LAUNCH OF THE ABSA AFRICA FINANCIAL MARKETS INDEX

Keynote Address

by

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I am delighted to be able to join you this morning to mark the official launch in Botswana of the ABSA Africa Financial Markets Index. It is even more of a pleasure to give the keynote address in the wake of the news that, in the 2018 update of the Index, the rank of Botswana has moved from third to second among the 20 countries covered in the Index.

Director of Ceremonies, I would like to preface my remarks by observing that, not so long ago, the “Africa rising” narrative was somewhat eclipsed by what one respectable magazine described as the “hopeless continent of Africa”, a label that was later retracted as inaccurate and inappropriate. And rightly so! The fact is that, despite a number of development challenges and pockets of civil strife and political unrest in parts of the continent, Africa has remained largely resilient. This is in the context of an increasingly competitive and interconnected global economy in which both developed and developing countries continue to be challenged by relatively low rates of economic growth, unsustainable levels of public debt, as well as rising trade and socio-political tensions. It is all the more impressive, therefore, that the broader trajectory in Africa is one of progressive entrenchment of the democratic dispensation, adherence to the rule of law, and sound economic reforms, with laudable returns in some cases, in terms of overall economic performance.

According to the 2018 World Investment Report by United Nations Conference on Trade and Development (UNCTAD), since 2010 FDI in Africa has averaged approximately USD 50 billion per annum. That the continent is increasingly regarded as an attractive investment destination is itself part of the new reality. But the on-going transformation of Africa is taking place in a broader new global reality; that is, one of increased economic interconnectedness in which there is a relative shift in the centre of gravity of economic power towards emerging markets. This shift brings with it increased opportunities for a more equitable sharing of the benefits of global wealth and income.

That said, investor interest in Africa remains unduly cautious and heavily focussed on specific sectors, typically commodity-related, in a few countries. The same UNCTAD report indicates that, in 2017, FDI flows into Africa fell by 21 percent compared to the previous year. Thus, there is a need to re-double efforts to not only make investors aware of the myriad opportunities in the continent of Africa but also provide tangible reassurance that levels of idiosyncratic risk are no longer prohibitive.

To this end, as I speak, the inaugural African Investment Forum organised by the African Development Bank has reached its final day nearby in Johannesburg. The event has the explicit aim of moving beyond talking about investment in Africa to providing a setting for moving specific projects towards bankable deals. It is also from this perspective that I welcome the ABSA Africa Financial Markets Index, as a practical tool that supports market development and, by extension, further improvement in the investment environment. But, before sharing some thoughts on the role of financial market indices, let me, very briefly, enunciate the key characteristics of a well-functioning financial sector.

Distinguished Guests, well-functioning financial markets should foster savings mobilisation and investments in a cost-effective manner, channelling surplus funds to their most productive uses, hence contributing to economic growth. They should inspire investor confidence; have breadth and depth in terms of product offerings, as well as liquidity. But more importantly, good governance and accountability structures, buttressed by a sound regulatory framework, good accounting and auditing standards, as well as efficient and independent judiciary are essential to embed public trust and investor confidence.

In this way, developed financial markets facilitate the financial interactions of households, corporations, financial institutions, and governments. Such markets provide a pool of savings that can be tapped into for funding investments by businesses and, also, offer a stable source of funding for governments that can be used to undertake infrastructure development. Furthermore, empirical evidence suggests that countries with well-developed financial markets gain significantly from increased FDI. Of equal importance, studies concur that a developed financial sector can also create opportunities for financial inclusion, especially embracing SMMEs and the undeserved segments of the population. In turn, this supports economic diversification, enables economic agents to pool and offset risks, and encourages savings and wealth creation, thereby contributing to inclusive growth and improved living standards.

Various indicators or sets of indicators have been used to measure financial development. The World Bank has developed a comprehensive conceptual framework to capture the multifaceted nature of the modern financial system. The framework has four dimensions that reflect the essential characteristics of a good and well-functioning financial system that is: depth, access, efficiency and stability. Staff of the International Monetary Fund (IMF) have built on the World Bank framework by developing indices to measure the level of development of financial institutions and markets in terms of depth, access and efficiency, thus expanding the range of indicators used to assess financial development. These multidimensional indices capture the fact that financial services are provided by multiple financial institutions offering a wide array of products and services.

The Africa Financial Markets Index is a valuable addition to this earlier work, where the ABSA Banking Group has partnered with the Official Monetary and Financial Institutions Forum (OMFIF), an independent think tank for central banking, economic policy and public investment. This is with the explicit objective of providing a toolkit for countries seeking to strengthen their financial markets infrastructure.

The Bank of Botswana was fortunate to be represented at the original launch of the Index in Washington DC during the 2017 Annual meetings of the IMF and World Bank. As already mentioned, the official launch in Botswana comes shortly after the release of the first annual update of the index. This is itself an important event, as it is through such regular updates that progress can be monitored. It is also to be welcomed that the coverage of the index has already increased, from the original 17 countries, to 20 in the 2018 update.

As already explained, the Index ranks the maturity, openness and accessibility of financial markets in Africa based on both qualitative and quantitative criteria, focussing on six fundamental pillars for financial market performance. The 2018 update also pays special attention to policies for enhancing market growth, including financial inclusion and investor education.

Most of the surveyed countries are implementing, or preparing to implement national policy frameworks for financial market development. The Index will, therefore, help provide them with valuable insights and tools to improve the state of their financial infrastructure and markets. As Maria Ramos, Chief Executive of the ABSA Group, has correctly observed, the index facilitates a meaningful debate about the maturity and accessibility of Africa's financial markets, thus helping policymakers, investors, regulators and other market participants to identify the areas and initiatives which will drive the most significant improvements.

In as much as I fully concur with the above observations, I should inject a note of caution at this point. In conducting the meaningful debate that Ms Ramos refers to, we should not just highlight the successes, but give equal weight to areas where more progress needs to be made. In this respect, the report highlights continuing room for improvement in several areas. These include, for many countries, the capacity of domestic investors, which hinders the development of new financial products and markets; and the need for further improvements in market infrastructure and regulatory frameworks.

Similarly, while we should celebrate the improvement in the ranking of Botswana from third to second in the 2018 index, ranked only behind South Africa and ahead of continental heavyweights such as Nigeria, there is no room for complacency. There is considerable work to be done if we are to develop a truly world class financial sector in Botswana. To put this in perspective, while the ABSA Index ranks Botswana second in Africa, in the latest update of the World Economic Forum Global Competitiveness Index, the country's financial sector is ranked only 69th out of 140 countries.

Thus, while the overall score of 65 percent is encouraging, the Index rightly highlights areas where there is considerable scope for further improvement, for example, low levels of interbank foreign exchange trading, very low bond market and equity turnover and limited product diversity. Similar observations were made in the 2017 Bank of Botswana Annual Report Theme Chapter, which focussed on the importance of financial sector development for inclusive and sustainable economic growth.

To some extent, these deficiencies reflect structural factors including the relatively small market size and limited need for government borrowing. But there is also scope for beneficial policy intervention with the relevant sectoral regulators working in partnership with market participants.

At this point, let me once again assure you of the Bank of Botswana's wholehearted commitment to supporting financial sector development in the country. First and foremost, this comes from a relentless and consistent focus on the core mandate of the central bank, namely, maintenance of price stability, thus contributing to broader macroeconomic stability for durable and sustainable growth; second, establishing structures that promote financial stability; and, third, adoption of a regulatory framework that balances prudential requirements with allowing sufficient scope for innovation. And, above all, recognition that "once inflation enters through the door, public confidence and trust in the national currency will escape through the other"!

At the recent sixth Botswana Stock Exchange Opening Bell Ceremony, I provided some details on the specific initiatives that the Bank is undertaking to spur the development of the government bond market and stimulate the interbank market, as well as on-going efforts to modernise both the central bank and banking laws.

It suffices to conclude these remarks by, once more, underscoring the importance of trust, governance and transparency as the bedrock and essential preconditions for a sound and sustainable financial sector. At the heart of any financial system is public trust; regulation can help confer legitimacy on regulated service providers, but the value of this support is quickly eroded if the underlying integrity of governance structures is not well-entrenched.

I do not need to remind you of the details of recent events in Botswana that have severely tested this core principle while, more broadly, in countries such as South Africa and the United Kingdom, the competence and integrity of the accounting profession is once more under intense public scrutiny. To their credit, in each case, the concerned regulators in Botswana have acted without fear or favour in addressing the challenges. The regulatory structure has been tested and not found wanting, and this is gratifying. But poor governance has a corrosive effect that, left unchecked, could undermine public confidence and trust in financial institutions and financial markets, however carefully designed. I trust that, notwithstanding these governance related challenges, Botswana will continue to make progress, cementing its lofty position in the continental rankings.

I thank you for your kind attention, and look forward to the next update of the ABSA Africa Financial Markets Index.