BOTSWANA STOCK EXCHANGE – A PLATFORM FOR ECONOMIC GROWTH AND DIVERSIFICATION

Closing Remarks

by

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March 8, 2018

Salutations,

I am cognisant of the fact that you have had a productive and busy day, and some of our guests may have the desire to explore the nightlife of our small, but vibrant City of Gaborone.

On behalf of the Botswana Stock Exchange, Delegates to this Conference and the Organising Committee and indeed on my own behalf, let me start by expressing our sincere gratitude to His Honour, the Vice President, Mr Mokgweetsi Masisi, for gracing this Conference and for the excellent and enriching Keynote Address. We thank you, Your Honour. Honourable Minister Matambo, thank you too, for your continuing encouragement and support, as well as for gracing this occasion with your presence.

We are also most grateful to the various Guest Speakers Moderators, Panelists and Resource Persons for the insightful contributions and the generous sharing of your knowledge and perspectives on this important Conference on the BSE as a Platform for Economic Growth and Diversification. The Chairman of the BSE Main Committee, Lieutenant General Tebogo Masire and Chief Executive, Mr Thapelo Tsheole, as well as your members and the staff, I wish to commend you for organising this Conference; this is indeed timely, relevant and a pertinent subject, particularly at a time when, in many respects, Botswana's economy is, arguably, at a crossroad.

To borrow from the introduction to the Financial Sector Development Strategy of 2012 - 2016, and I quote: "the economy has for many years been driven by mineral-led growth and remains dominated by the mining sector, particularly diamond mining. However, the end of the diamond-led growth is within sight. The Government of Botswana is undertaking ongoing efforts towards diversifying the economy and stimulating alternative engines of growth, including promotion of a services-led economy", close quote. In this respect, the role of the financial sector, including the BSE, in implementing the diversification strategy, is indeed very critical.

To offer another perspective, last year, in affirming Botswana's Sovereign Credit Rating of A2, with a stable outlook, Moody's Investors Service cited "progress with diamond beneficiation and economic diversification, combined with efficiency-enhancing public sector reforms as factors that could exert positive pressure on the rating over the medium term. In addition, private sector development leading to reduction in unemployment would also apply upward pressures on Botswana's creditworthiness. Moody's further indicated that slow progress on structural reforms and economic diversification could exert downward pressure on the government's fiscal position and the rating over the medium term, which could lead to a downgrade. In the near term, expansionary fiscal policies leading to a marked reduction of fiscal reserves and/or rapid debt accumulation would also put downward pressure on the rating". Therefore, the development agenda is clear to us all and the issues that you have, I believe, ably dealt with in this Conference resonates very well with the country's National Development Plans and Vision 2036.

Your Honour, the Vice President, Distinguished Delegates, it is not my intention to comment on all the issues that have been discussed today. Suffice to say, the wide-ranging agenda has touched on a host of issues that are fundamental to the success of enabling the BSE to serve as an effective platform for economic growth and diversification. In turn, this can be viewed as part of the wider challenge of making finance work for Africa. Empirical research has repeatedly indicated a positive correlation between financial sector development, economic growth and poverty reduction. Regrettably, however, the financial systems in most African countries remain small, fragmented and not well diversified, providing only a limited number of services and, evidently, at relatively high cost. Equally, while Botswana's financial sector is comparable in size to other countries in the region, it remains relatively smaller and less developed compared to that of its upper middle-income peers.

Director of Ceremonies, allow me, therefore to comment very briefly on five topics: <u>first</u>, the public perception of stock exchanges and the resulting need for effective outreach and public education; <u>second</u>, how a stock exchange fits into the financial sector more broadly; <u>third</u>, the need to develop an active market in Government securities in support of more general financial market development; <u>fourth</u>, the importance of macroeconomic stability for sustainable development; and, finally, the impact of developments in financial technology (the so-called FinTechs).

Stock Exchanges – the Public Perception

I very much doubt if many, or even any, of those attending this Conference have a negative view of the role of stock exchanges. I, too, am fully aligned with this positive perspective and, in this regard note, with some satisfaction, that 2017 was a record year for the BSE, with nearly 15 000 transactions at a total value of P2.5 billion. In recent years, the Exchange has continued to broaden its coverage away from the financial and mining sectors to include, among others, listing of property and retail firms.

That said, the scope of the BSE remains generally small and shallow. Some economic sectors are not represented among the listings; domestic market capitalisation is only about 25 percent of GDP; compared to an average of about 60 percent for middle income peers and well over 100 percent for high-income countries; while trading volumes and liquidity, although improving, remains relatively low.

But, among the wider public, you do not have to look far to find those who are critical, or at least mistrustful, of the role played by stock exchanges. This includes highly critical analysis from influential opinion formers. For example, the great economist John Maynard Keynes held a very dim view, opining that:

> “When the capital development of a country becomes a by-product of the activities of a casino, the job is likely to be ill-done”.

Keynes was, of course, writing before the idea of “rational expectations” and “efficient markets” gained credence, buttressing the case that stock exchanges play a useful role in financial intermediation. But the notion of irrational markets persists, notably in the view that stock markets encourage a “short-term” approach among listed companies, driven more by the need to boost quarterly earnings and annual dividends than planning productive long-term investment. This is commonly regarded as a major weakness of the “Anglo-Saxon” model of capitalism.

And such analysis readily strikes a chord with popular opinion, especially in the wake of the global financial crisis for which the activities of “speculators”, along with “animal spirits” were widely held responsible.

In media coverage, market movements are routinely described in pejorative terms such as “bubbles”, “crashes” and “mayhem”; the popularity of the movie “The Wolf of Wall Street” and various books with similarly sinister titles, also speaks to this sentiment. Only recently, in the early weeks of 2018, we were, once more, reminded of the potential for excessive market volatility, as renewed fears of inflation, especially in the USA sparked record-breaking single-day losses on Wall Street, followed by almost equally large rebounds. I suspect that many of you, with smartphones, are following these events as I speak!

In this environment, conducting effective public image building for a stock exchange can clearly be a hard sell! In Botswana, we are fortunate that discussions of the BSE have not sunk to this level. Public dissatisfaction with some financial institutions, especially with respect to what might be categorised as inappropriate market conduct, is directed mainly to other segments of the financial sector. But as the BSE continues to broaden its role in the economy and, inevitably, moves more into the public eye, it should be prepared for the negative aspects of this success. Therefore, in addition to the very commendable effort by the BSE, on the implementation of market development, notably through public education campaigns on both the supply and demand side, as well as motivating companies to list and issue bonds, consumer protection should not be overlooked. To be forewarned is to be forearmed.

Stock Exchanges and the Financial Sector

One way forward, in countering this sentiment of distrust by the public, is to focus on the role of a stock exchange, not in isolation, but as one strand in the full spectrum of financial institutions, where the whole is greater than the sum of the parts. As we are all aware, broad, liquid and efficient capital markets play a central role in channelling savings to the long-term investment needs of the economy. Many of you in this room will readily agree that "trust" is the basic foundation of markets; without trust, financial intermediation collapses.

From this broader perspective, a stock exchange is an important vehicle for raising corporate finance. By the way, this equally applies to privatisation of some parastatal organisations, which, if properly designed and implemented, could also benefit from domestic sources of long-term finance and other credit markets. That is why events, such as today's Listings and Investment Conference, can play an important role. But it is not the only option, and there are many instances where seeking a listing may not be the best choice. Financial institutions can be fierce competitors, but also complementary in many respects. Maintaining the appropriate balance between competition and cooperation, including through up-to-date legislation and institutional support, is, of course, a key function of the sectoral regulators.

Developing Markets in Government Securities

In Botswana, the absence of a vibrant market in government securities and the paucity of supply of fixed income instruments generally provide a particular challenge in the development of a broad-based and robust financial sector.

The fiscal prudence and cautious approach of Government to accumulating additional domestic debt is entirely understandable. Indeed, the Bank of Botswana is highly supportive of this prudent approach. However, with the share of public domestic debt standing at only about 7 percent of GDP, the shortage of high-quality, risk-free assets clearly has a negative impact on financial sector development, further encouraging the “buy and hold” behaviour prevalent among domestic investors. As a rough guideline, relevant benchmarks suggest that a ratio of government domestic debt to GDP, of at least 15 percent, is required for the necessary critical mass.

The Bank of Botswana is the Government’s agent for issuing such debt and, in this capacity, will continue to seek ways to achieve the necessary measured expansion of government domestic debt, within the parameters of the current fiscal rules, fiscal discipline and current ceiling on the domestic note issuance programme of P15 billion. Furthermore, the Bank will remain supportive of additional impetus, such as the recent launch of a Pula-denominated bond by the International Finance Corporation (a member of the World Bank Group) and other highly reputable issuers, to increase the supply of high-quality securities in the domestic market.

The Bank of Botswana is also supportive of the initiative to enhance market infrastructure through the establishment of a single Central Securities Depository, which, among other things, will allow for the trading of government bonds on the BSE and settlement of all securities directly in central bank money. This is in recognition that such a development should encourage secondary market activity, reduce settlement risk and, in general, enhance efficiency. However, for these benefits to be realised, it is crucial that this is a product of meticulous planning and execution to ensure that the existing levels of efficiency experienced in the current Over-the-Counter market, overseen by the Bank of Botswana, are fully replicated.

The Importance of Macroeconomic Stability

It is barely a week since the launch of the 2018 Monetary Policy Statement and I have little to add on that front, save to underscore the importance that we place on effective communication regarding the Bank's policy intentions. During 2018, further reforms will include the publication of a quarterly "Monetary Policy Report" to provide more detailed background analysis. I hope that the public, market analysts and financial journalism in particular, will make good use of this Report; the Bank of Botswana will continue to enhance communication to reduce any policy uncertainty or, rather promote policy predictability.

I should also remind you that the issue of price stability is fundamental to the long-term safety and soundness of the financial sector. Price volatility is just as disruptive to effective financial intermediation as it is to the economy more widely; a booming equity market fueled by inflation is inherently unstable. In this regard, the maintenance of inflation within the medium-term objective range of 3 - 6 percent, for an extended period since mid-2013, is a major achievement of this economy.

The Impact of FinTech on Sustainable Economic Growth

Last but certainly by no means least, is the impact of FinTech on sustainable economic growth. Indeed, it is of such central importance that it should be a standard agenda item for events such as this one. Appropriately, at the start of today's agenda, there was a presentation by Mr Brian Armstrong on the Future of the World. Here, to add my voice, I am of the view that technology and digitalisation serve as the backbone of the future of banking and finance and we should be prepared for all eventualities. Take the much-talked about Distributed Ledger Technology (DLT), for example: surely the very concept of DLT or block chain poses a challenge to the operation of centralised exchanges and securities depositories, that is the basic business model for the BSE.

Even now, the way stock exchanges operate is being revolutionised by the rise of algorithmic trading and associated passive and "quant" investment strategies, and the rise of so-called "dark trading" platforms that can bypass exchanges entirely. These developments may not yet be directly relevant to Botswana; but again, to be forewarned is to be forearmed. This applies equally to market participants and regulators, that is, the Bank of Botswana, NBFIRA, BOCRA, and the Financial Intelligence Agency, to name a few.

But the challenge of FinTech, although inherently disruptive, should be approached in a positive and open mind; seeking to embrace the opportunities as this technology matures, rather than resist the perceived threat. FinTech start-ups succeed for the simple reason that they combine innovative adoption of emerging technologies with appreciation of what customers are looking for in terms of functionality, ease of use and security.

A word of caution would be that, in as much as these developments are of great interest, as evidenced by a number of ongoing “proof of concept” initiatives undertaken by a number of jurisdictions, public sector regulation, of any kind, must be designed with a view to be welfare enhancing. This is a debate for another day.

With those few remarks, Your Honour the Vice President, Honourable Minister, MPs, Moderators, Panelists and Resource Persons, Distinguished Delegates, once more, I thank you all for your invaluable contributions to this important event; which I am happy to officially bring to a close.

I thank you for your kind attention.