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MOZAMBIQUE'S TOURISM COMPETITIVENESS

What are the Potential Impacts of the Resource Boom?

October 2014

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Resource Boom?

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Acronyms

AfDB	African Development Bank
AHLA	American Hotel and Lodging Association
AHSM	<i>Associação dos Hotéis do Sul de Moçambique</i>
AHTI	<i>Associação Hotel Turismo de Inhambane</i>
ASINHOS	<i>Associação Indust.Hoteleira e similar de Gaza</i>
BOM	Bank of Mozambique
CDTUR	<i>Associação de Hotelaria e Turismo de Cabo Delgado</i>
CSR	Corporate social responsibility
CTA	<i>Confederação das Associações Económicas de Moçambique</i>
DAI	Development Alternatives, Inc.
DD	Dutch Disease
DINATUR	<i>Direcção Nacional do Turismo</i>
ER	Nominal Exchange Rate
ERPT	Exchange rate pass-through
FDI	Foreign direct investment
FEMOTUR	<i>Federação Moçambicana de Turismo e Hotelaria</i>
FIT	Free and independent traveler
GDP	Gross Domestic Product
IMF	International Monetary Fund
INATUR	<i>Instituto Nacional do Turismo</i>
LAM	<i>Linhas Aéreas Mocambicanas</i>
LNG	Liquefied natural gas
MICE	Meetings, incentives, conferences and exhibitions
MITUR	Ministério do Turismo de Moçambique
MZN	Mozambican Metical
OECD	Organization for Economic Co-operation and Development
REER	Real effective exchange rate
SPEED	Support Program for Economic and Enterprise Development
SWF	Sovereign wealth fund
USAID	U.S. Agency for International Development
USD	United States Dollar
VAT	Value-added tax
VFR	Visiting friends and relatives
WEF	World Economic Forum
WTO	World Tourism Organization
WTTC	World Travel and Tourism Council

Executive Summary

The Support Program for Economic and Enterprise Development (SPEED), with support from the U.S. Agency for International Development (USAID), provides economic analysis to support Mozambique's private sector. SPEED and CTA (the Mozambican Confederation of Trade Associations) have undertaken a suite of studies that explore the potential impacts of Mozambique's natural resource boom on currency appreciation, competitiveness, the Mozambican labor market, and core economic sectors, namely, agriculture, manufacturing and tourism. The full set of reports is available from www.speed-program.com

Tourism's has the potential to make a significant contribution to the Mozambican economy not only through foreign exchange earnings but also through employment creation and socio-economic development in rural areas. Currently the sector employs 270,000 people and represents 3.4% of the country's gross domestic product (GDP).

The Mozambican tourism industry remains a small player in the international tourism market, receiving fewer visitors who in turn spend less when in the country, when compared with rival destinations. Firm profitability is affected by a series of enabling environment constraints which result in higher operating costs and make it more difficult to attract customers and therefore, increase revenue, than it would be in rival destinations such as Tanzania or Mauritius. This study shows that tourism in Mozambique is currently broadly uncompetitive and seen by visitors as having unreliable infrastructure, low levels of service, and a poor reputation for security. The problems which the sector currently faces are likely to be exacerbated by the resource boom and potential onset of Dutch disease.

The study analyses two key tourism value chains – corporate tourism and leisure tourism. A sample set of firms from these market segments was surveyed and survey results were fed into a model developed for this report. The model allows manipulation of figures based not only on the potential effects of Dutch disease (currency appreciation and labor cost increases) but also on policy reforms. This allows analysis of the potential cost-benefits of reforms both currently and under Dutch disease scenarios. The analysis is conducted in financial terms from the perspective of the firms, considering both operating costs, and opportunity costs stemming from business environment constraints.

Profitability is estimated in “economic” terms, i.e., valuing all factors of production and intermediate inputs, the opportunity costs of their use as well as the costs of any applicable taxes. The profitability analysis also presents sensitivity analyses of the potential impacts of (a) a 9.6 percent nominal strengthening of the metical (derived from IMF forecasts), (b) a 50 percent nominal strengthening of the metical from 30 MZN/\$ to 20 MZN/\$,¹ and (c) a scenario that

¹ At 30 MT/\$ 1 metical equals 0.03333 USD. Appreciation to 20 MT/\$ means that 1 metical equals 0.05 USD. The increase in value is 50 percent (0.05/0.03333 = 1.50).

repeats these metical appreciation under conditions of selected policy reforms expected to remove barriers to business competitiveness. The results are summarized below.

Table 1: Scenario Analysis: Corporate Tourism and the Impacts of Dutch Disease

	No ER Appreciation	9.6% ER Appreciation	50% ER Appreciation
PESSIMISTIC POLICY SCENARIO			
Total Revenue	1,390,565,243	1,367,871,218	1,272,367,197
Operating Costs	862,526,005	865,943,334	920,325,450
Taxes	421,930,642	409,919,049	347,807,930
Operating Revenue (MZN)	106,108,596	92,008,835	4,233,817
Operating Revenue (% of Revenue)	7.63%	6.73%	0.33%
OPTIMISTIC POLICY SCENARIO			
Total Revenue	1,622,267,846	1,595,793,411	1,484,380,166
Operating Costs	947,426,430	948,799,206	993,160,827
Taxes	507,289,149	494,055,123	427,135,232
Operating Revenue	167,552,267	152,939,082	64,084,106
Operating Revenue (% of Revenue)	10.33%	9.58%	4.32%

Source: Study Team Analysis

Table 2: Scenario Analysis: Leisure Tourism and the Impacts of Dutch Disease

	No ER Appreciation	9.6% ER Appreciation	50% ER Appreciation
PESSIMISTIC POLICY SCENARIO			
Total Revenue	297,373,921	292,520,779	272,097,138
Operating Costs	320,778,690	323,558,918	345,346,493
Taxes	59,025,052	58,284,218	55,627,058
Operating Revenue (MZN)	(82,429,821)	(89,322,357)	(128,876,413)
Operating Revenue (% of Revenue)	-27.72%	-30.54%	-47.36%
OPTIMISTIC POLICY SCENARIO			
Total Revenue	518,426,143	509,966,410	474,365,037
Operating Costs	520,645,111	520,011,259	527,632,055
Taxes	97,305,571	95,925,471	90,538,851
Operating Revenue	(99,524,539)	(105,970,320)	(143,805,870)
Operating Revenue (% of Revenue)	-19.20%	-20.78%	-30.32%

Source: Study Team Analysis

The baseline analyses (second column from left) suggest that corporate tourism is currently viable (7.63% net profit) within the current cost, revenue and enabling environment framework. The leisure tourism sample, however, suffered major losses in 2013 (-27.72%).

The relative situation remains the same for both samples if the metical strengthens by 9.6%, with profit margins in corporate tourism reducing to 6.73% and losses in the leisure tourism value chain increasing to -30.54%.

In an extreme appreciation scenario (50%), profits for the corporate tourism sector are significantly reduced (to less than 0.5% of total revenue) while losses in the leisure tourism sector increase so dramatically (to -47.36%) that most firms would likely exit the market, leaving a only a few who may be able to compete based on exclusive location, size and other significant advantages.

Where policy reform is undertaken alongside currency appreciation this allows the corporate sector to remain profitable in all appreciation scenarios. However even moderate policy reform is insufficient to assist the leisure tourism segment at even mild rates of currency appreciation, reforms would reduce losses but not result in overall profitability.

This analysis highlights the current crisis state of Mozambique's leisure tourism sector. The corporate segment is basically viable in the current operating environment though it would be somewhat threatened in an extreme currency appreciation scenario. However leisure tourism is the segment most likely to offer opportunities for small local businesses, create employment in rural areas and contribute to the development of a broad-based tourism sector as envisaged in government policies for the sector. Therefore even without the possible onset of Dutch disease there is reason for concern.

The outcomes of this study highlight the need for urgent and sweeping reform of the business environment, which would benefit not only the tourism sector. However specific areas such as air transport monopoly, visa policies, quotas on foreign employees and other labor market reforms are particularly critical for the tourism industry.

The report concludes with key takeaway messages about the importance of recognizing the potential threat of the natural resource boom to tourism competitiveness, particularly the leisure tourism sector, and of building a strategy to anticipate, manage, and respond to it. This will involve plans to manage natural resource-derived revenues directly, build labor productivity and invest in basic and transportation infrastructure that will enhance competitiveness and better resist competitive threats.

The study team strongly encourages CTA and its partners in dialogue to use the modeling tool developed for this study to prioritize policy reform to ensure the survival of the tourism industry. Updating the model, expanding the sample size, and disseminating the results would be a way to engage the public sector in a fact-based dialogue focused on improving the sector's competitiveness.

1. Tourism Competitiveness and Resource Boom Impacts

The present study is part of a series of undertaken by CTA and SPEED to support Mozambique's private sector and government policymakers anticipate the potential impacts of the country's natural resource boom on the Mozambican economy.

Much has been written about the resource boom and its potential impacts on the Mozambican economy – for further details visit www.speed-program.com The main point of discussion is what impact Dutch disease might have on various sectors of the economy, and in this case, tourism. Dutch disease arises in a resource boom situation when a strong surge in macroeconomic growth driven by extractive industries affects a country's export oriented sectors, such as tourism, and appreciation of the local currency takes place effectively reducing the competitiveness of these sectors.

TOURISM SECTOR COMPETITIVENESS

Dupeyras and McCallum (2013) define competitiveness in tourism as the ability of a destination to optimize its attractiveness for residents and non-residents, to deliver quality, innovative, and attractive tourism services to consumers (i.e. providing good value for money) and to gain market share on the domestic and global market, while ensuring that the available resources supporting tourism are used efficiently and in a sustainable way.²

In order to measure the performance of different destinations, a series of key indicators have been developed by different organizations around four categories:

- Industry performance and impacts;
- Ability of a destination to deliver quality and competitive tourism services;
- Attractiveness of a destination; and
- Policy responses and economic opportunities.

Understanding and measuring the relative performance of destinations in terms of competitiveness is challenging. Some countries with similar tourism systems and offers may differ considerably in terms of competitiveness. Developing and implementing policies that promote a competitive and sustainable tourism industry requires a good understanding of the determinants of competitiveness. A good understanding relies on appropriate information to support policy analysis and monitoring.

²Page 7 Dupeyras and MacCallum (2013).

One of the most comprehensive data sets on tourism competitiveness is the World Economic Forum's (WEF) Travel and Tourism Competitiveness Report (TTCR), the most recent edition of which ranked Mozambique 125th out of 140 countries, behind Tanzania, Namibia, Malawi and Zimbabwe. For eleven of the fourteen competitiveness indicators in TTCR (see Table 3) Mozambique falls below the 50th percentile.³

Table 3: WEF Tourism Competitiveness Indicators for Mozambique (2013)

Travel & Tourism Competitiveness Ranking, Mozambique (2013)	
Indicator	Rank (Out of 140)
T&T Regulatory Framework	121
1. Policy Rules and Regulations	90
2. Environmental Sustainability	49
3. Safety and Security	125
4. Health and Hygiene	136
5. Prioritization of the Travel & Tourism	87
Business Environment and Infrastructure	120
6. Air Transport Infrastructure	114
7. Ground transport Infrastructure	134
8. Tourism Infrastructure	106
9. ICT Infrastructure	133
10. Price competitiveness in the T&T Industry	30
T&T Human, Cultural, and Natural Resources	130
11. Human Resources	138
12. Affinity for Travel & Tourism	116
13. Natural Resources	64
14. Cultural Resources	120

Source: World Economic Forum, 2013

The TTCR highlights the presence of negative factors in Mozambique's operating environment which can be expected to result in considerable costs at firm level. Key challenges indicated in TTCR and relevant to this report are quality of human resources (wherein Mozambique ranks second lowest in the world), and transportation infrastructure.

However while TTCR allows for cross-country comparison, its analysis is not easily translated to firm-level because it does not provide quantitative evidence of *how* these barriers to competitiveness impact firms. The data is useful but does not contribute sufficiently to the type of information required to make policy decisions which will enhance competitiveness. One of the aims of the present report is to present a method of analyzing competitiveness constraints to the sector in a way that can easily highlight the potential positive impact of targeted policy reform.

³Page 260-261. World Economic Forum, *The Travel & Tourism Competitiveness Report, 2013*

POTENTIAL NATURAL RESOURCE BOOM IMPACTS ON THE TOURISM SECTOR

As the foregoing indicates, the tourism sector in Mozambique already faces a number of challenges without having felt the full effects of a natural resource boom.

The specific ways in which natural resource booms affect different sectors varies from place to place. Taking account of the composition and price structure of Mozambique's tourism industry as analyzed in TTCR two specific effects are likely to have the greatest impact:

- Appreciation of the country's exchange rate
- Increase in labor prices, particularly for skilled labor

DUTCH DISEASE EFFECT #1: APPRECIATION OF THE METICAL

Despite the large, persistent flows of investment and extractive sector revenues, Mozambique has yet to experience the rapid currency appreciation forecasted by many. This is likely caused in the short term, by revenue flows from mega-projects being off-set by the significant costs of start-up.⁴ These counter-balancing forces are not likely to last long, however. As mega-projects transition from start-up to operation, their revenues will greatly exceed import costs. Likewise, industry consolidation is a one-off phenomenon and will not support continuous future increases in productivity. The metical can therefore be expected to appreciate further as these trends take hold, making tradable goods and services, such as tourism, more expensive relative to their foreign competitors.

Barring significant productivity increases in the tourism sector, it is likely that the quality of tourism services will not keep pace with the relative increases in price, thus putting the sector at a competitive disadvantage internationally.

DUTCH DISEASE EFFECT #2: RISING LABOR COSTS

Mozambique's labor market presents a second major challenge to the competitiveness of its tourism sector. Demographically, the workforce is young and under-educated, with 65% of the country's workers under the age of 25 and a mean of 1.2 years of schooling⁵. New workers enter the labor force at a rate of roughly 300,000 a year, outpacing annual job creation by 20,000⁶. Tourism is traditionally a labor-intensive sector and as such is seen by many countries as a key driver of economic transformation, offering a wide range of relatively low-skilled jobs, often in rural as well as urban settings.

⁴ Page 161, IMF, *Mozambique Rising*.

⁵ (<http://hdr.undp.org/sites/default/files/Country-Profiles/MOZ.pdf>)

⁶ OECD and AfDB estimates put annual growth in labor force at 300,000. Mozambique's Ministry of Labor estimates annual job growth at 280,000. (Salinger and Ennis, 2014)

However in a Dutch disease scenario the cost of labor, particularly skilled labor, would be expected to rise thus affecting one of the major overheads for the tourism sector. Therefore while there may not be a reduction in labor supply due to levels of unskilled entrants into the job market, this report assumes that tourism remains vulnerable to rising labor costs at the semi-skilled and skilled end of the market, as well as resulting in overall minimum wage rises which would affect the cost to employers of employing at the lowest skilled end of the labor market.

TOURISM VALUE CHAINS, COMPARATIVE ADVANTAGE, AND COMPETITIVENESS

The tourism industry itself is not homogenous. Instead, like manufacturing and agriculture it can be divided into value chains. Different value chains may offer different types of comparative advantage within a country or region and some value chains may be more competitive than others. Tourism value chains are defined by Webber and Labaste (2010, 9) as follows:

Typically, “value chain” describes the full range of value-adding activities required to bring a product or service through the different phases of production, including procurement of raw materials and other inputs, assembly, physical transformation, acquisition of required services such as transport or cooling, and ultimately response to consumer demand (Kaplinsky and Morris 2002). As such, value chains include all of the vertically linked, interdependent processes that generate value for the consumer, as well as horizontal linkages to other value chains that provide intermediate goods and services. Value chains focus on value creation—typically via innovation in products or processes, as well as marketing—and also on the allocation of the incremental value.

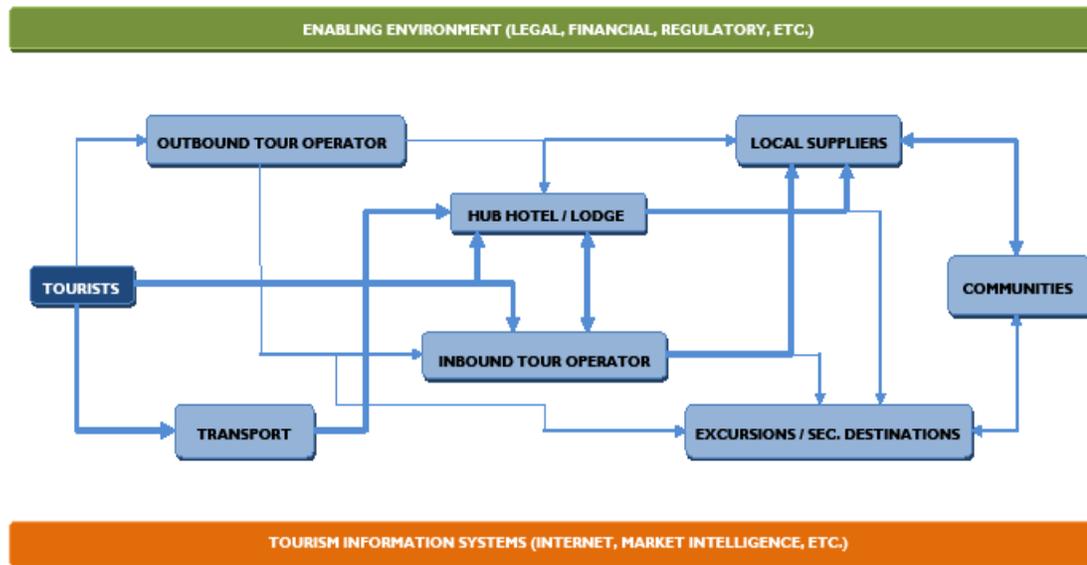
The tourist product is the final service delivered to a visitor. It comprises a series of “experience points” provided by different entities from air carriers and hotels to restaurants and tours. Failure to provide a good experience at any point may undermine the entire experience and accordingly destroy the competitiveness of the destination for that specific value chain. Tourism competitiveness is, therefore, complex and requires the interaction of a diverse set of interdependent actors including the public sector.

Understanding the constraints affecting a country's tourism industry therefore requires an understanding of the role of each value chain component in the overall tourism experience, including the relationship between the various links in the chain, and the performance of service providers, and institutions.

Tourism value chains are structured around the buyer - the tourist. Unlike in other industries, “producing” tourism without a specific consumer, does not take place. While this theoretically means there are potentially as many value chains as tourists, in general and for the purposes of analysis, the sector is broadly segmented according to type of visitor and activity they undertake at their destination. Each segment, or value chain requires different products and services, and therefore, different strategies, providers and distribution mechanisms.

Tourism value chains are usually mapped by economic organization, and industry and location specificity, within the parameters of expenditure patterns and commercial transactions:

Figure 1: Typical Tourism Value Chain Map



Source: Baca and Fertziger (2009)

Analysis along the chain then identifies how value is allocated among the various firms in the industry. To assess operator performance, and thus competitiveness, metrics and indicators are compiled. The approach focuses on the supply-side but also allows for identification of industry-specific constraints. The framework thus developed helps policymakers set priorities for targeted intervention not only at an industry and a location specific level, but also more broadly at national level.

The foregoing guided the process of developing an analytical model for Mozambique's tourism sector. It resulted in the development of a model which was applied to two value chains. These value chains were chosen based on their importance as drivers of growth, and employment, as well as being the two most significant from the point of view of market share. The selected value chains were:

- **Business and corporate travel.** The most important segment for Mozambique in terms of number of visitors, profitability and potential growth. The main destinations for business and corporate travel are Maputo, Pemba, Tete and Beira.
- **Leisure tourism.** This segment has seen its importance and competitiveness significantly reduced. It is currently focused on Ponta do Ouro (south of Maputo), Inhambane (including Bazaruto Archipelago), and Pemba/Cabo Delgado (including Quirimbas Archipelago).

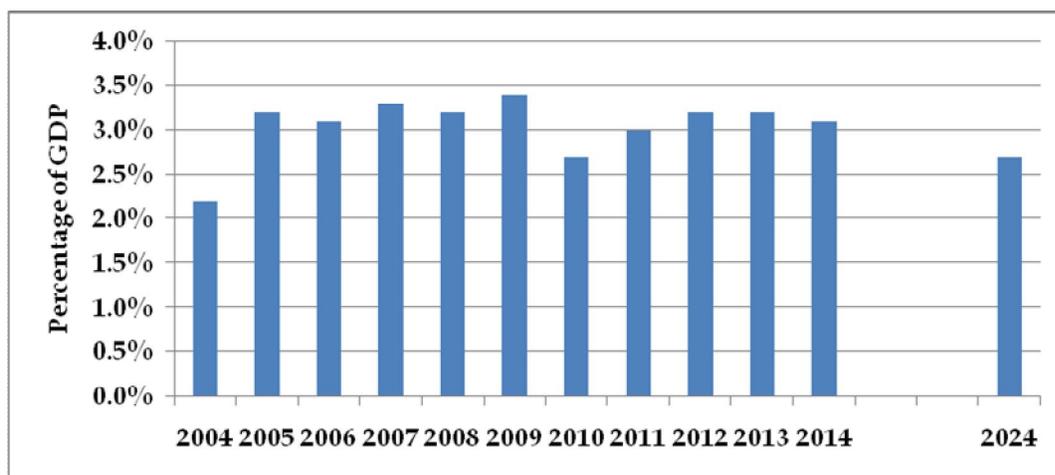
2. Overview of Mozambique's Tourism Sector

In contrast to elsewhere in Africa, the majority of international visitors to Mozambique are regional and corporate travelers. Regional visitors represent approximately 78% of total visitor numbers, compared to 55% in Namibia and 38% in South Africa.

South Africa accounts for the bulk of Mozambique's regional traffic with 45% of all visitors to Mozambique. The only inter-continental markets of any significance are Portugal with 77,500 arrivals in 2013 - a 4% share – and the United States, which represent a 3.5% of the total market. All other inter-continental (Europe, Americas and Asia) markets generate a total of 323,000 visitors.

In 2013, the tourism sector represented approximately 3.2% of total gross domestic product (GDP) and employed around 270,000 people⁷. The sector also generated 8.8 billion Meticaís in exports (i.e. revenue generated by international visitors), representing 6.8% of total exports. However, these figures represent an actual decline in the contribution of the industry to the overall economy. According to the World Travel and Tourism Council (WTTC)⁸, at its peak in 2009, tourism represented almost 4% of total GDP. It is expected to represent less than 2.6% in 2024:

Figure 2: Economic Contribution of Tourism to Mozambique's GDP



Source: WTTC 2014 Mozambique Country Analysis

⁷WTTC, Economic Impact Research, 2013.

⁸*Ibid.*

This relative shift in tourism's contribution to GDP is partially explained by the growth in other sectors of the economy, particularly those related to natural resource extraction. However, as the TTCR highlights, there are barriers to competitiveness related to visitor security, labor productivity, and regulatory reforms that have contributed not only to a relative reduction but also to an actual stalling or retrogression in the growth of the tourism sector. For example, in 2013⁹ the country saw an 11% decrease in the number of international and regional visitors, particularly from the main source markets of South Africa (-12%), Portugal (-14%), the United States (-13%) and the rest of Europe (-12%). Some of the major barriers include:

- **Policy and Regulation.** Tourist visas are expensive (e.g. greater than 100 USD for single entry). The application procedure is lengthy and governed by political – not economic – considerations. Legally-mandated minimum wages, the real value of which increases each year, have the potential to raise labor costs above workers' productivity and result in lower profit margins. The cost of financing is prohibitively high.
- **Air Transport Infrastructure.** The commercial air travel market lacks competition both into and within Mozambique, resulting in high prices. The virtual monopoly of the state-owned air carrier, *Linhas Aéreas de Moçambique* (LAM), makes domestic flights unreliable and costly, limiting the growth of a domestic and regional tourism market. This contributes to preventing Mozambique from becoming anything more than an “add-on” destination to South Africa.
- **Ground Transportation Infrastructure.** Ground infrastructure, including roads, is lacking or of poor quality. For example lack of signage reduces the usefulness of existing roads for tourism purposes. Road usage by tourists is further hampered by corrupt practices of customs and police officials.
- **Human Resources:** The lack of a comprehensive human resource development strategy for the sector results in lack of training in guiding, language, and other services. This is compounded by a lack of tourism training organizations, and of a system of professional tourism qualifications. Aside from labor costs and skill levels, the issue confronting the sector is the absence of a service-oriented culture. Inadequate employee conduct leads to negative tourism reviews and thus to reduced revenue.
- **Prioritization of Travel & Tourism.** The development of the tourism sector comprises only 2.5% of the annual state budget. Given the industry's potential as an engine for job creation, government support is insufficient. Marketing of the country as a destination, by the government, requires additional funding and should go beyond simply having a presence at international trade shows. Little has been done to create a unique national cultural narrative to market the country. This is an essential pre-requisite for building the country's brand and increasing its share of the global tourism market.

These barriers already affect tourism in Mozambique even before the effects of a resource boom are taken into account.

⁹ Ministerio de Turismo. Datos de Referencia (2013)

INDUSTRY PROFILE

Approximately 55% of all tourist arrivals to Mozambique in 2013 (about 842,000 people) are in the country either on business, or visiting friends and relatives (VFR). In the same year, most provinces saw only a very slight increase, or a decrease in the occupancy rates at hotels, with the exceptions of Tete and Niassa:

Table 4: Occupancy Rate by Province in Percentage Points (2009 – 2013)

Province	2009	2010	2011	2012	2013	Percent Change 2012/2013
Niassa	20,7	20,9	19	20,1	28,7	42,8
Tete	34,5	40,1	40,8	35,2	47,8	35,9
Gaza	9,4	8,8	8,6	7,5	7,9	4,8
Cabo Delgado	18,7	18,3	22,5	29,7	30,0	0,8
Sofala	34,9	38,3	33,3	33,1	33,1	0,1
Maputo City	44,3	53,8	62,0	39,8	38,2	-4,0
Inhambane	12,3	9,5	11,2	10,0	9,4	-6,1
Manica	13,0	14,4	13,4	13,0	12,2	-6,2
Zambézia	25,3	24,5	26,3	19,9	18,1	-8,9
Maputo Province	21,0	16,5	17,0	15,7	14,2	-9,7
Nampula	20,5	16,0	19,4	22,4	19,4	-13,2

Source: Ministry of Tourism, *Indicadores de Referencia na Area de Turismo, 2014*.

While the business and VFR segments have traditionally dominated the Mozambican tourism industry¹⁰, the importance of the corporate segment in particular has been fueled by the influx of foreign investment into the gas and mining sectors.

The preponderance of business and VFR tourists has implications for the distribution of tourism products along value chains. Both types of tourist are categorized as Free Independent Travelers (FITs). They organize and customize their trips through purchases of individual products (such as airline tickets) rather than tour-packages (e.g. airline ticket and hotel packaged together). In contrast the leisure segment is predominantly sold through professional customization of exclusive tour packages reserved for the high-yield market (e.g. safaris in the region coupled with a beach extension in Mozambique).

Most travel and tourism products in Mozambique are sold either directly by the service providers (e.g. hotels, airlines), their agents, or travel agencies. Compared to other regional destinations such as South Africa and Tanzania the volume of 'pre-packaged' or 'group' tours is very limited.

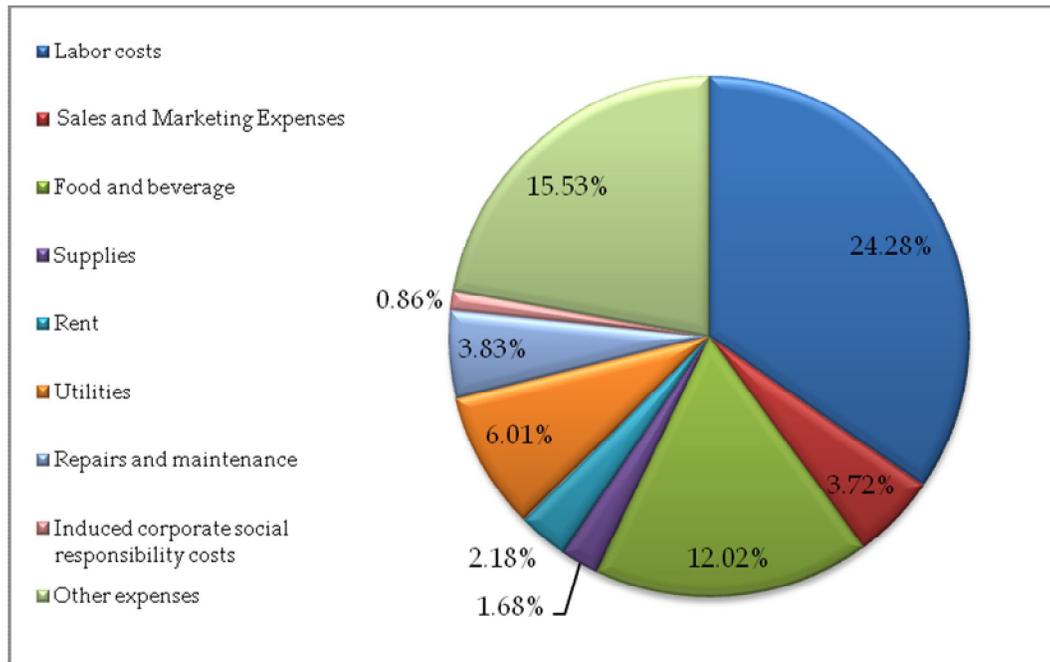
¹⁰“The Tourism Sector in Mozambique: A Value Chain Analysis, Volume I.” (International Finance Corporation (IFC), 2006)

This situation presents both opportunities and challenges. FITs tend to use more local suppliers than ‘group’ tourists, thus allowing more visitors’ revenue to stay in the country and development of a stronger local supply chain and more local tourism business. However, it also limits the growth of a more robust tourism industry because there are fewer market incentives to develop products catering to leisure tourism.

In the commercial distribution system (international tour operators) in the inter-continental markets, Mozambique is primarily sold as an exclusive island beach add-on to other standard travel (primarily safari) packages. This results only in the development of a few pockets of high-value, low-volume accommodation in the island tourism sub-segment.

The profitability of tourism in Mozambique is primarily determined by a handful of variables: labor productivity and costs, costs of imported inputs (primarily food and beverage), and efficiency in the movement of visitors. Analysis for this report identified the main operating costs as:

Figure 3: Operating Costs at Baseline, Full Sample



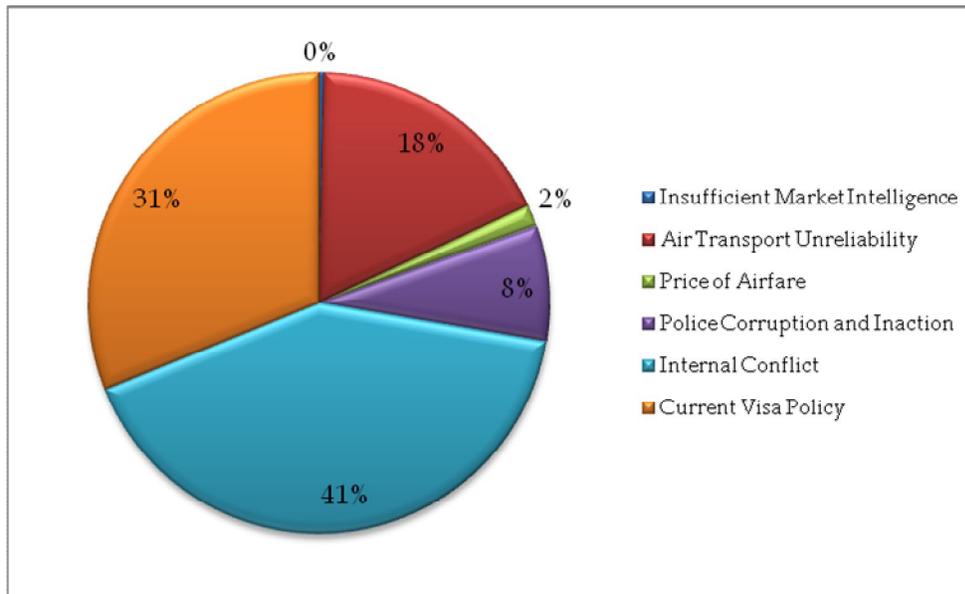
Source: Study Team Analysis

The requirement in tourism to provide personalized and around the clock service for customers means employing large numbers of workers. Low employee productivity makes total labor costs significantly higher for local businesses than in comparable tourism destinations. Total labor

costs as a percentage of revenue are almost 25% in Mozambique, whereas they are 22%¹¹ in South Africa and 18.4%¹² in India.

The efficient movement of visitors is also crucial to the competitiveness of the sector. As Figure 5 illustrates, the main limitations to increasing visitors, and therefore revenue, are all associated with policy constrains:

Figure 4: 2013 Profits Foregone by Tourism Business, Full Sample



Source: Study Team Analysis

Over 90% of profits foregone by businesses surveyed for this report result from security problems, visa policies and the air transport monopoly of LAM. In 2013, these foregone profits totaled almost 83.5 million Meticaiss, (2.8 million USD at current exchange rates), equivalent to almost 3 times the profits achieved by all the surveyed businesses combined.

Based on this survey, Mozambique's tourism sector has extremely low net profitability, which results at least partially from onerous taxes and high operating costs as a result of cost and unreliability of utilities (electricity and water), and ongoing investments in training and security.

Table 5 illustrates the costs and profitability margins of surveyed businesses:

¹¹ 2011 Annual Hotel Industry Survey of Operations South Africa (Horwath HTL Consulting 2012).

¹² Indian Hotel Industry Survey 2010 – 2011. (Federation of Hotels & Restaurants Associations of India and HVS Hospitality Services 2011)

Table 5: Full Sample: Cost & Profitability Estimates

	Full Sample (MZN)	Full Sample (% of Revenue)
Gross Revenue	1,687,939,164	N/A
Operating Costs	1,183,304,695	70.10%
Labor	409,858,012.63	24.28%
Sales and Marketing	62,765,089	3.72%
Food and Beverage	202,864,612	12.02%
Supplies	28,361,679	1.68%
Rent	36,725,236	2.18%
Utilities	101,515,903	6.01%
Repairs and Maintenance	64,619,044	3.83%
Induced Corporate Social Responsibility (CSR)	14,503,522	0.86%
Other Expenses	262,091,597	15.53%
Taxes (National & Municipal)	470,525,979	27.88%
Operating Profit	34,108,490	2.02%

Sources: Study Team Analysis

Under these circumstances, a shift towards less demand elastic market segments (corporate tourism) constitutes a rational business response to operating environment constraints. However, these aggregated data mask differences between the value chains examined (see Section 4) with the business travel value chain showing healthier financial and competitiveness indicators, and the leisure travel value chain being under significant financial stress. The current situation will be exacerbated by Dutch disease.

3. Study Methodology

Figure 5: Study Process Map



SELECTION OF VALUE CHAINS

The value chains analyzed in this study were selected in discussion with CTA's tourism sub-committee (*pelouro*) based on the statistical relevance of the segments according to MITUR's visitor arrivals and purpose of visit statistics¹³, and alignment with CTA's policy priorities for the sector.

Validation of the selected value chains was carried out by key stakeholders from government, the private sector, and other relevant organizations (for full list, see Annex A), and occurred throughout a series of individual discussions culminating in stakeholders' meetings in June and September 2014.

The selected value chains were leisure and business.

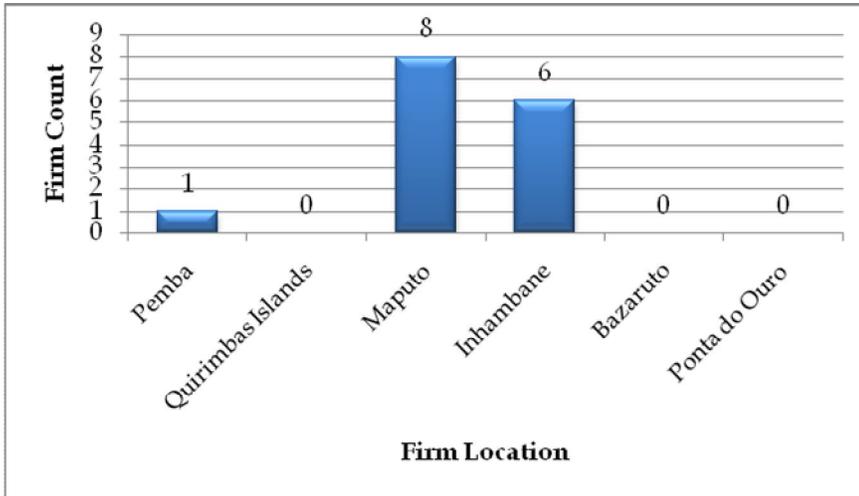
¹³Indicadores de Referencia da Area de Turismo 2013. (Ministerio de Turismo, 2014)

DATA COLLECTION

Data was gathered in Maputo, Inhambane, Bazaruto, Ponta do Ouro, Pemba, and the Quirimbas Islands. 29 firms of 62 approached took part. The sample included both Business (N=15) and Leisure (N=14) tourism value chains across the majority of target locations (see Figures 8, 10, 12, and 13 for distributions).

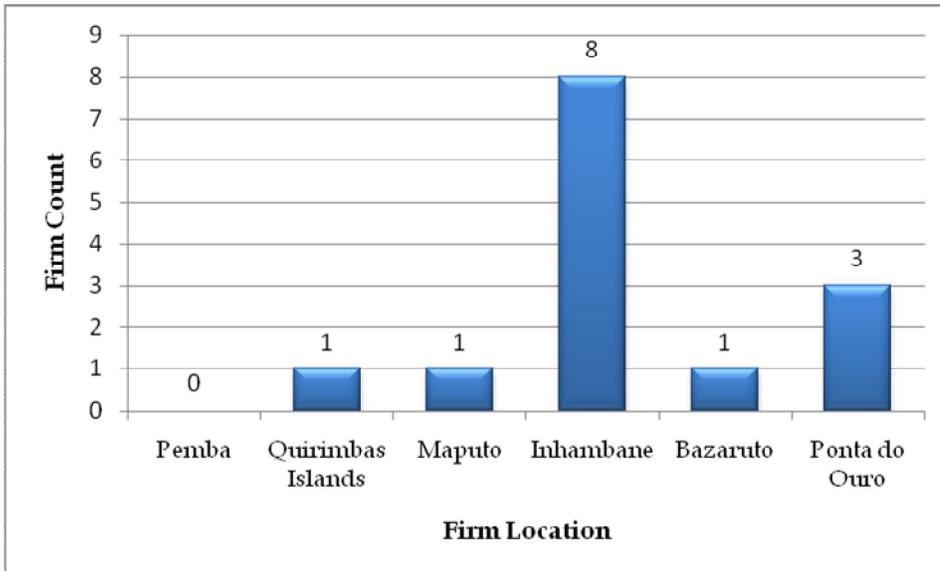
The following figures show sample distribution by segment, location and size:

Figure 6: Business Firm Sample Distribution, Firm Location



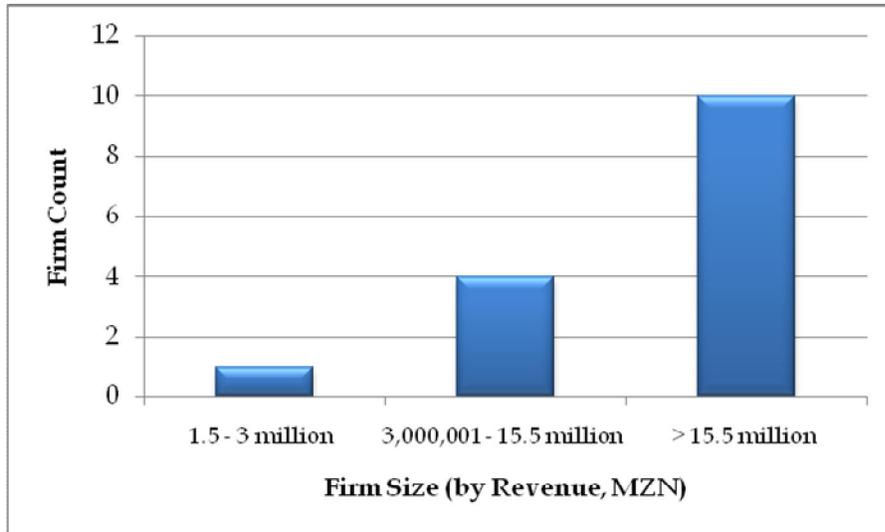
Source: Study Team Analysis

Figure 9: Leisure Firm Sample Distribution, Firm Location



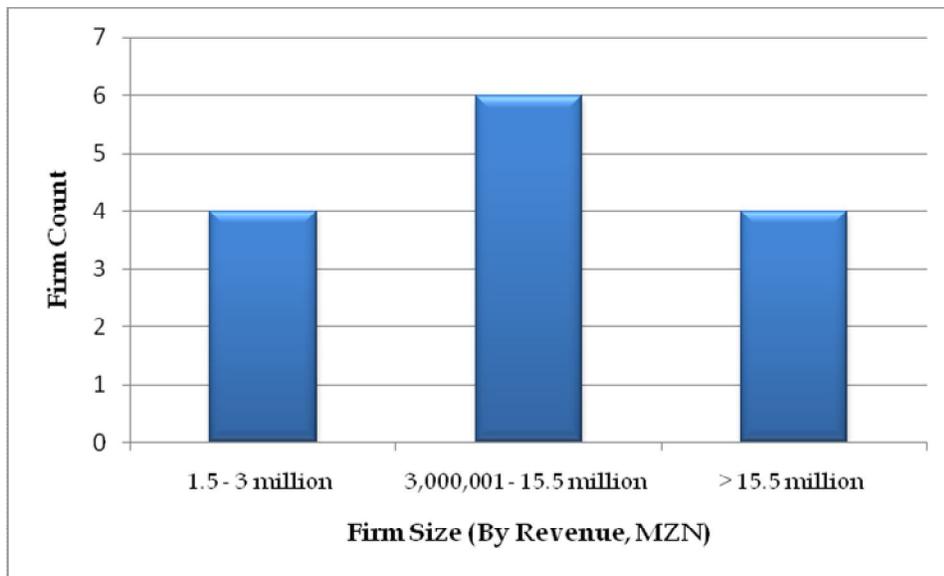
Source: Study Team Analysis

Figure 10: Business Firm Sample Distribution, Firm Size



Source: Study Team Analysis

Figure 11: Leisure Firm Sample Distribution, Firm Size



Source: Study Team Analysis

The survey instrument¹⁴ posed three types of questions: firm characteristics; 2013 financial performance; and non-financial enabling environment issues.

Questions on revenue and operating costs asked for the respective annual totals in local currency. To minimize reporting error, subsequent questions asked the respondents to quantify the

¹⁴ The template survey instrument is included in Annex C.

components of each of these totals on a percentage basis. While a small degree of reporting precision was sacrificed in reporting costs and revenues in this manner, it allowed smaller firms with less detailed financial records to provide accurate responses and prevented an over-sampling of larger businesses.

The non-financial enabling environment questions were designed to obtain estimates of firm-level effects of operating environment constraints within the tourism industry. The study team identified 23 constraints across the 14 tourism competitiveness components as defined in the TTCR (see Table 3). While these vary in subject matter they capture factors imposing additional operating costs on firms (negative externalities), or preventing firms from conducting additional business (opportunity costs). Responses regarding externalities were collected as percentages of total operating costs, while those regarding opportunity costs were recorded as the number of potential customers who were reported to have refused to patronize the surveyed firm because of concerns with the specified enabling environment constraint. These responses were then converted into local currency equivalents using data on total operating costs, total revenue, and number of customers served for each of the surveyed firms. In this way, the implicit costs to businesses were made explicit by estimating the values of non-financial constraints in financial terms (i.e. in local currency units) for each of the 23 identified constraints across the 29 firms. Table 6, below, gives a complete list of the constraints assessed by the survey instrument.

Table 6: Competitiveness Constraints Assessed by Survey Instrument

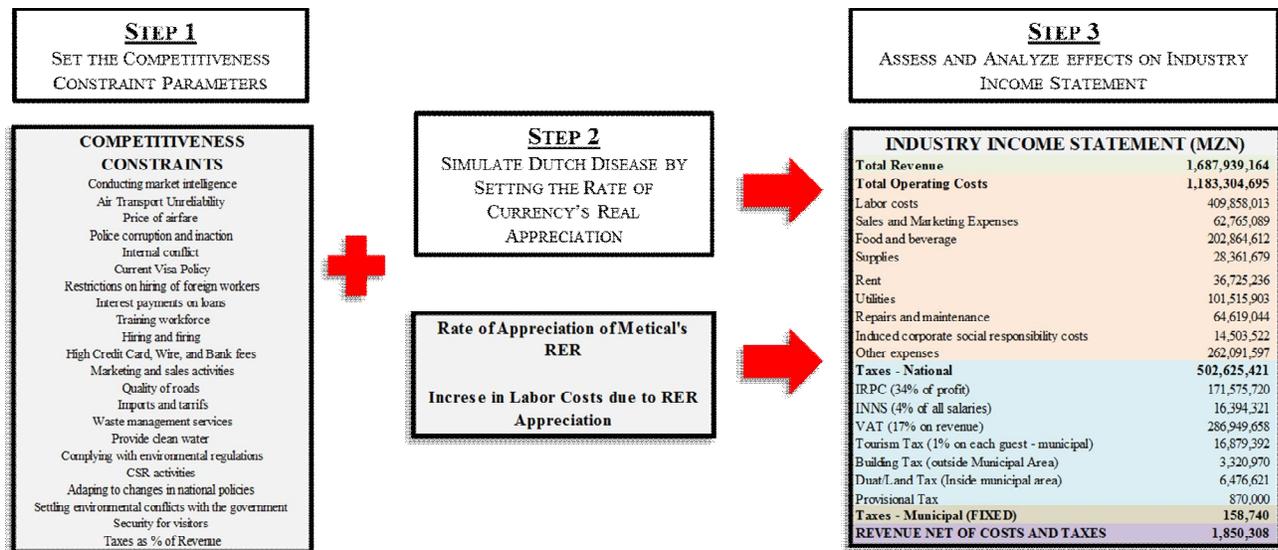
CONSTRAINT	FIRM-LEVEL EFFECT	HOW EXPRESSED IN MODEL (UNITS)
Market intelligence conducted by firms due to absence of third-party providers	Potential commercial activity forgone	Profit (in local currency) not realized
Unreliability of air transport	Potential commercial activity forgone	Profit (in local currency) not realized
High price of air transport	Potential commercial activity forgone	Profit (in local currency) not realized
Corruption and inaction by local police force	Potential commercial activity forgone	Profit (in local currency) not realized
Political strife within Mozambique	Potential commercial activity forgone	Profit (in local currency) not realized
Restrictiveness of visa policy for visitors	Potential commercial activity forgone	Profit (in local currency) not realized
Restrictions on the hiring of foreign workers	Additional, externally-imposed, cost to businesses	Percentage of sample's total operating cost
High interest payments on loans issued by domestic creditors	Additional, externally-imposed, cost to businesses	Percentage of sample's total operating cost
High employee training costs paid by firms	Additional, externally-imposed, cost to businesses	Percentage of sample's total operating cost
Costs associated with the hiring and firing of employees	Additional, externally-imposed, cost to businesses	Percentage of sample's total operating cost
Costs from high credit card, wire, and bank fees, etc.	Additional, externally-imposed, cost to businesses	Percentage of sample's total operating cost
Large marketing and sales expenses incurred due to the absence of coordinated country-wide tourism promotion strategy	Additional, externally-imposed, cost to businesses	Percentage of sample's total operating cost
Quality of roads	Additional, externally-imposed, cost to businesses	Percentage of sample's total operating cost
Import and tariffs costs	Additional, externally-imposed, cost to businesses	Percentage of sample's total operating cost
Costs of providing waste management services	Additional, externally-imposed, cost to businesses	Percentage of sample's total operating cost
Costs of providing clean water	Additional, externally-imposed, cost to businesses	Percentage of sample's total operating cost
Costs of complying with environmental regulations	Additional, externally-imposed, cost to businesses	Percentage of sample's total operating cost

Induced corporate social responsibility activities	Additional, externally-imposed, cost to businesses	Percentage of sample’s total operating cost
Costs borne in adapting to changes in national policies	Additional, externally-imposed, cost to businesses	Percentage of sample’s total operating cost
Costs borne in settling environmental conflicts with the government	Additional, externally-imposed, cost to businesses	Percentage of sample’s total operating cost
Costs of providing security for visitors	Additional, externally-imposed, cost to businesses	Percentage of sample’s total operating cost
Costs of low labor productivity	Costs to businesses of inefficient and poorly educated labor force	Percentage of sample’s total revenue
Tax burden	Additional, externally-imposed, cost to businesses	Percentage of sample’s total revenue

MODEL CONSTRUCTION

The model developed for study provides estimates of the financial health of the sample population of tourism firms under different policy and Dutch disease (DD) scenarios. Its structure is based on that of a traditional income statement and allows for policy and DD variables to be manipulated in a two-stage process. Figure 7 provides an illustration of the analytical process the model uses. To begin, financial data was extracted from the firm-level surveys, cleaned, and aggregated to provide industry-wide total values for each of the primary income statement components: revenue, operating costs, taxes, and operating profit. This captured the current financial condition of the industry’s economic competitiveness and served as the model’s baseline measurement.

Figure 12: Model of Industry Competitiveness in the Presence of Dutch Disease



In the first stage (“Step 1” in Figure 7) competitiveness constraint variables are adjusted to mimic changes in the business enabling environment. These 23 constraints represent the primary pathways through which business is impeded by an inefficient operating and policy environment. Baseline values quantifying financial harm are listed for each constraint (taken from the responses to the non-financial enabling environment questions in the firm-level survey). Thus, improvements or deteriorations in policy and enabling environment conditions are simulated by adjusting the values of each of these constraints from their baseline, resulting in changes to the sample’s income statement (via changes in revenue, costs, taxes, and profitability). Structured in

this way, the model allows for detailed financial impact assessments under a wide array of policy and enabling environment scenarios – allowing for the manipulation of both the number of constraints targeted as well as of their value.

Once the policy environment is configured, the DD effects are simulated by setting the rate of appreciation of the Metical's real exchange rate (RER) ("Step 2" in Figure 7). Setting the RER appreciation rate determines the appreciation rate of the nominal exchange rate (ER) and calculates the induced effects to labor costs and to import and export volumes. The changes in these variables, in turn, cause each of the components of the model's income statement (revenue, food and beverage expenses, labor costs, etc.) to adjust – either in direct response to one specific dynamic (e.g. labor costs in reaction to RER appreciation), or in response to several inter-related processes (e.g. revenue in reaction to both ER appreciation and decreased export volumes).

These calculations rely on partial elasticity estimates from empirical research by IMF staff, and are listed in Table 7, below.¹⁵

¹⁵ It is important to note is that the model in this study uses a combination of partial equilibrium calculations to derive its outputs. The principle applies, then, that the sum of partial equilibrium outcomes does not by rule equal their general equilibrium outcome. While the model outputs in this study are of excellent precision and provide important clarity and insight on the effects and relative importance of potential policy solutions, they by their nature do not capture the totality of indirect effects that would be derived from the simultaneous interaction of multiple variables. Were rigorous, detailed, and accurate data available, a general equilibrium analysis – modeling firm production, household demand, government spending, international trade and balance of payments, etc. – would be able to capture the full array of these interactions (albeit with far less precision). While this limitation is important to acknowledge, it should be clear that the indirect interaction effects not captured, while real, are minimal and do not compromise the model's effectiveness as a tool for policy assessment.

Table 7: Key Statistics Used in the Model Calculations

DESCRIPTION	VALUE	PURPOSE	SOURCE
Import Elasticity to Nominal Exchange Rate Change	0.36	For calculation of the change in various operating costs	<i>Exchange Rates and Trade Balance Adjustment in Emerging Market Economies</i> . IMF (2006) pg. 22
Export elasticity to Nominal Exchange Rate Change	-0.17	For calculation of the change in revenue	<i>Exchange Rates and Trade Balance Adjustment in Emerging Market Economies</i> . IMF (2006), pg. 17
Wage Elasticity to Real Exchange Rate Change	0.40	For calculation of the change in labor costs	Mishra and Spilimbergo. <i>Exchange Rates and Wages in an Integrated World</i> . IMF Working Paper WP/09/44, 2009.
IMF Inflation forecast for 2014-2019 period	5.60%	For conversion of the RER appreciation rate to that for the nominal exchange rate.	Available from IMF's World Economic Outlook Database, April 2014 available at http://www.imf.org/external/pubs/ft/weo/2014/01/weodata/index.aspx
Percentage of supplies imported	85.00%	For calculation of the change in cost of Supplies	<i>The Tourism Sector in Mozambique: A Value Chain Analysis, Volume I</i> . IFC (2006), pg. 51.
Percentage of food and beverage inputs imported	70.00%	For calculation of the change in Food and Beverage costs	Ibid.
Percentage of sales and marketing services imported	90.00%	For calculation of the change in Sales and Marketing costs	Ibid.

Calibrating the sets of variables under Steps 1 and 2 completes the model run. The resulting income statement displays new values for total revenues, costs, taxes, and profit as well as for their more detailed components (supplies, marketing, etc.) The model also quantifies the value of each of the 23 competitiveness constraints calibrated in Step 1 – both *before and after* the imposition of DD dynamics. This allows for analysis of specified policy reforms in the context of Dutch disease and to see how DD blunts (or sharpens) the effects of particular reforms.

In addition, the model's two-stage calibration process allows for analytical flexibility. Policy makers unconcerned with Dutch disease dynamics need only to set the RER appreciation variable in Step 2 to "0" to view the effects of specific policy reforms absent Dutch disease. Conversely, DD effects can be viewed in isolation by adjusting only the RER appreciation variable in the Step 2. While the analysis presented in this study considers only a select few scenarios in order to assess the tourism sector's economic competitiveness, a multitude of permutations exist and should prove useful for analysis and consideration by policymakers. It is to be hoped that this model is useful to practitioners in their efforts to promote the economic health of Mozambique's tourism industry.

ASSUMPTIONS AND ANALYSIS

The study team sought to investigate those potential scenarios that are of greatest interest to a wide variety of constituents. The sample data collected was set as the model’s baseline measurement. Five alternate scenarios varying those policy and DD effects of greatest interest to both policy and business leaders were then selected and run through the model, with the resulting output then compared against the baseline. To do this, both a “pessimistic” and an “optimistic” scenario for domestic policy reform were devised and then each subjected to two different Dutch disease simulations with ER appreciations of 9.6% and 50%.¹⁶ To complement the value chain analysis, however, it was necessary to not only view the full 29-firm sample, but to also disaggregate it according to the *type of tourism* each firm – business or leisure. Table 8 provides an outline of the scenarios run.

Table 8: Scenario Analyses Conducted by Study Team

PESSIMISTIC POLICY SCENARIO		
<u>Scenario:</u> Current Baseline Measurement (No Policy Reform)	<u>Scenario:</u> Baseline + 9.6% ER Appreciation Effects	<u>Scenario:</u> Baseline + 50% ER Appreciation Effects
<u>For Samples:</u> <ul style="list-style-type: none"> • Full (N=29) • Business (N=15) • Leisure (N=14) 	<u>For Samples:</u> <ul style="list-style-type: none"> • Full (N=29) • Business (N=15) • Leisure (N=14) 	<u>For Samples:</u> <ul style="list-style-type: none"> • Full (N=29) • Business (N=15) • Leisure (N=14)
OPTIMISTIC POLICY SCENARIO		
<u>Scenario:</u> Current Baseline Measurement + Selected Policy Reform	<u>Scenario:</u> Current Baseline Measurement + Selected Policy Reform + 9.6% ER Appreciation Effects	<u>Scenario:</u> Current Baseline Measurement + Selected Policy Reform + 50% ER Appreciation Effects
<u>For Samples:</u> <ul style="list-style-type: none"> • Full (N=29) • Business (N=15) • Leisure (N=14) 	<u>For Samples:</u> <ul style="list-style-type: none"> • Full (N=29) • Business (N=15) • Leisure (N=14) 	<u>For Samples:</u> <ul style="list-style-type: none"> • Full (N=29) • Business (N=15) • Leisure (N=14)

The “pessimistic” policy reform scenario assumes no policy changes are enacted to improve the competitiveness of firms in the tourism industry. None of the model variables are adjusted from their current value under this assumption. The “optimistic” scenario limits the number of

¹⁶ The choice of a 9.6% ER appreciation level was made through a combination of IMF forecasts of medium-term RER appreciation (4%) (IMF, *Mozambique Rising*, 2014, page 149) and inflation rate (5.6%) (IMF, World Economic Outlook Database, 2014). The choice of a 50% ER appreciation rate was made to allow comparability with the analyses performed in *Mozambique’s Natural Resource Boom: What Potential Impacts on Agriculture’s Competitiveness?* (Calima and Dengo, 2014)

competitiveness constraint variables adjusted to six and groups these into four competitiveness constraint themes to provide a conceptually clearer illustration for the viewer. The themes are *quality of labor* (aggregation of “restrictions on the hiring of foreign workers”, “employee training costs”, and “costs of low labor productivity” variables), *costs of air transport monopoly* (aggregation of the “unreliability of air transport” and “high price of air transport” variables), *restrictive visa policy* (the “restrictive visa policy” variable), and *costs of violence and corruption* (an aggregation of the “political strife within Mozambique”, “costs of providing security for visitors”, and “corruption of and inaction by local police” variables). These variables represent the majority of opportunity costs borne by the surveyed firms.

To ensure analytical feasibility, the analysis was also conducted under several simplifying assumptions for each of the 6 scenarios. They are as follows:

- 1) **The absorptive capacity of Mozambican economy and government remains low.** The appropriate public investments will not be made in sufficient time or at sufficient scale, allowing for large accumulations of foreign assets and increasing annual government revenue by almost 50%.¹⁷ The Government of Mozambique does not own or have access to sovereign wealth funds (SWF) or natural resource funds (NRF) for the purpose of regulating the appreciative effects of foreign asset inflows, nor will the Bank of Mozambique (BOM) engage in large-scale sterilized interventions to minimize the impact of the increasing foreign assets.
- 2) As service exporters, **Mozambican tourism firms are highly exposed to foreign markets and foreign competition.** This is because (a) the preponderance of their business is in the trade of services; (b) they compete against companies in other countries and thus operate in a fiercely competitive environment; and (c) hold a relatively large amount of foreign exchange in the course of their business.¹⁸
- 3) **Exchange rate pass-through (ERPT) to export prices for tourism firms outweighs the ERPT to import prices for Mozambican tourism firms.** This means that an appreciation will cause imports to become less expensive, but this benefit will be overridden by the loss in profits as firms are forced to reduce their prices to offset this same appreciation. In net terms, the ERPT differential will adversely impact the financial health of tourism firms.
- 4) **All taxes were paid by firms in the sample population.** While respondents were queried about their tax burden, overall response rate was insufficient for use in the model. As a result, a simplifying assumption was made that all firms paid taxes in accordance with prevailing tax law. Calculation of the tax burden was incorporated into the model formulas.

¹⁷ Page 146, IMF, *Mozambique Rising* (2014)

¹⁸ Pg. 28, Biggs (2011).

- 5) **Municipal taxes are fixed.** Survey data and the existing literature on taxation in Mozambique show municipal taxation plays a miniscule role in firms' cost structures. Given the poor quality data and high variation in rates (and in the application of those rates) among municipal tax regimes, it was determined that any effects from changes in the municipal tax burden would be minimal and for this study's purposes inconsequential.

These assumptions attempt to control for exogenous factors and for variables whose significance lies beyond the scope of the report. This allows for a more tractable analytical process and for comparability of scenarios.

A NOTE ON DATA LIMITATIONS

The results of this report should not be construed as statistically or econometrically robust. Such estimates require time, resources, and access to information that are beyond the scope of this work. Beyond this consideration, more comprehensive data and more precise results were precluded by pervasive problems in the Mozambican business environment. **Inconsistent, non-standardized, and poor quality financial record-keeping** by tourism firms severely circumscribes sample sizes, compromises accuracy, and renders thorough analytical treatments almost meaningless. **Low levels of trust in public institutions to ensure fair and transparent competition** prevent many firms from participating (even anonymously) in surveys and other data collection exercises. This also reduces sample sizes, and biases them "upwards" in that the largest and most dominant firms will be more pre-disposed to share confidential business information. The **lack of accurate national statistics** prevents external validation and leaves open the possibility of various biases caused by self-reporting data. Finally, **high levels of firm informality** throughout Mozambique¹⁹ imply that this analysis (or indeed any other that deals only with the formal sectors) may not be applicable to a large swath of Mozambican businesses. Combined, these issues prevent these results from being authoritative and preclude deriving precise and accurate estimates from them (e.g. firm-level productivity, wage growth, demand and supply elasticities, etc.)

This does not mean the results here are without use. The data collected, while not statistically rigorous, does represent the most accurate and detailed picture of the financial health of tourism firms to date. When combined with an understanding of the economy and its business enabling environment (as detailed above), it allows for detailed consideration of possible outcomes.

¹⁹While not a perfect proxy, estimates of labor participation in informal sectors provide reasonable insight into the size of Mozambique's informal sector. In 2013, for example, it is estimated that just less than 95% of the labor force worked in the informal sector. (Page 12, "Mozambique – Labour Market Profile 2013". (Ulandssekretariatet, 2013))

4. Value Chains: Structure, and Potential Impacts of Dutch Disease

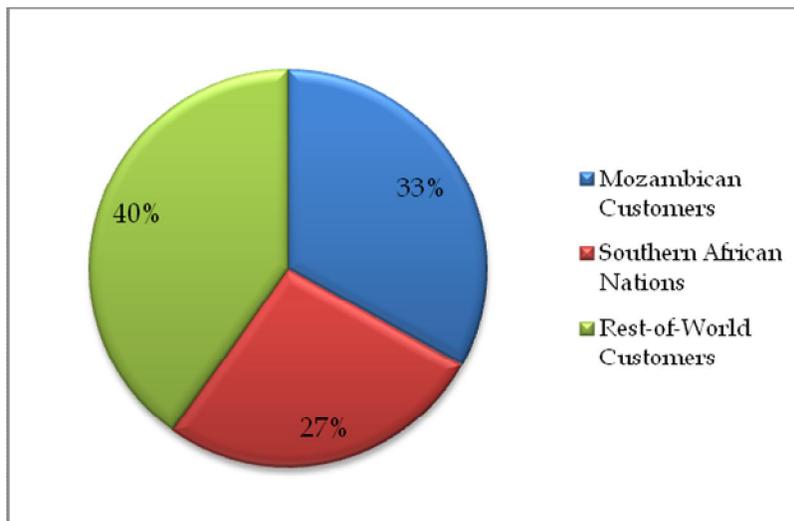
As discussed in Section 1, the profitability of tourism value chains is determined by a range of variables, e.g., productivity and costs of labor, cost of imported food and beverage inputs and efficiency in the movement of visitors. In this report, operating costs as well as opportunity costs (i.e. forgone profit for tourism businesses as a result of policy and regulatory constraints) are analyzed for surveyed firms to identify profitability and highlight points along the value chains where particular constraints arise.

BUSINESS AND CORPORATE TOURISM

This value chain's importance has grown along with foreign investment in extractive industries. In 2013, 312,000 visitors indicated they came to the country on business. Maputo is the main corporate destination, followed by Pemba and Tete. The natural resource boom has supported growth in business and corporate travel in Pemba, Beira and Tete.

The main source markets for this value chain are corporate travelers from the Southern Africa region (27%), Mozambique itself (33%) and the rest (40%) comprising Western Europe, the United States, Brazil and the Middle East. A growing number of international corporate visitors come from Asia, and China in particular.

Figure 13: 2013 Clientele Origin, Business Firm Sample



Source: Study Team Analysis

The predominant sourcing channels for corporate visitors in their country of origin are their own companies' corporate services and to a small extent, travel agencies. Regional corporate visitors, particularly from South Africa, are more likely to secure the services of local travel agents to arrange domestic flights and hotel reservations while domestic business travelers are more likely

to make their flight and hotel reservations as well as coordinate local transportation at their final destination.

Given the emerging importance of Tete, Beira and Pemba as corporate travel destinations, domestic flights constitute a key link in this value chain. Currently, the market is dominated by the national carrier, LAM. The resulting monopoly results in high rates for domestic flights as well as unreliability of service. This in turn, limits the possibility of linking regional and international corporate travelers to the leisure tourism market.

Despite increases in corporate travel, reported average annual occupancy rates are low (ranging from 30% in Pemba to 47% in Tete). Average daily rates in Maputo hotels are reported to have reduced by over 22% since 2011, and average revenues per available room have reduced by 42% since 2011.

Hotel managers surveyed in the business travel sector noted low staff productivity as reflected by a staff of 1.2 employees per room, instead of 1, which is the World Tourism Organization (WTO) industry standard or as compared with staffing levels in countries such as South Africa and India:

Table 9: Hotel Employee Productivity, Business and Corporate Sample

	Mean	Five Star	Four Star	Three Star
WTO Recommended Standard	1 : 1	2 : 1	1.2 : 1	0.8 : 1
Mozambique (Sample)	2.2 : 1	2.7 : 1	2.2 : 1	1.7 : 1
<i>Corporate and Business Travel</i>	<i>1.2 : 1</i>	<i>1.1 : 1</i>	<i>1.3 : 1</i>	<i>1.2 : 1</i>
India	1.8 : 1	2.7 : 1	1.8 : 1	1.6 : 1
South Africa	0.7 : 1	1.3 : 1	0.6 : 1	0.3 : 1
Eastern Europe	0.5 : 1	0.8 : 1	0.5 : 1	0.2 : 1

Sources: Study Team Analysis, WTO

Other issues raised by the sample include:

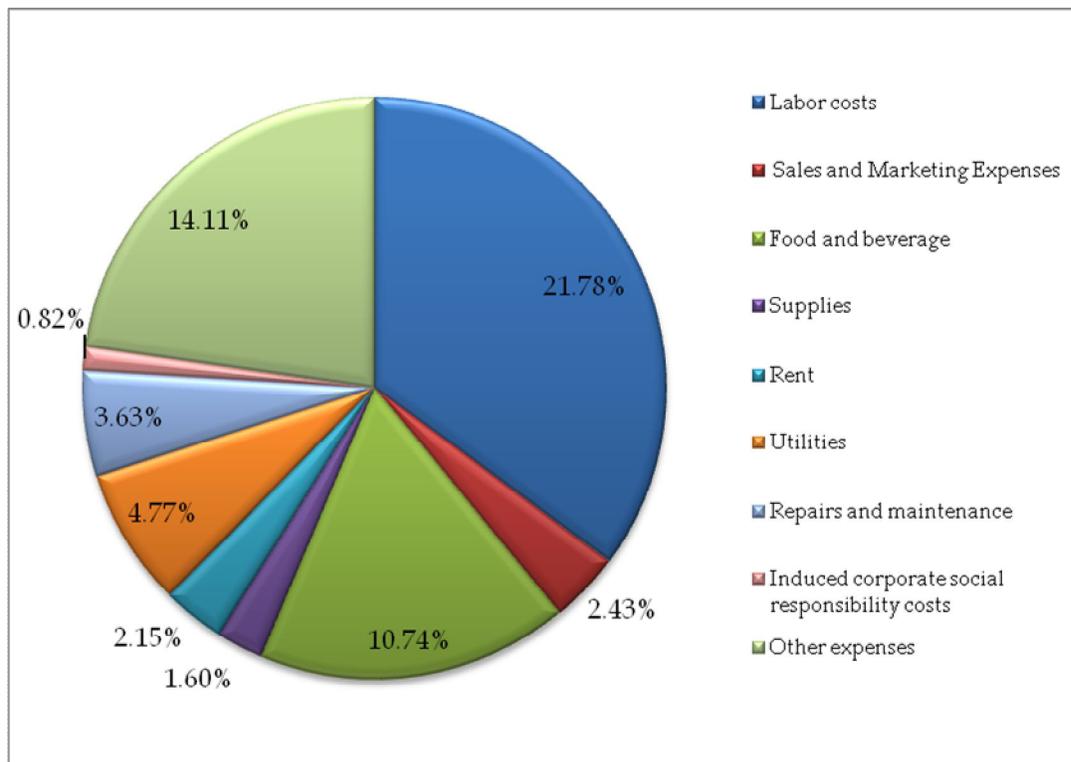
- Water quality
- Electricity quality and supply
- Utility costs (water and electricity)
- High inventory holdings due to regular breakdowns and lack of local service provision
- High cost of import and supply of equipment to compensate for the need to provide utilities in-house
- High cost of food and beverage, much of which is imported

There are limited numbers of ancillary services available with the sample reporting that local service provision from food to repairs and maintenance are poor or unreliable.

There are few options for excursions or add-ons which could potentially be sold to business travelers.

Cost Structure and Drivers

The analysis of profitability for the corporate tourism value chain is based on financial information provided by 15 firms catering to this segment of the market:

Figure 14: 2013 Operating Costs, Business Firm Sample

Source: Study Team Analysis

The costs of food and beverage inputs are high (representing 14% of total costs) since they are mostly imported. Fixed costs include security, rent, and utilities, which total over 15% of total operating costs. Sales and marketing expenses are low because of the heavy reliance on third-party distribution channels such as local branches and travel agents. Limited marketing and promotion is conducted in the main generating markets. While labor costs for this value chain are aligned with comparable international destinations (such as South Africa and India) and represent almost 22% of total costs, labor legislation requires that hotels maintain a minimum of three shifts per day of 8 hours each, regardless of the seasonality or occupancy rates. This poses a challenge to efficient management of labor costs and reduces the likelihood of creating full time positions at low skill levels.

Table 10: Business vs. Full Sample: Cost & Profitability Estimates

	Business Sample (MZN)	Business Sample (% of Revenue)	Full Sample (MZN)	Full Sample (% of Revenue)
Gross Revenue	1,390,565,243	N/A	1,687,939,164	N/A
Operating Costs	862,526,005	62.03%	1,183,304,695	70.10%
Labor	302,848,297	21.78%	409,858,012.63	24.28%
Sales and Marketing	33,795,562	2.43%	62,765,089	3.72%
Food and Beverage	149,388,140	10.74%	202,864,612	12.02%
Supplies	22,265,952	1.60%	28,361,679	1.68%
Rent	29,886,489	2.15%	36,725,236	2.18%
Utilities	66,302,602	4.77%	101,515,903	6.01%
Repairs and Maintenance	50,528,303	3.63%	64,619,044	3.83%
Induced Corporate Social	11,338,522	0.82%	14,503,522	0.86%

	Business Sample (MZN)	Business Sample (% of Revenue)	Full Sample (MZN)	Full Sample (% of Revenue)
Responsibility (CSR)				
Other Expenses	196,172,137	14.11%	262,091,597	15.53%
Taxes (National & Municipal)	421,930,642	30.34%	470,525,979	27.88%
Operating Profit	106,108,596	7.63%	34,108,490	2.02%

Sources: Study Team Analysis

Potential Impacts of Dutch disease on the Business Tourism Sector

Exchange Rate Effects: Under a “pessimistic” policy scenario, the exchange rate appreciation impacts firm finances through two pathways. The first is driven by nominal appreciation of the exchange rate, forcing an erosion of the firm’s price competitiveness and resulting in a reduction in revenue and an increase in imported inputs (principally food and beverage, marketing services, and other supplies). In addition, appreciation of the real exchange rate alters the demand for and price of labor and capital. This sets in motion a longer-run reallocation of factors within and across industries, leading to increased labor scarcity within tourism and putting upward pressure on wages and labor costs in the sector. Model results under these conditions show economic profitability declining sharply in both “pessimistic” and “optimistic” policy scenarios. Assuming an ER appreciation rate of 9.6%, the impacts are less significant although they still trigger a decline in profitability of almost 1% point in both policy scenarios.

Policy Reform Effects: As discussed above, most constraints to competitiveness and increased profitability stem from policy and regulatory barriers, such as labor regulations, security, air transport monopoly, and visa policies. If some of the most pressing issues were solved or improved, the effects of currency appreciation and increases in labor costs could be partially offset. The total accrued pre-tax profit from these reforms is presented in Table 11 below:

Table 11: Model Adjustments for Optimistic Policy Scenario, Business Sample

Variable	Value of Profit Realized by Sample in Optimistic Policy Scenario (MZN)
Labor Issues Improved	38,742,720
Unreliability of air transport	13,088,079
High price of air transport	282,907
Corruption and inaction by local police force	2,923,170
Political strife within Mozambique	26,015,724
Restrictiveness of visa policy for visitors	25,342,605
Costs of providing security for visitors	45,992,308

Source: Study Team Analysis

These reforms would significantly improve the financial performance of corporate tourism businesses and allow them to better withstand the potential impacts of Dutch disease, as illustrated below. However, it is important to notice that under a 50% currency appreciation

scenario, the impact would be severe unless revenue (and prices) increase, further reducing the competitiveness of the industry.

Table 12: Scenario Analysis: Corporate Tourism and the Impacts of Dutch Disease

	No ER Appreciation	9.6% ER Appreciation	50% ER Appreciation
PESSIMISTIC POLICY SCENARIO			
Total Revenue	1,390,565,243	1,367,871,218	1,272,367,197
Operating Costs	862,526,005	865,943,334	920,325,450
Taxes	421,930,642	409,919,049	347,807,930
Operating Revenue (MZN)	106,108,596	92,008,835	4,233,817
Operating Revenue (% of Revenue)	7.63%	6.73%	0.33%
OPTIMISTIC POLICY SCENARIO			
Total Revenue	1,622,267,846	1,595,793,411	1,484,380,166
Operating Costs	947,426,430	948,799,206	993,160,827
Taxes	507,289,149	494,055,123	427,135,232
Operating Revenue	167,552,267	152,939,082	64,084,106
Operating Revenue (% of Revenue)	10.33%	9.58%	4.32%

Source: Study Team Analysis

LEISURE TOURISM

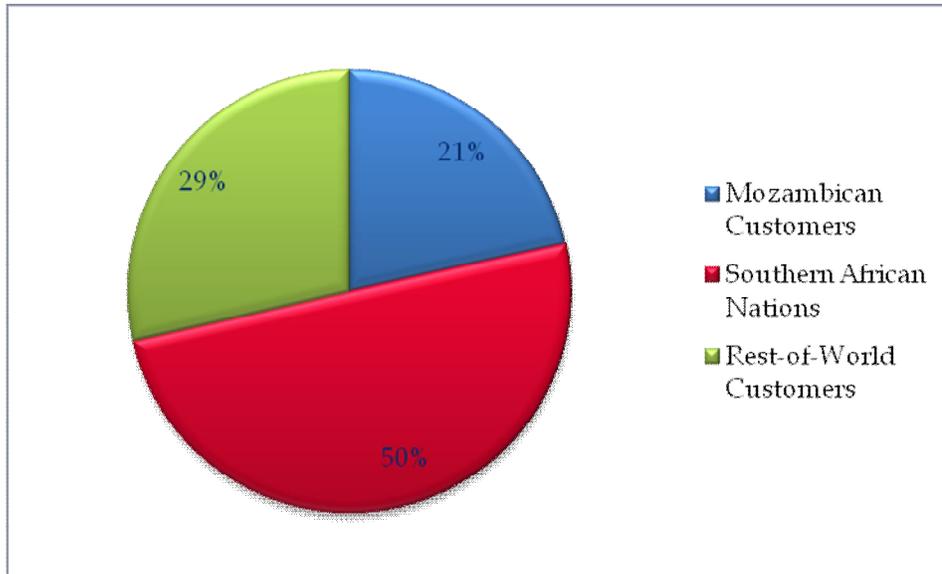
This value chain presents two distinct sub-products: island beach tourism centered on the archipelagos of the Quirimbas and Bazaruto; and the coastal beach product focused on the coast of Inhambane and Vilanculos (in the North) and Ponta do Ouro (south of Maputo). While the island product falls mostly into the luxury category, the coastal resorts cater to all types of travelers, though generally focused on the mid-market, both internationally and domestically.

This segment presents characteristics more aligned to a mature tourism value chain, where outbound and inbound operators and agents collaborate to provide services to domestic and regional visitors. This is particularly the case for the important South African market, where agents on both sides of the border are engaged in commercial relationships to meet the needs of their customers. Nevertheless, the management of leisure tourism is generally characterized by weak collaboration across different stakeholders. This leaves critical destination level issues to be managed by dispersed and individual efforts or not addressed at all.

Most firms in this value chain are medium or small in size which impacts their ability to access new markets and their financial resilience.

The main source markets for this value chain are South Africa (50%), Mozambique (21%), and other markets, primarily Western Europe and the United States (29%).

Figure 7: Clientele Origin, Leisure Firm Sample



Source: Study Team Analysis

There is a difference between the island product and the coastal beach product as customers for the former are drawn primarily as add-ons to safari itineraries centered on South Africa, Botswana, Namibia, and Tanzania. The traditional dominance of the Portuguese VFR market has been affected by visa requirements. There is evidence of a growing market of Mozambicans (15%), primarily from Maputo, traveling to the island resorts. The reduction in self-drive tourism from South Africa has affected Ponta do Ouro in particular.

The demand for international brokerage services and tour packages for the coastal beach product is weak. This situation is partly explained by the predominance of FITs from South Africa. However, there are other contributing factors such as tour operators and travel agencies in source markets being unable to issue domestic airline tickets. Foreign tour operators and agencies are also not able to access seat inventories on LAM making it more difficult for them to respond to last minute demand from tourists.

The island products are largely managed by international agents, including South African tour operators, by the resorts themselves which have sales representatives in source markets, and by outbound tour operators in the main source markets. This product has a very low rate of participation by domestic intermediaries and ground operators (e.g. ground transport organizers, taxis, car rental agents). The absence of local tour operators impacts lodges by reducing value, flexibility, and service provision and raises operating costs because of the need to engage in non-core activities such as “meet and greet” arrangements and local tour operation.

Infrastructure deficiencies affect the quality, cost, and time of operation for firms in this value chain. For example, the length and strength of the runway at Vilanculos’ airport is insufficient to accommodate anything but turbo-propelled aircrafts. The road to Ponta do Ouro is only suitable for 4x4 vehicles.

Small hotels and lodges constitute the bulk of accommodation in the leisure tourism value chain. Good quality accommodation in coastal resorts outside the islands is limited and considered expensive. Few are able to meet the expectations of upscale international tourists, and the standard and types of services and amenities offered vary widely.

Data suggests that demand and occupancy rates are low for most of the year and hotels and resorts rely heavily on intermediaries for the supply of tourist visitors.

Although hoteliers in northern Mozambique and in the Quirimbas highlighted the same main constraints to doing business as elsewhere, the impact of these is amplified given the remoteness and lack of adequate infrastructure these firms face. Most inputs for hotel and restaurant operations are sourced from Maputo, where most products are imported.

The leisure tourism value chain ranks low when compared to industry standard ratios of employee per room. As Table 13 illustrates, the Mozambican average for leisure hotels is over three times higher than the WTO standard:

Table 13: Hotel Employee Productivity, Leisure Sample

	Average	Five Star	Four Star	Three Star
WTO Recommended Standard	1 : 1	2 : 1	1.2 : 1	0.8 : 1
Mozambique (Full Sample)	2.2 : 1	2.7 : 1	2.2 : 1	1.7 : 1
<i>Mozambique (Leisure Sample)</i>	<i>3.2 : 1</i>	<i>4.2 : 1</i>	<i>3 : 1</i>	<i>2.2 : 1</i>
India	1.8 : 1	2.7 : 1	1.8 : 1	1.6 : 1
South Africa	0.7 : 1	1.3 : 1	0.6 : 1	0.3 : 1
Eastern Europe	0.5 : 1	0.8 : 1	0.5 : 1	0.2 : 1

Source: Study Team Analysis, World Tourism Organization

As is the case in the business value chain, the leisure segment faces issues with:

- Water quality
- Electricity quality and supply
- Utility costs (water and electricity)
- High inventory holdings due to regular breakdowns and lack of local service provision
- High cost of import and supply of equipment to compensate for the need to provide utilities in-house
- High cost of food and beverage, much of which is imported

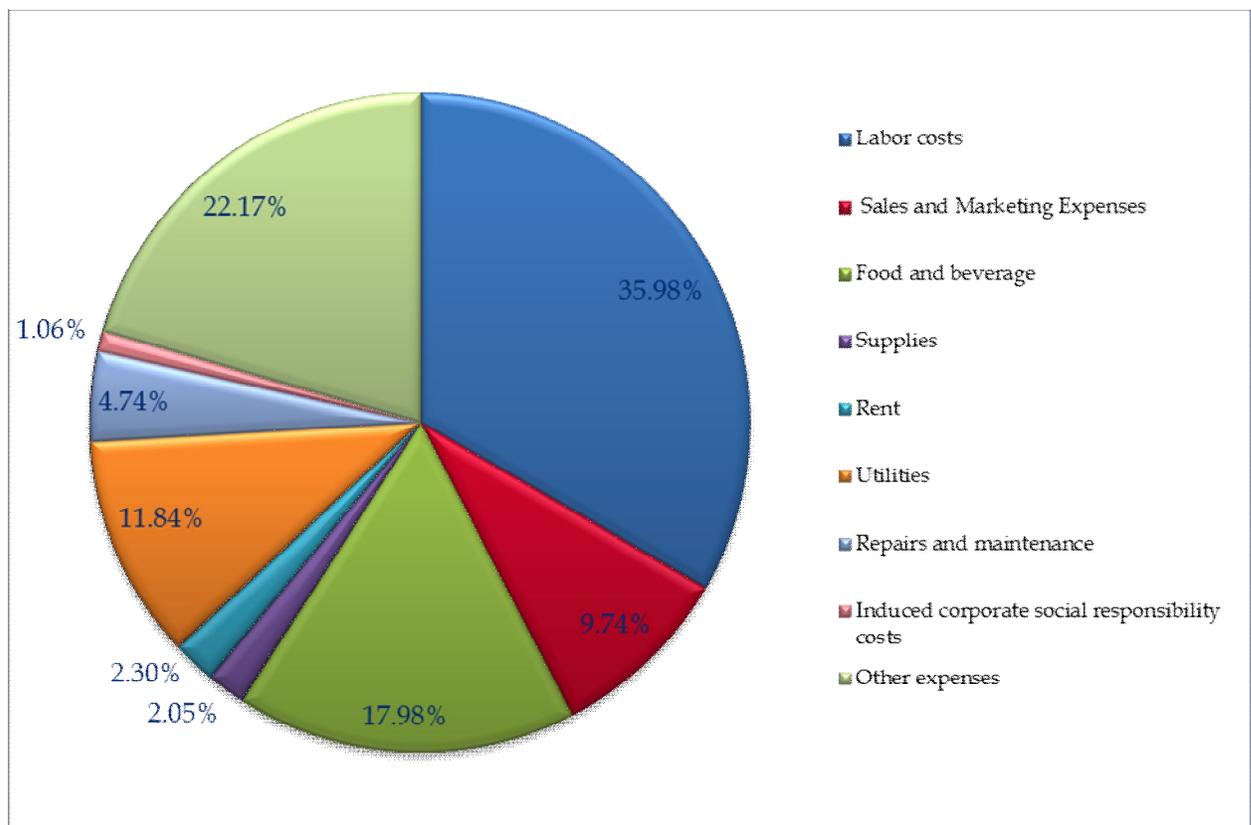
Here too there are limited numbers of ancillary services available with the sample reporting that local service provision from food to repairs and maintenance are poor or unreliable. There are few options for excursions or add-ons.

Cost Structure and Drivers

The analysis of profitability for the leisure tourism value chain is based on financial information provided by 14 firms catering to this segment of the market and presented in Figure 15.

Operating costs for hotels in the leisure tourism value chain are significantly higher than comparable costs for the corporate value chain. The costs of food and beverage inputs are very high (18% of total costs) since they are mostly sourced from outside Mozambique and difficult to replace given the consumption characteristics of the markets. Fixed costs include security, rent and utilities, which total almost 35% of total operating costs and are largely a consequence of the high costs of providing reliable electricity and water to customers in the remotes areas where firms are located. Sales and marketing expenses are higher than the average for the industry in Mozambique because of the need to invest in international promotion and marketing. Unlike firms in the corporate value chain, leisure tourism firms report participating in international and regional trade shows, which requires significant investment. Labor costs for this value chain are almost twice as high as in India and at least 1.5 higher than in South Africa. Moreover, labor costs for leisure segment firms are 10% higher than those for corporate tourism firms as a percentage of total revenue. As the model shows, labor costs represent the biggest threat to the financial viability of the leisure tourism value chain and place it at considerable risk in the face of Dutch disease. Based on current occupancy rates for the industry as a whole, the businesses in this value chain are operating at a significant loss. The information presented in Table 14 supports anecdotal evidence that many leisure tourism businesses rely on external funding (typically from diversified investments) to survive.

Figure 8: 2013 Operating Costs, Leisure Firm Sample



Source: Study Team Analysis

Table 14: Leisure vs. Full Sample: Cost & Profitability Estimates

	Leisure Sample (MZN)	Leisure Sample (% of Revenue)	Full Sample (MZN)	Full Sample (% of Revenue)
Gross Revenue	297,373,921	N/A	1,687,939,164	N/A
Operating Costs	320,778,690	107.87%	1,183,304,695	70.10%
Labor	107,009,715.93	35.98%	409,858,012.63	24.28%
Sales and Marketing	28,969,527	9.74%	62,765,089	3.72%
Food and Beverage	53,476,471	17.98%	202,864,612	12.02%
Supplies	6,095,727	2.05%	28,361,679	1.68%
Rent	6,838,746	2.30%	36,725,236	2.18%
Utilities	35,213,301	11.84%	101,515,903	6.01%
Repairs and Maintenance	14,090,741	4.74%	64,619,044	3.83%
Induced Corporate Social Responsibility (CSR)	3,165,000	1.06%	14,503,522	0.86%
Other Expenses	65,919,459	22.17%	262,091,597	15.53%
Taxes (National & Municipal)	59,025,052	19.85%	470,525,979	27.88%
Operating Profit	(82,429,821)	-27.72%	34,108,490	2.02%

Sources: Study Team Analysis

Potential Impacts of Dutch disease

Table 16 shows shifts in profitability in line with likely impacts of Dutch disease for the leisure value chain.

Exchange rate effect: Metical appreciation would affect firm profitability through the same channels as observed in the business and corporate sample. Nominal appreciation in the near-term will have ERPT effects on both input purchases and on sales but, as noted in the Section 3, its effects in reducing sales (due to loss in price competitiveness) will be exceeded the effects of reducing input costs (lower cost of imported food and beverage for example). Over time as wages become less sticky and real appreciation effects are reflected in inter-sectoral compensation differentials (between tradable and non-tradable), leisure tourism employees, or at least those with higher skills, will migrate towards higher-paying industries. This will spur leisure segment firm wages to rise, and productivity and quality of labor to fall (assuming it is the most productive employees who are able to successfully obtain work in other industries), increasing operating costs and worsening the financial picture (see Pessimistic Policy Scenario, Table 16).

It is also important to note one critical economic characteristic of the leisure tourism value chain not addressed by these model runs – that of the relatively elastic demand its firms face for their services. Unlike the corporate value chain firms, whose clientele usually have to travel due to business needs, leisure tourism firms are far more exposed to the effects of sudden shifts in demand due to changes in price competitiveness. Ironically were leisure value chain firms currently more competitive and their prices more appealing to international consumers, appreciation would have even greater effect on profitability, as there would be a larger volume of

customers potentially at risk of taking their business elsewhere. Given the poor health of the value chain as sampled, however, it is clear there is little current business to be affected. For this reason, the forecasts here represent a lower estimate of the financial effects of exchange rate appreciation than would be seen in healthier leisure tourism industries.

Policy Reform Effects: If the same policy issues considered above in the corporate value chain were resolved or improved, the effects of currency appreciation and resulting increase in labor costs on the leisure segment could be partially offset. The total accrued profit from these reforms is presented in Table 15:

Table 15: Model Adjustments for Optimistic Policy Scenario, Leisure Sample

Variable	Value of Profit Realized by Sample in Optimistic Policy Scenario (MZN)
Labor Issues Improved	19,178,251
Unreliability of air transport	1,705,952
High price of air transport	949,183
Corruption and inaction by local police force	3,840,068
Political strife within Mozambique	8,318,209
Restrictiveness of visa policy for visitors	599,328
Costs of providing security for visitors	13,548,210

Source: Study Team Analysis

Unlike the corporate and business tourism value chain, these reforms alone would not be enough to overcome the dire financial performance of leisure tourism businesses, they would only reduce the rate at which those in the leisure segment are losing money, as illustrated in Table 16. These effects would be amplified under a 50% currency appreciation scenario.

Table 16: Scenario Analysis: Leisure Tourism and the Impacts of Dutch Disease

	No ER Appreciation	9.6% ER Appreciation	50% ER Appreciation
PESSIMISTIC POLICY SCENARIO			
Total Revenue	297,373,921	292,520,779	272,097,138
Operating Costs	320,778,690	323,558,918	345,346,493
Taxes	59,025,052	58,284,218	55,627,058
Operating Revenue (MZN)	(82,429,821)	(89,322,357)	(128,876,413)
Operating Revenue (% of Revenue)	-27.72%	-30.54%	-47.36%
OPTIMISTIC POLICY SCENARIO			
Total Revenue	518,426,143	509,966,410	474,365,037
Operating Costs	520,645,111	520,011,259	527,632,055
Taxes	97,305,571	95,925,471	90,538,851
Operating Revenue	(99,524,539)	(105,970,320)	(143,805,870)
Operating Revenue (% of Revenue)	-19.20%	-20.78%	-30.32%

Source: Study Team Analysis

5. Main Findings and Key Messages

This report has reviewed factors affecting the competitiveness of two tourism value chains in Mozambique, the corporate segment and the leisure segment. Although the emphasis of the report is on cost analysis, qualitative dimensions such as productivity, quality, value-added service, and risk management were also considered. Nevertheless, because of shifting market dynamics, and the fact that Mozambique's tourism product is underdeveloped relative to international standards, competitiveness is mostly a cost issue, and one which is determined throughout the different stages in the value chain.

Like other industries, tourism produces products that vary in their competitiveness in international markets. One of the key findings of this study is that there is a difference in competitiveness between corporate, and leisure, tourism firms and in the products they offer. The corporate tourism value chain offers the best prospects for remaining competitive vis-à-vis the onset of Dutch disease. However that said, even the corporate tourism segment is not highly profitable and will become less so under DD.

The Tourism Divide: Although the Mozambican tourism industry has often been treated as monolithic, this study has identified two very different value chains in distinct situations in respect of their current and long-term competitiveness. The financial health of the corporate and business tourism sector has improved due to the natural resource boom. However, this same boom has reduced the sense of urgency at government level to remove longstanding barriers to competitiveness which are preventing the whole sector from growing. Lessons learned from other countries suggest that policy reform intended to open up markets, improve the quality of human resources and develop unique tourism products is the best way to guarantee continued financial success in the face of the economic pressures imposed by a natural resources boom.

In the case of the firms surveyed, it is clear that those active in the leisure tourism value chain are mainly locally owned, smaller in size, and lack easy access to international capital markets. They are currently vulnerable to financial stress and this would worsen under DD.

The inelasticity of demand for corporate and business travel makes the future for firms in that value chain somewhat brighter. However, profitability rates are low compared to international averages and highlight the additional cost of doing business resulting from operating environment constraints. There is evidence that companies operating in Mozambique are increasingly choosing to provide executives and workers with accommodation rather than using hotels, suggesting that there is finite tolerance for price increases in this segment, which suggests that the current growth in the segment is potentially unstable.

The Real Costs of Labor: The financial analysis undertaken for this study identified the cost of labor as the most significant driver of firms' profitability. Labor costs are high as a result of the low productivity rather than as a factor of actual wages paid. Mozambican hotels have, on average, twice as many employees as hotels in other parts of the world with similar occupancy rates. Firms operating in the leisure tourism value chain are particularly affected while firms in the corporate value chain present rates of employees per room that are more aligned with

international best practice. Increases in the cost of labor (resulting from DD) would significantly affect the sector. Even if all other barriers to competitiveness were removed, without changes in the cost of labor, firms will see their ability to compete restricted.

The Cost of Security: The combined effects of (perceived and actual) violence and corruption represent over 41 million Meticaís of foregone profit to the sampled firms, making it the most burdensome opportunity cost measured in this study. Two conclusions are significant. Firstly perceptions of the impacts of corruption are not reflected in evidence. The quantitative assessment found that police corruption represents “only” 8% of the overall value of all foregone profit in this category. The other components such as internal conflict, and the need for firms to provide their own security, were estimated to each be valued at more than *five times* that of police corruption. This suggests that while corruption is a very visible hindrance, other more indirect impacts of the lack of security are more harmful to business’ bottom line.

A second conclusion is that while these constraints contribute to substantial inefficiencies, relieving them will not off-set the negative effects of Dutch disease. Estimates from the model show that even if these constraints were lifted completely, a mild appreciation of the ER by 11.6% would reduce the sample’s operating profit to zero.

The Costs of Air Transport Monopoly: Unreliable logistics is a major challenge and the air transport situation is directly responsible for unrealized profit of 16 million Meticaís for surveyed firms. However, the most significant inhibitor of visitor growth is not the *cost* of air transportation but rather the *unreliability* of flights. Reservations canceled as a result of flight unreliability represented unrealized profits of almost 14.8 million Meticaís while the profit foregone due to the cost of airfares represented *less than one tenth* this amount (1.23 million Meticaís). While wholesale reform of the aviation sector might be unrealistic, improvements in air transport logistics offer should be a viable goal that could have a significant positive effect on the overall cost competitiveness of the sector. Nevertheless, it is important to highlight that these improvements alone would not suffice to entirely protect the industry from the onset of Dutch disease.

The Effects of Visa Policies: The restrictiveness of Mozambique’s visa policies is a clear hindrance to tourism competitiveness, yet at the same time reform in this area cannot be expected to off-set Dutch disease effects on its own. The current cost of the visa policy is 25.9 million Meticaís in foregone, pre-tax profit – representing 31% of the total foregone by the sampled firms in 2013 (see Figure 7). Setting aside Dutch disease specifically, comparison of the partial effects of visa policy reform also shows that benefits would accrue disproportionately to larger firms catering to international tourists.²⁰ This does not mean that visa policy reform would be inconsequential. But if not combined with targeted reforms addressing other key constraints,

²⁰ Corporate Firms (mean annual revenue of 92,704,350 MZN) would stand to realize the 97.69% of the 25,941,933 MZN estimated in foregone profits to the total sample. Leisure firms (mean annual revenue of 21,240,994 MZN) would stand to receive the remaining 2.31% in unrealized profit. A comparison of the target markets for the Corporate and Leisure value Chains (Figures 7 and 13, respectively) further illustrates this finding.

liberalization will at best provide marginal benefits to large, well-established firms without providing meaningful protection from Dutch disease effects to smaller firms.

KEY MESSAGES

The tourism sector is currently struggling, particularly in the leisure segment, which is the segment offering the best chance for small, local firms to develop. Under a Dutch disease scenario leisure tourism in Mozambique would all but cease to exist. It would be completely nonviable. Business tourism currently fares a little better. However under a Dutch disease scenario this currently profitable segment would also struggle to compete and survive.

The following messages are designed to assist CTA in discussing key policy proposals which will assist the tourism sector now, as well as in the future.

Improving Labor Productivity. The importance of labor cost and quality for the overall competitiveness of the tourism industry cannot be understated. The economic benefits derived from a more productive labor force will be the single most critical factor to enable firms increase their competitiveness – regardless of whether or not Dutch disease effects materialize. It is therefore important to develop a comprehensive strategy to improve the productivity of staff in the tourism sector through policy reform and training initiatives. The financial model discussed above allows for identification of three specific activities which would improve labor productivity and reduce cost:

- **Increase in-house training for hotel staff by 1% of total operating costs.** Currently, the businesses in the survey sample invest 8.3 million Meticais (or 0.7% of total operating costs) in training, equivalent to approximately 125 USD per employee per year. Firms operating in the business tourism value chain tend to spend less since most are located in urban areas where skilled staff is easier to find. Firms in the leisure tourism value chain invest an average of 143 USD per employee per year as they tend to be located in rural areas with less access to skilled staff. However, both value chains invest significantly less than hotels in other destinations:

Table 17: Tourism Firms' Investment in Employee Training, 2013

Country	Average Expenditure in Training per Employee per Year
Mozambique (Full Sample)	\$125
<i>Leisure Value Chain Sample</i>	<i>\$143</i>
<i>Business Value Chain Sample</i>	<i>\$113</i>
Rwanda	\$200
Australia	\$514
United States	\$955

Source: Study Team Analysis

Increasing training costs by 1% (or 11.8 million Meticaïs) would bring the average expenditure in training per employee up to 305 USD, which is more in line with international best practice. Extrapolating from the model, an increase of 1% in training budgets should have a positive effect (1.6% increase) on firm profits as a percentage of total revenue.

- **Remove restrictions on hiring foreign workers.** Current regulations are based on a quota and are intended to protect national staff. However there is a shortage of skills in the country and this particularly affects the tourism sector which needs not only to increase skills of local staff but to have highly skilled and qualified staff available during the time it takes to bring local staff up to the requisite levels. The model shows that removing restrictions on the hiring of foreign skilled workers would result in firm operating costs increasing by 2.8%, as staff with higher skills tends to be more expensive. This increase would however be off-set by revenue increases of an estimated 6% resulting from increased productivity.
- **Make labor regulations in the sector more flexible.** The labor law uniformly applies to all sectors and prevents tourism employees from working shifts longer than 8 hours. This therefore obliges firms to both increase the number of shifts and the number of employees in order to provide acceptable levels of service at all times.

The current legal framework also fails to take account of the flexibility required by the hospitality industry to deal with seasonality or periods of inactivity.

A comparative lesson can be drawn from the United States' hotel industry, which presents an interesting example of labor market flexibility in meeting the dynamic needs of firms. Rather than tackling issues of wages or taxes, the American Hotel and Lodging Association (AHLA) lobbied the government to incorporate legislation permitting alternative scheduling in the hospitality sector. The main tenets of the regulations can be found in Table 18.

Table 18: Alternative Scheduling in the American Hospitality Industry

Alternative Scheduling in the American Hotel Industry	Flexible Work Hours or Flexitime. Allows for more efficient allocation of workers in different departments
	Compressed Work Schedule. Allows for longer shifts during peak seasons.
	Job Sharing. Reduces the need for full-time staff during low seasons.

Source: AHLA

The model suggests that surveyed firms' profitability would increase to 4% of total revenue (or an additional 34 million Meticaïs per year) if these reforms were to be implemented:

Table 19: Partial Effects of Select Labor Policy Improvements, Full Sample

Select Policy Reforms	Profit in Baseline (% of Revenue)	Change from Baseline due to Policy Reform (% of Revenue)	Change from Baseline due to Policy Reform + 9.6% ER Appreciation (% of Revenue)	Change from Baseline due to Policy Reform + 50% ER Appreciation (% of Revenue)
1) Labor Costs	34,108,490 MZN	29,624,804 MZN	9,697,548 MZN	-99,296,676 MZN

Decrease by 10% Through Improved Scheduling		(86.85%)	(28.43%)	(-291.12%)
2) Restrictions Removed on Hiring of Foreign Workers	(2.02%)	29,668,548 MZN (86.98%)	8,029,828 MZN (23.54%)	-113,156,484 MZN (-331.75%)
3) Firms Increase Training Expenditures by 1% of Total Operating Costs		550,160 MZN (1.61%)	- 19,719,234 MZN (-57.81%)	-132,945,913 MZN (-389.77%)

Source: Study Team Analysis

These impacts would vary significantly between firms in the corporate, and leisure, value chains, particularly in the face of Dutch disease. Analysis of the leisure segment suggests that while these policy reforms could help firms turn around their present situation, and remain viable in the context of a moderate metical appreciation, faced with acute currency appreciation these reforms would only minimize operating losses. Tables 20 and 21 illustrate the different impacts of these reforms on profitability of participating firms:

Table 20: Partial Effects of Select Labor Policy Improvements, Business Sample

Select Policy Reforms	Profit in Baseline (% of Revenue)	Change from Baseline due to Policy Reform (% of Revenue)	Change from Baseline due to Policy Reform + 9.6% ER Appreciation (% of Revenue)	Change from Baseline due to Policy Reform + 50% ER Appreciation (% of Revenue)
1) Labor Productivity Increases, such that Labor Costs Decrease by 10%		21,877,761 MZN (20.62%)	8,128,044 MZN (7.66%)	-76,111,528 MZN (-71.73%)
2) Restrictions Removed on Hiring of Foreign Workers	106,108,596 MZN (7.63%)	16,862,997 MZN (15.89%)	2,151,468 MZN (2.03%)	-89,179,716 MZN (-84.05%)
3) Firms Increase Training Expenditures by 1% of Total Operating Costs		404,525 MZN (0.38%)	-13,599,179 MZN (-12.82%)	-100,969,955 MZN (-95.16%)

Source: Study Team Analysis

Table 21: Partial Effects of Select Labor Policy Improvements, Leisure Sample

Select Policy Reforms	Profit in Baseline (% of Revenue)	Change due to Policy Reform (% of Revenue)	Change due to Policy Reform + 9.6% ER Appreciation (% of Revenue)	Change due to Policy Reform + 50% ER Appreciation (% of Revenue)
4) Labor Productivity Increases, such that Labor Costs Decrease by 10%	-82,429,821 MZN (-27.72%)	11,189,494 MZN (13.57%)	4,475,989 MZN (5.43%)	-33,269,844 MZN (-40.36%)
5) Restrictions Removed on Hiring of Foreign Workers		7,981,128 MZN (9.68%)	541,292 MZN (0.66%)	-42,532,364 MZN (-51.60%)
6) Firms Increase Training Expenditures by 1% of Total Operating Costs		581,404 MZN (0.71%)	-6,258,485 MZN (-7.59%)	-45,590,985 MZN (-55.31%)

Source: Study Team Analysis

Policy vs Firm-Level Reform. Any response to the current situation in the sector as well as preparation for potential Dutch disease must include a combination of policy and firm-level reforms. Policy reform must ensure that the efficient arrival and mobility of visitors results in increased revenue for tourism business, while reforms at firm level will improve business profitability.

The example above of labor reform is one example of how the modeling tool developed by the study team can be used by the private sector to prioritize barriers to competitiveness. While theoretical approaches to competitiveness are important, CTA should primarily be concerned with ensuring the financial health of businesses. It is our hope that this study is of benefit as they work towards achieving that goal.

Annex A. Stakeholder Interviews

International Private, Public, and Multilateral Organizations

- **CBE Southern Africa**
 - Nuno S. Uinge, Chief Executive Officer
- **Keben & Associates**
 - Kwasi Agleby, Director
- **Nathan Associates**
 - Lynn Salinger, Principal Associate
- **World Tourism Organization – Mozambique National Tourism Strategy Team**
 - Mike Fabricius, International Consultant
- **Mozambique SPEED**
 - Brigit Helms, Director
- **USAID/Mozambique**
 - Timothy Born, Director of Trade and Business

Private Sector Tourism National Organization

- **CTA – Executive Direction**
 - Hipólito Hamela, Senior Economic Advisor
- **CTA – Tourism *Pelouro***
 - Noor Moamad, President
 - Joao das Neves, Vice President
- **FEMOTUR**
 - Q. Matsombe, President
 - Mario Mendonca, Vice President
- **AHSM (Assoc. Dos Hoteis do Sul de Moç.)**
 - Vasco Manhica, President
 - J.L.G. de Sousa, Secretary
 - Rui Monteiro, Member of the Board
 - Marco Veiga, Member of the Board
 - Koenrad Collier, Member of the Board
 - Jorge Teixeira, Member of the Board
 - Teresa Gomes, Member of the Board
- **ASINHOS (Assoc. Indust. Hoteleira e similar de Gaza)**
 - Rogerio Gomes, President
- **AHTI (Assoc. Hotel. Turismo de Inhambane)**
 - Rauf Usta, President
- **CDTUR (Assoc. de Hotelaria e Turismo de Cabo Delgado)**
 - H. Ildfonso, Acting President
 - Isabel Ferreira, Adviser to the Board
- **ASSOTARQ**
 - Zeferino Madiera, President

- **Ass Ag. Economicos Marracuene**
 - Lester Mouton, Vice President
 - Americo Dalpate, Member of the Board

Tourism Public Sector Institutions

- **MITUR (Ministério do Turismo de Moçambique)**
 - Mohamed Harun, Personal Adviser to the Minister
 - Z. Sumbana. Development Coordinator
 - Gisela Malauene, Head of Planning Department
- **MITUR – DINATUR (Direcção Nacional do Turismo)**
 - M. Muatxiwa, National Director
 - Eduardo Zuber, Head of Licensing Department
- **INATUR**
 - J. Manussa, Head of Marketing Department
 - Katia Momade, Marketing Department
- **DPTURI – Inhambane Province**
 - Bento Nhassengo, Provincial Director
- **DPTCD – Cabo Delgado Province**
 - Fatima Romero, Provincial Director

Private Sector Operators

- **Dana Tours**
 - Natalie T. Silva, Manager
- **Aquarium**
 - Dercio Parker, Head of Sales and Marketing
- **Top Atlantico Mozambique**
 - Aiuca Bay, Head of Sales and Marketing
- **Rani Group**
 - Patricia Guerra, Sales Representative
- **Promotur**
 - Pacheco Faria, Chief Executive Officer

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Annex C. Study Survey Instrument

CONTROL INFORMATION

A1. What market is your business focused on primarily? Select all that apply.

- a. Business Tourism
- b. Island Leisure Tourism
- c. Coastal tourism
- d. Other

A2. What type of business does this establishment conduct? Select all that apply.

- a. Accommodation
- b. Restaurant
- c. Tour Operator
- d. Travel Agency
- e. Transportation only (including car rental, etc.)

A3. Where is the firm located? Select one.

- a. Pemba
- b. Quirimbas Islands
- c. Maputo
- d. Inhambane
- e. Bazaruto
- f. Ponta do Ouro

A4. Is the establishment part of a larger firm?

- a. Yes
- b. No

A5. In 2013, how many people were employed by your company, including managers?

- a. Number of people employed by your company in 2013: ____
- b. DON'T KNOW
- c. REFUSAL

A6. Does your company have temporary or non-permanent workers?

- a. Yes
- b. No
- c. REFUSAL

A7. If yes, what percentage of the total number of employees is not permanent?

- a. % of non-permanent employees?
- b. DON'T KNOW
- c. REFUSAL

A8. According to your revenue in 2013, how large would you say your business is? Select one.

- a. 1.5 - 3.0 M MZN
- b. 3,000,001 - 15.5 MZN
- c. > 15.5 MZN
- d. REFUSAL

FINANCIAL INFORMATION

The following was read to the respondents: *Now, we would like to ask you a few questions about the financial results of this establishment. It is important that this information be as accurate as possible. The individual data are treated as confidential, and the identity of your establishment will not be revealed at any point to any third party, be it public or private sector. Please provide the following information from the financial statements of this establishment.*

B1. In 2013, what was the approximate amount of revenue this establishment earned?

	Amount (MZN)	DON'T KNOW	REFUSAL
Total sales revenue for 2013			

B2. In 2013, how many customers did your establishment service?

- Number of Customers: _____
- DON'T KNOW
- REFUSAL

B3. Of this total number of customers, what percentage would you say were from the domestic market (that is, were Mozambican or Mozambican residents)?

	% of Customers	DON'T KNOW	REFUSAL
Percentage of customers from Mozambique			

B4. What percentage originated from the regional market (South Africa, Zimbabwe, etc.)?

	% of Customers	DON'T KNOW	REFUSAL
Total operating costs for 2013			
CROSS-CHECK: ANSWERS TO B.03 AND B.04 IMPLY THAT REST-OF-WORLD ACCOUNTS FOR THIS % OF THEIR CLIENTELE IN 2013. IF THIS % SEEMS UNUSUAL, CONFIRM WITH RESPONDENT.	100%		

The following was read to the respondents: *Now, we would like to ask you a few questions about the costs your establishments incurred in 2013. The information you provide will tell us what types of costs your establishment incurs, the nature of each cost (variable or fixed), and each cost's proportion of your establishment's total costs. This information is critical for our report and allows us to create a representative picture of an average firm in the country's tourism sector.*

B5. In 2013, approximately what was the total amount of operating costs for your establishment?

	AMOUNT (MZN)	DON'T KNOW	REFUSAL
Total operating costs for 2013			

B6. The following was read to the respondents: *Now, we are going to read to you the names of a few types of costs that are generally considered a part of what a business defines as its operating costs. For each, please tell us what percentage it is of your total operating costs for the year - that is, what percentage of the number you gave us in the preceding question. I (INTERVIEWER) am happy to repeat your response for total operating costs, if you would like. Additionally, please tell us whether each type of cost is considered by your establishment to be "fixed" or "variable". That is, whether the cost increases or decreases with number of customers serviced.*

	% of operating costs in 2013?	DON'T KNOW	REFUSAL
Labor costs (exclusive of taxes)			
Sales and Marketing Expenses			
Food and beverage			
Supplies (furniture, computers, dishware, etc.)			
Rent			
Utilities (telephone, internet, water, gas, electricity, etc.)			
Repairs and maintenance (building, structures, vehicles, etc.)			
Induced corporate social responsibility costs (i.e. supporting local hospitals, schools, etc.)			
Other expenses (AUTOMATICALLY CALCULATED - DO NOT NEED TO ASK)			

B7. What types of materials and services did you import in 2013? Please list them below.

	Description of imported goods/services
Good/Service 1	
Good/Service 2	
Good/Service 3	
ADD ADDITIONAL GOODS/SERVICES IF MENTIONED	
REFUSAL	

B8. Approximately how much did your establishment pay for each of these goods and services in 2013?

	Amount spent on imported goods/services (in MZN)	DON'T KNOW	REFUSAL
Good/Service 1			
Good/Service 2			
Good/Service 3			
ADD ADDITIONAL GOODS/SERVICES IF MENTIONED			

B9. For each of these imports, what percentage would you say is paid in transportation costs?

	% of import costs due to transportation
Good/Service 1	
Good/Service 2	
Good/Service 3	
ADD ADDITIONAL GOODS/SERVICES IF MENTIONED	
REFUSAL	

B10. What types of taxes applied to your business in 2013?

- a. Tax 1: _____
- b. Tax 2: _____
- c. Tax 3: _____
- d. ADD ADDITIONAL TAXES IF MENTIONED
- e. REFUSAL

B11. At this time, does this establishment have a loan from a financial institution?

- a. Yes
- b. No
- c. DON'T KNOW

- d. REFUSAL
- B12. If so, roughly what percentage of your operating expenses is paid for using loans from financial institutions?
- a. 2013 Operating Costs in MZN (from survey response): _____
 - b. OR percentage of operating costs paid for with loans from financial institutions: _____
 - c. DON'T KNOW
 - d. REFUSAL

INFORMATION ON OPPORTUNITY COSTS AND EXTERNALITIES

The following was read to the respondents: *Finally, we would like to ask you a few questions about some specific costs your establishment may have incurred in 2013. These questions are grouped according to categories that we believe are relevant to the international economic competitiveness of Mozambique's tourism industry. The information you provide will give us an idea of the costs businesses are incurring that are due to problems with the business environment in Mozambique. Like the previous series of questions, this information is critical for our report and allows us to understand how uncompetitive aspects of the business environment affect the financial health of the tourism industry. The individual data are treated as confidential, and the identity of your establishment will not be revealed at any point to any third party, be it public or private.*

- C1.** Do you spend time regularly to find out the prices and behavior of competing firms (doing "market research")?
- Yes
 - No
- C2.** If yes, what do you do to discover this information? WRITE "REFUSAL" IF RESPONSE WILL NOT BE GIVEN
- _____
- C3.** How many hours would you estimate you spend in the typical week researching your competition?
- Number of Hours: _____
 - DON'T KNOW
 - REFUSAL
- C4.** In 2013, how many customers cancelled their bookings due to cost of air transport?
- Number of Customers: _____
 - DON'T KNOW
 - REFUSAL
- C5.** In 2013, how many customers cancelled their bookings due to unreliability of air transport?
- Number of Customers: _____
 - DON'T KNOW
 - REFUSAL
- C6.** In 2013, how many customers cancelled their bookings due to unreliability of air transport?
- Number of Customers: _____
 - DON'T KNOW
 - REFUSAL
- C7.** How much in sales revenue did you generate via the internet in 2013?
- Amount of sales revenue done via the internet: _____
 - DON'T KNOW
 - REFUSAL
- C8.** What percentage of your operating costs in 2013 would you say were spent on credit card use fees, bank wires, etc.? If you would rather provide the amount instead of a percentage, please do so here. REPEAT OPERATING COSTS AMOUNT FOR RESPONDENT IF THEY WOULD LIKE TO PROVIDE A PERCENTAGE. IF RESPONDENT KNOWS ACTUAL AMOUNT THEN ALLOW HIM/HER TO PROVIDE THIS NUMBER.
- Percentage of operating costs used for credit card use fees, bank wires, etc.: _____
 - DON'T KNOW
 - REFUSAL
- C9.** Have you included these costs in your responses to question B.06?

- a. Yes
 - b. No
- C10.**FOR THOSE CARTERING TO BUSINESS TOURISM ONLY: How much in revenue did you make in 2013 from leisure extension trips?
- a. Amount of sales revenue made from leisure extension trips (in MZN): _____
 - b. DON'T KNOW
 - c. REFUSAL
- C11.**What percentage of your operating costs in 2013 would you say were spent on providing access to clean water? If you would rather provide the amount instead of a percentage, please do so here. REPEAT OPERATING COSTS AMOUNT FOR RESPONDENT IF THEY WOULD LIKE TO PROVIDE A PERCENTAGE. IF RESPONDENT KNOWS ACTUAL AMOUNT THEN ALLOW HIM/HER TO PROVIDE THIS NUMBER.
- a. Percentage of operating costs used for clean water access: _____
 - b. DON'T KNOW
 - c. REFUSAL
- C12.**Have you included these costs for clean water access in your responses to question B.06?
- a. Yes
 - b. No
- C13.**What percentage of your operating costs in 2013 would you say were spent on waste management services? If you would rather provide the amount instead of a percentage, please do so here. REPEAT OPERATING COSTS AMOUNT FOR RESPONDENT IF THEY WOULD LIKE TO PROVIDE A PERCENTAGE. IF RESPONDENT KNOWS ACTUAL AMOUNT THEN ALLOW HIM/HER TO PROVIDE THIS NUMBER.
- a. Percentage of operating costs used for waste management services: _____
 - b. DON'T KNOW
 - c. REFUSAL
- C14.**Have you included these costs for waste management services in your responses to question B.06?
- a. Yes
 - b. No
- C15.**What percentage of your operating costs in 2013 would you say were spent to comply with environmental requirements? If you would rather provide the amount instead of a percentage, please do so here. REPEAT OPERATING COSTS AMOUNT FOR RESPONDENT IF THEY WOULD LIKE TO PROVIDE A PERCENTAGE. IF RESPONDENT KNOWS ACTUAL AMOUNT THEN ALLOW HIM/HER TO PROVIDE THIS NUMBER.
- a. Percentage of operating costs used to settle environmental requirements:

 - b. DON'T KNOW
 - c. REFUSAL
- C16.**Have you included these environmental regulation compliance costs in your responses to question B.06?
- a. Yes
 - b. No
- C17.**In fiscal year 2013, did you make payments to local or national governments to settle environmentally related disputes?
- a. Yes
 - b. No
 - c. DON'T KNOW
 - d. REFUSAL
- C18.**If so, what percentage of your operating costs in 2013 would you say were spent on these payments? If you would rather provide the amount instead of a percentage, please do so here. INTERVIEWER, PLEASE REPEAT OPERATING COSTS AMOUNT FOR RESPONDENT IF THEY WOULD LIKE TO PROVIDE A PERCENTAGE.

INTERVIEWER, IF RESPONDENT KNOWS ACTUAL AMOUNT THEN ALLOW HIM TO PROVIDE THIS NUMBER.

- a. Percentage of operating costs used to settle environmental disputes: _____
- b. DON'T KNOW
- c. REFUSAL

C19. If so, have you included these environmental dispute payments in your responses to question B.06?

- a. Yes
- b. No

C20. In 2013, what payments did you make to secure the use of the land? ALLOW TIME FOR THE RESPONDENT TO LIST COSTS WITHOUT CUES. IF NO COSTS ARE PROVIDED, ASK IF THERE WERE ANY COSTS.

	Description of Cost
Cost #1	
Cost #2	
Cost #3	
There were no such costs	
DON'T KNOW	
REFUSAL	

C21. If payments were made, approximately how much would you say each of these costs were, as a percentage of your total operating cost? If you would rather provide the amount instead of a percentage, please do so here. PLEASE REPEAT OPERATING COSTS AMOUNT FOR RESPONDENT IF THEY WOULD LIKE TO PROVIDE A PERCENTAGE. IF RESPONDENT KNOWS ACTUAL AMOUNT THEN ALLOW HIM TO PROVIDE THIS NUMBER

	% operating costs or amount (in MZN)	DON'T KNOW	REFUSAL
Cost #1			
Cost #2			
Cost #3			

C22. If so, have you included these costs relating to use of land in your responses to question B.06?

- a. Yes
- b. No

C23. In 2013, did this establishment pay for security, for example equipment, personnel, or professional security services?

- a. Yes
- b. No
- c. REFUSAL

C24. If so, what percentage of your operating costs in 2013 was for these security services? If you would rather provide the amount instead of a percentage, please do so here. PLEASE REPEAT OPERATING COSTS AMOUNT FOR RESPONDENT IF THEY WOULD LIKE TO PROVIDE A PERCENTAGE. IF RESPONDENT KNOWS ACTUAL AMOUNT THEN ALLOW HIM TO PROVIDE THIS NUMBER.

- a. Percentage of operating costs used for security services: _____
- b. DON'T KNOW
- c. REFUSAL

C25. If so, have you included these security costs in your responses to question B.06?

- a. Yes
- b. No

C26. In 2013, did this establishment experience losses as a result of theft, robbery, vandalism or arson on this establishment's premises?

- a. Yes
 - b. No
 - c. DON'T KNOW
 - d. REFUSAL
- C27.C1.** If so, what percentage of your operating costs in 2013 would you estimate were due to losses as a result of theft, robbery, vandalism, or arson? If you would rather provide the amount instead of a percentage, please do so here. PLEASE REPEAT OPERATING COSTS AMOUNT FOR RESPONDENT IF THEY WOULD LIKE TO PROVIDE A PERCENTAGE. IF RESPONDENT KNOWS ACTUAL AMOUNT THEN ALLOW HIM TO PROVIDE THIS NUMBER.
- a. Percentage of operating costs from theft, robbery, vandalism, etc.: _____
 - b. DON'T KNOW
 - c. REFUSAL
- C28.** Have you included these theft, robbery, arson costs in your responses to question B.06?
- a. Yes
 - b. No
- C29.** In 2013, how many customers do you believe you have lost as a result of cancellations due to the unreliability of the police?
- a. Estimated number of customers lost in 2013: _____
 - b. DON'T KNOW
 - c. REFUSAL
- C30.** In 2013, how many customers do you believe you have lost due to "internal conflict" in the country?
- a. Estimated number of customers lost in 2013: _____
 - b. DON'T KNOW
 - c. REFUSAL
- C31.** How many customers do you believe you have lost due to visa issues during 2013?
- a. Estimated number of customers lost in 2013: _____
 - b. DON'T KNOW
 - c. REFUSAL
- C32.** In 2013, did your establishment incur costs in order to comply with changes in national or local policies and regulation? CLARIFY THAT THESE ARE COSTS DUE ONLY TO CHANGES IN POLICIES AND REGULATIONS.
- a. Yes
 - b. No
 - c. DON'T KNOW
 - d. REFUSAL
- C33.** If so, what percentage of your operating costs in 2013 would you say were incurred to remain compliant with these policy and/or regulation changes? If you would rather provide the amount instead of a percentage, please do so here. PLEASE REPEAT OPERATING COSTS AMOUNT FOR RESPONDENT IF THEY WOULD LIKE TO PROVIDE A PERCENTAGE. IF RESPONDENT KNOWS ACTUAL AMOUNT THEN ALLOW HIM TO PROVIDE THIS NUMBER.
- a. Percentage of operating costs from adapting to changing policies and regulations: _____
 - b. DON'T KNOW
 - c. REFUSAL
- C34.** Have you included these costs in your responses to question B.06?
- a. Yes
 - b. No
- C35.** During 2013, did this establishment have formal training programs for its employees?
- a. Yes
 - b. No

c. DON'T KNOW

C36. If so, what percentage of your operating costs in 2013 did you spend on formal training?

If you would rather provide the amount instead of a percentage, please do so here.

PLEASE REPEAT OPERATING COSTS AMOUNT FOR RESPONDENT IF THEY WOULD LIKE TO PROVIDE A PERCENTAGE. IF RESPONDENT KNOWS ACTUAL AMOUNT THEN ALLOW HIM TO PROVIDE THIS NUMBER.

a. Percentage of operating costs used for formal training: _____

b. DON'T KNOW

c. REFUSAL

C37. Have you included these formal training costs in your responses to question B.06?

a. Yes

b. No

C38. Does your establishment provide informal training or training given on an ad hoc basis?

a. Yes

b. No

c. DON'T KNOW

d. REFUSAL

C39. If so, how many hours in the typical week would you spend providing this informal training?

a. Estimated number of hours spent per week for informal instruction: _____

b. DON'T KNOW

c. REFUSAL

C40. If there was no cap on foreign labor, what % of employees would be foreign?

a. % of employees that would be foreign: _____

b. DON'T KNOW

c. REFUSAL

C41. If there were no cap on foreign labor, by what percentage do you believe your total annual revenue would increase?

a. % change in annual revenue: _____

b. DON'T KNOW

c. REFUSAL

C42. If there were no cap on foreign labor, by what percentage do you believe your total annual operating costs would increase?

a. % change in operating costs: _____

b. DON'T KNOW

c. REFUSAL