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Policy for Industrial Development:
A Case Study of the Clothing Industry in Mauritius

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Industrial Strategy Project

Introduction

During the 1960s, the performance of the Mauritius economy was below the average for Africa. The unemployment level was 20%, Gross Domestic Product (GDP) was declining and the largely agriculturally based economy was not deemed sustainable. Growth prospects were bleak.

Over the following three decades, between 1973 and 1999, an intense period of economic growth was experienced in Mauritius. GDP grew at 5.9% compared with 2.4% for Africa; life expectancy increased from 61 years in 1965 to 71 years in 1996, Income inequality improved and consumer price inflation in Mauritius (7.8%) remained far below the average African price level (25%).

A major cause of the economic success enjoyed by Mauritius was the rapid growth of the clothing industry. This policy brief presents the key industrial policies responsible for developing the clothing industry. The brief also highlights the challenges faced by the clothing industry and examines the mechanisms used by policy makers to meet such challenges in order to overcome growth constraints.

Extent of the Clothing Industry in Mauritius

- The growth of the clothing industry was reflected in its share of GDP, which rose from 25% in 1970 to 33% in 1995.

- Employment by the clothing sector rose from 9% in 1970 to 35% in 1995, reducing the total unemployment rate to less than 2%.

- Growth in clothing industry dominated the industrial sector during the 1980s.

- In 1985, the rate of export of sugar had been eclipsed by EPZ exports and by 1993 accounted for 70% of exports, 78% of which were clothing and textiles. Clothing and textiles produced 53% of overall exports.

- Manufactured exports established themselves in the lower and middle market segments in the EU and US markets.

- By 1993, 62% of manufacturing employment was involved in clothing.

Factors that Contributed to the Growth of the Clothing Industry, 1980s

Investment

- Cheap labour and quota-freedom in Maurtius.

- Demand for clothing increased rapidly in the two major markets of Europe and the United States

- Family connections between Mauritius and Hong Kong

Competitiveness

- From the mid-1980s, the competitiveness of Mauritian clothing was bolstered by a favourable exchange-rate regime.

Policy Approaches to the Clothing Industry

The turn-around in the economy of Mauritius began in the 1970s, when the economy diversified away from the monocrop agricultural product, sugar, into industry, made up mainly of tourism and export-focused manufacture. In fact, the biggest contributor to economic growth was the rapid growth in the manufacturing industry, especially the clothing industry.

This section highlights the major policy initiatives undertaken to spur the growth of the clothing industry in Mauritius between 1973 and 1999.

Export Processing Zone

Before independence, the manufacturing industry was involved mainly in import substitution. In 1970, an Export Processing Zone (EPZ) programme was launched. The programme was modelled on similar programmes used in the Far East, which produced excellent results in the start-up of a range of industries.

Policy for EPZ Programmes:

Duty free access was provided to all imported manufacturing inputs, so that domestic taxes could not raise the cost of inputs and thus undermine the global competitiveness of EPZ firms.

Tax incentives effectively subsidised EPZ firms. Tax incentives included a 10-year tax holiday on retained earnings and a partial tax holiday for periods beyond that; free repatriation of capital and profits, and preferential interest rates for EPZ firms.

Labour market conditions were less restrictive for EPZ firms. Employers had greater flexibility in discharging workers, for example, severance packages were not mandatory for retrenched workers, and it was also not necessary to notify a statutory body before retrenching workers. Overtime conditions were more flexible. Although the basic rate of pay was the same as non-EPZ firms, the rate of pay for female workers was below the standard wage. As the majority of manufacturers employed females, it effectively subsidised EPZ industries.

Results of the EPZ Programme:

- Mauritius became Africa's leading clothing exporter and the third largest producer of woollens globally.
- Of the new industries, clothing and textiles accounted for more than 80% of EPZ exports.
- The creation of the EPZ effectively liberalised trade.
- New opportunities of employment and trade were created, especially for women.

International Agreements

Trade in Mauritius has benefited greatly from participation in international groups and treaties. Mauritius belongs to the:

- *World Trade Organisation* (Mauritius is a founding member of the WTO)
- *Lomé Convention* (under which the products of Mauritius are able to enter the European Union quote-free and duty-free)
- *Common Market for Eastern and Southern Africa* (members of COMESA enjoy preferential access to other member markets. Mauritian exports to this market have increased from Rs 11 million in 1986 to Rs 1 billion in 1995)

- Southern African Development Community (SADC)

Mauritius has *bilateral trade agreements* with the Central African Republic, Egypt, Hungary, Madagascar, Pakistan and Zimbabwe and is a beneficiary of the *Generalised Systems of Preferences* (GSP), which offers tariff preferences or duty-free entry on the export of a wide range of products to Australia, Austria, Canada, the EU, Japan, Norway, Switzerland, and the United States. The *African Growth and Opportunity Act* (AGOA) also offers preferential access to American markets.

Double taxation agreements have been signed with the following trading partners: Germany, France, United Kingdom, Italy, Sweden, India, Pakistan, Singapore, Malaysia, Swaziland, Zimbabwe, China, Botswana and Madagascar.

Investment in Human Capital

Mauritius recognises that human capital as a very valuable resource, as reflected by various policies in different spheres of education and training.

Primary and Secondary Education

Mauritius has offered free education to all since 1976, with primary school education compulsory.

Tertiary Education

The University of Mauritius offers postgraduate courses in civil, mechanical and production, electrical and electronics engineering computer science and textile technology and sugar technology. The emphasis is on scientific study, and the Faculty of Engineering is equipped with modern and sophisticated machinery for the specific training of personnel for manufacture.

Industrial Training

The Export Processing Zone Development Authority (EPZDA) was set up in September 1992. EPZDA promotes technology, research and information dissemination, provides training to industry and supports services in regional co-operation.

A Training Advisory Committee (TAC) was set up to advise on training programmes that will specifically meet the needs of Mauritian industry. TAC advises the Industrial and Vocational Training Board (IVTB) on what courses are needed. The IVTB then co-ordinates with the various vocational training institutes that offer a range of courses, such as engineering, electronics, jewellery, printing and textiles. Companies are able to apply for training grants, up to 70% of cost, for courses either in-house or abroad.

The culture of training extends from government to clothing manufactures – who aggressively support training and bonus schemes for their employees since they regard labour as a key factor in improving productivity.

Today Mauritius claims the highest literacy rate in Africa.

Gender Equality

New legislation was introduced to ensure equal treatment and employment opportunities. Government focused specific attention to the fact that so many girls drop out of high school, and have a poor level of entry into subjects that are viewed as traditionally male.

Statistics from a 1990 census shows that 72% of elderly men had attended school against only 47% of elderly women. The Government has turned these statistics around because, at present, primary school attendance for girls is 100%.

The Government is also working with the UNDP to integrate a gender perspective in its budget process through staff training.

Environmental Issues

Environmental degradation is a serious impediment to economic growth. In tension with the planned growth of the tourist trade, the Government is increasingly aware of the importance of sound environmental practice, and the importance of protecting the natural assets of the environment and has formulated a *National Environmental Action Plan*.

Coastal zone development was threatened by overexploitation and pollution. Thus, the Government further formulated an *Integrated Coastal zone Management Plan* to manage coastal shores and other shorelines. It is hoped that this plan will reduce the risk of damage through proper long-term planning and control.

Policy Responses to challenges faced by Industrial Development

In order to achieve economic success, Mauritius had to meet many challenges. A key explanatory factor in the success story of Mauritius has been effective policy coordination.

EPZ Programme Development

Although the creation of the EPZ was the main reason for the growth in the clothing industry, it was not without its challenges. In 1976, EPZ firms struggled with internal and external challenges, such as wage demands, stagnation of the world market and high appreciation of the Rupee.

This resulted in one-third of the new EPZ firms which numbered 84, closing down and saw the rate of unemployment climb back up to its former level of 20%.

Policy makers in Mauritius responded with five strategies to create a favourable environment for exports and investments in the early 1980s:

- Adoption of a flexible exchange rate policy
- Adoption of a cautious wage policy (part of a structural adjustment programme agreed upon with the IMF and the World Bank)
- Creation of the Mauritius Export Development & Investment Authority (MEDIA) to actively promote the EPZ to foreign investors.
- Double taxation agreements with countries that were main investment and trade partners
- Introduction of an export credit insurance scheme, which included incentives for productivity and attendance bonuses, free transportation and improved working conditions.

These strategies involved co-ordination among a series of government departments and other support institutions. This collective response to the specific challenges that the EPZ programme faced assisted in creating a more coherent incentive environment for business.

Productivity Decreases

In the late 1980s, larger, foreign owned firms began to outsource more labour-intensive, cut-and-sew work to local, smaller firms, referred to as cut, make and trim (CMT) in order to fill the long run orders.

Although CMTs received financial assistance from government, they found it difficult to survive as owners lacked experience and training. The expansion of CMTs was associated with a *decline in productivity*.

Labour Market Pressures

During the 1990s, pressure from a *decreasing labour market* and pressure from *changes in the demands of the American and European clothing markets* presented challenges to the clothing industry.

The unemployment rate was only 1.6% in 1994 so due to the decrease in available labour, wages increased. Temporary labour from China, India and Sri Lanka were contracted. Meanwhile manufacturing costs were rising because of bonus schemes that were being implemented to keep and motivate staff. Profit margins fell and industries no longer enjoyed the advantage of cheap labour costs in comparison with other developing countries.

At the same time, the core export markets began to change their demand patterns. Increasingly, EU and US buyers were demanding better product quality and wider product ranges. The prices did not rise to compensate for the extra burden on manufacturers, particularly on basic lines, as the EU and US buyers extended their sourcing to lower-cost regions.

By mid-1990, the clothing industry faced serious problems, namely real output had declined, many clothing firms and CMTs were forced to shut down, productivity had stagnated, dependency on foreign labour was increasing, profitability was falling and debt was rising.

Policy makers responded to these challenges faced by the clothing industry by promoting the *modernisation of the production system* and *quality improvement*. Policies directed toward these aims included:

- A *Technology Diffusion Scheme* (TDS) was introduced by the government, assisted by the World Bank. The scheme offered to support half of any consultant fees involved in introducing new technology. More than 200 companies are now using this programme.

- The *Mauritius Export Processing Zone Association* (MEPZA) organised the *National Quality* award to promote quality control.

- The government also offers 85% of the training fees for employees trained at the *Industrial and Vocational Training Board*.

Government response to the additional pressure was complemented by efforts successfully undertaken by the Mauritian manufacturers themselves. In order to overcome the obstacles, manufacturers began to

- Diversify export markets, and looked towards the markets of East Europe, Scandinavian countries and Eastern and Southern Africa

- Search for regional locations that offered cheaper labour.

The process of *delocalisation* began in 1991and speeded up between 1996 and 1997. Madagascar was the major destination of the Mauritian clothing manufacturers, other operations delocalised to

India. Besides cheaper labour, the move presented new opportunities to manufacturers, namely:

- A much larger proportion of longer runs of labour-intensive basics could be produced
- Ironically, there was a movement back to the basics and toward volume production.
- Clothing exports from Madagascar could penetrate the US market without any quotes.

Country-specific Obstacles

Every country faces unique obstacles that require special policy attention and industry response. For Mauritius, the relative *geographical remoteness* of Mauritius to major markets was a major challenge facing manufacturers. They met this challenge by producing highly labour-intensive basic or classic garments such as shirts and woollen sweaters. Production runs were thus not seasonal, and enjoyed a relatively long lead-time so that planning was done well in advance of delivery.

Looking Ahead: Sustaining Economic Growth through Industrial Diversification

The strength of the Mauritian economy lies in the growth of manufactures, particularly the clothing industry. Due to the commodity dependency on Western markets, there is recognition that the growth cycle of the 1970s and 1980s cannot be sustained, and that further industrial diversification must take place. The government has therefore turned its attention to the *service sector.*

The service sector includes the *hospitality industry, financial services, and information and communications technology*.

Financial Services

In the last few years, there has been a growing trend for banks and other financial services to establish themselves offshore to gain a competitive edge by lowering administrative costs. To promote the service sector, policy makers have:

- Established a regulatory framework for offshore banking and other offshore financial services, along with the liberalisation of financial markets.
- Created the *Mauritius Offshore Business Activities Authority* to attract international financial business.
- Launched the Stock Exchange of Mauritius.

Tourism

Tourism is a big foreign exchange earner in Mauritius and there is still ample room for growth. Government initiatives to promote this industry include the funding of a public relations campaign in the United States.

The Governments *National Long Term Perspective Study* states that the following conditions are needed to improve receipts from the tourism sector:

- More investment, including foreign investment
- Continuing high standards of quality in hotels
- Well-trained staff

- Development of the national airline
- Exclusion of cheap charters
- Development of supporting infrastructure
- Provision of some inland attractions
- Effective marketing
- Continuing partnership between government and business
- Effective environmental regulation
- Retaining the position of upper niche tourist destination.

Future policy must strive to retain the occupation of the upper niche in the tourism market as well as awareness of the pressure placed on natural resources. To this end, government is focusing on the quality of the product offered, and is placing more importance on the training of staff in the hospitality industry.

IT Services

The IT sector is an important source of income for many countries. For example, in Ireland, an influx of IT companies and professionals contributed to an 8% annual increase in economic growth between 1993 and 1998. Unemployment fell from 20% to 5% in the same period.

The Mauritius government is committed to developing its IT sector, for example,

- The primary school curriculum has been revised in order to offer computer training for all, including the 5 to 8 age group.
- MEDIA promotes its state-of-the-art telecommunication infrastructure, offered at competitive prices.

- A *One Stop Shop* has been set up to smooth the path for potential investors (it assists in dealings with all government departments, as well as provides information on issues such as investment incentives).
- Financing schemes for existing firms to update their technology are offered, as well as computer loan schemes and soft loans to enable the children of sugar workers to obtain computers.

Policy for Industrial Development

Government response to challenges faced during the growth face of the clothing industry produced industrial policies that worked well for Mauritius. This section highlights the types of policies needed to promote industrial development, based on those used by policy makers during the growth period in Mauritius.

1. **Export Processing Zone (EPZ) programmes** - provide duty free access, tax incentives and flexible labour market conditions.

2. **Creation of a favourable environment for exports and investments** - policy instruments include a flexible exchange rate policy; cautious wage policy; doubling of the taxation agreements with countries that are main investment and trade partners; introduction of export credit insurance schemes and promotion of EPZs to foreign investors

3. **Participation in international groups and treaties** - improves trade relations and provides incentives for exporters.

4. **Investment in human capital** - equips the workforce with skills necessary to develop industry. Courses offered at schooling and

tertiary education levels can provide training in areas crucial for future industrial development, e.g. IT. Industrial training programmes can be subsidised. This is especially important to sustain and improve productivity levels.

5. **Promotion of gender equality**

6. **Sound environmental practices** - to sustain the resources needed for industry, e.g. tourism.

7. **Solutions to country-specific problems** - e.g. to overcome the problem of geographical remoteness, Mauritius produced non-seasonal clothes.

8. **Policy responsiveness and flexibility** - demand patterns continually change in new industries, e.g. greater demands for improved quality. Industrial policy should find ways to assist industry in adapting to new demands, e.g. subsidising new technology and promoting quality.

9. **Promotion of delocalisation** - to reap benefits offered in other countries.

10. **Industry diversification -** diversifying into parts of the service sector such as tourism, financial services and information and communications technology can unleash great economic potential.