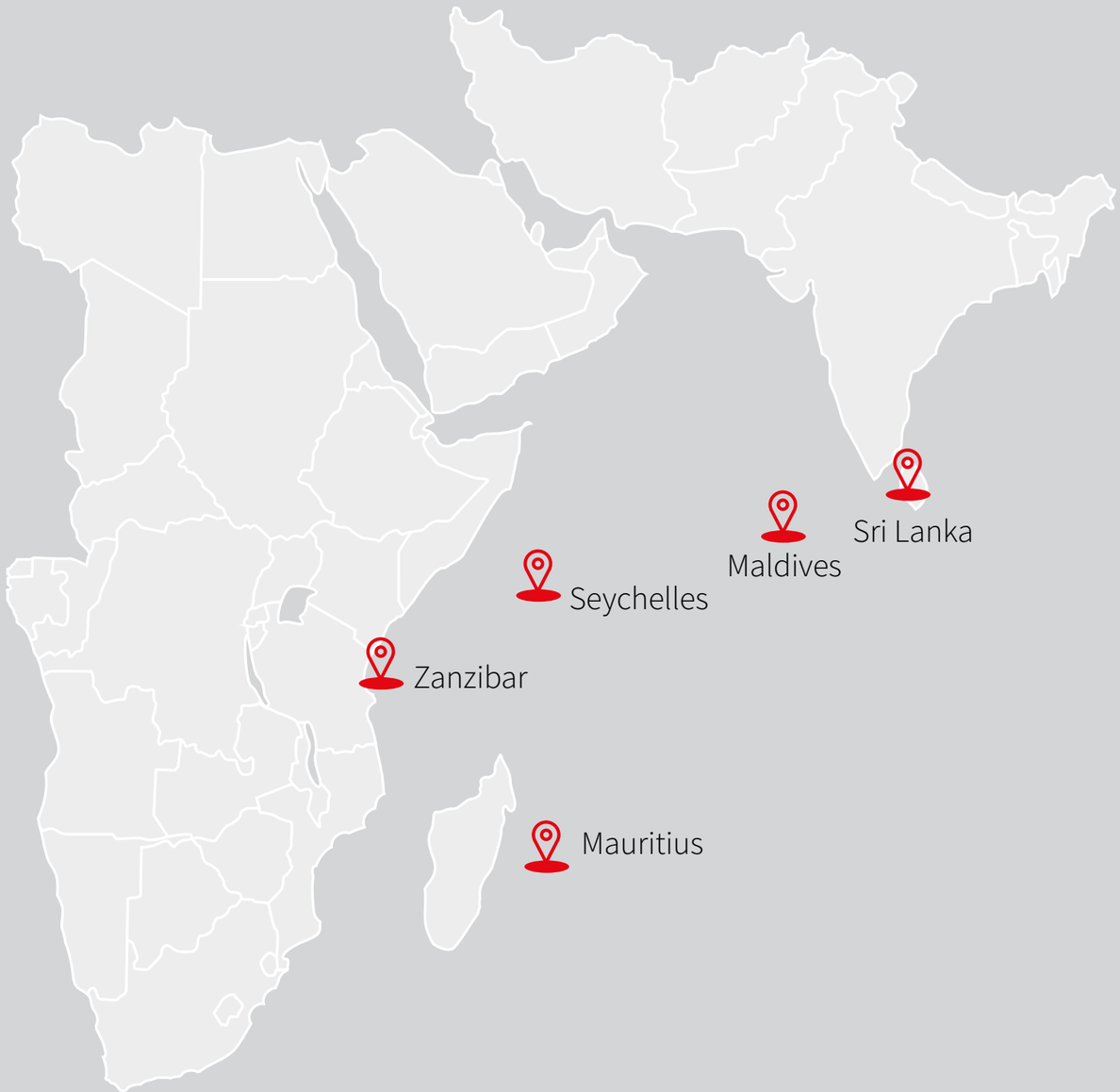
JLL

Hotels & Hospitality Group

Indian Ocean
Trends and Outlook

September 2022



With international borders reopened, destinations in the Indian Ocean are on the way to a full recovery

With beautiful natural landscapes and crystal-clear waters, the Indian Ocean destinations have spurred a fast-growing interest over the years, fuelled by the desire to spend holidays in a postcard-like tropical environment. Indeed, since 2014, the Indian Ocean has registered continued growth in the number of international tourist arrivals. More specifically, Zanzibar topped the podium with an average of +9.5% each year between 2014 and 2019, followed by the Seychelles with a Compound Annual Growth Rate (CAGR) of +8.7%, thanks to improved airlift and notable efforts to develop the local tourism industry.

However, 2019 set a first bump to the continued growth in tourist arrivals in Sri Lanka and Mauritius, having recorded a decrease in international visitation on the back of geopolitical uncertainties and terrorist attacks.

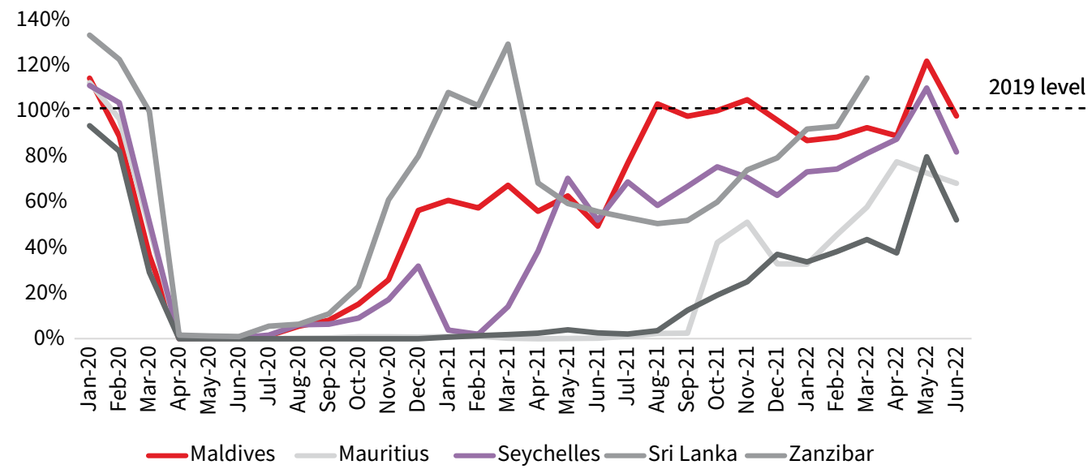
The COVID-19 pandemic was a major setback to the tourism expansion in the Indian Ocean destinations. Although the pandemic has impacted all countries worldwide, the drop in international tourist arrivals was less severe in Zanzibar and in the Maldives, with Zanzibar borders having stayed open to international visitors, and the Maldives having reopened on 15 July 2020. Conversely, Mauritius recorded the strongest decline in international tourists.

In 2021, the Maldives showed the most significant rebound in international visitation as the "one island, one resort" concept allowed the country to provide a sense of assurance regarding COVID-19 safety protocols for guests visiting the resorts, especially from leisure tourists staying in luxury and ultra-luxury resorts. With more than 1.3 million foreign visitors, the Maldives welcomed as many tourists in 2021 as in 2016/2017.

The pandemic has also had an notable impact on source markets in Zanzibar, in particular on Russians, as the destination has remained open to international tourists. Between the end of 2020 and the first half of 2021, Zanzibar has benefitted from a significant pick-up in Russian tourists, before dropping off again. Indeed, between November 2020 and April 2021, Zanzibar has welcomed more than ten times the number of Russian tourists of the whole 2019.

Since January 2022, international visitation continued to grow in all these Indian Ocean destinations, with numbers of tourists reaching between 52% and almost 100% of 2019 levels in June 2022. However, the near-term outlook is uncertain for Sri Lanka, as the country faces major economic and political headwinds.

Monthly international tourist arrivals relative to 2019



Source: Ministry of Tourism Maldives, Statistics Mauritius, National Bureau of Statistics Seychelles, Sri Lanka Tourism Development Authority, Zanzibar Commission for Tourism

Reopening of borders has boosted hotel trading performance in the Indian Ocean, with the Maldives, Mauritius and Seychelles exceeding pre-COVID RevPAR levels

With less international tourist arrivals recorded at the beginning of the pandemic in 2020, hotels in the Indian Ocean destinations have recorded significant drop in performance, in line with the rest of the world.

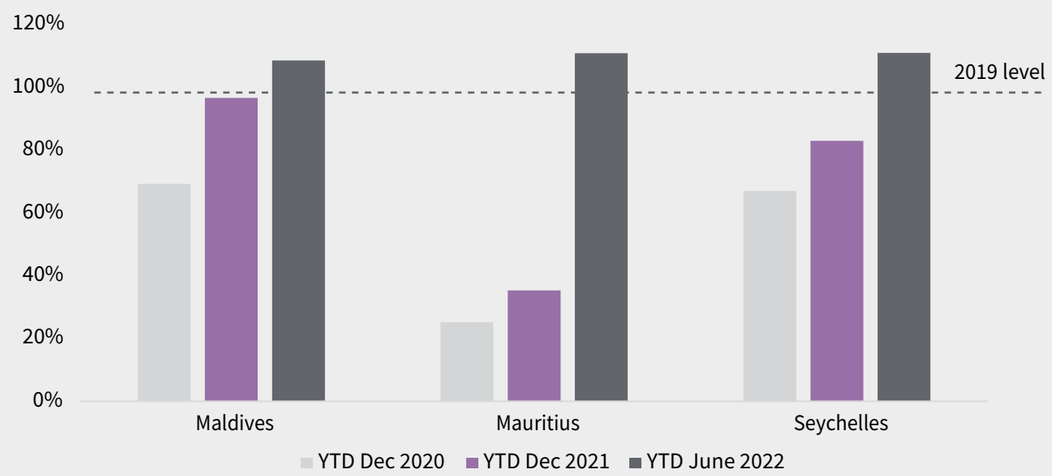
The Maldives stood out of the rest at the end of 2020: its hotels' RevPAR stood at 69% of 2019 level, as the country had reopened its borders to international visitation in July 2020, and with tourism accounting for more than 55% of its GDP on average. Considered as an ultimate luxury destination, performance in the luxury and ultra-luxury segments has pulled the overall market up. In the Maldives, wealthy international visitors came and stayed for a longer period, enabling hotels to register high levels of RevPAR during the peak of the pandemic.

Trading performance in the Indian Ocean has continued to improve as restrictions are gradually easing and borders reopening in 2021 and in the first half of 2022.

As the world emerges from one of the worst crisis induced by COVID-19, additional macro economical and global geopolitical headwinds hold back an improvement in the tourism situation which might have been even faster in all the Indian Ocean destinations, putting the spotlight on three major trends for the next 6 to 12 months:

1. Less new developments in favour of acquisitions,
2. Disparate demand and diversification of source markets,
3. Inflation headwinds leading to optimisation of cost management.

YTD RevPAR recovery relative to 2019



Notes: YTD RevPAR recovery calculated based on the same period in 2019. Sri Lanka and Zanzibar are excluded from the chart due to data constraints.
Source: STR, JLL

Top 3 trends that will shape the tourism industry in the Indian Ocean in the next twelve months

1 Less new developments in favour of acquisitions

2 Disparate demand and diversification of source markets

3 Inflation headwinds leading to optimisation of cost management

1 Less new developments in favour of acquisitions

Indian Ocean Key takeaways

- **Limited land available for development**
- **Increased interest from new pools of capital**
- **Diversification/conversion to other types of accommodation**
- **Less distress assets and need to dispose**
- **Activity around repositioning, expanding and refurbishing existing assets**
- **Gap remains between owners' and investors' pricing expectations**

Maldives

The early re-opening of the Maldives during the peak of the pandemic period coupled with high levels of trading performance has strengthen the country's attractiveness among hotel investors and operators.

Hotel players who are looking to have a footprint in the Maldives are eager to acquire lagoons to develop new resorts, but face challenges linked to global macroeconomic headwinds and access to financing, additionally to the usual burdens of a development.

Acquisition of existing assets continues to keep the momentum, as evidenced by the recent first ever portfolio transaction of the W and Sheraton to a global private equity fund. This deal sets the tone for the months and years to come as we witness increased interest from European and Middle Eastern investors.

Mauritius

The impact of the pandemic has been particularly pronounced for Mauritius, and despite government funding and wage support, local owners in particular, will need to raise fresh capital over the next five years.

By contrast, there are limited sites available for new developments and funders are proceeding cautiously with new developments until there is more certainty on how the recovery will impact their existing loan book.

However, a number of strong local owners are looking to develop out land around their resorts as a means to raise capital through the Apart Hotel scheme.

Seychelles

Relative to other Indian Ocean islands, the Seychelles enjoyed some respite from an earlier re-opening and less restrictive access. Together with the Ultra High Net Worth ownership profile, the country has seen less distress and the need to sell.

The majority of capital targeting the Seychelles hospitality market has been from the Middle East, and this is set to continue, albeit that a number of Middle Eastern owners are diversifying their focus to the Maldives, Zanzibar and other Indian Ocean destinations.

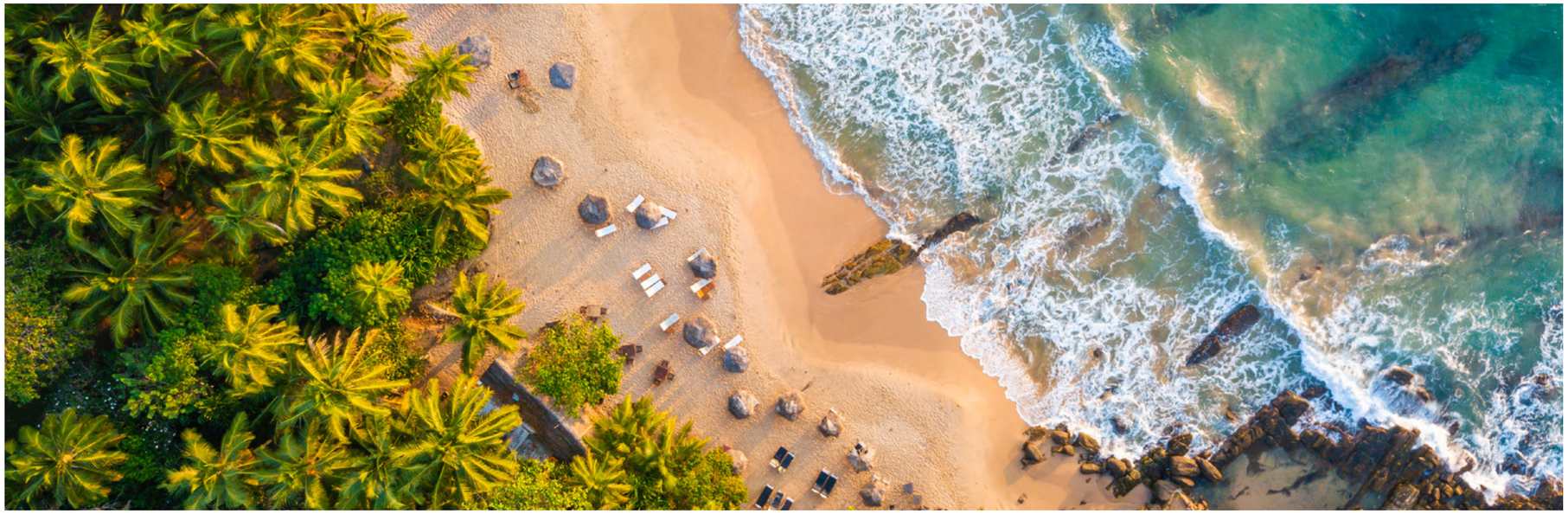
There is more development activity around repositioning, expanding and refurbishing existing resorts, than there is around developing new sites. Indeed, development is still challenging, on the back of current high construction costs.

Sri Lanka

With the high dependence and rising costs of imported construction materials, greenfield development has become increasingly challenging in Sri Lanka and we have observed a thinner fresh development pipeline.

There has been strong interest from a wide range of investors in acquiring operational assets, with a focus on Colombo and the South-west Coast. However, there continues to be a significant gap between owners and investor's pricing expectations.

With the continued stress in the hospitality industry, we expect to see softening in valuations and expect to see more traction in the hotel transaction space, once the political and economic turmoil has reduced.



Zanzibar

With fundamentals such as the opening of the new airport, positive political changes in Tanzania and relatively better performance through the COVID-19 pandemic, Zanzibar has see stronger interest in both new developments and acquisitions.

The government has made a number of strategic sites available on the main island and private islands, and this has attracted interest from local and Middle Eastern capital.

In Zanzibar, the lack of available investment grade assets is prompting investors to develop new hotels. Additionally, the drop in market values has not been as pronounced as in Mauritius or the Seychelles. However, there will be a handful of assets that come to the open market, and given the stronger market fundamental and liquidity, should attract strong interest.

2 Disparate demand and diversification of source markets

Indian Ocean Key takeaways

- Diversification of source markets
- Improved airlift with new markets and regions
- Expansion and upgrade of airports
- Focused marketing efforts to target new markets
- Proximity and open countries to attract new market sources

Maldives

The Russia/Ukraine conflict has considerably limited tourist arrivals from Russia and Eastern Europe. Indeed, from being the top first source market in 1Q 2022, Russia downgraded to third place as at YTD July 2022, displaced by India and the United Kingdom.

Currently, apart from India and Singapore, majority of the existing flight connectivity is to cities in Europe and Middle East, with those regions having dropped all travel restrictions. While flight connectivity to Asia remains limited, it is likely to improve in the coming months amid a reopening of international borders in the region.

With multiple airport expansion and upgrade of Velana International Airport, Gan International Airport and Hanimaadhoo International Airport, the Maldives will be able to accommodate more visitors to meet the growing demand of international tourists, and also diversify its source markets in the longer term.

Mauritius

Mauritius reopened its borders on the 15 July 2021 and saw demand return almost immediately from traditional source markets in Europe and South Africa, while Asian markets remained in lockdown until more recently. The outbreak of the Omnicron variant and subsequent ban of travel from South Africa in November impacted the extent of recovery in Q4.

However, from early 2022, the recovery has gathered more momentum, with most markets now able to reach the island from Q2 2022.

Improved airlift had opened up markets from Asia, the Middle East and North America over the last decade, but seat capacity outside of the major source market of Europe has declined and this will see a more fragmented recovery and the need to recover this seat capacity to continue positioning the destination for growth in the longer term.

Seychelles

Seychelles was able to open up for travel much earlier than many other markets in the region, with the island's small population of 80,000 having achieved a high vaccination rate.

The market is well connected from the gulf, and demand from the Middle East has been strong. However, the number of tourists from Russia and Eastern Europe has declined since the onset of the Ukraine crisis.

In recent years, the market has seen strong growth from the UAE and Qatar, given the high expatriate population in these two countries.

Indeed, the strong economic and migratory growth to the UAE in recent years bodes very well for the Seychelles and Zanzibar in particular, which are strategically located to leverage these economic and demographic headwinds.

Sri Lanka

India had been Sri Lanka's biggest source market before COVID-19 and continued to remain so even after the peak of the pandemic.

While long-haul markets such as the UK and Western Europe have seen a severe decline during COVID-19, Sri Lanka had seen promising growth from Central Europe, with focused marketing efforts and air bubble arrangements in place. However, the Ukraine crisis has put a stop to demand from Russia and Ukraine, once again shutting off tourism from this region.

Despite large scale infrastructure and capacity improvements underway, Sri Lanka is facing what is said to be the worst economic and political crisis in the country, compromising the tourism growth and recovery in the near to medium term.

Zanzibar

Zanzibar's decision to remain open through COVID-19, has shaped the source market mix significantly. While outbound travel was not permitted from most countries post March 2020, a number of Eastern European markets remained open, with Zanzibar being one of the few markets available for travel.

This trend continued through 2021 and into 2022, but the conflict in Ukraine has now resulted in a steep drop off in travel from Russia and Eastern Europe, while traditional source markets from Europe and Africa are recovering to see a demand profile more akin to historical segmentation.

While Eastern and Southern Europe have historically been larger markets, the Middle East is emerging as a strong alternative given the geographic proximity and excellent connectivity.

3 Inflation headwinds leading to optimisation of cost management

Indian Ocean Key takeaways

- Increased energy cost leading to use of alternative sources
- Frequency of food delivery reduced
- Purchasing as 'clusters' for economies of scale
- Imported labour leading to higher costs
- Improved air connectivity to help reduce costs

Maldives

With the ongoing Russia/Ukraine conflict and the increased fuel prices, some resorts in the Maldives generate electricity and other energies within the island, with some of them exploring alternative sources of energy such as roof spaces at the staff island for solar panes, as a supplement to diesel power house. Resorts have also implemented measures to reduce energy usages such as turning up the temperature of aircon in the villas or reducing the pool pumps.

Hotels in the Maldives are tackling supply chain disruptions by reducing the frequency of deliveries from 4 times a week to 2 to 3 times for example. Additionally, while owners and operators of multiple resorts are able to purchase items as a cluster for economies of scale, some resorts with a large island have introduced own farms, to associate with the "farm-to-table" concept whilst reducing costs.

Mauritius

Mauritius has historically enjoyed lower operational costs than some of the other Indian Ocean islands, with relatively stronger supply chains and lower energy and labour costs.

This, together with the fact that most accommodation packages are set in Euro's, while the local currency has depreciated to the Euro, providing a revenue windfall that will offset the inflationary headwinds better than other markets in the Indian Ocean.

Seychelles

The absence of local supply chains and reliance on imported goods makes the Seychelles particularly exposed to inflationary headwinds.

Resorts on the outerlying islands are more exposed to these headwinds than supply on the main islands of Mahe and Praslin. Given the small size of the population, Seychelles has to import labour to support the sector and this generally leads to higher labour costs.

Sri Lanka

In this midst of its worst economic crisis since independence, hotels have seen an alarming increase in costs. In a drive to reduce imports, taxes on luxury items have increased substantially including duty on imported foods and alcohol, widely used by hotels.

The country is facing an acute shortage of fuel, food and other essential materials, while it is also struggles with lengthy electricity blackouts and rapidly rising inflation rates. While Sri Lankan hotels have streamlined operations during the pandemic period, with lower operating costs and leaner staffing structures, the current operating environment has proved to be an additional challenge.

Zanzibar

The conflict in Ukraine has been particularly disruptive to supply chains in Tanzania and Zanzibar. Food and energy inflation are seeing the brunt of this, with Tanzania historically reliant on Russian oil imports, and like many other East African countries, Ukrainian grain.

However, the opening up of the new airport will mitigate this impact, particularly of higher oil prices, with larger aircraft now able to access the island directly, rather than through the mainland.

Performance and investment outlook in the Indian Ocean is strong, despite macro headwinds and volatility

The Maldives, Mauritius, Seychelles and Zanzibar have already recorded a robust recovery since the pandemic due to progressive border policies and pent up demand for luxury and idyllic resort destinations. As airlift continues to recover and global tourism picks up, we expect the Indian Ocean to be a strong beneficiary of this demand, which will in turn continue to attract hotel investment.

In the short to medium term source market diversification and progressive destination marketing will be important to counter some of the macro headwinds around the globe. Inflationary pressure will squeeze consumers as well as putting pressure on operating margins, whilst increased fuel and airline pricing will increase the overall budgets needed for (predominantly) long-haul travel into the Indian Ocean. Given the ecological sensitive nature of the Indian Ocean region, we expect real commitment to sustainability to become a necessity for the destination and operators, yet also an opportunity to positively differentiate.

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