Ahmed Naseer: The role of institutional investors in long-term financing for growth and development

Keynote speech by Mr Ahmed Naseer, Governor of the Maldives Monetary Authority, at The Maldives Finance Forum 2018 "The role of institutional investors in long-term financing for growth and development", Malé, 22 May 2018.

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Chairman of the Maldives Pension Administration Office Board (MPAO), Mr. Ibrahim Nasir, CEO of MPAO, Mr. Mohamed Hussain Maniku, CEO of STELCO, Mr. Ahmed Zuhoor, Auditor General, Mr. Hassan Ziyath, senior officials of the MMA and financial institutions, distinguished delegates.

Assalaamu Alaikum, and good morning.

It is a great honour and privilege to be here at the 7th Maldives Finance Forum as the keynote speaker. I sincerely thank the Maldives Pension Administration Office for giving me this opportunity.

The Maldives Finance Forum initiative of MPAO has become one of the keystone financial sector related events to be held in the Maldives a regular frequency. The Forum provides a platform for key players in the financial sector to come together and discuss about pressing topics and issues in our economy, which is something that we need more of. This year's Forum is on the theme: "The role of institutional investors in long-term financing for growth and development", which I believe is of central importance to us at this point in time.

We have excellent speakers and presentations lined up throughout the day focused specifically on the theme of the forum. So, my plan is to tackle a more diverse set of areas, all of which are, in my opinion, important issues that we need to think about and address.

I will start off with a macroeconomic overview of the Maldivian economy, followed by some highlights of the recent economic developments in the global arena.

The tourism sector of the Maldives has performed remarkably well during the past few months. In fact, we just had the best peak season of the past 5 years. Tourist arrivals grew 18% year-on-year from December 2017 to March 2018, while tourist bednights grew 19% during the same period. Inflation has generally been low during the past few years, but picked up in 2017 due to the impact of policy measures such as increases in the tariffs of selected goods. However, other changes such as the reduction in electricity tariffs and surcharges put down ward pressure on inflation, and CPI inflation is now edging downwards in 2018.

Looking at the external sector, the current account deficit widened significantly from 2016 due to the hike in imports related to the infrastructure projects that are currently ongoing. The deficit stood at 21% of GDP in 2017, and is expected to remain almost at the same level at 20% in 2018. However, due to the strong increase in receipts from the tourism sector and due to the large infrastructure projects gradually wind up, the current account deficit is expected to narrow in the medium term. Net outflows from foreign exchange reserves persist, but reserve levels remain stable due to short term reserve management activities and large inflows from public debt issuances. As such, gross international reserves are expected to be at US$728 million at the end of 2018. On account of the strong performance by the tourism and construction sectors, GDP is expected to grow at around 6% during the year.

Looking at developments in the global economy, economic activity is picking up in both the advanced and emerging economies. Emerging Asia is expected to maintain its high growth rate at current levels in 2018. This is mainly because the impact of an acceleration in the Indian economy is expected to be offset by a slight slowdown in the growth in the Chinese economy in

2018. The slowdown in the Chinese economy, which is the largest tourism source market for us, could pose risks for us in the form of lower tourist arrivals and spending. Global consumer prices are expected to pick up further in 2018, which is somewhat in contrast to the conditions here in the Maldivian economy. This is because current developments in inflation in our domestic economy is being driven primarily by policy related factors.

This is a time where global attention on international trade has increased, with talks of a trade war between the US and China at the forefront. Being a highly import dependent country, we need to be aware and keep on top of these developments. Any such event can have major implications for our competitiveness and terms of trade positions, especially with the sizable share China accounts as an inbound tourism market and import source market.

From here on, I intend to talk about 3 issues that I believe are of key importance to us at this point in time. The first of these issues is fund management practices and the need to streamline the practices currently being followed.

Despite the small size of the Maldivian economy, we currently have 3 professionally managed funds being administered. Two are being managed by the Maldives Monetary Authority, one being the official foreign exchange reserves which in a loose sense is also a type of managed pool of assets, and the other being the Sovereign Development Fund (SDF) of the government. The other fund in the Maldives is the pension fund administered by the Maldives Pension Administration Office.

Diversification and investment abroad is important, which can help to overcome business cycle downturns. These pools of funds can also ensure our capacity to meet our foreign currency obligation even in times of economic distress. Monitoring and analyzing economic market conditions, both foreign and domestic, therefore becomes essential, and is something that needs to be integrated into our work to a greater extent.

Considering the infancy of our established funds and our existing institutional framework, the fund management practices currently being followed work relatively well. However, there is always room for further development. Identifying globally accepted frameworks and customizing them to our context is often the most straightforward way to achieve this. In this regard, the existing gold standard for fund management is the Generally Accepted Principles and Practices for Sovereign Wealth Funds, which is more commonly known as the Santiago Principles. The Principles consist of 24 practices that have also been endorsed by the International Monetary Fund, and the major themes addressed are transparency and the clear identification of the fund’s objectives.

All these practices are subject to domestic laws and regulations in that specific jurisdiction, which makes the Santiago Principles more of a best practice guide rather than a hard and fast rulebook. The flexibility this allows can guide the development of tailor made fund management principles that are specific to an individual country’s or fund’s context. Therefore, I urge current fund managers and relevant stakeholders to work together to bring some degree of harmonization, both between the fund management practices and policies of our respective institutions and between ours and the globally accepted standards. Well managed funds have the potential of minimizing the impact of business cycle downturns and can increase the resilience of our economy to shocks, both external and domestic. For this reason, wealth funds have to become key players in our economy, and it is my hope that a well-functioning Sovereign Wealth Fund will be established in the Maldives in the near future.

I now turn to a pressing issue that we need to address today to prevent future distress on public finances and the macroeconomy, which is the retirement pension scheme framework. The Maldives Retirement Pension Scheme is an essential mechanism intended to provide a basic income for all retirees without the state bearing the entire burden. According to the statistics of MPAO, the current stock value of the pension fund is MVR10.6 billion. The monthly active contribution per active contributor is MVR 654, while the average value of retirement savings accumulated per member is MVR77,058.

Looking at the population dynamics of the Maldives, we have a disproportionately large share of the population in the youth age bracket. While we can enjoy the benefits of a large youth population today, this also implies that within 35 to 40 years, this group of people will become retirees and the payouts from the pension fund will increase dramatically. Also, we have made remarkable progress over the years with regard to life expectancy. The life expectancy at birth in 2016 was 77 years, which is contrast to just 49 years in 1976. This means that the average Maldivian lives 12 years beyond retirement. Aligning this figure with the retirement pension savings of approximately MVR77,000 translates to just over MVR500 per month during post-retirement years. Once inflation is accounted for, the future value of the payouts will be lower still. Therefore, if the status quo is maintained, we will have an ageing population expected to live increasingly longer, and the bulk of the social welfare burden will still be on the government. There are issues that this poses that we need to start addressing now in order to prevent future economic and social issues. We need to reap demographic dividends of the large youth population now in order to mitigate this.

After touching on the potential for rising government expenditure, I would like to briefly talk about how we are financing that expenditure, especially in times when large scale infrastructure development projects are ongoing. The right mix between alternative sources of financing is important. Exclusive reliance on debt could be problematic for a country like the Maldives, especially in the medium to long term when the repayments fall due. Also, debt denominated in foreign currency brings along the additional issue of foreign currency convertibility for repayment. There is also a revaluation risk should there be any changes to the value of Maldivian rufiyaa. The Sovereign Development Fund, which is intended to be a sinking fund to ensure our capacity to meet future foreign currency obligations incurred to execute public sector development projects, is a good initiative to mitigate the risk. However, the underlying issue of rising debt levels remain unresolved. Therefore, striking the right balance between alternative means of financing is essential. Attracting foreign direct investment is one avenue through which we can continuously achieve development without incurring additional debt. FDI under public-private initiatives should be explored more, as it could present a number of advantages for countries like the Maldives.

Our level of indebtedness, and in particular, the level of public sector debt is something to always be mindful of. We have to evaluate our capacity to repay our obligations before incurring new debt in order to avoid walking into a debt trap. Currently, the economy is performing exceptionally well, and it is during these times that we must take measures to get our financial affairs in order. We have to learn from the experience of other countries and think about what led them to fall into debt traps, and also identify what they did to escape those traps. We are in a position to tackle the issues the economy has been facing for years, and this opportunity should not be missed.

In conclusion, I would like to once again thank the MPAO for giving me the opportunity to speak here today, and applaud their efforts to make such excellent arrangements for the Forum.

Assalaamu Alaikum.