CONJONCTURE
www.pluriconseil.com
ISSN 1694-318X
Bilingual Journal of PluriConseil
Numéro 124 : Juillet-Août 2023

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

Why actual inflation is understated

By Sameer Sharma

Just on 15 June, and more than six months into its new flexible inflation targeting regime, the Monetary Policy Committee (MPC) of the Bank of Mauritius finally met to decide on the appropriate monetary policy stance of the central bank and left the key policy rate unchanged at 4.5 percent per annum. The brief monetary policy statement which followed had the MPC take credit for the base effect driven drop in year on year and core inflation which had already peaked in March 2023 and had nothing to do with them. The statement was dovish on the inflation outlook and more upbeat on both local and global growth prospects.

An unchanged stance was not surprising given the level of fiscal dominance over the central bank and given the increasing reliance on draining the foreign exchange market of liquidity via a moderate form of capital controls in order to significantly slow the speed of rupee depreciation. With public debt at close to half a trillion rupees, with the present value of unfunded liabilities on both the Basic Retirement Pension and state related defined benefits plans at more than 300 billion rupees (using the ten-year bond as a discount rate) and with private debt at more than 451 billion rupees (including household debt of 149 billion rupees), inflation is a key factor when it comes to deflating the real value of the debt and saving Mauritius from a credit downgrade.

The Mauritian government not only relies on inflation to bloat its revenues versus traditional taxation, but it also needs inflation in order to fund its liabilities. Given the correlation between inflation and land and property assets locally over the longer term, the private sector is also in on the decision. Was this the right decision and what could the consequences be?

An electronic journal published by PluriConseil Ltd
Director: Eric Ng Ping Cheun
Address: 38, Aldrin Street, Pointe aux Sables, 11128, Mauritius
Tel: +230 289 6719 Fax: +230 234 2761 Email: pluriconseil@intnet.mu

More demand destruction may be needed

In order to assess this decision, one must first focus on the assumptions made by the Bank of Mauritius. When it comes to the global growth outlook, the Chinese economy is beginning to slow again given de-globalization, the continued balkanization of global supply chains and China's own debt fuelled property market woes. The US economy remains more resilient given strong corporate balance sheets and tight labour markets which continue to translate into strong consumer spending despite falling consumer confidence.

However, while long term inflation expectations in the US remain well anchored, services inflation remains high and as base effects fade, the tightness in labour markets and supply chain bottlenecks will keep inflation moderately higher than the Fed's comfort zone for longer and until at least late 2024. The real interest on the Fed funds rate is already at 3 per cent, which is above US potential GDP growth when taking expected inflation into account with real rates needing to remain tighter for longer in order to slow down the economy more and allow the Fed to meet its target.

Demand must slow further in order to meet constrained supply. Corporate profits are beginning to decline now on aggregate, and layoffs, which will finally trigger this long-awaited US recession, are coming next. The delay in these recession inducing dynamics is likely why core inflation has remained so stubborn. The 2023 US recession is likely to occur early next year, and markets are only likely to reprice this by September. The first US interest rate cuts will only occur by the middle of next year at best as recession dynamics take their toll.

The European economy is on its part already in a technical recession with two straight quarters of slightly negative growth. Both consumer spending and investment continued to decline during the same period. Inflation remains too high with real interest rates in Europe remaining near zero to negative. More demand destruction may be needed in order to meet constrained supply via some more tightening and keeping rates on hold until the end of 2024 while the US begins to cut earlier.

Inflation expectations in Mauritius remain loosely anchored

We are in a new normal of heightened market and macro volatility, and central banks will no longer be able to come to the rescue as they did before. The Bank of Mauritius uses Purchasing Managers' Index data as evidence for a recovery in global growth, but it is again missing the plot. It is also ignoring the persistent nature of global inflation dynamics.

In March 2023, Statistics Mauritius predicted a 5 percent rate of growth for the economy and a mere 3 percent increase for the deflator, which was unrealistic. The real growth number was moderately overstated while the deflator number was understated. Three months later, the Ministry of Finance put out a very optimistic and unrealistic real growth estimate which is divorced from that of Statistics Mauritius, even when we adjust for calendar year effects. Given the inflation bias of the budget, the deflator on its part was forecast to stand at more than 9 per cent for the financial year. While that deflator number may seem too high, the Bank of Mauritius came out with a very different and significantly Consumer Price Index (CPI) forecast for 2024.

> Real interest rates in Mauritius remain negative and cannot be defined as tight.

Now the GDP deflator is a broader and more complicated measure of inflation to calculate and should typically be moderately lower than inflation as measured by the more narrowly defined CPI basket. The gap between the BoM inflation forecast and the Ministry of Finance deflator forecast is significantly higher than what can be deemed realistic. The Monetary Policy Committee makes no mention of the budget and its deflator forecast.

It should also be noted here that the current CPI basket weights are still based on the 2017 Household Budget Survey with the weights from the 2022 survey not being made public yet.

Given what has happened over the past 6 years, we would expect the current level of inflation to be moderately understating actual inflation itself. We should also not be surprised by the base effect induced drop in core and year-on-year inflation. Looking at the latest inflation expectations survey conducted by the Bank of Mauritius itself, one-year ahead expectations remain above 8 percent while five-year ahead expectations stood at a very high 6 percent.

Hence, inflation expectations in Mauritius remain loosely anchored and well above the BoMs upper bound target. In sum, not only do the forecasts of different bodies contradict themselves or not take budget factors into account properly, but the market is pricing higher levels of inflation versus the BoM itself.

No long-term trade-off between growth and inflation

When it comes to growth, the potential real growth rate of the Mauritian economy is in the low 3 percent range, and the economy is already showing signs of overheating with tight labour market conditions and still high core inflation rates. The base effect induced impact on core inflation will also fade away early next year, and both year-on-year and core inflation will then move up to between 4.8 and 6.5 percent after briefly falling to below 4 percent during the first quarter of 2024.

Given the extent of the expected output gap made worse by the budget and given market expectations of inflation one year ahead, real interest rates in Mauritius remain negative and cannot be defined as tight. In fact, the stance is very loose and applying the adjusted Taylor rule equation as published in the paper entitled “Towards Full-Fledged Inflation Targeting Monetary Policy Regime in Mauritius” (Ashwin Madhou, Tayushma Sewak, Imad Moosa, Vikash Ramiah and Florian Gerth), the key policy rate should currently be above 6 percent.

However, given complete fiscal dominance fuelled by the need to keep on pumping the debt fuelled consumption model along, real rates in Mauritius will remain negative for longer, which will force the Bank of Mauritius to maintain stronger capital controls in order to offset the budget impact on the current account deficit. The lack of credibility of the BoM however, when coupled with the need to deflate the real value of debt, keep a Moody's rating downgrade at bay (without reviewing a broken and unfair tax system), and populist pension spending will keep inflation well above a required level of 3 percent over the medium term, a level required to maintain external competitiveness.

There is no long-term trade-off between growth and inflation. Predictable and low levels of inflation are good for investment and growth, which is why other central banks do not mind short-term pain for longer term gain. This is unfortunately not the Mauritian approach.

Sameer Sharma is a chartered alternative investment analyst and a certified financial risk manager.

Une économie inflationniste

Par Eric Ng Ping Cheun

On attendait de Renganaden Padayachy une indication d’élections anticipées cette année, mais il parle, dès le début de son discours budgétaire, d’un « *penultimate budget* ». Le gouvernement compte donc présenter un autre budget, mais il peut très bien aller aux urnes plus tôt. Le quatrième grand oral du grand argentier, lui, n’a rien d’exceptionnel par rapport aux trois précédents, mis à part la réforme du régime d’imposition. Il a certes distribué des sucreries habituelles, mais pas au point de nous rendre diabétiques !

Petit changement de forme : le discours commence par les fondations de l'économie, et non du social, soulignant l'objectif d'améliorer la facilitation des affaires et de « *ensure implementation of reforms in line with the recommendations of the World Bank* ». C'est là un signal envoyé aux agences de notation qui s'impatientent de voir enclencher de véritables réformes économiques.

Sinon, le ministre des finances est resté fidèle à lui-même, c'est-à-dire un fort prodigue en aides et subventions en tous genres. Il faut reconnaître qu'il apporte un grand soulagement à la population qui a vu s'effriter son pouvoir d'achat : le revenu minimum garanti, doublement de l'allocation CSG pour certains salariés, hausse de la pension de vieillesse, enlèvement de la TVA sur des produits de consommation et baisse du prix de l'essence.

Même les gros salariés sont comblés avec l'abolition de la taxe de solidarité qui représentait un taux marginal d'imposition de 25% (au-delà du taux normal de 15%). Le pays peut donc souffler en tant que centre financier international, mais il n'est pas certain que la juridiction gagne en compétitivité avec le nouveau système de taxation. Le problème n'est pas tant la progressivité que le nombre excessif de tranches d'imposition (onze). De la simplification de l'impôt plat (*flat tax*) dans le passé, on en vient maintenant à une complexification de l'imposition, susceptible de favoriser la fraude fiscale. Un gain de seulement 0,6 point de pourcentage de la croissance économique risque d'être insuffisant pour justifier le coût additionnel de l'administration fiscale.

> L'expansionnisme budgétaire, soutenant la consommation, va à l'encontre d'une politique monétaire restrictive.

Progressif n'est pas progressiste

Le système fiscal d'un pays reflète la couleur idéologique du gouvernement. Le quatrième budget de Padayachy veut plaire à tout le monde, du plus vulnérable au gros salarié. En même temps qu'il multiplie les aides, subventions et dégrèvements fiscaux, il allège la taxation des particuliers et abolit la taxe de solidarité (ce qui fait perdre Rs 3 milliards au Trésor public, selon Maurice Stratégie). Se pose alors une question fondamentale : une économie peut-elle soutenir à la fois un État-providence de plus en plus budgétivore et une fiscalité relativement légère ? C'est fiscalement impossible, mais c'est possible grâce à l'inflation.

On a qualifié le budget 2023-24 de « socialiste », voire de « gauchiste ». En l'occurrence, le nouveau régime d'imposition, qui est progressif, serait socialement plus juste que le système proportionnel de l'impôt plat, tel que le taux de 15 % introduit par Rama Sithanen en 2007. Pourtant, celui ayant un revenu imposable de Rs 4 millions paiera moins d'impôts sous le régime proposé (Rs 594 800) que s'il était assujetti à un taux uniforme de 15 % (Rs 600 000). Ainsi, les hauts revenus (ceux dont le revenu imposable se situe entre un et quatre millions de roupies) seront moins taxés sous ce système progressif. Progressiste, ça ?

Il est vrai que les bas revenus paieront moins d'impôts sous le nouveau régime fiscal, et que les très hauts revenus dont le revenu imposable dépasse Rs 4,1 millions seront plus pénalisés qu'avec l'impôt plat de 15 %. Dès lors, on peut qualifier la nouvelle philosophie du ministre des finances de « socialisme libéral », comme un clin d'oeil au *Libéralisme et justice sociale* de Jean-Pierre Dupuy (2009). Elle épouse le principe de différence de Rawls, selon lequel les inégalités économiques et sociales doivent être agencées pour le plus grand bénéfice des individus les moins favorisés de la société.

> La progressivité n'encourage pas les employés productifs à travailler plus pour gagner plus.

La progressivité, toutefois, n'encourage pas les employés productifs à travailler plus pour gagner plus. Surtout qu'il existe trop de tranches d'imposition, et que plus elles sont restreintes, plus

elles incitent les contribuables à frauder. Du reste, ils ne voudront pas faire des heures supplémentaires pour basculer dans une tranche supérieure où ils paieront plus d'impôts.

Donc, la progressivité ne favorisera pas la productivité du travail, déjà mal en point. On aura le même effet pervers avec le revenu minimum garanti (Rs 15 000) qui est une extension du salaire minimum (Rs 11 575) auquel s'ajoutent des allocations de l'État (Rs 3 425). Même si l'employeur ne paie que le salaire minimum, il sera sous pression pour augmenter les salaires qui se trouvent juste au-dessus du revenu minimum (entre Rs 15 000 et Rs 18 425) afin de respecter la hiérarchie salariale. Faute de quoi, les salariés qui tombent dans cette catégorie se sentiront dévalorisés et démotivés face à leurs subalternes.

Enchaînement prix-salaire

Ainsi, l'intervention, même indirecte, de l'État dans la politique salariale des firmes, via ses allocations de revenu, ne peut qu'engendrer une hausse des coûts de l'entreprise. C'est ainsi qu'opère l'enchaînement prix-salaire qui fait galoper l'inflation. Elle ne sera pas maîtrisée tant que les autorités continueront à injecter de l'argent dans l'économie sans que suive la production. Même si demain les prix des marchandises importées baissent, il y aura toujours de l'inflation domestique, du fait que le gouvernement donne aux gens les moyens de dépenser.

> L'inflation crée une fausse atmosphère de prospérité en stimulant le PIB en termes nominaux.

L'expansionnisme budgétaire, soutenant la consommation, va à l'encontre d'une politique monétaire restrictive. Avec la dépréciation de la roupie qui résulte de l'accroissement des importations, il devient plus difficile de combattre l'inflation par un resserrement monétaire. Ce n'est pas là une excuse pour assouplir le taux d'intérêt, mais c'est au contraire une raison de plus pour la Banque de Maurice de durcir les conditions financières devant tant de laxisme fiscal.

C'est tout dire que le discours budgétaire ne mentionne pas une seule fois le mot épargne, ni ne donne une estimation du taux d'inflation pour la prochaine année fiscale. On note, néanmoins, que l'inflation dans l'ensemble de l'économie, mesurée par le déflateur du PIB, sera de 9 % en 2023-24, comme en 2022-23. C'est énorme, d'où il est prévu encore Rs 12 milliards de TVA de plus.

Dans une telle économie inflationniste, on assistera à une guerre de surenchères entre tous les partis politiques confondus. Ils aiment l'inflation qui crée une fausse atmosphère de prospérité en stimulant le PIB en termes nominaux. Personne n'osera revenir sur les gratuités, devenues des « acquis sociaux », jusqu'à ce qu'une contraction économique force le gouvernement à une austérité budgétaire. Car c'est en termes réels, hors effet prix, que se mesure la richesse d'un pays.

Enfin, l'inflation déprécie la somme principale et les intérêts d'une dette. Malgré tout, le budget prévoit que « *Rs 1,000 monthly will be provided to individuals who have contracted loans of up to Rs 5 million for the purchase of their home* ». Sur un capital de Rs 2,5 millions en moyenne, cette subvention représente un taux d'intérêt annuel de 0,48 %. À charge pour le comité de politique monétaire de prendre, après six mois d'inactivité, la seule décision qui vaille sur le taux directeur : une hausse d'au moins 50 points de base.

Alors que la pandémie est derrière nous, et qu'on se targue d'avoir réalisé « *higher economic growth, more jobs, higher revenue, higher investment, higher FDI, higher exports* », on ne comprend pas pourquoi le gouvernement maintient les aides dues au Covid. L'inflation se chargera de nous ramener à la dure réalité économique.

Eric Ng Ping Cheun est l'auteur de Maurice la cigale *(2019), en vente chez Bookcourt, Librairie Petrusmok et Librairie Le Cygne.*

La Banque de Maurice toujours derrière la courbe

Par Amit Bakhirta

« Il est en effet difficile pour le fort d'être juste envers le faible, mais agir avec justice a ses récompenses »

Eamon de Valera

Alors que la Fed américaine a fait une pause pour la première fois depuis 2022 (mais a maintenu son ton belliciste) et que la Banque centrale européenne a augmenté de 25 points de base supplémentaires, portant son principal taux d'intérêt à 3,5 % (le plus haut niveau en 22 ans, et sans aucune indication d'une pause imminente), la Banque de Maurice a maintenu son taux directeur à 4,50% - une incompréhensible léthargie qui dure depuis décembre 2022 !

Bien que ce statu quo ait pu être attendu, les conditions monétaires encore raisonnablement souples sont toutefois en contradiction avec tout soutien apporté à la roupie. Ce dernier s'échangeait à Rs 46,17 contre le dollar américain tandis que Rs 50,50 contre l'euro (niveaux les plus bas respectifs de son histoire récente). La banque centrale n'est guère intervenue sur le marché de change jusqu'à présent cette année. Un maigre 50 millions de dollars vendus, contre environ 489 millions de dollars l'an dernier pour la période correspondante (et donc moins 90% d'intervention, d'où la roupie a dégringolé de 9% vis-à-vis du dollar américain depuis le début de l'année).

Eh bien, compte tenu de nos déficits commerciaux et courants et du resserrement des réserves de change, il n'est pas étonnant que toute appréciation reste une réalité insaisissable à ce carrefour. Bien que le budget 2023-24 ait été de nature gauchiste, on pourrait supposer que les conditions monétaires sont plus strictes, plus cohérentes, et pourtant, ce n'est pas le cas. Pourquoi cela ?

Les conditions monétaires restent raisonnablement souples

Notre graphique décrit ici clairement les conditions encore raisonnables du marché du crédit.

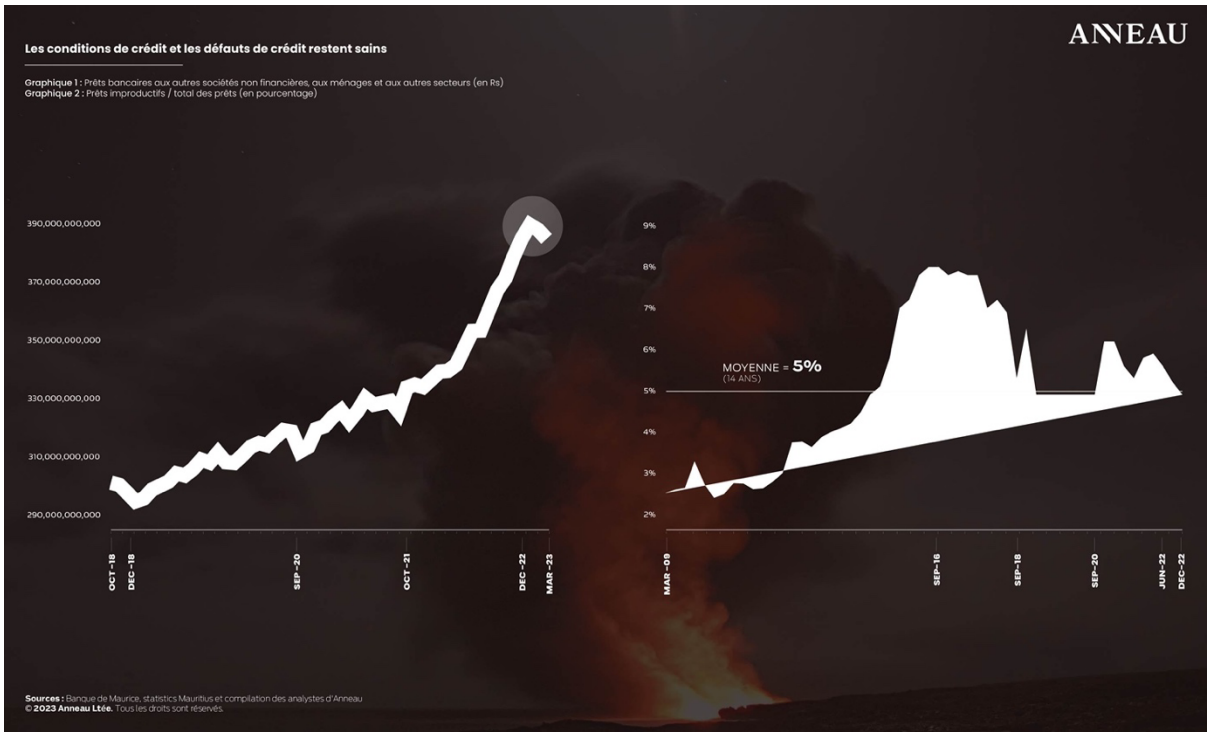
L'extension totale du crédit (dans l'économie hors secteur offshore) commence seulement à ralentir (la croissance du crédit au premier trimestre de 2023 est restée stable, orientée à la baisse, contrairement à une croissance de 1,7 % au premier trimestre 2022). La croissance du crédit aux ménages reste toutefois saine par rapport au premier trimestre 2022, avec une croissance oscillant autour de 2,4 % tandis que l'extension du crédit au logement a augmenté de 2,6 %. Le soutien budgétaire récent aux emprunteurs est susceptible de soutenir l'extension du crédit aux ménages (en particulier dans le segment des bas revenus).

Les niveaux de prêts non performants (indicatifs des défauts de crédit dans le secteur bancaire), en décembre 2022, oscillaient autour de 4,9 % (une moyenne de 5 % sur 14 ans), encore loin des pics de juin/septembre 2016 de 8 % et des creux de 2,4 % de juin 2010. Les récentes mesures budgétaires relatives à l'abandon de toutes les dettes impayées (y compris pénalités et intérêts) dans le cadre du prélèvement Covid-19 à compter du 20 Janvier 2023 devrait contenir toute pression à la hausse sur les défauts de crédit à très court terme.

Alors pourquoi les conditions monétaires ne sont-elles pas encore resserrées ?

Depuis décembre, nos différentiels de taux d'intérêt vis-à-vis de nos principaux partenaires commerciaux se sont creusés alors que nous avons fait une pause prématurée ! Cela a conduit

la roupie à descendre en spirale à son pire niveau de l'histoire récente (en cours de correction, jamais !).



Et aussi improbable que cela puisse paraître, aucune âme ne semble s'en soucier, ce qui est d'autant plus inquiétant que tout l'impact de soutien des mesures budgétaires annoncées récemment sont susceptibles d'être érodées et l'inflation importée, alimentée davantage (qui aurait dû être sensiblement inférieure à ce jour). Il y a dans notre pays une nette déconnexion entre les politiques budgétaires et monétaires en ce moment.

Avec le récent changement de régime fiscal, à mesure que les marchés de travail et de capitaux s'ajustent et s'optimisent, il semble que les attentes budgétaires soient orientées vers la consommation (c'est-à-dire la taxe sur la valeur ajoutée), mais cela reste à ancrer pleinement et à prouver empiriquement, car l'impulsion à consommer dans cet environnement inflationniste persistant reste tiède. Les prix de l'énergie sont également encore artificiellement et déraisonnablement élevés, ce qui, à un moment donné, explosera probablement, car la vache ne peut être traitée que jusqu'aux os !

Si la roupie mauricienne s'apprécie de manière significative, notre déficit budgétaire gonflera.

L'impact d'une monnaie dévaluée sur le budget et sur les revenus de notre pays, comme prévu, a été important et donc, dans un scénario où la roupie se pivote et ainsi s'apprécie de 10 à 20 % (en supposant un changement dans la politique de change et l'amélioration des fondamentaux et de la confiance du marché dans la monnaie de notre peuple), le déficit budgétaire va gonfler à mesure que la consommation et les impôts sur les sociétés chutent !

> Il y a dans notre pays une nette déconnexion entre les politiques budgétaires et monétaires.

À cela, si nous ajoutons une crise quelconque et un effondrement du prix du pétrole, le double coup dur fera très probablement exploser les finances de notre pays (non, très peu regardent dans cette direction ; une saine philosophie de gestion des risques le devrait, cependant).

Par conséquent, dans ce scénario intéressant, une appréciation matérielle de la roupie (une bénédiction pour notre peuple) est très susceptible de se faire au détriment non seulement du bilan de la Banque de Maurice, mais aussi de celui de notre gouvernement souverain (également pour les grandes entreprises avec des forts revenus en devises ?). Quoi qu'il en soit, la compétitivité de Maurice ainsi que l'inflation importée devraient alors, invariablement, baisser à des niveaux équitables.

Ainsi, la beauté du jeu économique est telle que lorsque nous ne contrôlons pas toutes les variables clés d'une pièce à double face, les résultats plausibles restent dans une existence probabiliste, et cela jusqu'à matérialisation.

Bon ou mauvais déficit commercial ?

En règle générale, si notre déficit commercial reflète un excès d'importations sur les exportations, cela peut être le signe de problèmes de compétitivité, mais comme le déficit du compte courant implique également un excès d'investissement sur l'épargne, il pourrait aussi indiquer une économie en croissance hautement productive.

Si le déficit reflète une faible épargne plutôt qu'un investissement élevé, il pourrait être causé par une politique budgétaire imprudente ou une frénésie de consommation. Ou cela pourrait refléter un commerce intertemporel parfaitement raisonnable, peut-être en raison d'un choc temporaire ou d'un changement démographique. Sans savoir lequel de ces éléments est en jeu, il est peu logique de parler d'un déficit comme étant bon ou mauvais (dans un cycle macroéconomique spécifique). Les déficits reflètent les tendances économiques sous-jacentes, qui peuvent être souhaitables ou indésirables pour un pays à un moment donné.

Par conséquent, pour nous, il est important d'aplanir les impacts spécifiques de la politique de la devise sur les soldes commerciaux et courants du pays et donc, l'impact sous-jacent sur les réserves de change ainsi que sur la compétitivité nationale, et ici les observations sont beaucoup plus confuses au décideur rationnel et cartésien, car les politiques budgétaires et monétaires non coordonnées sont particulières dans ce cycle macroéconomique !

Là où la cohésion s'estompe, la confusion monte…

Conditions de liquidité plus strictes

La déconnexion entre les conditions de liquidité monétaire et de marché a souvent résulté en un excédent même de liquidité. Cependant, depuis 2022, cet excès de liquidité s'est resserré. Ceci est clairement indiqué par les faibles niveaux de liquidités excédentaires en devises étrangères (FCY) sur 3 ans et le ratio de réserve de trésorerie FCY (« Cash Reserve Ratio »).

Notre base monétaire s'est aussi effondrée de 30% depuis décembre. En mars 2023, la base monétaire de Maurice était de Rs 175 milliards. Comme prévu, 2023 est l'année où le pincement devrait se faire sentir, car nous prévoyons des conditions de liquidité plus strictes jusqu'au quatrième trimestre.

Tout le monde n'aime pas une roupie forte. Ainsi, nous pouvons noter que si les conditions monétaires dans l'économie restent toujours accommodantes, les conditions de liquidité, en revanche, commencent à s'affaiblir, surtout, supposons-le, avec la contraction de la base monétaire et l'évolution des outils de mise en œuvre des politiques vers des émissions/adjudications beaucoup plus courtes et plus fréquentes.

Il est encore peu probable que la devise connaisse une amélioration significative, du moins à très court terme. Un régime monétaire faible, au fil du temps, détruit la compétitivité d'une nation.

*Amit Bakhirta est le fondateur et CEO d'*Anneau*, une société de services financiers (www.anneau.co).*

For a Council of Professional Valuers

By Kentish Moorghen

Very often the presentation of a budget is viewed as political motives. To my opinion, we must think beyond that and have a constructive attitude to recover from the worst two years we have all been through.

It is a fact that the global economy has still a long way to go to get out from that "fragile" environment. However, it is important to point out that confidence has been improving after the unprecedented slowdown due to the pandemic. It is normal that measures should be taken to alleviate the pressure and come forward with measures that will make the economy conducive for development and growth. In the same breath of reconstruction, we should not ignore the fact that at a point in time a rebalancing of the incentives and measures should be considered so that it is not taken for granted that they will always exist.

Inflation, which is of a great concern, is expected to slow down when we refer to the forecast of reliable and capable economists. As a real estate professional, I will prefer to venture on how the incentives related to the real estate industry can help in the reconstruction process and how the industry can contribute positively to the gross domestic product (GDP).

For many years incentives around real estate was with regards to registration duty and land transfer tax. In one budget it will be removed and yet in another one it will be reinstated; and this has been going on for many years. However, the extension of the Home Ownership Scheme is a laudable effort and in a disguised way a zero-rated registration duty for transactions up to Rs 10 million. I stress the fact that most of the transactions emanating from the middle-income earners is below Rs 10 million. I am of the opinion that this scheme should have been applied not only on sales through the VEFA structure, but should have been extended to "Société Civile Immobilière d'Attribution" as well. This incentive would have given some impetus to small developers as we are well aware that using VEFA as a structure is not only expensive but also ambiguous.

> It would be crucial that there is a proper legal framework for property valuers.

Inflation, disruption in the supply chain and high volatility in the cost of construction materials have led to many housing projects being either abandoned or scaled down. Coupled with that is the rate of default with regards to loan repayments because of increase in interest rates. I believe that this is a major issue which should have been addressed. It is true that the Home Loan Payment Scheme is in a way helping, but it is not enough. A price control mechanism on certain important construction materials should have been implemented.

Since the introduction of the various schemes for attracting foreign buyers, the market has been constantly expanding and the contribution in terms of foreign direct investment (FDI) has grown over the years. Today, there are various options of selling to a non-citizen and, whether we like it or not, it has contributed towards creating that multiplying effect conducive for growth and development.

To conclude, it was a very good initiative to set up the Real Estate Authority some months ago. However, since then, we have not seen anything tangible that the authority has done to professionalise the sector. It is high time that real estate professionals have a proper platform to propose some constructive reforms. One of them which I strongly support is the creation of a Council of Professional Valuers. We have in Mauritius legal frameworks for architects, engineers, quantity surveyors and so on. Valuation playing an important role in both mortgage lending and

assessing property values for accounting purposes, it would be crucial that there is a proper legal framework for property valuers so that valuation reports are strictly done in line with the International Valuation Practice Standards.

Kentish Moorghen is the CEO of Prime Pillar Group.

Turning around loss-making businesses

By Mubarak Sooltangos

The turning around of a company with dwindling or complete loss of profitability is very often beyond the capacity of the normal business driver, otherwise he would have taken timely steps to prevent the downturn. This turn around and salvaging operation is often entrusted to consultant firms. Consultants with an accounting background have a standard set of measures which can be effective in giving short-term equilibrium to the profit and loss account, but which is detrimental to the company in the medium term.

The cost cutting strategy and staff lay off syndrome

Accounting professionals invariably have the reflex of looking at costs as a priority. In eight out of ten cases, the first costs which they tackle are staff costs, because it is an easy task, but this gives rise to several drawbacks. In the laying off of staff motivated by purely financial logic, the most common practice is to go by the “last in first out” principle. This consists of making staff with short lengths of service redundant, in order to pay lesser severance compensations. Consultants forget the fact that they are laying off young people who represent promises for the future and keeping in place older staff who probably are at the very root of the bad performance and the profitability problem.

In their redundancy program they will also target low performers, which is not irrational. In the meantime, good performers would be asking themselves the question of whether they are next in line. They will start looking for alternative jobs elsewhere and they will be successful in this attempt because of their track record. While the end goal of saving a company by staff redundancy may finally be achievable, the very first step which is taken is one which leads to misery. Human feelings and considerations are completely left aside, overlooking the trauma which is being undergone by a head of family losing his job and having at the same time to ensure the upkeep of his family and the servicing of housing loans and other credits he may have taken. We can add to this trauma the impossibility of a relatively unskilled employee, like a store keeper, having reached 45 years of age to find an alternative job.

Alongside this, they will also eliminate staff benefits, which is highly demotivating. I have seen accountants even reducing the number of cups of tea to which an employee was entitled during the day. They will also put an end to advertising activity and expenses, which in their thinking are superfluous expenses having no immediate return.

At the end of this exercise, it may well be that the accounts show an improvement in the magnitude of the loss by sheer cost cutting, however reckless this may be. But in the end, the company is left with a skeleton of a business, without a soul, with underperforming and completely demotivated staff and a portfolio of products which has not been maintained by proper advertising and which is losing market share. In this situation, the management has no alternative than to sacrifice margins and to give more customer credit in an endeavour to “buy sales”. We can imagine the set of new problems to which such measures may give rise, undermining the company’s possibility of going back to cruising speed.

The revenue-driven strategy

We can imagine alternative scenarios based on different strategies, but as long as these stem from theoretical or mathematical reasoning, the end result will remain in the domain of the uncertain. If at the end of the exercise, the result hoped for does not materialise, the business owners will have incurred additional and unproductive expenses which will have worsened their problem. Deep thinking may show a few avenues worth trying.

As a hands-on business driver who has turned around more than 10 sizable loss-making businesses, with a 100% success rate and without ever having destroyed a single job, I will talk about my preferred method, which has proved its worth in different sectors of activity. My strategy is one which is revenue driven rather than cost driven. Generally, a business is loss making when the cost of its structure, namely its personnel, its production and administrative premises, its transport equipment, its bank borrowings and its administrative set up is too high for the turnover, and hence for the gross profit that it generates.

> The image of a company creates confidence in customers' minds to trust the whole gamut of goods that it sells.

When having to improve the bottom line of a company, I lay side by side the financials of the last three years of operation on a spread sheet so that I can get an evolutionary view of the performance over three years as opposed to a static view, for the last year. All the items of expenditure, from year to year, are expressed as a percentage of sales to know which are the expenses that are progressing at a lower rate than the turnover, hence gaining in profitability and which are the expenses that are eating up higher and higher percentages of sales (and hence gross margin), thereby causing loss in productivity.

Essential unlocking of cash

My priority is to look at interest paid because this is the best eye opener. If this charge is too high and on top of this, increasing from year to year when expressed as a percentage of turnover, meaning high and increasing indebtedness, which is a common feature of failing companies, my natural reflex is to look at the following.

1) Stock level, with the aim of determining whether the company is over stocked and in which compartment (raw materials or finished goods), and whether there are stocks of obsolete items which have not been disposed of in a timely manner. With this information in mind, I can take necessary steps to dispose of excess and obsolete stocks, albeit at discounted prices and generate cash, to reduce the interest-bearing borrowings.

2) The level of debtors and more particularly overdue debts. Debtors may be too high for the level of the company's activity, and this may also be the result of faulty collection of debtors, doubtful or irrecuperable debts originating from reckless selling with generous credit terms to customers. This analysis will trigger immediate action by an aggressive collection campaign and if necessary, the hiring of professional debt collectors to do a quick job with a view to unlocking cash which can be used to reduce bank borrowings.

3) Unproductive assets like idle land and buildings and transport equipment from which spare parts have been cannibalised to be used on other vehicles. Sometimes these are heavy burdens on companies, locking up cash and must be disposed of as quickly as possible to obtain liquidity.

4) I also look at the possibility of selling and leasing back productive equipment with a view to unlocking cash. Sometimes it may be advisable to sell assets like land and buildings and continue to operate in rented premises. We must not forget that an ailing business has practically no chance of getting additional bank credit to restructure its activities. The above stripping of assets is essential to unlock cash for more productive purposes.

When the above actions have started to yield their fruits, there is a reduction in financial charges and more importantly cash in reserve (or available borrowing capacity) which will be used to beef up sales, which often requires the injection of cash to support marketing and selling activities. Already the company will be healthier in financial terms, having been oxygenated by fresh cash. Additional interest-free financing can be obtained by a larger recourse to supplier credits if the company's level of purchase from its suppliers increases. This boils down to a "rapport de force" between buyer and seller, which is a common feature in business.

Beefing up sales

Next, I look at sales. If sales are on a downward trend, it may be due to several factors, for example, difficulty to sell due to low product quality or high prices or insufficient credit facilities to customers. It may also mean that the product portfolio is poor or unbalanced, or not properly maintained by regular advertising. In the short term, sales can be increased by improved, but well monitored credit facilities after the cash unlocking operations mentioned above, and price promotions with a view to selling in larger quantities, albeit at lower margins.

Additionally, a review of the remuneration structure of the sales team may lead to higher performance. As a rule, the most productive way of fixing a sales person's remuneration is to give a low basic salary and an interesting rate of commission on sales which will make the commission account for a higher percentage of the total remuneration than the basic salary. If the major component of a salesman's remuneration is variable commission based on sales, it will prompt him to work harder and not have the comfort of having a high and guaranteed basic salary which does not prompt additional effort in selling.

Adding value to the product portfolio

Improving the quality of the product portfolio may take some more time. It may entail the elimination of products having slow rotation combined with low profitability. It may also entail the research of new products having better promises. In my mind, an ideal product portfolio of a sizeable business should consist of three components: (a) fast moving and cash generating items, albeit with low margins, (b) slower moving items with high profitability and (3) optionally one or two lines which give image to the company as a seller of quality goods under nationally or internationally known brands. Very often, the image of a company creates confidence in customers' minds to trust the whole gamut of goods that it sells. As an example, if a company like Nestle launches a new product, the image of the company will itself help the product to have a head start.

Multi-activity conglomerates often burden themselves with small, accessory businesses which they set up to recuperate all the profit that, in their mind, benefits the service providers to whom they give business, namely advertising agencies, transport companies or fleet management agencies. This syndrome, which has the name of "empire building", eventually burdens the mother company with a number of satellite businesses which most of the time end up making losses because their staff has no proficiency in running them. Besides this, they do not stand a chance of getting any business from other big companies which one way or the other, happen to be competing with them on certain lines. When a company faces difficulties, such satellite companies must be disposed of, even at a loss, because this will eliminate all the overheads associated with them and will save valuable management time allotted to their running.

Decreasing costs versus increasing revenue

While the accountant's approach is to downsize the structure and make it cost less, my approach is to squeeze more out of this same structure in terms of productivity to make it produce more revenue. This is a different thinking, and it is geared towards making this same structure work harder to produce 20 or 30% more revenue to be able to absorb more of its cost.

On the cost side, expenses which increase from year to year when expressed as a percentage of sales, reveal a loss in productivity. Ideally, as the activity of a business increases, the percentage of sales going into each item of expenses must decrease, otherwise there are no economies of scale. If it is normal that marketing and selling expenses decrease only marginally when expressed as a percentage of sales, because these expenses are variable and are drivers of sales, administrative expenses must reduce substantially when viewed against increasing sales, because these are generally fixed expenses having no direct relationship with sales.

The option of working on revenue in priority to cost has the advantage of inculcating a winner attitude in staff as they see sales progressing.

The revenue-based strategy relegates to second position the necessity of drastically cutting down costs which affect staff morale and the very activity of the company in the medium term. If revenue is made to increase with the same cost of structure, the cost problem will finally take care of itself, because expenses will eat up a lower percentage of sales and gross profit. Of course, the door to staff redundancy should not be closed definitely, but laying off staff should be a last resort and only activated if there is an imperative necessity to do so.

Cost cutting across the board and laying off staff cause demotivation and take all urge to innovate and work harder out of people.

The option of working on revenue in priority to cost has the advantage of inculcating a winner attitude in staff as they see sales progressing. It also avoids the painful exercise of cutting jobs and creating misery when the need of the hour is better dedication to work and higher productivity in which all helpful hands and brains are needed. It is because of reckless job destruction that company re-engineering has acquired such a bad connotation of being a ruthless exercise. But there are less painful ways of doing this overhauling, which enables smart operators to see light after the tunnel, as explained above.

Essential communication

An essential non-financial measure is to communicate to the staff the exact magnitude of the difficulty and make them take ownership of the problem. Only then we can have a well-knit team working towards one goal with dedication and with the objective of saving their own jobs. Cost cutting across the board and laying off staff cause demotivation and take all urge to innovate and work harder out of people. Working to enhance revenue, and keeping staff aware, at regular intervals, of the progress made, creates a winner attitude in them and an urge to work harder, with brains and dedication because, at the end of the day, they are toiling to salvage their company and to save their jobs.

I have tried this revenue-based strategy of turning around distressed companies over and over again, in different sectors of activity, and it has proved to be the best strategy, which is a forward looking one, an aggressive one as opposed to a defensive one.

Mubarak Sooltangos (msooltangos@gmail.com) is a business trainer, a strategy and management consultant and author of Business Inside Out *(2018) and* World Crisis – The Only Way Out *(2020).*

Mixed messages from Powell

By Ryan McMaken

The Federal Reserve's Federal Open Market Committee (FOMC) left the target policy interest rate (the federal funds rate) unchanged at 5.25 percent. This "pause" in the target rate suggests the FOMC believes it has raised the target rate high enough to rein in price inflation which has run well above the Fed's arbitrary two-percent inflation target since mid-2021.

Yet, at Wednesday's press conference announcing the FOMC's decision, Fed Chair Jerome Powell also claimed that "Inflation remains well above our longer-run 2 percent goal" and "inflation pressures continue to run high and the process of getting inflation back down to 2 percent has a long way to go."

Moreover, according to Powell, the labor market is red hot, with Powell stating "The labor market remains very tight" and "labor demand still substantially exceeds the supply of available workers."

The Fed wants it both ways

Both of these sentiments suggest that the Fed should keep allowing the target rate to rise. After all, if job demand is so high, that means continued increases to wage costs for employers plus more consumer demand for goods and services. That suggests more price inflation. Meanwhile, if measures of price inflation show that we have "a long way to go" that also suggests the Fed should keep allowing rates to rise.

In other words, all the facts presented by Powell himself point to a need for the Fed to stop pushing down interest rates and let them rise further. Yet, the Fed, for some reason, has decided now is a good time to hold the rate steady at 5.25 percent.

The Fed is certainly sending mixed messages, and apparently wants to have it both ways. Powell wants to announce he and the FOMC are firmly committed to combating price inflation by allowing interest rates to rise—and, by the way, allowing more securities to roll off the Fed's $8.3 trillion balance sheet. At the same time, Powell also wants to claim that now is a good time to pause on rate hikes, even though the Fed's favored PCE measure of price inflation is more than double the Fed's target rate of two percent.

Of course, the reason for muddled messaging is not completely mysterious. The answer lies in examining the political situation. Fantasies about "fed independence" might blind some observers to the reality, but the Fed is a profoundly political institution and must juggle a variety of political pressures. As it is, the Fed must seem like it is "doing something" about price inflation while simultaneously avoiding any moves that will cause the economy to slow to the point where it becomes politically problematic for the administration. The incoherence we now see from Powell is a direct result of the Fed's desire to send several conflicting messages at once.

The Fed rarely resumes substantial hikes after a "pause"

For cynical veteran Fed watchers, the pause immediately raises the question of whether or not this will turn out to be a permanent pause, followed in, say, six months by a drop in the target interest rate. After all, historical experience shows that when the Fed "pauses" it rarely goes back to any sort of sustained period of monetary tightening.

Over the past thirty years, there have only been a few occasions during which the Fed paused for more than a single month, and then went back to allowing the target rate to move upward again.

This occurred briefly in 2017, and in 1996 and 1997. In the quantitative tightening period between the Dot-com Bust and the Great Recession, however, the Fed never "paused" longer than a single month. If the Fed fails to allow rates to climb again next month, we'll have good reason to suspect that the Fed is done with this current round of rate hikes.

So, now that the FOMC has "paused," will it ever start up with rate hikes again? The odds are against it, but it is possible. It will all come down to how much the Fed fears that price inflation will again head upward to politically damaging levels. That fear, after all, is the only reason the Fed has ever entertained the idea of allowing rates to rise anywhere near the current level of 5.25 percent. The last decade has shown us that the Fed clings to a bias very much in favor of ramming down interest rates again and again. This is what happened in the ten years of near-zero rates that followed the 2008 financial crisis. Every month, the FOMC would come out and say that the economy was "growing" and was showing "strength" yet repeatedly refused to raise rates.

> The Fed is a profoundly political institution and must juggle a variety of political pressures.

The Fed is making it up as it goes

This Fed's contradictory messages are so apparent that even some members of the media asked why the Fed is bothering to pause at all. As one reporter asked at the press conference, "what's the value in pausing and signaling future hikes versus just hiking? … so why not just rip off the Band-Aid and raise rates today?"

Powell's answer was to admit that the Fed and its legions of economists don't actually know what the results will be of the Fed's tightening, so they're just going to take a wait-and-see attitude. This non-response from Powell highlights the fact that the Fed has long since abandoned its claim to have in place some kind of long-term plan for monetary policy. Gone are the days of "forward guidance" and we're now in the days of "we'll tinker with the economy and see what happens next."

This makes sense given that a look back at the FOMC's economic projects have been very, very wrong in recent years. According to the FOMC's Summary of Economic Projections (SEP) from September 2020, for example, every FOMC member but one predicted that the target interest rate in 2022 would remain at 0.25 percent, with only one member venturing to suggest that the rate might get up to 0.75 percent in 2022. Projections for 2023 were not much more accurate with only three FOMC members predicting that the target rate would rise above 0.25 percent. By March 2022, most FOMC members were still predicting that the target rate in 2022 would be below three percent, and only five members guessed the rate might exceed three percent in 2023. Members were also way off on projections about price inflation and GDP growth.

The Fed has kept the target interest rate very low for a very long time

In fact, the Fed was so committed to ultra-low rates between 2008 and 2023 that the mismatch between price inflation rates and the federal funds rate was larger than anything we've ever seen before. That is, if we compare the federal funds rate to the Fed's favored measure of price inflation – PCE inflation – we see that historically, the target rate was usually above the PCE inflation rate. The exceptions were in periods we know to be inflationary, such as in the mid 1970s under the Burns Fed.

If we look at this gap between the PCE and the target rate, however, the period between 2008 and 2023 really stands out as a remarkably long period during which the target interest rate remained at rock-bottom levels, well below the official price inflation rate. Indeed, this graph shows that going back at least as far as 1960, no other period comes even close to keeping the target rate so far below the price inflation rate for so long. Out of 177 months since the 2008 financial crisis was revving up in August 2008, only 16 months have seen the target interest rate rise above the official inflation rate.

With all that easy money sloshing around for so long, we can see that FOMC members have good reason to fear that inflation has not yet been tamed.

Politics is guiding Fed policy

On the other hand, the Fed will encounter immense opposition to ongoing rate hikes if the economy obviously slows. But how to decide if the economy is getting "bad" or not? A lot will depend on whether or not policymakers at the Fed and in the federal government actually believe that the labor market is as tight as Powell has repeatedly insisted.

The Fed only ever refers to the job-growth data from the establishment survey. Powell conveniently ignores the data from the household survey which has actually shown a collapse in self-employment, and several declines in total employed persons in recent months. The establishment survey's job-growth data is among the few economic indicators pointing to a strong economy right now. Numerous other indicators of manufacturing activity, consumer debt, bankruptcies, and the yield curve all point to economic trouble. If we consider these other metrics – and not just the Fed's rosy labor picture – then the Fed pause is more easily explained: the Fed is pausing out of fear of weakening the economy to the point of alarming voters.

What Powell says publicly and what is actually going on behind the scenes are two different things.

With the Fed, however, what Powell says publicly and what is actually going on behind the scenes are two different things. We can only guess what their real motivations are. It is a safe bet, however, that the Fed is trying to thread a needle here in which it somehow manages to bring down price inflation while also allowing the Biden administration to claim that the economy is in great shape. What happens next will depend heavily on what the regime will feel is necessary to buoy public support for the regime and its current ruling party.

Ryan McMaken is executive editor at the Mises Institute. Culled from mises.org.