Yandraduth Googoolye: The need to adapt regulatory and supervisory structures to changing technologies and business models

Speech by Mr Yandraduth Googoolye, Governor of the Bank of Mauritius, at the 15th Meeting of the FSB Regional Consultative Group for Sub-Saharan Africa, Port Louis, 2 May 2019.

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Honourable Governors,

Ladies and Gentlemen,

Good afternoon and welcome to this fifteenth meeting of our Regional Consultative Group. It gives me great pleasure to share my thoughts with this august forum whose work serves as inputs for the FSB Plenary.

We must all take pride that the democratic deficit at the level of the participation of developing economies in international discussions has been gradually addressed. The establishment of the different Regional Consultative Groups in 2011 was a step in the right direction. It has enabled our voice to be heard.

The global financial system has undergone positive transformation in the past decades. Improvements in technology, product innovation, market integration, fierce competition, as well as policy and regulatory reforms have resulted in a dynamic and sophisticated financial industry. The pace of development and innovation in the financial industry even surpassed the authorities' ability to adequately regulate and establish suitable oversight mechanisms.

Ladies and gentlemen, I need not reiterate the importance of a stable financial system as a prerequisite for sustainable and inclusive economic development. We are all aware of the causes of the run-up to the global financial crisis and the consequences. We have seen percentage points to economic growth and employment rate being knocked off. Many countries relied on taxpayers' money to bailout distressed financial institutions. Returns to savers are now relatively lower and borrower's access to credit has become more complex.

Standard-setters and regulators need to ensure that the financial industry continues to deliver on its essential services, whilst doing their best to correctly regulate and oversee the financial system. Regulating a financial industry has nothing in common with how other industries are regulated. Failures in the financial industry have devastating consequences on the real economy. Adequate understanding of the financial sector as well as identifying risks and vulnerabilities should therefore be of prime concern to regulators and supervisors.

Financial stability is today one of the most widely discussed themes in economic literature. The relevance of analyses on financial stability stemmed from the late 90s international financial crises. It was reinforced by the financial and economic crisis that unfolded in August 2007. These economic tremors accentuated the need for constant up-to-date and exact snapshots of a given country's financial sector.

We should aim not only at promoting efficiency, but also transparency around operations in the financial system and about participants. In our region, the availability of information on the financial services industry needs to be further broadened, and financial literacy further enhanced. A comprehensive, timely and globally comparative collection and dissemination of information is critical. This will undoubtedly benefit all stakeholders, ranging from industry and markets players to the public at large.

Another element that requires our attention is the proliferation of new investment products. These products are often fairly complex. We must remain vigilant over the operations of non-bank institutions that, in some form, take part in financial intermediation using complex products. This sector may include brokerage firms, investment funds, insurers and other forms of entities. Investment opportunities have also expanded far beyond national borders. While this allows individuals to invest in a broad range of assets and currencies, it also opens the doors to mistakes which can be costly both at the micro and the macro level.

Ladies and gentlemen, knowledge of the financial system constitutes not an option but a must! Indeed, when evaluating the stability of the financial industry, we need to have the resources and information needed to assess the degree to which it is capable of resisting shocks, both external and internal. We need to be confident that we have the tools to identify and mitigate the risks that can potentially trigger financial instability.

At its last meeting, the FSB identified four main priorities for 2019. These are:

- How to address new and emerging vulnerabilities in the financial system;
- How to finalise and operationalise post-crisis reforms;
- How to evaluate the effects of the reforms; and
- How to reinforce outreach to stakeholders.

All of these are of concern to the economies of our region. This meeting comes at an opportune time as we shall be able to discuss these topics and take stock of the latest developments on the global front.

Speaking of development, allow me, ladies and gentlemen, to share with you some of the work that the Government of Mauritius has been doing to shape the future of our country's financial industry. A financial sector blueprint was prepared in 2018. It has identified three strategic pillars as key drivers of the growth of the Mauritian IFC:

- First, cross-border investment;
- Second, cross-border corporate banking and private banking; and
- Third, wealth management.

All of these fall either directly or indirectly under the work programme of the FSB. We will indeed be called upon to ensure that Mauritius adequately mitigates risks and that it remains a well-regulated and properly supervised jurisdiction.

As a small country with a population of nearly 1.3 million, the limited size of the Mauritian domestic market constrains opportunities for banks in the domestic segment. This is what has paved the way for diversification of banks' operations by offering cross-border banking services. As at date, cross-border banking assets of our banks account for 60 per cent of total banking sector assets.

However, cross-border banking entails risks which are not present in domestic banking. These include differences in legal frameworks and political risks. In that regard, the Bank of Mauritius is coming up with a Guideline on Cross Border Lending Risk Management. This guideline will set out a minimum set of standards to which banks wishing to enter into cross-border lending will need to adhere. These requirements will vary depending on the structure of those banks and on whether a banking group already has a presence in the foreign country where lending is being effected.

The identification and assessment of money laundering risks remain one of the overarching priorities of the Bank of Mauritius. This is particularly important in view of the far-reaching implications on the correspondent banking field and reputation of the jurisdiction. At the level of the Bank of Mauritius, we have a zero tolerance approach for breach of guidelines, particularly those relating to anti-money laundering and financing of terrorism.

Mauritius had recently undergone a Mutual Evaluation Exercise under the auspices of the ESAAMLG. Some areas warranting remedial action in the AML/CFT regulatory and supervisory framework had been identified. The country has already taken the necessary corrective steps and addressed many of the shortcomings. The legal framework has been enhanced with relevant amendments to the Banking Act and Bank of Mauritius Act.

We are also upgrading our supervisory and regulatory framework. As from September 2018, the Bank has a full-fledged unit for monitoring AML/CFT risks and conducting on-site examination in institutions. We are also in the process of moving towards a risk-based supervisory approach. A separate module is being developed to capture AML/CFT risks. The Bank has also signed a tripartite memorandum of understanding with the Financial Services Commission and the Financial Intelligence Unit to enhance, among others, the effectiveness of the implementation of AML/CFT measures.

Once the risk-based supervisory framework becomes fully operational, banks posing higher risks to the system will be subject to more intensive supervision. We have also introduced a framework for Domestic–Systemically Important Banks since July 2014. All banks which have been identified as being systemically important are required to hold a capital surcharge in the range of 1% to 2.5%.

Mauritius, as a highly open economy, has a few large corporates that dominate economic activity. These corporates require a close monitoring. A large exposure limit is in place to curtail the exposure of any borrower or group of borrowers. The basis for computing the large exposure limit was recently enhanced from capital base to Tier 1 capital. Further, in our framework for Domestic–Systemically Important Banks, exposure to large groups is a supplementary indicator. These large groups have been defined as having an exposure of at least Rs2 billion to the banking sector.

Another topic that warrants attention is climate change and the reduction of global carbon emissions. The financial services industry has an important role to play in that area. I know that some central banks are already at an advanced stage in their work and that much work has already been done on that subject at the level of the FSB. In Sub-Saharan Africa, central banks have not focused extensively on climate change. We are eager to know more about the work that has been carried out by the FSB. Climate change related measures could also, perhaps, be on the agenda for future meetings.

An area on which we must also focus is that of the application of technology in finance. The emergence of FinTech represents an opportunity for Africa. Advances in areas of finance-related technology, such as blockchain, mobile payments and Artificial Intelligence are opening up new possibilities for financial service firms. This is an area where regional cooperation will be of paramount importance. The setting up of the FinTech Association will give the impetus to position Mauritius as a Regional Hub for that industry.

Ladies and gentlemen, our common ambition is to transform Africa into an innovative and technologically-enabled continent. However, as regulators, we have an important role to play in fostering innovation. It is our responsibility to ensure that banks operate safely and comply with applicable laws. This is why we must ensure that our regulatory and supervisory structures remain effective by constantly adapting them to changing technologies and business models.

Since 2017, banks are allowed to have recourse to cloud-based services subject to the fulfilment of certain conditions. Our approach is one of open-mindedness. We indeed welcome change by banks. But this change is welcome so long as banks are able to demonstrate that risks are being appropriately and adequately managed. Our staff will make a presentation on cloud-based services in this meeting. I look forward to some stimulating debates for our common benefit.

Ladies and Gentlemen, I am convinced that our agenda will stimulate exciting and constructive discussions. The presence of our partners from the IMF, World Bank and the FSB can only enrich the debate.

Let me end by quoting Timothy Geithner, the 75th US Secretary of the Treasury who served under President Barack Obama. I quote: "***Looking past the immediate crisis, a more resilient system must be built on stronger and better designed shock absorbers, both in the major institutions and in the infrastructure of the financial system***". Unquote.

Ladies and gentlemen, this is for what we must ultimately aim.

Along these lines, I wish all of you a pleasant stay in Mauritius and fruitful deliberations over these two days. I invite those of you who have some spare time to experience the beauty of our island.

Thank you.