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Post COV-19 Mauritius: The start of a Marathon Recovery, not a Sprint

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Introduction

The 2019–20 coronavirus pandemic turmoil, reached Mauritius in March 2020. On the 19th March 2020, the Prime Minister Pravind Jugnauth announced that the country would be under "sanitary" lockdown for two weeks as from 6:00am on the 20th March 2020, which was subsequently extended to the 1st June 2020.

In assessing the nature of the Government response in managing the crisis, we considered amongst others the following :

- Case reviews from China and Europe indicate that Covid - 19 victims with Type 2 diabetes have mortality rates of 2 to 3 times, that of healthy victims;
- Approximately 25% of Mauritius' adult population is diagnosed with Type 2 Diabetes, and a similar number are diagnosed in a Pre-diabetes phase, that is nearly 50% of the adult population being more vulnerable. The comparable number is 5% in the United Kingdom, and 10% in the USA;
- Population density seems to play a significant role in the speed at which the virus is able to spread in the absence of social distancing rules. Mauritius has the 19th highest population density in the world when compared on a country to country basis https://worldpopulationreview.com/countries/countries-by-density/;
- Mauritius' high population density, closed sea borders, good primary healthcare infrastructure and single airport access (let's call these Mauritius' *island characteristics*) also gave it an advantage in that it is relatively easy to manage the spread of the virus through effective lock downs. It should also be noted that **Mauritius declared Covid – 19 free, as of the 11th May 2020.**

The combination of:

- having a thriving democracy;
- a particularly vulnerable adult population (high diabetes prevalence);
- the ability to manage the infection rate because of its *island characteristics*;
- a successful initial lock–down, with no new cases for weeks;
- the resultant low rate of Covid – 19 immunity amongst the Mauritian population.
- narrows the policy options for the Mauritian Government on how to re-activate the economy – it **simply has to be done in a way that limits the risk of re-introduction of new cases from abroad**.

Given the significant role played by the Tourism industry in the Mauritian economy (with the number of international arrivals per annum equalling the Mauritian population), the timing of the opening of Mauritius' airport (without placing quarantine or self-isolation restrictions on inbound travellers) is a key issue, somewhat complicated with Air Mauritius having recently been put into administration.

On the 18th April 2020, Mauritius Prime Minister Pravind Jugnauth, was interviewed on BBC; which profiled the *quick and efficient steps* taken by the Nation to minimise the impact of the virus on the population from a population health protection point of view.

What are the implications for Mauritius as an International Financial Centre

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So, what does the pandemic mean for Mauritius going forward, both domestically and internationally as a developed International Financial Centre (“**IFC**”) ?

- ❖ The international Tourism/Hotel industry is a key contributor to the Mauritian economy at an estimated direct and indirect contribution of 25% of GDP. It has been decimated by the global pandemic and has little chance of recovering in the short term. A more detailed summary of our views are set out in Annexure A below;
- ❖ The Construction and Real Estate industries, which directly employ 7% of the total workforce in Mauritius is severely damaged, and many instances businesses in these industries will be forced to lay off the bulk of their employees. A more detailed summary of our views are set out in Annexure B below;
- ❖ The Textile industry’s international order books will have been decimated by the decline in international retailing (except for online), and its declining contribution to the Mauritian economy will pick up speed without external intervention;
- ❖ Financial services (12% of GDP with a 5.5% growth rate) and Information Technology (5.6%) are likely to be key contributors to the Mauritian economy in future. The groundwork has already been laid with a robust and dynamic communications infrastructure, and there has been a prominent push to establish Mauritius as Africa's FinTech hub. Notably, the successful establishment and subsequent growth of the Mauritius Africa FinTech Hub in late 2018 has spawned an ecosystem that transcends pan-African borders and promotes technological advancement. The Hub's introduction is particularly timely, with the African FinTech sector (according to Ecobank predictions) expected to grow from a $200m market to one worth $3bn by 2020;

- The Mauritian Government has since the outbreak of Covid – 19 announced a raft of economic measures to reduce the economic impact on individuals, and the liquidity squeeze on businesses. A big question remains as to how this will be funded? The recent change in legislation, authorizing the Central Bank ("Bank of Mauritius") to fund the Government directly, and for it to acquire equity interests in companies deemed strategic for Mauritius' economy; gives a strong hint that the Government intends to print Mauritian Rupees as a mechanism to avoid a freezing up of liquidity during the crisis, and as a tool to recapitalize companies (possibly including local banks) that require additional equity to continue operations. ***The proposed legislation is currently being debated in Parliament, (and likely to pass because of the governing party majority);***

- This will put the Rupee under further pressure and will require a fine balancing act as the Mauritian Rupee had weakened against major trading currencies by between 10 – 15% over the past year prior to the outbreak of Covid – 19. Mauritius relies on imports for a very significant percentage of basic consumer products, and food inflation will be a major problem. We see this as a structural problem until foreign exchange earnings from tourism, textiles and real estate sales to foreigners are restored;

- In addition to the Cov – 19 related challenges, the European Commission is set to include Mauritius to its list of Countries that pose a financial risk to the bloc because of anti-money laundering and terrorism financing shortfalls. Under European Union law, banks and other financial and tax firms are obliged to scrutinise more closely their clients, who have dealings with countries on the list. This in itself could jeopardise the attractiveness of Mauritius as a recognised IFC.

Is the Financial Services Sector the catalyst for recovery?

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- The Financial Services sector, comprising of Banks, Insurance and Offshore Fiduciary Service Provider, has been one of the biggest contributors to GDP growth in the past decade, comprising around 12% of GDP pre Covid – 19 and as such a highly valued provider of white-collar jobs to university graduates.
- Covid – 19's impact is expected to be harder on local banks with large Mauritian client bases, than on International banks that are more focused on servicing the offshore sector.
- Using Mauritius Commercial Bank ('MCB') (with a dominant local market share as a proxy for the local banking industry) we make the following observations as to its financial standing pre Cov-19:
  - It was well capitalised with a capital adequacy ratio of 16.6%, shareholders' funds of MUR 48bn, a local Moody's Baa2 credit rating, profit before tax of MUR 10bn, and a return on equity of 19% as of June 2019;
  - It has more than a million clients (20% online), serviced by 2,850 staff members, and 57% of its asset base is in Mauritius;
  - It has 10% of its loan book (MUR 21bn) extended to the Tourism industry, and 7% (MUR 16bn) to the Construction industry.
- Given that MCB has more individual bank accounts than the adult population of Mauritius, it will clearly be considered systemic and be given whatever short-term liquidity support it needs by Government (if it ever requires it). MCB will in our view have to play a crucial role in general providing liquidity to the economy, in particular recapitalising the Tourism Industry in due course.
- The Mauritian Government announced in 2018 that the Banking and Offshore Sector will be transformed from a "Treaty Centric" to a "Substance Centric" jurisdiction (aimed at providing services to Africa), and that the Government is setting up the new regulatory framework and legislation to accommodate these changes.

- In the two decades leading up to today, Mauritius has been very successful in:
  - establishing a small International banking industry with a liquid pool of foreign currency deposits;
  - growing an IFC to provide banking, legal incorporation and ongoing accounting and administrative services to clients mainly in India and Africa;
  - contributing to the setup of a small number of international legal and audit firms;
  - establishing a small number of international asset managers;
  - building up a stock exchange, mainly for local companies, and currently with limited liquidity.
  - Modernising and growing the Financial Service Sector (and employment opportunities in it) makes enormous sense, given that mechanisation of the agricultural industry, and the unattractive wages of the textile industry. Note that Mauritian youth unemployment has grown to 23% during 2019.

We believe the main requirements for the policy of modernising the Financial Services Sector to succeed are:

- an enhanced regulatory framework for banks and offshore service providers;
- improved regulatory oversight;
- an enhanced focus on providing world class training facilities to improve education;
- creating conditions and regulations that make it attractive to import skills in order to grow and deepen the pool of international legal, audit, insurance and fund managers;
- improving the cost, frequency of flights and number of destinations in Africa that can be easily accessed from Mauritius.

- The requirements for creating the right conditions to attract foreign skills to Mauritius often run into local political debate, with citizenship and land ownership being highly sensitive issues. However, the rate of success of this key Government initiative is in our view directly correlated to making it easier for highly skilled international professionals to;
    - obtain residency rights (with employment rights for spouses) with certainty that these can be extended;
    - have adequate choice of schools for their children which award following international qualifications;
    - further relaxation of local property ownership (private and commercial) and ability to conclude leases beyond the current four years by foreigners;
    - clearly understand citizenship qualification rules.

Restructuring Airline Access

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As regards to air links, prior to Covid – 19, Mauritius as a long-haul destination was one of the most expensive air routes in the world. Emirates, which flew two A380's a day into Mauritius, charged on average 20% more for this 6 hour flight than what they charged flying to Johannesburg, an 8 hour flight, effectively a 40% premium. The second busiest air route was Johannesburg / Mauritius, which on a cost per km basis was one of the most expensive routes in the world.

The Mauritian Tourism and Financial Services industries will reap enormous benefit from competitive air travel rates, and increasing the choice of destinations. Given the rising dominance of Ethiopian Airlines in Africa, giving them access to Mauritius will already resolve a lot. We sincerely hope the Mauritian Government takes this to heart in the reshaping of landing rights to increase airline competition.

Conclusion

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In conclusion, Mauritius is facing an enormously challenging period, but its people have, over the past 50 years post its independence, surprised the world and many International economists with the enterprising way it responded in growing and diversifying its economy with limited resources.

This should be seen as a further credit to a country, which in the past has been nimble to adapt its policies in light of Global changes and which have resulted in the Nation being a key player in the channelling of Investment capital, required for the ongoing development in Africa.

Stay healthy.

Brendon Jones

CEO

Annexure A - Impact on Tourism

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- By most credible accounts the development and effective administration of a Covid – 19 vaccine will be delayed until the second half of 2021. Similarly, the availability of accurate, cheap and timely test kits to either test for anti-bodies or for the virus itself seems to be some time off – it is our **thesis that the Mauritius international airport will not be opened** for general tourism until a vaccine has been administered to the population, or an effective test is widely available to receive non-infectious tourists.

- Tourism not only employs 7% of the workforce (approximately 45,000) directly; but is a foundational industry in that many service providers from other industries (food, logistics, construction, banking), depend on it for a significant share of their revenues. Estimates are that the fortunes of over 100,000 workers and many businesses are directly and indirectly linked to Tourism.

- According to Knoema, an international data research and analytical service, Tourism in Mauritius in total contributed around 25% of GDP pre Cov-19. https://knoema.com/atlas/Mauritius/topics/Tourism/Travel-and-Tourism-Total-Contribution-to-GDP/Contribution-of-travel-and-tourism-to-GDP-percent-of-GDP

- Hotels will only start trading once the International airport is open, with no quarantine restrictions on arriving tourists, and it will take between 18 months to 3 years to get hotel occupancies and rack rates to acceptable levels - remember tourists globally are all a lot poorer than before and possibly less inclined to travel to a long destination for a while.

- Tourism accommodation providers will not only have to bear the losses of being closed for the better part of 2020 (and possibly a big part into 2021), but will face significant start-up cost as they will not be able to operate at normal capacity for some time to come.
    - Many Mauritian hotels owners (on average fully geared before the Covid – 19 crisis) are likely to be wiped out financially given the extended period of low/no occupancy, and the relatively high fixed cost structure of running a hotel, and will thus need to be recapitalised before they can open up again.
    - The Mauritian Rupee has weakened between 10 – 15% against its major trading currencies (USD and EUR) in the past year, which will soften the loss of foreign currency earnings for the Tourism industry once it opens up.

Annexure B - Impact on Construction and Real Estate industries

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- As a result of the lock-down, activity in the Construction industry was previously driven by the offshore residential buyers’ market, building of new hotels, and Government infrastructure projects.
- Foreign direct investment (“FDI”) into Mauritian residential property, which comprised more than 50% of total FDI in recent years, is expected to drop off sharply, and demand for high–end residential property (which was in an oversupply position before) will take years to come back, further delayed by the inability of wealthy potential investors to visit Mauritius until the airport re-opens for tourism.
- We expect many smaller residential property developers to go out of business in the coming year, no new hotels to be built, and with the Government applying most of its resources to immediate areas of urgent financial support, limited capital will be available to fund new infrastructure projects.