Rundheersing Bheenick: Looking beyond vision 2020

Address by Mr Rundheersing Bheenick, Governor of the Bank of Mauritius, at the Annual Dinner in honour of Economic Operators, Pailles, 6 December 2013.

* * *

"*Without … extra resources, the only OMO's that your Central Bank will be able to undertake will be, not Open Market Operations, but Open Mouth Operations – with no money to put where our mouth is!*"

1. Before we begin may I ask you all to rise to pay our respects and tribute to that great leader in this region, Nelson Mandela, who passed away last night and whose character and example in his Long Walk to Freedom have inspired so many in Africa and the world. Nelson Mandela, Madiba, Thank you! Now let me welcome you all here tonight. For I want to bring some cheer to a year marked, once again, by the dismal lingering legacy of the global financial crisis. Tonight, I want us to raise our vision from the immediate past, beyond the immediate horizon, and even beyond ***Vision 2020***, to a longer-term perspective for the country and for its people.

Global revenge on the banksters abroad

2. For banksters abroad, it has been a year of retribution, regulatory condemnation, and multi-billion-dollar penalties: their just deserts! But here, in Mauritius, it has been different. We have suffered no contagion from questionable practices and misdemeanors which had become common currency in the top echelons of global banking and finance. By judicious regulation, by innovative intervention, by much prudent action by our banks themselves − and also, I must say, by a fair bit of luck − we have managed to avoid the calamitous plight of so many hard-hit countries in the world.

3. *The Economist*, examining some of the worst excesses of casino banking abroad, has declared that to politicians – not with us tonight –

> "*banks are both incompetent behemoths waiting for public bailouts and conniving profiteers, pulling a fast one on their customers"*[1]

The Economist might think that… But I could not possibly say so… could I? As we well know, our banks, here, are not too-big-to-fail, and are engagingly customer-friendly, most of the time. And they had better be, as I am pleased to see that the competition is really hotting up. Even as I speak, we have half a dozen different applications for bank licenses pending – a record number for us.

4. Elsewhere, bankers have traded recklessly − with other people's money. They have been guilty of LIBOR rigging. You would have thought that the forex market – the largest and most liquid market in the world, with a daily trading volume of USD 4 trillion – would have been immune to market-rigging. Well, you would have been wrong! Bank forex trading desks fixed that, too. Bankers may yet be found guilty of commodity price rigging as well. They have made whole countries broke from the huge cost of the bank bailouts, spreading misery and devastation. You know, it's almost as if these foreign banksters and traders have taken that Hollywood vamp, Mae West, as their mentor. Remember her quip?

> *"Between two evils, I always pick the one I never tried before."*

5. The jury is still out, as they say, on the punishment for bank fraud. *Business Week,* in November this year, estimated that US banks have paid out USD 93 billion in fines and

---

[1] *The Economist, 27 July 2013*

penalties. The toll is still rising. Early this week, EU antitrust authorities fined eight banks a combined total of USD 2.5 billion for collusion to manipulate benchmark interest rates. Some in the West are now in jail. Four Iranian bank fraudsters copped the death penalty last year. And the *Wall Street Journal* reports that over 450 US banks have failed since 2008.

6. In the UK, Barclays has paid out over USD400 million in fines to US regulators. It also sacrificed its Chairman and Chief Executive. Little wonder, then, that the UK ***Parliamentary Commission on Bank Standards*** proposes to criminalise reckless misconduct in bank management and has recommended that all bankers should be licensed and sign up to standard rules.

7. But I suppose one thing that can be said after all this litany of misdemeanors and malfeasance, is that banking is no longer a boring subject. We have certainly all become more financially-savvy. Who would have thought that grand larceny on a global scale would have had such a favourable impact on financial literacy?

A makeover for the real economy

8. But, tonight, it is not my intention to pillory the banksters abroad. We can safely leave that to the fearsome foreign regulators, the civil courts, and in some cases the criminal courts. Indeed the regulators, exacting such heavy fines, seem to be following the advice Ivana Trump gave to wronged wives:

"Don't get mad: get everything!"

Moving closer home, some believe that a bash like this dinner tonight could not be complete without a dose of bank bashing – I wonder why? Let me assure you there is no such item on the menu tonight! What a sigh of relief I hear from our bankers present here! My subject tonight is the real economy in Mauritius and its future. Does it need a makeover?

Lifting our eyes to the future

9. How well are we doing? Let us step back a little to gain some perspective. Let's measure our progress against the where we thought we would be in our ***Vision 2020*** some fifteen years ago, which I had the privilege to develop with many of you. Many of you, present here tonight, contributed to developing ***Vision 2020***, as we looked ahead to what our country could become in the span of 25 years. Ownership could not have been more widespread. In what was probably a unique feature, ***Vision 2020*** bridged the party-political divide. Conceived and conducted under Prime Minister Sir Anerood Jugnauth – who actually attended a working meeting with his entire Cabinet − it was delivered under the Prime Ministership of Dr Navin Ramgoolam who gave it a ringing endorsement in an enthusiastic preface, commending the final report to the nation.

10. ***Vision 2020*** has remarkable come to pass. Since December 1990, our GDP has grown nine-fold, while GDP *per capita* shot up from Rs37,000 to Rs266,000 − more than seven times. We were spot on when we predicted that tourism and ICT would emerge as major contributors to jobs and incomes. They now account for an average of 8.2% and 6.4% of GDP. In parallel, King Sugar has been dislodged from its pedestal, falling from 10.3% of GDP in 1990 to just 1.6% in 2012. Manufacturing also fell from 23.6% to 16.7%. As anticipated, our economy transformed into a more service-oriented economy, with the weight of the services sector increasing from 57% in 1990 to 73% in 2012. Our openness and readiness to adapt to globalisation pressures to maintain our competitiveness, saw us judiciously combining foreign labour with the domestic labour force. The share of foreign labour in total employment thus increased from 0.2% in 1990 to 4.1% in 2012. Our transformation has been remarkable.

11. I believe that ***Vision 2020*** served as a guiding star for our economic operators and policy-makers as we set out on separate, but convergent, ways to address the succession of

obstacles that we encountered. Obstacles, of course, there will always be. The international environment confronting us today is extremely challenging. Uncertainty has increased. So has competition for market share as countries adjust to the new competitive requirements of global supply chains.

12 As we edge our way out of the still-lingering financial crisis, I believe the time is ripe for us to embark on a new visioning project to look ***Beyond Vision 2020*** to realise the further promise of our potential. Our public-private partnership has gained in maturity. I see no reason why a thriving private sector cannot take the lead in setting our perspective for the future. Don't wait for government. Set up your own think-tank on strategic issues. Let the government be the facilitator of change. I believe that we have now reached a stage of development where we can best flourish with government responding to your strategy, your initiatives, and your vision. This is my call to our private sector partners tonight, re-echoing the call at the launch of ***Vision 2020***, that the private sector should take the lead in future national visioning exercises.

Extending the miracle

13. We might begin by asking how well are we responding to current challenges. A new IMF working paper on Mauritius, tauntingly entitled "*Mauritius: The Drivers of Growth – Can the Past be Extended*"*?*[2] examines our growth record as the economy revved up from an average growth rate of 2.4% in the 1960's to 6% in the 1970's, to then decelerate to 4.4% in the 2000's. It uses the growth-accounting framework to decompose the respective contributions of capital and labour. It dissects the sources of past growth, and projects growth to 2030. It concludes that growth will most likely be in the 3–4% range. It could possibly reach 5% but this can only happen if strong pro-active policies are taken in five areas. First is an increase in investment rates. Second comes an increase in savings rates. Third is labour market reform. Fourth is education reform. And fifth is the need for further reforms to reduce bottlenecks and increase productivity. Except for the much-needed increase in our domestic savings rate, now alarmingly below 15% − or nearly half its historical peak – the measures are of a structural nature and not within the domain of monetary policy. The Bank has long been fighting to normalise interest rates to induce a greater savings effort but much of the time, as you are aware, it has unfortunately been a losing battle.

14. To return to the question put, can the past Mauritian "miracle" – be extended into the future? How are our institutions faring? Are we getting the best from our state-owned enterprises? They command such a large chunk of our national resources that they impact national competitiveness. Are we doing enough bench-marking with the best in the world?

How far are our firms cutting costs, increasing competitiveness, and improving productivity? Embarrassing as some of the answers may be, such questions must be confronted head-on so that "the miracle", if such it is, can be projected for generations to come?

15. The message of the past is adaptation or disaster. In the last two decades, in both commerce and banking, we have been confronted by seeming miracles of technological change. We have had the microchip, the fibre-optic cable, the World Wide Web, satellite media, the smart phone, CCTV systems, videoconferencing, call centres, on-line sales, nano-technology, and so on and on. Some of you have been quick to pick up the kit and adapt it to your needs, but much of the old Mauritius still surrounds us, with a reluctance to change.

---

[2] Svirydzenka K., and M. Petri, "*Mauritius: The Drivers of Growth – Can the Past be Extended?*", IMF Working Paper, October 2013

Innovations in banking

16. In banking, I am pleased to report, we are in the midst of, not merely a spring cleaning, but a veritable banking reformation. It is a reformation that embraces the instant digital process of trade in bills of exchange, letters of credit, and the emergence of a global payments and settlements system. Mobile payments, electronic wallets, and internet banking are here to stay. We are moving into paperless banking and, indeed, to a cashless society. A new digital currency, Bitcoin, made headlines this year, challenging governments' monopoly in the issuance of currency. Which means that even the new polymer notes may go the way of the Dodo. The financial management of commerce and banking is now being transformed in a generation by the very best in the business. But if we are all to be part of this new Mauritian miracle, then we must beware of being left out.

The legacy of the global crisis: central banks taking a hit

17. Even as we ready up to face new threats, the legacy of the global crisis is still very much with us. Many central banks themselves have taken a hit. First, the revenue we derive from our reserves portfolio, which is the only source of revenue for the central bank, came tumbling down. It fell from Rs 2.1 billion in FY 2006/07 to Rs 794 million in FY 2012/2013 as the average annual yield declined from 4.4% to 0.8% over the same years. Second, is the hefty bill that came with the 2012 rescue job which the Bank had to do to protect our inherently vulnerable small economy from the global crisis. Allow me to sketch in the reality and cost of the action we had to take to prop up the economy and maintain financial stability in Mauritius.

18 The rupee was getting out of line with our economic fundamentals, gradually becoming overvalued, and beginning to affect trade. We had no option but to step up our intervention on the forex market to combat currency appreciation. We had very limited firepower – a fact not obvious at the time to some policy-makers who were inclined to believe that the Bank could just print all the rupees required to buy up the flow of foreign currencies. The constraint came from the other leg of the operation. To prevent the disruptive effects of the flood of rupee liquidity on financial and banking sector stability, the Bank had to buy up the rupees by issuing its own instruments. The cost of these instruments was a multiple of the yield on the currencies purchased. By way of example, let us take US dollars: reserves in this currency yielded 0.3% on average in 2012. The average cost incurred by the Bank to sterilise the proceeds of forex purchases stood at 3.4% in the same year – that is ten times higher.

19. Central Bank losses were expected and very much at the heart of our initial reluctance to intervene. We had support from the IMF who recommended that the cost of the process of sterilisation should be borne by the fiscal authorities up front, without waiting to recapitalise the central bank after it has incurred the losses. It was on that understanding, that we issued more than twice the volume of Bank securities than our normal level. That was indeed more than ten times our capital holdings. Our 2012 rescue job on the currency front cost us nearly Rs20 billion in Bank paper – that is ten times our capital. But it seems to be working although we are not yet out of the woods.

ORR to the rescue

20. Our rapid response, with the Operation Reserves Reconstitution, halted and reversed the appreciation of the rupee, kept the export machine going and the economy purring along normally. But the Central Bank took quite a hit. And I must emphasise tonight that neither the pace nor the level of the ORR-style intervention can be sustained by the Bank on its own resources.

The fiscal expectations of the monetary agent

21. We were, of course, not alone in being forced to play such an active interventionist role – and in paying for the consequences. Brazil protested that a "currency war" had been declared surreptitiously. It slapped taxes on inward capital flows. The Swiss central bank almost lost its shirt in trying, successfully, to contain appreciation of its currency, much to the displeasure of its cantonal shareholders. Last month, the Australian government made a massive capital transfer to the Reserve Bank of Australia to allow it to sustain its Open Market Operations. India suffered a severe bout of rupee depreciation, together with capital outflows. Zimbabwe has just taken over the debts of its central bank – but that is another story.

22. When "tapering" begins in earnest, the world will have to confront the new challenge of returning to a "normal" monetary policy. It's a safe bet that still more currency volatility will follow, and even more vigorous action will be necessary to stabilise the affected currencies. But central bank balance sheets cannot keep taking hits like this. They cannot continue to rescue private sector balance sheets, prop up the economy, but go under themselves, with unsustainable losses. Central banks need to have up some extra cards their sleeve.

23. Topmost among these, I would place additional capitalisation, or resourcing, of central banks, as in Australia, without waiting for them to actually make losses first, as is the norm in central bank legislation. Dynamic provisioning, which flies in the face of accounting practice, is equally important. This would allow us to carry on the battle against currency volatility, conduct Open Market Operations, or OMO's, in the low-yield environment. Without these extra resources, the only OMO's that your Central Bank will be able to undertake will be, not Open Market Operations, but Open Mouth Operations – with no money to put where our mouth is!

24. As I reflect on the timing of "tapering", an astute observation of a former Chairman of the US Federal Reserve, William McChesney Martin (Jr), comes to mind:

> *"The job of the FED is to take away the punch bowl just as the party is getting going."*

I suspect that the macroprudential measures, that we introduced recently, to minimise the risk of overheating in the construction sector, must have evoked similar sentiments in the industry. The Bank is now seen as the killjoy, preventing enthusiastic promoters from turning the whole country into a gigantic building site. Where they see only benefits, the Bank sees Risk, with a capital R.

Igniting the new engines of growth

25. But let us not end on a dismal note for my hopes are high for a steady recovery. I believe Mauritius can move into the premier league of small states, and become one of the Tigers of tomorrow's commerce, by igniting new engines of growth.

26. Writing, in the 1940's, William Henry Beveridge, social reformer *extraordinaire,* defined the road to progress as the elimination of the five giants, of ***want, disease, ignorance, squalor and idleness.*** We have done much in Mauritius to eliminate want, disease, and squalor. We still have much work ahead to tackle more vigorously the giants of ***ignorance*** and ***idleness***. We absolutely must increase savings; reform the public sector and make it more a servant than a master of the people; engage women more in our society, in our businesses and indeed in our banks; extract greater efficiency in education and health; and develop greater productivity and innovation in our economy.

27. I believe we shall see the drivers of growth sustained but we must do more, much more, to ignite innovation in business and in Mauritian society at large. The Mauritian miracle is not just a thing of the past. But it requires a new spirit of adventure to match our talents to the opportunities of the cyber age. We must overcome the new threats through a concerted

pursuit of macro-economic and macro-prudential policy. Only then can we secure economic and financial stability and growth with equity.

The keys to our future prosperity

28. The keys to the future are increased personal and corporate accountability and multi-sector collaboration. We need the private sector to take a lead role. We need more stimulation and nurturing of new start-ups. We need to challenge the monopolies of the past. We need a slimmer, more effective and efficient public sector, which is seriously in need of reform. Some task there! For it has been well said:

> *"Reorganising the civil service is like drawing a knife through a bowl of marbles."*

29. But in racing ahead on this path, holding forth the torch of new technology, we must face up to the many risks of the cyber age. And in this, I am pleased to see, many of our brightest bankers are taking a lead. For, above all we need the continuing positive role of our highly competitive banking sector in an even closer and more effective working relationship with the real economy. And we need more inclusive management in the public and the private sector. Here I'm reminded of the story of that great British military leader, the Duke of Wellington, who vanquished Napoleon at the battle of Waterloo in 1815. Later he became Prime Minister and found government to be a harder nut to crack. After his first Cabinet meeting, he was heard to remark:

> *"I gave them my orders, and then, damn it, they just sat down and started to discuss them all!"*

Hats off to our local bankers

30. So, let's now take our hats off to our local bankers! They have never been part of casino banking. And they have a long history of serving the nation through their customers. As a central bank we are proud of our 46-year history: just imagine how much more so must be *les grandes dames de la Place d'Armes!.* MCB inaugurated here in 1838; HSBC in 1916; and Barclays in 1919. That is a span of over 175 years, with decades and decades of experience and skill, serving the people of this country. The State Bank of Mauritius − which as many may not be aware, was actually promoted by the Bank of Mauritius just after the country's independence − is an upstart by comparison. And a very successful one, too. The brilliant new stars on the banking scene are keeping our established bankers all on their toes. I say to our bankers here tonight, Hats off to you all.

The fundamental laws of the unproductive state

31. Finally, as is my wont on these occasions, may I leave you with two laws which may possibly inspire us in the pursuit of a second Mauritian miracle. In the past you have been served: Maradona's law of interest rates, Einstein's law of success, and Newton's law on physical response, amongst others. For your delectation, I even rolled out Sutton's law, named after a bank robber where he explained why he robbed banks.

32. In the same vein, I now turn to Parkinson – no, I am not referring to the Parkinson who gave his name to a debilitating disease which figures high on the risk map of humans in advancing years. I am invoking another Parkinson, Cyril Northcote Parkinson, who turned his attention to an equally-debilitating disease affecting, not persons, but institutions and corporates. ***Parkinson's Law of Triviality*** may strike home for some *habitués* of board rooms. It states that:

> *The time spent by a committee on any item on the Agenda will be in inverse proportion to the sum of the money involved.*

33. This is where a trivial item, like the allocation of parking spaces, or the colour of new uniforms for staff, dominates discussion at the Board. This leaves no time to review strategic items such as a multibillion capital scheme. The big issue is then waved through on the nod. Members of the Board have exhausted themselves over the triviality and realise they must now break off for lunch!

34. Now, as we approach a festive season, when traders vie with one another with sales gimmicks, I thought I should do the same with our *persiflage*. May I therefore offer you two laws for the price of one? I am coupling the Law of Triviality with ***Parkinson's Law of the Organisational Pyramid***. It states that:

> *The number of subordinates in any organisation will increase linearly by 5% a year, regardless of the amount of work to be done.*
>
> We might call this the middle age spread of the middle income trap!

35. Finally, as I leave you ruminate over Parkinson's Laws, I shall conclude, that such ineffable laws stand as warnings to us all. But if we can escape their pernicious embrace, I believe, our long-term future can be just as miraculous as our past. To achieve this, we must work together. We must put aside trivialities. And, above all, we must give strategic thinking and visioneering, priority on the national Agenda of economic operators and political decision-makers. It is high time to look beyond ***Vision 2020***.