CONJONCTURE

PluriConseil
THINKING OUT OF THE BOX !

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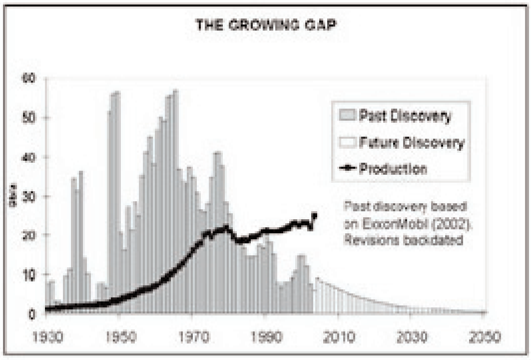
"Tout l'art de la politique est de se servir des conjonctures."
Louis XIV

Energy for transport

By Stefan Atchia

When we talk about energy and transport, Michael Meacher of the *Financial Times* (5 January 2004) goes right to the point by stating the following: *"Today we enjoy a daily* [world] *production of 75m bpd* [million barrels of oil per day]. *But to meet projected demand in 2015, we would need to open new oilfields that can give an additional 60m bpd. This is frankly impossible. It would require the equivalent of more than 10 new regions, each the size of the North Sea. Maybe Iraq with enormous new investments will increase production by 6m bpd, and the rest of the Middle East might be able to do the same. But to suggest that the rest of the world could produce an extra 40m barrels daily is just moonshine… Yet no major primary energy alternative can replace oil and gas in the short-to-medium term. The implications of this are mind-blowing, since oil provides 40 per cent of all traded energy and no less than 90 per cent of transport fuel* [100% for Mauritius]. *It is hard to envisage the effects of a radically reduced oil supply on a modern economy or society. Yet just such a radical reduction is staring us in the face… The world faces a stark choice. It can continue down the existing path of rising oil consumption, trying to pre-empt available remaining oil supplies, if necessary by military force, but without avoiding a steady exhaustion of global capacity. Or it could switch to renewable sources of energy, much more stringent standards of energy efficiency, and a steady reduction in oil use. The latter course would involve huge new investment in energy generation and transportation technologies."*



We don't like to hear the secrets of scary people, or the scary truth of good people, nonetheless, we are running out of oil and this is the bottom line. This is the sad reality and no matter how positive or grumpy we get, nothing will change this state of affairs.

So what do we do? What are we to do in Mauritius, especially concerning transport, especially urban transport? The transport sector brings children to school, people to work, t-shirts on containers to ships, sugar from the fields, food to the supermarkets, tourists to our hotels, my bottle of water on my table, near my laptop (which came by ship from Asia). Wait a minute, every single one of these examples – we could have fun listing all of them for next 10 days – required mechanized, oil powered transport. And we are running out of oil.

Should we think the unthinkable? Stopping only the few of the activities listed, and our country would come to a screechy halt. In the movie Apollo 13, starring Tom Hanks, the engineers said it very well when the mission crew, on the way to the moon, was in serious trouble: energy is everything! Think about it again. Without it, you don't eat, you don't move, you don't work, you don't communicate, you site there and watch the sun set.

Some think that the forces of the market will enter the arena and fix the problem when matters become very bad, that is when the price of oil becomes simply too high and the alternatives technology become economically sustainable. But that is a wait-and-see strategy that might be risky, and one would not like to see the country be caught, high and dry (on oil). As the old say goes, failing to plan is planning to fail. And in this case, the stakes are simply too high to take it lightly.

Cycling makes economic sense

So where should we be heading? With regards to public transport, options are already available. Buses will have to stick to diesel for a while longer but a mass transit system in the Curepipe-Port Louis corridor, as the government is proposing, could run on electricity, even though it may start as diesel, or diesel electric hybrid in the beginning. Since buses are nine times more efficient than cars, the economic savings in the switch to more public transport, including the mass transit system, in the urban areas would be staggering. Investing in public transport simply makes economic and energy sense and, in a small and densely populated country, the target is easy to achieve.

There isn't much that can be done about the transport of goods from our fields, ports and supermarkets for now. However, with regard to private mobility, diversity and efficiency are the current platform for change. I remember the Dutch Government investing massively on the cycle network for the whole of the Netherlands in the 1970s, following the oil shocks. This was not a heart decision, seeing nice Dutch ladies on cycles, but a hard economic reality: cycling makes economic sense.

Did you know that under 4km, in an urban environment, the bicycle will reach destination before the car, which will have to find a parking, walk to the destination and so forth. Under the current oil environment, it would be highly favourable for Mauritius to do likewise. Invest into cycle networks, with the appropriate cycle parking racks and facility, and the target market could touch nearly half of all urban trips in the country. Oh, but we have hills in Mauritius and Holland is flat. Well, Switzerland makes Mauritius look flat and they have achieved a staggering percentage of all trips by cycle. So, beyond planning, engineering, economics and traffic management, cycling in Mauritius simply makes sense.

So what should the urban future look like? You may have a beautiful car in your garage, but in the morning, you walk or cycle to the bus station or to the mass transit and go to work. In the evening, you arrive fresh as a rose at the station and cycle to the supermarket on the way home. In the evening, you can then take your car for a tour visiting friends and family. In the world of high oil prices, does that look so bad? Let's remember that the most advanced countries on the UN development list are Scandinavian, and they all have invested massively on cycling. It may sound funny at first, but it is not really. It is about thinking clear and understanding our environment responsibly.

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Making corporate control work

By Kris Seeburn

Somehow we need to evolve and bring about the good governance practices in our own companies. Our government is trying to push a bit hard on this situation, but to be honest how much of this reality is being thought of? There is so much talk about it, yet Corporate Governance is still a mystery or a reality. Going through so many reviews and practices, we can only find that there is no magic wand that can give us an upfront solution. We need to try and try and use the best of experiences. Each situation is different. The predominant question, though, is: How are we making the Corporate Control work?

Amongst the events that predictably lead to demands for government action are business failures and corporate scandals.Demands for government action to improve corporate governance are, however, based on a dual mistake. They wrongly presuppose that the problems have been caused by a lack of sufficient regulation, and they erroneously assume that government regulation can make things better.

Experience from various big companies in the US and Europe has shown, however, that all such pronouncements need to be considered sceptically. Best practice rather than regulation may indeed be the government's publicly preferred starting point. But judging from their past performance, it is unlikely to be the preferred – or the actual – outcome.

The best way to bring about beneficial changes would be to encourage maximum experimentation in the marketplace, and to allow different forms of corporate governance to compete for the support of investors.

Today there are suggestions that 'best practice' guidelines should be enforced by the Government specific authorities. The danger of 'regulatory creep', in which guidelines are transformed over time into mandatory requirements, is all too real.

The likelihood of regulation is exacerbated because many of the respondents who participate in corporate-governance reviews regularly advocate regulatory strictures. Some seek government regulation to make directors serve a social or political agenda other than the direct interests of shareholders. Others, including many who ostensibly represent business interests, would enlist government support to prescribe some favoured model of best practice, regardless of shareholders' own preferences.

Both such approaches are mistaken: by its very nature, corporate governance should be the responsibility of the shareholders themselves. There is much that could and should be done to increase the effectiveness of non-executive directors, but it should be up to the shareholders of each corporation to determine the rights and responsibilities of their directors, both executive and non-executive.

Most of the changes that are needed to improve corporate governance do not involve any government action. They can and should be provided by the marketplace itself. In the US, many firms have already voluntarily chosen to show the cost of granting options as an expense in their profit and loss accounts, and investors are voting down far more option plans than they did five years ago. The best way to bring about beneficial changes would be to encourage maximum experimentation in the marketplace, and to allow different forms of corporate governance to compete for the support of investors.

Contrary to popular belief, the free-rider problem is not an insuperable barrier to such non-regulatory solutions. An investor acting independently would unilaterally incur the costs of action from which all shareholders would benefit. But if the costs of the corporate governance action were for the account of the corporation, they would be automatically shared by all shareholders, in proportion to their shareholdings.

The kinds and amounts of shareholder support paid for by the corporation could be one of the ways in which companies competed in a genuine 'market for corporate control'. The 'market for corporate control' conventionally refers to the use of takeovers to transfer corporate ownership. But it can be used more broadly, to refer to the market in which companies compete for shareholders, and investment managers compete for funds, in part on the degree and kinds of accountability they afford to owners and investors.

Subjects of such competition might include, for example, the nature of the constitutional corporate objectives, the extent to which strategic and operational matters required shareholder approval, company election procedures, the independence and quality of directors, the extent and quality of performance-related remuneration, and the types of disclosure and audits.

One of the many advantages of free market is that it elicits innovative solutions to problems as they arise in all their real-life variety and complexity.

Companies could compete for shareholders on the different ways in which their directors were selected and elected. Or experiment with the levels of disclosure they required from directors (including their reasons for resignation), with the personal or professional or other qualifications they required directorial candidates to have, and with the number of times that directors could be re-elected. Or they might try varying the responsibilities of the lead non-executive director, and having differing percentages of non-executive directors.

Corporations might even vary in the extent to which they allowed their directors to be executives of other companies. Shareholders might seek to employ the services of 'professional directors' – directors who would not be the executives of any firm, but who would be chosen specifically for their ability to safeguard shareholder interests. Even if such directors acted in a non-executive capacity for more than one firm, they might be less prone to the damaging conflicts of interest which now typically arise between executive directors and owners.

Companies could also compete for shareholders on the basis of the different sorts of financial and structural support offered to directors. Companies might reimburse some or all of the expenses that directors incurred in investigating company matters, and in taking specialist advice. Companies could also vary the extent to which directors' (and advisors') liabilities were indemnified, contractually limited, or covered by errors and omissions insurance at company expense.

But these are just a few of the very many different ways in which companies might compete in respect of corporate governance. One of the many advantages of free market is that it elicits innovative solutions to problems as they arise in all their real-life variety and complexity. Markets also effectively test those solutions and efficiently disseminate best practice.

The best way to ensure good corporate governance is to allow shareholders the greatest possible freedom to control their own corporations. The value of doing so is clear. According to a recent analysis of 1,500 stocks by the (US) National Bureau of Economic Research, companies with the most restricted shareholder rights had annual earnings and valuations between 1990 and 1999 that were almost 9% lower than companies with the fewest restrictions. Shareholder freedom is associated with both good corporate governance and superior corporate performance.

OUTLOOK FROM SINGAPORE - By Daryl Liew

Global Economy

Oil prices hit a three-month low as the US oil industry recovers from hurricane damage, and warmer than normal temperatures reduce demand for heating fuels. While the supply side is improving, oil production from the Gulf region is only expected to completely recover by the middle of next year.

US payrolls for October came in 56,000 higher, with a net 35,000 downward revision made to the figures for August and September. This increase implies fundamentally stronger activity due to post-hurricane relief and restoration work. The October ISM ("Institute for Supply Management") reports also showed strong results. Manufacturing eased 0.3 points to 59.1, while non-manufacturing rose to 60. Consumer spending however has showed signs of weakening on lower new car sales and a fall in mortgage applications. The US economy remains on track for 3-3.5% growth for the year 2005.

Indicators show that growth in the Japanese economy moderated in the third quarter as consumers and companies curbed spending. Higher oil prices affected consumer spending while capacity constraints have limited capital spending. Despite this, analysts still believe that Japan is well positioned to maintain a balanced, domestically driven recovery. The world's second largest economy is on track to grow 2.4% this year.

Economic conditions are gradually improving in the euro zone. Lastest October numbers show a pick up in industrial activity, with regional purchasing managers reporting gains in both services and manufacturing. The recovery, however, is constrained by sluggish consumer spending, as household disposable income is affected by higher energy costs and increases in indirect taxes. Employment growth also remains subdued. While the general conditions have improved, it remains to be seen whether the current economic recovery is sustainable.

On the political front, Europe continues to be plagued by turmoil. First, avian flu has been reported in the region. Then, the already fragile political situation in Germany became even murkier with the resignations of two senior politicians, one from each of the two main coalition partners. This complication raises fresh concerns over the Social and Christian Democrats ability to smoothly work towards a common policy. Finally, racially-motivated violence in France has escalated in recent weeks, sparking fears that this unrest may spread to other parts of Europe.

Interest Rate

As expected, the Fed continued on their "measured approach" and raised interest rates by another 25 basis points on 1st November. With interest rates currently standing at 4%, most analysts believe that Alan Greenspan will continue to hike rates in 0.25% increments at the next two meetings before he officially steps down on 31st January. Ben Bernanke, George W. Bush's top economic adviser and former Fed governor, is slated to take over as chairman. Bernanke is viewed as extremely qualified for the post and is expected to be equally zealous in fighting inflation. Despite this, expect some uncertainty in the financial markets after the handover, as the new chairman establishes his credibility.

The Bank of Japan has again hinted that a shift in monetary policy is in the pipeline. As the country slowly emerges from a long deflationary environment, expect the BOJ to focus on short-term interest rates as the key policy target. The BOJ however has reassured the market that it can continue to expect a period of very low short-term rates.

The ECB has continued to tease the market by hinting at imminent rate hikes in order to fight inflationary pressures. However, it has kept rates at 2.0% on concerns over the economic struggles in the region, Germany in particular. With core inflation at a modest 1.3%, it seems likely that any action would probably only take place in the first quarter of 2006.

Technicals

Short-term technical indicators continue to point downwards with most indices hitting new lows in October. While the indicators have tested the lower support levels, the market may fall a little further before stabilising.

The technicals for bonds remain bleak, with prices falling in tandem with equity markets.

The fundamental and technical considerations are still supportive of our preference for equities over bonds on a tactical basis. While the inflationary concerns of September have died down somewhat with the release of more benign numbers, the threat of avian flu and growing racial unrest in Europe have come to the fore. Having said this, November and December are traditionally periods where we see strong equity market rallies due to increased consumer spending for the holiday season and window-dressing by corporates. Despite the many problems in the external environment, we do believe equity markets will pick up in the next two months.

Valuation

Global equity valuations are looking significantly more attractive on the back of the price correction last month and stronger 3rd Quarter earnings in the US. Forward earnings are still in line with expectations.

Bond prices have fallen as inflationary fears take hold. 10 year US bond yields are now hovering around 4.60%. Despite this, bonds continue to look expensive relative to equities.

Scenarios

Base Case: Equity markets recover as inflationary fears in the US prove unfounded. The global economy grows at a sustainable pace on the back of more stable oil prices and a calmer geo-political climate.

Worst Case: An avian flu pandemic breaks out, causing a loss of lives and affecting global trade. Inflationary pressures work its way through the system forcing central banks to raise rates faster than previously expected, adversely affecting both equity and bond markets. A harsher winter season and further disruptions to oil supplies cause oil prices to escalate, fuelling spiralling inflation. Terrorist attacks and escalating violence in Europe spread, increasing the geo-political risk premium and paralysing markets.

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GDP growth down to 3.3% for 2005

The EPZ sector, of which clothing is the major activity, continues to face competitiveness problems. As from September 2005, the third country fabric exemption granted for a period of one-year to Mauritian exporters to the U.S. market under the AGOA has expired. Although renewal possibilities for the same for three more years exist, there are currently some obstructions to the negotiation.

During the year June 2004 to June 2005, the number of firms in the clothing and textile sector fell from 265 to 260 and the number of employees in that sector fell from 59,381 to 55,990. Wearing apparels exports during the first semester 2005 showed a decline of 17.8% compared to the same period in 2004 (Rs 9.6 billion compared to Rs 11.7 billion in 2004). This decline in exports of wearing apparels plays an important role in the decline of overall EPZ exports which fell by 10.3% during the first semester of 2005 compared to the same period in 2004. Exports to the U.S., a major importer of Mauritian clothing, fell by 24.2 % - a matter of great concern. We fear this situation can be even more dramatic after the recent announcement of the EU and the USA for a possibly more liberal trade policy of wearing apparel imports.

The contribution of the EPZ sector to GDP for the first semester of 2005 fell by 8.5% to Rs 6 billion compared to Rs 6.6 billion for the same period of last year. Taking into account the continuous depreciation of the rupee vis-à-vis the major currencies (Euro and Dollar) and based on the above trends, we anticipate a contraction of -10.9% of the EPZ sector in 2005.

The Crop Estimate Coordinating Committee, on 7th October 2005, revised their estimated production of sugar downwards from 550,000 tonnes to 535,000 tonnes. Therefore, growth in the sugar sector, initially estimated at -3.9%, is now estimated at -6.9%. The fall in production is due to the average sugar cane extraction estimates being downgraded from 10.8% to 10.5%. The reason behind this fall in extraction estimates is the heavy and excessive rainfalls over the island during September.

There was an increase of 5.1% in the number of tourists arrivals during the first nine months of this year compared to the same period of last year. The authorities are committed to increase the importance of the tourism sector in our economy by opening up air access to other main airlines and by promoting Mauritius as much as possible. Still, we believe that tourist arrivals will not increase by more than 4.9% to reach 754,000 for the whole year 2005. There is always a time lag between what is intended and what is achieved, if ever rightly achieved. On account of our projected growth rate for tourist arrivals, we expect the hotels and restaurants sector to grow by 4.6% in 2005.

Following the tariff cuts decided in April, the wholesale and retail trade sector grew by 12.1% year-to-year in the 2nd quarter of 2005 compared to 0.4% in 1st quarter 2005. This is mainly explained by the year-to-year growth of 7.8% in household expenditure in 2nd quarter 2005 as compared to 5.7% in 1st quarter 2005. Consequently, we revise our growth estimates for retail and wholesale sector upwards to 5% for the year 2005.

Evolution of our growth forecast for 2005

	Sep-05	*Dec-05*
Export Processing Zone	-7.1%	-10.9%
Hotels and restaurants	+4.4%	+4.6%
Wholesale and retail trade	+4.6%	+5.0%
Financial intermediation	+8.0%	+8.0%
Overall GDP	**+3.9%**	**+3.3%**

The construction sector contracted, year-to-year, by -15.4% in 1st quarter 2005 and by -20.4% in 2nd quarter 2005. Unless a real boost is given to that sector, we believe that it will undergo a contraction rate of -11% for the whole year 2005. So far, there is not much initiative on behalf of the authorities towards reviving this sector.

Taking into account the continued increase in activity of the banking sector, particularly the offshore banking sector, we maintain our prediction of 8% growth rate in the financial intermediation sector.

Owing to the higher contraction rate in the EPZ, we revise downwards our estimated GDP growth for the current year to 3.3% from 3.9% forecasted in September.

Methodology used for forecasting

The ARIMA methodology has been used in the prediction process. This method is based on the philosophy of *"let the data speak for themselves"*. In this methodology, the dependant variable has the characteristics of both Autoregressive process and Moving Average process.

ÉCLAIRAGE : CROISSANCE

Quand on parle de croissance, on se réfère à la croissance économique, à la croissance globale de l'économie. Elle a trait au Produit intérieur brut (PIB) qui est calculé au coût des facteurs de production, incluant les profits réalisés dans la production des biens et services. En d'autres mots, le *PIB au coût des facteurs de production*, c'est la somme reçue par les producteurs sur leurs produits, incluant les subsides mais excluant les impôts sur les produits. Si l'on inclut les impôts, on obtiendra le *PIB aux prix du marché* – les prix payés par l'utilisateur final qu'est le consommateur.

C'est par rapport au *PIB aux prix du marché* qu'on calcule le taux du déficit budgétaire. Mais on utilise le *PIB au coût des facteurs de production* pour calculer le taux de croissance économique. La raison est que les impôts constituent un prix supplémentaire sur la valeur de ce que l'économie produit véritablement.

Ainsi donc, la croissance économique désigne l'accroissement du *PIB au coût des facteurs de production*. Mais seulement, il faut éliminer l'effet des prix dans l'accroissement de la production pour ne prendre en compte que le volume. Quand on dit croissance, on parle de croissance réelle, puisque l'effet des prix a été éliminé par un déflateur *(deflator)*, celui-ci étant toutefois un ajustement technique qui n'échappe pas à un jugement arbitraire. Le déflateur représente une mesure très large de l'inflation au sein de l'économie. Si le PIB en roupies courantes augmente de 10%, mais le taux d'inflation représenté par le déflateur est de 6%, la croissance sera de 4% (10 moins 6).

Extraits de : Eric Ng Ping Cheun, *Mieux comprendre l'économie*, 2005

FORECAST - By Sawkut Rojid