetary policy has been subject to much criticism by economic agents and doubts were cast on whether we should not throw overboard our IT-lite monetary regime in favour of – in the order proposed, and at roughly one-year intervals – (i) pegged exchange rates vis-à-vis each of *three* major currencies of export interest (which would have been quite a feat!), (ii) exchange-rate targeting and (iii) nominal GDP-targeting. Predictably, the Bank resisted these calls – just as we had resisted earlier calls from the IMF to move from our hybrid regime to a pure Inflation-Targeting framework.

18. ***Rethinking our economic strategy.*** A rethinking of our economic strategy is warranted in the light of the new global economic paradigm characterised by muted growth prospects in our traditional advanced economy partner countries, combined with a slowdown in growth momentum in emerging economies. I strongly believe that a rebalancing of the economy, away from consumption and towards investment and exports, is urgently required if we want to contain rising current account deficits, sustain strong growth, and graduate to a high-income economy. While monetary policy through an appropriate level of the Key Repo Rate (KRR), could contribute to a more balanced economy, it should be accompanied by appropriate fiscal policies and supported by bold structural policies to raise productivity across public and private sector enterprises.

19. ***New roles of central banks***. Central banks have been responsible for cushioning some of the financial damage arising from the disorderly financial and monetary conditions triggered by the global financial crisis. However, this has come at a dear price, with central banks' buffers dwindling and their fire-power compromised by the continued ultra-low returns on their investment portfolios. Central banks in key economies have become the new economic game-changers, taking the strain of propping up their financial sector and their economies on their own balance sheets. The Bank has faced similar challenges and has not been immune from some of the problems affecting its (bigger) peers elsewhere, such as the US Federal Reserve, the Bank of England, the Bank of Japan, the Swiss National Bank, and the Reserve Bank of India.

20. Restoring the health of the Mauritian economy is no longer the only item on the agenda anymore, as the Bank's efforts to prop up the economy by combating appreciation and absorbing liquidity have combined with negligible returns on its reserves to raise serious concerns about the health of the Bank's balance sheet. Expansionary monetary policy has recently been scrutinized by global fund managers and economists, who argue that the effect of monetary easing is felt only by big corporations and ignores SME's. Some have gone even further, declaring that in recent times, expansionary monetary policy might have been of purely cosmetic benefit. Central banks such as the Bank of England and the US Federal Reserve have launched initiatives to aid SME's, thus making their own policy decisions more significant. With the advent of the crisis, it is normal that the roles of central banks changed to tackle the issues in hand. Now that we are emerging from the crisis, there are increasing calls for central banks to return to their core mandate and avoid taking on extra responsibilities which they are ill-equipped to handle.

21. ***The continuing challenge of "negative carry" for the Bank's balance sheet.*** Faced with a low interest-rate environment, compounded by heightened volatility in financial markets – especially in the fixed income space where bank reserves are traditionally concentrated – we have strived to generate a decent return on our reserve assets without compromising on their safety. The Bank was trapped in a pincer movement of low-yielding reserves and a rising volume of reserves. On the one hand, reserves continued to be affected by the near-zero return on US- and Euro-denominated assets and by the significant decline in gold prices in 2013. On the other hand, reserves increased as a result of our actions, prompting the structural excess rupee liquidity in the banking system which was showing disturbing signs of getting dangerously out of hand. We had no alternative but to issue longer-term paper, in the form of 5-Year Bank of Mauritius (BOM) Bonds, in addition to

the BOM Bills and Notes which we have been issuing since 2010 to bring the excess liquidity to a reasonable level. The "carry", that is the difference in yields between the rising volume of reserve assets in our portfolio and the weighted yield on BOM paper issued to mop up excess liquidity, continued to remain negative and currently stands at around 3 percentage points.

22. The impact on the Bank's finances would have been even worse had we not pursued a conservative diversification strategy in search of safe, liquid, and higher-yielding currency assets. Because our statutory mandate as the international reserves manager of the country is security, liquidity, and then return, – in precisely that order – we have been constrained in terms of how much we could potentially expand the risk envelope in search of higher yield. With revenues generated from external assets showing little upside, considering the risk limits, and with the supply of Government paper remaining constrained, at least partly because of greater recourse to foreign currency debt, the Bank has suffered rising balance sheet stress. With the large volume of BOM paper outstanding at end-December 2013, the sterilisation cost is expected to reach Rs700 million in the coming year.

23. ***Danish debt management model.*** The transfer of the debt management function, for both domestic and external debt to the Bank, was an initiative of MOFED and was inspired by the Danish model. We did not, however, consider it appropriate to set up a full-fledged Debt Management Unit within the Bank as this was not justified by the low level of transactions and would have caused much duplication of work already done by other Divisions at the Bank. The International Monetary Fund reviewed the current debt management arrangements in December 2013. It identified some duplication in the work done by the Bank and within MOFED, and has noted several inefficiencies. These will need to be addressed, along with the obstacles preventing the development of a secondary market for Government paper.

24. ***The problem of excess liquidity exacerbated by Special Funds.*** Large and growing balances in Special Funds such as the *National Resilience Fund*, the *Build Mauritius Fund* and the *Road Decongestion Program Fund*, all financed by Budget measures and transfers, are creating difficulties for the Bank to achieve its objective of monetary and financial stability. The Treasury places these funds with commercial banks, further inflating the level of excess liquidity, and handicapping the Bank in the management of liquidity in the banking system. To add insult to injury, the Bank's actions and authority were further undermined by the Treasury effectively acting *as a lender of first resort* via the deployment of these funds to cash-strapped commercial banks, which would otherwise have taken the normal route of seeking accommodation from the Bank and enabled the repo rate corridor to gain traction. I have complained against both of these practices as I believe that a *Single Treasury Account,* placed at the central bank, does represent best practice and that it is unhealthy for the single largest player on the financial market to frustrate the Bank by its actions. We are now exploring the possibility of requiring a higher Cash Reserve Ratio from Special Fund deposits in excess of transaction balances.

25. ***Dynamic provisioning – Too late in the game.*** At the core of the Bank's problem lies a weak balance sheet. The combination of Operation Reserves Reconstitution (ORR), embarked upon hesitantly – and, that too, only after securing a now-problematic agreement to co-share the attendant costs with the Treasury −, open market operations at rising volumes, and low yields on reserve assets, allied with a "negative carry", has proved lethal for the Bank's finances. In a much-earlier letter, I had mentioned dynamic provisioning – allowed by the *Bank of Mauritius Act 2004*, incidentally – as a mechanism for the Bank to salt away some profits for the lean years ahead. We tried to apply this approach in July 2007 to our profits for the Financial Year 2006/2007. At that time, we were clearly ahead of the game – only to be charged with accounting trickery. Some will recall how the Bank was pressured into reversing these provisions and distribute them as profits via a *second* dividend payment in July 2008. Had the concept of dynamic provisioning then gained support from the Bank's board and from the Treasury, the Bank would have been in better shape today and would

have absorbed sterilization costs reasonably well. It is too late in the game to hanker after dynamic provisioning. I can only renew my call to the authorities concerned to help alleviate the Bank's fragile balance sheet, and possibly draw some inspiration from Australia which shored up the fire-power of its central bank by a massive injection of resources in the final quarter of 2013.

26. ***Islamic banking products – On hold?*** Since 2007, we have taken a number of initiatives to promote the development of Islamic banking in Mauritius, including the establishment of an appropriate legislative framework for Islamic finance as well as becoming a full member of the ***Islamic Financial Services Board*** and a founder-member of the ***International Islamic Liquidity Management Corporation***, both key institutions in international Islamic finance. The Public Debt Management Act 2008 was amended to provide for the issuance of *Sharia*-compliant instruments such as sovereign *Sukuks* by Government. Unfortunately, the public debt issuance calendar has never provided for the issuance of *Sukuks*, as proposed by the Bank in its capacity as debt adviser to Government, and this severely compromises the prospect of our jurisdiction playing a bigger role in the growing world of international Islamic finance. ***(More on this issue)***

27. We are finalising preparations for the conduct of Commodity *Murabahah* Transactions (CMT's) to provide Islamic Banking Institutions (IBI's) operating in Mauritius with an instrument for liquidity management. The CMT's, to be conducted under the umbrella of a Master Agreement, which will be finalised in consultation with the IBI's and the banking industry, will extend the range of tools available to the Bank for the conduct of Open Market Operations.

III. A year of measurable progress

28. ***Economy.*** The Mauritian economy maintained its positive growth momentum in spite of soft external economic conditions in our main trading-partner countries, thus maintaining its unblemished record of positive GDP growth throughout the global financial crisis. GDP is estimated to have grown by 3.2 per cent in 2013. All the major economic sectors recorded positive growth rates, with the exception of *Construction* and *Agriculture*. Rigidities in the labour market, coupled with a growing structural skills mismatch, continued. Female and youth unemployment remained matters of concern. First-time job-seekers were not helped by generous salary increases which went into effect in the second half of the year. Although downside risks to growth persist, mainly emanating from the uncertain recovery and soft external demand for our exports of goods and services, with their knock-on effects on subdued domestic private investment and consumer spending, there is some upside potential with the Eurozone expected to emerge from recession in 2014. ***(More on this issue)***

29. ***Monetary policy.*** Recent MPC meetings have witnessed persistent divergence of views on the appropriate monetary policy stance between, on the one hand, the three Bank executives, and, on the other, the external members who predominate on the MPC. The majority held the view that given what they perceived to be subdued inflation risks, monetary policy should support growth and employment. My two Deputy Governors and I were in favour of a small hike in the KRR to signal our concerns about inflation risks, and risks to financial stability, stemming from a prolonged period of low interest rates in the country. We thus saw a 25 basis points cut in June to 4.65 per cent after fifteen straight months on hold. The cut was effected against a backdrop of rising inflation, from 2.9 per cent year-on-year in January 2013 to 3.7 per cent in May, the latest data point available to the June MPC meeting. We ended the year with year-on-year inflation at 4 per cent in December. ***(More on this issue)***

30. In my opinion, negative real interest rates – relative to saving deposit rates offered by banks, typically 25–115 basis points below the KRR – have contributed to a significant decline in the savings rate, given a boost to consumption leading to a sharp deterioration in

the current account deficit, and fuelled speculation in search of higher yield beyond the safety of bank deposits. Little wonder then that Gross National Saving continued its downward slide from 15.1 per cent of GDP in 2012 to 14 per cent in 2013. Low on-lending rates have in turn induced growing indebtedness of the corporate sector, driven partly by speculative investment in the property sector. The misallocation of credit has increased vulnerabilities in the banking sector and the economy at large. Given such risks, we strongly believe that the MPC should start normalizing interest rates.

31. ***Exchange rate policy.*** Stressed conditions on export markets sparked considerable support for currency depreciation among exporters and their lobbyists, including the crypto-lobbyists embedded in different parts of the economic and financial establishment. Consumers rarely get invited to the debate on the subject and their voices go unheard. We thus tend to lose sight of the fact that Mauritius imports twice as much as it actually exports, with food and fuel accounting for a major part of the import bill, which makes the exchange rate a strong detonator for social unrest, if mismanaged. It is our responsibility to manage the exchange rate in the best interest of all our countrymen, as provided for in the Bank's statutes. We have held the view that supporting a narrow sectional interest, at the expense of the wider public interest, is a matter of fiscal/industrial policy.

32. The year 2013 saw the Bank stepping up its intervention on the foreign exchange market – we intervened on 238 days, that is, almost every working day, and successfully transacted nearly 80 per cent of the time – to combat unwarranted appreciation not in line with fundamentals, smoothe out volatility, and continue the ORR programme on which we embarked in mid-2012. Have we succeeded in our objective of aiming for exchange rate stability? The exchange rate statistics speak for themselves. At the start of my first mandate as Governor in 2007, the rupee was under considerable pressure from speculative transactions and over-borrowing, resulting in a volatile currency. I am happy to record that our rupee did not suffer from the extreme volatility affecting most countries across all continents, whether BRICS, emerging markets, or frontier economies, during 2013. In Sub-Saharan Africa, our currency came second, behind the Botswana *pula.* I draw some satisfaction from the fact that we have been able to stabilise the rupee. This is no mean feat for a small open African economy, with euro-biased exports and dollar-biased imports.

33. ***Liquidity in the banking system.*** I have discussed earlier the factors underlying the excess liquidity in the banking system. We continued with our efforts to mop up/sterilise this veritable deluge of liquidity through the issuance of our own instruments – which reached an all-time record of Rs20 billion outstanding in August 2013. The management of this surplus liquidity, which threatened to de-stabilise domestic financial conditions, stretched the resources of the Bank. Given the structural nature of the excess liquidity, the Bank went beyond its traditional short-term liquidity management instruments and started issuing 5-Year BOM Bonds in addition to the 3-Year BOM Notes. We took extra care not to create any financial fragmentation by piggy-backing the issuance of BOM securities on the regular auctions of the corresponding tenors that we conduct on behalf of the Treasury. ***(More on this issue)***

34. ***Debt management.*** The lengthening of the maturity profile of Government debt is part of the Debt Management Strategy, on which the Bank advised the Treasury, to mitigate rollover and refinancing risks. The exercise continued during 2013 with the issuance of more medium- and long-term Government securities, relative to maturing securities. Correspondingly, the share of short-term obligations by original maturity (inclusive of short-term borrowings) was halved, plunging from 36 per cent in June 2007 to 18 per cent in December 2013. The share of medium- and long-term obligations surged from 64 per cent to 82 per cent over the period. In addition, greater recourse by Government, especially since calendar year 2009, to long-term foreign loans and grants to finance a significant part of its budget deficit – irrespective of its devastating double effect on rupee liquidity, which I discuss elsewhere – also contributed to lengthen the maturity structure of public debt. Provisional

data for end-September 2013 record external debt at around Rs45 billion, three times the level of June 2007 when it was Rs13.5 billion. ***(More on this issue)***

35. ***Reserve management***. At the start of my Governorship in 2007, the reserve portfolio of Rs43.1 billion, or USD1,289 million, was overwhelmingly invested in USD, GBP and Euro which accounted for just above 75 per cent of reserve assets. This was not unusual for central banks as these were the three major currencies. We were ahead of the game when I initiated an active portfolio diversification strategy to hedge against portfolio risk arising from this concentration. We sought out currencies such as the Swedish Krona and the Norwegian Kroner, which were less correlated to the three major currencies, and included them in our reserve portfolio, thus reducing the key currencies to just below 60 per cent in December 2013. We diversified our reserve portfolio further through increasing our gold holdings, when we bought two tons of gold from the IMF Gold Sales in 2009.

36. Few now recall how we came under attack from two opposite fronts at the time: one charged that we should not have bought any gold in the first place while the other attacked for not buying a bigger volume! When gold prices soared in the period 2010–2012, there were murmurs of reserve mismanagement, supported by hypothetical estimates of the notional “losses” we suffered by not investing up to 50 per cent of our reserves in gold. Gold prices fell nearly 30 per cent to USD1,204 in 2013, its sharpest decline since 2001, pushing, for example, the Swiss National Bank to a SFR9 billion loss in 2013. I wonder how our Bank would have coped if we had followed the advice to invest half of our reserves in the yellow metal! In hindsight, the diversification strategy, which we pursued primarily in search of greater security, has clearly paid off, especially when viewed against the backdrop of several other central banks actually incurring capital losses in their portfolio during the financial crisis.

37. The Euro Zone struggled with recessionary conditions, with attendant risk to the global growth outlook for most of 2013. For a small economy like Mauritius, critically dependent on export demand from the Euro Zone, there is a clear need for more vigilance, and a more aggressive diversification drive. In mid-2012, when the country’s import cover was at 4.5 months, the Bank decided to embark on ORR to increase the level of Bank foreign reserves to 6 months’ import cover. The year 2013 saw the external reserves topping Rs100 billion for the first time, to stand at Rs103.5 billion at end-December 2013, or USD3.43 billion, representing 5.6 months of import cover. The Bank is well on the way to meet the basic objective of the ORR.

38. ***Forex intervention***. We continued to intervene actively, almost on a daily basis, on the domestic foreign exchange market during the year to remove unwarranted volatility. The Bank purchased foreign currency of nearly USD1.1 billion – a record – and sold the equivalent of USD470 million. We thus doubled our foreign currency purchases from the level of the previous year when we bought nearly USD525 million. It would have been extremely dangerous for the Bank to envisage forex purchases at such elevated levels if we did not have an alternative to placing the accumulating reserves arising therefrom in low-yielding traditional reserve assets. We used a major part of the proceeds to provide foreign currency to the State Trading Corporation, at its request, to finance the import of food and fuel, major items in the consumer price basket, at stable exchange rates which in turn led to stability in the prices of these products in the domestic market. Our forex intervention has turned out to be the proverbial stone that helped us to bag the two birds of exchange rate stability and price stability, both major policy objectives of the Bank. ***(More on this issue)***

39. ***Safety of systemically-important banks***. We achieved definite progress in 2013 in our endeavours to enhance the resilience of the banking industry and reduce financial stability risks. Back in 2012, I had urged the large banks to reduce the complexity of their group structures and segregate their banking and non-banking activities. This measure seeks to limit the risk of contagion to the banks, enhance market discipline and transparency, and ensure that bank boards and management focus attention on the core business of banking. We also pressed for periodic rotation of directors at the level of bank boards. The

restructure will benefit depositors, bank creditors, and shareholders. The law was reviewed in 2013 to facilitate the restructuring process. Three banking groups have already reached an advanced stage in reorganising their corporate structure, which will safeguard their banking activities from risks arising from other business segments of the same corporate group. Further, one bank, formerly operating as a branch of an international bank, incorporated as a subsidiary in May 2013. The objective is to protect affiliates of foreign banks operating in Mauritius from any potential problem affecting their parent banks in their home country. ***(More on this issue)***

40. A long-standing characteristic of the domestic banking sector is the predominant presence of a few large banks. Any problem arising in these banks could trigger contagion across the financial system and affect the real sector. The Bank has the duty to mitigate this risk for the safety of the financial system and the economy generally. I first publicly flagged this issue for attention in September 2011. We are now proceeding to establish a framework for Domestic-Systemically Important Banks, drawing on the recommendations made by the Basel Committee on Banking Supervision in October 2012. The draft framework has been issued to the industry for comments. Under our approach, banks reckoned as systemically-important will be subject to more stringent conditions, including the maintenance of a capital surcharge for their systemic importance. This measure will be applicable to banks as from the first quarter of 2016, thus giving them ample time to prepare for the change.

41. ***Macroprudential measures.*** We had to roll out quite rapidly a wide range of macroprudential measures to cope with rapidly-emerging vulnerabilities in the financial system. I first drew attention to the matter in my Statement of 5 October 2013, prefacing the ***Annual Report of the Bank*** for the Financial Year 2012–2013. We issued relevant guidelines in October 2013. The macroprudential measures are now being implemented. Banks will apply the measures in a phased manner to allow them and their customers to adjust smoothly to the new requirements. The measures encourage banks to adhere to more prudent lending standards, thus reducing the vulnerability of the banking sector to credit concentration and customer default risk in the targeted sectors. ***(More on this issue)***

42. ***Basel III.*** We followed up on the *Consultation Paper on the Implementation of Basel III in Mauritius,* which we issued in October 2012, by circulating a draft *Guideline on Scope of Application of Basel III and Eligible Capital* to the banking industry. This sets out the rules and tentative timelines to implement some of the elements of the stronger Basel III capital framework. Higher capital requirements under Basel III will strengthen the ability of banks to operate under stress conditions and will help to protect depositors. We shall ensure that the transitional arrangements to implement the new standards allow the banking sector to meet the higher capital standards through adequate earnings retention and capital raising, while still supporting lending to the economy.

43. ***Disclosure of information to guarantors.*** Guarantors have rarely been apprised of their extant financial liability in case of default by any borrower whose original debt they may have guaranteed, typically years before the borrower defaults and the guarantee is actually enforced. I had asked for an amendment in the banking legislation to empower the Bank to require every financial institution to make a statement of account available to the guarantor of any credit facility. The law was amended in December 2012. Accordingly, we issued the *Guideline on Disclosure of Information to Guarantors* to the industry for consultation in September 2013, and it became effective in January 2014. The guideline provides guidance to financial institutions, setting out the framework, and prescribing the instances, for issuing statements of accounts in written or electronic form to guarantors of credit facilities. ***(More on this issue)***

44. ***Future of banking.*** Rapid developments in the banking and payments technology landscape, combined with increasing competition for banking business, are fuelling a drive for more efficient, automated, and reliable delivery platforms and information systems. The year 2013 saw a number of domestic financial institutions upgrading their IT systems to reap

efficiency gains, enhance their capacity to grow their business, cater for new products, and offer better service to their customers. Enabling technology allows banks to move closer to their customers, while gradually shifting from the conventional "brick and mortar" branch-banking model to adapt to the needs of customers on the look-out for faster, 24/7, on-the-spot access to banking services. We are fast moving towards a cash-lite society, with consumers accessing banking services through the Internet and mobile phones. The entry of mobile financial service providers in the low-value payments space has brought some much-needed competition, to the benefit of customers. To meet these challenges, we have been adapting our regulatory framework to cater for electronic delivery of banking services. We introduced the *Guideline on Mobile Banking and Payment Systems* in February 2013 to complement the *Guideline on Internet Banking* which we had issued in 2001. ***(More on the issue)***

45. The Bank's monitoring and surveillance functions require it to obtain and analyse a large volume of data from banks and other regulated financial institutions. We are concerned by the rising reporting burden on banks and run the risk of suffering from data overload at our end. We are now embarking on a landmark project to automate dataflow from financial institutions, set up a data warehouse, and introduce Business Intelligence tools for users. The project will radically improve the entire system of data management at the Bank as well as reduce the reporting burden on financial institutions. The technology envisaged for the transmission of information, XBRL – or eXtensible Business Reporting Language – is used by major regulators and authorities across the world. We expect to roll out the new system in the next 18 months. It will drastically improve the collection, storage, and processing of information at the Bank. ***(More on this issue)***

46. ***Protection of customers of financial institutions.*** Ever since I joined the Bank, I have been stressing the need to have an Ombudsperson for the entire financial sector to provide a low-cost recourse for consumers of financial services to address and resolve their grievances. However, the law makes provision for the post of an Ombudsperson for *banks* only, to be filled by an officer of the Bank. This is clearly insufficient. Some progress has been achieved in the protection of customers with an amendment to the *Banking Act 2004* in December 2012 to give powers to the Bank to require financial institutions to establish procedures to that effect. We accordingly issued the *Guideline on Complaints Handling Procedures* in August 2013, detailing a broad range of measures to be implemented by financial institutions to deal with complaints and grievances from their customers. The Bank has been collecting information on complaints received by banks. ***(More on this issue)***

47. It has also been quite some time since I began urging banks to review their rates and charges. The increasing number of complaints received at the Bank from the public prompted us to set up a Task Force in July 2012 to inquire into the terms and conditions of banking and related financial contracts, including fees, commission and charges. Members of the public were invited to submit their comments and proposals. The Task Force has been considering the issues raised during the representations and will be releasing a public consultation document this year with a view to ensuring that both consumers and banks have a fair deal. The recent amendments to the *Banking Act 2004* to protect consumers of financial services are welcome and support the same objective. ***(More on this issue)***

48. ***Exchange of information among regulators.*** We broke new ground in sharing information with foreign regulators from countries where our domestic banks have extended their footprint. I felt it imperative to improve cross-border supervisory collaboration and sharing of information between ourselves as home regulator and the host regulators. We already had in place bilateral agreements, or memoranda of understanding, with the concerned host supervisors. We achieved a new milestone in cross-border supervisory cooperation by organising "Supervisory Colleges" for our two systemically-important banking groups, namely, the Mauritius Commercial Bank and State Bank of Mauritius, in November 2013. The Bank is among the first central banks in Africa to have organised such Supervisory Colleges. We capitalised on the presence of the host supervisors at the Bank to

hold an inaugural workshop on Crisis Management for the two banking groups. ***(More on this issue)***

49. ***Mauritius Credit Information Bureau.*** The Mauritius Credit Information Bureau (MCIB) has proved to be instrumental in supporting credit intermediation by offering a platform for information sharing on borrowers' characteristics and indebtedness. We have successfully enlarged the range of participants in MCIB, which now includes utility bodies. MCIB has facilitated prudent lending by financial institutions. This is well captured in the *Depth of Getting Credit* index of the World Bank's ***Doing Business 2014*** survey where Mauritius has topped the list of African countries for several years. This year, we have scored 6 over 6 in the *Depth of Getting Credit* index and the country's overall rank improved by ten notches to 42nd in the 2014 edition of the survey.

50. ***Reinforcing the surveillance process.*** The financial crisis has forced bank regulators and supervisors to re-examine their approach to fulfilling their functions. We drew on the experience of other countries and our own deep knowledge of local conditions to upgrade our compliance-based and risk-based approach to regulation and supervision. We enhanced our off-site surveillance by extending coverage of information collected, and the parameters monitored, which in turn enabled a deeper analysis of the evolving conditions. We streamlined the templates used to gather information. Concurrently, during the year, we reviewed the methodology for conducting on-site examination on the operations and affairs of financial institutions. The new risk-focused methodology is more comprehensive and is modelled on the internationally-acknowledged CAMEL framework – quite familiar to the Bank as we have been using it for years now for off-site surveillance. Emerging risks can be proactively identified, at the level of both individual institutions and the industry as a whole, and measures can be taken rapidly to address them. We applied this new approach in 21 on-site examinations carried out in 2013.

51. ***Shadow banking.*** The financial scam, unfurling over the country in early 2013, underlined the necessity to review the domestic regulatory and supervisory framework which is characterised by the presence of several agencies. Legislative changes were brought in December 2013 to transfer the supervision of credit unions and money lenders to the Bank from the Registrar of Co-operative Societies and the Accountant General, respectively. It is a step in the right direction towards consolidating oversight of financial intermediaries. We have already earmarked a dedicated team to look into the various issues associated with this added responsibility. However, credit unions and money lenders represent a small fraction of the financial sector. Insurance companies, for instance, are offering certain quasi-banking products and have a more dominant position in the financial sector. Financial intermediation outside the banking sector tends to undermine the role of the Bank in effectively conducting monetary policy and ensuring the soundness of the financial sector. We may have plucked the low-hanging fruit but much more needs to be done to minimise risk to the system and to our jurisdiction.

52. ***Islamic banking.*** In September 2013, I had the signal honour of being elected Deputy Chairman of the Governing Board of the International Islamic Liquidity Management Corporation (IILM) – a supranational body, launched in October 2010 and headquartered in Malaysia, which is engaged in issuing Islamic liquidity instruments to facilitate liquidity management by Islamic banking institutions. The Bank is a founder-member of IILM. This election raises the profile of our jurisdiction in the global Islamic financial services industry. We shall get a further boost from the 2014 Summit of the Islamic Financial Services Board (IFSB), which the Bank will be hosting in Mauritius in May 2014. This will see the participation of some 300 leading lights in the world of Islamic finance around the theme "New Markets and Frontiers for Islamic Finance: Innovation and the Regulatory Perimeter". We ended the year with an application for an Islamic "window" operation from an established bank. ***(More on this issue)***

53. ***Polymer banknotes.*** Another "first" in the year was the issue of polymer banknotes, in three denominations (Rs25, Rs50 and Rs500) from two different note-printers. Launching these new generation notes, on 22 August 2013 during the Annual Meeting of the AACB in Mauritius (itself, yet another "first") – in the presence of a *parterre* of guests comprising 32 Governors and heads of central bank delegations representing 44 countries, the General Manager of the Bank for International Settlements, and the President of the African Development Bank – Dr The Honourable Navinchandra Ramgoolam, GCSK, FRCP, Prime Minister of the Republic of Mauritius, delighted his audience by calling Governors "the new rock stars of the day, with some of you actually younger than the Rolling Stones!". The Mauritian currency-using public is also delighted by these notes and has given it an enthusiastic reception. Sadly, our attempt to introduce such notes several years earlier, in a previous currency procurement cycle, was stymied by a narrow, legalistic, interpretation of the applicable law in some decision-making quarters, which necessitated an amendment to legislation before we could proceed down this line. I am not aware of any other central bank which faced such a situation. Currency in circulation crossed the Rs30-billion mark for the first time in December 2013. ***(More on this issue)***

54. ***Payments system.*** A robust and efficient payments system is at the heart of a modern economy. The payments landscape is evolving rapidly and its effective oversight is becoming a matter of increasing concern. I laid much emphasis on the full modernization of retail payments which impact on high-volume, low-value transactions. When I joined the Bank in 2007, Electronic Funds Transfer did not exist and cheques were cleared manually. We now have a modern and effective electronic clearing system, with the Cheque Truncation project fully rolled out on 5 December 2013. This was preceded by a historic event early in the year when cheques were cleared manually for the last time on 31 January 2013. In some countries, cheques themselves are becoming history as the world moves to a cash-lite or cashless society.

55. We are setting the scene to move to the next stage which will entail making still greater use of electronic money. Unfortunately, we have failed to make any progress with the NPS – on which we have been engaged since 2009 and to which I alluded in my 2010 Letter to Stakeholders. It has been delayed for reasons beyond the control of the Bank. While we are entangled in fighting incomprehension, in some decision-making quarters, and overcoming resistance from vested interests, Mauritius has become a laggard in this area as several African countries have gone ahead and implemented NPS's to achieve greater efficiency and lower transaction costs in their jurisdictions. I believe the main hurdles have now been cleared and the Bank is moving ahead with the implementation of the project in the course of 2014. We have a lot of catching-up to do. ***(More on this issue)***

56. ***Virtual currencies.*** It is quite possible that virtual or digital currencies may play an increasing role and become the currency of the future, replacing notes and coins. This would be the logical continuation of the process that includes electronic banking, electronic payments and electronic settlement. If such a scenario materialises, financial regulation and oversight will no doubt change beyond recognition to cope with the new financial landscape that will go hand-in-hand with a bigger role for virtual currencies. We are not there yet, and not likely to do so in the foreseeable future.

57. No currency is safe as such, but there is greater comfort in a currency issued by a sovereign, and regulated by an official institution. The virtual "currencies" making the headlines do not offer such comfort, even if they offer greater convenience in settlements in some cases. Additionally, some have a high degree of anonymity and can be misused for criminal activities. The growing popularity of Bitcoin, for example, — which had seen at one point an increase in its value of 5,000 per cent – is tempting for individuals seeking rapid returns on their outlays. Whether such outlays should be termed "speculation" or "investment" is a matter of judgement. These virtual "currencies" are unregulated digital money and are not issued, or guaranteed, by any central bank. During the year, the Bank

issued an Advisory, cautioning the general public to exercise utmost diligence when dealing with virtual “currencies”.

Box – Ponzi schemes

This year, the Bank exposed two large scams which seriously damaged thousands of Mauritians financially. The Ponzi schemes we uncovered followed the classic model of those in the USA in the 1920’s, where one fraudster, Charles Ponzi, offered abnormally high and unusually consistent yields from a fake investment scheme, paying out the returns not from profits, but from the capital, and then running off with the capital itself.

Similarly, following complaints from victims, we discovered in 2013 that unscrupulous local criminals had slipped through the existing regulatory framework to trick people to invest their savings in similar Ponzi schemes. The ill-effects of the local Ponzi schemes soon gave rise to a growing number of complaints to regulators as many thousands of local people realised they were being defrauded.

As the fraudulent schemes came to light in December 2012, I immediately informed the police, as the two schemes at the centre of the evident fraud had been set up by companies that were not licensed to receive funds for investment. I also then asked banks to provide details of any accounts they were handling for the two principal fraudulent companies involved, and the nature of the due diligence procedures they had carried out on these companies.

In January 2013, the Bank began to conduct extensive on-site investigations of banks and other financial institutions to find the sources of the known fraud, to check for any similar undetected practices and to review action to prevent any further deception. In March 2013, in the light of the growing number of complaints and public controversy, I set up a help desk at the Bank for people to provide information on the investments they had made with the companies and to present any further complaints. We also allowed people to use the help-desk to check the credentials of any other financial schemes in which they were proposing to invest, to ensure such schemes were properly licensed. From the date of setting up the help desk, the Bank had received by 31 December 2013, a total of 3,630 complaints covering a sum of Rs937 million identified by potential victims.

The consequences of these scams on the financial sector were fortunately limited. By taking swift action, we at the Bank were able to limit the monetary damage done by this financial fraud. Furthermore, on the basis of the results of our investigations, we levied penalties on a number of banks for failing to protect their customers from the scams and failing to identify the fraudulent schemes operating through their systems. In addition, we called upon banks in Mauritius to radically review their oversight of customer accounts and their due diligence procedures for vetting financial schemes.

Moreover, I considered it timely to have a thorough assessment of the flaws in our system that led to the failure to detect the Ponzi schemes. So I called on assistance from the Reserve Bank of India (RBI), which had had extensive experience in dealing with such types of financial scams. The two assessors from the RBI came up with 29 recommendations to improve our regulation of banks and their practices, out of which 25 measures are being implemented to tighten up our systems. The RBI report also noted that “different agencies and banks were appreciative of the pro-active role played by the Bank of Mauritius in handling the issues related to the Ponzi frauds.” They added that the “BOM’s examiners did a commendable job (at one bank) in bringing out KYC/AML weakness in the bank.” The RBI report revealed many dubious practices in the banks concerned and a lack of computer-based systems for screening for fraud. In particular, the RBI report was critical of the high proportion of large transactions in cash handled by the banks for these companies without this alerting them to the fraudulent activities. In addition, there had been strange events involving alterations in the status of the directors of the fraudulent companies, changes in company names which the banks had ignored, and no checks had been made on whether the companies had appropriate licences for the activities in which they were involved.

The RBI report in its recommendations called for extension of the powers of the Bank in line with those of the Financial Services Commission under the Financial Services Act of 2007. This would allow it to take legal proceeding against such fraudsters and to freeze their assets. The RBI report considered that “the quantum of financial penalties imposed by BOM on banks is paltry and does not provide effective deterrence. There is a need to substantially increase the same. Moreover, imposition of these penalties also should be disclosed in the public domain.”

Part of the radical improvement we are introducing is that the Bank has made it mandatory for all financial institutions to put in place an internal whistleblowing policy. Financial institutions have a special position of trust in the national economy, and employees working with them have an individual and collective responsibility regarding their conduct and practices. We believe that there should be a proper framework in place for people to report any irregularities or unethical practices within financial institutions where they work, without fear of recrimination. We have also extended our programme of customer education, our checks on hiring employees, and their in-service training to prevent Ponzi schemes going undetected in the future.

In addition, the Bank has set up a *Market Intelligence Cell* which has been mandated to collect information from formal and informal sources to help detect any existing or potential financial crime and fraud, and carry out investigations.

In the wake of the Ponzi scams and financial frauds, proposals were made to amend the existing Memorandum of Understanding between Bank of Mauritius and the Financial Services Commission to include a framework for handling exigencies, such as the Ponzi scams. We expect amendments to be agreed and implemented in 2014.

Could these frauds have been prevented? There is no easy answer to this question. However, lessons have been learnt. I believe that one key way of preventing the recurrence of Ponzi schemes is through financial literacy programmes. Although the 2012 World Bank report indicates a relatively high percentage of adults accessing formal financial institutions (80.1 per cent in Mauritius, compared to 24.1 per cent in Sub-Saharan Africa), I believe that there is still room for improvement. Human nature often falls prey to greed and this has certainly been the case for thousands of our citizens in search of above-market returns. People need to recognise that if a scheme looks too good to be true, it probably is. They should take advice, before investing their lifetime’s savings. Promoting banking access to the uneducated and retirees should be a foremost priority for the banking sector, eventually resulting in benefit for both parties, but basic education about banking, its risks and advantages is clearly needed as part of the package. So too is the need for better surveillance by banks and regulators. ***(More on this issue)***

IV. Other highlights of the year

58. ***Regional cooperation.*** We scored another “first” on the regional cooperation scene in 2013 when the Bank hosted the 37th Assembly of Governors of the ***Association of African Central Banks*** in August and I assumed chairmanship of the Association. The Assembly was preceded by a Symposium on the theme “Financial Inclusion in Africa: the Challenges of Financial Innovations for Monetary Policy and the Stability of Financial System”. The Prime Minister of the Republic of Mauritius delivered the Keynote Address at the Symposium when, as mentioned earlier, he launched the first-ever polymer notes issued by the Bank. The presence of Mr Jaime Caruana, General Manager of the BIS, Mr Donald Kaberuka, President of the African Development Bank, and Mr Jaseem Ahmed, Secretary General of the Islamic Financial Services Board, amidst a record turn-out of Governors at

AACB meetings, raised the profile of the meeting and enriched discussions. As Chairman of the AACB, my overarching priority for 2014 will be to operationalise the Community of African Banking Supervisors, established at the beginning of the year and help to carve out a coordinating role for it in overseeing the work and initiatives in this area at the level of the various sub-regional groupings on the continent. ***(More on this issue)***

59. ***Financial Stability Board.*** Another honour bestowed on us was my appointment in July 2013 as the non-FSB Co-Chair of the FSB-RCG (SSA) for a term of two years. Let me elucidate these mysterious-sounding acronyms. First, the FSB, or Financial Stability Board: this is an emanation of the Group of Twenty leading economies (G-20) and was established in April 2009 when it was tasked with the coordination, at the international level, of the work of national financial authorities and international standard-setting bodies to develop and promote the implementation of effective regulatory, supervisory and other financial sector policies. The only African country in the G-20 is the Republic of South Africa. Second, the RCG: this stands for Regional Consultative Group, which the FSB set up in 2010 to extend its global reach beyond the G-20 membership and help it to address financial stability issues from a wider perspective. Six RCG's have been set up and are supported by the FSB Secretariat, based at the Bank for International Settlements in Basel. Each RCG has two co-chairs, one from the FSB members and the other from the non-FSB members. Third, SSA stands for Sub-Saharan Africa. We accepted the invitation to join the RCG (SSA) at its inception in 2011. As non-FSB Co-Chair of the RCG (SSA), I was honoured to participate in the November 2013 FSB plenary session at the Central Bank of Russia, under the Chairmanship of Governor Mark Carney of the Bank of England, where I reported on the work of our RCG and shared our concerns.

60. ***Overseas engagements.*** The Bank's presence was well appreciated on the international scene by our peers and international financial institutions and this is reflected in the ever-growing invitations addressed to the Bank to attend regional and international events. Representing the Bank on the global stage offers benefits such as increased visibility, networking, sharing ideas and exposure to cutting-edge solutions to domestic issues. Key staff represented the Bank, at both regional and global level, attending conferences such as Financial Stability Board Regional Consultative Group, IMF/World Bank Annual Meetings, COMESA Committee of Central Bank Governors, and the Committee of Central Bank Governors in SADC. I believe that our exposure to the global community through meetings and conferences is indeed the way forward to broadening our horizon.

61. ***Corporate Social Responsibility: Bamboo Garden.*** Work progressed on the Bamboo Garden Project, which we launched as part of the Bank's Corporate Social Responsibility initiative. The Garden, to be located at Dubreuil, Midlands, in the centre of the island, covers a plot of land of around 10 acres. We have enlisted the services of the Agricultural Research and Extension Unit, of the Ministry of Agro-Industry, Food Production and Security, for its implementation. The project also benefits from the support of an Advisory Panel which we have established to oversee the botanical, aesthetic, and design aspects of this innovative project. ***(More on this issue)***

62. ***Corporate Social Responsibility: Athletics.*** We have been collaborating with the Mauritius Athletics Association since 2007 to organise the *Bank of Mauritius Inter Club Youth Championship Competition*. The 7th Edition of the Championship was held over two days in November at Maryse Justin Stadium, Réduit, and saw two new national records, bringing to 34 the rich harvest of records since 2007. Several commercial banks have joined us since 2011 to co-sponsor the Championship, enabling us to provide greater and more sustained support throughout the year to promising atheletes. ***(More on this issue)***

63. ***Communication with stakeholders.*** I have continued to maintain the high degree of interaction with stakeholders which I initiated when I joined the Bank in 2007. I could not have engaged in the process of reinforcing the regulatory landscape without consultation with the banking industry. Effective policy-making is best achieved through discussion with

stakeholders. Regular dialogue with them has undoubtedly helped the Bank to move quite rapidly on several fronts. Besides, the outbreak of the financial scams in early 2013 made it essential for the Bank to intensify communication with members of the public to keep them informed of developments as well as cautioning them against scammers and fraudulent schemes.

64. Here, I would like to highlight that, as far back as November 2009, the Bank had released a series of statements on its website under the caption ***Financial Education*** to draw the attention of the public to various types of financial frauds. The statements contain tips on how to identify scams and the procedures to report suspicious financial activities. I urge members of the public to visit the Bank's website – which is itself in the process of being revamped to make it more user-friendly – to familiarise themselves with the recent updates and help us detect any suspicious financial activity. I wish to reiterate the necessity for the public to exercise utmost diligence when dealing with individuals or companies with whom they are placing money. ***(More on this issue)***

V. Closing remarks

65. I would like to place on record my deep appreciation for the work accomplished by Mr Iqbal Belath, former Second Deputy Governor, who left the Bank in October 2013 at the end of his tenure. He had complemented our senior leadership line-up with unparalleled commitment. I had much pleasure serving the Bank alongside him and drawing on his steady support. He facilitated the integration of his successor at the Bank during the handing-over period. I welcome Mr Issa Soormally, who took over as Second Deputy Governor, on this engaging journey in the top echelons of the central bank.

66. Although 2013 has been a relatively decent year for the Bank, I believe we could have achieved much more. Our successes – in areas such as price stability, exchange rate stability, and financial stability – are either taken for granted or only understood by the *cognoscenti;* our failures are exposed to the public eye and known to all and sundry. Although we have been fairly successful in achieving our mandate of price and financial stability, I am left to wonder how much better our results would have been with greater cooperation from our stakeholders. I can only renew my call for strengthened collaboration and hope that this time my call does not fall on deaf ears.

67. We are striving to find the right balance between inflation and interest rate in the context of slowing growth rate. Our exchange rate policy has yielded the desired results over time and we are confident we can further fine-tune our exchange rate management policies. The domestic economy remains exposed to growing threats such as elevated consumer imports, stagnating exports, a quasi-structural current account deficit, high corporate indebtedness, and low household savings. The mandate of the central bank is traditionally restrictive in nature and the tools in our arsenal are limited, thereby bounding our influence on every macroeconomic indicator. The public is quite right in having high expectations of its central bank, but these should not be unrealistic.

68. With a new year comes new challenges and we have to be ready to face them head on. The world economy is on a still nascent recovery path. As a small economy, dependent on the export outlook arising from this recovery, we have to remain vigilant to external threats, including a possible relapse, and the heightened volatility likely to be provoked by the withdrawal of the massive stimulus that has propped up developed economies. We have already borne the brunt of the prolonged global crisis without too much wear and tear. I have no doubt that 2014 will see brightening prospects for the country and its citizens.

Annex

Domestic developments

New guidelines

7.1 ***Guideline on Mobile Banking and Mobile Payment Systems.*** The Bank issued the *Guideline on Mobile Banking and Mobile Payment Systems* in February 2013. The objective of the guideline, which is intended for providers of mobile banking and mobile payment services, is to promote a sound financial system in Mauritius and regulate the mobile banking and mobile payment systems.

7.2 ***Guideline on Complaints Handling Procedures.*** The amendments to the *Banking Act 2004* in December 2012 laid down specific provisions in relation to the protection of customers of financial institutions. The *Guideline on Complaints Handling Procedures* was issued in August 2013. It requires all banks to appoint a complaints officer to deal with complaints and grievances from their customers. *(More details on this issue are provided at paragraph 46.1)*

7.3 ***Guideline on Disclosure of Information to Guarantors.*** The *Guideline on Disclosure of Information to Guarantors*, issued in September 2013, sets out the responsibilities of financial institutions towards guarantors. Section 37(7) of the *Banking Act 2004* requires every financial institution to provide a statement of account to the guarantor of a credit facility extended by it, in line with guidelines issued by the Bank. *(More details on this issue are provided at paragraph 43.1)*

7.4 ***Guideline on Maintenance of Accounting and Other Records and Internal Control Systems.*** In November 2013, the Bank issued a new *Guideline on Maintenance of Accounting and Other Records and Internal Control Systems*. The purpose of this Guideline is to incorporate up-to-date best practices into the existing *Guidance Note on General Principles for Maintenance of Accounting and Other Records and Internal Control Systems*, issued by the Bank in November 1994.

Revised guidelines

7.5 ***Guidelines on Section 46(2) of the Banking Act 2004 – Appointment or Reappointment of Senior Officers.*** The guideline was reviewed in July 2013 to enhance the definition of a *senior officer* and to introduce a cooling period for a senior officer who has taken up employment in another financial institution. However, the revised Guideline was kept in abeyance until further notice following representations made by the Mauritius Bankers Association.

7.6 ***Guideline on Credit Concentration Risk.*** The *Guideline on Credit Concentration Risk* was amended in September 2013 following the review of the aggregate large credit exposure limits that apply to banks and non-bank deposit taking institutions. The guideline was again reviewed in November 2013 to incorporate certain macroprudential measures, namely sectoral concentration limits to be put in place by banks.

7.7 ***Guideline on Standardised Approach to Credit Risk.*** In December 2013, the Bank reviewed the *Guideline on Standardised Approach to Credit Risk*. This Guideline now incorporates the new risk weights, as prescribed by the macroprudential measures, for claims secured either by residential property and/or commercial real estate.

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8.1 In line with the mandate of the Bank to ensure the stability of the financial system, and using powers in the banking legislation, I decided to take the initial steps to implement a *Deposit Insurance Scheme* in Mauritius. In July 2012, after consultation with banks, I sent to the Ministry of Finance and Economic Development (MOFED) a Deposit Insurance Bill for submission to Parliament. In October 2013, I again approached the MOFED to bring the proposed Bill before Parliament. I am still awaiting a response from them.

8.2 One of the outcomes of the global financial crisis abroad was the adoption of new rules governing bank recovery and resolution. In December 2013, after nearly one year of deliberation, the member-states of the European Union finally reached an agreement to ensure that failing banks can be wound up in a predictable and efficient way, with minimum recourse to public money. It is now one of the requirements of the European Financial Stability Board (EFSB) that an effective bank resolution mechanism is provided in the banking laws. Similarly, one of the mandates of the Financial Sector Assessment Programmes of the World Bank and the IMF is to make sure that each country under review has an effective legal framework for bank resolution. Since an ailing bank which has an international presence may have cross-border implications, it is necessary that proper safeguards are provided in the law to address cross-border issues. In line with these measures abroad, we have informed MOFED of our decision to come forward with proposals for changes to the *Banking Act 2004* to provide for an effective bank resolution mechanism for Mauritius.

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26.1 ***Islamic banking products – On hold?*** The Public Debt Management Act 2008 amended the legislative framework to enlarge the scope of Government securities to include the issue of *Sukuk* bonds in Mauritius. Whilst this legislative amendment provides the Bank with the power to issue *Sharia*-compliant instruments, this project has not come to fruition yet. The Bank has continually pressed MOFED on this matter, but no progress has been made, no discussions held and no support provided to agree on a framework for the issuance and management of *Sukuk* bonds. My original aim was to position Mauritius as a regional financial centre that incorporates a niche market for Islamic finance. But other African countries have now taken the lead and already issued *Sharia*-compliant sovereign papers that have gained acceptance and recognition worldwide. So it seems we have missed the boat on this one.

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28.1 ***Economy.*** Growth in the Mauritian economy slowed down to 3.2 per cent in 2013, from 3.4 per cent in 2012. All the major economic sectors however registered positive growth rates, with the exception of *Construction* where real output contracted by 9.4 per cent: *Information and Communication* expanded by 7.7 per cent; *Finance and Insurance Activities* by 5.3 per cent; *Wholesale and Retail Trade* by 3.5 per cent; *Real Estate Activities* by 2.9 per cent; *Transport and Storage* by 2.6 per cent and *Accommodation and Food Service Activities* by 2.5 per cent. Final consumption expenditure growth is estimated at 2.6 per cent. Excluding aircraft and marine vessels, investment posted negative growth of 5.7 per cent in 2013, compared with a marginal contraction of 0.8 per cent in 2012. The forecast for the savings rate is 14.2 per cent of GDP at market prices in 2013, compared with 15.1 per cent in 2012.

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29.1 ***Monetary policy.*** Three major changes were brought to the MPC during 2013: first, the composition of the MPC was once again amended to provide, in addition to the Governor and the two Deputy Governors, for two external members appointed by the Prime Minister and a further three external members appointed by the Minister of Finance and Economic Development; second, the MPC published a Code of Conduct to govern the MPC meetings; and third, explicit provisions were made for the MPC to take into consideration the views of the Bank, MOFED and any other appropriate institution in order to improve the coordination between monetary and fiscal policy.

a. Under the new arrangements, the MPC has to publish a Code of Conduct to govern its meeting and to report once a year to the Board of Directors of the Bank on how well it has complied with that Code. The objective of the Code of Conduct is to provide guidance and set ethical standards to be adhered to, at all times, by the members of the MPC. The MPC adopted a Code of Conduct for its members and this was published on the Bank's website in July 2013.

b. Under the new arrangements, the MPC has to take into account the views of the Bank, those of the MOFED and the views of such other institution or organisation as the MPC thinks fit to do its work. Accordingly, the Financial Secretary expressed the views of MOFED at the March, June and September 2013 meetings while representatives from the *Association des Consommateurs de l'Ile Maurice* and a freelance consultant shared their observations at the June and September 2013 meetings, respectively. I firmly believe that monetary policy needs to be forward-looking, accompanied by transparent communication to the stakeholders. The presentations by the Bank's Staff, MOFED, external consultants, and other organisations are henceforth published one week after the release of the minutes of the MPC meeting.

29.2 At the March 2013 meeting of the MPC, with domestic and external economic conditions still subdued and the threats to the growth outlook seen to continue outweighing inflation worries, the MPC decided, by majority vote, that the KRR remained broadly appropriate at the current juncture and left it unchanged at 4.90 per cent per annum. Then, at the June 2013 meeting, as the same majority considered the domestic economy still vulnerable to the subdued external environment against a benign global inflation outlook, the MPC cut the KRR by 25 basis points to 4.65 per cent per annum. In September 2013, the MPC maintained the KRR at 4.65 per cent, again by a majority decision.

Click at

- https://www.bom.mu/?id=20285&Archive=Y for the Minutes of the MPC meetings released in 2013, and
- https://www.bom.mu/pdf/Research_and_Publications/Inflation_Report/Inflation Report_Oct13/contents.htm for the Inflation Report, October 2013.

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33.1 ***Liquidity in the banking system*** The Bank reviewed the Cash Reserve Ratio (CRR) requirements, with effect from the *maintenance period* starting 26 July 2013, and banks are now required to keep cash reserves of their rupee deposit base in Mauritian rupees. For Euro- and GBP-denominated deposits, balances at the Bank should be in Euro and GBP, respectively. USD balances should be kept for USD-denominated as well as for all foreign currency-denominated deposits other than Euro and GBP. The CRR has now been imposed on all Government deposits as well.

33.2 To address the persistent excess liquidity in the banking system, the Bank further refined the computation of the CRR with effect from the fortnight beginning 4 October 2013. The average CRR on rupee deposits was increased from 7.0 per cent to 8.0 per cent, and the daily minimum for rupee deposits from 5.0 per cent to 5.5 per cent. The fortnightly average CRR and the daily minimum balance on foreign currency deposits were reduced from 7.0 per cent and 5.0 per cent to 6.0 per cent and 4.5 per cent, respectively. I am pleased to note that the increase in the CRR has indeed resulted in the normalisation of the money market rates.

33.3 Against the backdrop of recent rigging scandals of benchmark rates in some jurisdictions abroad, the Bank has been monitoring the procedures regarding contributions submitted for computation of PLIBOR, the Port Louis Interbank Offered Rate. In the light of developments taking place worldwide and in consultation with the stakeholders in the industry, the Bank decided to publish rates for tenors that are actively traded. So from 2 December 2013, the Bank only publishes Overnight and the One-Week tenors, where most of the transactions take place.

33.4 The Bank has continued to support the reforms in the sugar industry through stimulus packages. As part of this support, the Bank renewed the *Protocol d'Accord* with the Mauritius Sugar Syndicate to grant them facilities under the Special Line of Credit for Sugar Crop Year 2013 for loans to small and medium planters. The Bank has made Rs1.2 billion available, at the rate of 3 per cent, for banks to on-lend at a maximum rate of interest of 3.5 per cent. This facility has been extended up to 31 January 2014, with repayment at latest by 31 May 2014. The Bank has also continued the Special Line of Credit in Foreign Currency scheme, introduced in June 2012, aimed at enabling eligible export and tourism operators to refinance rupee-denominated debt to address currency mismatch between their income streams and their existing debt servicing commitments.

33.5 Unfortunately, I have to report there has been no real progress with the project for the secondary trading of medium- and long-term government securities. We have already made amendments to the *Bank of Mauritius Act 2004* and to regulations made by the Financial Services Commission (FSC), in respect of fees. The main item yet to be agreed on is the exit facility for banks engaging in this line of business. We are still discussing a draft Memorandum of Understanding for trading of the securities on the Stock Exchange with the FSC, and the exit mechanism with MOFED.

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34.1 ***Debt management.*** In 2013, the Bank issued Treasury Bills and Treasury Notes for nominal amounts of Rs33.3 billion and Rs12.3 billion, respectively. The Bank also issued 5-Year, 10-Year and 15-Year Government of Mauritius Bonds as well as 15-Year Inflation-Indexed Government of Mauritius Bonds for total nominal amounts of Rs6.9 billion, Rs3.3 billion, Rs2.6 billion and Rs1.0 billion, respectively. Overall, in 2013 the Bank issued a net amount of Rs9.4 billion as Government securities.

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38.1 ***Forex intervention.*** During 2013, banks and foreign exchange dealers made total purchases in foreign exchange of the equivalent of USD4.1 billion, compared with USD3.9 billion in 2012, an increase of nearly 5 per cent. Total sales in 2013 in foreign exchange amounted to USD4.0 billion, compared with USD3.9 billion in 2012, an increase of just over 2 per cent. The total turnover of foreign exchange transactions in 2013 clearly shows that there was no liquidity constraint in this market and the level of business activity in foreign currency remained relatively stable compared with the previous year.

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39.1 ***Banking sector performance.*** The banking sector continued to grow in 2013, with assets reaching over Rs1 trillion. Growth in banks' assets was mainly driven by Segment A business. Banks remained profitable and adequately capitalised with a comfortable buffer over the minimum regulatory capital adequacy ratio of 10 per cent. One of the key strengths of our banks is the quality of capital, with Tier 1 capital representing a considerable proportion of the capital base. At end-December 2013, the Capital Adequacy Ratio stood at 16.4 per cent.

39.2 The quality of the credit portfolios of banks remained strong, despite a slight increase in the ratio of non-performing loans to gross loans. At the end of September 2013, non-performing loans accounted for 3.5 per cent of gross loans, against 3.1 per cent a year earlier. We are closely monitoring the evolution in credit quality. The cover ratio (specific provision to non-performing loans) was 41.3 per cent in September 2013.

39.3 Banks continued to expand their domestic network with six additional branches set up in 2013. This brought the total number of branches, including head offices, of banks operating in Mauritius to 227 at the end of December 2013, while there were a total of 450 ATM's compared with 441 at the end of December 2012.

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41.1 ***Macroprudential measures.*** The global financial crisis underscored the necessity to rely on macroprudential regulation, in addition to other measures, as a policy tool to curb potential systemic risk. The Bank introduced the following five macroprudential measures in October 2013:

a. The loan-to-value (LTV) ratio aims at constraining excessive credit growth and restricting losses in the event of customer default, or decline in property prices, by imposing a cap on the size of the loans relative to the value of the properties financed. The Bank introduced the maximum LTV limits as a macroprudential measure to discourage speculation, prevent excessive leverage, and reduce systemic risk associated with the rapid expansion of credit in the construction sector. Customers borrowing from banks to purchase property for the first time will not be affected by these measures.

b. The debt-to income (DTI) ratio provides protection to households from debt traps and aims at containing housing credit growth. Banks in Mauritius use the DTI as a microprudential measure to assess borrowers' repayment capability. Concerned with the growing level of household indebtedness, we introduced the DTI ratio to ensure that borrowers are not overleveraged whenever they borrow for the purchase or construction of a property.

c. The three additional macroprudential measures consist of risk-weighted assets, additional portfolio provisions, and sectoral limits. The measure on risk-weighted assets requires banks to maintain higher risk weights in the targeted borrower segments. The additional portfolio provision ensures early provisioning against future credit losses in more vulnerable sectors. The objective behind the sectoral credit limits is to contain exposure of banks to three sectors, namely, *Commercial, residential and land parceling*, *Tourism* and *Personal*. Overall, these measures should strengthen the resilience of our banking sector.

Click here at http://www.bom.mu/?id=72427 for the guidelines on macroprudential measures.

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43.1 ***Disclosure of information to guarantors.*** Section 37 of the *Banking Act 2004* was amended in December 2012 to enable the Bank to require every financial institution to provide a statement of account to the guarantor of a credit facility extended by it, in accordance with guidelines issued by the Bank. Accordingly, a Draft Guideline on Disclosure of Information to Guarantors providing guidance to financial institutions was circulated to banks, to non-bank deposit taking financial institutions, and to the MBA for views and comments. Following the consultation process, the Guideline was issued to the industry in September 2013 and became effective on 1 January 2014.

Click here at http://www.bom.mu/?id=90738 for the Guideline.

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44.1 ***Future of banking.*** Technology is changing rapidly today and is having an impact on banks' business models. Whilst electronic delivery channels for banking products and services have been around for years now, accessing banking services through the Internet and mobile phones is becoming increasingly popular in Mauritius. Consumers make payments using credit cards, debit cards and they transfer funds electronically or shop online instead of paying by cash or bank cheque. I welcome this trend as another step towards a cash-lite society.

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45.1 A staff study visit to the Reserve Bank of India has led to a better understanding of the integrated system of data collection, storage and processing, using an automated system. It enabled the project team to prepare the Request for Proposal to invite bids for the envisaged system. The bids received are presently at evaluation stage.

45.2 As a producer of macroeconomic statistics, the Bank is an active player in national and international fora. The Bank has decided to implement the most up-to-date internationally-agreed standards. The Statistics Division has contributed to the preparation of the forthcoming *IMF Balance of Payments Compilation Guide*, due for release soon. In particular, we have shared our experience in the collection of data on offshore entities. With the new powers conferred upon the Bank to regulate credit unions and money lenders, the *Depository Corporations Survey* will eventually be extended to include these financial institutions as well. At the national level, together with other official data-producing agencies, the Bank has actively participated in the sub-committee on "Harmonisation of Business Surveys" to reduce the reporting burden of the private sector.

45.3 Keeping in line with usual practice, we have posted the *Advance Release Calendar* on our website at the start of the year to inform users of the forthcoming releases. For the 6th year running, the Bank has conformed with the *Special Data Dissemination Standard* by keeping the public briefed on the dates of specific data releases. According to set timelines, the Bank has conducted its annual *Foreign Assets and Liabilities Survey*, the annual *Global Business Companies Category 1 Survey* and the quarterly *Inflation Expectations Survey* in 2013. The Statistical reports with varying frequencies (daily, weekly, monthly and annual) are freely available and are published on the Bank's website.

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46.1 ***Protection of customers of financial institutions.*** Section 96A of the *Banking Act 2004* requires all banks to appoint a complaints officer to deal with complaints and grievances from customers. Following consultation with the banking industry, we issued the *Guideline on Complaints Handling Procedures* in August 2013. It became effective on 1 November 2013. The key features of the Guideline are as follows:

a. Banks have to set up a complaints desk, duly indicated for that purpose, at their main office to receive customers.

b. For branches, there is no need to have a formal complaints desk but there should be a place for complainants, duly indicated, which may be with any front desk officer.

c. Financial institutions are required to retain details of complaints for at least a period of 7 years as from the date of their receipt.

d. Financial institutions are required to provide the Bank, on a quarterly basis, with information on complaints they have received.

46.2 In terms of information available at the Bank, the most frequent complaints made by bank customers are in relation to the following:

– Funds have been taken from their accounts by the use of cheques with forged signatures

– Early repayment fees

– Insurance Premiums on loans

– Excessive fees and commissions have been charged

– Charges have been applied when the account falls below a minimum balance
– Delay in crediting bank accounts on cheque deposits
– Rescheduling of loans
– Investment in banking products where capital is not guaranteed
– Withdrawals on ATM
– Fraudulent withdrawals over the counter
– Interest rate on fixed deposits

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47.1 The *Economic and Financial Measures (Miscellaneous Provisions) Act 2013* brought amendments to the *Banking Act 2004* for the protection of consumers of financial services. The new legal provisions have capped at 2 per cent the amount of penal interest rate that can be charged by financial institutions on a loan or credit facility granted in Mauritius currency to an individual on or after 1 January 2014. For borrowers who find themselves in difficulty, provision has also been made for the contractual rate of interest to cease to apply and for interest rate at the KRR to apply subject to certain conditions. I welcome these amendments to the law.

47.2 I hope to share the work of the *Task Force on Unfair Terms and Conditions in Banking and Related Financial Contracts* with the public in the course of this year which should pave the way for a better deal for users of banking and financial services.

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48.1 ***Exchange of information among regulators.*** Supervisory colleges have evolved the world over as an important component of effective supervisory oversight of an international banking group. They assist in reducing supervisory overlap and filling in the gaps for better supervisory co-operation. The revised *Core Principles for Effective Banking Supervision* include the enhanced *Core Principle on Home-Host Relationships*. This requires the home supervisor to establish bank-specific supervisory colleges for banking groups. The Bank has endorsed this principle from the Basel banking-standards setter and has set up a Supervisory College for the two largest local banks which have established either subsidiaries or branches in several overseas jurisdictions. The initiative aims at dealing with supervisory issues and establishing a co-operation mechanism for cross-border supervision of these institutions. Each college comprises home and host supervisors of the Mauritius Commercial Bank and the State Bank of Mauritius on the African Continent and in the Indian Ocean Region. This has offered an excellent opportunity for the supervisors, as well as the banks themselves, to share information that will help the Bank in the conduct of consolidated supervision. Participants have expressed interest for the supervisory colleges to be held on a regular basis.

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52.1 ***Islamic banking.*** Since joining the Bank in 2007, I have taken a number of initiatives to promote the development of Islamic finance in Mauritius. These include a legislative and regulatory framework for the conduct of Islamic banking in Mauritius. In November 2007, the Bank was admitted as an Associate Member of the IFSB and was subsequently upgraded to full membership in September 2009. Such adherence of the Bank to international organizations conveys the commitment of the Mauritian authorities towards the implementation of comprehensive Islamic financial services industry in our country. The IFSB Summit brings together a wide range of interested partners. This includes Governors and deputy governors of member central banks, senior officials from supervisory and regulatory bodies and other stakeholders of the Islamic financial services industry, representatives from international institutions, industry experts and academia participating as speakers at meetings and other events.

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53.1 ***Polymer banknotes.*** The Prime Minister of the Republic of Mauritius was the Guest of Honour at the ceremony for the launch of the new polymer banknotes. After a video clip was shown on the history of banknotes in Mauritius, the new polymer notes were launched. The Chief Executive of *De La Rue* (printer of the new Rs25 and Rs50 banknotes) and the Representative of *Oberthur Fiduciaire* (printer of the new Rs500 banknotes) presented mementos to the Prime Minister.

53.2 The polymer notes of Rs25, Rs50 and Rs500 denominations have innovative security features designed exclusively for the polymer material. The polymer notes last longer than paper banknotes thereby reducing processing, replacement costs and environmental impact. The polymer banknotes are now in circulation alongside the paper banknotes. Following the issue of polymer banknotes on 22 August 2013, a total value of Rs761.8 million was in circulation by 31 December 2013. (This was made up of Rs82.2 million worth of the Rs25 notes; Rs100.2 million worth of the Rs50 notes; and Rs579.4 million worth of the Rs500 notes.)

53.3 The *Bank of Mauritius Act 2004* was amended in December 2013 and a new section 43A entitled “Reproduction of currency notes, bank notes or coins” was added. It is now an offence for any person, without the written permission of the Bank, to use, in any size, scale or colour, any photograph of, or any drawing or design resembling, any Mauritius currency note, bank note or coin in any advertisement or on any merchandise or product which that person manufactures, sells, circulates or otherwise distributes.

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55.1 ***Payments system.*** I have personally ensured that our payments infrastructure is modern, resilient and stable. In 2007, as part of a major re-structuring exercise, I set up a new division to look exclusively into payments system matters. Since then several new payment schemes have been introduced and existing ones are being constantly revisited and improved. In 2013 we took new initiatives to further improve the payments system.

55.2 The NPS will be a central infrastructure for routing all electronic-based payment transactions from cards, Automated Teller Machines (ATM’s), Point-of-Sale (POS) terminals, and mobile devices for local clearing and settlement. Current electronic-based payments, even for local transactions, mostly use international networks and are very costly for both merchants and consumers. The NPS has the potential to provide value-added services such as pre-paid cards, e-payment gateways and mobile payments. It should not be viewed as a replacement for card-based transactions as many people believe, but rather, as a public good to help the Bank achieve its statutory goals of maintaining financial stability, create new opportunities and provide a level playing field to all banks.

55.3 The Bank has put much emphasis on designing and being part of an integrated African regional payment system. We have pursued this objective through our presence in two main regional blocks, namely, the Southern African Development Community (SADC) and the Common Market for Eastern and Southern Africa (COMESA). Besides being a settlement bank, we also host the platform for the *Regional Payment and Settlement System* (REPSS) which is a cross-border payment system for COMESA. The Bank is also an active member of the SADC Payment Systems initiative. During the course of 2013, we have worked towards enhancing the REPSS by providing training and technical support to member-states. The Bank hosted delegations from Malawi and Burundi for on-site training and guidance which then led to Malawi joining Rwanda, Swaziland and Mauritius as active participants in the system. I expect that the system will gain further momentum through the forthcoming participation of Kenya and Egypt.

55.4 In order to further facilitate trade flows between Mauritius and region, the Bank has also taken the decision to join the cross-border payment system of the Common Monetary Area (CMA) countries. The CMA member-states are South Africa, Swaziland, Lesotho and Namibia. As South Africa is not a member of COMESA, participation in this initiative will allow all Rand-based payments to be cleared directly and at a lower cost within the same day. In the longer run, this system will encourage our importers to request their Southern African trade partners to invoice them in Rand rather than US dollars.

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Ponzi schemes. This year I initiated a series of actions to deal with the issues arising from the financial scams known commonly as Ponzi schemes. The recommendations of the RBI assessors ranged from the reinforcement of "Know Your Customer" procedures and due diligence in banks, to the setting up of dedicated cells to gather market intelligence and enhanced coordination among regulators. These recommendations are in line with the restructuring and redefining of our mandate. They reinforce our commitment towards financial literacy, consumer education and fair treatment of consumers, on all of which we had initiated work in early 2012. Among the lessons of the recent financial scam is the need for everyone – both young and old – to acquire a basic knowledge of finance and economics. Such knowledge is necessary for anyone who is faced with managing a household budget, making financial investments, and preparing financially for retirement among others.

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58.1 ***Regional cooperation.*** Another priority for me as Chairman of the AACB is to enlist the support of my colleagues in the Bureau in our joint efforts to improve performance on meeting the convergence criteria set out in the *African Monetary Co-operation Programme*. This is all part of the overall objective of the long-term pursuit of regional and continental monetary union. Despite some positive signs of global economic recovery, we still have to remain vigilant in this region to protect our economies from adverse global shocks. The Bank hosted the meeting of the Working Committee on the Detailed Programme and Budget of the CABS, which was established upon a decision of the *Association of African Central Banks* Assembly of Governors taken at its 37th meeting. The meeting was held in Mauritius from 20 to 22 January 2014 to develop a comprehensive plan and budget as directed by the Governors.

58.2 The Bank hosted the meeting of the SADC Subcommittee of Banking Supervisors from 5 to 7 March 2013.

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61.1 ***Corporate Social Responsibility.*** A Landscape Architect has been appointed for the design of the Bamboo Garden. A Project Management Committee, chaired by the Second Deputy Governor and including representatives of the Bank's employees, oversees the project. The garden will initially have 120 varieties of bamboo, from both local and imported sources. 50 varieties of local species have been collected and propagated at Wooton, not far from the Midlands site, on our behalf by the Agricultural Research and Extension Unit. Additional varieties will be introduced subsequently. In addition to bamboo plants, the project will also include a bamboo museum, an administrative unit, a restaurant and an amphitheatre. The project, which is in line with the *Maurice Ile Durable* concept, is expected to attract local and foreign visitors.

62.1 Young athletes aged 9 to 14 years participated in the 7th Edition of the *Bank of Mauritius Inter Club Youth Championship Competition* held in collaboration with the *Mauritius Athletics Association*. The event, which has become part of the Bank's Corporate Social Responsibility to the nation, and which is in conformity with the Government's policy to democratize sports, has more than surpassed our initial objectives. A number of athletes who have competed in the Bank's Inter Clubs Youth Championships since the maiden edition in 2007 are now representing Mauritius in international tournaments. This year, around 950 athletes, 650 athletes from Mauritius and 300 from Rodrigues participated in the event. The preliminaries in Rodrigues were held on 9 November 2013. During the two-day competition, two records were established:

– Relay Colt 4x50 m – girls in 31.11s established by Jane Brabant, Selena Ramsamy, Laeticia Favory and Anastasia Monique of *Beau Bassin Athletic Club* as compared with the previous record of 32.08s; and

– Pentathlon with 161 points established by Bryan Tonta of *Rose Hill Athletic Club*, improving his own previous record of 155 points.

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64.1 ***Communication with stakeholders.*** Click here at http://www.bom.mu to access the section on "Financial Education" located in the menu of the Bank's website. Information on financial frauds and their prevention is provided in the sub-sections "Types of financial frauds" and "Prevention of financial crime" under the section "Financial Education".

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