Macroeconomic and Financial Management Institute of Eastern and Southern Africa

Investec Asset Management

# HIGHLIGHTS OF THE 2019 MEFMI REGION GOVERNORS' FORUM

28 June 2019
Bank for International Settlements
Basel, Switzerland

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# FOREWORD

Given the role of our client institutions as regulators and policy makers who are entrusted with policy formulation and implementation, including for safeguardingpublic funds, fostering good governance in these institutions is of paramount importance in the maintenance of public confidence in them. Addressing governance vulnerabilities in these institutions increases resources available for use in critical areas like social sector and investment through increasing value for money/expenditure and minimising revenue leakages. In addition, the confidence of the private sector, a key player in economic growth and development, is increased through reducing the cost of doing business which is often facilitated by malpractices like corruption, bribery, and inefficient public service delivery and infrastructure. The cost of policy implementation also reduces when the public has trust in these institution.



Against this background, the MEFMI Secretariat chose 'Governance'as its theme for the 2019 Executive Fora series. The theme, in line with MEFMI's objective of raising awareness amongst policy makers on causes, impact, challenges as well as successes achieved in addressing governance vulnerabilities in its client institutions. In this spirit, the Governors' Forum, which is now in its fifth consecutive year since it was revived, was held in Basel on 29 June 2019. Delegates deliberated on these issues and focused on the International Monetary Fund (IMF) new framework for enhanced engagement on governance with its membership which is designed to promote a more systematic, effective, candid and even-handed engagement on governance vulnerabilities; and on corruption in countries where its judged to be of macro-critical nature. In addition, the discussions also focused on how countries can foster competitive markets through higher corporate governance standards in Africa.

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I would like to extend my special thanks to Investec Asset Management and the Bank for International Settlement (BIS) who continue to support this important event every year and to the International Monetary Fund for providing on a gratis basis a resource person.

It is my sincere hope that the deliberations from this Forum will provide the much-needed guidance for countries as they develop their institutional governance frameworks. Going forward, MEFMI is committed to identifying its future capacity building efforts that take into account the findings and recommendations arising from this Forum.

Michael Atingi-Ego

**MEFMI Executive Director**

# EXECUTIVE SUMMARY

Policy makers are becoming increasingly aware of the significant role good governance plays in poverty reduction, economic growth, financial market stability and investment.Poor governance promotes incentives and opportunities for corruption which in turn undermines public trust in governments, compromises market integrity, distorts competition and threatens economic development.

Investec Asset Management, the financial partner for this event,shared their global experiences, commitment and approach-based work, being done on Environmental, Social and Governance (ESG). ESG is a set of criteria that incorporates environmental, social and governance factors when measuring the sustainability and ethical impact of investing in a company or business. ESG has a robust stewardship policy which applies key principles to governances. The International Monetary Fund highlighted the key aspects of its New Framework for Enhanced Fund Engagement on Governance and Corruption that was adopted in 2018. The framework aims at promoting systematic, effective, candid and even-handed engagement with member countries, regarding governance vulnerabilities.

In this regard, discussions at the 2019 MEFMI Central Bank Governor's Forum focused on the role of good corporate standards in enhancing competitiveness in financial markets and IMF's engagement of its membership on governance vulnerabilities and, where macro-economically critical, on corruption. This report thus provides a synopsis of the deliberations made during the Forum and the recommendations thereof. These are summarised below:

- Political will to fight corruption and address governance vulnerabilities are key and the membership should only seek support from, and not wait on, external parties like the IMF to lead the way on this.
- Despite governments' willingness to combat corruption, countries in the region still lack capacity to build effective economic institutions, strengthen governance and reduce vulnerabilities to corruption.
- Development partners such as the IMF still have a significant role to play in shaping governance in member countries through supported lending, policy advice and when warranted, program conditionality.
- Regional efforts to fight financial crime and corruption, such as the Eastern and Southern African Anti-Money Laundering Group (ESAAMLG) have been seen to bear fruit by increasing transparency and accountability in public institutions; and should be recognized even as the Fund engages the membership.

The International Monetary Fund highlighted the key aspects of its New Framework for Enhanced Fund Engagement on Governance and Corruption that was adopted in 2018. The framework aims at promoting systematic, effective, candid and even-handed engagement with member countries, regarding governance vulnerabilities.

- Countries are cautioned against compromising their governance standards as a means to creating incentives to attract capital into their markets.

- One of the new trends in corporate governance is creating a diverse board of directors. It is now widely believed that a diverse board in terms of background, experience, gender, race or ethnicity moves corporations towards greater success.

- Proceeds from corruption are often laundered through the formal financial sector channels – a sector within the purview of central banks. Central Banks can play a vital role by ensuring the integrity of national payment systems to protect them from corruption.

# 1. WELCOME AND OPENING REMARKS

## 1.1 WELCOME REMARKS: Mr. MICHAEL ATINGI-EGO, EXECUTIVE DIRECTOR, MEFMI

Mr. Michael Atingi-Ego, the Executive Director of the MEFMI Secretariat, opened the 2019MEFMI Central Bank Governors' Forum by welcoming delegates to Basel and pointed out the encouraging response received at this year's event in terms of attendance. He thanked the Governors for taking the time to attend one of MEFMI's key events on its annual calendar.

Mr. Atingi-Egoalso expressed MEFMI's gratitude towards Investec Asset Management, for supporting the Forum for the fifth year running. He acknowledged, in absentia, Mr. Agustin Carstens who is the General Manager of the Bank for International Settlements (BIS) and former Governor of the Bank of Mexico for continuing to provide meeting facilities for the Forum on a gratis basis. He also thankedthe International Monetary Fund for the provision on a gratis basis of a resource person, and Ms.Wenke Soeteber and her team who continue to offer seamless administrative support to MEFMI for the event.



## 1.2 OPENING REMARKS: MR JAMES HAITIKULIPI, INVESTEC ASSET MANAGEMENT

Mr. James Hatuikulipi pointed out that Investec Asset Management was committed to the long-term development of Africa's economies and markets. He added that the deliberations at the forum focused on the topic of Governance as a critical and necessary condition in the development of the MEFMI region economies and markets.

Mr. Hatuikulipi advised that as a long-term investor in emerging markets, Investec is encouraged by the concerted efforts countries are making with respect to mitigating and managing environmental and social risks as well as strengthening their corporate governance systems. He urged the policy makers and regulators to view credible corporate governance frameworks that are supported by effective supervision and enforcement mechanisms as an incentive that will improve confidence that reinforces the good functioning of financial markets.

Mr. Hatuikulipi also expressed his gratitude to the MEFMI team for the invitation to, once again, support the Governors forum. He reiterated Investec's support to the region's capacity building initiatives that he pointed out, are critical for the development of the region's economies and financial markets.

# 2. FORUM PRESENTATIONS AND DISCUSSIONS

## 2.1 SESSION 1: NEW FRAMEWORK FOR ENHANCED FUND ENGAGEMENT ON GOVERNMENT AND CORRUPTION

**Presenter:** Mr. Ceda Ogada, Deputy General Counsel, International Monetary Fund

**Moderator:** Mr. John Rwangombwa, Governor, National Bank of Rwanda

The session aimed to highlight, IMF's effort in helping its member countries to address governance and corruption issues. It introduced the new framework that supplements the policy on governance detailed in the 'The Role of the IMF in Governance Issues: Guidance Note', that was adopted in 1997.

The IMF has been engaging the membership s through its 1997 Governance Policy and while considerable progress has been made in implementing this Policy, the Fund identified several areas in which engagement on governance and corruption issues could be enhanced. The policy was implemented in an uneven manner, targeting smaller economies and inclined to focus on countries that borrowed from the IMF as an instrument of conditionality. The Fund also recognised that the policy was not effective in diagnosing governance issues in a clear way and providing concrete policy advice that members could use to strengthen their governance structures. Consequently, in 2017, the IMF carried out a review of the 1997 Policy in an effort to address the highlighted gaps. The Framework was designed to promote a more systematic, effective, candid, and even-handed engagement with member countries regarding governance vulnerabilities.



The New Framework consists of four elements as described below:

### First Element

This is designed to enable the Fund  assess the nature and severity of governance vulnerabilities. The Fund identified six state functions that are considered more relevant to economic activity these include – Fiscal governance, Financial Sector Oversight, Central Bank Governance, Market Regulation, Rule of Law, AML/CFT and Corruption.

### Second Element

Aims at guiding the Fund's assessment of the macroeconomic implications of governance vulnerabilities taking into account the applicable standards for surveillance and use of Fund resources. Once the IMF analysis determines that governance vulnerabilities are severe in any of the categories mentioned in the six state functions, the overall assumption is that the macroeconomic impact will be significant in the long term and would compel an assessment and policy recommendations in surveillance or warrant conditionality in lending.

### Third Element

Provides a framework for policy advice and capacity development to support members where Fund engagement is warranted. The Fund has faced criticism for providing policy advice that was unspecific and not actionable. By anchoring the corruption diagnosis in these broader governance areas, the Fund believes it should be able to provide much more needed tailored, concrete and granular recommendations.

## Fourth Element

Thiselement assesses measures designed to prevent private actors in a country from offering bribes or providing services that facilitate the concealment of corruption proceeds. The element addresses the transnational aspects of corruption recognising that corruption does not only arise in the domestic markets but could be facilitated by foreign parties. Over the past two decades, various international efforts have been established to curb corruption at international level. The OECD Convention on Combating Bribery of Foreign Public officials in International Business Transactions criminalises foreign companies that offer bribes to public officials in domestic markets. In addition, the United Nation's Convention Against Corruption (UNCAC) has developed efforts to deter concealment of funds acquired by corrupt officials by application of robust AML/CFT laws and institutional frameworks.

## Key Discussion points

Subsequent to the presentation, a lively discussion ensued. Key points are noted as follows:

a) IMF's willingness to candidly address the observed weaknesses in the Fund's previous policy on corruption is commended. By providing clear indicators to members, the new policy will help in guiding the formulation of governance frameworks and ease compliance. The use of clear language in staff reports was also applauded.

b) Agencies such as the IMF have a significant role to play in influencing policy in the countries that would compel governments to combat corruption. This could be by setting minimum standards for governance or even imposing conditionality where it is warranted. In addition, regional initiatives like the Eastern and Southern African Anti-Money Laundering Group (ESAAMLAG)would greatly benefit from some of the insights of the new IMF policy and their role in advancing this framework ought to be recognized.

c) The fight against corruption is rendered more difficult in some countries as state institutions, like the judiciary, are largely compromised and the state is often controlled by entrenched interest groups. Furthermore, in some instances, despite governments' willingness to combat corruption, there are challenges in the capacity of law enforcement bodies to detect corrupt activities and countries often had weak enforcement mechanisms.

d) Authorities in the Central Bank have the influence within their sphere to promote and improve governance. As overseers of the national payments system, central banks are key in developing frameworks that prevent corruption practices like illicit financial flows.

e) Having the developed world involved in the fight against corruption thorough international organisations like the OECD is an advantage. It provides for a more concerted and sustained effort in supporting the anti-corruption agenda in developing economies.

f) Political will to fight corruption is the first necessary step for any progress on this front. External parties like the Fund should only come in to support government efforts with the necessary country reforms and addressing any resultant capacity gaps.

## 2.2 SESSION 2: FOSTERING COMPETITIVE MARKETS THROUGH HIGHER CORPORATE GOVERNANCE STANDARDS IN AFRICA

**Presenter:** Ms. Therese Niklasson, Head of Global ESG, Investec Asset Management

**Moderator:** Dr. Dalitso Kabambe, Governor, Bank of Malawi

The session helped to highlight the importance of good governance in promoting market development in Africa. Using examples from Asia, the session demonstrated that lack of certainty in governance systems tends to drive up the cost of capital and tend to lower operational efficiencies in these markets...

The global financial crisis was caused partially by lack of active ownership[1] in financial markets, lack of corporate oversight and excessive risk-taking. This has led to reforms as seen in the UK, with the development of market Stewardship Codes intended to foster a more engaged environment between companies and investors. Since then, this model has been replicated in many markets. In South Africa, the King Code, that incorporates some ESG criteria, is seen as the highest standard across Africa in terms of governance codes and many markets are trying to adopt versions of the code to raise the standards of governance in their countries.

The case of Korea perfectly illustrates how markets can be dragged down by a governance discount[2]. While the country has been going through a successful economic reform for the past decades, there have been marked concerns over complicated ownership structures, sub-par corporate governance frameworks and poor market business ethics. Korea is one of the biggest stock markets in Asia but it has been trading at a fifth below the valuation of comparable markets and many investors argue that this discount has been widening over the years. Asset managers are under pressure from their investors to divest from companies in such markets that have weak corporate governance structures.

### Key Discussion points

a) Countries were cautioned against the tendency for market authorities to relax governance standards as a way of creating incentives to attract capital into their markets. This trend has been seen in both developed and emerging economies. Such an approach lacks foresight and compromises the long-term quality of financial markets.

b) Corporate governance arrangements are incredibly important for all type of assets classes and discounts in markets exist for companies that do not have strong corporate governance frameworks. There is a real incentive to build governance systemsin markets so as to raise the overall valuation of business and attract more capital.

c) Governments and markets need to hasten engagement with other stakeholders and exchanges around proposed changes to corporate governance codes. There is need for investors to understand the local nuances in the various markets so as to work with relevant stakeholders to set up governance arrangements that are most suitable for the respective circumstances.

[1]Where shareholders take a more involved role in ensuring that companies they are investing in are operating responsibly and more sustainable

[2]The amount by which investors undervalue aparticular market's stocks due to a perceived higher investment risk in that country than markets in other countries.

d) Stock exchanges play a critical role as key holders of standards, accountability and disclosure. If capital markets regulator[3] can engage stock exchanges with the view to ensuring that they maintain strong rules and investment requirements, then markets are able to build a much higher standard in general.

e) Though the extent differs considerably across the different markets, ESG issues in emerging markets are showing a positive trend from a generic perspective. Developing markets are showing better transparency, more engagement and a larger incentive to comply with global norms of good governance.



[3] e.g. the capital markets authority or securities and exchange commission

# 3. LUNCHEON AND CONCLUDING REMARKS

A luncheon was held at the Les Trois Rois and the closing remarks were given by the Governor, Central Bank of eSwatini – Mr. Majozi Sithole. Governor Sithole thanked the MEFMI Secretariat for organising yet another successful event. He pointed out that the theme of Governance was timely as it comes at a time when dialogue on the issue of Governance is intensifying across the globe. He pointed out that in the region, there are concerted efforts to improve governance in order to improve policy and meet international accepted levels.

Governor Sithole expressed gratitude to the presenters Mr. Ceda Ogada and Ms. Therese Niklasson for their enriching presentations that aided thoughtful but candid discussions in terms of what the challenges have been and possible way forward.

Governor Sithole concluded his remarks by thanking the BIS and Investec for the support in organising the event. He thanked the Governors for attending the event and appealed to them to attend the Combined Forum which will be held at the margins of the IMF/World Bank Annual Meetings in October. He also urged them to encourage the ministers to attend the Combined Forum emphasising that the outcomes including recommendations at such forums could only be implemented effectively, if there is collaboration between the central bank and the Finance ministry.

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