INTERNATIONAL MONETARY FUND

IMF Country Report No. 19/386

SEYCHELLES

FOURTH REVIEW UNDER THE POLICY COORDINATION INSTRUMENT AND REQUEST FOR MODIFICATION OF TARGETS

December 2019

In the context of the Staff Report for the Fourth Review Under the Policy Coordination Instrument and Request for Modification of Targets, the following documents have been released and are included in this package:

- A **Press Release** including a statement by the Chair of the Executive Board and summarizing the views of the Executive Board as expressed during its December 17, 2019 consideration of the staff report on issues related to Fourth Review Under the Policy Coordination Instrument and Request for Modification of Targets and the IMF arrangement.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on a lapse-of-time basis, following discussions that ended on September 24, and in Washington DC that ended on October 18, 2019, with the officials of Seychelles on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on December 3, 2019.

The IMF's transparency policy allows for the deletion of market-sensitive information and premature disclosure of the authorities' policy intentions in published staff reports and other documents.

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IMF Executive Board Completes Fourth Review Under the Policy Coordination Instrument for Seychelles

- The implementation of the Seychelles' economic program is largely on track.
- The 2019 economic growth is estimated to reach about 4 percent, reflecting strong output in the tourism and communication sectors.
- The near-to-medium-term economic outlook continues to be favorable, provided that the authorities maintain their prudent policies under the Policy Coordination Instrument.

On December 17, 2019, the Executive Board of the International Monetary Fund (IMF) completed the fourth review under the Policy Coordination Instrument (PCI) for Seychelles.[1] The Executive Board's decision was taken without a meeting.[2]

The PCI was approved on December 13, 2017 (see Press Release No. 17/492). Seychelles was the first IMF member country to request a PCI, since the Executive Board of the IMF approved the PCI as a new non-financing instrument to further enhance the effectiveness of the Fund's toolkit.

Macroeconomic performance continued to be strong in 2019. Economic growth is estimated to reach around 4 percent, reflecting strong output in the tourism and communication sectors. Inflation has been on a declining trend since early 2018. The gross international reserves remain at an adequate level. The Central Bank of Seychelles (CBS) lowered the monetary policy rate at end-September 2019, citing benign inflationary pressures in the coming months. Program implementation is largely on track, while the 2020 budget submitted to the National Assembly is in line with the program. The near-to-medium-term economic outlook

[1] The PCI is available to all IMF members that do not need Fund financial resources at the time of approval. It is designed for countries seeking to demonstrate commitment to a reform agenda or to unlock and coordinate financing from other official creditors or private investors. (see https://www.imf.org/en/About/Factsheets/Sheets/2017/07/25/policy-coordination-instrument).

[2] The Executive Board takes decisions without a meeting (based on lapse-of-time procedures) when it is agreed by the Board that a proposal can be considered without convening formal discussions.

continues to be favorable, provided that the authorities maintain their prudent policies under the PCI.

The authorities are committed to the primary fiscal surplus target of 2½ percent of GDP through 2022, by steadily reducing the public debt-to-GDP ratio over the medium term and implementing permanent measures envisaged in the 2020 budget. The government intends to keep a very tight rein on Air Seychelles' financial position. The CBS is committed to a flexible exchange rate, while being vigilant to both upside and downside risks to inflation. The structural agenda focuses on strengthening the AML/CFT framework, buttressing financial stability, and enhancing inclusive growth, including by improving the business climate.

INTERNATIONAL MONETARY FUND

SEYCHELLES

December 3, 2019

FOURTH REVIEW UNDER THE POLICY COORDINATION INSTRUMENT AND REQUEST FOR MODIFICATION OF TARGETS

KEY ISSUES

Context: Economic developments since the completion of the 2019 Article IV consultation and the third review under the Policy Coordination Instrument (PCI) in June 2019 have been broadly in line with expectations. The program is largely on track. The 2020 budget recently submitted to the National Assembly is in line with the program and the major infrastructure and climate change related projects would be implemented within the fiscal parameters under the PCI.

Program performance: All quantitative targets (QTs) for end-June 2019, the program's fourth review test date, were met except for the primary fiscal surplus target, which was missed by a very small margin due to a delay in receipts from the 2016–17 sales of a telecom company. Inflation was well within the inner bound of the monetary policy consultation clause (MPCC) for end-June 2019. Implementation of a few structural reform targets is delayed for technical reasons and capacity constraints. Staff recommends completion of the fourth review under the PCI.

Outlook and Risks: The economic outlook continues to be favorable. Downside risks to the outlook largely stem from possible external shocks, including weakness in the key tourism markets and global banks' withdrawal of correspondent banking relationships (CBRs). Domestic risks center on potential fiscal slippages related to the election year and Air Seychelles: the latter has partially materialized and further slippages could threaten the baseline projection of a steady reduction of the public debt-to-GDP ratio over the medium term. Risks to the program are considered moderate, given Seychelles' strong track record and continued commitment to safeguarding macroeconomic stability.

Key policies: The authorities are committed to the primary surplus target of 2½ percent of GDP through 2022, which would shore up a steady reduction of the debt-to-GDP ratio over the medium term, by implementing permanent measures envisaged in the 2020 budget. The government intends to keep a very tight rein on Air Seychelles. The CBS will be vigilant to both upside and downside risks to inflation and is committed to a flexible exchange rate. The structural agenda focuses on strengthening the AML/CFT framework; buttressing financial stability; and enhancing inclusive growth including by improving the business climate.

Approved By
David Owen (AFR) and Martin Sommer (SPR)

Discussions were held in Victoria during September 16–24, and in Washington DC during October 15–18, 2019. The staff team comprised Mr. Konuki (head), Messrs. Dhungana and Massara (all AFR). The mission met with the Minister of Finance, the Governor of the Central Bank, other senior officials, and representatives of the private sector. Mr. Khurelbaatar (OED) also participated in the discussions. Ms. Gupta provided research support and Ms. Bieleu provided assistance for the preparation of this report.

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RECENT DEVELOPMENTS, OUTLOOK AND RISKS

1. **Economic conditions continue to be favorable (Figures 1–3, Tables 1-5).** Growth momentum appears to remain strong. Tourism receipts increased by 5 percent year-on-year (yoy) for the first eight months of 2019 with robust growth from the major European markets, according to the Central Bank of Seychelles (CBS) survey. Production in tourism and communication sectors grew strongly in the first half of 2019. The nominal exchange rate has been stable in recent months. The headline yoy CPI inflation rate declined to 1.4 percent in September from over 4½ percent in early 2018, due to the tight monetary policy stance since the second quarter of 2018, a decline in international commodity prices in recent months, and increased competition among local retailers. Citing benign inflation pressures in coming months, the Central Bank of Seychelles (CBS) lowered the monetary policy rate by 0.5 percentage points at end-September 2019.[1] Private sector credit growth accerelated to 16.2 percent at end-September from 11½ percent at end-2018 driven by a pick-up in loans to tourism and fishery sectors in recent months. Financial soundness indicators suggest that commercial banks are adequately capitalized and profitable.

2. **The near- and medium-term economic outlook continues to be benign provided that the authorities maintain their prudent policies under the PCI.** Growth is projected to moderate to around 3½–4 percent during 2019–20, around the potential rate, due to the moderation of tourism and fishery sector growth compared with 2016–17, and the moratorium on large hotel construction projects until end-2020.[2] Growth and foreign direct investments (FDI) should pick up after the lifting of the moratorium on large hotel construction projects at end-2020. The external current account deficit is projected to be around 17–18 percent of GDP for the next several years and would continue to be mostly financed by FDI. The gross international reserves' (GIR's) ARA metric is expected to remain adequate, at around the current level of about 122 percent in the medium term. Despite potential demand pressures arising from public-sector wage adjustment to be implemented in late 2019 and the brisk pace of private sector credit growth, weakening international fuel prices in recent months and the increased competition in the domestic retail sector should contain inflation in coming months.[3]

3. **Risks to the outlook presented above are broadly unchanged from those presented at the 2019 Article IV consultation and remain tilted toward the downside**. The most significant sources of downside risks relate to external shocks. Intensification of geopolitical tensions and security risks could considerably reduce tourist arrivals, while structurally weaker global growth could dampen tourism performance and tuna exports in the medium term. Seychelles' financial sector could be affected by international banks' potential withdrawal of correspondent bank relationships (CBRs). Higher-than-projected international energy prices could negatively affect

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[1] The mid-point of the interest rate corridor serves as the policy rate of the CBS.

[2] The large hotel moratorium introduced in late 2015 prohibits construction of new large hotels until end-2020.

[3] Implementation of a 5 percent increase on the salary table for public services, which was originally scheduled in April 2019, will be delayed to late 2019 because of a legal challenge brought to the court in the Spring of 2019. The salary scale revision is done every five years as stipulated in the Salary Act and reflected in the 2019 budget.

Seychelles' external balance, inflation, and Air Seychelles' financial position. Domestic risks are centered around potential fiscal slippages. Risk related to Air Seychelles has already materialized partially in the form of unexpected provision of guarantees despite the company's operational restructuring being implemented as planned so far (see ¶6). Any slippages in Air Seychelles' restructuring could place additional pressures on the budget and negatively affect the public debt dynamics. The government may face challenges in achieving the primary surplus target in 2020 when the Presidential election will take place.[4] On the upside, tourism sector growth could be stronger than projected in the next few years. Meanwhile, lower-than-projected international fuel prices would help strengthen Seychelles' external position, contain inflation, and enhance growth.

PROGRAM PERFORMANCE

4. Most quantitative targets (QTs) were met while the implementation of a few reform targets (RTs) is delayed due to technical reasons:

- **The end-June floor on the primary fiscal surplus was missed by a razor-thin margin** (SCR 11 million, 0.05 percent of GDP) due to a delay in stamp duty receipts from the 2016–17 sales of a major telecom company to a new operator, which was expected in June (SCR98 million, 0.5 percent of GDP)[5] and of dividends from a few state-owned enterprises (SOEs).

- **The end-June floor on net international reserves (NIR) was met,** exceeded by US$13 million thanks to the buoyant tourism receipts. 12-month average inflation at end-June was well within the inner bound of the monetary policy consultation clause (MPCC).

- **All continuous targets have been met.**

- **While the implementation of a few RTs is delayed, the authorities are making progress toward meeting the 5th and 6th review RTs proposed at the time of the 3rd review**. Amendments on Public Enterprise Monitoring Committee (PEMC) Act, which will give PEMC more enforcement powers, will be submitted to the Cabinet in December 2019, slightly delayed from the original target of end-September because the government intends to ensure consistency with other PFM related regulations, including a new Public Enterprise Act which is currently under consideration (Program Statement (PS)¶20). Although the Cabinet approved the policy framework paper for crisis management, bank resolution and safety nets in December 2018, the relevant draft legislation will be submitted to Cabinet in November 2020, reset from the target of end-March 2020, due to staffing constraints of the Attorney General's office (PS¶31). The authorities are making good progress in achieving all other 5th and 6th review RTs set at the time of the 3rd review (see below).

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[4] While the presidential elections is due to be held by September 2020, the opposition is vocal in demanding early elections.

[5] The government expects to receive this stamp duty in coming weeks.

POLICIES IN THE PERIOD AHEAD

A. Buttressing Fiscal Sustainability

5. **The 2019 primary surplus is likely to be in line with the target under the PCI.** Supported by the expected underspending of wage bills, due to the delayed implementation of the 5 percent salary scale adjustment, and small under execution of goods and services and capital expenditures, the primary surplus is projected to reach 2½ percent of GDP in 2019. Given the lower-than-expected collection of fees and charges for the first eight months of 2019, the authorities requested a very small downward revision to the end-December 2019 floor on primary surplus (SCR5 million, 0.02 percent of GDP).

6. **The authorities remain committed to the prudent fiscal policy envisaged under the PCI.** The 2020 budget, together with 3-year revenue and expenditure projections, recently submitted to the National Assembly targets the primary surplus of 2½ percent of GDP through 2022, in line with the fiscal parameters under the PCI. Nonetheless, with a planned injection of guarantees of $30 million (about 2 percent of GDP) to protect the other shareholder's preference shares of Air Seychelles (see PS¶22), the public debt-to-GDP ratio is projected at around 51¾ percent, marginally above the authorities' debt reduction goal of below 50 percent by end-2021. However, under the baseline, this primary surplus would lead to a steady decline of the public debt-to-GDP ratio from the current level of about 61½ percent to around 47 percent by end-2022, assuming an unwinding of SCR200–300 million each year during 2020–22 of government debt issued for monetary policy purposes (Annex I). This is in line with medium-term fiscal sustainability and would not complicate CBS' monetary policy conduct, striking the right balance between preserving economic stability and addressing the authorities' priority investment needs to build up infrastructure and enhance resilience to climate change (Annex I of Country Report No 19/194).

7. **To secure the primary surplus targets from 2020 onwards, the authorities have introduced permanent revenue enhancing and expenditure saving measures in their 2020 budget and intend to keep a tight rein on current expenditure.** The one-off stamp duty receipts from the telecom company sales of about 1 percent of GDP will expire in 2020. President Faure recently announced an increase in pension benefits and the minimum wage from SCR5,250 to SCR5,750 a month from the beginning of 2020, which is estimated to cost about ½ percent of GDP starting in 2020. The 2020 budget introduces various permanent fiscal saving measures to bring the primary surplus in line with the program target. On the revenue side, the government would introduce permanent measures: increase an environmental levy on motor vehicles and various fees; change the excise structure for alcoholic beverages; introduce property tax,[6] personalized license plate numbers, and processing fees for postage and courier services. These measures are estimated

[6] Implementation of the property tax was delayed into early 2020 due to the technical issues to be resolved by the AG office. This tax discriminates between residents and nonresidents and is thus a capital flow management measure

to enhance revenues by about 1 percent of GDP, largely offsetting the loss of the one-off stamp duty (text table).On the expenditure side, better targeting of social welfare programs would create savings of about 0.1 percent of GDP in 2020 (Box 1) while the 2020 budget imposes a freeze on recruitment of non-essential staff and a reduction of low-priority goods and services spending, which are estimated to create a saving of about ¼ percent of GDP (PS¶11). In addition to these permanent expenditure saving measures, cessation of one-off spending in 2019, such as international sports events, would reduce the spending on goods and services by around ¼ percent of GDP in 2020 compared with 2019. The total savings from these above-listed revenue-enhancing and expenditure-saving measures would be enough to plug the hole of the loss of one-off revenue and finance the costs of pension and minimum wage increases and capacity enhancement of institutions relevant for AML/CFT in 2020. Beyond 2020, the nominal growth of current expenditure would be contained by various measures, including procurement reforms, by removing duplication of government services performed by different agencies and by new staffing and recruitment planning[7], as well as continued implementation of better targeting of social welfare spending.

Fiscal Saving Measures Incorporated in the 2020 Budget

Measures	Saving impact in 2020	
	In SCR million	In percent of GDP
Revenue side		
Inreased environmental revy on motor vehicles	42.1	0.17
Change in excise structure for alcoholic beverages	43.4	0.18
Introduction of property tax	40	0.16
Increase in Financial Services Authority (FSA) registration fees	50	0.20
Inrease in Gainful Occupation Permit (GOP) fees for foreigners	30	0.12
Introduction of a personalized licence plate	10	0.04
Introduction of a processing fees for postage and courier services	6.8	0.03
Subtotal	222.3	0.91
Expenditure side		
Better targetting of social welfare programs	30	0.12
Freeze in hiring of non-essential staff	38	0.16
Reduction of low-priority goods and services	36.4	0.15
Cessation of one-off spending in 2019	43.2	0.18
Subtotal	147.63	0.60
Total	369.93	1.51

Source: Ministry of Fince, Seychelles

Box 1. Social Welfare Programs in Seychelles

The government intends to create savings by better targeting the social welfare spending. While Seychelles spends 5¾ percent of GDP on social welfare programs, the current social protection system supports households that are not needy, while most households in need do not get assistance, according to the World Bank's analysis. Eligibility criteria create inequities through a complex system of exclusions, deductions, and cost sharing arrangements.

With the help of the World Bank experts, the authorities recently delineated a medium-term plan to better target and enhance the quality of social protection. Starting in 2020, measures to enhance efficiency in service delivery of home care services, targeting needy individuals, will be implemented, while stricter criteria for invalidity and disability benefits will be introduced (PS¶12). Over the medium term, a household level database will be established to better identify the needs of potential beneficiaries while a new assessment methodology to define the eligibility criteria and benefit level of various welfare programs, including the home care program and disability pensions, will be introduced. These better targeting and rationalization measures are estimated to produce fiscal saving of 0.1 percent of GDP in 2020 and 0.3–0.4 percent of GDP over the medium term. Meanwhile, such measures could bring a significant number of homes careers and recipients of various benefits into the labor force in the medium term, which could help enhance prospects for potential growth and expand the income tax base.

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by virtue of its design according to the Fund's Institutional View on capital flows. Staff reiterated its advice to remove the discriminatory feature in the tax (see Country Report 19/194.).

[7] Over the medium term, procurement reform and removing of duplication of government services are estimated to produce savings in goods and services by about ½ percent of GDP while new staffing and recruitment policies, together with the removal of duplication of services, are projected to reduce wage bill by about ¾ percent of GDP.

8. The authorities intend to take a phased approach in executing large infrastructure and climate change related projects, in line with the staff's advice at the time of the 2019 Article IV consultation. The authorities are committed to implementing the large investment projects announced in the 2018 State of the Nation Address (SONA) and other climate change related projects[8] within the envelope of the primary surplus targets of 2½ percent of GDP through 2022 and a steady reduction of public debt-to-GDP ratio for the next several years. The authorities plan to rely on concessional external financing and public-private-partnerships (PPPs) to the extent possible to finance these large projects, with a view to shoring up the steady reduction of public debt (PS¶13). For instance, the conversion of electricity generation from heavy fuel to Liquefied Natural Gas (LNG), which accounts for about one-third of total cost of the authorities' climate change mitigation and adaptation efforts will be done through a PPP with advice from the International Finance Corporation (IFC).[9] To create further space beyond the debt reduction through 2022, the government intends to explore the possibility of taking additional policy measures discussed at the time of the 2017 climate change policy assessment (CCPA) over the medium term, including a gradual introduction of a carbon tax in the context of a comprehensive tax reform.[10]

9. The government's efforts to reduce potential risks arising from PPPs and to enhance the efficiency of public investments continue. Staff welcomed the PPP bill that was recently submitted to the National Assembly (PS¶17). The bill would provide a strong institutional framework, including detailed procedures for project approval, screening, and contract management for PPPs. The government plans to undertake the Fund's Public Investment Management Assessment (PIMA) by mid-2020.

B. Minimizing Fiscal Risks

10. The government continues its efforts to further reduce debt-related risks. Although the public debt path remains below the high-risk benchmark under all shock scenarios, major sources of risks to public debt sustainability center around high gross financing needs as highlighted in Annex I, which arise from the still high level of debt and the short maturity of domestic debt. The authorities plan to issue 3-, 5-, and 7-year bonds to replace maturing short-term debts during 2020, as they did in August 2019. Such extension of domestic debt maturities would help reduce rollover risk and gross financing needs over the medium term. It would also help develop the domestic debt market, which would play a role in enhancing the transmission mechanism of the monetary policy. The government decided to cancel a liability management exercise to swap current US dollar obligations of around US$130 million into Euros (PS¶19). The authorities recognize the potential

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[8] The total cost of these projects whose financing is yet to be identified is estimated at around 40 percent of 2018 GDP over their life span. See Country Report No. 19/194 for staff's analysis on long-term implication of these projects on the country's external stability and fiscal sustainability.

[9] Meanwhile, negotiations to secure external grants to finance the Grand Anse Dam, another large project aimed at enhancing resilience to climate change, are at an advanced stage.

[10] In addition to a carbon tax, (i) raising household electricity tariffs to cover marginal costs; (ii) changing vehicle taxation to an ad valorem rate, and (iii) introducing congestion fees or tools were discussed in the CCPA as possible medium-term revenue measures.

merit of such an operation to reduce currency risks by better aligning the repayment currency with Seychelles' foreign exchange earnings (mostly in Euros). However, they have recently decided that commission costs would outweigh such potential benefit.[11]

11. Staff urged the authorities to carry on their intensified efforts to minimize fiscal risks from SOEs, particularly from Air Seychelles. Air Seychelles has begun its comprehensive operational restructuring, including staff redundancy and the closure of loss-making international routes. Its financial performance improved significantly this year thanks to the progress in operational restructuring.[12] Staff reiterated that the government should closely monitor the progress in Air Seychelles' restructuring and take corrective actions, if needed, to ensure that no budget impact would materialize beyond that already assumed in their latest medium-term expenditure and debt projections.[13] The company's unguaranteed "project box bond" of $71.5 million owed to the other shareholder could pose roll-over risk to the company in 2020, and especially in 2021. The government does not intend to take on this liability. In case any additional government support to the company beyond that assumed in the medium-term baseline needs to be considered in future, corrective actions to offset any fiscal impact would be discussed with the Fund in the context of future program reviews (PS¶22). The government recently received a long-term business viability analysis of the company from the World Bank TA experts. Meanwhile, the government is conducting a comprehensive governance assessment of the company to be completed by end-December 2019 (5th review RT). The government will propose a RT for the 6th review to address any remaining weaknesses of the company, based on its assessment and the World Bank TA. Meanwhile, a new government ownership and dividend policy for SOEs will be submitted to the Cabinet by end-October (PS¶21), which would help reduce uncertainty in the budgeting of non-tax revenue as well as strengthen the oversight of the entire SOE sector.

C. Preserving Price and External Stability

12. With inflationary pressures abated, the CBS should stay vigilant to both upside and downside risks to inflation. Staff supported the CBS' recent monetary policy easing given the continued inflation underperformance since the 2nd review and the benign inflation outlook in coming months. Annual average inflation forecasts for 2019 and for 2020 have been revised down by 0.6 and 0.9 percentage points, respectively, compared with those at the time of the 3rd review. Although the acceleration of private sector credit growth in recent months has been driven by productive sectors and no adverse impact on asset quality of banks has been observed (¶1), demand pressures on the back of higher public wages could pose upside risks to inflation in coming months.

[11] Although the government also expected significant interest cost savings from such an exercise given the interest differentials between the US$-denominated bonds and €-denominated bonds, the World Bank experts pointed out that a net interest saving would be negligible over the life span of the bond as the current interest differentials reflects a market expectation of future exchange rates.

[12] The loss in the first nine months of this year declined to $9.7 million from $38.5 million from the same period in 2018.

[13] Government's assistance included in the baseline projection consists of guarantees to working capital of $12.5 million and to the other shareholder's preference shares of $30 million starting in 2019, and $6 million of transfers to the company each year financed by grants during 2019–23.

Meanwhile, downside risks center around lower-than-expected international fuel and imported food prices and increased competition among domestic retailers (¶2). In this context, staff agreed with the CBS on the need to stand ready to adjust the monetary policy stance promptly in response to significant upward or downward deviations of inflation from the projections. Staff welcomed that the CBS and the Ministry of Finance recently set up a working group to enhance coordination and ensure that the planned unwinding of the monetary debt, in line with the government's debt reduction, does not hamper the CBS' monetary policy operations (PS¶29). It would help improve liquidity forecasting which would benefit the conduct of monetary policy.

13. The CBS's efforts to ensure a smooth transition to a new monetary policy framework continues. The CBS has made significant progress to further strengthen its capacity for inflation forecasting and liquidity management, including implementing its 6-phase plan (PS¶30). A working group has been set up to advise the CBS and banking sector regarding the development of the interbank market. Staff encouraged the CBS to continue finetuning its communication policy with the help of the Fund TA. The CBS noted that work is ongoing to formalize and expand the survey of inflation expectations in coordination with the National Bureau of Statistics (NBS) with a view to increasing the traction of monetary policy.

14. Staff reiterated its advice to maintain a flexible exchange rate policy and to keep international reserves coverage at around the current level. The CBS requested to revise down the NIR targets for the rest of the program slightly, citing stronger-than-expected imports in recent months and a possibility that forthcoming elections may lead to a tightness in foreign exchange markets, given the experience in the previous Presidential election. The revised projected level of GIR would still stand at about 121 percent of the relevant ARA metric during 2019–20 under the baseline, which is adequate as illustrated in the 2019 Article IV consultation. Meanwhile, staff's recent external sector assessment indicates a moderate level of overvaluation of the real effective exchange rate and an external position moderately weaker than implied by fundamentals.[14] Large foreign exchange purchases would lead to further issuance of monetary debt or increase excess liquidity in the system, which would be detrimental both to the debt reduction and inflation objectives. Thus, staff advised the CBS to maintain its flexible exchange rate policy and to limit foreign exchange purchases to the extent needed to preserve reserve coverage ratio at around the current level.

D. Supporting Financial Stability

15. Staff welcomed the authorities' stepped-up efforts to address the risks of potential loss of CBRs. The authorities have reached an agreement with the World Bank to assist in capacity building of relevant AML/CFT institutions of the country, as well as reviewing and drafting relevant legislation (PS¶35). A resident advisor was recently contracted, and the 2020 budget allocates additional resources to the relevant institutions. Drafting of a new AML bill, which will allow the authorities to implement a risk-based approach to AML/CFT supervision of banks, trusts, and company service providers in line with Financial Action Task Force (FATF) standards, is almost

[14] See Annex II of Country Report No. 19/194.

complete. The draft bill will be submitted to the Cabinet by end-March 2020 (5th review RT, PS¶35). The authorities are also making progress in their plan to submit to the Cabinet draft amendments to the legal framework to strengthen the entity transparency of both domestic and international business companies consistent with the FATF standards by end-December 2019 (PS¶37, 5th review RT). Moreover, the authorities will establish a beneficial ownership register for the offshore sector, and are articulating a comprehensive financial sector strategy, covering both domestic and offshore sectors, which would be in line with international best practices in terms of addressing AML/CFT issues, to be submitted by mid-2020 (PS¶37). As the September 2019 Eastern and Southern African Anti-Money Laundering Group (ESAAMLG) mission to Seychelles pointed out, a steadfast progress in strengthening the AML/CFT framework in Seychelles would go a long way to make the case to maintain CBRs to the international community.

16. Staff encouraged the authorities to continue efforts to strengthen the financial stability framework. With a view to implementing a transition to Basel II and adoption of the Basel III capital definition, a policy framework paper for an implementation of Basel II pillar 1 and Basel III capital definition is on track to be submitted to the Cabinet by end-December 2019 (PS¶34, 5th review RT).[15] This would not only provide a framework to buttress financial stability, but also support on-going efforts to reduce the risk of further loss of CBRs, especially through international capital adequacy requirements and the adoption of a more risk-based supervisory approach. Furthermore, the CBS is formulating a policy framework paper on a Financial Sector Stability Act, which will assign macro prudential powers to the relevant institutions, to be submitted to the Cabinet by September 2020 (PS¶31, 6th review RT). This will enable the CBS and relevant institutions to take corrective actions to tackle risks from a potential consumer credit build-up.

E. Enhancing Inclusive Growth

17. Enhancing the business environment would help boost prospects for inclusive and sustainable growth. High electricity costs, which partly result from cross-subsidies, are among the major bottlenecks to do business in Seychelles. A comprehensive utility tariff review by World Bank experts, aimed at better targeting utility subsidies to households and possibly lowering the utility costs to business and government, will be completed by end-2019. Furthermore, the government intends to amend the Company Act and Insolvency Act to speed up the insolvency resolution process. Policy papers on these amendments will be submitted to the Cabinet by September 2020 (6th review RT, PS¶23). Meanwhile, the government's efforts to digitize some of its services, including tax filing, property and company registration, continue.

18. The authorities continue efforts to diversify the tourism sector and upgrade the fishery industry, which should support inclusive growth. The authorities recently reformulated the tourism master plan. Focal points of the new plan include increasing local content by industry-wide human resource developments, promoting trade between local food producers and

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[15] A full transition to Basel II and adaptation of Basel III capital definition was targeted to be completed by end-December 2019 at the time of the 3rd review. However, the CBS requested a modification for the 5th review RT on this issue because a one-year transition would be needed for the Basel II Pillar 2 to take effect.

accommodation establishments, and addressing costs of doing businesses for local small- and medium-sized enterprises (SMEs). The authorities' efforts to upgrade the fisheries industries continue, including the ongoing development around Victoria port area to establish it as a long-line base and building of new handling facilities.

19. The authorities plan to intensify efforts to increase the financial sector's contribution to inclusive growth. The authorities' National Financial Inclusion Strategy (NFIS) would focus on SMEs' access to financing, along with innovative financial services, competition, and consumer protection in the financial sector (PS¶39–43). The authorities concurred with the staff's advice that any SME financing scheme should be targeted, transparent, and not impede the conduct of monetary policy. Steady implementation of NFIS would help enhance financial stability and deepening, leading to an enhanced monetary transmission mechanism over the medium term.

PROGRAM AND OTHER ISSUES

20. The program will continue to be monitored on a semi-annual basis. Seychelles does not need the Fund's financial assistance under the baseline and is not seeking financial assistance from the Fund as the program is fully financed. Reviews are set out in Table 6. Quantitative targets for the key set of macroeconomic variables monitored under the PCI and a continuous target on the non-accumulation of external arrears are set out in Table 1a of the PS. In addition, the applicable standard continuous targets are set out in Table 1b of the PS. The authorities requested to modify slightly the end-December 2019 fiscal primary surplus (¶5) and NIR (¶12) targets. End-June 2020 quantitative targets are also proposed. RTs for 2019–20 are reflected in Table 2 of the PS.

21. Downside risks to the PCI remain modest. Seychelles' remaining obligations to the Fund are small and its capacity to repay the Fund is strong (Table 7). Despite risks stemming predominantly from external factors (¶3) and the restructuring of Air Seychelles (¶11), downside risks to the PCI seem moderate given Seychelles' strong track record and continued commitment to prudent policies. The CBS has made further progress in implementing recommendations from the 2018 voluntary safeguard assessment. A compliance function has been established and an AML/CFT policy for its banking operations is under internal review. Strengthening the CBS Act remains work in progress and is now envisaged for September 2020 (PS¶44).

22. The authorities' capacity development efforts will continue to focus on AML/CFT, monetary policy operations, PFM, and macroeconomic statistics with the help of the Fund and other international financial institutions. The authorities' efforts to build up capacity relevant to the AML/CFT framework play an integral role under the PCI. Fund's TA on monetary policy operations would help ensure a successful transition to the new monetary policy framework. Capacity development in PFM, focusing on SOE monitoring and public investment management, would help buttress medium-term fiscal sustainability. The authorities plan to complete the rebasing of GDP by mid-2020 with the help of Fund TA. Meanwhile, the CBS' efforts to improve the quality of external statistics continue (PS¶45).

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23. The authorities remain committed to reinforcing the hard-won economic stability and sustainability. Program implementation has been strong. Economic growth has been strong while inflation has been steadily declining. The authorities are fully aware that any potential fiscal slippages could put the steady debt reduction at risk. The authorities' 2020 budget targets a primary surplus of 2½ percent of GDP through 2022, while introducing permanent fiscal saving measures in 2020. Due to the need to inject immediately $30 million (about 2 percent of GDP) into Air Seychelles in response to the Etihad's request, end-2021 debt-GDP ratio is expected to be marginally above the authorities' debt reduction target of below 50 percent by that time. However, the fiscal path under the 2020 budget is consistent with a steady decline of public debt and fiscal sustainability in the medium term, striking a balance between the need to ensure economic stability and to build up investments for priority infrastructure and climate change related projects.

24. Staff encouraged the authorities to implement the permanent saving measures incorporated in the 2020 budget to strengthen the medium-term fiscal sustainability. The 2020 budget which was recently submitted to the National Assembly is in line with the primary surplus target under the PCI. It includes permanent revenue enhancing and expenditure saving measures. The authorities will start implementing measures to streamline and better target social welfare programs in 2020 and continue to keep a tight rein on other current spending for next three years. In line with the staff's advice, the authorities intend to implement major public investments announced in the 2018 SONA and other climate change related projects within the envelope of the fiscal parameters under the PCI. Beyond the next few years, they should explore the possibility of additional revenue measures discussed at the time of the 2017 Article IV consultation to create further fiscal space for priority projects, as well as implement structural reforms to improve the efficiency of public investments and appropriately manage potential fiscal risks arising from PPPs.

25. The authorities should keep a tight rein on Air Seychelles to reduce fiscal risks arising from the company. While the company's financial performance improved significantly this year thanks to the progress in operational restructuring, it still poses the biggest risk to the program. The government is urged to keep closely monitoring the company's operations and progress in operational restructuring. The authorities should refrain from issuing additional guarantees for the company or taking on its liabilities. With a view to ensuring that no fiscal impact would materialize beyond that already assumed in the medium-term baseline of the program, the authorities should take corrective actions promptly if needed. Based on the government's ongoing comprehensive governance monitoring of the company and the World Bank's TA, the authorities should articulate measures to address any remaining weaknesses of the company.

26. The authorities are committed to be vigilant to both upside and downside risks to inflation. The CBS' prudent monetary policy, combined with softening of international commodity prices and increased competition in the domestic retail sector, has helped contain inflationary pressures. Staff supports the CBS' recent monetary policy easing given the benign inflation outlook in coming months and its intention to stand ready to adjust the monetary policy stance promptly in response to significant upward or downward deviations of inflation from the projections. Staff welcomed that the authorities have recently taken a step to develop interbank markets in cooperation with stakeholders. Staff also support enhanced coordination between the CBS and the Ministry of Finance to ensure that the planned unwinding of the monetary debt, in line with the government's debt reduction, does not hamper the CBS' monetary policy operations. Given that the real exchange rate is moderately overvalued and the GIR coverage is estimated to be adequate, the CBS should stick to a flexible exchange rate policy with minimal intervention to preserve reserves coverage ratios at around the current level.

27. Staff welcomed the authorities' efforts to strengthen the AML/CFT framework and address the risks of further potential loss of CBRs. The authorities are making good progress in the capacity enhancement of the relevant AML/CFT institutions, strengthening the AML/CFT framework in line with international standards and best practices, and enhancing entity transparency in the offshore sector, in line with the FATF standards and TA recommendations of the Fund Legal department.

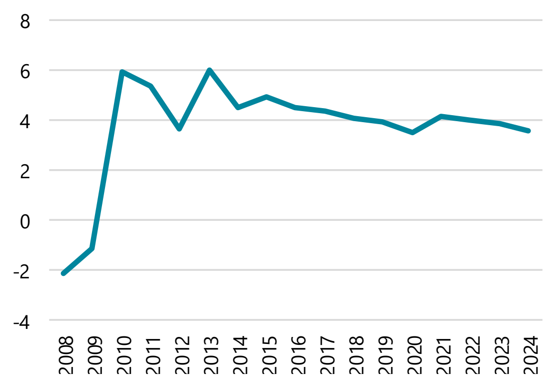
28. The authorities are encouraged to stay focused on structural reforms to enhance prospects for inclusive growth. While the authorities' efforts to diversify tourism and upgrade the fishery industry continues, economic diversification requires improving the business environment. Better targeting of utility subsidies for households could create room to reduce costs for businesses and the government. The authorities are also encouraged to keep momentum on efforts to increase the financial sector's contribution to inclusive growth.

29. Given the authorities' strong program implementation and sustained commitment to safeguarding macroeconomic stability, staff supports the authorities' request for the completion of the fourth review under the PCI. Staff also supports the authorities' requests to modify the end-December 2019 targets on primary fiscal surplus and NIR, end-December 2019 inflation projection for MPCC, and the RTs for the 5th and 6th reviews.

Figure 1. Seychelles: Macroeconomic Developments and Projections

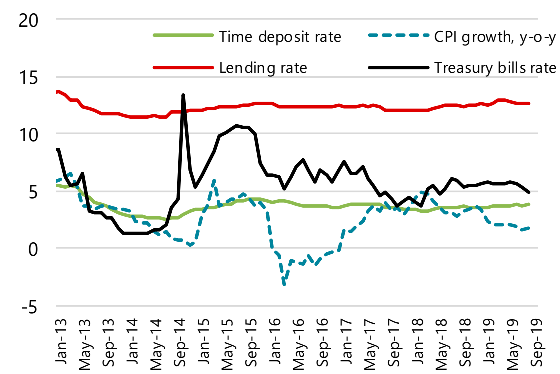
The strong recent growth momentum is projected to continue with a slight moderation in 2019-20 …

Real GDP Growth, 2008-24
(In Percent)



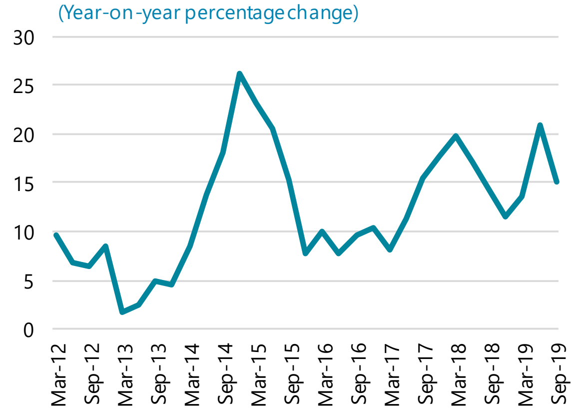
and inflation has slowed down in the first half of 2019 after rising in 2017-18 …

Inflation and interest rates, Jan'13–Aug'19



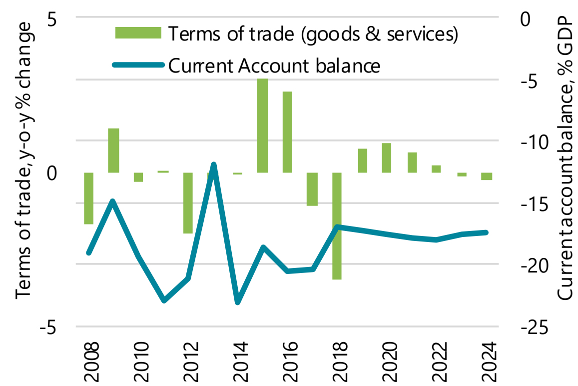
While private sector credit growth picked up again in the 2nd quarter of 2019 …

Credit to the Private Sector, Mar'12-Sep'19
(Year-on-year percentage change)



The current account deficit is projected to stabilize around 17% of GDP….

External Balance and Terms of Trade, 2008–24

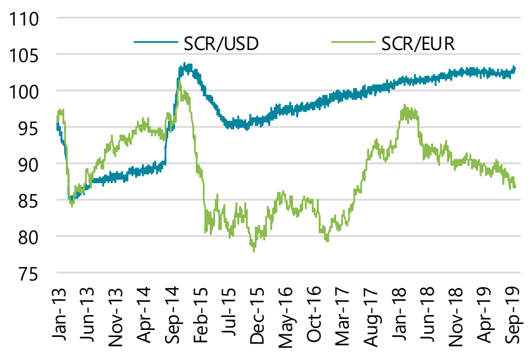


Sources: Seychelles authorities, and IMF staff estimates.

Figure 2. Seychelles: Additional Macroeconomic Developments and Projections

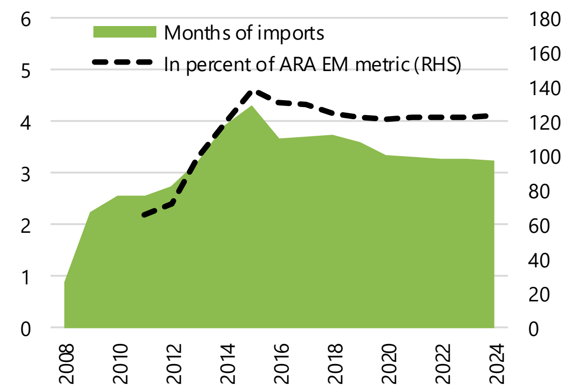
The rupee has stayed stable with respect to the dollar in 2019…

Daily exchange rates index, Jan'13-Sep'19
(December 31, 2011 = 100)



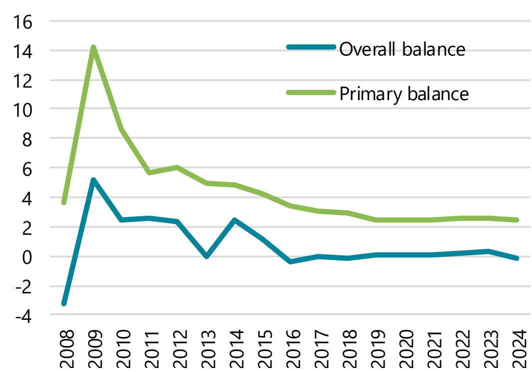
While reserves coverage is adequate and stable, based on the ARA metric ….

Reserves Adequacy, 2008-24 [1]



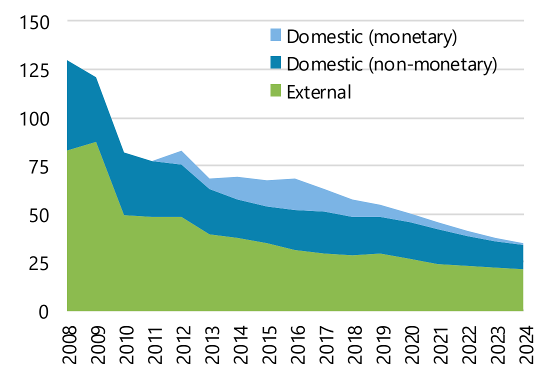
Fiscal primary balance targets have been consistently met in recent years…

Fiscal balances, 2008–24
(Percent of GDP)



And public debt remains on a firm declining path.

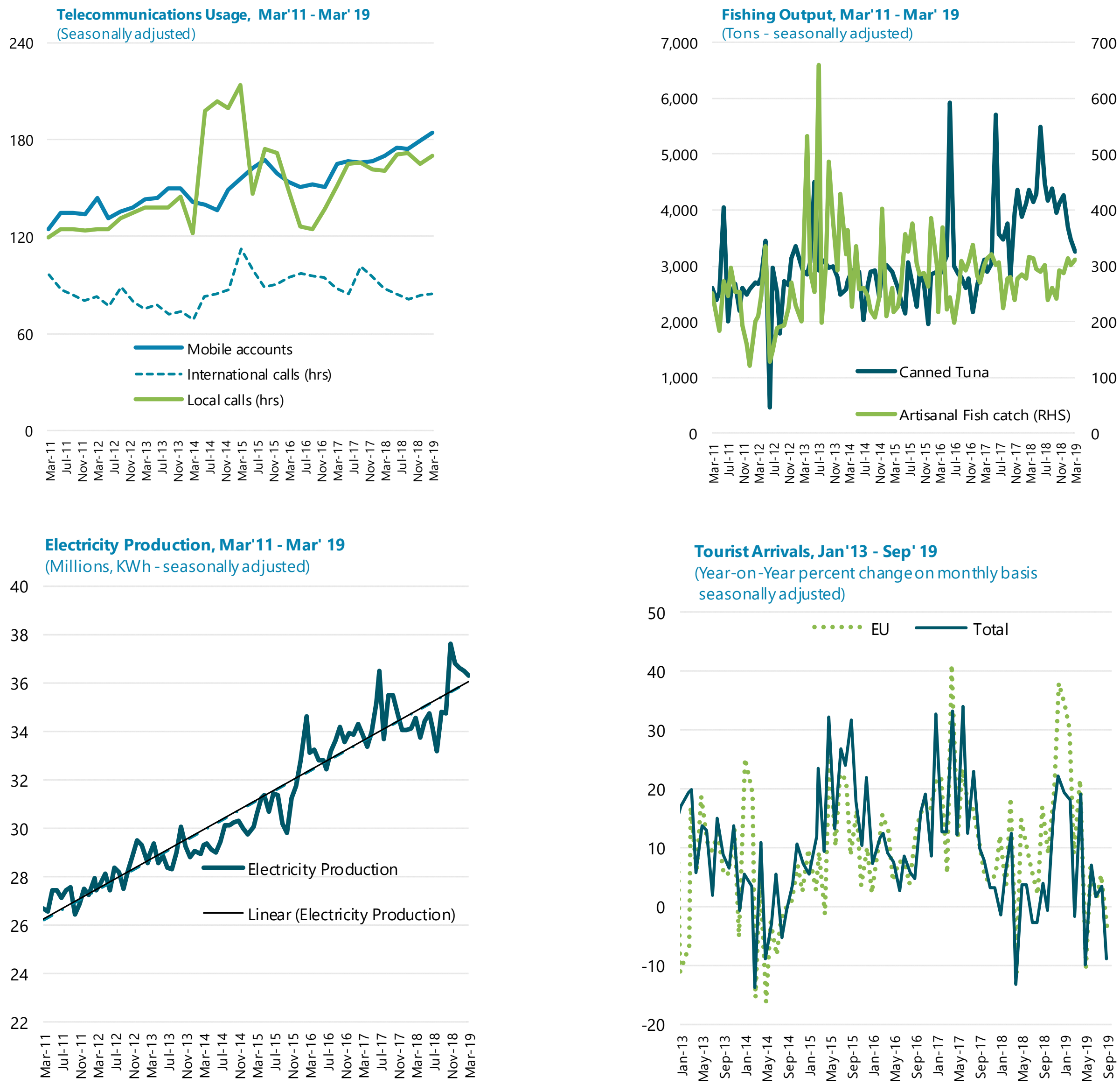
Stock of public debt, 2008–24
(Percent of GDP)



Sources: Seychelles authorities, and IMF staff estimates.

[1] Data for the ARA EM metric are not available prior to 2011.

Figure 3. Seychelles: Monthly Indicators of Economic Activity



Sources: Seychelles authorities, and IMF staff estimates.

Table 1. Seychelles: Selected Economic and Financial Indicators, 2016–24

Nominal GDP (2017): US$1,498 million
Per capita GDP (2017): US$15,735
Population, end-year (2016): 94,677
Literacy rate (2015): 95.3 percent
Main products and exports: Tourism, Canned Tuna

	2016	2017	2018	2019		2020	2021	2022	2023	2024
	Act.	Act.	Prel.	3rd Rev.	Proj.			Proj.		
	(Annual percent change, unless otherwise indicated)									
National income and prices										
Nominal GDP (millions of Seychelles rupees)	19,014	20,515	22,019	23,274	23,200	24,447	26,198	28,011	29,959	31,963
Real GDP	4.5	4.3	4.1	3.5	3.9	3.5	4.1	4.0	3.8	3.6
CPI (annual average)	-1.0	2.9	3.7	2.6	2.0	2.1	2.9	2.9	3.0	3.0
CPI (end-of-period)	-0.2	3.5	3.4	3.2	2.3	2.5	3.0	3.0	3.0	3.0
GDP deflator average	-0.8	3.4	3.1	2.2	1.4	1.8	2.9	2.8	3.0	3.0
Money and credit										
Broad money	12.1	16.4	7.7	5.6	9.7	6.4	…	…	…	…
Reserve money (end-of-period)	14.5	18.9	4.5	8.3	6.9	4.8	…	…	…	…
Velocity (GDP/broad money)	1.4	1.3	1.3	1.3	1.2	1.2	…	…	…	…
Money multiplier (broad money/reserve money)	4.6	4.5	4.6	4.5	4.7	4.8	…	…	…	…
Credit to the private sector	10.3	17.8	11.5	10.7	16.0	10.1	…	…	…	…
	(Percent of GDP, unless otherwise indicated)									
Savings-Investment balance										
External savings	20.6	20.4	17.0	17.0	17.3	17.6	17.9	18.0	17.5	17.5
Gross national savings	9.7	8.5	10.1	10.9	10.3	10.7	11.3	12.5	13.5	13.0
Of which: government savings	3.8	3.6	4.7	5.2	5.1	4.1	4.3	6.1	7.1	6.6
private savings	5.9	4.9	5.4	5.7	5.2	6.6	7.1	6.4	6.4	6.4
Gross investment	30.2	28.9	27.1	27.9	27.6	28.4	29.3	30.5	31.0	30.5
Of which: public investment [1]	5.0	4.4	5.6	5.4	5.1	5.9	6.8	7.1	7.1	7.1
private investment	25.2	24.5	21.5	22.5	22.5	22.5	22.5	23.4	23.9	23.4
Private consumption	47.1	50.9	53.2	51.1	50.8	49.1	50.5	51.7	51.3	50.7
	(Percent of GDP)									
Government budget										
Total revenue, excluding grants	36.6	35.5	36.3	37.3	37.5	37.7	36.2	35.5	35.5	35.3
Expenditure and net lending	38.1	37.0	38.4	38.6	38.3	40.2	39.1	36.8	36.6	36.6
Current expenditure	33.1	32.6	32.8	33.2	33.2	34.3	32.5	30.7	30.1	30.4
Capital expenditure [1]	5.0	4.4	5.6	5.4	5.1	5.9	6.8	7.1	6.5	6.4
Overall balance, including grants	-1.4	0.0	0.7	-0.1	0.0	0.1	0.0	0.2	0.4	-0.2
Program primary balance	3.4	3.0	2.9	2.5	2.5	2.5	2.5	2.5	2.5	2.5
Total government and government-guaranteed debt [2]	72.7	66.8	61.0	57.7	61.4	57.3	51.7	46.9	43.1	40.3
Domestic (including debt issued for monetary purposes)	40.4	36.7	32.4	31.0	32.1	29.9	27.0	23.3	20.7	18.8
of which: Monetary debt	16.2	11.4	9.3	7.9	6.2	4.7	3.2	2.3	1.7	1.1
External	32.2	30.1	28.6	26.7	29.3	27.4	24.7	23.6	22.4	21.5
External sector										
Current account balance including official transfers (in percent of GDP)	-20.6	-20.4	-17.0	-17.0	-17.3	-17.6	-17.9	-18.0	-17.5	-17.5
Total external debt outstanding (millions of U.S. dollars) [3]	1,505	1,639	1,762	1,772	1,884	1,939	2,020	2,120	2,219	2,321
(percent of GDP)	105.4	109.0	111.3	107.4	114.0	113.4	112.0	111.4	110.6	110.2
Terms of trade (-=deterioration)	2.6	-1.1	-3.5	1.5	0.7	0.9	0.6	0.2	-0.1	-0.3
Real effective exchange rate (average, percent change)	0.1	-5.2	…	…	…	…	…	…	…	…
Gross official reserves (end of year, millions of U.S. dollars)	522.6	546	548	551	542	541	564	588	613	616
Months of imports, c.i.f.	3.7	3.7	3.7	3.5	3.6	3.3	3.3	3.3	3.3	3.2
In percent of Assessing Reserve Adequacy (ARA) metric	131.0	129.3	124.5	124.9	122.5	120.8	122.3	122.4	122.0	122.7
Exchange rate										
Seychelles rupees per US$1 (end-of-period)	13.5	13.8	…	…	…	…	…	…	…	…
Seychelles rupees per US$1 (period average)	13.3	13.6	…	…	…	…	…	…	…	…

Sources: Central Bank of Seychelles; Ministry of Finance; and IMF staff estimates and projections.

[1] Includes onlending to the parastatals for investment purposes.

[2] Includes debt issued by the Ministry of Finance for monetary purposes.

[3] Includes private external debt.

Table 2. Seychelles: Balance of Payments, 2016-24

	2016	2017	2018	2019	2020	2021	2022	2023	2024
	Est.	Est.	Prel.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.
	(In millions of US dollars, unless otherwise indicated)								
Current account balance (+ surplus; - deficit)	-293	-307	-269	-287	-300	-324	-342	-351	-368
(percent of GDP)	-20.6	-20.4	-17.0	-17.3	-17.6	-17.9	-18.0	-17.5	-17.5
Balance of goods and services (+ surplus; - deficit)	-146	-175	-188	-179	-187	-210	-219	-214	-210
Exports of goods	459	536	562	565	581	621	648	734	776
Of which: oil re-exports	131	150	183	169	179	179	180	234	250
Of which: tuna exports	270	268	286	252	285	316	335	359	377
Imports of goods	991	1,155	1,234	1,215	1,258	1,359	1,427	1,521	1,596
Of which: oil imports	162	209	288	237	241	259	247	317	348
Exports of services	894	998	1,016	1,021	1,052	1,111	1,169	1,210	1,270
Of which: tourism earnings[1]	414	483	564	600	625	662	695	736	772
Imports of services	507	554	533	549	562	583	609	636	661
Balance on primary income (+ surplus; - deficit)	-133	-136	-99	-93	-96	-99	-108	-117	-129
Of which: interest due	40	25	26	36	38	40	41	47	56
transfers of profits and dividends	19	17	22	17	18	19	19	19	19
Balance on secondary income (+ surplus; - deficit)	-15	5	18	-14	-17	-14	-15	-20	-29
Of which: general government, net	50	42	54	30	36	37	40	39	32
Capital account	54	52	50	45	59	59	46	45	46
Financial account	237	276	228	242	247	294	325	335	328
Direct investment, net [1]	182	270	116	238	261	318	332	324	326
Abroad	-4	-6	8	8	8	8	8	8	8
In Seychelles	178	264	124	246	268	326	340	332	334
Of which: offshore sector	0	0	0	0	0	0	0	0	0
Portfolio investment, net	-52	-57	-45	-60	-34	-32	-32	-32	-22
Other investment, net	107	63	156	64	20	8	25	43	24
Government and government-guaranteed	-35	-16	-1	-7	-12	-15	7	-1	3
Disbursements	5	5	25	22	27	30	64	55	54
Project loans	5	0	25	22	27	30	64	55	54
Program loans	10	15	0	0	0	0	0	0	0
Amortization	-54	-19	-34	-32	-39	-43	-51	-51	-46
Private sector	142	80	158	72	32	23	18	45	21
Net errors and omissions	-11	0	0	0	0	0	0	0	0
Overall balance	-2	22	8	1	6	29	29	29	5
Financing	13	-22	-8	-1	-6	-29	-29	-29	-5
Change in net international reserves (increase: –)	13	-22	-8	-1	-6	-29	-29	-29	-5
Change in gross official reserves (increase: –)	14	-24	-2	6	1	-23	-24	-26	-3
Liabilities to IMF, net	-1	2	-6	-7	-7	-6	-5	-4	-2
Other net foreign assets (increase: –)	0	0	0	0	0	0	0	0	0
Exceptional financing	0	0	0	0	0	0	0	0	0
Financing gap	0	0	0	0	0	0	0	0	0
Memorandum items:									
Exports G&S growth, percent	4.3	13.4	2.9	0.5	3.0	6.0	4.9	7.0	5.3
Tourism growth, percent	5.4	16.7	16.8	6.3	4.2	6.0	5.0	5.8	4.9
Exports of goods volume growth, percent	8.7	0.6	4.7	-4.0	7.6	7.0	4.5	5.0	4.1
Imports G&S growth, percent	5.5	14.1	3.3	-0.1	3.2	6.7	4.9	6.0	4.6
Imports of goods volume growth, percent	14.4	10.8	-0.1	0.6	5.0	7.8	4.6	6.0	3.7
Exports G&S, percent of GDP	94.77	102	100	96	96	96	95	97	97
Imports G&S, percent of GDP	105	114	112	107	106	108	107	108	107
FDI, percent of GDP [2]	12.8	18.0	7.3	14.4	15.2	17.6	17.4	16.1	15.5
Gross official reserves (stock, e.o.p.)	523	546	548	542	541	564	588	613	616
(Months of imports of goods & services)	3.7	3.7	3.7	3.6	3.3	3.3	3.3	3.3	3.2
Percentage of IMF reserve adequacy metric	131	129	124	123	121	122	122	122	123
Government and government-guaranteed external debt	454	446	449	484	464	442	446	445	450
(Percent of GDP)	31.8	29.7	28.4	29.3	27.2	24.5	23.5	22.2	21.3
GDP (Millions of U.S. dollars)	1,427	1,503	1,583	1,652	1,710	1,804	1,903	2,006	2,107

Sources: Central Bank of Seychelles; Ministry of Finance; and IMF staff estimates and projections.

[1] From 2015 onwards the data reflect the findings of the IIP survey, which indicated that the proportion of equity to debt in FDI flows was being significantly overestimated

[2] Per STA recommendations, renewals of off-shore licenses are excluded.

Table 3a. Seychelles: Consolidated Government Operations, 2016-21[1]
(millions of Seychelles rupees)

	2016	2017	2018	2019	2020 Q1	2020 Q2	2020 Q3	2020 Q4	2020	2021
	Act.	Act.	Act.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.
	(Millions of Seychelles rupees)									
Total revenue and grants	7,205	7,446	8,274	8,920	1,973	2,456	2,513	2,912	9,854	10,263
Total revenue	6,965	7,274	7,997	8,695	1,849	2,302	2,438	2,618	9,207	9,472
Tax	6,188	6,600	7,083	7,497	1,724	1,956	2,033	2,017	7,730	8,101
Personal income tax	939	900	965	966	251	263	246	256	1,015	1,077
Trade tax	359	285	315	331	87	81	92	88	348	361
Excise tax	1,144	1,312	1,281	1,407	360	367	385	429	1,540	1,596
Goods and services tax (GST) / VAT [2]	1,996	2,151	2,495	2,651	638	721	708	727	2,794	2,995
Business tax [3]	1,039	1,364	1,376	1,351	255	406	450	317	1,428	1,444
Corporate Social Responsibility Tax (CSR) [3]	87	95	106	117	31	29	32	32	123	132
Marketing Tourism Tax (MTT) [3]	45	60	70	75	18	19	21	21	79	85
Other	581	434	474	598	85	70	99	148	403	411
Nontax	777	673	914	1,198	126	346	404	601	1,477	1,370
Fees and charges	403	349	335	352	49	129	116	156	450	455
Dividends from parastatals	330	280	426	694	25	193	235	372	826	756
Other	44	44	153	152	52	24	53	73	201	160
External grants	240	173	277	225	123	154	76	294	647	792
Expenditure and net lending	7,277	7,455	8,318	8,909	2,051	2,400	2,338	3,035	9,825	10,255
Current expenditure	6,295	6,687	7,231	7,707	1,791	2,041	2,105	2,438	8,374	8,505
Primary current expenditure	5,581	6,056	6,541	7,134	1,669	1,930	1,930	2,264	7,792	7,859
Wages and salaries [4]	2,002	2,074	2,268	2,617	761	721	751	771	3,004	3,054
Goods and services [4]	2,489	2,562	2,800	2,799	544	758	713	947	2,962	2,962
Transfers [4]	1,063	1,380	1,443	1,679	348	440	459	545	1,792	1,808
Social program of central government	130	114	114	160	37	35	38	65	175	180
Transfers to public sector from central government	80	97	55	162	34	39	40	46	159	140
Benefits and programs of Social Security Fund	853	1,169	1,273	1,357	277	366	381	433	1,458	1,487
Other	27	41	31	40	16	11	7	2	35	35
Interest due	714	631	689	573	121	111	175	173	581	646
Foreign interest	190	218	227	254	71	58	119	31	280	305
Domestic interest	524	413	463	319	50	53	56	143	302	341
Capital expenditure	909	747	954	994	225	260	227	546	1,258	1,625
Domestically financed	644	564	455	731	77	79	105	228	488	638
Foreign financed	265	183	499	263	148	181	122	319	770	986
Net lending	35	-1	86	159	27	86	-4	38	148	81
Contingency	38	21	47	50	9	13	10	14	45	45
Primary balance	642	622	646	584	43	168	350	50	611	655
Overall balance, commitment basis [5]	-72	-9	-43	11	-78	57	175	-123	30	9
Change in float	-201	3	194	0	0	0	0	0	0	0
Overall balance, cash basis (after grants)	-273	-6	151	11	-78	57	175	-123	30	9
Financing	273	6	-151	-11	78	-57	-175	123	-30	-9
Foreign financing	-304	-407	-35	-139	-93	-88	-52	65	-168	-190
Disbursements	287	11	305	312	45	50	86	204	385	431
Project loans	25	11	305	312	45	50	86	204	385	431
Program/budget support	262	0	0	0	0	0	0	0	0	0
Scheduled amortization	-591	-418	-340	-451	-138	-138	-138	-138	-553	-621
Of which Paris Club buy-back	-269	…	…	…	…	…	…	…		
Domestic financing, net	578	316	-272	76	171	31	-123	58	138	82
Bank financing	389	419	-571	69	167	27	-127	54	121	73
CBS	-191	438	88	600	75	75	75	75	300	300
Commercial banks	579	-19	-659	-531	92	-48	-202	-21	-179	-227
Nonbank financing	190	-103	299	8	4	4	4	4	18	8
Privatization and long-term lease of fixed assets	76	82	0	0	0	0	0	0	0	100
Transfer of SSF deposits to SPF	…	…	…	…	…	…	…	…		
Statistical discrepancy	-77	16	156	52	0	0	0	0	0	0
Memorandum item:			0							
External debt service due	781	636	567	705	210	197	257	169	832	927

Sources: Seychelles authorities; and IMF staff estimates and projections.

[1] Includes the central government and the social security system.

[2] VAT replaced GST in January 2013.

[3] CSR and MTT were subsumed into Business Tax in CR 14/186.

[4] From 2015 onwards, wage and salaries and goods and services (to be) spent by government agencies other than Ministries are reclassified into these items from transfers.

[5] Only interest payments on foreign debt are on a commitment basis. Other expenditures are recorded when checks are issued or transfers initiated.

Table 3b. Seychelles: Consolidated Government Operations, 2016-21[1]

(percent of GDP)

	2016	2017	2018	2019	2020				2020	2021
					Q1	Q2	Q3	Q4		
	Prel.	Proj.	Prel.	Proj.					Proj.	Proj.
	(Percent of GDP, unless otherwise indicated)									
Total revenue and grants	37.9	36.3	37.6	38.4	8.1	10.0	10.3	11.9	40.3	39.2
Total revenue	36.6	35.5	36.3	37.5	7.6	9.4	10.0	10.7	37.7	36.2
Tax	32.5	32.2	32.2	32.3	7.1	8.0	8.3	8.3	31.6	30.9
Personal income tax	4.9	4.4	4.4	4.2	1.0	1.1	1.0	1.0	4.2	4.1
Trade tax	1.9	1.4	1.4	1.4	0.4	0.3	0.4	0.4	1.4	1.4
Excise tax	6.0	6.4	5.8	6.1	1.5	1.5	1.6	1.8	6.3	6.1
Goods and services tax (GST) / VAT [2]	10.5	10.5	11.3	11.4	2.6	2.9	2.9	3.0	11.4	11.4
Business tax	5.5	6.6	6.3	5.8	1.0	1.7	1.8	1.3	5.8	5.5
Corporate Social Responsibility Tax (CSR)	0.5	0.5	0.5	0.5	0.1	0.1	0.1	0.1	0.5	0.5
Marketing Tourism Tax (MTT)	0.2	0.3	0.3	0.3	0.1	0.1	0.1	0.1	0.3	0.3
Other	3.1	2.1	2.2	2.6	0.3	0.3	0.4	0.6	1.6	1.6
Nontax	4.1	3.3	4.2	5.2	0.5	1.4	1.7	2.5	6.0	5.2
Fees and charges	2.1	1.7	1.5	1.5	0.2	0.5	0.5	0.6	1.8	1.7
Dividends from parastatals	1.7	1.4	1.9	3.0	0.1	0.8	1.0	1.5	3.4	2.9
Other	0.2	0.2	0.7	0.7	0.2	0.1	0.2	0.3	0.8	0.6
External grants	1.3	0.8	1.3	1.0	0.5	0.6	0.3	1.2	2.6	3.0
Expenditure and net lending	38.3	36.3	37.8	38.4	8.4	9.8	9.6	12.4	40.2	39.1
Current expenditure	33.1	32.6	32.8	33.2	7.3	8.3	8.6	10.0	34.3	32.5
Primary current expenditure	29.4	29.5	29.7	30.8	6.8	7.9	7.9	9.3	31.9	30.0
Wages and salaries [3]	10.5	10.1	10.3	11.3	3.1	3.0	3.1	3.2	12.3	11.7
Goods and services [3]	13.1	12.5	12.7	12.1	2.2	3.1	2.9	3.9	12.1	11.3
Transfers [3]	5.6	6.7	6.6	7.2	1.4	1.8	1.9	2.2	7.3	6.9
Social program of central government	0.7	0.6	0.5	0.7	0.2	0.1	0.2	0.3	0.7	0.7
Transfers to public sector from central government	0.4	0.5	0.2	0.7	0.1	0.2	0.2	0.2	0.7	0.5
Benefits and programs of Social Security Fund	4.5	5.7	5.8	5.9	1.1	1.5	1.6	1.8	6.0	5.7
Other	0.1	0.2	0.1	0.2	0.1	0.0	0.0	0.0	0.1	0.1
Interest due	3.8	3.1	3.1	2.5	0.5	0.5	0.7	0.7	2.4	2.5
Foreign interest	1.0	1.1	1.0	1.1	0.3	0.2	0.5	0.1	1.1	1.2
Domestic interest	2.8	2.0	2.1	1.4	0.2	0.2	0.2	0.6	1.2	1.3
Capital expenditure	4.8	3.6	4.3	4.3	0.9	1.1	0.9	2.2	5.1	6.2
Domestically financed	3.4	2.7	2.1	3.1	0.3	0.3	0.4	0.9	2.0	2.4
Foreign financed	1.4	0.9	2.3	1.1	0.6	0.7	0.5	1.3	3.1	3.8
Net lending	0.2	0.0	0.4	0.7	0.1	0.4	0.0	0.2	0.6	0.3
Contingency	0.2	0.1	0.2	0.2	0.0	0.1	0.0	0.1	0.2	0.2
Primary balance	3.4	3.0	2.9	2.5	0.2	0.7	1.4	0.2	2.5	2.5
Overall balance, commitment basis [4]	-0.4	0.0	-0.2	0.0	-0.3	0.2	0.7	-0.5	0.1	0.0
Change in arrears	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Change in float	-1.1	0.0	0.9	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance, cash basis (after grants)	-1.4	0.0	0.7	0.0	-0.3	0.2	0.7	-0.5	0.1	0.0
Financing	1.4	0.0	-0.7	0.0	0.3	-0.2	-0.7	0.5	-0.1	0.0
Foreign financing	-1.6	-2.0	-0.2	-0.6	-0.4	-0.4	-0.2	0.3	-0.7	-0.7
Disbursements	1.5	0.1	1.4	1.3	0.2	0.2	0.4	0.8	1.6	1.6
Project loans	0.1	0.1	1.4	1.3	0.2	0.2	0.4	0.8	1.6	1.6
Program/budget support	1.4	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Scheduled amortization	-3.1	-2.0	-1.5	-1.9	-0.6	-0.6	-0.6	-0.6	-2.3	-2.4
Of which Paris Club buy-back	-1.4	…	…		…	…	…	…		
Domestic financing, net	3.0	1.5	-1.2	0.3	0.7	0.1	-0.5	0.2	0.6	0.3
Bank financing	2.0	2.0	-2.6	0.3	0.7	0.1	-0.5	0.2	0.5	0.3
CBS	-1.0	2.1	0.4	2.6	0.3	0.3	0.3	0.3	1.2	1.1
Commercial banks	3.0	-0.1	-3.0	-2.3	0.4	-0.2	-0.8	-0.1	-0.7	-0.9
Nonbank	1.0	-0.5	1.4	0.0	0.0	0.0	0.0	0.0	0.1	0.0
Privatization and long-term lease of fixed assets	0.4	0.4	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.4
Transfer of SSF deposits to SPF	…	…	…		…	…	…	…		
Statistical discrepancy	-0.4	0.1	0.7	0.2	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items:										
Nominal GDP (millions of Seychelles Rupees)	19,014	20,515	22,019	23,200	24,447	24,447	24,447	24,447	24,447	26,198
Public domestic debt [5]	36.8	33.1	29.2	25.5					23.5	21.1
Excluding t-bills issued for monetary purposes	20.7	21.7	19.9	19.2					18.8	17.9
Publicly guaranteed domestic debt	3.6	3.6	3.2	6.6					6.3	5.9

Sources: Seychelles authorities; and IMF staff estimates and projections.

[1] Includes the central government and the social security system.

[2] VAT replaced GST in January 2013.

[3] From 2015 onwards, wage and salaries and goods and services (to be) spent by government agencies other than Ministries are reclassified into these items from transfers.

[4] Only interest payments on foreign debt are on a commitment basis. Other expenditures are recorded when checks are issued or transfers initiated.

[5] Includes debt issued by the Ministry of Finance for monetary purposes, excludes guarantees.

Table 4. Seychelles: Depository Corporations Survey and Central Bank Accounts, 2016–20

	2016	2017	2018	2019				2020			
				Mar.	Jun.	Sep.	Dec.	Mar.	Jun.	Sep.	Dec.
	Act.	Act.	Act.	Act.	Act.	Proj.	Proj.	Proj.			
	(Millions of Seychelles rupees)										
Depository corporations survey											
Net foreign assets	9,817	10,754	11,948	11,948	11,533	11,979	12,110	12,266	12,387	12,508	12,656
Central bank	6,550	6,982	7,248	7,265	7,287	7,167	7,236	7,301	7,359	7,418	7,496
Deposit money banks	3,267	3,771	4,700	4,683	4,246	4,811	4,874	4,965	5,027	5,090	5,160
Net domestic assets	3,831	5,134	5,166	5,519	6,084	6,074	6,660	6,777	6,950	7,076	7,317
Domestic credit	7,110	8,476	8,620	9,090	9,859	9,655	9,719	9,763	10,558	10,355	10,708
Net claims on the government	1,791	2,209	1,699	1,864	1,959	1,684	1,516	1,554	1,901	1,612	1,716
Of which : Government deposits at the Central Bank	-3,355	-3,355	-2,829	-2,741	-2,394	-2,733	-2,629	-2,591	-2,244	-2,533	-2,429
Of which : Change in monetary debt [1]	-191	670.0	380.7	280.5	292.7	15.0	26.8	75.0	75.0	75.0	75.0
Credit to the economy	5,319	6,267	6,921	7,226	7,900	7,971	8,203	8,209	8,657	8,743	8,991
Of which : credit to the private sector	5,122	6,032	6,727	6,973	7,500	7,571	7,803	7,810	8,258	8,343	8,592
Other items, net	-3,279	-3,342	-3,453	-3,571	-3,775	-3,581	-3,060	-2,986	-3,609	-3,279	-3,391
Broad money	13,648	15,888	17,115	17,467	17,617	18,053	18,769	19,043	19,336	19,584	19,973
Currency in circulation	1,026	1,116	1,169	1,166	1,175	1,210	1,232	1,229	1,238	1,275	1,298
Foreign currency deposits	5,029	6,115	7,060	7,062	7,129	7,343	7,563	7,790	8,024	8,185	8,348
Local currency deposits	7,592	8,657	8,886	9,238	9,313	9,499	9,974	10,024	10,074	10,124	10,327
Central bank											
Net foreign assets	6,550	6,982	7,248	7,265	7,287	7,167	7,236	7,301	7,359	7,418	7,496
Foreign assets	7,059	7,560	7,731	7,738	7,727	7,638	7,621	7,663	7,705	7,747	7,789
Foreign liabilities	508	578	483	473	440	470	385	363	346	329	293
Net domestic assets	-3,558	-3,423	-3,528	-3,469	-3,542	-3,308	-3,258	-3,297	-2,976	-3,342	-3,329
Domestic credit	-2,855	-2,629	-2,651	-2,631	-2,638	-2,386	-2,332	-2,324	-1,957	-2,276	-2,217
Government (net)	-2,170	-1,731	-1,644	-1,556	-1,209	-1,548	-1,444	-1,406	-1,059	-1,348	-1,244
Commercial banks	-610	-705	-845	-935	-1,211	-620	-670	-700	-680	-710	-755
Other (parastatals)	-75	-192	-162	-140	-218	-218	-218	-218	-218	-218	-218
Other items, net	-703	-794	-877	-838	-905	-922	-926	-973	-1,019	-1,066	-1,112
Reserve money	2,992	3,559	3,720	3,796	3,745	3,860	3,978	4,004	4,383	4,076	4,167
Currency in circulation	1,026	1,116	1,169	1,166	1,175	1,210	1,232	1,229	1,238	1,275	1,298
Commercial bank reserves (includes cash in vault)	1,966	2,443	2,551	2,630	2,569	2,649	2,746	2,775	3,145	2,801	2,869
Of which : vault cash	193	212	…	…	…	…	…	…	…	…	…
Of which : excess reserves (excl. bank vault cash)	9	182	…	…	…	…	…	…	…	…	…
Of which : required reserves in foreign currency [2, 3]	703	841	924	924	924	1,011	1,042	1,073	1,105	1,127	1,150
required reserves in domestic currency [2]	1,061	1,208	1,346	1,407	1,389	1,367	1,430	1,438	1,447	1,455	1,483
Memorandum items:											
Gross official reserves (millions of U.S. dollars) [4]	523	546	548	551	547	544	542	542	541	541	540
Foreign currency deposits (millions of U.S. dollars)	372	442	503	507	509	523	538	551	563	571	579
Broad money growth (12–month percent change)	12.1	16.4	7.7	7.3	7.3	9.3	9.7	9.0	9.8	8.5	6.4
Credit to the private sector (12–month percent change)	10.3	17.8	11.5	13.6	20.8	15.0	16.0	12.0	10.1	10.2	10.1
Reserve money (end-of-period; 12–month percent change)	14.5	18.9	4.5	-0.3	11.6	2.5	6.9	5.5	17.1	5.6	4.8
Reserve money (daily average over quarter; 12–month percent change)	10.4	19.0	…	…	…	…	…	…	…	…	…
Money multiplier (broad money/reserve money)	4.6	4.5	4.6	4.6	4.7	4.7	4.7	4.8	4.4	4.8	4.8
Velocity (GDP/broad money; end-of-period)	1.4	1.3	1.3	1.3	1.3	1.3	1.2	1.2	1.2	1.2	1.2

Sources: Central Bank of Seychelles; and IMF staff estimates and projections.

[1] Negative shows accumulation, positive shows retiring (debt that is not rolled over)

[2] Reserve requirements on foreign currency deposits were introduced in 2009.

[2] Reserve requirements were lowered from 13% to 10% in 2009, but raised back to 13% in April 2011.

[4] The definition was revised in June 2011 to include foreign-currency denominated required reserves held by banks and project and blocked accounts at the CBS.

Table 5. Seychelles: Financial Soundness Indicators for the Banking Sector, 2012-2019[1]

	2012	2013	2014	2015	2016	2017	2018	2019	
	Q4	Q4	Q4	Q4	Q4	Q4	Q4	Q1	Q2
	(Percent, end-of-period)								
Capital adequacy									
Regulatory capital to risk weighted assets	26.7	26.7	21.7	25.5	26.6	23.5	20.5	21.0	20.2
Regulatory tier 1 capital to risk weighted assets	19.3	21.0	16.3	18.1	20.4	18.1	16.8	16.1	17.4
Capital to assets (net worth)	10.3	9.7	8.5	11.0	11.8	11.0	10.1	10.2	10.3
Net tangible capitalization [2]	10.4	9.8	8.6	11.2	12.0	11.2	10.1	10.3	10.4
Asset quality									
Foreign exchange loans to total loans	18.7	18.7	23.8	28.6	25.0	27.7	24.2	23.6	25.2
Non-performing loans to gross loans	9.3	9.4	8.2	7.6	6.8	7.1	3.5	3.5	3.5
Provision as percentage of non-performing loans	29.5	39.2	43.9	41.1	37.4	31.9	19.2	20.3	21.8
Provisions as percentage of total loans	2.7	3.7	3.6	3.1	2.5	2.3	0.7	0.7	0.8
Earnings and profitability									
Return on assets (annualized)	3.1	1.9	3.3	3.8	3.8	3.9	3.7	2.8	3.0
Return on equity (annualized)	29.8	19.6	38.2	34.7	32.7	35.1	35.7	27.5	29.0
Interest margin to gross income	62.7	56.6	57.5	60.1	62.7	53.1	54.5	60.8	63.9
Noninterest expense to gross income	56.6	65.1	50.3	52.9	45.5	49.7	55.9	58.0	54.8
Net interest margin (annualized) [3]	4.1	3.2	2.8	4.3	4.6	4.1	4.2	4.0	4.1
Net noninterest margin (annualized) [4]	0.0	-0.4	0.0	-0.4	-1.0	-0.2	-0.8	-1.2	-1.2
Expense to income	46.4	54.5	52.6	50.3	55.2	54.2	61.4	64.1	61.0
Interest expense to gross income	11.8	15.3	10.7	11.1	10.7	12.5	14.4	16.9	15.9
Liquidity									
Core liquid assets to total assets [5]	39.6	41.6	40.8	33.0	28.6	38.2	45.2	44.6	44.2
Broad liquid assets to total assets [6]	52.0	54.7	54.2	49.1	47.9	55.4	58.2	57.8	55.7
Liquid assets (broad) to short term liabilities	58.1	61.2	60.0	55.9	55.0	62.4	63.7	63.4	60.6
Liquid assets (broad) to total liabilities	58.0	60.6	59.2	55.2	54.3	62.2	64.7	64.3	62.1
Liquid assets to deposit liabilities	62.5	64.3	62.7	59.5	57.8	65.7	68.5	48.5	47.6
Foreign exchange exposure									
Net open foreign exchange position to capital	7.9	8.9	8.8	1.9	3.0	0.0	3.4	4.5	-4.0

Source: Central Bank of Seychelles.

[1] Data from 2015 onwards include purely offshore banks.

[2] Defined as: equity capital/(assets-interest in suspense-provisions).

[3] Defined as: (Interest income - interest expense)/average assets.

[4] Defined as: (Noninterest income - noninterest expense)/average assets.

[5] Core liquid assets include cash, balances with CBS, and deposits with other banks.

[6] Broad liquid assets include core liquid assets plus investments in government securities.

Table 6. Seychelles: Schedule of Reviews Under the Policy Coordination Instrument, 2017–20

Program Review	Test Date	Review Date
Board discussion of a PCI request		December 13, 2017
First Review	December 31, 2017	April 30, 2018
Second Review	June 30, 2018	October 31, 2018
Third Review	December 31, 2018	April 30, 2019
Fourth Review	June 30, 2019	October 31, 2019
Fifth Review	December 31, 2019	April 30, 2020
Sixth Review	June 30, 2020	October 31, 2020

Source: IMF

Table 7. Seychelles: Indicators of Fund Credit, 2016-24

	2016	2017	2018	2019	2020	2021	2022	2023	2024
			(Millions of SDR)						
Existing Fund credit									
Stock [1]	28.0	27.9	24.8	19.9	14.7	10.7	7.0	4.2	2.5
Obligation	0.9	3.0	1.7	1.9	5.5	4.4	3.9	2.9	1.9
Principal (repayments/repurchases)	0.9	2.8	1.7	1.8	5.2	4.1	3.7	2.7	1.8
Charges and interest	0.0	0.2	0.0	0.1	0.4	0.3	0.2	0.2	0.1
Disbursements	…	3.3	…	…	…	…	…	…	…
Prospective Fund credit									
Disbursement	0.0	1.6	…	…	…	…	…	…	…
Stock [1]	13.1	14.8	14.8	14.8	14.8	14.8	14.8	14.8	14.8
Obligations [2]	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Principal (repayments/repurchases)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Charges and interest	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Stock of existing and prospective Fund credit [1]	28.0	29.5	24.8	19.9	14.7	10.7	7.0	4.2	2.5
In percent of quota	122.2	128.8	108.2	86.9	64.3	46.6	30.4	18.4	10.7
In percent of GDP	2.8	2.8	2.2	1.7	1.2	0.9	0.5	0.3	0.2
In percent of exports of goods and services	2.9	2.7	2.2	1.8	1.3	0.9	0.6	0.3	0.2
In percent of gross reserves	7.6	7.7	6.4	5.3	3.9	2.8	1.9	1.1	0.7
Obligations to the Fund from existing and prospective Fund arrangements									
Disbursements	0.0	4.9	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Obligations	0.9	3.0	1.7	1.9	5.5	4.4	3.9	2.9	1.9
Principal (repayments/repurchases)	0.92	2.77	1.71	1.80	5.16	4.07	3.70	2.73	1.77
Charges and interest	0.00	0.25	0.00	0.11	0.37	0.29	0.21	0.15	0.11
In percent of quota [3]	4.0	13.2	7.5	8.3	24.1	19.0	17.1	12.6	8.2
In percent of GDP	0.1	0.3	0.2	0.2	0.5	0.4	0.3	0.2	0.1
In percent of exports of goods and services	0.1	0.3	0.2	0.2	0.5	0.4	0.3	0.2	0.1
In percent of gross reserves	0.2	0.8	0.4	0.5	1.5	1.2	1.0	0.8	0.5

Sources: IMF Finance Department; and IMF staff estimates and projections.

[1] End-of-period.

[2] Repayment schedule based on repurchase obligations. Obligations to the Fund from Existing and Prospective Fund Arrangements includes charges.

[3] Effective February 2016, the new quota of SDR 22.9 million is applied.

Annex I. Debt Sustainability Analysis

Seychelles' public debt trajectory is projected to remain on a steadily downward path if the authorities take the necessary fiscal measures to ensure primary surpluses of 2½ percent of GDP as envisaged under the PCI. Public debt is expected to fall below 50 percent (46.9 percent) of GDP by end-2022 and decline further thereafter. The authorities' public debt management and steadfast reduction in the level of public debt would reduce gross financing needs and vulnerabilities in the heat map significantly over the medium term. External private debt remains elevated, but this largely reflects foreign investment in the tourism industry, with the foreign currency earnings of the sector mitigating risks. However, as a small island economy, Seychelles remains vulnerable to various shocks: gross public and external financing needs remain very high for the foreseeable future, and the large foreign currency-denominated debt remains a key source of risk. Further progress in reducing the public debt stock and extending the maturities of domestic public debt is therefore warranted.

1. **Evolution of the public debt stock since the previous DSA:** The DSA is broadly in line with the previous DSA conducted for the 2nd PCI review. The projected level of end-2019 public debt stock is slightly higher than previously projected, because of the injection of $30 million (about 2 percent of GDP) of guarantees to protect the preference share of Air Seychelles owned by Etihad, which was not expected at the time of the previous DSA. Due to this new guarantee, public debt to GDP ratio at end-2021 under the baseline is expected at around 51¾ percent, marginally above the authorities' debt reduction goal of below 50 percent by that time. Nonetheless, the public debt ratio is projected to decline steadily throughout the projection period under the baseline, similarly to what was projected at the previous DSA. The impact of all shock scenarios on public debt to GDP ratio is muted compared with the previous DSA, given the downward revision to the external borrowing and effective interest rate under the baseline.

2. **Macroeconomic and fiscal assumptions:** The assumptions underpinning the DSA are those of the baseline scenario of this Staff Report (SR), which is similar to those assumed under the previous DSA. Real GDP growth is projected at around 3.9 percent in 2019 and hovering in the range of between 3.5 and 4.1 percent in the medium term—around the estimated potential rate, similarly to the previous DSA. Inflation projections for 2019–20 were revised down compared with the previous DSA. Projections for effective interest rate were revised down compared with the previous DSA given the downward revision to the inflation projections and lower-than-expected interest rate in 2018. The program primary fiscal surplus is expected to be 2½ percent of GDP from 2019 onwards, in line with the authorities' target envisaged under the PCI.[1]

3. **The definition of public debt in this DSA includes:** (i) central government debt as reported by the authorities; (ii) government guarantees issued for loans extended to state-owned enterprises; and (iii) obligations to the IMF. In view of the structural excess liquidity in Seychelles,

[1] The program primary surplus includes net lending to SOEs.

debt issued by the central government for monetary purposes, which stood at 9.3 percent of GDP at end-2018, is included in the public debt stock in this analysis: while there is an offsetting unremunerated deposit in the central bank, the debt does impose an interest cost and rollover need for the public sector.[2] However, a portion of this monetary debt is projected to be unwound as the central bank develops other instruments for managing monetary policy.

4. The DSA framework suggests that Seychelles' public debt (including government guarantees) is currently close to the high-risk benchmark but is expected to continue falling steadily provided that the authorities implement fiscal consolidation as envisaged under the PCI. Debt was still high at around 60 percent of GDP at end-2018, close to the indicative threshold used in the DSA framework to highlight the high debt level. However, assuming the authorities' commitment to debt reduction and fiscal discipline remains unchanged with no major negative economic shocks, the debt level is projected to fall significantly over the medium term under the baseline scenario, falling below 50 percent (46.9 percent) by end-2022, or by end-2021 if the domestic debt issued for monetary purposes is excluded.

5. The authorities are urged to steadfastly implement fiscal consolidation to reduce public debt vulnerability. The red (high vulnerability) blocks of the heat map arise from the large gross financing needs resulting from the high level of public debt and the short maturity of domestic debt.[3] In addition to the fiscal consolidation, the authorities would need to extend the maturities of the domestic debt, where possible, as indicated at the time of the 2019 Article IV consultation, to mitigate the risks arising from the high gross financing needs.

6. Realism of the baseline assumptions is balanced. With forecast errors for real GDP growth over the period 2009–17 broadly centered around the median, staff projections have been fairly unbiased in the past, suggesting little tendency towards over optimism. While the projected primary balances imply a relatively high fiscal surplus, Seychelles' strong track record since 2009 means that this does not require any further fiscal adjustment.

7. The debt path remains below the high-risk benchmark under all shock scenarios. Under the real exchange rate shock (real depreciation by around 16 percent after 2020), the debt-to-GDP ratio would peak at around 61 percent in 2020 and fall thereafter but would remain around 2¼ percentage points above the 50 percent target for 2022. Other one-time shocks to real GDP growth (lower than the baseline by 2 percent during 2020–21) and the real interest rate (667 basis points after 2020) would merely moderate the pace of the fall in the debt-to-GDP ratio, but could delay the authorities' attainment of their debt reduction goal by a few years. The asymmetric fan chart, however, highlights that a persistently looser fiscal position

[2] The negative residuals after 2020 are accounted for by the amortization of the publicly-guaranteed debt and the repayment of debt to the IMF (which is a liability of the CBS).

[3] While there is virtually no short-term external public debt (on original maturity basis), most of the domestic debt has a maturity of less than one year.

would keep debt at an elevated level and could prevent the authorities' debt target from being attained in the foreseeable future.

8. A combined macro-fiscal shock would send the debt-to-GDP ratio to 67½ percent, still below the critical value of 70 percent. The combined macro-fiscal shock is an aggregation of the shocks to real growth, the interest rate, the primary balance and the exchange rate. Under this scenario, the debt-to-GDP ratio would peak at around 67½ percent before falling very gradually thereafter, while the debt-to-revenue ratio would increase to around 170 percent and the gross financing needs would hover in the range between 29¼ and 33½ percent.

9. The baseline scenario and the various shocks produced by the DSA template indicate that, while Seychelles remains vulnerable to exogenous shocks, continued strong policy implementation should see these risks diminish over the medium term. Under the baseline, gross financing needs fall over the projection period but remain elevated at over 20 percent of GDP until 2022, reflecting the short tenor of most of the domestic debt. Moreover, gross financing needs increase significantly under various shocks, especially under the combined macro-fiscal shock or the real GDP growth shock, and remain above the indicative threshold until 2022 even under the baseline. While the steadfast implementation of fiscal consolidation will help to reduce gross financing needs, further measures to extend the average maturity of domestic issuance wherever possible would also reduce rollover risks.

10. The existence of substantial debt contracted by state-owned enterprises requires careful analysis of the related potential risks. Staff's analysis suggests additional debt liabilities of the SOEs total around 13 percent of GDP, the majority of which is owed by SEYPEC and Air Seychelles. While these debts do not benefit from an explicit government guarantee, in the past, such obligations have at times been assumed by the government. In 2012, for example, the government assumed liabilities and obligations of Air Seychelles amounting to around 5 percent of GDP. Meanwhile, Air Seychelles' project box bond of $71.5 million (around 5 percent of GDP) owed to Etihad could pose roll over risks to the company in 2020 and 2021.[4] This DSA therefore provides a scenario where SOEs' external debts of a similar magnitude (5 percent of GDP) are assumed by the government in 2020. Under this scenario, the government's goal of reducing the public debt below 50 percent of GDP would be delayed by two years, highlighting the need to monitor such debts carefully with a view to mitigating any risk of SOEs' obligations migrating to the government balance sheet.

11. The results of the updated external DSA reveals that total external debt remains elevated in the range of 110–114 percent of GDP throughout the projection period.[5] However, the risks continue to be mitigated by the composition of external debt and maturity

[4] See Country Report No. 19/194.

[5] Total external debt at end-2019 has been revised upwards due to government's injection of external guarantees and revision of 2019 FDI composition towards more debt and less equity based on data up to mid-2019.

profile: Seychelles' debt stock consists largely of borrowing by the public and tourism sectors. As of end-2018, about one quarter of the country's external debt is medium to long-term government borrowing, largely from official sources and at favorable interest rates and

maturities, and close to half is FDI-related borrowing, largely to the hotel sector, with the short-term debt being largely trade credits and other lines of credit.

12. Standardized stress tests confirm that the country's external debt is particularly sensitive to currency depreciation shocks. A 30 percent depreciation of the domestic currency would lead to a spike in external debt-to-GDP ratio to around 175 percent in 2020 and it would reach 178 percent by the end of the projection period, compared to about 110 percent under the baseline scenario. The interest rate, growth and current account shocks would have a more muted, yet significant effect on the country's external debt profile. A permanent ¼ standard deviation shock to either growth or the current account (excluding interest payments) would lead to a gradual increase in the external debt-to-GDP ratio to around 144 percent by the end of the projection period

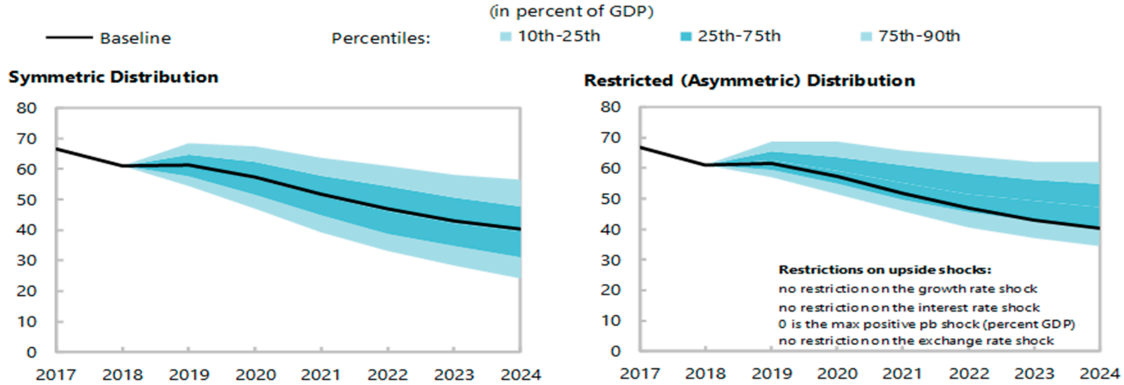
Figure 1. Seychelles: Public DSA Risk Assessment

Heat Map

Debt level 1/	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability shock
Gross financing needs 2/	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability Shock
Debt profile 3/	Market Perception	External Financing Requirements	Change in the Share of Short-Term Debt	Public Debt Held by Non-Residents	Foreign Currency Debt

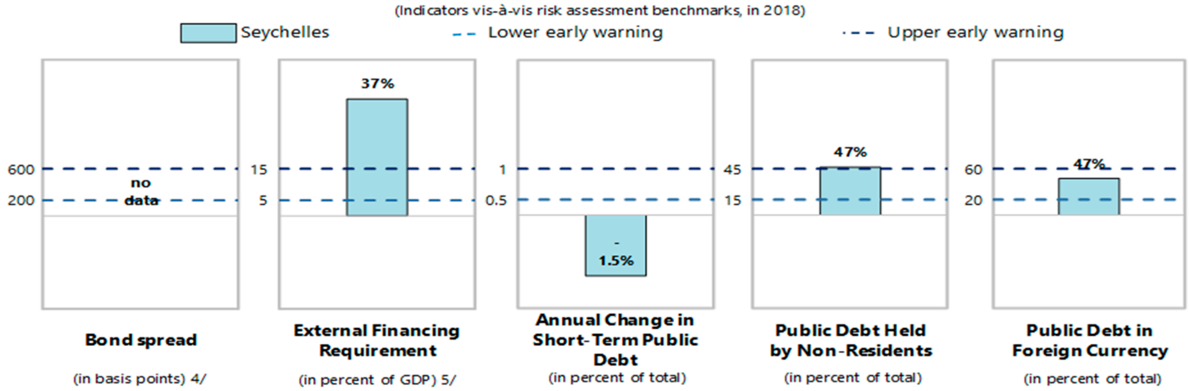
Evolution of Predictive Densities of Gross Nominal Public Debt

(in percent of GDP)



Debt Profile Vulnerabilities

(Indicators vis-à-vis risk assessment benchmarks, in 2018)



Source: IMF staff.

1/ The cell is highlighted in green if debt burden benchmark of 70% is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

2/ The cell is highlighted in green if gross financing needs benchmark of 15% is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

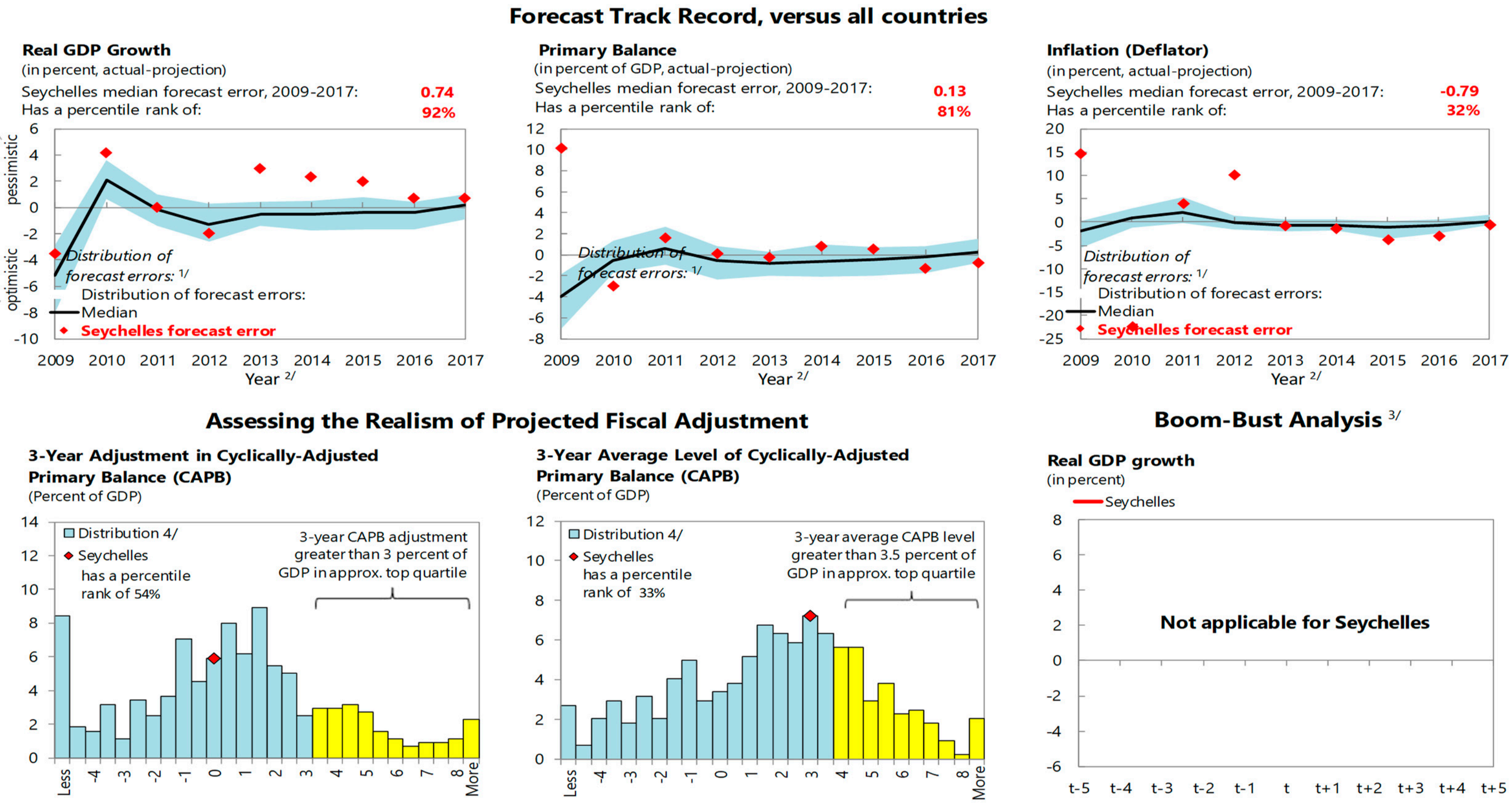
3/ The cell is highlighted in green if country value is less than the lower risk-assessment benchmark, red if country value exceeds the upper risk-assessment benchmark, yellow if country value is between the lower and upper risk-assessment benchmarks. If data are unavailable or indicator is not relevant, cell is white.
Lower and upper risk-assessment benchmarks are:

200 and 600 basis points for bond spreads; 5 and 15 percent of GDP for external financing requirement; 0.5 and 1 percent for change in the share of short-term debt; 15 and 45 percent for the public debt held by non-residents; and 20 and 60 percent for the share of foreign-currency denominated debt.

4/ Long-term bond spread over U.S. bonds, an average over the last 3 months, 23-Mar-19 through 21-Jun-19.

5/ External financing requirement is defined as the sum of current account deficit, amortization of medium and long-term total external debt, and short-term total external debt at the end of previous period.

Figure 2. Seychelles: Public DSA – Realism of Baseline Assumptions



Source : IMF Staff.

1/ Plotted distribution includes all countries, percentile rank refers to all countries.

2/ Projections made in the spring WEO vintage of the preceding year.

3/ Not applicable for Seychelles, as it meets neither the positive output gap criterion nor the private credit growth criterion.

4/ Data cover annual obervations from 1990 to 2011 for advanced and emerging economies with debt greater than 60 percent of GDP. Percent of sample on vertical axis.

Figure 3. Seychelles: Public Sector Debt Sustainability Analysis (DSA) – Baseline Scenario

(In percent of GDP unless otherwise indicated)

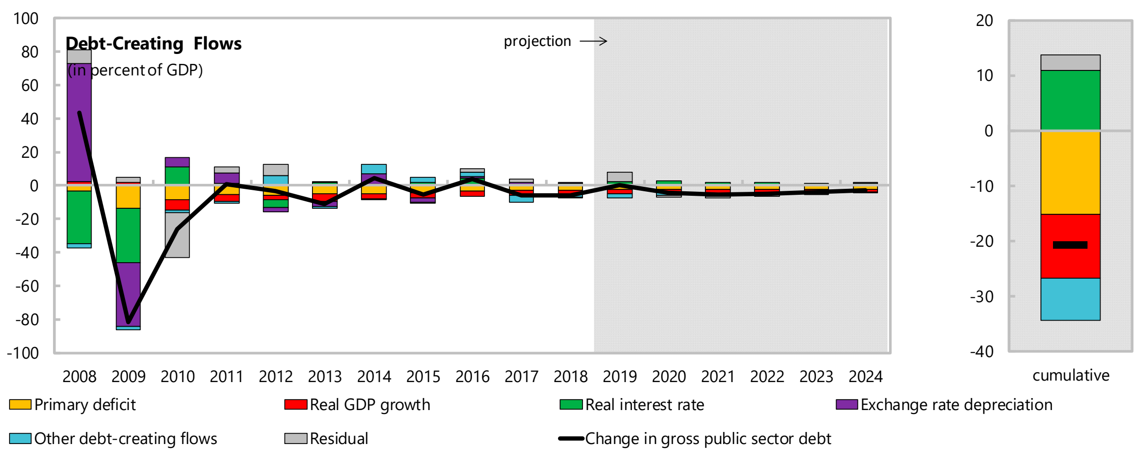
Debt, Economic and Market Indicators [1/]

	Actual			Projections					
	2008-2016 [2/]	2017	2018	2019	2020	2021	2022	2023	2024
Nominal gross public debt	93.2	66.8	61.0	61.4	57.3	51.7	46.9	43.1	40.3
Of which: guarantees	1.7	3.6	3.2	6.6	6.3	5.9	5.5	5.1	4.8
Public gross financing needs	23.5	30.1	27.9	24.0	27.7	25.0	21.5	17.1	17.0
Net public debt		55.4	51.7	55.2	52.6	48.4	44.6	41.4	39.2
Real GDP growth (in percent)	3.5	4.3	4.1	3.9	3.5	4.1	4.0	3.8	3.6
Inflation (GDP deflator, in percent)	8.8	3.4	3.1	1.4	1.8	2.9	2.8	3.0	3.0
Nominal GDP growth (in percent)	12.3	7.9	7.3	5.4	5.4	7.2	6.9	7.0	6.7
Effective interest rate (in percent) [4/]	5.3	4.8	5.3	5.2	6.3	6.6	6.4	6.2	6.1

As of June 21, 2019		
Sovereign Spreads		
EMBIG (bp) 3/		478 bp
5Y CDS (bp)		N/A
Ratings	Foreign	Local
Moody's	Baa2	Baa2
S&Ps	BB	BB
Fitch	BB	BB

Contribution to Changes in Public Debt

	Actual			Projections							
	2008-2016	2017	2018	2019	2020	2021	2022	2023	2024	cumulative	debt-stabilizing primary balance [9/]
Change in gross public sector debt	-8.4	-5.9	-5.8	0.5	-4.2	-5.6	-4.8	-3.8	-2.7	-20.6	
Identified debt-creating flows	-8.0	-8.3	-5.1	-5.2	-3.2	-4.3	-3.9	-3.6	-3.2	-23.4	
Primary deficit	-6.1	-3.0	-2.9	-2.5	-2.5	-2.5	-2.5	-2.5	-2.5	-15.1	-0.7
Primary (noninterest) revenue and grants	37.3	36.3	37.6	38.4	40.3	39.2	37.1	36.9	36.5	228.4	
Primary (noninterest) expenditure	31.1	33.3	34.6	35.9	37.8	36.7	34.5	34.4	34.0	213.3	
Automatic debt dynamics [5/]	-3.0	-1.3	-0.9	-0.1	0.6	-0.3	-0.3	-0.3	-0.2	-0.7	
Interest rate/growth differential [6/]	-7.8	-2.1	-1.2	-0.1	0.6	-0.3	-0.3	-0.3	-0.2	-0.7	
Of which: real interest rate	-5.3	0.8	1.3	2.2	2.6	1.9	1.7	1.4	1.2	10.9	
Of which: real GDP growth	-2.6	-2.9	-2.5	-2.3	-2.1	-2.2	-1.9	-1.7	-1.4	-11.6	
Exchange rate depreciation [7/]	4.9	0.8	0.3	...	...	...	...	...	...	...	
Other identified debt-creating flows	1.1	-4.0	-1.3	-2.6	-1.2	-1.5	-1.1	-0.8	-0.5	-7.6	
Privatization Proceeds (negative)	-0.9	-0.4	0.0	0.0	0.0	-0.4	-0.4	-0.3	0.0	-1.0	
Contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Domestic debt issuance for monetary purposes	2.0	-3.6	-1.3	-2.6	-1.2	-1.1	-0.7	-0.5	-0.5	-6.6	
Residual, including asset changes [8/]	-0.4	2.4	-0.7	5.7	-1.0	-1.3	-0.9	-0.2	0.5	2.7	



Source: IMF staff.

1/ Public sector is defined as general government and includes public guarantees.

2/ Based on available data.

3/ Long-term bond spread over U.S. bonds.

4/ Defined as interest payments divided by debt stock (excluding guarantees) at the end of previous year.

5/ Derived as [(r - π(1+g) - g + ae(1+r)]/(1+g+π+gπ)) times previous period debt ratio, with r = interest rate; π = growth rate of GDP deflator; g = real GDP growth rate; a = share of foreign-currency denominated debt; and e = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).

6/ The real interest rate contribution is derived from the numerator in footnote 5 as r - π (1+g) and the real growth contribution as -g.

7/ The exchange rate contribution is derived from the numerator in footnote 5 as ae(1+r).

8/ Includes changes in the stock of guarantees, asset changes, and interest revenues (if any). For projections, includes exchange rate changes during the projection period.

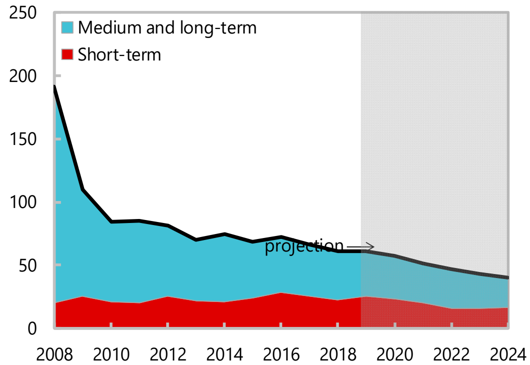
9/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

Figure 4. Seychelles: Public DSA – Composition of Public Dept and Alternative Scenarios

Composition of Public Debt

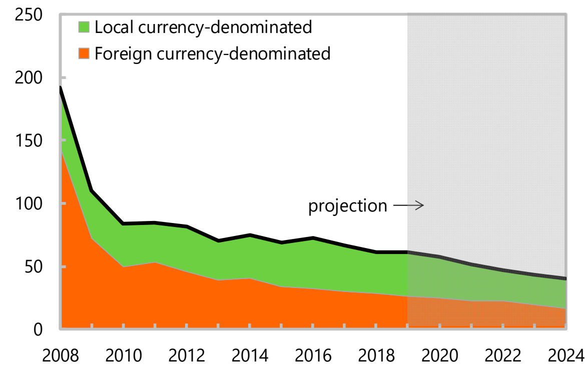
By Maturity

(in percent of GDP)



By Currency

(in percent of GDP)

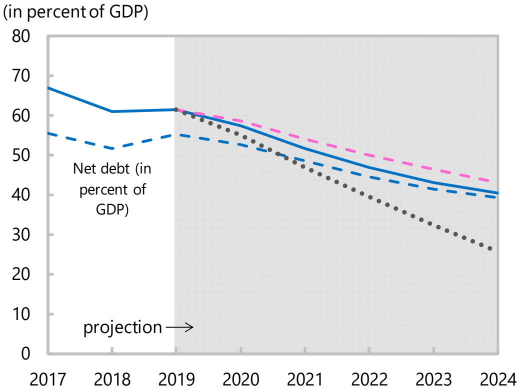


Alternative Scenarios

Baseline　Historical　Constant Primary Balance

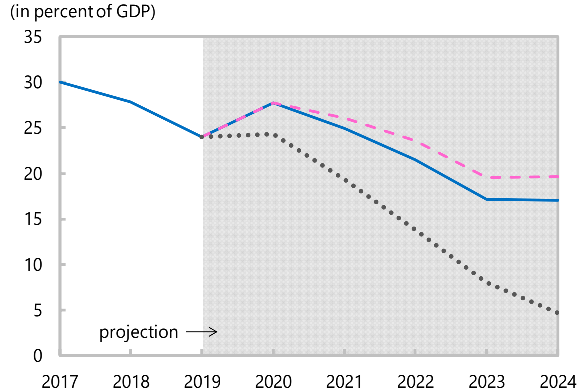
Gross Nominal Public Debt

(in percent of GDP)



Public Gross Financing Needs

(in percent of GDP)



Underlying Assumptions

(in percent)

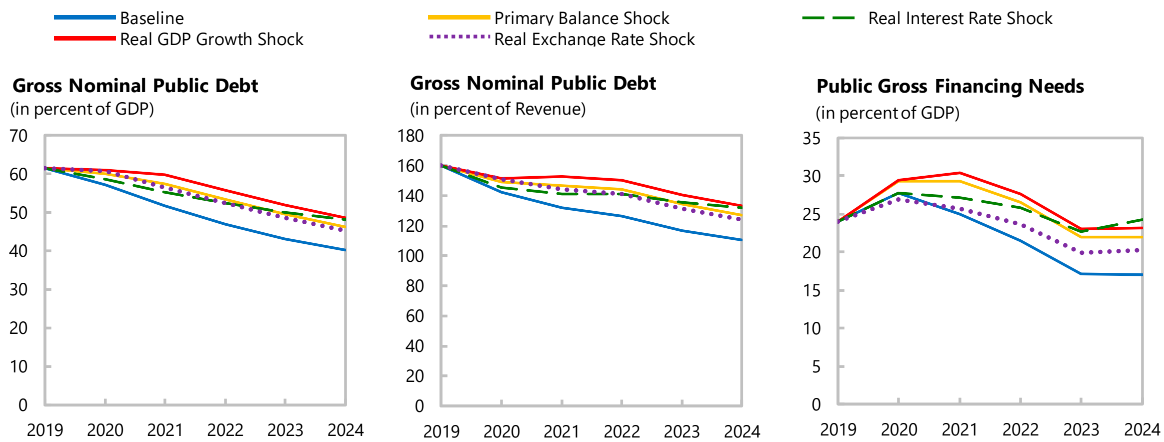
Baseline Scenario	2019	2020	2021	2022	2023	2024
Real GDP growth	3.9	3.5	4.1	4.0	3.8	3.6
Inflation	1.4	1.8	2.9	2.8	3.0	3.0
Primary Balance	2.5	2.5	2.5	2.5	2.5	2.5
Effective interest rate	5.2	6.3	6.6	6.4	6.2	6.1
Constant Primary Balance Scenario						
Real GDP growth	3.9	3.5	4.1	4.0	3.8	3.6
Inflation	1.4	1.8	2.9	2.8	3.0	3.0
Primary Balance	2.5	2.5	2.5	2.5	2.5	2.5
Effective interest rate	5.2	6.3	6.5	6.2	6.0	5.9

Historical Scenario	2019	2020	2021	2022	2023	2024
Real GDP growth	3.9	4.2	4.2	4.2	4.2	4.2
Inflation	1.4	1.8	2.9	2.8	3.0	3.0
Primary Balance	2.5	5.7	5.7	5.7	5.7	5.7
Effective interest rate	5.2	6.3	5.8	5.7	5.7	5.9

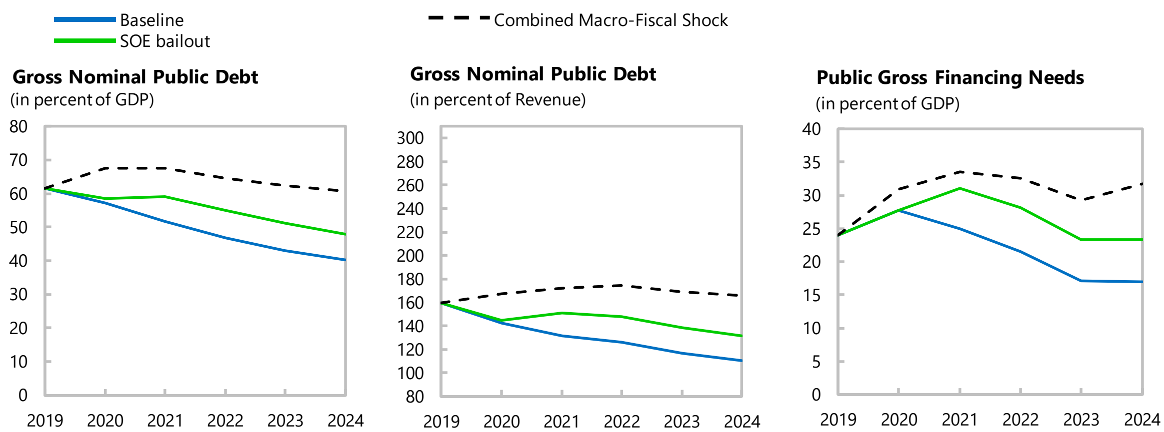
Source: IMF staff.

Figure 5. Seychelles: Public DSA – Stress Tests

Macro-Fiscal Stress Tests



Additional Stress Tests



Underlying Assumptions
(in percent)

Primary Balance Shock	2019	2020	2021	2022	2023	2024
Real GDP growth	3.9	3.5	4.1	4.0	3.8	3.6
Inflation	1.4	1.8	2.9	2.8	3.0	3.0
Primary balance	2.5	0.9	0.8	2.5	2.5	2.5
Effective interest rate	5.2	6.3	6.5	6.2	5.9	5.8
Real Interest Rate Shock						
Real GDP growth	3.9	3.5	4.1	4.0	3.8	3.6
Inflation	1.4	1.8	2.9	2.8	3.0	3.0
Primary balance	2.5	2.5	2.5	2.5	2.5	2.5
Effective interest rate	5.2	6.3	8.8	8.8	9.1	9.4
Combined Shock						
Real GDP growth	3.9	1.5	2.1	4.0	3.8	3.6
Inflation	1.4	1.3	2.4	2.8	3.0	3.0
Primary balance	2.5	0.9	0.6	2.5	2.5	2.5
Effective interest rate	5.2	6.7	8.2	8.3	8.6	9.0

Real GDP Growth Shock	2019	2020	2021	2022	2023	2024
Real GDP growth	3.9	1.5	2.1	4.0	3.8	3.6
Inflation	1.4	1.3	2.4	2.8	3.0	3.0
Primary balance	2.5	1.6	0.6	2.5	2.5	2.5
Effective interest rate	5.2	6.3	6.5	6.2	5.9	5.8
Real Exchange Rate Shock						
Real GDP growth	3.9	3.5	4.1	4.0	3.8	3.6
Inflation	1.4	7.2	2.9	2.8	3.0	3.0
Primary balance	2.5	2.5	2.5	2.5	2.5	2.5
Effective interest rate	5.2	6.7	6.2	5.9	5.7	5.6

Source: IMF staff.

Table 1. Seychelles: External Debt Sustainability Framework, 2013-2024

(In percentage of GDP; unless otherwise indicated)

		Actual						Projections						
		2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	Debt-stabilizing non-interest current account 6/
1	**Baseline: External debt**	125.2	100.2	100.8	105.4	109.0	111.3	**114.0**	**113.4**	**112.0**	**111.4**	**110.6**	**110.2**	-15.7
2	Change in external debt	-42.5	-25.0	0.6	4.6	3.6	2.3	2.7	-0.6	-1.4	-0.6	-0.8	-0.4	
3	Identified external debt-creating flows (4+8+9)	-14.4	0.3	8.7	13.1	5.6	9.8	3.6	2.0	0.6	0.8	1.6	1.5	
4	Current account deficit, excluding interest payments	10.8	22.1	18.1	19.2	20.0	16.6	16.2	16.4	16.8	16.8	16.3	15.7	
5	Deficit in balance of goods and services	-196.2	15.7	9.0	10.2	11.7	11.9	10.8	10.9	11.6	11.5	10.7	10.0	
6	Exports	94.7	102.2	94.2	94.8	102.0	99.7	96.0	95.5	96.0	95.5	96.9	97.1	
7	Imports	-101.5	118.0	103.2	105.0	113.7	111.6	106.8	106.5	107.6	107.0	107.6	107.1	
8	Net non-debt creating capital inflows (negative)	7.5	-21.4	-7.5	-3.9	-9.5	-1.8	-9.6	-11.7	-12.9	-13.0	-11.8	-12.1	
9	Automatic debt dynamics 1/	-32.7	-0.4	-2.0	-2.2	-4.9	-5.1	-3.0	-2.7	-3.3	-3.1	-2.9	-2.0	
10	Contribution from nominal interest rate	1.2	1.0	0.5	1.3	0.4	0.4	1.1	1.2	1.2	1.1	1.2	1.7	
11	Contribution from real GDP growth	-8.1	-5.6	-4.8	-4.4	-4.3	-4.2	-4.2	-3.9	-4.5	-4.3	-4.1	-3.8	
12	Contribution from price and exchange rate changes 2/	-25.8	4.2	2.3	0.8	-1.0	-1.3	...	...	...	...	...	...	
13	Residual, incl. change in gross foreign assets (2-3) 3/	-28.1	-25.3	-8.0	-8.5	-2.0	-7.5	-0.9	-2.6	-2.0	-1.3	-2.4	-2.0	
	External debt-to-exports ratio (in percent)	132.3	98.0	107.1	111.2	106.8	111.7	118.8	118.7	116.7	116.7	114.2	113.4	
	Gross external financing need (in billions of US dollars) 4/	772.2	828.7	533.3	639.9	557.7	590.3	518.1	575.2	635.7	637.0	611.4	600.8	
	in percent of GDP	58.2	61.7	38.7	44.8	37.1	37.3	31.4	33.6	35.2	33.5	30.5	28.5	
	Scenario with key variables at their historical averages 5/							**119.1**	**122.7**	**126.7**	**131.1**	**135.2**	**138.1**	-14.4
	Key Macroeconomic Assumptions Underlying Baseline													
	Real GDP growth (in percent)	6.0	4.5	4.9	4.5	4.3	4.1	3.9	3.5	4.1	4.0	3.8	3.6	
	GDP deflator in US dollars (change in percent)	18.2	-3.2	-2.3	-0.8	0.9	1.2	0.5	-0.1	1.3	1.4	1.5	1.4	
	Nominal external interest rate (in percent)	0.9	0.8	0.5	1.4	0.4	0.4	1.0	1.1	1.1	1.1	1.1	1.7	
	Growth of exports (US dollar terms, in percent)	12.8	9.2	-5.5	4.3	13.4	2.9	0.5	3.0	6.0	4.9	7.0	5.3	
	Growth of imports (US dollar terms, in percent)	3.9	17.5	-10.3	5.5	14.1	3.3	-0.1	3.2	6.7	4.9	6.0	4.6	
	Current account balance, excluding interest payments	-10.8	-22.1	-18.1	-19.2	-20.0	-16.6	-16.2	-16.4	-16.8	-16.8	-16.3	-15.7	
	Net non-debt creating capital inflows	-7.5	21.4	7.5	3.9	9.5	1.8	9.6	11.7	12.9	13.0	11.8	12.1	

1/ Derived as [r - g - r(1+g) + ea(1+r)]/(1+g+r+gr) times previous period debt stock, with r = nominal effective interest rate on external debt; r = change in domestic GDP deflator in US dollar terms, g = real GDP growth rate, e = nominal appreciation (increase in dollar value of domestic currency), and a = share of domestic-currency denominated debt in total external debt.

2/ The contribution from price and exchange rate changes is defined as [-r(1+g) + ea(1+r)]/(1+g+r+gr) times previous period debt stock. r increases with an appreciating domestic currency (e > 0) and rising inflation (based on GDP deflator).

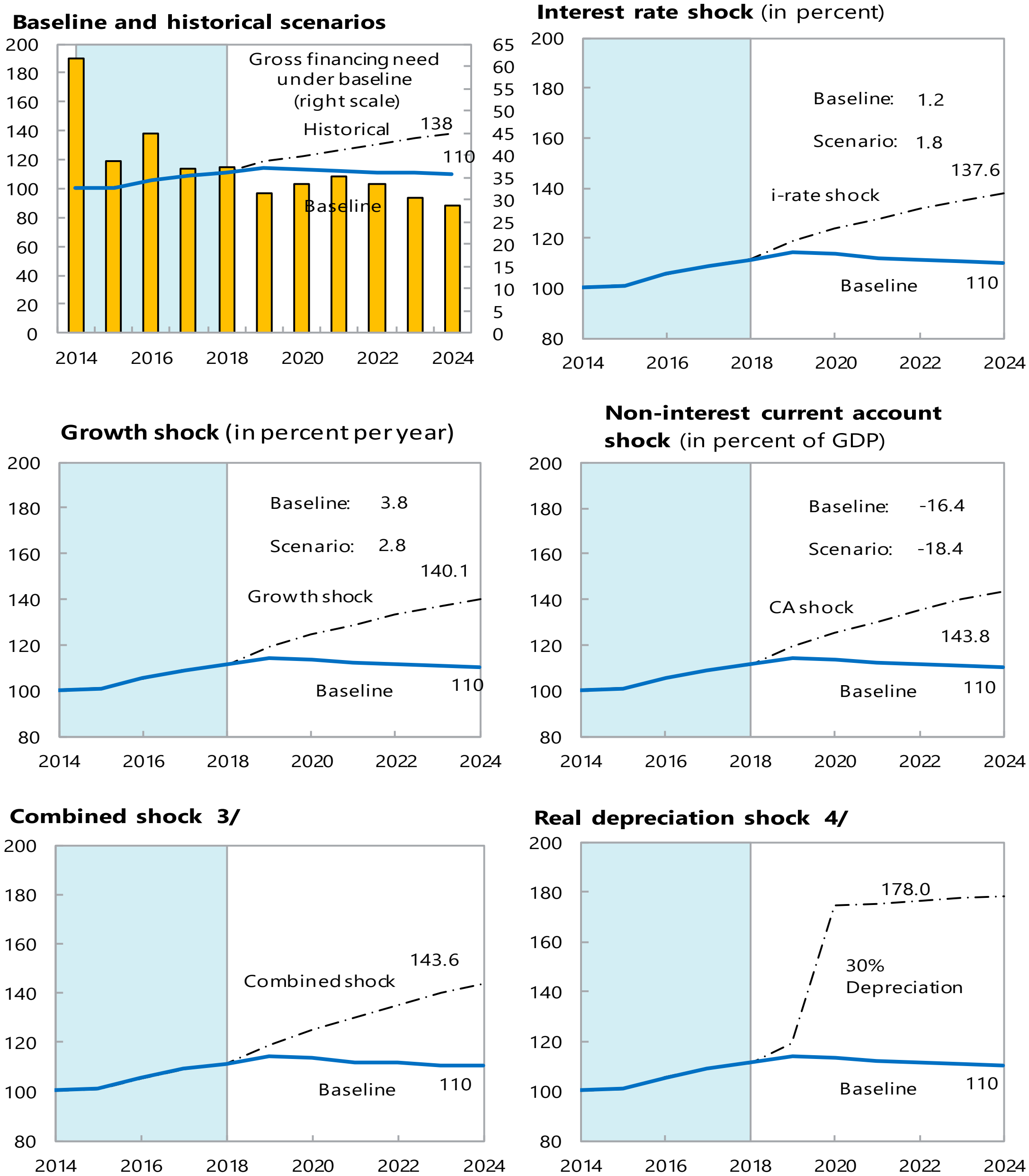
3/ For projection, line includes the impact of price and exchange rate changes.

4/ Defined as current account deficit, plus amortization on medium- and long-term debt, plus short-term debt at end of previous period.

5/ The key variables include real GDP growth; nominal interest rate; dollar deflator growth; and both non-interest current account and non-debt inflows in percent of GDP.

6/ Long-run, constant balance that stabilizes the debt ratio assuming that key variables (real GDP growth, nominal interest rate, dollar deflator growth, and non-debt inflows in percent of GDP) remain at their levels of the last projection year.

Figure 6. Seychelles: External Debt Sustainability: Bound Tests 1/ 2/



Sources: International Monetary Fund, Country desk data, and staff estimates.
1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.
2/ For historical scenarios, the historical averages are calculated over the ten-year period, and the information is used to project debt dynamics five years ahead.
3/ Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and current account balance.
4/ One-time real depreciation of 30 percent occurs in 2020.

Appendix I. Program Statement

Victoria,
November 25, 2019

Madame Kristalina Georgieva
Managing Director
International Monetary Fund
700 19th Street, N.W.
Washington, D.C. 20431
USA

Madame Managing Director:

Following is an updated Program Statement (PS) that provides a description of Seychelles' recent economic and financial performance and policies for 2019 and 2020.

Macroeconomic performance continues to be strong in 2019 and outlook remains favorable. Program implementation is largely on track.

The government continues to believe that the policies and measures set forth in the attached PS are adequate for achieving the objectives of the Policy Coordination Instruments (PCI)-supported program, which was approved by the IMF Executive Board on December 13, 2017. Given our commitment to macroeconomic stability, the government will promptly take any additional measures needed to achieve the program objectives. It will consult with the IMF—at its own initiative or whenever the Managing Director requests such consultation—before adopting any such measures or in advance of revisions to the policies contained in the attached PS. Moreover, the government will provide the IMF with such information as the IMF may request as regards to the progress made in implementing the economic and financial policies and in achieving the program objectives.

Based on our performance under the program and the sustainability of our planned policies, we are requesting that the IMF Executive Board complete the fourth review of the PCI-supported program and approve the proposed modification of the end-December 2019 quantitative targets as reflected in Table 1a in the attached PS.

In line with our commitment to transparency, we request that the IMF publish this letter, the attached statement, and the staff report. We will simultaneously publish these documents in Seychelles.

Sincerely yours,

/s/

Ambassador Maurice J Loustau Lalanne

Minister of Finance, Trade, Investment and Economic Planning

/s/

Caroline Abel

Governor,

Central Bank of Seychelles

Attachment: Technical Memorandum of Understanding (TMU)

Updated Program Statement for the Period December 2017–December 2020

1. This Updated Program Statement describes Seychelles' recent economic and financial performance as well as our policies for 2020 and updates the Program Statement dated May 29, 2019.

A. Macroeconomic Performance in 2019 and Outlook for 2020

2. Economic performance in 2019 has been satisfactory, with real GDP growth rate now estimated to attain 3.9% as against an initial forecast of 3. 5% at the time of the third program review. GDP growth was sustained by a good performance of the tourism sector, production of manufactured goods, construction, and information and communication. Tourism earnings are increasing by around 5 %, in line with tourist arrivals for the first 8 months of 2019 which is up by 7.1 %.

3. Consumer price inflation in 2019, now expected at 2.0 % on average for the year, is lower than previously expected 2.6%, reflecting the lower-than expected actual inflation for the first 8 months due to increased competition in retail sector and smaller-than-projected size of utility tariff adjustments in July.

4. In 2020, it is expected that real GDP growth will decelerate slightly to 3.5%; value added in the tourism sector should continue to rise by about 5%, food sector and information and communication should also continue to have a favorable growth of around 5%. The average inflation for the year 2020 is projected at 2.1%.

5. On the external side, the external current account deficit in percent of GDP in 2019 is projected at 17.3%, slightly higher than in 2018. In 2020 the external current account deficit is projected at 17.6% of GDP. Foreign direct investment is expected to increase, related to new projects in tourism, and this will lead to higher imports; at the same time fishing sector exports are also projected to increase.

6. The program target for net international reserves at end-December 2019 is proposed to be revised down by $9 million compared with the target proposed at the time of the 3rd review because of the higher-than-expected imports in recent months. During 2020, gross and net international reserves is expected at roughly the same level as at end-2019.

7. The ratio of government and government guaranteed debt to GDP at end-2019 is expected to be at 61.5%, against the forecast of 57.7% at the time of the third review; the difference is largely due to new government guarantees that are planned to be issued in favor of Air Seychelles before end 2019, equivalent to 2 % of GDP. This ratio is expected to decline to 57.2 % by end-2020.

B. Performance Under the PCI in 2019

8. The program is largely on track. The floor the primary surplus and net international reserves (NIR) for end-June 2019 was attained with some margin. End-June annual average inflation was at 2.7%, well within the inner bound under the monetary policy consultation clause (MPCC). However, end-June primary surplus stood at SR 254 million compare to a program target of SR 265 million as at June 2019: missed the target by SR 11 million. This is mainly because of the cable and wireless sanctions fees that were expected to be received in June 2019 amounting to US$14 million (SR 98 million) will only be received in the fourth quarter of 2019. The sanction agreement is being finalised for signature before end of September 2019. Regarding structural RTs, the amendments on Public Enterprise Monitoring Committee (PEMC) Act will be submitted to Cabinet by end-December 2019, slightly delayed from end-September 2019 targeted at the time of the third review. The amended legal framework for crisis management, bank resolution and safety nets will be submitted to Cabinet by December 2020. Concerning bank regulations, a policy framework paper for an implementation of Basel II pillar 1 and Basel III capital definitions will be submitted to the Cabinet by end-December 2019 (5th review RT).

C. Budgetary Performance in 2019, Outlook for 2020 and Medium-Term Framework

9. The budget performance in 2019 was in line with the program, and the primary surplus target, at 2.5 % of GDP, is expected to be reached. Tax revenue is expected to be in line with the initial budget, with a shortfall in business tax offset by higher personal income tax receipts. Current expenditure has been boosted by the 5% public sector wage adjustment, which subject to the current judicial process, is expected to be implemented in the fourth quarter, as well as the long-term services allowance implemented in July 2019. This was offset by a freeze on recruitment which came into force as from end August. Only posts in priority sectors such as Health, Education and returning graduates are being allowed for recruitment. In addition, a budget cut of up to 11% in the Goods and Services for the 2019 budget across Government has been applied. As a result, Wages and Salaries are expected to be revised downwards by 2% and Goods and Services by 1% for 2019. Capital expenditure is expected to be lower than expected, mainly because of slower project execution. Given the lower-than-expected collection of fees and charges so far this year, the program target for the primary surplus at end-December 2019 is proposed to be revised down by SCR 5 million to SR 584 million (still at 2.5% of GDP in 2019) compared with the target proposed at the time of the 3rd review.

10. In 2019 the measures taken to boost tax revenue have had the desired effect. They include: (i) the reduction in the fuel tax exemptions for the tourism sector; (ii) the introduction of a sugar tax on beverages. In total these measures have yielded the equivalent of 0.4 % of GDP.

11. The 2020 budget has been prepared with the aim to maintain a primary surplus of 2.5 %. New tax measures include an upward revision of the levy on the import of motorcars, which are expected to yield 0.2% of GDP. The property tax introduced in early 2020 is expected to yield revenue of 0.2% of GDP. Tax arrears collection, in particular in regard to the business tax, have been accelerated.

Fiscal Measures for 2020 budget	SR' million
Introduction of a Personalised License Plate Number	10
Tax Review on Motor Vehicles; Increase of Environmental Levy	42.1
Change in Tax Structure for Alcoholic Beverages; taxed according to their alcohol content	43.4
Increase in FSA registration Fees (as dividend from SFA)	50
Increase in GOP fees for the foreigner that stay in the country for more than 5 years;	30
Budget Freeze on the recruitment	38
Reduction in Goods and Services by 4%	36.4
Introduction of a processing Fee for Postage and Courier service	6.8
TOTAL	**256.7**

12. On the expenditure side, the effort of rationalizing functions and programs in the area of social services will continue, with the aim to increase efficiency in service delivery and achieve savings, which will produce a saving of 0.1% of GDP in 2020. Some of the immediate measures will be to (i) establish the appropriate structure that will directly employ, dispatch and monitor the work of domiciliary care workers, (ii) move away from a Full and Half Day care system to one that is based on the needs of the individuals and (iii) adopt the WHO Disability Assessment Schedule 2.0, as the assessment tool, moving away from the existing Bartell Assessment tool. Over the medium term, a household level database (a social registry) will be created to allow relevant ministries to see the household as a whole. Creating such a database will promote collaboration across Ministries, Departments, and Agencies (MDAs) involved in providing social protection benefits and services. The database can then be used to identify the needs of potential beneficiary households, referring or linking them to other existing or new services and service providers, either through a case management approach or on an automatic basis. There is also a plan to reform the Invalidity and disability pensions to include application of a new assessment methodology focusing on functional capacity rather than only physical capacity, and consequently will include providing retraining and rehabilitation for invalid and disabled individuals to allow them to benefit from joining the labor force. Finally, reforms for social welfare assistance beneficiaries will provide them the training, job search, rehabilitation, and counseling services that will help put them on an upward career path. Wages and salaries expenditure will be contained by recruitment freeze: maintaining more or less the same number of vacant posts as 2019 and re-allocating these posts from low to higher priority areas such as the Seychelles Revenue Commission (SRC), Ministries of Health (MOH) and Education (MOE). Revisions of schemes and new schemes of services are also being rationalized with only critical schemes funded such as Judiciary, SRC, and Department of Immigration and Civil status.

13. The process of rationalizing capital expenditure in 2019 will continue in 2020 through alternative financing plan. The construction of a "Government house "financed through a grant will lead to savings in rental costs from 2022. The government is keeping under review the large public investment projects announced in the 2018 State of the Nation Address (SONA), with the view to minimizing costs and obtain favorable financing, including grants, so as not to jeopardize the medium-term target to maintain the public debt – GDP ratio below 50% after 2021. The feasibility study for a new LNG power plant is proceeding with the IFC assistance. The land reclamation scheme under consideration will be based on a private public partnership approach, with the private sector having to pay upfront for land leases, so as to provide upfront financing for the reclamation cost.

14. The renewable energy development plan detailed in the previous program statement, **which is a corner stone of the sustainable development agenda, is being executed as announced**. This include the 2 solar farms on Romainville built by the Public Utility Company (PUC), the 5 MW solar farm financed by IRENA and the Abu Dhabi Development Fund, the 1 MW solar plants on Praslin and La Digue, the smart energy in public spaces program financed by the government of India.

D. The Implementation of the Structural Reform Agenda

Revenue Management

15. The SRC continues to pursue the achievement of its strategic objectives. Emphasis is being placed in areas such as (i) modernization and reform initiatives, (ii) improving revenue and debt collection with focus on reduction of arrears, and (iii) improving the efficiency and effectiveness of SRC operations and service delivery to ultimately reduce revenue leakage and improve voluntary compliance. SRC has developed a new approach for recovery of debts, whereby the debt collection functions for Tax and Customs are separated. The proposed approach involves structural change, whereby debt collection function will be centralized under the Director for Enforcement, in the Domestic Tax Division. In addition to the changes in its structure, SRC has also increased efforts in debt collection. The collection of large debts is being closely monitored by SRC management on monthly basis. Furthermore, SRC has increased the number of cases undergoing prosecution compared to the previous years. SRC recently underwent a TADAT. The rationale behind TADAT was to help SRC in obtaining an independent, evidence-based, all round assessment of the performance and health of the tax administration. Based on the results of the assessment, SRC will be drafting an action plan with specific tasks to be undertaken to improve its performance.

Results Based Management Framework

16. The Government will continue its effort in enhancing public sector efficiency, effectiveness, transparency and accountability through its result- based management, Strategic Planning, Programme Performance Based Budgeting, Performance Monitoring and Evaluation, and Personnel Management Systems.

Public Private Partnership (PPP)

17. With large national projects identified to be implemented through PPPs, the Government recently submitted the PPP Bill for approval by National Assembly in fourth quarter of 2019. The process of improving efficiency in public investment will continue through 2020, with the authorities aiming to carry out a Public Investment Management Assessment (PIMA) in the second quarter of 2020.

Review of Public Finance Management Regulatory Framework

18. **The Public Finance Management Act 2012 and Regulations 2014 are in the process of being revised to integrate new developments and facilitate the implementation of the accounting manual.** The Public Debt Management Act was also revised in 2019, to establish a formal authorization process for any new borrowing, be it guaranteed or not, by State-Owned Enterprises (SOEs) or parastatals, and to establish a guarantee strategy and define clearly the organization of public debt and guarantee governance.

19. The government will continue its efforts to reduce debt-related risks. As part of the plan to lengthen maturity of domestic debt, the Government will guarantee a five-year bond to be issued by the Property Management Company (PMC) to finance infrastructure projects. The liability management exercise previously discussed with the World Bank will no longer be pursued by the Government. The objective of the exercise was to convert the Bond from USD to Euros in order to align the debt to our earnings (most of the country's earnings are in Euros) and to benefit in terms of slightly lower interest rate on Euro denominated, debts. After careful considerations, the authorities have decided not to proceed with this exercise in view that the initial cost savings that was being anticipated will now not materialize.

SOE Reform

20. Government continues to intensify its efforts to strengthen the overall corporate governance and strengthen fiscal risks management and reporting of SOEs. PEMC has proposed a new piece of legislation entitled "Public Enterprise Act". The new Act will accommodate best practices in ownership, oversight and of Public Enterprises, including compliance mechanisms with sanctions for non-compliance and mechanisms to identify and manage financial risks.

21. An ownership policy and dividend policy has been drafted and will be submitted to Cabinet by end-October. One main objective of the ownership policy is to have a coherent approach to SOEs oversight and monitoring. The dividend policy strives to give the appropriate balance between the need to retain earnings for re-investment without going to the government coffer and the need to give the owner returns on its investments.

Minimizing Fiscal Risk of SOEs

22. **Government remains committed to minimizing the fiscal risk of SOEs and continues to pay close attention to the unprofitable ones.** The Government requested the World Bank to review the Air Seychelles strategy with the scope of providing a good understanding of its financial viability and long-term sustainability. Based on the analysis, the restructured network of Air Seychelles' improves the bottom-line of the company by drastically reducing losses, but the risk remains. The Etihad shareholder requested a upfront guarantee by the government of its US$30 million preferred share by end-2019. It will increase the debt-GDP ratio by about 2%. The Government does not intend to issue further guarantees in connection with the Air Seychelles restructuring. Should additional government support, including assuming of the company's liabilities and/or extending guarantees, beyond that assumed in the medium-term baseline, need to be considered in future, corrective actions to offset any fiscal impact would be discussed with the IMF in the context of future program reviews. PEMC will submit a comprehensive operational and governance assessments of Air Seychelles to the Cabinet by end-December 2019 (5th review RT). If the assessments find remaining weaknesses in the company's operation and governance, the government will formulate an action plan to address such weaknesses as a new RT for the 6th review.

Improving Business Environment

23. **The Government will continue its efforts in improving the business climate.** An action plan detailing the necessary measures to be undertaken for the period 2019-2021 has been developed and currently being implemented. Its implementation is being monitored by a High-Level Ease of Doing Business Committee. The investment framework of the country is also being reviewed and UNCTAD is providing the necessary technical assistance to review the investment policy. Furthermore, the policy paper on the amendments to the Companies Act and Insolvency Act will be submitted to Cabinet by end-September 2020 (6th review RT).

E. Monetary and Exchange Rate Policy.

24. Thanks to the tightened monetary policy stance implemented since the second quarter of 2018, inflationary pressures have eased during 2019. The 12-month average inflation rate which stood at 3.7 per cent at the end of 2018 fell to 2.4 per cent in August 2019 whilst on a year-on-year basis, the price increase slowed from an average of 3.4 per cent at the end of 2018 to 1.8 per cent in August 2019. In view of such developments, coupled with the projected moderate increase in the general price level, the CBS loosened monetary policy in the fourth quarter of 2019.

25. **The CBS introduced a Monetary Policy Rate (MPR) to serve as the key policy signal for communications of monetary policy effective January 2019.** The focus of monetary policy has since then shifted from indirectly influencing the intermediate target of money supply growth to guiding short-term interest rates through the MPR. The revision to the monetary policy framework is part of a gradual process deemed necessary to improve the transmission of the policy signal to the real economy. The MPR was initially set at 5.5 per cent to be consistent with the tight monetary policy stance for the first quarter of 2019. The interest rates on the Bank's Standing Deposit Facility (SDF) and Standing Credit Facility (SCF) were raised to 2.5% and 8.5% respectively. Such stance was maintained until the fourth quarter of 2019 when monetary policy was loosened in view of expected ease in inflationary pressures. As a result, the MPR was reduced to 5.0 per cent whilst the SDF and SCF to 2.0% and 8.0% respectively.

26. **Gross International Reserves are expected to remain at a level sufficient to buffer against external shocks.** This is consistent with the IMF-calculated metrics on foreign reserves adequacy. Nonetheless, the CBS will continue with its opportunistic purchases of foreign exchange from the market through foreign exchange auctions (FEAs) with the objective to at least sustain the reserves level.

27. The Advisory and Asset Management agreement signed in January 2019 between the IBRD and the CBS remains effective. As part of the engagement, US$100 million worth of assets is being managed by the Reserves Advisory Management Program (RAMP). With the aim to further build capacity in the area of reserves management, the CBS staff attended numerous trainings sponsored by RAMP in line with the agreement including training in the support role of PAT2 for staff in the middle, back and front offices including IT. Moreover, the CBS is receiving technical assistance from RAMP through advisory services to convert its internally managed bond portfolio from a passive to an enhanced indexation portfolio strategy.

28. The CBS remains committed to a floating exchange rate. The CBS intervention in the foreign exchange market will only be to smooth out excess volatility. All opportunistic purchases of foreign exchange from the market to enhance the level of international reserves will be done in a manner that does not compromise CBS' primary objective of promoting domestic price stability.

29. To ensure policy coordination, the CBS will continue to work in close collaboration with the Ministry responsible for Finance on the issuance of government securities for monetary policy purposes. Such coordination remains critical given the environment of structural excess liquidity as well as the reserves accumulation objective of the country. However, such fiscal support will be done in line with government's debt reduction strategy. A working group has been set up comprising of technical staff from the CBS and the Ministry of Finance with the aim of contributing towards the improvement in liquidity management by the two agencies and the development of the government securities market. Furthermore, it will facilitate the co-operation and communication among technical staff across the two institutions in the coordination of relevant analytical work and/or research being conducted. The meetings will be held on monthly basis and ad-hoc meetings may be organized to discuss pertinent issues.

30. The CBS has successfully completed phase 1 and phase 2 of the six-phase action plan on monetary policy implementation following the IMF TA mission in October 2017. Following the approval of the policy paper for revision of the CBS Act for monetary reserve requirement in January 2019, the instruction paper in preparation for the minimum reserve requirement (MRR) regulation has been submitted to the Attorney General's Office for further legal procedures. Some of the outstanding tasks as part of the action plan, relate to the online portal updates, where a first round of testing is being conducted to cater for the revisions to liquidity management operations. This project is expected to be completed by December 2019. The project to operationalize the CAA module on the online portal is expected to be completed by the end of 2020. In the interim, the CBS has started work to establish a manual process for CAA with the preparation of relevant procedures manual and guidelines. The CBS is exploring alternative platforms for the conduct of domestic market operations by liaising with relevant stakeholders, both internally and externally as part of the project to develop and modernize the national payment system. With the aim to develop the interbank markets, the terms of reference (ToR) of the interbank markets working group was approved in July 2019. This working group is mandated to act in an advisory capacity to the CBS and the banking industry.

F. Financial Sector

31. The CBS continues efforts to strengthen the framework for financial stability. Whilst the banking sector remains profitable and well capitalized, work is ongoing to strengthen the macro-prudential framework to ensure that any potential emerging risk can be addressed. To this end, work is ongoing to formulate a Financial Stability Act with relevant macro-prudential tools that can be utilized to address emerging risk. A revised timeline for the drafting of a Financial Stability policy paper has been drawn, wherein submission of the policy paper for a Financial Stability Act to the Cabinet of Ministers has been set for end-September 2020 (6^{th} review RT). Furthermore, Cabinet approved the policy framework for crisis management, bank resolution, and safety nets in December 2018. This will make provision for the resolution authority to have adequate powers and tools to ensure it is capable of dealing with problematic banks and non-bank financial institutions under the purview of the CBS, without leading to financial stability issues. The CBS is currently seeking assistance for a legal expert to assist the AG's office to draft the law in view of capacity constraints for this specialized legislation. Draft legislation to solidify the legal framework for crisis management, bank resolution, and safety nets will be submitted to Cabinet by November 2020, delayed from the target of March 2020 set at the time of the 3^{rd} review, due to staffing constraints of the AG's office.

32. The CBS has been in close dialogue with banks with regards to the implementation of IFRS9. Consultations between the CBS, Financial Institutions (FIs) and external auditors on the implementation of IFRS 9 are on-going. Amendments have been made to the Financial Institutions (Credit Classifications and Provisioning) regulations to replace the term IAS 39 by IFRS 9. Building on the technical support received from the IMF, the CBS has issued a new set of IFRS 9 return. Subsequently, training on the compilation of the return was organized for all the FIs. Furthermore, the internal working group on IFRS9 is preparing a framework aimed at communicating forward looking macroeconomic indicators to FIs to support their adherence to the IFRS 9 requirements. The CBS is receiving follow up technical assistance from Afritac South in October 2019, with fair value measurement implications on IFRS 9 as the main focus area.

33. The CBS remains committed to ensure its prudential regulatory framework remains in line with international best practice and is effective in safeguarding the safety and soundness of the financial sector. Work on the development of the risk-based supervision framework for the prudential supervision of banks is still ongoing. It is expected that the model will be finalized by the end of 2019 with planned implementation from 2020 onwards. Moreover, the CBS continues to make progress on the work being undertaken as part of the Financial Institutions Act amendments. This is with the aim of ensuring that the legislative frameworks remain on par with international standards and best practices. It is anticipated that the policy proposals for the amendments will be finalized by end of 2019 after which they will be shared with the IMF for peer review. With regards to the adoption and implementation of a risk-based approach to AML/CFT supervision, as per the RAS agreed with the World Bank, the development of a manual and other relevant documentation is expected to be undertaken between August and December 2020.

34. The adoption of the Basel II framework is on track to be implemented by end-December 2020. The CBS has started engagement with the Attorney General's office regarding revision of the Financial Institutions (Capital Adequacy) Regulations to incorporate Basel II pillar 1. Policy paper for Basel II pillar 1 is expected to be approved by Cabinet before end-December 2019 (5th review RT). As part of the consultancy to develop the risk-based supervision framework, Basel II pillar II will also be implemented as of 2020 onwards along with relevant disclosure requirements under Basel II pillar III. As regards to the adoption of capital definition under Basel III, the CBS will be finalizing its policy paper by end of 2019 (5th review RT) after which amendments to legislations will be affected before end of 2020 with the required changes to the Financial Institutions Act.

35. To address potential risk emanating from the de-risking phenomenon, the authorities remain committed to improving the jurisdiction's AML/CFT framework. In October 2018 Cabinet approved the policy paper for the new AML Act which addresses the legislative deficiencies which had been identified by the mutual evaluation report (MER) conducted by ESAAMLG. The new AML Act will empower sectoral supervisors in order to ensure that all sectors are adequately supervised, making effective use of available resources within the regulatory environment. The law will also make provisions to allow for risk-based approach to supervision. It will further ensure that the necessary recommendations under the FATF standards are encased in the regulatory framework. Further to that a legal expert has been contracted to assist the AG's office in drafting the Act. It is expected that the Bill will be submitted to Cabinet by March 2020 (5th review RT). Moreover, a National AML/CFT Committee has been appointed in order to improve national coordination and ensure that the deficiencies as noted in the MER are addressed in a timely manner. Additionally, a Technical Committee has also been appointed to assist the National Committee. The Cabinet of Ministers has also approved for a Reimbursable Advisory Services (RAS) agreement with the World Bank to provide technical assistance in reviewing and drafting legislative amendments to laws relevant to preventing money laundering and terrorist financing as well as National Strategy. In addition, this agreement will provide for capacity building of relevant AML supervisors (in formulating a Risk Based approach), law enforcement agencies, as well as the prosecution office and judiciary. RAS has been signed and a country mission was held from August 27 - 29, 2019 to look at the Proceeds of Crime Act and the Prevention of Terrorism Act. Another mission which took place from October 07 – 10, 2019 served to lay the groundwork for the development of the AML/CFT risk-based supervision framework. The next mission is tentatively scheduled for December 2019 with subsequent missions prior to March 2020 to implement the framework. In addition, a residential advisor has been contracted and will provide advice, support and mentoring and assist the national counterparts involved in AML/CFT matters, such as on policies, operations and structures inclusive of trainings to the different sectors. Government is also allocating additional resources in the 2020 budget for the law enforcement agencies and regulatory authorities to ensure that the country enhances its AML/CFT capacity and ensure that it has an effective AML/CFT framework as per the National AML/CFT action plan.

36. **Development of the oversight framework of the national payment system is continuing.** A Principles for Financial Market Infrastructures (PFMI) Assessment was completed in March 2019. An action plan to implement the recommendations of the PFMI assessment is in the process of being finalized. One of the key components is the drafting of a revised payment system oversight framework. A first draft of the oversight framework has been prepared and is expected to be finalized by December 2019. In addition, research for amendments to the National Payment System Act is progressing and is expected to be finalized by end of 2019. Such amendments aim to address shortcomings of the current legislation that impair oversight and enforcement measures undertaken by the CBS as well as align the CBS' regulatory framework with international standards and best practices.

37. Efforts are ongoing to formulate the financial sector strategy. Work is well advanced on the Fintech and AML CFT strategy respectively. Government will also before end-2019 start the process of drafting its digital economy strategy. The diagnostic has already been concluded with the assistance of the World Bank. All these strategies will help to inform the finalization of a comprehensive Financial Sector strategy, including both on-shore and offshore sectors, in line with international best practices, by June 2020. Cabinet has approved the policy to strengthen entity transparency (including on basic and beneficial ownership information on the domestic companies and international financial services companies and the establishment of a master registry of beneficial owners) in line with the FATF standards and the IMF's capacity development recommendations. A new Beneficial Ownership Act will be submitted to the Cabinet by end-March 2020 (5^{th} review RT).

G. Financial Inclusion and Market Conduct

38. The CBS continues to pursue its endeavor to modernize the national payment system to achieve more efficient, convenient and affordable innovative payment facilities. Being a core pillar of the Financial Sector Development Implementation Plan, an efficient and effective national payment system is a critical contributor in serving a reliable foundation for the growth of FinTech, expanding the exploitation gaps for small- and medium-sized enterprises (SMEs) to foster and building public confidence in the financial system. It also serves in bringing about the growth of affordable innovative payments not only from an end user perspective but also that of other parties in the value chain, i.e., merchants thereby ensuring financial inclusion in all its aspects. It is within this context that, the CBS is in the process of liaising with relevant stakeholders, both internally and externally to conclude the formulation of the road map regarding the most viable and feasible model to adopt. 2020 is being targeted to start the implementation of the road map.

39. To promote financial inclusion and create an enabling environment for SMEs to have improved access to finance, the CBS continues on its path to reinforce the legal framework for credit reporting and enhance the Credit Information System. This includes broadening the coverage of credit information and improving on the credit worthiness assessment. With a significant number of stakeholders to be consulted and with more aspects to look at in the design of the system due to the broadening of the coverage for credit reporting, the target to have a new credit reporting act in place and the system effective is expected to be 2020.

40. Complementing the work being done on infrastructure, competition remains an important element in promoting financial inclusion in the local financial services sector. Regardless of an efficient and reliable infrastructure, restrictive market practices can impede the start-up and growth of SMEs and consumer choice. Interlinked with the work on building a sound legal framework for market conduct and consumer protection, aspects of competition will be looked at through the Risk Based Market Conduct Framework that the CBS is contemplating for adoption in 2020. It is also envisaged that the adoption of Fintech could potentially address some of the barriers to competition in the financial sector.

41. Work kicked off in early 2019 through a workshop incorporating both awareness on FinTech and consultation with relevant stakeholders in order for the CBS and FSA to commence the formulation a National Financial Technologies (Fintech) Strategy. The workshop served as a starting point for the CBS and FSA to gauge the public's views in the subject matter. The most critical factor brought forth and which will inform the heart of the FinTech Strategy is how FinTech can contribute towards local economic and financial development, with particular focus on creating an enabling environment as well as safeguards to minimize associated risks relating to Fintech. The Strategy aims at identifying value-adding Fintech companies to the local context. It will further identify risks that Fintech poses for the country and related policy directions relating to different forms of Fintech and is expected to be completed before the end of 2019.

42. Considering the current context and the significant work being done to develop the financial sector, the protection of consumers is also a key aspect. It has to be looked at especially with the introduction of new technologies in financial services. This is to be achieved through the enactment of a Financial Consumer Protection Act, expected to be submitted to the National Assembly for approval before the end of 2019. The Financial Consumer Protection Bill aims at providing for a comprehensive regulatory framework for the equitable and fair treatment of financial consumers, including Digital Financial Consumer Protection.

43. With the recognition that consumer protection is also complemented by consumer education initiatives, the CBS and FSA has worked diligently to implement the National Financial Education Strategy launched in December 2017. In its second year of implementation, it is therefore deemed fit that a Monitoring and Evaluation Framework is formulated to assess the implementation of the strategy. The Monitoring and Evaluation Framework is being drafted internally which will subsequently be reviewed by the Alliance for Financial Inclusion. The Framework is expected to be completed in 2020.

H. Safeguards at the CBS

44. The CBS continued to implement the recommendations of the voluntary safeguards assessment that were completed in February 2018. Draft amendments to the CBS Act, including provisions to enhance the governance arrangements, are expected to be presented to the National Assembly in September 2020. The CBS has drafted an AML/CFT Policy which is being reviewed internally. This Policy will establish the full scope of work that the Bank will undertake to be compliant with domestic laws and international standard for AML and CFT. Following the External Quality Assessment, internal audit division (IAD) continues to strengthen its internal processes in order to address the gaps identified in the assessment.

I. Efforts to Improve External Sector Statistics

45. The CBS plans to improve external sector statistics, particularly the estimate of tourism receipts. The CBS is of the view that the current estimate does not fully capture the total value of the sector's foreign exchange income which leads to an over-estimation of current account deficit. The new estimate will be incorporated in the compiled BOP statistics following completion of the internal review process and receipts of comments from the IMF Statistics Department.

J. Program Monitoring

46 The modification of end-December 2019 quantitative targets on primary fiscal balance and net international reserves and end-December 2019 monetary consultation clause are being proposed (Table 1a of the PS). The government, the CBS, and the IMF also agreed on the reform targets shown in Table 2 of the PS. The fifth review is scheduled to be completed by April 30, 2020, and sixth review by October 31, 2020.

Table 1. Seychelles: Quantitative Targets (QTs) Under the PCI, December 2019 – December 2020

	2019					2020	
	June QT			December QT		June QT	December Projection
	3rd Review	Act.	Status	3rd Review	Proposed	Proposed	Projection
Quantitative Targets							
Net international reserves of the CBS, millions of U.S. dollars (floor) [1]	396	409	Met	412	403	402	402
Primary balance of the consolidated government (cumulative floor)	265	254	Not Met	589	584	211	611
Accumulation of external payments arrears by the public sector (ceiling) [3]	0.0	0.0	Met	0.0	0.0	0.0	0.0
Monetary Policy Consultation Clause [4]							
Inflation (mid-point, percent) [5]	2.8	2.7		2.6	2.0	1.8	2.1
Inflation (upper bound, percent) [5]	4.8			4.6	4.0	3.8	4.1
Inflation (lower bound, percent) [5]	0.8			0.6	0.0	-0.2	0.1
Inflation (upper inner-bound, percent) [5]	4.3			4.1	3.5	3.3	3.6
Inflation (lower inner-bound, percent) [5]	1.3			1.1	0.5	0.3	0.6
Memorandum items:							
Nominal public debt (millions of Seychelles Rupees, ceiling) [1,2]	13,301	13,001		13,342	14,257	14,352	13,836
Program accounting exchange rates [6]							
SR/US$ (end-of-quarter)		14.02			14.06	14.06	14.06
US$/Euro (end-of-quarter)		1.14			1.10	1.10	1.10
US$/UK pound (end-of-quarter)		1.33			1.22	1.22	1.22
US$/AUD (end-of-quarter)		0.71			0.67	0.67	0.67
US$/CAD (end-of-quarter)		0.76			0.75	0.75	0.75
US$/CNY (end-of-quarter)		0.15			0.14	0.14	0.14
US$/SDR (end-of-quarter)		1.40			1.37	1.37	1.37

Sources: Seychelles authorities; and IMF staff estimates and projections.

[1] Measured at program accounting exchange rate. The NIR floor is adjusted as defined in the TMU. End-June 2019 target is adjusted downward by $7 million due to the shortfall of receipts from sales of Cable and Wireless Company, in accordance with TMU.

[2] Nominal public debt includes government guarantees.

[3] The nonaccumulation of new external payment arrears constitutes a standard continuous target. Excludes arrears for which a rescheduling agreement is sought.

[4] When the end of period annual average headline inflation is above/below the upper/lower bound, a formal consultation with the Executive Board would be triggered.

[5] Average of year-on-year headline inflation for the past 12 months.

[6] Program exchange rates have been set according to prevailing market rates at the latest available update.

Table 2. Seychelles : Continuous Targets

- Not to impose or intensify restrictions on the making of payments and transfers for current international transactions
- Not to introduce or modify multiple currency practices
- Not to conclude bilateral payments agreements that are inconsistent with Article VIII
- Not to impose or intensify import restrictions for balance of payments reasons

Table 3. Seychelles. Reform Targets Under the PCI, 2019–20

Actions	Timing	Objective/Status
Prior Action		
Submit a 2020 budget consistent with primary surplus target of 2.5 percent of GDP to National Assembly.		Met in November 2019.
State-Owned Enterprises (SOEs)		
Submit the amendments on Public Enterprise Monitoring Committee (PEMC) Act to the Cabinet to strengthen enforcement power of PEMC.	End September 2019 (4th review)	Not met. To be implemented in December 2019.
Submit operational and governance assessments of Air Seychelles to the Cabinet.	End December 2019 (5th review)	Reduce the potential fiscal risks arising from Air Seychelles.
Business environment		
Submit the policy paper on the draft amendments to the Companies Act and Insolvency Act to the Cabinet	End September 2020 (6th review)	Improve Business environment
Financial Sector Stability		
Submit to the Cabinet amendments to legal framework that allows to implement a risk-based approach to the supervision of banks and trusts and company service providers, consistent with the FATF standard.	End-March 2020 (5th review)	Reduce AML risks in financial and off-shore sectors.
Submit draft legislation for crisis management, bank resolution, and safety nets to the Cabinet.	End-November 2020 (6th review), reset from end-March 2020	Buttress financial sector stability.
Complete a full transition to Basel II and adopt the Basel III capital definition.	End-December 2019 (5th review)	This reform target is proposed to be revised (see below).
Submit a policy framework paper for an implementation of Basel II pillar 1 and Basel III capital definition to the Cabinet.	End-December 2019 (5th review)	Buttress financial sector stability.
Submit a policy framework paper on Financial Stability Act to the Cabinet to assign macro prudential power to relevant institutions.	End-September 2020 (6th review)	Strengthen macro prudential framework.
Submit amendments to the Cabinet to the legal framework to strengthen entity transparency (including on basic and beneficial ownership information on the domestic companies and international financial services companies and the establishment of a master registry of beneficial owners) in line with the FATF standard and the IMF's capacity development recommendations.	End-March 2020 (5th review)	Reduce AML risks in financial and international financial services sectors.

Attachment I. Technical Memorandum of Understanding

1. This technical memorandum of understanding presents the definitions of variables included in the quantitative targets and continuous targets set out in the Program Statement (PS), the key assumptions, and the reporting requirements of the Government and the Central Bank of Seychelles (CBS) needed to adequately monitor economic and financial developments. The quantitative targets, the continuous targets, and the reforms targets for 2018–19 are listed in Tables 1 and 2 attached to the PS, respectively. The quantitative targets and reform targets are listed in Tables 1 and 2 respectively. Reviews will assess quantitative targets as of specified test dates. Specifically, the fourth review will assess end-June 2019 test date, the fifth review will assess end-December 2019 test date, and sixth review will assess end-June 2020 test date.

2. Program exchange rate: For the program, the exchange rates of the Seychellois Rupee (SCR) to the U.S. dollar will be SCR14.06 per US$1 for end-December 2019 and for the year 2020. Similarly, the exchange rates of the US$ to other currencies for end-December 2019 and for the year 2020 are as follows (US$/1 other currency).

EUR	1.10
GBP	1.22
SDR	1.37
AUD	0.67
CAD	0.75
ZAR	0.07
CNY	0.14

I. QUANTITATIVE AND CONTINUOUS TARGETS

A. Net International Reserves of the CBS (Floor)

Definition

3. Net international reserves (NIR) of the CBS are defined for program monitoring purposes as reserve assets of the CBS, minus reserve liabilities of the CBS (including liabilities to the IMF). Reserve assets of the CBS are claims on nonresidents that are readily available (i.e., liquid and marketable assets, free of any pledges or encumberments and excluding project balances and blocked or escrow accounts, and bank reserves in foreign currency maintained for the purpose of meeting the reserve requirements), controlled by the CBS, and held for the purpose of intervening in foreign exchange markets. They include holdings of SDRs, holdings of foreign exchange, demand and short-term deposits at foreign banks abroad, fixed-term deposits abroad that can be liquidated without penalty, and any holdings of investment-grade securities. Reserve liabilities of the CBS comprise liabilities to nonresidents contracted by the CBS, any net off-balance-sheet position of the CBS (futures, forwards, swaps, or options) with either residents or nonresidents, including those to the IMF.

Calculation Method

4. For program monitoring purposes, reserves assets and liabilities at each test date must be converted into U.S. dollars using the end of period exchange rates assumed in the program.

Monitoring and Reporting

5. Semiannually, at each test date for program quantitative targets, the net international reserves data submitted by the CBS to the IMF will be audited by the CBS' internal audit division in accordance with International Standards on Auditing, to ensure conformity with the program definition and calculation methods. Reports will be submitted to the IMF no later than two months after each test date.

Adjusters

6. The floor on the CBS's NIR will be adjusted upward (downward) by the amount by which the external non-project loans and non-project cash grants exceeds (falls short of) the amounts assumed in the program. The floors will also be adjusted upwards (downwards) by the amount that external debt service payments fall short (exceed) the amounts assumed in the program. The floors will also be adjusted upwards (downwards) by the amount that receipts from sales of Cable and Wireless Company in Seychelles exceed (fall short of) the amounts assumed in the program.

Projections: June – December 2020 (millions of US$)

	2019		2020	
	June	December	June	December
External non-project loan 1/	0.0	0.0	0.0	0.0
External non-project cash grants 1/	0.0	0.0	0.0	0.0
External debt service payments 1/	25.7	48.6	26.3	52.4
Receipts from sales of Cable and Wireless 2/	7.0	19.0	19.0	19.0

1/ Cumulative from the beginning of each year
2/ Cumulative from the beginning of 2019

B. Monetary Policy Consultation Clause (MPCC)

Definition

7. MPCC headline inflation is defined as the year-on-year rate of change of the Consumer Price Index (CPI), averaged for the past 12 months, as measured by Seychelles' National Bureau of Statistics (NBS).

- If the observed headline inflation falls outside the ±2 percentage point range around the mid-point of projected value for end-December 2019 and end-June 2020 test dates, the authorities will complete a consultation with the Executive Board which would focus on : (i) the stance of monetary policy and whether the Fund-supported program remains on track; (ii) the reasons for program deviation, taking into account compensating factors; and (iii) proposed remedial actions if deemed necessary.

- If the observed headline inflation falls outside the ± 1.5 percentage point range around the mid-point of projected value for end-December 2019 and end-June 2020 test dates, the authorities will conduct discussions with the Fund staff.

C. Program Primary Balance of the Consolidated Government (Cumulative Floor)

8. The program consolidated government primary balance from above the line on a commitment basis is defined as total consolidated government and social security fund revenues (excluding privatization and long-term lease income receipts) less all noninterest (primary) expenditures and net lending of the government and social security fund. For program purposes the transfer of assets from the Social Security Fund to the Seychelles Pension Fund planned for 2015 will be excluded from expenditures.

D. Ceiling on the Overall Stock of Public Debt (Memorandum Item)

9. The ceiling applies to the overall stock of public debt). Public debt includes (i) central government debt; (ii) government guarantees; and (iii) obligation to the IMF. It will be defined for the purposes of the program as total outstanding gross debt liabilities. It will include, but not be limited to, liabilities in the form of securities and loans. It will exclude accounts payable. Debt will be measured at nominal value. The program exchange rate will apply to all non-SCR denominated debt. External debt is defined on a residency basis.

10. For the purposes of this memorandum item, the definition of debt is set out in Point 8(a) of the Guidelines on Public Debt Conditionality in Fund Arrangements attached to Executive Board Decision No. 15688-(14/107), adopted December 5, 2014.

(a) the term "debt" will be understood to mean a current, i.e., not contingent, liability, created under a contractual arrangement through the provision of value in the form of assets (including currency) or services, and which requires the obligor to make one or more payments in the form of assets (including currency) or services, at some future point(s) in time; these payments will discharge the principal and/or interest liabilities incurred under the contract. Debts can take a number of forms, the primary ones being as follows:

(i) loans, i.e., advances of money to the obligor by the lender made on the basis of an undertaking that the obligor will repay the funds in the future (including deposits, bonds, debentures, commercial loans and buyers' credits) and temporary exchanges of assets that are equivalent to fully collateralized loans under which the obligor is required to repay the funds, and usually pay interest, by repurchasing the collateral from the buyer in the future (such as repurchase agreements and official swap arrangements);

(ii) suppliers' credits, i.e., contracts where the supplier permits the obligor to defer payments until sometime after the date on which the goods are delivered or services are provided; and

(iii) leases, i.e., arrangements under which property is provided which the lessee has the right to use for one or more specified period(s) of time that are usually shorter than the total expected service life of the property, while the lessor retains the title to the property. For the purpose of these guidelines, the debt is the present value (at the inception of the lease) of all lease payments expected to be made during the period of the agreement excluding those payments that cover the operation, repair, or maintenance of the property.

(b) Under the definition of debt set out in this paragraph, arrears, penalties, and judicially awarded damages arising from the failure to make payment under a contractual obligation that constitutes debt are debt. Failure to make payment on an obligation that is not considered debt under this definition (e.g., payment on delivery) will not give rise to debt."

E. External Arrears of the Public Sector

11. The no accumulation of arrears to external creditors will be a continuous target under the program. External payments arrears for program monitoring purposes are defined as the amount of external debt service due and not paid within the contractually agreed period, subject to any applicable grace period, including contractual and late interest. Arrears resulting from the nonpayment of debt service for which a clearance framework has been agreed or a rescheduling agreement is sought are excluded from this definition.

II. DATA AND INFORMATION

12. The Seychelles authorities (government and CBS) will provide Fund staff with the following data and information according to the schedule provided.

The CBS will report

Weekly (within one week from the end of the period)

- Daily reserve money data.
- Foreign exchange reserves position.
- A summary table on the foreign exchange market transactions.
- The results of the liquidity deposit auctions, primary Treasury bill auctions, and secondary auctions.

Monthly (within four weeks from the end of the month)

- The monetary survey in the standardized report form format.
- The foreign exchange cash flow, actual and updated.
- Financial soundness indicators.
- Stock of government securities in circulation by holder (banks and nonbanks) and by original maturity and the debt service profile report.

The Ministry of Finance will report

Monthly (within four weeks from the end of the month):

- Consolidated government operations on a commitment basis and cash basis in the IMF-supported program format and in GFSM2001 format.
- The detailed revenues and expenditures of the central government and social security fund.
- Import and export data from the customs department.
- Public debt report reconciled with the cash operations to minimize any statistical discrepancy.
- Consolidated creditors schedule on domestic expenditure arrears of the government.

Quarterly (within one month from the end of the quarter)

- Accounts of the public nonbank financial institutions.

The government and CBS will consult with Fund staff on all economic and financial measures that would have an impact on program implementation and will provide any additional relevant information as requested by Fund staff.

The National Bureau of Statistics will report

Monthly (within 10 days from the end of the month):

CPI headline inflation, by category.