

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

As a sector which has developed within the preference dependent framework, the Textiles and Garments export-manufacturing industry in Mauritius has been under increasing pressure from the forces of Globalisation and Liberalisation. The operational word for any plan to create a future for the Textiles and Garments industry in Mauritius will be competitiveness. The definition which we attach to competitiveness is that it is the ability to convince customers to choose a particular source of supply over competing alternatives on a sustainable basis. To achieve such competitiveness, we shall propose a business model based on the benefits of FOCUS, CONCENTRATION and NETWORKING.

In a small economy far from its main markets one of the main obstacles to development of the industry is co-ordination and informational failures. Explicit industrial policy is needed to overcome such constraints. To confront the new conditions created by the end of the Multi-Fibre Agreement and the emergence of countries such as China and India on the global market we shall have to position ourselves as a differentiated sourcing base. This can be achieved principally by a process of up-gradation of the industry and by re-positioning it in the Global Commodity Chain (GCC) in the more knowledge/information intensive value segment of the global market.

The share of total expenditure of households in developed countries on sports and leisure activities has been constantly increasing over the past decades, even in times of otherwise difficult economic conditions generally. This trend is not fashion related and is very unlikely to change in the foreseeable future since it is steeped in profound sociological transformations related to the lifestyles of families, with spending power, in developed countries. Recent observations have shown that the spending behaviour in the markets for sports and leisure products are less price sensitive and more responsive to innovation and research.

These are the market characteristics which most lend themselves to the development of a niche market approach and would therefore fit in our general strategic approach for repositioning Mauritius in the Global Commodity Chain.

On the supply side, Mauritius is well positioned to take full advantage of this market because of its existing vertically integrated production process in this area.

A competitive response to globalisation

By Rajiv Servansingh

Mauritius as a source of supply in the global market

Mauritius' reputation as a source of supply in the global market has been seriously dented by the recent mass migration of some of the most important companies, which had been established in the country for a long time. This can prove to be damaging if no action is taken to revamp the country's image as a reliable source of supply.

Among the criteria, which are important for buyers in the selection of sourcing countries, are sea and air connections, (tele)communications infrastructure and levels of political stability and, more and more often, the human rights situation.

While Mauritius will score well on all these points, the principal concern of buyers still remains the capacities of individual suppliers. If one or several potentially interesting suppliers are present, then this makes a country interesting. This is why we are proposing the sort of specialization that will position Mauritius as an important source of supply and maintain its reputation as an important player in the global market for textiles and garments.

The critical value proposition which we are making is about turning what is viewed as an intrinsic weakness – the small size of Mauritius – into a strength. For this to happen, government will have an important role to play in shaping the context and institutional structure surrounding companies and in creating an environment that stimulates companies to gain competitive advantage.

In this context the concepts of networking and clustering are fundamental to the extent that they provide the mechanism through which a number of small and medium enterprises can each leverage the economies of scale resulting from the sharing of information and knowledge.

In Mauritius, the emphasis on clustering and networking would not be so much geographical or spatial homogeneity but rather the institutional mechanisms and policy framework which will allow the sharing of knowledge about market trends and technology innovations.

Repositioning the textile and clothing industry in the global commodity chain through a systematic upgradation of the processes and products

Gary Gereffi first developed the concept of GLOBAL COMMODITY CHAIN (GCC) in 1994 in his seminal work on the geographical distribution of the global garments manufacturing industry.

In this approach clothing is seen as a sector dominated by a governance structure in which profits and control are concentrated in the functions of marketing, distribution and retailing, while production is globally outsourced on the basis of a BUYER DRIVEN network of independent manufacturers, located mainly in developing countries.

Gereffi observes that while, initially outsourcing was simply cut-and-sew work from the US to manufacturers in Hong Kong, Taiwan and Korea, manufacturers in these countries later set up their own networks of producers, distributed among other developing countries including Mauritius. Success of exports from Mauritius by these mostly Hong Kong based companies, depended on the presence of a particular mode of operations.

This was characterized by scale, specialization in long runs of a narrow and basic product range and specialization in an equally narrow range of functional activities: a description which incontestably captures the activities of the largest foreign manufacturers who had invested in Mauritius and have for the most part abandoned the country with the quasi disappearance of preferential market access and the market liberalization following the end of the MultiFibre Agreement.

It is on the basis of the above that we can safely argue that the "worst is behind us" in terms of the departures of large manufacturing units. Those for whom Mauritius no longer fits into their GVC have gone to look for other manufacturing bases more appropriate to their requirements.

The way forward for the Textiles and Garments Industry will depend on our ability to reposition the textile and clothing industry of Mauritius in the global commodity chain through a systematic upgradation of the manufacturing processes and products.

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The companies which have chosen to stay on invest in modernisation, restructure their processes and are gearing themselves for such a totally new business model based on competitive market penetration in different market segments with more value added products and capacity to meet the requirements of the new market conditions, such as short lead time and lean retailing. In Mauritius, it would seem that the presence of an established entrepreneurial community, together with a number of favourable social and cultural conditions have facilitated a rapid movement up the learning curve and provided the right conditions for such an up-gradation to happen.

A Road Map to position Mauritius in beachwear and fashion leisurewear

We propose that Mauritius should position itself to be a key world player in beachwear and fashion leisurewear. Following many interviews with operators, we are convinced that there are many synergies which can be realized between the two lines of products along the supply chain. Given these synergies, this will also create the critical mass that is necessary to validate our approach.

The main rationale behind this proposition is, of course, the need to FOCUS and concentrate our efforts in the use of scarce resources such as specialized labour with appropriate skills, marketing and design expertise as well as Research and Development. Many success stories are testimony to the principle that growth is obtained by concentrating one's strength in markets where a competitive advantage can be obtained by doing so. Such an approach, of course, also responds to the critical need for defining the product and the market segment to create a sustainable business.

Deciding which groups of customers are going to represent the focus of our attention on the basis of some specific appeal and then designing a combination of tactics that will give us a definite competitive advantage in the well-defined market, constitute an important strategic choice.

The Road Map that we propose is based on the following arguments:

1) VISION AND APPROACH: Success stories are always characterized by a combination of visionary leadership, long term determination, sensible government policy, effective co-ordination among a wide range of stakeholders, risk-taking by those in the best position to take it, and a lot of hard work. To our mind these characteristics are precisely the strong points of Mauritius and a hallmark of its strategic approach to successful development over the past thirty years or so.

2) BRANDING: Mauritius is well known today as a high class tourist destination and is already positioned in the minds of large numbers of Europeans as the dream destination for sand, sun

A competitive response to globalisation

By Rajiv Servansingh (cont., from Pg 1)

and sea. This should facilitate the branding exercise, which is a necessary condition for the successful implementation of the project. Creativity, research and development and innovation will be necessary to leverage this reputation and produce the fashion products, which are in line with demand in the targeted markets.

3) VALUE CHAIN INTEGRATION: T-shirts have proven to be the most resilient products during the most difficult years of the Export Processing Zone. This is not by accident but rather a reflection of the fact that the industry is vertically integrated and we have more control on the pre-production stages of the value chain. A few companies in the sector have already started experimenting with their own design and marketing. Such backward and forward integration, by providing further control on supply, distribution and marketing, further integrates the value chain. Up-gradation of the product lines in fashion leisurewear will be based on the acquired strengths of backward integration but will require systematic efforts into forward integration – Design, Marketing and Distribution.

4) HIGH VALUE ADDITION: In its post-MFA survey report entitled "The Global Textile and Clothing Industry post the Agreement on Textiles and Clothing", the World Trade Organization has this to say concerning sportswear: *"The textile and clothing industry has high-value segments where design, research and development are important competitive factors. The high end of the fashion industry uses human capital intensively in design and marketing. The same applies to market segments such as sportswear where both design and material technology are important."*

5) SIZE AND NETWORKING (CLUSTERING): This is a great opportunity for operationalizing the concept of "small is beautiful" and turning it into a competitive advantage. The small size of Mauritius is a "weakness" which can be turned to our best advantage by providing the ideal geographical space for the most effective co-ordination and networking policies for a competitive industry to thrive. Co-ordination and networking are meant to provide the advantages of scale to an industry constituted of small and medium enterprises with the nimbleness and flexibility to compete in demanding competitive conditions of short lead times and lean retailing. It is well known that in the garment industry the economics of the process are such that economies are achieved at relatively modest volumes, leaving plenty of rooms for the small producers.

Accordingly, we see the following critical implications for success:

- the need for an environment which shall promote

"innovation and creativity" in the areas of specialisation,

- focussed Research and Development in Design and Fashion to respond to the need for differentiating our offer to meet the expectations of the selected market segments,

- the development of networking and clustering which should be facilitated in a situation where the roadmap is being defined in consultation with all industry stakeholders,

- the need to give serious attention to branding the industry, preferably within a larger exercise of country branding for Mauritius as a nation.

Scarce resources should be invested where they yield attractive returns

Potent competitive advantage will materialize only to the extent that an appropriate context and institutional environment are present. As far as the role of the government is concerned we would like to quote from Michael Porter's **Competitive Advantage of Nations**: *"Government's proper role is as a catalyst and challenger, it is to encourage – or even push – companies to raise their aspirations and move to higher levels of competitive performance, even though this process may be inherently unpleasant and difficult. Government cannot create competitive industries; only companies can do that. Government plays a role that is inherently partial, that succeeds only when working in tandem with underlying favourable conditions."*

We are not in the game of picking winners. Government must not intervene to "tilt the market" in favour of specific firms, but in a small developing economy like ours, engaged in a process of integration in the global economy, scarce resources should be invested where they are most likely to yield attractive returns.

Government and Private sector will need to work hand in hand to build the international profile and awareness about the proposed industry clusters that we are proposing. The concept of seamless BRANDING between industry and the country image will be critical in creating the kind of synergy that will support the development of the industry.

Finally we must emphasize that the success in implementation of the Road Map is not realizable in a policy vacuum. Important questions concerning trade policy issues or the delocalisation of a substantial part of the "basic production" capacities to neighbouring countries will have to be dealt with. These issues will be important because they will seriously impact on the critical mass and consequent economies of volume and scope that is needed to make a success of the proposed Road Map.

Rajiv Servansingh has been appointed Regional Director for the Board of Investment in New Delhi, India, effective in October. This article is a digest of a recently published document bearing the same title.

Don't bet your entire farm on commodities

By Christopher Tan

Commodities are hot, or at least everyone is saying they are. But are they really? Let's first try to understand what commodities are. They are "raw materials", "natural resources", "hard assets" and "real things" that surround us. There are soft commodities such as wheat, corn, cotton, soybeans, cocoa. Base metals such as lead, copper, aluminum and zinc. Precious metals such as gold, silver and platinum. Energy such as oil and natural gas. In fact there are about 80 types of commodities listed in the commodity bible known as the Commodity Research Bureau Yearbook. So what drives commodity prices? Well, mainly this – Demand and Supply.

There are always unlimited demands but limited supply of these commodities and as such, any factors that cause an increase in demand or reduce the supply will drive the prices of these materials. Understanding the demand and supply situation will allow us to be a better investor of commodities. When demand is greater than supply, commodity prices will soar. When supply becomes in excess relative to demand, the prices will fall.

Buy shares in companies that produce commodities

We can be exposed to the commodities market and participate in the rising prices of commodities by investing directly in companies such as Phelps Dodge (US-based copper company) traded on the NYSE, or Chevron Texaco, Exxon Mobil (Oil Company) etc. However, the downside of it is that we are very narrowly focused on a few stocks and that we participate in the risk of the market and the company that may have nothing to do with the commodity itself.

For example, we are exposed to the sentiments of the stock market, government policies, corporate scandals, business risks and so on. Some of the issues such as government policies and political risks can be positive for the price of the commodity in question but negative for the company shares. So in a sense, we are not getting the real advantage of investing in commodities. To diversify company specific risk, we can invest via a mutual fund or a unit trust, which will spread our monies across various commodity companies. This is the most practical for us to have exposure to this asset class.

Invest in countries that produce commodities

When commodity prices rise, the economies of the countries that produce those commodities will grow too. Canada and Australia are two examples of major commodity-producing countries. Both are rich in natural resources and home to some of the largest mines in the world. Brazil is the world's biggest producer and exporter of sugar. Chile is the world's leading exporter of copper. Bolivia is sitting on huge

deposits of natural gas; however, the downside of investing in commodity producing countries is that you are exposed to country-specific risk.

This is especially so when many of these countries are emerging economies and are always susceptible to external and internal threats. For example, any pullback in China will affect countries such as Chile & Brazil, both exporters of copper. China is now the world's greatest consumer of copper. Russia and Nigeria are also extremely rich in natural resources such as oil, but they are politically unstable and facing a lot of internal tensions.

Perhaps, the best way to get exposed to rising commodity prices is to buy the commodity itself. The problem is, where would we store \$100,000 worth of copper, corn or sugar? Fortunately, there are other ways to buy commodities without physically owning them. Besides trading commodity futures on your own which can be risky, especially if we don't understand the game, we can buy commodity mutual funds or unit trust or buy into an index fund investing into a diversified basket of commodities.

There aren't many commodity mutual funds available globally. Example of such a fund is the PIMCO Commodity RealReturn Strategy Fund which takes position in commodities through derivative instruments linked to the Dow Jones-AIG Commodity Index. Index investing is probably one of the cheapest and safest ways to invest in commodities. Examples of these indexes are the Goldman Sachs Commodity Index (a basket of 24 commodities) and Rogers International Commodities Index (a basket of 35 commodities).

Why commodities now?

Because the current demand and supply balance for commodities worldwide is out of balance. During these last few years, Asia boomed and the economies of the rest of the world including the west also grew. The world began consuming commodities at an expansive and carefree rate. Years of cheap oil and relative cheap cars had everyone buying MPVs and SUVs. Many Americans also began building big houses which requires lots of energy for heating and cooling. Big cars and houses also ate up huge supplies of lumber, steel, aluminum, platinum, palladium and lead for vehicle batteries.

With the economic recovery of Asia after the Asian crisis in 1997, demand for energy and industrial metals sector increased. China, the world's fastest growing economy and the factory of the world, is gobbling up commodities like never before. They are now the world's no. 2 consumer of oil and the number 1 consumer for copper and steel. China is also importing soy from as far as Brazil and Australia. As demand increases, worldwide supply of commodities

is diminishing.

No major oil field has been discovered in the world for more than 35 years. The giant ones like the Alaska's giant North Slope Reservoir are declining in production. US have not built a new oil refinery since 1976 and domestic refineries have actually decreased. Oil rigs for the purpose of oil and natural gas exploration have decreased too. Oil is getting more and more expensive to find.

The production of natural gas has not kept pace with demand and like oil fields around the world, the known gas deposits are getting on in years. New deposits have been identified but, like new oil, the gas is deeper and more expensive to extract. Gas fields in Canada and the northern slope of Alaska are still without the pipeline infrastructure necessary to speed the gas to market.

Regarding metals, no new mine shafts have been opened in 20 years worldwide. As the demand for copper, silver, iron ore, aluminum, palladium and lead increases, no new mines are available. But even if there are new metal mines, there are no new smelters to make them available.

Sugar supplies are diminishing and sugar has now become an energy commodity. It is used for the production of ethanol; a clear alcohol that can be used in its pure form to power vehicles with special engines or blended with gasoline to produce "gasohol". More than 60 percent of the world's ethanol is produced from sugar. Brazil has been using half its sugar production to power the nation's cars. Ethanol use is also increasing in the US, though most of it is made from corn. With more sugar and corn in the tank, it just means higher prices for these commodities.

Low supplies, increase demand and nothing in the pipeline means rising prices for commodities.

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Published by PluriConseil Ltd

Director: Eric Ng Ping Cheun

Address: 27, Mgr. Gonin Street, Port Louis, Mauritius

Tel: (230) 294 8800 / 213 6719

Fax: (230) 234 2761

Email: conjoncture@pluriconseil.com

Website: www.pluriconseil.com

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Trois impôts libéraux

Par Eric Ng Ping Cheun

La loi de finances 2006 prévoit l'introduction d'un impôt plat de 15% sur les revenus des entreprises et des particuliers en 2009-2010. Il n'y aura alors plus d'impôt progressif. Devant la détermination du gouvernement d'aller de l'avant avec l'impôt sur les intérêts et la National Residential Property Tax, certains commencent même à regretter qu'il n'ait pas choisi plutôt de relever le taux de la taxe à la valeur ajoutée (TVA). Le ferait-il que les conséquences seraient, selon nous, dramatiques, car c'est toute l'économie mauricienne qui serait pénalisée. A cela nous préférons trois impôts libéraux, ce que nous suggérons dans un article écrit pour Business Magazine il y a quatre ans déjà, soit le 24 avril 2002, sous le titre "Quand l'Etat manie l'arme fiscale". Nous en reproduisons, ci-après, des extraits.

Le respect des contrats, la protection de la personne et la protection de la propriété justifient une imposition fiscale

La taxe générale qu'est la TVA offre l'inconvénient de pouvoir être augmentée trop facilement, tant par son taux que par son assiette fiscale. Il est impensable que "la TVA aide à combattre l'inflation, à réduire la consommation". Ce qu'on aurait pu attendre d'une hausse de la TVA, c'est qu'elle fasse jouer l'effet de substitution entre les produits consommés : ce ne sera pas le cas à Maurice, puisque la TVA est applicable sur les produits domestiques comme sur les produits importés.

De plus, la TVA est imposée après l'inclusion des droits de douane dans le prix du produit importé. Comme notre pays s'avère être un importateur net de produits, des taxes

générales sur la consommation ne peuvent qu'alimenter l'inflation importée et exacerber des pressions sur la roupie.

L'impôt progressif sur le revenu, proposé par Marx et Engels en 1848, offre à l'Etat un outil commode de redistribution du revenu. John Stuart Mill décrivait l'impôt progressif comme "une forme adoucie du vol". Il serait plus juste de le remplacer par un impôt proportionnel sur le revenu à taux uniforme appliqué à partir d'un certain seuil d'imposition. L'Etat ne perdrait pas totalement l'avantage de la progressivité avec l'impôt proportionnel, car le montant absolu de l'impôt augmenterait avec le revenu.

Au lieu d'avoir deux tranches fiscales, il serait préférable d'imposer les contribuables de manière égale, soit avec un taux uniforme de 15%. Pour faire plus simple encore, on pourrait éliminer les seuils des déductions et autres exemptions pour que seul le revenu consommé, c'est-à-dire non épargné, soit soumis à l'impôt sur le revenu, qui se transformerait ainsi en impôt sur la dépense. Pour encourager l'épargne, il faudrait moins d'impôt, et non plus de TVA !

Maintenant, où l'Etat va-t-il recouvrer des impôts pour exercer une certaine forme de justice sociale ? Par souci de cohérence, nous dirons qu'il existe trois impôts libéraux qui soient conformes aux fonctions régaliennes de l'Etat, celles-ci étant le respect des contrats, la protection de la personne et celle de la propriété. En premier lieu, on peut imaginer un timbre sur tous les contrats comme prix de l'assurance que l'Etat les fera respecter le cas échéant.

En deuxième lieu, s'appuyant sur le rétablissement du *Law and Order*, le gouvernement peut créer un impôt qui correspond au prix dû par chaque individu pour la protection égale de sa personne. Ce sera une capitation nationale, cet impôt par

tête d'origine féodale, prélevée par l'administration centrale et qui financera la police et les tribunaux. L'assistance publique de l'Etat prendra en charge la capitation des citoyens pauvres. L'inconvénient de la vaste assiette fiscale de la capitation sera contrebalancé par l'uniformité absolue de cet impôt : il sera politiquement difficile à augmenter parce que tous les contribuables seront affectés de manière égale.

En troisième lieu, la protection des propriétés matérielles par l'Etat doit avoir un prix : l'impôt foncier et immobilier. Payé directement par les propriétaires, ou en partie indirectement par les locataires, cet impôt frappera tous ceux qui ont des intérêts tangibles liés au territoire du pays, dans les villes comme dans les régions rurales. Il est préférable que l'impôt foncier et immobilier soit levé par les collectivités locales pour qu'il soit mieux contrôlé par les contribuables qui, insatisfaits des services rendus par l'administration locale, voteront avec leurs pieds.

L'évaluation de la valeur d'une propriété donnée ne nécessitera pas de déclaration signée du propriétaire ni d'inquisition fiscale. L'impôt sera purement indiciaire : il suffit que le fonctionnaire se promène dans la rue et établisse des indices indiscutables et impersonnels (la surface de la maison, le nombre de fenêtres) pour estimer approximativement le prix du marché et calculer l'impôt sur cette base. Pour éviter l'impôt foncier, l'individu investira dans des propriétés non corporelles et augmentera leur valeur.

Ne soyons pas naïfs. Tant qu'on ne limite pas la capacité de l'Etat de lever des impôts, l'Etat sera incapable de réduire véritablement ses dépenses. L'Etat ne se disciplinera pas tout seul. Il faudra lui imposer des contraintes institutionnelles et constitutionnelles pour le forcer à restreindre ses interventions et le retenir dans son domaine propre.

Don't bet your entire farm on commodities

By Christopher Tan (Cont., from Pg 3)

Another reason for investing in commodities now is that historically, there has been a negative correlation between the stock market and commodities. Between 1906 and 1923, commodities were hot but stocks went nowhere. In the 20s, the reverse became true. In the 1970s, commodities were hot again and stock went downhill and in the 1980s and 90s, stocks were hot but commodities were bearish. And now, many believe that it is time for commodities to rise again as equities market become more expensive after a good run since 2003.

Why should you be wary about commodities?

Because everyone is investing into it now. This must surely mean that the markets are peaking.

Although it is true that worldwide economic growth has increased the demand for commodities and depleted the supply, it is also true that speculators have pushed the price well beyond that caused by simply demand and supply differentials.

On oil, the International Energy Agency has downgraded its demand for oil this year. On supply side, there doesn't seem to be a problem also. A lot of the current oil price is due to political risk in the political problem in Iran. When and if this problem subsides, oil prices may fall back to normal level again.

How about economic slowdown? What if Americans stop buying SUVs and MPVs when they no longer have the money to do so due to increase interest rates? What if they stop building huge houses? What if China sneeze and demand for commodities fall?

These are factors to consider before we invest into

commodities.

It is true that commodities are hot now, demand is high and supply is limited. But it is also true that the current prices may be driven by speculative money. A correction may be in the horizon.

It is true that commodities are a good hedge to equities because of its low correlation. Commodities are good for an inflationary environment but equities are not. But don't put all your monies into this asset class. There are other alternative asset classes such as hedge funds and property funds that can provide a good diversification as well. Finally, an asset allocation plan is the best way to get consistent return at a controlled risk level.

Christopher Tan is the Chief Executive Officer of **PROVIDEND**, an Independent Financial Adviser and Investment Manager licensed by the Monetary Authority of Singapore.