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# SEYCHELLES

July 2013

## 2013 ARTICLE IV CONSULTATION, SEVENTH REVIEW UNDER THE EXTENDED ARRANGEMENT AND REQUEST FOR MODIFICATION OF PERFORMANCE CRITERION

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2013 Article IV consultation with Seychelles, and the seventh review under the Extended Arrangement and request for modification of performance criterion, the following documents have been released and are included in this package:

- Staff Report for the 2013 Article IV consultation, seventh review under the Extended Arrangement and request for modification of performance criterion, prepared by a staff team of the IMF, following discussions that ended on March 5, 2013, 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 April 22, 2013. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.
- Informational Annex prepared by the IMF.
- Public Information Notice (PIN) summarizing the views of the Executive Board as expressed during its May 8, 2013 discussion of the staff report that concluded the Article IV consultation.
- A Press Release summarizing the views of the Executive Board as expressed during its May 8, 2013 discussion of the staff report that completed the request and/or review.
- Statement by the Executive Director for Seychelles.

The documents listed below have been or will be separately released.

Letter of Intent sent to the IMF by the authorities of Seychelles*
Technical Memorandum of Understanding*

*Also included in Staff Report

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

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**International Monetary Fund**
**Washington, D.C.**

# SEYCHELLES

April 22, 2013

## STAFF REPORT FOR THE 2013 ARTICLE IV CONSULTATION, SEVENTH REVIEW UNDER THE EXTENDED ARRANGEMENT AND REQUEST FOR MODIFICATION OF PERFORMANCE CRITERION

## KEY ISSUES

**Context:** Seychelles is a middle income island economy which is recovering strongly from a 2008 debt crisis and is transitioning to market-based economic policies. Like other microstates, it potentially faces a middle income trap, having achieved high living standards but with limited opportunities to attain high-income status, held back in part by geographical and population constraints.

**Focus:** Macroeconomic stabilization has been successful and the authorities have made significant strides toward improving financial discipline at the central government level. Discussions focused on: (i) firmly cementing macrostability through ensuring fiscal sustainability and strengthening the monetary framework; and (ii) policies to support growth and employment to raise inclusiveness.

**Program performance:** The program is on track. The authorities met all end-December quantitative performance criteria and structural benchmarks.

**Outlook and risks:** Macroeconomic performance has been broadly favorable and the authorities are on track to achieve their objective of bringing public debt down to 50 percent of GDP by 2018. The outlook is benign, but the economy will remain highly vulnerable to global developments and domestic shocks. While risks are broadly balanced, external downside risks are centered on a protracted period of slow European growth and rising commodity prices, while parastatals pose potential risks to fiscal sustainability.

**Recommendations:** Policies should aim to raise reserve buffers, improve the oversight and financial performance of parastatals, and strengthen the monetary policy framework. Structural measures should focus on raising inclusiveness through fostering private sector-led growth and capacity building.

**Data**: Data provision is broadly adequate for surveillance. Priority areas include completing compilation of quarterly GDP statistics, producing consolidated public sector accounts, strengthening external sector statistics, and compiling the international investment position.

Approved By
**David Robinson and Vivek Arora**

Discussions were held in Victoria February 20–March 5, 2013. The staff team comprised Ms. Baker (head), Mr. Roy, Mr. Culiuc (all AFR) and Ms. Mwase (SPR). Ms. Luu (OED) joined the mission for the policy discussions. The mission overlapped in the field with an MCM technical assistance mission studying steps to strengthen the monetary framework headed by Mr. Kovanen (MCM-CO). The mission met with Minister of Finance Laporte, CBS governor Abel, other senior officials, members of parliament, and representatives of the private sector and civil society.

The three-year Extended Arrangement under the Extended Fund Facility (EFF) approved December 22, 2009 (SDR 19.8 million, 182 percent of quota) was extended for one year on December 17, 2012 and access augmented by SDR 6.6 million, 60.6 percent of quota. SDR 3.3 million will be available upon completion of this review. The CBS is currently undergoing an update safeguards assessment.

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# CONTEXT AND CONJUNCTURE

**1. Seychelles is a middle-income country—the smallest in sub-Saharan Africa—and is recovering strongly from a debt crisis in 2008**. Economic and social indicators are well above those of other microstates and comparable to the most advanced small island economies.[1] Macroeconomic stability has been re-established (Box 1) and the authorities have demonstrated a high level of commitment to reform. The authorities have a strong record of implementing past Fund advice. Moreover, they are implementing a significant structural reform agenda (Annex 1) supported by extensive technical assistance from donors, including from the Fund (Informational Annex).

**Seychelles vs. other small islands, 2011**

| | **HDI** rank | **GDP per capita** PPP $ | **Public debt** percent of GDP | **Intl. reserves** mo. of imports | **Tourism** (2010) percent of GDP |
|---|---|---|---|---|---|
| Bahamas | 53 | 30,415 | 49.5 | 2.70 | 26.6 |
| Barbados | 47 | 24,989 | 75.9 | 4.16 | 26.0 |
| Fiji | 100 | 4,643 | 54.4 | 4.17 | 22.5 |
| Maldives | 109 | 8,603 | 71.0 | 2.16 | 34.3 |
| Mauritius | 77 | 14,962 | 50.9 | 4.13 | 16.4 |
| Seychelles | 52 | 25,357 | 77.4 | 2.40 | 36.6 |

Sources: UNDP, World Development Indicators, and International Financial Statistics

**2. In the span of a few years, Seychelles has made remarkable strides in creating room for private-sector led investment, transcending a model characterized by state intervention as the primary source for employment and growth.** There are currently 20 companies with state participation. In 2009, the civil service was downsized and in 2011–12 administered prices of goods provided by parastatals began to be adjusted toward cost recovery levels. To temper the impact of economic transformation, the ample social protection system was further strengthened, while increasing the use of means testing (Annex 2). Despite these measures, some working poor have struggled under economic reform, supplementing income through welfare.

# RECENT DEVELOPMENTS AND OUTLOOK

*Macroeconomic performance has been broadly favorable (Figure 1) and the outlook is benign, but the island economy will remain highly vulnerable to global developments and domestic shocks.*

**3. Growth is holding up**. The tourism industry successfully weathered weakness in traditional European arrivals (France, Italy, Great Britain), registering high growth rates in non-traditional markets (Germany, Russia, the Middle East, China). Despite the elimination of non-stop flights to Europe—part of the 2012 Air Seychelles restructuring—traditional markets rebounded in the first ten weeks of 2013 with arrivals up 19 percent over the same period of 2012. The telecom sector is seeing a boost from the deployment of the new fiber-optic cable. At the same time, activity in the construction sector has moderated following a 2006–11 surge in FDI.

**4. Inflation is abating following a spike in mid-2012 and the foreign exchange market is buoyant**. Rising food and fuel prices and an unhinging of exchange rate expectations from mid-2011 to mid-2012 led to an inflation-depreciation spiral (Country Report No. 13/24, Box 1).

[1] Seychelles is a microstate (population 88,000). The overall area is 455 km$^2$, but virtually the entire population and all tourism activities are concentrated on three main islands—mostly mountainous—totaling 203 km$^2$ (of which over 30 km$^2$ comprise a national park). This is comparable to the size of Washington, D.C. (177 km$^2$).

Monetary tightening was successful in bringing inflation below 6 percent by end-2012, with only a modest tick up in January/February 2013 following VAT rollout. Recent strong tourism receipts and lower imports of investment-related goods have pushed the exchange rate to levels last seen in 2010, further supporting disinflation.

5. **The external position has improved modestly.** Preliminary data for 2012 point to a slight reduction in the current account deficit to around 22 percent of GDP. A rapid increase in imports of consumer goods was partly offset by lower FDI-related imports and fewer services, associated with the downsizing of Air Seychelles. The current account deficit was fully financed by FDI and external borrowing, leading to a modest rise in reserves—reserve coverage ticked up to 2.6 months of imports, slightly above the level suggested by the reserve adequacy metric for small states with floating exchange rates (Box 2). However, given Seychelles' high vulnerability to shocks and data weaknesses regarding private sector external debt obligations, additional reserve coverage may be warranted to ensure adequate policy buffers. The debt restructuring which began in 2009 is nearly complete, with only one loan agreement awaiting signature. Yet, while domestic debt continued a downward path, external debt ticked up as the government assumed liabilities of Air Seychelles (about 2 percent of GDP in 2012).

6. **Despite the intra-year nominal exchange rate volatility, the real effective exchange rate is estimated to be broadly in line with fundamentals** (Annex 3). A comparative analysis of external vulnerabilities, export performance and non-price indicators also suggests that Seychelles has remained competitive relative to peers. The underlying current account is broadly in line with the equilibrium current account—the deficit was about 17 percent in 2012, one percent wider than the current account norm (See Annex 3).

**Estimated REER Misalignment [1]**

| | 2012 | 2013 | 2017 |
|---|---|---|---|
| MB | 1.0 | 5.5 | -2.1 |
| ES | -0.6 | 4.2 | -3.6 |
| ERER | -20.9 | -17.1 | -16.6 |
| **Median** | **-0.6** | **4.2** | **-3.6** |

[1] Overvaluation (+); undervaluation (-)

7. **The financial system appears sound.** The banking sector is well-capitalized, profitable and liquid (Table 5), although non-performing loans ticked at end-2011 and have remained stable at the somewhat higher level. Stress tests (Annex 4) indicate that the system is resilient to exchange rate risk, but less so to credit risk and interest-rate risk from maturity mismatches.

8. **The outlook is benign.** Prospects are favorable, but barring a major natural resource discovery,[2] growth will likely remain moderate and stable, supported by traditional sectors like tourism services and fishing as well as the telecoms/IT sector (fiber-optic cable). The resumption of a large FDI project in 2013 is unlikely to have a significant direct impact on GDP due to the high import content of construction (materials and labor). Over the medium term, growth is projected to average 3½ percent and inflation to come down to 3 percent, with some intra-period volatility as administered prices are liberalized. At current projected global commodity prices, the large current account deficit should decline over time because of improving terms of trade and the moderation of FDI flows, but will remain in double digits.

[2] Recent petroleum discoveries off East Africa and seismic tests indicate the possible presence of hydrocarbon.

9. **However, the small open island economy will remain highly vulnerable** to global developments, notably in Europe and commodity prices (Box 3), while homegrown vulnerabilities pose risks to fiscal sustainability. A protracted period of slow European growth would require farther-reaching efforts at tourism market diversification which could dilute Seychelles' high-end tourism brand and lower export receipts. A failure to strengthen oversight and financial performance of parastatals could result in additional fiscal costs, which amounted to over 5 per-cent of GDP in 2012. Future oil and mineral exploration are upside risks to the longer term.

# PROGRAM PERFORMANCE

10. **The program is on track.**

- *All end-December 2012 and continuous quantitative PCs were met, most by a comfortable margin*. The primary fiscal surplus exceeded the target by 0.3 percent of GDP. Strong business tax collection and receipts from unanticipated out-of-court settlements more than offset weakness in taxes and excises on imports, with further contributions from lower current spending, including delayed hiring. Monetary policy was loosened as expected, and the December 2012 reserve money target was met by a comfortable margin. NIR over performed because of a stronger than anticipated balance of payments and windfall revenues; the authorities are requesting modification of the end-June 2013 NIR performance criterion to adjust it upward by the full amount of the end-December overperformance, as well as the end-September and end-December 2013 NIR indicative targets.

- *Structural benchmarks were also met*. Notably, the Cabinet approved the public sector investment program (September) and the Electronic Clearing House System was activated ahead of time (August). Progress is also being made on reforms which were re-phased in the context of the sixth review. VAT was rolled out as planned on January 1, the cabinet approved an action plan to rebalance utility tariffs (end-March benchmark) and the authorities are making good progress on the drafting of the Financial Instructions and Accounting Manuals related to the Public Financial Management (PFM) Act (end-June). However, the manuals may not be ready for Cabinet approval in June due to delays in the delivery of technical assistance.

**Program performance at end-December 2012**

| | Performance Criteria [1] | Act. | Status |
|---|---|---|---|
| Net international reserves (floor) | 224 | 234 | met |
| Reserve money (ceiling) | 1920 | 1816 | met |
| Primary balance (floor) | 837 | 877 | met |
| Contracting external debt (ceiling) | 40 | 36 | met |

Sources: Seychelles authorities

[1] Adjusted Performance Criteria for net international reserves

11. **The authorities' policy plans remain unchanged and appropriate** (Country Report No. 13/24, MEFP, November 30, 2012). Consistent with the authorities' statutory commitment to reduce public debt to 50 percent of GDP by 2018,[3] the authorities aim to run a primary surplus of

[3] The end-2013 primary surplus is 0.4 percent of GDP lower than projected at the time of the sixth review because two external loans, originally programmed as publically guaranteed, have been/will be contracted directly by the central government and then on-lent to parastatals. This reclassification has no effect on the stock of public and publically guaranteed debt, but reduces the primary surplus by the amount of the onlending.

around 5 percent of GDP per year over the medium term. Such a target leaves sufficient space for needed investment expenditure,[4] while supporting declining inflation and foreign exchange market stability. The structural reform agenda (Annex 1) aims to strengthen financial discipline of the broader public sector and improve PFM. Key reform areas extending beyond the program period include adoption of program-based budgeting as a means to better align resource allocation with policy priorities, and strengthening the financial performance and oversight of public enterprises.

# REPORT ON DISCUSSIONS

*Macroeconomic stabilization was successful and the authorities have made significant strides toward improving financial discipline at the central government level. Discussions focused on: (i) firmly cementing macrostability through ensuring fiscal sustainability and improving the monetary framework; and (ii) policies to support growth and employment to raise inclusiveness.*

## A. Cementing Macroeconomic Stability

**Ensuring fiscal sustainability**

12. **Fiscal performance has improved markedly since the crisis of 2008, and the goal now is to ensure fiscal sustainability.** As mentioned, the government is targeting a primary fiscal surplus of around 5 percent of GDP per year over the medium term in order to reach its statutory goal of reducing public debt to 50 percent of GDP by 2018. However, recent events have shown parastatals are a key risk to sustainability. The cost of restructuring Air Seychelles amounted to about 6 percent of GDP in 2011–12, and the financial position of SEYPEC (the domestic fuel distribution company) is burdened by heavy losses on its oil tanker business and indirect subsidies in domestic fuel distribution.[5] Following tariff adjustments in 2012, the Public Utility Company (PUC) was able to post a small operating surplus but cannot cover its sizable capital budget and has been slow at addressing management weaknesses. Apart from parastatals, more can also be done to improve expenditure efficiency at the central government level.

13. **Staff's advice centered around the need to improve financial performance of the broader public sector while continuing to strengthen PFM, and stressed the importance of strong implementation of recent measures.** There was broad agreement that the adoption of the utility price indexation mechanism (March 2013) and continuing to raise the prices of fuel and utilities until they reach cost recovery levels would strengthen financial performance, while better monitoring and oversight of parastatals would limit the possibility of incurring large losses which would need to be borne by the central government. Moreover, the new Utility Tariff Rebalancing

[4] The authorities have a Public Sector Investment Plan (PSIP) and the African Development Bank is planning to conduct an infrastructure needs study in 2013. Under the baseline, public investment declines as a share of GDP as investment by parastatals is increasingly funded by operational income.

[5] After receiving $15 million in government resources in 2012, Air Seychelles posted a $1 million profit in 2012; with the airline in the black, a planned $10 million capital injection scheduled for 2013 has been delayed. SEYPEC is making losses of about $1 million per month on its tanker business; indirect subsidies on domestic fuel are estimated at 0.7 percent of GDP.

Plan should help reduce cross-subsidization between residential and commercial consumers, and improve resource allocation. Staff welcomed recent steps to improve monitoring, including establishment of the Public Enterprising Monitoring Commission (PEMC) but cautioned against the proliferation of oversight mechanisms and entities.[6] On PFM, staff noted that while important measures have recently been adopted—the PFM Act, new chart of accounts, a move toward program-based budgeting—their effectiveness lies in rigorous implementation.

14. **The authorities broadly agreed with the staff's recommendations, but noted that comprehensive reform takes time.** Efforts are underway in parallel to strengthen the capacity of PEMC staff to produce consolidated (i.e., central government plus public enterprises) public sector fiscal reports and to improve parastatals' compliance with reporting requirements. Work is also advancing toward publication of financial instructions and accounting manuals which will operationalize many provisions of the PFM Act. Central government data are being compiled using the new chart of accounts, even as further refinements to the chart are being made, and work is advancing toward the piloting of program performance based budgeting for the ministries of education and natural resources in 2014. Looking ahead, the new Public Sector Investment Program (PSIP) will eventually feed into a medium-term budget framework. The authorities appreciated the strong TA support they had received from donors, and reiterated their commitment to seeing the reforms through, despite some staffing constraints.

**Strengthening the monetary framework**

15. **Within the current monetary framework, the reserve money target poses significant challenges to anchoring inflation expectations** (Annex 5). Staff noted that the repayment of domestic debt, a preference for foreign financing[7] and shallow domestic financial markets have resulted in significant structural rupee liquidity in the banking system. High sterilization costs have deterred the Central Bank of Seychelles (CBS) from issuing monetary instruments in order to avoid losses,[8] leading to occasional massive build ups of excess liquidity (21 percent of the money base at end February), which undermine the monetary anchor and retards the monetary transmission mechanism. The CBS noted that rather than lend, domestic banks prefer to wait until the end of the quarter when they know the CBS must issue risk-free instruments to mop up liquidity to meet the reserve money target. As a result, credit to the private sector grew by only 0.9 percent in 2012 and interest rates have become very volatile. Moreover, without a clear anchor, market participants continue to look to the exchange rate to guide their views on future inflation.

16. **A further increase in international reserves would provide a stronger buffer against shocks.** Import coverage of reserves continues to hover just below three months (the standard benchmark), despite a steady increase in official reserves since end-2008, and official debt service

[6] The Société Seychellois d'Investissement (SSI) is a state-owned company originally created to manage the government's minority share in the Indian Ocean Tuna joint venture. In January 2013, it took over the management of the government's stake in 10 strategic parastatals. SSI operates in parallel to PEMC.

[7] In addition to the higher cost of domestic funds over concessional financing, the use of external financing for projects reduces near-term pressure on the balance of payments and reserves due to the high import content.

[8] Sterilization costs related to excess liquidity are estimated at 0.7–1.4 percent of GDP, implying potential central bank losses and the need to go to parliament to request recapitalization.

is set to rise following the debt restructuring. This, together with balance of payments vulnerabilities and exposure to external shocks, provides a strong case for strengthening buffers, including by increasing reserve coverage (Box 2). Staff and CBS agreed that reserves build-up is best pursued through opportunistic purchases of forex in periods when central bank interaction is not likely to have an impact on the exchange rate.

**17. The authorities are beginning to take steps to strengthen the monetary framework ahead of a move to a flexible form of inflation targeting.** In line with recommendations of the recent MCM technical assistance mission, as a first step within the reserve money framework, the authorities will coordinate closely with the Ministry of Finance to durably tie up a portion of the liquidity overhang, including by exploring the feasibility of issuing longer dated T-bonds.[9] This will open space to establish a money market interest rate, supported by short-term CBS instruments. Better forecasting tools will strengthen liquidity control and the role of the policy interest rate, allowing the CBS to develop a forward-looking inflation forecasting model. A more efficient monetary framework will also contribute to easing access to and lowering costs of bank credit to the private sector.

**18. It was agreed that the changes in train alone may not be sufficient to generate higher growth in credit to the economy.** Staff acknowledged that other factors are also contributing to low access to credit (see paragraph 22), but pointed out that the current reserve money framework is exacerbating the problem by providing disincentives to lending.

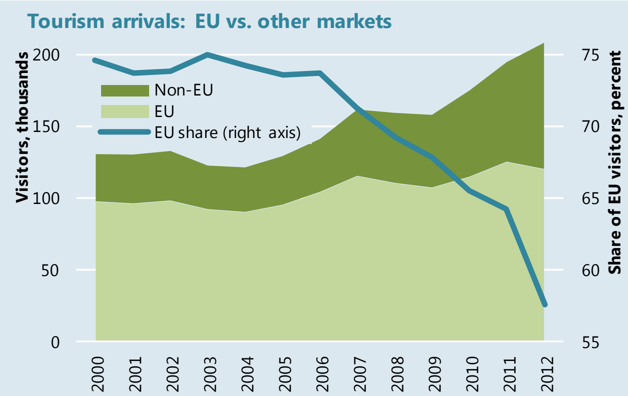
## B. Growth, Employment and Inclusion

*Like other microstates, Seychelles potentially faces a middle income trap as geographical and population constraints limit opportunities for growth and domestic income generation. Growth will likely be driven by traditional labor-intensive sectors, supported by a continued inflow of foreign labor, and improvements in the business climate. A key aspect of raising inclusiveness will be capacity development of domestic labor and ensuring that the social welfare system does not deter labor market participation.*

### Growth drivers and private sector participation

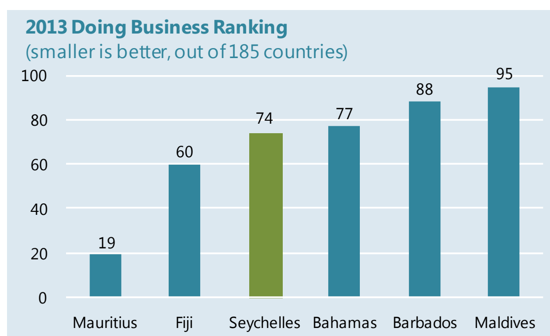
**19. Tourism has been the main driver of growth, but there is a tension with the number of tourists the islands can absorb.** Despite the challenging global environment, tourist arrivals have grown strongly, with diversification toward non-traditional markets more than offsetting stalling European arrivals. Indeed, an analysis of global tourism indicates that Seychelles has outperformed nearly all small islands after controlling for standard gravity model variables (Annex 6). However, high arrivals growth rates may prove unsustainable in the long term if the country wants to maintain its image as a luxury getaway with a pristine environment, and the industry remains vulnerable to prolonged downturns in its main European markets.

[9] Such issuance could take place only after June in order to incorporate the findings of a TA mission on debt management scheduled for May.


**20. There was broad agreement that tourism services would remain a key driver of growth, with upside potential for financial services.** While land for construction of new hotels on the three main islands is reaching its limit, development of smaller, more remote islands holds potential for increasing the number of hotel beds. In addition, tourism-related services—which are limited relative to peers—is a dependable area for growth, through product diversification and increased sector linkages with local small and medium enterprises (SMEs). In other areas, improved connectivity via the underwater cable has renewed interest in financial services. The stock market was established in late 2012, and is currently in discussions with potential listers,[10] while the off-shore sector is developing steadily. However, scarcity of supporting local professional services (lawyers, but also accountants, auditors) may limit growth. It will also be important to advance transparency of legal persons and arrangements in line with international standards on AML/CFT and tax cooperation to ensure integrity of the off-shore sector.

**21. The authorities aim to support broader-based growth through creating an environment conducive to private sector participation in the economy.** They noted that reform efforts are paying off—Seychelles was ranked 74th in the 2013 Doing Business Indicators—and further reform steps have been taken to simplify business registration. They continue to work closely with the World Bank—reforms focus on creation of an online platform for business interaction with government, modernization of the Companies Act in line with international best practice, introduction of a modern insolvency framework, and expediting the process through establishing a commercial division within the Supreme Court and a mediation framework.[11] However, under-staffing relative to the reform load at key agencies, such as the Attorney General's office, has led to delays in enacting certain pieces of legislation.




[10] The stock market has three boards: a main board, a venture capital board and a board for SMEs. The company plans to have 10 listings by end-2013, with a medium-term strategy of providing a pan-African trading platform.

[11] A Sustainability and Competitiveness Development Policy Loan (DPL1) was approved September 2012. A follow up operation is under discussion with the World Bank.

**22. While recognizing the progress to date, discussions focused on bottlenecks in infrastructure and the cost of and access to credit**.

- *Infrastructure*. Gaps are significant in water and electricity distribution, and the road network on the main island is overburdened. Staff welcomed passage of the PSIP comprising investment needs identified by ministries, and suggested that this be complemented by the Infrastructure Plan being developed with the assistance of the African Development Bank (AfDB) planned for mid-2013. It will be important that the Infrastructure Plan be comprehensive in nature; identify priorities; and ensure development is financed in a viable way, supported by strong PFM. Together these documents form a key input to moving towards a medium-term fiscal framework.[12]

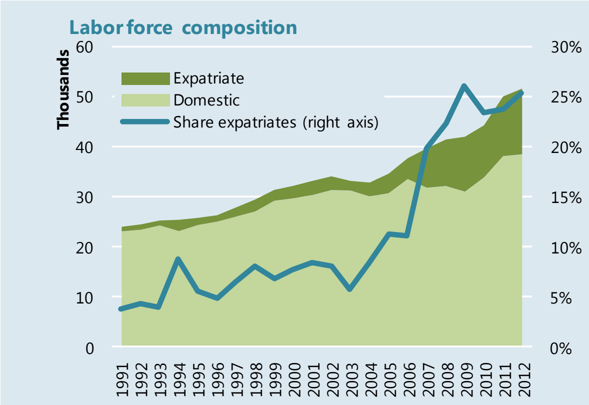
- *Credit.* There was broad agreement that bottlenecks in the area of credit were a challenge. The banking system shares characteristics of both LICs and other small states (Annex 7), namely high interest rates and interest rate spreads; lack of economies of scale; maturity mismatch stemming from a lack of medium- and long-term bank funding; low capacity of firms, especially SMEs, to develop a business plan; and given the short-term nature of lending, few bankable projects. The authorities noted they are working on a dual approach, increasing onlending to the Development Bank of Seychelles[13] while collaborating with the AfDB and the World Bank on financial sector issues such as housing finance development. The new law regulating financial leasing activities will broaden the availability of credit to small businesses. The transition towards forward-looking risk-based supervision should help reduce the cost of credit, while the recent establishment of the credit information bureau works toward raising access.

**Labor and inclusiveness: capacity building for higher value added jobs**

**23. Tourism and other growth sectors in Seychelles are labor intensive; full employment of domestic labor implies that growth will need to be supported by foreign labor.** Unlike most African MICs, job offerings outpace job seekers in every labor category. Unemployment is low (3–5 percent) and structural in nature, reflecting a skills mismatch (Annex 8). As the economy has grown, local labor supply has remained broadly unchanged, while foreign labor has increased from around one-tenth to a quarter of the labor force (one-third of private sector employment), mostly in high-growth sectors. Concerns with the rapid increase in expatriate labor prompted changes in the regulations regarding issuance of work permits. Staff underscored the importance of regulatory certainty regarding the ability of businesses to hire expatriate workers to fill jobs which they are unable to fill locally, and encouraged open dialogue between stakeholders.

[12] IMF technical assistance in developing a medium-term fiscal framework is slated to begin in FY14.

[13] DBS was established in 1977 to finance development projects, with a focus on SMEs. Onlending in 2013–14 is projected to amount to $10.2 million, financed by loans from the European Investment Bank and India.





**24. Staff welcomed the authorities' focus on capacity building to reduce skills mismatch in higher value-added jobs.** Expatriate labor is concentrated in professional services, managerial positions and productive sectors (tourism, construction). While recognizing the long-term nature of the solution, the authorities pointed to recent progress, such as the opening of the University of Seychelles in 2009, the transfer of management of the Seychelles Tourism Academy to the Seychelles Tourism Board, and the continued use of government sponsored training programs.[14] Work is also beginning to develop a medium-term strategy for education (financed by EU budget support) and a National Human Resources Development Strategy for 2015 (supported by the AfDB). They are currently targeting middle management positions, with a goal of reaching 50 percent of positions held by Seychellois (currently 20 percent). In the meantime, social protection was strengthened in 2009 to mitigate the impact of economic transformation on the vulnerable.

**25. Staff encouraged the authorities to continue efforts in train, including an overhaul of the Employment Act, while ensuring that social protection supports labor market participation.** The authorities are reviewing the Employment Act with the assistance of the ILO, with a view to increasing labor market flexibility and clarifying key legal terms (i.e., "equal pay", "harassment", "non-discrimination"). However, views of the public and private sectors on the impact of social protection on labor participation varied. Staff inquired about the results of previous studies[15] that had concluded that regulations regarding the hiring of retirees, relatively high pension replacement rates and ample social welfare were a disincentive to labor force participation and/or raised the reservation wage. Most respondents noted that labor issues were complicated, and while there may be scope to align incentives, the already high participation rate means that such regulatory changes may not yield sizeable benefits. That said, the government has taken steps to encourage welfare recipients to return to work, is increasing use of means testing for home health care providers and is strengthening data management and tracking through linking ministry/agency databases to cross check income and benefit information.

[14] Seychelles has two government-supported training programs, the Skills Acquisition Program and the Skills Development Program. See Annex 8.

[15] See for example, World Bank Public Expenditure Review II (2011),

# STAFF APPRAISAL

26. **The economy has recovered strongly from a debt and currency crisis in 2008, and the high-level commitment to reform demonstrated by authorities has supported macroeconomic stability.** The outlook is benign, with moderate growth driven by traditional sectors such as tourism and fishing. Improvement in the business climate may boost private sector participation in economic activity, but like other microstates Seychelles potentially faces a middle income trap.

27. **Given the unsettled global environment and Seychelles' high vulnerability, the authorities should continue to build buffers.** External risks are broadly balanced but remain elevated, while parastatals pose potential risks to fiscal sustainability. The authorities' intention to sustain a primary surplus over the medium term is appropriate, with the large revenue base supporting achievement of their 2018 debt objective while providing space for needed investment expenditure. Debt restructuring is nearly complete, and caution should be exercised when contracting new debt, including for onlending purposes. Foreign exchange reserves have increased and are slightly above the levels implied by reserve adequacy metrics for small states, but efforts should be made to increase reserve coverage when foreign exchange market conditions permit.

28. **The floating exchange rate has facilitated macroeconomic adjustment.** The Seychellois rupee is broadly in line with medium-term fundamentals, and tourism remains competitive among peers. Exchange market intervention should aim at smoothing market disruptions, with foreign exchange purchases aimed at reserve accumulation clearly communicated to the market.

29. **The authorities have made continuous progress under the EFF-supported program, and the program is on track.** All end-December quantitative performance criteria and structural benchmarks were met.

30. **The priority now is to cement macroeconomic stability through ensuring fiscal sustainability and improving the monetary framework.** Staff welcomes progress made towards improving financial discipline at the central government level, and the strengthening of the efficiency of the tax system through the introduction of the VAT on January 1, 2013. Going forward, improving financial performance of the broader public sector is key to ensuring fiscal sustainability. The establishment of the Public Enterprise Monitoring Commission and efforts to produce consolidated fiscal accounts are welcome, but must be accompanied by strict compliance by parastatals with reporting requirements. The effectiveness of the PFM Act will depend on rigorous implementation of recently adopted measures. On monetary policy, durably removing excess liquidity is the first step toward strengthening the monetary transmission mechanism and will require a transparent and credible mechanism to cover the fiscal cost of sterilization. At the same time, steps should be taken to improve liquidity forecasting and develop a forward-looking inflation forecasting model.

**31. The government is implementing an appropriately broad structural reform agenda that will be key to facilitating a deepening of markets more capable of sustaining growth.** Ongoing efforts to modernize the Companies Act and insolvency framework will complement measures already taken to simplify business registration. Like many microstates, bottlenecks are also present in infrastructure and access to credit. Passage of the public sector investment plan is welcome, and should be prioritized and financed in a viable way. It is important to bring the tariffs and prices of select parastatals (in particular the Public Utility Corporation) to full cost recovery in a useful timeframe, which will free up central government resources for other priority investments.

**32. Reducing the cost of, and increasing access to, credit will be important for private sector development.** While a substantial increase in the provision of longer-term credit would require capital market development beyond the current model narrowly centered on bank intermediation, improved guidance of market expectations through a stronger monetary policy framework will facilitate the banking system's capacity to mobilize and allocate financial resources.

**33. Key aspects of raising inclusiveness are capacity development and ensuring that the social welfare system supports labor market participation.** With the economy at full employment, foreign labor will continue to play an important role in supporting growth, and regulatory certainty regarding the employment of expatriates is necessary to promote private investment. Development of a medium-term strategy for education and a National Human Resources Development Strategy should help identify avenues for reducing skills mismatch, allowing domestic labor to access higher value-added jobs. Increased reliance on means–tested social programs should also contribute to higher domestic labor force participation.

**34. Data provision is broadly adequate for surveillance.** Seychelles participates in the General Data Dissemination System (GDDS) and is working toward participation in the Special Data Dissemination Standard (SDDS). Priority areas include completing compilation of quarterly GDP statistics, producing consolidated public sector accounts, strengthening external sector statistics by improving its coverage, and compiling the international investment position.

**35. It is recommended that the next Article IV consultation with Seychelles be held in accordance with the decision on Article IV Consultation Cycles adopted on September 28, 2010, as amended.** Staff recommends completion of the seventh review under the Extended Arrangement and the associated purchase in an amount equivalent to SDR 3.30 million. Staff also recommends approval of the authorities' request for modification of the end-June 2013 performance criterion on net international reserves.

### Box 1. The 2008 Crisis and Macroeconomic Stabilization

**Economic policy during 1977–2004 was socialist in orientation,** characterized by multiple controls (over prices, trade and foreign exchange) and a prominent role for parastatals. Limited economic liberalization in the 1990s reduced the state's role in some sectors—notably telecommunications and tourism—although debt-funded development spending continued at a high level.

**Expansionary fiscal and monetary policies were unsustainable and led to a debt crisis.** By 2007, the overall fiscal deficit had reached 9.8 percent of GDP; total public debt stood at 146 percent of GDP; and. gross official reserves were depleted to $9.8 million, or 0.1 month of imports. External arrears of $160 million were accumulated and in July and October 2008 the government of Seychelles failed to make payments on private foreign debt—S&P downgraded Seychelles to 'selective default'.

**The debt crisis culminated in a balance of payments and currency crisis.** Several step adjustments in the value of the rupee against the dollar in 2006–07, exchange restrictions and credit rationing had not stemmed the balance of payment crisis, compounded by the 2008 food and fuel price shocks. The parallel market premium over the official USD-pegged rate reached 55 percent.

**An economic reform program was launched in November 2008 supported by a Stand-by Arrangement**. The authorities removed exchange restrictions, floated the currency, liberalized interest rates, introduced a reserve money targeting framework, and increased reserve requirements. The rupee/dollar exchange rate more than doubled, temporarily overshooting the parallel rate, leading 12-month inflation to peak at 63 percent in December 2008. The exchange rate appreciated over the subsequent two quarters, bringing down prices (negative 12-month inflation throughout 2010) and short-term money market interest rates.

**Macroeconomic stabilization was supported by strong and sustained fiscal adjustment.** The heavily frontloaded fiscal tightening (primary surpluses of 14.3 and 8.7 percent of GDP in 2009 and 2010, respectively) was achieved through deep cuts in public sector employment, only modest increases in nominal wages, and the removal of many product subsidies. Retrenched public sector workers were absorbed by the private sector, albeit at lower real wages. An expanded and more targeted social safety net was implemented to mitigate the social impact of the reforms.

**Tax reforms and improvements in revenue administration and expenditure management buttressed the credibility of the fiscal adjustment.** The tax base was broadened by increasing the coverage of GST and rolling back tax exemptions that had long compensated foreign investors for the overvalued currency. The GST rate was then increased in steps and replaced by the VAT in 2013. The Ministry of Finance has built capacity internally to strengthen budget processes. Key achievements include the conduct of mid-year formal expenditure reviews, the adoption of new procurement and transparent tendering processes, and the establishment of a macroeconomic and revenue forecasting unit (prior to 2008 the budget did not report revenue numbers, nor a measure of the fiscal balance).

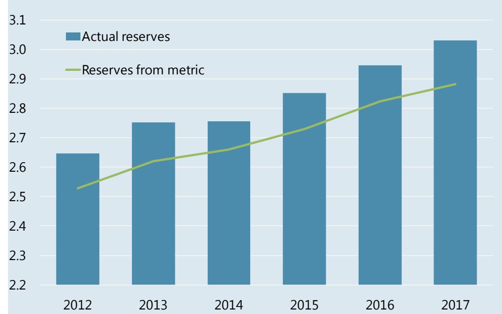
**The turnaround in economic policies facilitated debt reduction**. In early 2009 Paris Club creditors provided a 45 percent debt write-off in nominal terms, very exceptional for a middle-income country. Despite a fragmented private creditor base, Seychelles' debt exchange was successful (50 percent haircut). Thereafter, the authorities adopted an overarching macroeconomic policy objective of reducing public debt to 50 percent of GDP by 2018. The debt restructuring process started in 2009 is nearly complete, with one agreement awaiting signature. While public debt is on trend to meet the objective, debt dynamics demonstrate an elevated sensitivity to shocks representative of small island economies.

## Box 2. Policy Buffers—Reserve Adequacy and the Debt Ceiling

This box assesses two key policy buffers in Seychelles, namely reserve adequacy and the debt ceiling. While international reserves provide a direct defense against shocks, an appropriate debt ceiling aims to provide room for policy maneuver in the event of shocks. Reserve coverage and the authorities' 2018 debt objective appear adequate, but there is a case for building further buffers given Seychelles' high vulnerability to shocks.

**Reserve Adequacy. While panel estimates suggest broadly appropriate coverage, Seychelles reserves could be further increased to ensure adequate policy buffers.**[1] The risk-weighted reserve metric for flexible currency regimes comprises 40 percent of short-term debt on remaining maturity basis, 10 percent exports of goods and services and 30 percent of broad money. Reserves have increased steadily from 0.7 months of prospective imports in 2008 during the debt crisis to 2.6 months in 2012, and are projected to remain modestly above the metric over the medium term. However, given Seychelles' high vulnerability and data weaknesses regarding private sector external debt obligations, additional reserve coverage may be warranted to ensure adequate policy buffers.

**Reserves against risk-weighted metric**




Source: IMF staff calculations

**The Authorities' Debt Ceiling. Staff analysis indicates that the authorities' debt target is in line with the results of standard models of debt intolerance, but still somewhat above peers—a further reduction may be warranted over the long-term.**[2] The approaches include (i) a cross country comparison of debt ratios; (ii) an examination of debt intolerance,[3] (iii) the maximum debt level consistent with intertemporal solvency under various assumptions for the primary balance, real growth and interest rate following IMF (2003);[4] and (iv) sovereign ratings.

**While individual approaches are inconclusive, taken together they suggest that a reasonable and feasible public debt ceiling for Seychelles over the longer-term could be in the order of 35–50 percent.** The first three approaches support the current target. Cross country comparison of small states with floating exchange rate regimes suggests that the average public debt was 52 percent in 1995-2011. Public debt thresholds of debt intolerance for Seychelles range from 30-75 percent. Staff sensitivity analysis reveals that 49 percent of GDP can be sustained under reasonable assumptions about Seychelles' long-run primary balance and discount factor. However, in comparison to other countries sharing Seychelles' B rating, Seychelles has a substantially higher debt-to-GDP ratio (i.e., the median country with a Fitch sovereign rating of B has debt-to-GDP ratio of 30 percent). Therefore, a lower debt ceiling may be needed not only to warrant a higher rating but also to remain in its current grade given the wide gap relative to peers.

**Benchmark public debt-to-GDP ratio: sensitivity to primary surplus and interest-growth rate differential**

| Primary Surplus (percent of GDP) | Discount Factor (r-g): 0.20 | 0.61 | 1.79 | 2.20 | 2.49 | 4.60 |
|---|---|---|---|---|---|---|
| 0.14 | 70 | 23 | 8 | 6 | 6 | 3 |
| 0.39 | 195 | 64 | 22 | 18 | 16 | 8 |
| 1.07 | 535 | 175 | 60 | **49** | 43 | 23 |
| 2.37 | 1185 | 389 | 132 | 108 | 95 | 52 |
| 3.28 | 1640 | 538 | 183 | 149 | 132 | 71 |

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[1]Based on Mwase, 2012 "How much should I hold? Reserve Adequacy in Emerging Markets and Small Islands" IMF Working paper WP/ 12/205.

[2] See Mwase, forthcoming, "Debt limits in small states" IMF Working Paper

[3]See Reinhart C., K. Rogoff, and M. Savastano (2003), "Debt Intolerance", Brookings Papers on Economic Activity, 2003 (1), 1-74.

[4] IMF (2003), World Economic Outlook, "Chapter 3. Public Debt in Emerging Markets: Is it too high?"

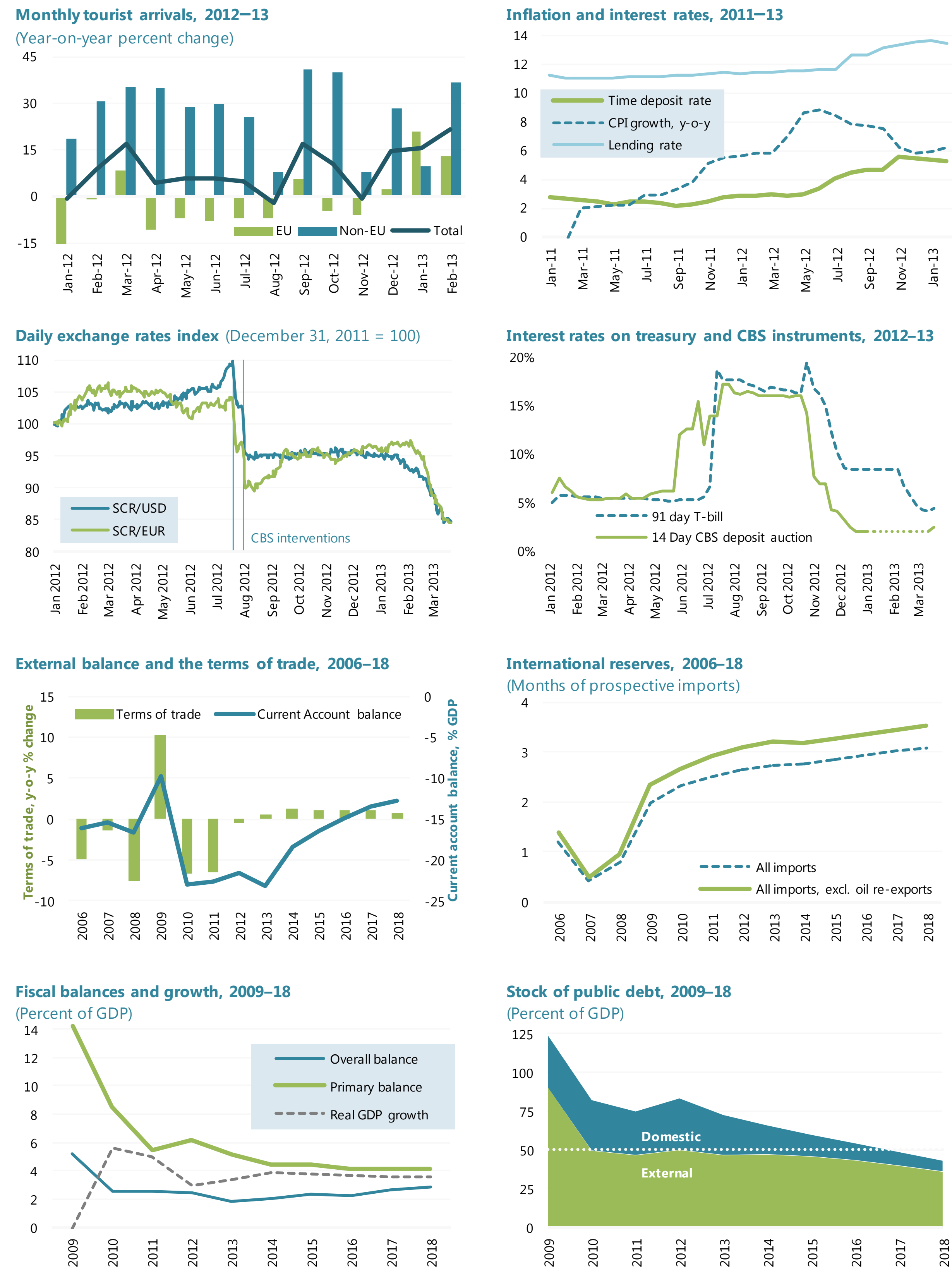
**Box 3. Risk Assessment Matrix**

| Source of threat | Likelihood | Severity | Impact | Policy response |
|---|---|---|---|---|
| | | *Domestic risks* | | |
| Financial distress at a major parastatals | M | M | Plummeting fiscal balance, a spike in public debt and/or a squeezing of priority expenditure areas as the government bails out the parastatal. | Prevent by actively auditing largest parastatals. Ensure bailout accompanied by addressing the root cause of the problems (tariff structure, mismanagement, etc.) |
| Erratic monetary policy | L-M | M-H | Unwarranted large policy swings may undermine Central Bank's credibility and result in further dollarization, accompanied by inflation and/or loss of reserves. | Minimize policy swings by adopting a clear and predictable monetary policy framework. |
| Over-borrowing for development projects | L | M-H | A rapid increase in external debt contracted by parastatals could nullify the fiscal consolidation efforts of the central government. Accumulation of implicit claims against the stock of reserves could trigger a run on the currency and an inflationary spike. | Prevent by auditing all capital investment project, especially foreign-financed. |
| | | *External risks* | | |
| Protracted period of slow European growth | M | H | A drop in tourism receipts from Europe would depress growth, deteriorate the balance of payments. An attempt to defend the exchange rate could deplete CBS's modest international reserves. | Accelerate tourism diversification by negotiating air links with growth markets. Ensure exchange rate adapts to deteriorated external conditions, while curbing second-round inflationary effects. |
| Oil price shock | L | M | Significant impact on current account deficit, inflation, exchange rate and – if PUC tariffs are not fully adjusted – an increase in implicit fiscal liabilities. | Maintain full pass-through onto domestic prices to contain fiscal impact and parastatal losses, while minimizing impact on the poor through means-tested subsidies. |
| Natural disaster | L | M-H | A strong cyclone or tsunami could inflict widespread damage to the fishing and tourism industries and damage key public infrastructure (deep sea port, airport). | Continue to build policy buffers for emergency response by increasing international reserves coverage. Explore options for contracting natural-disaster insurance. |

*"L" – Low; "M" – Medium; "H" – High.*

*The matrix shows events that could materially alter the baseline path (the scenario most likely to materialize in the view of IMF staff). The relative likelihood of risks is the staff's subjective assessment of the risks surrounding the baseline.*

## Figure 1. Seychelles: Macroeconomic Developments and Projections



## Table 1. Seychelles: Selected Economic and Financial Indicators, 2010–18

| | 2010 | 2011 | 2012 | | 2013 | | 2014 | 2015 | 2016 | 2017 | 2018 |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | | | Prog. | Est. | Prog. | Proj. | Proj. | Proj. | Proj. | Proj. | Proj. |
| National income and prices | | | (Percentage change, unless otherwise indicated) | | | | | | | | |
| Nominal GDP (millions of Seychelles rupees) | 11,746 | 13,119 | 14,159 | 14,145 | 15,055 | 15,292 | 16,461 | 17,636 | 18,866 | 20,171 | 21,538 |
| Real GDP | 5.6 | 5.0 | 2.7 | 2.9 | 3.0 | 3.3 | 3.9 | 3.8 | 3.7 | 3.6 | 3.5 |
| CPI (annual average) | -2.4 | 2.6 | 7.2 | 7.1 | 5.1 | 4.5 | 3.4 | 3.0 | 3.0 | 3.0 | 3.0 |
| CPI (end-of-period) | 0.4 | 5.5 | 6.7 | 5.8 | 4.1 | 4.3 | 3.1 | 3.0 | 3.0 | 3.0 | 3.0 |
| GDP deflator average | -3.6 | 6.4 | 5.1 | 4.8 | 3.2 | 4.6 | 3.6 | 3.2 | 3.2 | 3.2 | 3.2 |
| Money and credit | | | (Percentage change, unless otherwise indicated) | | | | | | | | |
| Credit to the economy | 21.4 | 6.2 | 1.7 | 2.5 | 13.2 | 13.0 | ... | ... | ... | ... | ... |
| Broad money | 13.5 | 4.5 | -2.7 | -2.3 | 1.6 | 0.1 | ... | ... | ... | ... | ... |
| Reserve money | 34.7 | -2.7 | 13.0 | 6.9 | 6.3 | 12.3 | ... | ... | ... | ... | ... |
| Velocity (GDP/broad money) | 1.6 | 1.7 | 1.9 | 1.9 | 2.0 | 2.1 | ... | ... | ... | ... | ... |
| Money multiplier (broad money/reserve money) | 4.2 | 4.5 | 3.9 | 4.1 | 3.7 | 3.6 | ... | ... | ... | ... | ... |
| Savings-Investment balance | | | | (Percent of GDP) | | | | | | | |
| External savings | 23.0 | 22.7 | 22.4 | 21.7 | 18.9 | 23.2 | 18.4 | 16.4 | 14.9 | 13.4 | 12.8 |
| Gross national savings | 13.6 | 12.4 | 16.4 | 17.3 | 16.0 | 15.1 | 15.5 | 14.4 | 14.5 | 16.0 | 16.5 |
| *Of which*: government savings | 7.8 | 10.6 | 13.6 | 14.3 | 12.0 | 12.1 | 11.0 | 11.0 | 10.7 | 10.9 | 11.0 |
| Gross investment | 36.6 | 35.1 | 38.8 | 39.0 | 34.9 | 38.2 | 33.8 | 30.8 | 29.5 | 29.5 | 29.3 |
| *Of which*: government investment | 8.6 | 8.1 | 11.8 | 12.0 | 9.5 | 9.2 | 7.8 | 7.8 | 7.5 | 8.0 | 8.3 |
| Government budget | | | | | | | | | | | |
| Total revenue, excluding grants | 34.1 | 35.8 | 37.2 | 37.6 | 36.9 | 36.4 | 35.6 | 35.6 | 35.5 | 35.5 | 35.5 |
| Expenditure and net lending | 32.5 | 35.7 | 41.0 | 40.2 | 39.3 | 38.5 | 36.0 | 35.2 | 34.7 | 34.2 | 33.9 |
| Current expenditure | 27.2 | 27.6 | 29.6 | 28.8 | 29.5 | 28.8 | 27.3 | 26.8 | 26.5 | 26.1 | 25.9 |
| Capital expenditure and net lending | 5.3 | 8.1 | 11.3 | 11.4 | 9.8 | 9.8 | 8.7 | 8.4 | 8.2 | 8.1 | 8.0 |
| Overall balance, including grants | 2.5 | 2.5 | 1.8 | 2.4 | 1.8 | 1.8 | 2.0 | 2.3 | 2.2 | 2.6 | 2.8 |
| Primary balance | 8.6 | 5.4 | 5.9 | 6.2 | 5.6 | 5.1 | 4.4 | 4.4 | 4.1 | 4.1 | 4.1 |
| Total public debt | 81.6 | 74.3 | 78.1 | 77.3 | 73.6 | 72.0 | 65.3 | 59.2 | 53.7 | 48.0 | 42.4 |
| Domestic [1] | 32.5 | 28.0 | 27.4 | 27.7 | 21.6 | 25.7 | 18.6 | 13.8 | 10.8 | 8.6 | 6.8 |
| External | 49.1 | 46.2 | 50.7 | 49.6 | 52.0 | 46.3 | 46.7 | 45.4 | 42.9 | 39.5 | 35.7 |
| External sector | | | (Percent of GDP, unless otherwise indicated) | | | | | | | | |
| Current account balance including official transfers | -23.0 | -22.7 | -22.4 | -21.7 | -18.9 | -23.2 | -18.4 | -16.4 | -14.9 | -13.4 | -12.8 |
| Total stock of arrears (millions of U.S. dollars) | 30.3 | 9.0 | ... | 2.7 | ... | ... | ... | ... | ... | ... | ... |
| Total public external debt outstanding (millions of U.S. dollars) | 478 | 490 | 520 | 512 | 566 | 558 | 597 | 614 | 614 | 598 | 572 |
| (percent of GDP) | 49.1 | 46.2 | 50.7 | 49.6 | 52.0 | 46.3 | 46.7 | 45.4 | 42.9 | 39.5 | 35.7 |
| Terms of trade (= - deterioration) | -6.7 | -6.4 | 0.4 | -0.4 | 0.5 | 0.6 | 1.2 | 1.2 | 1.0 | 1.1 | 0.8 |
| Real effective exchange rate (average, percent change) | 4.4 | -7.4 | ... | ... | ... | ... | ... | ... | ... | ... | ... |
| Gross official reserves (end of year, millions of U.S. dollars) | 254 | 277 | 296 | 305 | 306 | 317 | 326 | 346 | 368 | 390 | 414 |
| Months of imports, c.i.f. | 2.3 | 2.5 | 2.7 | 2.6 | 2.7 | 2.7 | 2.7 | 2.8 | 2.9 | 3.0 | 3.1 |
| Exchange rate | | | | | | | | | | | |
| Seychelles rupees per US$1 (end of period) | 12.1 | 13.7 | ... | 13.0 | ... | ... | ... | ... | ... | ... | ... |
| Seychelles rupees per US$1 (period average) | 12.1 | 12.4 | ... | 13.7 | ... | ... | ... | ... | ... | ... | ... |

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

[1] Excludes debt issued in 2012 for monetary purposes (5.4 percent of GDP), as proceeds are kept in a blocked account with the Central Bank.

## Table 2. Seychelles: Balance of Payments, 2010–18
## (millions of U.S. dollars)

| | 2010 | 2011 | 2012 | | 2013 | | 2014 | 2015 | 2016 | 2017 | 2018 |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | | Est. | Prog. | Est. | Prog. | Proj. | Proj. | Proj. | Proj. | Proj. | Proj. |
| Current account | -223 | -240 | -230 | -224 | -206 | -279 | -235 | -222 | -214 | -203 | -205 |
| (percent of GDP) | -23.0 | -22.7 | -22.4 | -21.7 | -18.9 | -23.2 | -18.4 | -16.4 | -14.9 | -13.4 | -12.8 |
| Balance of goods and services | -202 | -225 | -263 | -231 | -211 | -251 | -199 | -183 | -166 | -160 | -158 |
| Exports of goods | 400 | 465 | 499 | 497 | 517 | 505 | 516 | 529 | 542 | 556 | 571 |
| *Of which:* oil re-exports | 158 | 182 | 200 | 200 | 204 | 196 | 191 | 189 | 191 | 195 | 200 |
| *Of which:* tuna exports | 210 | 242 | 249 | 249 | 259 | 269 | 284 | 297 | 306 | 315 | 323 |
| Imports of goods | -762 | -882 | -918 | -960 | -892 | -976 | -961 | -971 | -989 | -1,009 | -1,034 |
| *Of which:* oil imports | -219 | -244 | -269 | -300 | -284 | -307 | -307 | -310 | -318 | -326 | -336 |
| FDI-related | -151 | -141 | -115 | -91 | -102 | -120 | -95 | -111 | -110 | -108 | -107 |
| grants- and loans-related | -59 | -85 | -90 | -106 | -87 | -97 | -93 | -76 | -65 | -57 | -49 |
| other | -333 | -412 | -445 | -462 | -420 | -452 | -466 | -474 | -496 | -518 | -542 |
| Exports of services | 592 | 617 | 567 | 592 | 585 | 632 | 670 | 711 | 754 | 788 | 823 |
| *Of which:* tourism earnings | 274 | 291 | 305 | 310 | 317 | 331 | 352 | 373 | 395 | 413 | 432 |
| Imports of services | -432 | -425 | -411 | -361 | -422 | -412 | -425 | -451 | -472 | -495 | -519 |
| Income, net | -47 | -51 | -35 | -46 | -35 | -48 | -48 | -52 | -52 | -50 | -49 |
| *Of which:* interest due [1] | -24 | -17 | -13 | -19 | -16 | -22 | -22 | -23 | -24 | -23 | -22 |
| transfers of profits and dividends | -6 | -19 | -6 | -12 | -6 | -12 | -13 | -13 | -13 | -14 | -14 |
| Current transfers, net | 25 | 36 | 68 | 54 | 40 | 20 | 12 | 13 | 4 | 7 | 2 |
| *Of which:* general government, net | 26 | 29 | 52 | 55 | 18 | 20 | 17 | 15 | 11 | 11 | 11 |
| Capital and financial account | 476 | 191 | 224 | 210 | 214 | 289 | 247 | 245 | 239 | 231 | 236 |
| Capital account | 275 | 61 | 62 | 61 | 36 | 40 | 34 | 31 | 25 | 20 | 20 |
| *Of which:* debt forgiveness | 267 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Financial account | 201 | 131 | 162 | 149 | 178 | 249 | 213 | 215 | 214 | 211 | 216 |
| Direct investment, net | 195 | 180 | 147 | 145 | 130 | 174 | 130 | 142 | 140 | 138 | 136 |
| Portfolio investment, net [1] | 10 | -30 | 11 | -32 | 15 | 33 | 31 | 43 | 41 | 54 | 66 |
| Other investment, net | -3 | -19 | 3 | 37 | 34 | 42 | 53 | 30 | 34 | 20 | 14 |
| Government and government-guaranteed | 19 | 10 | 8 | 12 | 21 | 32 | 40 | 13 | -2 | -17 | -24 |
| Disbursements | 48 | 12 | 19 | 21 | 37 | 48 | 58 | 38 | 37 | 33 | 23 |
| Project loans | 20 | 12 | 12 | 14 | 20 | 31 | 41 | 38 | 37 | 33 | 23 |
| Program loans | 28 | 0 | 7 | 7 | 17 | 17 | 17 | 0 | 0 | 0 | 0 |
| Amortization | -46 | -10 | -11 | -9 | -16 | -16 | -18 | -25 | -39 | -49 | -47 |
| Private sector [2] | -22 | -53 | 11 | 31 | 29 | 26 | 22 | 23 | 21 | 22 | 24 |
| Net errors and omissions | 14 | 58 | 21 | 36 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Overall balance | 267 | 9 | 14 | 22 | 8 | 10 | 13 | 23 | 26 | 28 | 30 |
| Financing | -267 | -9 | -14 | -22 | -8 | -10 | -13 | -23 | -26 | -28 | -30 |
| Change in net international reserves (increase: –) | -43 | -17 | -14 | -23 | -8 | -10 | -13 | -23 | -26 | -28 | -30 |
| Change in gross official reserves (increase: –) | -58 | -23 | -20 | -29 | -10 | -12 | -9 | -20 | -22 | -23 | -24 |
| Liabilities to IMF, net | 13 | 6 | 6 | 6 | 2 | 2 | -4 | -3 | -4 | -5 | -7 |
| Other net foreign assets (increase: –) | 10 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Exceptional financing | -234 | 8 | 0 | 1 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Financing gap | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| *Memorandum items:* | | | | | | | | | | | |
| Exports G&S growth, percent | -3.9 | 9.0 | -2.6 | 0.7 | 3.5 | 4.4 | 4.4 | 4.5 | 4.5 | 3.7 | 3.8 |
| Tourism growth, percent | 7.0 | 6.1 | 4.9 | 6.6 | 3.9 | 6.7 | 6.1 | 6.0 | 6.1 | 4.5 | 4.5 |
| Imports G&S growth, percent | 6.9 | 9.5 | 0.8 | 1.0 | -1.1 | 5.1 | -0.2 | 2.7 | 2.7 | 2.9 | 3.3 |
| Exports G&S, percent of GDP | 102 | 102 | 104 | 105 | 101 | 94 | 93 | 92 | 91 | 89 | 87 |
| Imports G&S, percent of GDP | 123 | 123 | 129 | 128 | 121 | 115 | 108 | 105 | 102 | 99 | 97 |
| FDI (incl. loans) | 195 | 180 | 147 | 145 | 130 | 174 | 130 | 142 | 140 | 138 | 136 |
| FDI (incl. loans), percent of GDP | 20.0 | 17.0 | 14.4 | 14.0 | 11.9 | 14.4 | 10.1 | 10.5 | 9.8 | 9.1 | 8.5 |
| Gross international reserves (stock, e.o.p.) | 254 | 277 | 296 | 305 | 306 | 317 | 326 | 346 | 368 | 390 | 414 |
| *Of which:* program definition[3] | 238 | 254 | 265 | 277 | 275 | 289 | 297 | 318 | 340 | 362 | 386 |
| (Months of imports of goods & services) | 2.3 | 2.5 | 2.7 | 2.6 | 2.7 | 2.7 | 2.7 | 2.8 | 2.9 | 3.0 | 3.1 |
| Scheduled public external debt service | 72 | 22 | 25 | 22 | 31 | 35 | 32 | 42 | 57 | 66 | 64 |
| (Percent of exports of goods & services) | 7.3 | 2.0 | 2.3 | 2.1 | 2.8 | 3.1 | 2.7 | 3.4 | 4.4 | 4.9 | 4.6 |
| Public and publicly guaranteed external debt [4] | 478 | 490 | 520 | 512 | 566 | 558 | 597 | 614 | 614 | 598 | 572 |
| (Percent of GDP) | 49.1 | 46.2 | 50.7 | 49.6 | 52.0 | 46.3 | 46.7 | 45.4 | 42.9 | 39.5 | 35.7 |
| GDP | 973 | 1,060 | 1,027 | 1,032 | 1,090 | 1,205 | 1,278 | 1,352 | 1,431 | 1,515 | 1,604 |

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

[1] Including coupons on the eurobonds, amortizing notes and bonds issued after the commercial debt exchange.

[2] Includes parastatals for which data are available.

[3] Excludes foreign-currency denominated required reserves held by banks and project and blocked accounts at the CBS.

[4] Includes outstanding IMF credit.

## Table 3. Seychelles: Consolidated Government Operations, 2010–18[1]
## (millions of Seychelles rupees; cumulative from the start of the year)

| | 2010 | 2011 | 2012 | | 2013 | | | | 2014 | 2015 | 2016 | 2017 | 2018 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | | | | | Q1 | Q2 | Q3 | Q4 | | | | | |
| | | | Prog. | Prel. | Proj. | Proj. | Proj. | Proj. | Proj. | Proj. | Proj. | Proj. | Proj. |
| Total revenue and grants | 4,108 | 5,014 | 6,051 | 6,024 | 1,444 | 2,972 | 4,509 | 6,172 | 6,247 | 6,613 | 6,968 | 7,429 | 7,904 |
| Total revenue | 4,008 | 4,695 | 5,263 | 5,322 | 1,220 | 2,620 | 4,041 | 5,566 | 5,867 | 6,275 | 6,704 | 7,162 | 7,636 |
| Tax | 3,533 | 4,165 | 4,573 | 4,600 | 1,042 | 2,206 | 3,516 | 4,897 | 5,253 | 5,618 | 6,001 | 6,411 | 6,833 |
| Personal income tax | 195 | 612 | 686 | 702 | 184 | 380 | 566 | 764 | 815 | 873 | 931 | 993 | 1,056 |
| Social security tax | 220 | … | … | … | … | … | … | … | … | … | … | … | … |
| Trade tax | 356 | 421 | 415 | 401 | 101 | 204 | 314 | 433 | 460 | 490 | 523 | 556 | 589 |
| Excise tax | 580 | 727 | 744 | 726 | 175 | 362 | 548 | 751 | 803 | 857 | 912 | 975 | 1,038 |
| Goods and services tax (GST) / VAT [2] | 1,047 | 1,208 | 1,485 | 1,465 | 334 | 687 | 1,108 | 1,564 | 1,684 | 1,808 | 1,934 | 2,067 | 2,208 |
| Business tax | 790 | 893 | 770 | 816 | 164 | 394 | 703 | 935 | 1,007 | 1,072 | 1,146 | 1,225 | 1,309 |
| Other | 346 | 304 | 474 | 491 | 84 | 180 | 277 | 450 | 484 | 519 | 555 | 593 | 634 |
| Nontax | 474 | 530 | 689 | 722 | 179 | 414 | 525 | 670 | 614 | 657 | 703 | 752 | 803 |
| Fees and charges | 191 | 306 | 342 | 398 | 81 | 150 | 219 | 275 | 265 | 284 | 303 | 324 | 346 |
| Dividends from parastatals | 206 | 161 | 282 | 266 | 85 | 241 | 266 | 330 | 279 | 299 | 320 | 342 | 366 |
| Other | 77 | 63 | 65 | 58 | 13 | 24 | 41 | 64 | 69 | 74 | 80 | 85 | 91 |
| External grants | 101 | 319 | 788 | 702 | 224 | 352 | 468 | 605 | 380 | 338 | 264 | 266 | 269 |
| Expenditure and net lending | 3,815 | 4,689 | 5,800 | 5,687 | 1,413 | 2,804 | 4,224 | 5,893 | 5,920 | 6,201 | 6,546 | 6,904 | 7,306 |
| Current expenditure | 3,194 | 3,620 | 4,121 | 3,997 | 1,030 | 2,027 | 3,093 | 4,323 | 4,437 | 4,672 | 4,954 | 5,222 | 5,526 |
| Primary current expenditure | 2,482 | 3,236 | 3,535 | 3,457 | 884 | 1,772 | 2,694 | 3,817 | 4,036 | 4,310 | 4,608 | 4,914 | 5,240 |
| Wages and salaries | 693 | 891 | 1,023 | 1,003 | 281 | 561 | 843 | 1,129 | 1,205 | 1,278 | 1,354 | 1,435 | 1,526 |
| Goods and services | 843 | 999 | 1,164 | 1,134 | 220 | 493 | 789 | 1,212 | 1,286 | 1,378 | 1,483 | 1,586 | 1,693 |
| Transfers | 935 | 1,330 | 1,326 | 1,298 | 365 | 696 | 1,037 | 1,448 | 1,515 | 1,623 | 1,736 | 1,856 | 1,982 |
| Social program of central government | 233 | 266 | 300 | 290 | 76 | 164 | 253 | 355 | 410 | 439 | 469 | 502 | 536 |
| Transfers to public sector from central government | 349 | 727 | 685 | 660 | 195 | 343 | 500 | 715 | 698 | 748 | 800 | 856 | 913 |
| Benefits and programs of Social Security Fund | 353 | 338 | 340 | 348 | 95 | 189 | 284 | 378 | 407 | 436 | 466 | 499 | 532 |
| Other | 12 | 15 | 22 | 23 | 18 | 23 | 26 | 28 | 30 | 32 | 34 | 37 | 39 |
| Interest due | 712 | 384 | 586 | 540 | 146 | 254 | 399 | 506 | 402 | 362 | 347 | 308 | 286 |
| Foreign interest | 402 | 137 | 188 | 174 | 64 | 90 | 153 | 178 | 180 | 201 | 221 | 207 | 199 |
| Domestic interest | 310 | 247 | 398 | 366 | 82 | 164 | 246 | 328 | 222 | 160 | 126 | 102 | 86 |
| Capital expenditure | 1,009 | 1,060 | 1,601 | 1,613 | 368 | 622 | 921 | 1,339 | 1,241 | 1,326 | 1,362 | 1,552 | 1,724 |
| Net lending | -389 | 9 | 4 | -6 | -3 | 110 | 149 | 157 | 191 | 153 | 179 | 78 | 0 |
| Contingency | 0 | 0 | 75 | 83 | 19 | 45 | 60 | 75 | 50 | 50 | 50 | 52 | 55 |
| Primary balance | 1,006 | 709 | 837 | 877 | 176 | 422 | 684 | 785 | 729 | 773 | 769 | 833 | 885 |
| Overall balance, commitment basis [3] | 293 | 325 | 251 | 337 | 31 | 168 | 285 | 279 | 327 | 411 | 422 | 524 | 599 |
| Change in arrears | -3 | 16 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| External interest | 90 | 27 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Budget | -92 | -11 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Change in float | 0 | -217 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Overall balance, cash basis (after grants) | 291 | 124 | 251 | 338 | 31 | 168 | 285 | 279 | 327 | 411 | 422 | 524 | 599 |
| Financing | -291 | -124 | -251 | -338 | -31 | -168 | -285 | -279 | -327 | -411 | -422 | -524 | -599 |
| Foreign financing | 236 | 2 | 110 | 53 | 42 | 119 | 192 | 405 | 513 | 170 | -20 | -220 | -325 |
| Disbursements | 584 | 83 | 260 | 168 | 60 | 208 | 299 | 609 | 742 | 501 | 493 | 434 | 309 |
| Project loans | 247 | 83 | 163 | 79 | 60 | 208 | 299 | 393 | 523 | 501 | 493 | 434 | 309 |
| Program/budget support | 337 | 0 | 97 | 89 | 0 | 0 | 0 | 216 | 219 | 0 | 0 | 0 | 0 |
| Scheduled amortization | -554 | -126 | -149 | -121 | -18 | -89 | -106 | -203 | -228 | -331 | -513 | -654 | -634 |
| Change in amortization arrears | -2,811 | 44 | 0 | 6 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Clearance of arrears | 3,017 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Debt service relief | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Domestic financing, net [4] | -701 | -177 | -471 | -493 | -91 | -322 | -530 | -754 | -879 | -620 | -402 | -304 | -273 |
| Bank financing | -346 | -181 | -589 | -642 | -82 | -290 | -477 | -679 | -791 | -558 | -362 | -274 | -246 |
| CBS | -131 | 45 | -1,146 | -1,194 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| CBS recapitalization | 188 | … | … | … | … | … | … | … | … | … | … | … | … |
| Commercial banks | -403 | -226 | 557 | 552 | -82 | -290 | -477 | -679 | -791 | -558 | -362 | -274 | -246 |
| Nonbank financing | -355 | 4 | 118 | 148 | -9 | -32 | -53 | -75 | -88 | -62 | -40 | -30 | -27 |
| Privatization and long-term lease of fixed assets | 156 | 99 | 113 | 84 | 18 | 35 | 53 | 70 | 38 | 38 | 0 | 0 | 0 |
| Statistical discrepancy | 18 | -47 | -3 | 19 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Fiscal financing gap | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| *Memorandum item:* | | | | | | | | | | | | | |
| Pension Fund contribution | … | 67 | 102 | 105 | 26 | 51 | 77 | 102 | 109 | 115 | 121 | 128 | 135 |
| Pension Fund benefits payment | … | 78 | 94 | 100 | 26 | 53 | 79 | 105 | 110 | 115 | 120 | 126 | 131 |
| Pension Fund operating expenses | … | … | … | … | 5 | 12 | 17 | 23 | 24 | 25 | 27 | 29 | 31 |
| External debt service due | 957 | 263 | 338 | 294 | 82 | 179 | 260 | 382 | 408 | 532 | 733 | 860 | 834 |

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

[4] Includes one-off operations in 2011: repayment of recently recognized domestic obligation (SR 90 million) and the increase in IMF quota (SR 10 million).

## Table 3. Seychelles: Consolidated Government Operations, 2010–18[1] (continued)
## (Percent of GDP; cumulative from the start of the year)

| | 2010 | 2011 | 2012 | | 2013 | | | | 2014 | 2015 | 2016 | 2017 | 2018 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | | | | | Q1 | Q2 | Q3 | Q4 | | | | | |
| | | | Prog. | Prel. | Proj. | Proj. | Proj. | Proj. | Proj. | Proj. | Proj. | Proj. | Proj. |
| Total revenue and grants | 35.0 | 38.2 | 42.7 | 42.6 | 9.4 | 19.4 | 29.5 | 40.4 | 37.9 | 37.5 | 36.9 | 36.8 | 36.7 |
| Total revenue | 34.1 | 35.8 | 37.2 | 37.6 | 8.0 | 17.1 | 26.4 | 36.4 | 35.6 | 35.6 | 35.5 | 35.5 | 35.5 |
| Tax | 30.1 | 31.8 | 32.3 | 32.5 | 6.8 | 14.4 | 23.0 | 32.0 | 31.9 | 31.9 | 31.8 | 31.8 | 31.7 |
| Personal income tax | 1.7 | 4.7 | 4.8 | 5.0 | 1.2 | 2.5 | 3.7 | 5.0 | 5.0 | 5.0 | 4.9 | 4.9 | 4.9 |
| Social security tax | 1.9 | … | … | … | … | … | … | … | … | … | … | … | … |
| Trade tax | 3.0 | 3.2 | 2.9 | 2.8 | 0.7 | 1.3 | 2.1 | 2.8 | 2.8 | 2.8 | 2.8 | 2.8 | 2.7 |
| Excise tax | 4.9 | 5.5 | 5.3 | 5.1 | 1.1 | 2.4 | 3.6 | 4.9 | 4.9 | 4.9 | 4.8 | 4.8 | 4.8 |
| Goods and services tax (GST) / VAT [2] | 8.9 | 9.2 | 10.5 | 10.4 | 2.2 | 4.5 | 7.2 | 10.2 | 10.2 | 10.2 | 10.2 | 10.2 | 10.2 |
| Business tax | 6.7 | 6.8 | 5.4 | 5.8 | 1.1 | 2.6 | 4.6 | 6.1 | 6.1 | 6.1 | 6.1 | 6.1 | 6.1 |
| Other | 2.9 | 2.3 | 3.3 | 3.5 | 0.5 | 1.2 | 1.8 | 2.9 | 2.9 | 2.9 | 2.9 | 2.9 | 2.9 |
| Nontax | 4.0 | 4.0 | 4.9 | 5.1 | 1.2 | 2.7 | 3.4 | 4.4 | 3.7 | 3.7 | 3.7 | 3.7 | 3.7 |
| Fees and charges | 1.6 | 2.3 | 2.4 | 2.8 | 0.5 | 1.0 | 1.4 | 1.8 | 1.6 | 1.6 | 1.6 | 1.6 | 1.6 |
| Dividends from parastatals | 1.8 | 1.2 | 2.0 | 1.9 | 0.6 | 1.6 | 1.7 | 2.2 | 1.7 | 1.7 | 1.7 | 1.7 | 1.7 |
| Other | 0.7 | 0.5 | 0.5 | 0.4 | 0.1 | 0.2 | 0.3 | 0.4 | 0.4 | 0.4 | 0.4 | 0.4 | 0.4 |
| External grants | 0.9 | 2.4 | 5.6 | 5.0 | 1.5 | 2.3 | 3.1 | 4.0 | 2.3 | 1.9 | 1.4 | 1.3 | 1.2 |
| Expenditure and net lending | 32.5 | 35.7 | 41.0 | 40.2 | 9.2 | 18.3 | 27.6 | 38.5 | 36.0 | 35.2 | 34.7 | 34.2 | 33.9 |
| Current expenditure | 27.2 | 27.6 | 29.1 | 28.3 | 6.7 | 13.3 | 20.2 | 28.3 | 27.0 | 26.5 | 26.3 | 25.9 | 25.7 |
| Primary current expenditure | 21.1 | 24.7 | 25.0 | 24.4 | 5.8 | 11.6 | 17.6 | 25.0 | 24.5 | 24.4 | 24.4 | 24.4 | 24.3 |
| Wages and salaries | 5.9 | 6.8 | 7.2 | 7.1 | 1.8 | 3.7 | 5.5 | 7.4 | 7.3 | 7.2 | 7.2 | 7.1 | 7.1 |
| Goods and services | 7.2 | 7.6 | 8.2 | 8.0 | 1.4 | 3.2 | 5.2 | 7.9 | 7.8 | 7.8 | 7.9 | 7.9 | 7.9 |
| Transfers | 8.0 | 10.1 | 9.4 | 9.2 | 2.4 | 4.6 | 6.8 | 9.5 | 9.2 | 9.2 | 9.2 | 9.2 | 9.2 |
| Social program of central government | 2.0 | 2.0 | 2.1 | 2.0 | 0.5 | 1.1 | 1.7 | 2.3 | 2.5 | 2.5 | 2.5 | 2.5 | 2.5 |
| Transfers to public sector from central government | 3.0 | 5.5 | 4.8 | 4.7 | 1.3 | 2.2 | 3.3 | 4.7 | 4.2 | 4.2 | 4.2 | 4.2 | 4.2 |
| Benefits and programs of Social Security Fund | 3.0 | 2.6 | 2.4 | 2.5 | 0.6 | 1.2 | 1.9 | 2.5 | 2.5 | 2.5 | 2.5 | 2.5 | 2.5 |
| Other | 0.1 | 0.1 | 0.2 | 0.2 | 0.1 | 0.1 | 0.2 | 0.2 | 0.2 | 0.2 | 0.2 | 0.2 | 0.2 |
| Interest due | 6.1 | 2.9 | 4.1 | 3.8 | 1.0 | 1.7 | 2.6 | 3.3 | 2.4 | 2.1 | 1.8 | 1.5 | 1.3 |
| Foreign interest | 3.4 | 1.0 | 1.3 | 1.2 | 0.4 | 0.6 | 1.0 | 1.2 | 1.1 | 1.1 | 1.2 | 1.0 | 0.9 |
| Domestic interest | 2.6 | 1.9 | 2.8 | 2.6 | 0.5 | 1.1 | 1.6 | 2.1 | 1.3 | 0.9 | 0.7 | 0.5 | 0.4 |
| Capital expenditure | 8.6 | 8.1 | 11.3 | 11.4 | 2.4 | 4.1 | 6.0 | 8.8 | 7.5 | 7.5 | 7.2 | 7.7 | 8.0 |
| Net lending | -3.3 | 0.1 | 0.0 | 0.0 | 0.0 | 0.7 | 1.0 | 1.0 | 1.2 | 0.9 | 1.0 | 0.4 | 0.0 |
| Contingency | 0.0 | 0.0 | 0.5 | 0.6 | 0.1 | 0.3 | 0.4 | 0.5 | 0.3 | 0.3 | 0.3 | 0.3 | 0.3 |
| Primary balance | 8.6 | 5.4 | 5.9 | 6.2 | 1.2 | 2.8 | 4.5 | 5.1 | 4.4 | 4.4 | 4.1 | 4.1 | 4.1 |
| Overall balance, commitment basis [3] | 2.5 | 2.5 | 1.8 | 2.4 | 0.2 | 1.1 | 1.9 | 1.8 | 2.0 | 2.3 | 2.2 | 2.6 | 2.8 |
| Change in arrears | 0.0 | 0.1 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| External interest | 0.8 | 0.2 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Budget | -0.8 | -0.1 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Change in float | 0.0 | -1.7 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Overall balance, cash basis (after grants) | 2.5 | 0.9 | 1.8 | 2.4 | 0.2 | 1.1 | 1.9 | 1.8 | 2.0 | 2.3 | 2.2 | 2.6 | 2.8 |
| Financing | -2.5 | -0.9 | -1.8 | -2.4 | -0.2 | -1.1 | -1.9 | -1.8 | -2.0 | -2.3 | -2.2 | -2.6 | -2.8 |
| Foreign financing | 2.0 | 0.0 | 0.8 | 0.4 | 0.3 | 0.8 | 1.3 | 2.7 | 3.1 | 1.0 | -0.1 | -1.1 | -1.5 |
| Disbursements | 5.0 | 0.6 | 1.8 | 1.2 | 0.4 | 1.4 | 2.0 | 4.0 | 4.5 | 2.8 | 2.6 | 2.2 | 1.4 |
| Project loans | 2.1 | 0.6 | 1.2 | 0.6 | 0.4 | 1.4 | 2.0 | 2.6 | 3.2 | 2.8 | 2.6 | 2.2 | 1.4 |
| Program/budget support | 2.9 | 0.0 | 0.7 | 0.6 | 0.0 | 0.0 | 0.0 | 1.4 | 1.3 | 0.0 | 0.0 | 0.0 | 0.0 |
| Scheduled amortization | -4.7 | -1.0 | -1.1 | -0.9 | -0.1 | -0.6 | -0.7 | -1.3 | -1.4 | -1.9 | -2.7 | -3.2 | -2.9 |
| Change in amortization arrears | -23.9 | 0.3 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Clearance of arrears | 25.7 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Debt service relief | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Domestic financing, net [4] | -6.0 | -1.3 | -3.3 | -3.5 | -0.6 | -2.1 | -3.5 | -4.9 | -5.3 | -3.5 | -2.1 | -1.5 | -1.3 |
| Bank financing | -2.9 | -1.4 | -4.2 | -4.5 | -0.5 | -1.9 | -3.1 | -4.4 | -4.8 | -3.2 | -1.9 | -1.4 | -1.1 |
| CBS | -1.1 | 0.3 | -8.1 | -8.4 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| CBS recapitalization | 1.6 | … | … | … | … | … | … | … | … | … | … | … | … |
| Commercial banks | -3.4 | -1.7 | 3.9 | 3.9 | -0.5 | -1.9 | -3.1 | -4.4 | -4.8 | -3.2 | -1.9 | -1.4 | -1.1 |
| Nonbank | -3.0 | 0.0 | 0.8 | 1.0 | -0.1 | -0.2 | -0.3 | -0.5 | -0.5 | -0.4 | -0.2 | -0.2 | -0.1 |
| Privatization and long-term lease of fixed assets | 1.3 | 0.8 | 0.8 | 0.6 | 0.1 | 0.2 | 0.3 | 0.5 | 0.2 | 0.2 | 0.0 | 0.0 | 0.0 |
| Statistical discrepancy | 0.2 | -0.4 | 0.0 | 0.1 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| *Memorandum items:* | | | | | | | | | | | | | |
| Nominal GDP (millions of Seychelles Rupees) | 11,746 | 13,119 | 14,159 | 14,145 | 15,292 | 15,292 | 15,292 | 15,292 | 16,461 | 17,636 | 18,866 | 20,171 | 21,538 |
| Pension Fund contribution | … | 0.5 | 0.7 | 0.7 | 0.2 | 0.3 | 0.5 | 0.7 | 0.7 | 0.7 | 0.6 | 0.6 | 0.6 |
| Pension Fund benefits payment | … | 0.6 | 0.7 | 0.7 | 0.2 | 0.3 | 0.5 | 0.7 | 0.7 | 0.7 | 0.6 | 0.6 | 0.6 |
| Pension Fund operating expenses | … | … | … | … | 0.0 | 0.1 | 0.1 | 0.2 | 0.1 | 0.1 | 0.1 | 0.1 | 0.1 |
| Public domestic debt (% GDP) | 32.5 | 28.0 | 32.8 | 33.1 | 30.1 | 28.6 | 27.2 | 25.7 | 18.6 | 13.8 | 10.8 | 8.6 | 6.8 |
| Excl. t-bills issued for monetary purposes | … | … | 27.4 | 27.7 | 25.1 | 23.5 | 22.2 | 25.7 | 18.6 | 13.8 | 10.8 | 8.6 | 6.8 |
| Publicly guaranteed domestic debt (% GDP) | 2.1 | 2.4 | 1.0 | 2.2 | 0.0 | 1.2 | 1.2 | 1.2 | 1.0 | 0.3 | 0.2 | 0.1 | 0.0 |

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

[4] Includes one-off operations in 2011: repayment of recently recognized domestic obligation (SR 90 million) and the increase in IMF quota (SR 10 million).

## Table 4. Seychelles: Monetary Survey and Central Bank Accounts, 2010–13
## (millions of Seychelles rupees)

| | 2010 | 2011 | 2012 | | 2013 | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | | | | | Mar. | | June | | Sep. | | Dec. | |
| | | | Prog. | Actual | Prog. | Proj. | Prog. | Proj. | Prog. | Proj. | Prog. | Proj. |
| **Monetary survey** | | | | | | | | | | | | |
| Net foreign assets | 3,644 | 4,450 | 4,901 | 5,252 | 5,034 | 5,172 | 5,112 | 5,235 | 5,211 | 5,309 | 5,362 | 5,474 |
| Central bank | 2,709 | 3,303 | 3,485 | 3,434 | 3,563 | 3,378 | 3,574 | 3,377 | 3,609 | 3,386 | 3,696 | 3,495 |
| Deposit money banks | 935 | 1,147 | 1,416 | 1,818 | 1,470 | 1,794 | 1,538 | 1,858 | 1,602 | 1,923 | 1,666 | 1,979 |
| Net domestic assets | 3,622 | 3,145 | 2,491 | 2,170 | 2,513 | 2,238 | 2,352 | 2,051 | 2,267 | 2,007 | 2,145 | 1,952 |
| Domestic credit | 5,652 | 5,657 | 5,167 | 5,144 | 5,249 | 5,118 | 5,150 | 4,970 | 5,109 | 4,951 | 5,037 | 4,900 |
| Net claims on the government | 2,567 | 2,380 | 1,834 | 1,786 | 1,693 | 1,704 | 1,580 | 1,496 | 1,437 | 1,309 | 1,264 | 1,107 |
| Credit to the economy | 3,085 | 3,277 | 3,333 | 3,358 | 3,556 | 3,414 | 3,569 | 3,474 | 3,672 | 3,643 | 3,773 | 3,793 |
| Other items, net | -2,029 | -2,511 | -2,676 | -2,974 | -2,736 | -2,880 | -2,797 | -2,919 | -2,842 | -2,944 | -2,892 | -2,948 |
| Broad money | 7,266 | 7,596 | 7,392 | 7,422 | 7,547 | 7,410 | 7,465 | 7,286 | 7,477 | 7,316 | 7,507 | 7,426 |
| Currency in circulation | 580 | 623 | 652 | 631 | 662 | 678 | 672 | 688 | 682 | 699 | 693 | 709 |
| Foreign currency deposits | 1,708 | 2,406 | 2,961 | 2,441 | 2,984 | 2,437 | 3,054 | 2,427 | 3,115 | 2,282 | 3,175 | 2,281 |
| Local currency deposits | 4,979 | 4,566 | 3,779 | 4,350 | 3,901 | 4,296 | 3,738 | 4,171 | 3,680 | 4,335 | 3,640 | 4,435 |
| **Central bank** | | | | | | | | | | | | |
| Net foreign assets | 2,709 | 3,303 | 3,485 | 3,434 | 3,563 | 3,378 | 3,574 | 3,377 | 3,609 | 3,386 | 3,696 | 3,495 |
| Foreign assets | 3,087 | 3,800 | 4,055 | 3,972 | 4,114 | 3,881 | 4,170 | 3,922 | 4,179 | 3,908 | 4,306 | 4,052 |
| Foreign liabilities | 379 | 497 | 570 | 538 | 550 | 504 | 596 | 545 | 570 | 522 | 609 | 557 |
| Net domestic assets | -962 | -1,604 | -1,565 | -1,617 | -1,613 | -1,428 | -1,594 | -1,397 | -1,599 | -1,376 | -1,656 | -1,455 |
| Domestic credit | -506 | -883 | -888 | -1,113 | -868 | -1,036 | -787 | -967 | -747 | -920 | -764 | -976 |
| Government (net) | 780 | 835 | -311 | -358 | -311 | -358 | -311 | -358 | -311 | -358 | -311 | -358 |
| Commercial banks | -1,135 | -1,512 | -470 | -636 | -450 | -559 | -369 | -490 | -329 | -443 | -345 | -499 |
| Other (parastatals) | -151 | -206 | -107 | -119 | -107 | -119 | -107 | -119 | -107 | -119 | -107 | -119 |
| Other items, net | -456 | -721 | -677 | -504 | -745 | -392 | -807 | -431 | -852 | -456 | -892 | -479 |
| Reserve money | 1,746 | 1,699 | 1,920 | 1,816 | 1,950 | 1,950 | 1,980 | 1,980 | 2,010 | 2,010 | 2,040 | 2,040 |
| Currency in circulation | 580 | 623 | 652 | 631 | 662 | 678 | 672 | 688 | 682 | 699 | 693 | 709 |
| Commercial bank reserves (includes cash in vault) | 1,166 | 1,075 | 1,268 | 1,185 | 1,288 | 1,272 | 1,308 | 1,292 | 1,328 | 1,311 | 1,347 | 1,331 |
| *Of which* : required reserves in foreign currency [1, 2] | 193 | 322 | 415 | 350 | 418 | 348 | 428 | 357 | 436 | 365 | 445 | 372 |
| required reserves in domestic currency [2] | 545 | 679 | 638 | 667 | 654 | 704 | 633 | 688 | 625 | 709 | 620 | 722 |
| *Memorandum items:* | | | | | | | | | | | | |
| Gross international reserves (millions of U.S. dollars) [3] | 254 | 277 | 298 | 305 | 300 | 309 | 301 | 310 | 300 | 307 | 308 | 317 |
| Foreign currency deposits (millions of U.S. dollars) | 141 | 175 | 218 | 188 | 217 | 194 | 221 | 192 | 224 | 179 | 227 | 178 |
| Broad money growth (12–month percent change) | 13.5 | 4.5 | -2.7 | -2.3 | -3.4 | -5.2 | -5.2 | -7.5 | 2.7 | 0.5 | 1.6 | 0.1 |
| Credit to the economy (12–month percent change) | 21.4 | 6.2 | 1.7 | 2.5 | 7.3 | 3.0 | 8.7 | 5.8 | 11.0 | 10.1 | 13.2 | 13.0 |
| Reserve money (12–month percent change) | 34.7 | -2.7 | 13.0 | 6.9 | 11.5 | 11.5 | 13.5 | 13.5 | 18.8 | 18.8 | 6.3 | 12.3 |
| Money multiplier (broad money/reserve money) | 4.2 | 4.5 | 3.9 | 4.1 | 3.9 | 3.8 | 3.8 | 3.7 | 3.7 | 3.6 | 3.7 | 3.6 |
| Velocity (GDP/broad money; end of period) | 1.6 | 1.7 | 1.9 | 1.9 | 2.0 | 2.1 | 2.0 | 2.1 | 2.0 | 2.1 | 2.0 | 2.1 |

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

[1] 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.

[3] 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, 2009–12 1
### (Percent, end of period)

| | 2009 | | | | 2010 | | | | 2011 | | | | 2012 | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Q1 | Q2 | Q3 | Q4 | Q1 | Q2 | Q3 | Q4 | Q1 | Q2 | Q3 | Q4 | Q1 | Q2 | Q3 | Q4 |
| **Capital adequacy** | | | | | | | | | | | | | | | | |
| Regulatory capital to risk weighted assets | 13.6 | 17.8 | 22.0 | 21.7 | 21.4 | 22.1 | 21.7 | 21.5 | 23.3 | 24.8 | 26.3 | 24.2 | 24.9 | 25.9 | 26.2 | 26.7 |
| Regulatory tier 1 capital to risk weighted assets | 12.9 | 17.1 | 21.3 | 21.0 | 20.7 | 21.5 | 21.1 | 20.8 | 16.8 | 21.0 | 21.1 | 17.3 | 18.1 | 21.6 | 19.9 | 19.3 |
| Capital to assets (net worth) | 9.6 | 8.7 | 9.7 | 9.9 | 9.3 | 8.7 | 9.1 | 9.2 | 9.3 | 9.6 | 10.1 | 9.0 | 9.1 | 9.5 | 9.8 | 10.3 |
| Net tangible capitalization [2] | 9.6 | 8.7 | 9.8 | 9.9 | 9.4 | 8.8 | 9.1 | 9.3 | 9.4 | 9.7 | 10.2 | 9.1 | 9.3 | 9.6 | 9.9 | 10.4 |
| **Asset quality** | | | | | | | | | | | | | | | | |
| Foreign exchange loans to total loans | 50.5 | 43.0 | 41.1 | 37.2 | 34.3 | 29.7 | 27.8 | 25.5 | 23.7 | 20.1 | 18.5 | 18.4 | 20.9 | 20.0 | 17.9 | 18.7 |
| Nonperforming loans to gross loans | 2.3 | 4.3 | 4.2 | 3.8 | 4.1 | 6.9 | 6.4 | 5.5 | 5.4 | 5.6 | 5.3 | 8.1 | 8.3 | 9.2 | 8.3 | 9.3 |
| Provisions as percentage of nonperforming loans | 56.8 | 35.2 | 32.6 | 33.8 | 41.7 | 26.0 | 26.0 | 31.4 | 30.9 | 37.3 | 40.4 | 33.8 | 33.9 | 32.1 | 33.3 | 29.5 |
| Provisions as percentage of total loans | 1.3 | 1.5 | 1.4 | 1.3 | 1.7 | 1.8 | 1.7 | 1.7 | 1.7 | 2.1 | 2.2 | 2.7 | 2.8 | 3.0 | 2.7 | 2.7 |
| **Earnings and profitability** | | | | | | | | | | | | | | | | |
| Return on assets (annualized) | 5.3 | 3.0 | -0.2 | 3.2 | 3.4 | 5.0 | 3.0 | 3.7 | 3.9 | 3.1 | 3.6 | 5.6 | 3.5 | 3.9 | 4.2 | 3.1 |
| Return on equity (annualized) | 55.1 | 35.4 | -2.8 | 32.4 | 33.6 | 54.3 | 33.7 | 40.0 | 40.8 | 32.6 | 36.4 | 61.6 | 38.3 | 40.8 | 41.3 | 29.8 |
| Interest margin to gross income | 62.1 | 83.7 | 105.5 | 68.6 | 56.5 | 60.2 | 59.9 | 50.6 | 46.8 | 56.3 | 61.6 | 55.8 | 52.8 | 57.5 | 64.6 | 62.7 |
| Noninterest expense to gross income | 36.4 | 48.7 | 116.5 | 49.1 | 44.0 | 52.0 | 47.6 | 39.9 | 46.7 | 49.3 | 46.4 | 22.3 | 44.0 | 40.7 | 39.0 | 56.6 |
| Net interest margin (annualized)[3] | 5.1 | 4.8 | 4.2 | 4.0 | 3.1 | 3.6 | 3.4 | 3.1 | 3.0 | 3.5 | 4.2 | 3.9 | 3.6 | 3.5 | 3.9 | 4.1 |
| Net noninterest margin (annualized)[4] | 0.1 | -1.9 | -4.9 | -1.0 | 0.0 | -0.7 | -0.4 | 0.6 | 0.4 | -0.3 | -0.5 | 1.5 | 0.3 | 0.2 | 0.1 | 0.0 |
| Expense to income | 52.3 | 62.2 | 111.2 | 58.0 | 53.0 | 58.0 | 53.6 | 46.6 | 50.8 | 53.6 | 50.1 | 28.5 | 44.7 | 45.4 | 45.4 | 46.4 |
| Interest expense to gross income | 33.2 | 35.8 | 47.1 | 21.2 | 19.0 | 14.2 | 12.8 | 12.5 | 8.5 | 9.3 | 7.4 | 8.7 | 9.3 | 9.7 | 10.9 | 11.8 |
| **Liquidity** | | | | | | | | | | | | | | | | |
| Core liquid assets to total assets[5] | 36.0 | 35.0 | 37.7 | 43.2 | 43.5 | 44.7 | 44.7 | 46.9 | 47.1 | 47.1 | 47.7 | 49.9 | 49.6 | 48.6 | 47.9 | 39.6 |
| Broad liquid assets to total assets[6] | 50.8 | 53.0 | 57.6 | 58.4 | 58.6 | 60.0 | 58.1 | 58.9 | 56.6 | 55.7 | 57.0 | 58.8 | 59.3 | 57.9 | 59.6 | 52.0 |
| Liquid assets (broad) to short term liabilities | 53.2 | 56.2 | 62.1 | 62.7 | 65.0 | 63.4 | 62.1 | 62.9 | 60.0 | 58.8 | 60.9 | 63.0 | 65.4 | 64.6 | 66.6 | 58.1 |
| Liquid assets (broad) to total liabilities | 56.2 | 58.0 | 63.8 | 64.7 | 64.7 | 65.7 | 63.8 | 64.9 | 62.4 | 61.6 | 63.4 | 64.7 | 65.3 | 64.0 | 66.1 | 58.0 |
| Liquid assets to deposit liabilities | 63.1 | 63.8 | 71.4 | 69.4 | 72.4 | 72.0 | 69.1 | 69.1 | 65.5 | 64.5 | 68.7 | 71.0 | 70.9 | 69.7 | 71.0 | 62.5 |
| **Foreign exchange exposure** | | | | | | | | | | | | | | | | |
| Net open foreign exchange position to capital | 44.4 | 32.4 | 21.9 | 33.1 | 22.2 | 24.7 | 29.2 | 5.6 | 3.8 | 2.2 | 1.5 | 1.9 | 2.9 | -3.9 | -0.8 | 7.9 |

Source: Central Bank of Seychelles.

[1] Excluding 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 and Purchases Under the Extended Arrangement Table 6., 2009–13le

| Program Review | Date of availability | Conditions | Amount | |
|---|---|---|---|---|
| | | | (Millions of SDR) | (Percent of quota) |
| | December 23, 2009 | Board approval of the Extended Arrangement | 0.88 | 8.1 |
| | March 15, 2010 | Compliance with end-December 2009 quantitative performance criteria and completion of a financing assurances review (if needed) | 2.20 | 20.2 |
| First | June 15, 2010 | Completion of first program review and financing assurances review (if needed) and compliance with end-March 2010 quantitative performance criteria | 2.20 | 20.2 |
| | September 15, 2010 | Compliance with end-June 2010 quantitative performance criteria and completion of a financing assurances review (if needed) | 2.20 | 20.2 |
| Second | December 15, 2010 | Completion of second program review and financing assurances review (if needed) and compliance with end-September 2010 quantitative performance criteria | 1.76 | 16.1 |
| Third | March 31, 2011 | Compliance with end-December 2010 quantitative performance criteria and completion of a financing assurances review (if needed) | 3.52 | 32.3 |
| Fourth | September 30, 2011 | Compliance with end-June 2011 quantitative performance criteria and completion of a financing assurances review (if needed) | 3.08 | 28.3 |
| Fifth | March 31, 2012 | Compliance with end-December 2011 quantitative performance criteria and completion of a financing assurances review (if needed) | 2.64 | 24.2 |
| Sixth | September 30, 2012 | Compliance with end-June 2012 quantitative performance criteria | 1.32 | 12.1 |
| Seventh | March 31, 2013 | Compliance with end-December 2012 quantitative performance criteria | 3.30 | 30.3 |
| Eighth | September 30, 2013 | Compliance with end-June 2013 quantitative performance criteria | 3.30 | 30.3 |
| **Total** | | | **26.4** | **242.3** |

## Table 7. Seychelles: Indicators of Fund Credit, 2008–18
### (millions SDR)

| | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 |
|---|---|---|---|---|---|---|---|---|---|---|---|
| **Existing Fund credit** | | | | | | | | | | | |
| Stock [1] | 6.2 | 11.9 | 20.2 | 23.8 | 27.2 | 21.9 | 19.5 | 17.6 | 15.0 | 11.7 | 8.4 |
| Obligation | 0.0 | 0.1 | 0.2 | 0.4 | 3.9 | 5.5 | 2.7 | 2.0 | 2.8 | 3.5 | 3.4 |
| Principal (repayments/repurchases) | 0.0 | 0.0 | 0.0 | 0.0 | 3.6 | 5.3 | 2.4 | 1.8 | 2.6 | 3.3 | 3.3 |
| Charges and interest | 0.0 | 0.1 | 0.2 | 0.4 | 0.3 | 0.2 | 0.2 | 0.2 | 0.2 | 0.2 | 0.1 |
| Disbursements | 6.2 | 5.7 | 8.4 | 3.5 | 7.0 | … | … | … | … | … | … |
| **Projected EFF** | | | | | | | | | | | |
| Disbursement | | | | | | 6.6 | … | … | … | … | … |
| Stock [1] | | | | | | 6.6 | 6.6 | 6.6 | 6.6 | 6.3 | 5.2 |
| Obligations [3] | | | | | | 0.1 | 0.1 | 0.1 | 0.1 | 0.4 | 1.2 |
| Principal (repayments/repurchases) | | | | | | 0.0 | 0.0 | 0.0 | 0.0 | 0.3 | 1.1 |
| Charges and interest | | | | | | 0.1 | 0.1 | 0.1 | 0.1 | 0.1 | 0.1 |
| **Stock of existing and prospective Fund credit [1]** | 6.2 | 11.9 | 20.2 | 23.8 | 27.4 | 28.5 | 26.1 | 24.2 | 21.6 | 18.1 | 13.7 |
| In percent of quota | 70.0 | 135.0 | 230.0 | 218.0 | 251.3 | 261.4 | 239.2 | 222.4 | 198.4 | 165.7 | 125.3 |
| In percent of GDP | 1.0 | 2.2 | 3.2 | 3.5 | 4.1 | 3.6 | 3.1 | 2.7 | 2.3 | 1.8 | 1.3 |
| In percent of exports of goods and services | 0.9 | 1.8 | 3.1 | 3.4 | 3.9 | 3.8 | 3.4 | 3.0 | 2.5 | 2.0 | 1.5 |
| In percent of gross reserves | 12.9 | 9.6 | 12.2 | 13.3 | 13.8 | 13.8 | 12.3 | 10.7 | 9.0 | 7.0 | 5.0 |
| **Obligations to the Fund from existing and prospective Fund arrangements** | | | | | | | | | | | |
| Disbursements | 6.2 | 5.7 | 8.4 | 3.5 | 7.0 | 6.6 | … | … | … | … | … |
| Obligations | 0.0 | 0.1 | 0.2 | 0.4 | 3.9 | 5.6 | 2.7 | 2.1 | 2.9 | 3.8 | 4.6 |
| Principal (repayments/repurchases) | 0.0 | 0.0 | 0.0 | 0.0 | 3.6 | 5.3 | 2.4 | 1.8 | 2.6 | 3.6 | 4.4 |
| Charges and interest | 0.0 | 0.1 | 0.2 | 0.4 | 0.3 | 0.3 | 0.3 | 0.3 | 0.3 | 0.2 | 0.2 |
| In percent of quota | 0.3 | 0.9 | 2.0 | 3.4 | 35.7 | 51.0 | 25.1 | 19.4 | 26.3 | 35.0 | 42.2 |
| In percent of GDP | 0.0 | 0.0 | 0.0 | 0.1 | 0.6 | 0.7 | 0.3 | 0.2 | 0.3 | 0.4 | 0.4 |
| In percent of exports of goods and services | 0.0 | 0.0 | 0.0 | 0.1 | 0.5 | 0.8 | 0.4 | 0.3 | 0.3 | 0.4 | 0.5 |
| In percent of gross reserves | 0.1 | 0.1 | 0.1 | 0.2 | 2.0 | 2.7 | 1.3 | 0.9 | 1.2 | 1.5 | 1.7 |

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

[1] Assumes a one year extension of the EFF-supported arrangement and an augmentation of 60.6 percent of quota (SDR 6.6 million, approximately $10.2 million), disbursed following reviews of December 2012 and June 2013 test dates.

[2] End of period.

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

# APPENDIX I. SUPPLEMENTAL LETTER OF INTENT

April 19, 2013

Ms. Christine Lagarde
Managing Director
International Monetary Fund

Dear Managing Director Lagarde:

We are writing to request completion of the seventh and penultimate review under our Extended Arrangement, and the availability for purchase of the tenth tranche of SDR 3.30 million (30.3 percent of quota).

We met all end-December quantitative performance criteria under the program, and economic performance during 2012 was highly satisfactory, with most key indicators exceeding expectations. Real GDP growth is estimated to have been slightly higher than projection at 2.9 percent (projection was 2.7 percent). We also exceeded our end-of-year targets with regard to the primary fiscal surplus and net international reserves. Early indicators of economic activity in 2013 are highly encouraging, with the tourism sector – our mainstay – performing strongly, as indicated by a 19 percent growth in visitor arrivals for the first ten weeks of the year compared to the same period last year. This puts us in a good position to exceed the projected real growth target of 3.3 percent for 2013.

We remain strongly committed to maintain fiscal discipline that is vital for attaining long-term debt sustainability. Nevertheless we are cognizant of some downside risks due, among other things, to the tropical cyclone that affected Seychelles in late January, as well as revised bases for tax collections following introduction of the VAT and a number of other taxes. As a result of the heavy rains, Government established a special Fund for donations from the international community. However, the fundraising is not expected to cover the total costs for damage and losses (estimated at $8 mil-lion by the World Bank), and it is anticipated that a certain level of expenditure will need to be incurred by the Budget. Moreover, the tax performance for the last two months of 2012 was less favorable than forecast at the time of preparing the 2013 budget, and consequently the base for the 2013 projections was revised downwards. Combined with a strong rupee this could negatively impact revenues. We are nevertheless committed to achieving a primary surplus in excess of 5 percent of GDP for the year.

We also remain strongly committed to our structural reform agenda. One of the key reforms under the program supported by the Extended Fund Facility—introduction of a Value Added Tax—was implemented on January 1, 2013. Besides a few teething problems the transition has been satisfactory. In terms of Public Finance Management, the reforms are on track and the Ministry of

Finance is on schedule for the introduction of new accounting manuals and procedures towards the middle of this year. In March, the Cabinet approved a policy for indexation of utility tariffs, as well as a roadmap for the re-balancing of tariffs to ensure the sustainability of the state-owned utility company. Implementation of this rebalancing exercise will begin on July 1 this year.

We have raised our net international reserves target because of the good performance of the export sector underpinned by strong inflows from tourism, and request modification of the end-June 2013 performance criterion. The Central Bank will accumulate reserves by opportunistically buying foreign currency such that the Bank's presence in the market does not influence the exchange rate level. Our target remains for gross official reserves to reach at least three months import cover by end-2013.

We will continue to implement monetary policy under the reserve money targeting framework. However, we intend to broaden our range of indicators for macroeconomic conditions in the short term so as to improve the transmission mechanism and make the monetary policy framework more flexible.

In line with the commitments made in the memorandum of economic and financial policies (MEFP) of November last year, we are confident of maintaining our course to achieve the objectives of the program. Nonetheless, we stand ready to take any further measures that may prove necessary to meet our objectives. We will consult with the Fund on the adoption of these measures, and in advance of revisions to the policies contained in the MEFP and this letter, in accordance with the Fund's policies on such consultations.

The eighth and final review under the EFF Arrangement based on performance criteria for end-June 2013 is expected to be completed on or after September 30, 2013.

In line with our commitment to transparency, we request that the IMF publish this letter, the attached technical memorandum of understanding (TMU), and the staff report for the seventh review and Article IV consultation. We will simultaneously publish these documents in Seychelles.

Sincerely Yours,

| | |
|---|---|
| /s/ | /s/ |
| Pierre Laporte | Caroline Abel |
| Minister of Finance, Trade and Investment | Governor |
| Republic of Seychelles | Central Bank of Seychelles |

## Attachment 1—Table 1. Quantitative Performance Criteria Under the Extended Arrangement, 2012–13 (millions of Seychelles rupees; end-of-period)

| | 2012 | | | | 2013 | | | |
|---|---|---|---|---|---|---|---|---|
| | December | | | | March | June | September | December |
| | Performance Criteria | Adjusted | Actual (prog rate) | Actual (market rate) | Indicative Target | Performance Criteria | Indicative Target | Indicative Target |
| **Performance criteria** | | | | | | | | |
| Net international reserves of the CBS, millions of U.S. dollars (floor) [1] | 223 | 224 | 234 | 235 | 227 | 236 | 234 | 241 |
| Reserve money (ceiling) | 1,920 | ... | 1,816 | ... | 1,950 | 1,980 | 2,010 | 2,040 |
| Primary balance of the consolidated government (cumulative floor) [2] | 837 | ... | 877 | ... | 136 | 412 | 684 | 785 |
| Contracting or guaranteeing of new external debt by the public sector (Millions of U.S. dollars; cumulative ceiling) [2] | 40 | ... | 36 | ... | 25 | 40 | 55 | 55 |
| Contracting or guaranteeing of new short-term external debt by the public sector (millions of U.S. dollars; cumulative ceiling) [2] | 0.0 | ... | 0.0 | ... | 0.0 | 0.0 | 0.0 | 0.0 |
| Accumulation of external payments arrears by the public sector (ceiling) [3] | 0.0 | ... | 0.0 | ... | 0.0 | 0.0 | 0.0 | 0.0 |
| Accumulation of domestic payment arrears by the government (ceiling) | 0.0 | ... | 0.0 | ... | 0.0 | 0.0 | 0.0 | 0.0 |
| ***Memorandum items:*** | | | | | | | | |
| Net external non-project financing (millions of U.S. dollars; cumulative) [2, 4] | -13.1 | ... | -12.3 | ... | -2.0 | -15.3 | -17.4 | -12.2 |
| External budget loans | 7.0 | ... | 7.0 | ... | 0.0 | 0.0 | 0.0 | 17.0 |
| Cash payments on foreign debt service | 25.1 | ... | 23.6 | ... | 2.0 | 15.3 | 17.4 | 32.1 |
| External budget grants | 5.0 | ... | 4.2 | ... | 0.0 | 0.0 | 0.0 | 2.9 |
| **Program accounting exchange rates** | | | | | | | | |
| SR/US$ (end-of-quarter) | 13.02 | ... | 13.02 | 13.00 | 13.02 | 12.80 | 12.80 | 12.80 |
| US$/Euro (end-of-quarter) | 1.29 | ... | 1.29 | 1.32 | 1.29 | 1.36 | 1.36 | 1.36 |
| US$/UK pound (end-of-quarter) | 1.62 | ... | 1.62 | 1.62 | 1.62 | 1.59 | 1.59 | 1.59 |
| US$/AUD (end-of-quarter) | 1.04 | ... | 1.04 | 1.04 | 1.04 | 1.04 | 1.04 | 1.04 |
| US$/SDR (end-of-quarter) | 1.54 | ... | 1.54 | 1.54 | 1.54 | 1.54 | 1.54 | 1.54 |

Sources: Seychelles authorities and IMF staff estimates and projections.

[1] The NIR floor is adjusted as defined in the TMU.

[2] Cumulative net flows from the beginning of the calendar year; includes external non-project loans and cash grants net of external debt service payments.

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

[4] Includes external non-project loans and cash grants net of external debt service payments.

## Attachment 2—Table 2. Structural Benchmarks, June 2012–13

| Measure | Target Date | Macroeconomic Rationale | Status |
|---|---|---|---|
| Commission and complete a study on optimal tariffs for utilities (4th Review MEFP, ¶51). | End-June 2012 | To ensure cost recovery and long-term sustainability of utilities. | Met. Final version received October 2012. |
| Cabinet approval of the Public Sector Investment Program to be used for the 2013 budget planning (4th Review MEFP, ¶28). | End-September 2012 | To improve efficiency of public finance management and planning in capital investments by costing capital projects over the entirety of their implementation phase. | Met. |
| Implementation of Electronic Clearing House system (5th Review MEFP, ¶38). | End-September 2012 | To improve transmission of monetary policy and reduce cost of financial transactions. | Met. |
| Introduce VAT. | January 1, 2013 | To modernize the tax system and remove tax distortions. | Met. |
| Cabinet approval of the action plan to rebalance utility tariffs. | End-March 2013 | To ensure cost recovery and long-term sustainability of utilities. | Met. |
| Cabinet approval of Financial Instructions and Accounting Manuals in line with new PFM Act and IPSAS standards (6th Review MEFP, ¶27). | End-June 2013 | To improve efficiency of public finance management. | |
| Approval of Leasing Bill by National Assembly (6th Review MEFP, ¶35).. | End-June 2013 | To improve access to credit. | |
| Implement the first step of the utilities tariffs rebalancing (6th Review MEFP, ¶11). | July 1, 2013 | To ensure long-term financial sustainability of utilities. | |

# Attachment 3: Technical Memorandum of Understanding

1. This technical memorandum of understanding presents the definitions of variables included in the quantitative performance criteria and indicative targets set out in the supplemental letter of intent (LOI), 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 performance criteria and indicative targets, and the benchmarks for 2013 are listed in Tables 1 and 2 attached to the LOI, respectively.

## I. QUANTITATIVE PERFORMANCE CRITERIA

### A. Net International Reserves of the CBS (Floor)

#### Definition

2. 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

3. 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

4. At each program test date, the quarterly 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

5. 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 (LOI Table 1). 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.

## B. Reserve Money (Ceiling)

### Definition

6. Reserve money is equivalent to currency issued and deposits held by financial institutions at the central bank (bank reserves), including those denominated in foreign currencies. Evaluation of performance of reserve money with respect to the program ceiling will be done at the program accounting exchange rate.

### Monitoring and reporting

7. For each program test date, the quarterly reserve money 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. Reports will be submitted to the IMF no later than two months after each test date.

## A. Primary Balance of the Consolidated Government (Cumulative Floor)

8. The 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 of the government and social security fund.

## B. Public External Debt (Ceiling)

9. The ceiling applies to the contracting or guaranteeing of new external liabilities by the public sector (including the central government, the CBS, and all public agencies and parastatals for operations that are not directly linked to commercial activities). The ceiling does not apply to the use of Fund resources, operations related to external debt restructuring; normal import related credits; purchases of treasury securities by nonresidents; or borrowing by parastatals in the conduct of normal commercial operations. The non-zero ceilings on the contracting or guaranteeing of external debt are to allow for normal public project finance and program support from multilateral institutions exclusively. Debt shall be valued in U.S. dollars at program exchange rates. A zero sub-ceiling on short-term external debt applies to the contracting or guaranteeing of short-term external debt by the public sector, with an original maturity of up to and including one year.

10. For the purposes of this performance criterion, the definition of debt is set out in Point 9 of the "Guidelines on Performance Criteria with Respect to External Debt in Fund Arrangements," attached to Executive Board Decision No.6230-(79/140), as amended. Debt is understood to mean a current, non 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 points in time; these payments will discharge the principal and/or interest liabilities incurred under the contract. The ceiling on contracting official and officially guaranteed external debt includes all form of debt, including:

a. loans, that is, 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);

b. suppliers credits, that is, 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,

c. leases, that is, 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 leasor retains title to the property. 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.

d. 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.

## C. External Arrears of the Public Sector

11. The nonaccumulation of arrears to external creditors will be a continuous performance criterion 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.

## D. Domestic Arrears of Government

12. The nonaccumulation of budget expenditure arrears will be a performance criterion under the program and will be measured on net basis from the beginning of a calendar year. Budget expenditure arrears are defined as the sum of (1) any invoice that has been received by a spending agency from a supplier of goods, services, and capital goods delivered and verified, and for which payment has not been made within the contractually agreed period, or in the absence of a grace period, within 30 days; (2) unpaid wages, pensions, or transfers, pending for longer than 30 days to domestic or foreign residents, irrespective of the currency denomination of the debt; and (3) debt service payment on domestic debt of the government or guaranteed by the government that has not been made within the contractually agreed period.

## II. DATA AND INFORMATION

13. 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)

- Reserve money.
- 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 two weeks from the end of the month):

- Consolidated government operations on a commitment basis and cash basis in the IMF-supported program format.
- The detailed revenues and expenditures of the central government and social security fund.
- Accounts of the public nonbank financial institutions.
- Import and export data from the customs department.
- Public debt report.
- Statements of Stabilization Fund operations
- Consolidated creditors schedule on domestic expenditure arrears of the government.

**Quarterly** (within a month from the end of the quarter):

- Financial statements of Air Seychelles

14. 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.

# Annex 1. Structural Reforms in Train or Planned

| Reform | Objectives and description | Status |
|---|---|---|
| | ***Business Climate*** | |
| One-stop shop for starting a business | At the Office of Registrar General. Provides a single point of entry which has resulted in a reduction in the estimated number of days to start a business to 3 days (from 39 days). At registration, a unique business registration number and tax identification number is issued. Outdated legal framework and manual processes preclude online registration; this will be resolved through modernization of the Companies Act (below). There are plans to extend the window to cover processes throughout the lifespan of a business entity. | Operational since August 2012.<br><br>Online version planned for 2013.<br><br>2014 |
| Elimination of requirement to use a notary or lawyer | Speed up the registration process and reduce cost. | Part of reform of Companies Act |
| On-line permit application for import/export | Facilitate international trade | |
| Modernization of the 1972 Companies Act | Revisions to 20 sections/provisions of the current Act. Aims to modernize in line with international best practices and support online registration and other e-government services. | Outline approved by Cabinet; drafting team is preparing the draft Bill. Submit to Parliament in May 2013. |
| E-payment for government services | Introduce electronic payment facilities for all government services, including tax payments. Objectives: Increase transparency; ensure fair treatment across firms and reduce opportunities for corruption; increase access to information; ensure payment security; reduce time and cost for the client; reduce staffing of government offices. | May 2013 |
| Commercial division within the Supreme Court and establishment of a mediation framework | Speed up the process by creating a separate docket. Commercial division has started operations. A new judge with the requisite experience will be appointed over the medium term (currently headed by the Chief Justice). Next steps include reforming insolvency laws (below) and establishing alternative dispute resolution mechanisms for commercial cases, including mediation. | Effective April 1, 2012 |
| Reform insolvency law | Introduce a modern insolvency law to replace the fragmented and outdated framework; facilitate business rescue and bankruptcy. | Cabinet memorandum for unified insolvency legislation approved. Submit to Parliament May 2013. |
| | ***Public Financial Management*** | |
| Program Based Budgeting | Objective: align resource allocation with policy priorities and increase efficiency of public service delivery. A new Chart of Accounts has been adopted for the 2013 budget featuring a functional classification of expenditure (in line with GFSM 2001). Other processes in the expenditure train have been automated (commitment control, recording and reporting of payables, cash planning). | 2014 pilot in Ministry of Education and Ministry of Natural Resources.<br><br>2015 full roll out. |

| Reform | Objectives and description | Status |
| --- | --- | --- |
| | ***Business Climate*** | |
| Implementation of new PFM Act | From January 2013, all accounting staffs in government are placed on MoF payroll and report to Comptroller General; they are posted to different ministries and departments.<br>Government Audit Committee created to advise Minister of Finance on governance and inefficiencies. | November 2012 |
| Strengthen oversight of public enterprises | Committee established to review investments by public enterprises | Appointed in May 2012, but yet to be operational |
| | State participation in 10 main public enterprises transferred to the Societe Seychelloise D'Investissement (SSI), responsible for strategic direction, objective setting and performance oversight of the publicly owned enterprises. | January 2013 |
| | Draft amendments to the Public Enterprise Monitoring Commission (PEMC). Revisions include the requirement to adopt International Accounting Standards within three years (applicable to all government departments and ministries), and mandatory reporting to PEMC (annual report and audited accounts). | Submitted to Cabinet in January 2013 and currently with Attorney General's office.<br>Submit to Parliament in 2013 |
| Raise utility tariffs to cost recovery, adopt an automatic price adjustment mechanism and begin tariff rebalancing | Objective: improve financial viability of Public Utility Company (PUC) and improve allocative efficiency. In October 2012, the government received the consultant's Tariff Reform Strategy. The authorities are developing an action plan to rebalance tariffs which is scheduled for Cabinet approval by end-March 2013; implementation of the first steps of the tariff rebalancing planned for July 1, 2013 (structural benchmark under the EFF). | Implement automatic price adjustment mechanism April 2013.<br>Begin rebalancing starting in July 2013 (planned for 7 years) |
| | ***Social Protection and Housing*** | |
| Reform of housing finance and the Housing Finance Company (HFC) | Split HFC functions: HFC restricted to lending; management of government housing passed to Property Management Company. | Completed |
| | Government is considering the recommendations in the TA report on improved targeting (Smart Subsidy). Focus on low income households and first-time buyers. | Submit suggestions to Cabinet in May 2013 |
| Title registration | Automate title registration to reduce the time needed to get a title which deters banks from providing housing finance. Objective: increase share of mortgages held by the private sector from 25 percent to 50 percent by 2015. | May 2014 |
| Implement Integrated MIS | Use means testing for all programs managed by the Agency for Social Protection (ASP). Integrate other benefits into the system to improve overall efficiency of the social assistance program and strengthen monitoring. | MoUs between ASP and five other Govt agencies signed in 2012 |
| | Perform automated cross-checks on beneficiary's declarations. | 2013 |
| Improve targeting | Change computation formula for total household income to include retirement pension and other social benefits used to assess social welfare eligibility. | ASP Act of 2012 |
| | Consolidate the Family Support and Home Carers programs into one means tested program. | Proposal will be submitted to Cabinet in April 2013 |
| | Strengthen monitoring of the sickness benefit, and analyze options for discouraging abuse of sickness benefit. | |

| Reform | Objectives and description | Status |
|---|---|---|
| | ***Business Climate*** | |
| Eliminate discretion in the administration of social assistance | Eliminate management discretion to determine eligibility if the income test is not met. Establish a Review Panel, with clear guidelines to assess appeals to ensure objectivity and transparency in the review process | ASP Act 2012 Operational.<br>300 cases reviewed and 25 approved. |
| Revise disability assessment criteria | Maximize return to work and promote social inclusion of people with disabilities. Adopt WHO International Classification of Functioning, Disability and Health (ICF). | Study tour in February/ March 2013; approval of guidelines May. |
| Ensure fiscal sustainability of pension system which is projected to deteriorate due to the ageing of the population | Increase incentives to contribute to the pension system after the vesting period and improve fiscal sustainability of the contributory pension system by gradually increasing contribution rate and improving benefit formula by tying benefits to years of contributions (accruals). | 1 percent increase in contributory rate from 2014.<br><br>Improved benefit formula in 2015. |

*Note: Structural reforms are also ongoing in the fishing sector and in the oil sector. In fisheries, activities focus on transparency and governance aiming to raise accountability to the Seychellois people. Regarding oil, exploration activity is at an early stage, but the government is reviewing the legal framework for the petroleum sector, and adopting EITI principles. PetroSeychelles (a new state-owned company) is charged with the supervision, monitoring, and investment in upstream activities. If and when extraction begins, an independent regulatory body will be established.*

Prepared by C. Baker and A. Culiuc with inputs from the World Bank

# Annex 2. Social Protection and Assistance

Seychelles has in place a comprehensive social safety net aimed at providing support to vulnerable groups, protecting people's incomes in their old age, ensuring a minimum standard of basic needs can be met, and helping specific groups meet specific costs (such as pensioners and students meeting the costs of transportation). The right to social protection is enshrined in the 1993 constitution, which also establishes the State's responsibility to "undertake and maintain a system of social security" and that all Seychellois have the right to "adequate and decent shelter". In 2007, social protection programs were further strengthened in order to mitigate the impact of economic restructuring. A strong social safety net is desirable given the country's high vulnerability to external shocks.

The social protection system comprises (Table A2.1): entitlement programs; discretionary cash and in-kind social assistance; and a cash transfer system to keep households above the "poverty line".[1] It also includes (i) a government built housing scheme in which houses are rented to "low-income" households (households with monthly income less than SR10,000 ($770) per month); (ii) a subsidized mortgage scheme which extends credit to "almost creditworthy" households (households with monthly income between SR10,000 and SR15,000); (iii) human capital development programs, such as the Skills Acquisition Program (for youth) and Skills Development Program; (iv) administered prices for 14 "basic" goods purchased through the Seychelles Trading Company; (v) subsidized LPG for residential use and electricity (both are in the process of moving to cost recovery); (vi) subsidized bus fares; and (vii) social programs provided by charitable organizations, including with public funds. Education is free and compulsory to 16 years of age, and there is universal free basic health care.

The benefits under the social protection system are quite generous and contribute to a high quality of life (rank 46 on the 2013 Human Development Index), but may negatively impact labor supply choices. For example, replacement rates (i.e., the amount received as a pension as a share of income received while working) under combined social security (SSF) and pension fund (SPF) for the average wage earner are 74 percent (somewhat above other middle income countries) while replacement rates for those earning half of the average exceed 100 percent, providing a disincentive to remain employed after age 60. The authorities have taken measures to get people off social assistance and back to work, through increased use of means testing and making registration with an employment agency a condition for receiving welfare. The generous benefits may also be negatively affecting other areas of the economy, including private sector participation in the housing and mortgage market (subsidies reach into the 70$^{th}$ percentile of the income distribution). The authorities are currently reviewing the housing subsidy and are seeking to implement policies to strengthen financial sector development.

[1]Seychelles does not have a national poverty line. The 2011 Living Conditions Survey conducted by the UNDP estimates the poverty line at about $3 per day per adult (SR 13,554 per year). The poverty rate is estimated at 17 percent of the population, with the incidence of poverty rising with household size. Poverty is higher in households led by unemployed heads, females and those with little education.

As of January 2013 there are approximately 14,000 people (16 percent of the population) receiving benefits under the SSF, about half of which are retirees earning an old age pension. Of the over 2,300 families receiving means-tested welfare payments, most are working poor with children, while unemployed households with no income comprise about 10 percent of welfare families.

Given their comprehensive nature, the total cost of social programs including the investment budget for housing construction and infrastructure exceeds 7½ percent of GDP. However, the cost of the social assistance program is more or less in line with comparator countries.

**Social programs, 2012**

| Program | SR million | percent of GDP |
|---|---|---|
| **Central Government budget** | **980.9** | **6.9** |
| Agency for Social Protection | 427.8 | 3.0 |
| Statutory benefits | 348.2 | 2.5 |
| Means-tested benefits | 79.5 | 0.6 |
| Other budgetary social programs | 140.6 | 1.0 |
| Social housing construction | 333.0 | 2.4 |
| **Seychelles Pension Fund** | **94.4** | **0.7** |
| **Grand total** | **1,075.3** | **7.6** |

The small population of Seychelles allows much better data management and tracking than is often the case. According to the World Bank Public Expenditure Review Selected Issues (2011), every citizen is issued a unique personal identification number at birth, all child births are registered, and death registries are up to date. Moreover, the IT system for the Agency for Social Protection is currently being upgraded to link databases of various ministries and agencies to cross check income and benefit information.

Prepared by A. Culiuc and C. Baker

**Table A2.1. Social Programs in Seychelles**

| Program | Cost in 2012, SR Million (share of GDP) | *Recipients in 2012, monthly ave.* | Social need addressed and/or purpose | Category | Description |
|---|---|---|---|---|---|
| **SSF programs** | **340.4 (2.4%)** | | | | Administered by Agency for Social Protection (formerly by the Social Security Fund). |
| Retirement Benefits | 211.3 (1.5%) | *6,900* | Provide income after statutory retirement age. | Perm., Univ. | All citizens 63 years and older with 5 years of residency.<br><br>Flat rate pension of SR2,550 up to 2,750 in 2013 per month (above official poverty threshold; about 35 percent of average wage). No formal adjustment criterion; informally indexed to CPI inflation.<br><br>Prior to June 2010, combined contribution rate of 22½ percent. This was eliminated in exchange for 15 percent payroll tax. |
| Invalidity Benefits | 33.53 | *1,100* | Income supplement to offset impact of disability. | Temp., Univ. | Full or partial. Benefit is conditioned on disability (as assessed by a Medical Board); capacity to undertake gainful employment or his-her actual income; and family income below the official subsistence minimum.<br><br>Capped at 2,580 in 2013 per month (2013). |
| Supplementary Benefits | 1.3 | *n/a* | Disaster relief assistance and covers foster care allowances. | Temp., Univ. | Provides assistance when natural disaster (e.g., fire, floods) strikes as a one off lump-sum payment not exceeding SR25,000 per household and other natural disasters.<br><br>Covers approved repatriation of bodies from other islands to Mahe and in rare cases from overseas.<br><br>Finances foster care. |
| Other Post Secondary Students Bursary | 3.9 | *178* | Post-secondary allowances. | | Allowance for students on apprenticeship schemes and those that have completed their advance level studies awaiting postings to universities. |

| Program | **Cost in 2012, SR Million** (share of GDP) | ***Recipients in 2012,*** *monthly ave.* | **Social need addressed and/or purpose** | **Category** | **Description** |
|---|---|---|---|---|---|
| Sickness Benefits | 7.48 | n/a | Partial offset of income for employed/self employed individuals as a result of sickness. | Temp., Means Tested | To qualify one must be in formal employment, claimed based on sickness certificates and covers up to 60 days continuous leave capped at SR 2,250 for 2013. After which period the person becomes eligible for invalidity benefit as per criterion above. |
| Maternity Benefits | 0.78 | n/a | Partial offset of income for employed/self employed individuals as a result of pregnancy. | Temp., Univ. | Payable 2 weeks prior to confinement to 12 weeks after delivery. Conditional on registering the pregnancy and childbirth.<br>80 percent of the mother's basic salary at the time of application, subject to a ceiling of SR2,250 for per month (2013). |
| Funeral Benefits | 0.85 | n/a | Partially offset funeral expenses borne by the family. | | Capped at SR1,600 and payable against receipts. |
| Survivors Benefits | 0.093 | n/a | Partial offset of income loss following death of principal breadwinner in the household. | | Flat rate (SR 2,250 per month) to spouse 45 years or older dependent on deceased spouse's income, and supplemented with dependents allowance for surviving children (SR 1,070 per child). |
| Orphans Benefits | 0.88 | 65 | Supplement income to care for an orphan. | | Application via district social worker for child still in school and under the age of 18 whose parents have both passed away or have been imprisoned. |
| Injury Benefits | 0.67 | 69 | Partial offset of income loss following injury at work. | | Similar to sickness benefit but illness as a result of work injury. |
| Home Carers Scheme and Family Support Scheme (to be merged) | 64.90 | 2,437 | Care for elderly in need of regular assistance. | Temp., Univ. | Homecare provider can be a family member. For family members, the scheme acts as a supplementary income. |
| Unemployment Relief Scheme | 0.26 | 13 | | Temp., Univ. | Being phased out. |
| Youth Training Scheme | 0.05 | 101 | | Temp., Univ. | Being phased out. |
| Specialized Children Treatment Scheme | 2.97 | 19 | Health care assistance. | Temp., Univ. | Covers overseas treatment of children: travel, medical and overseas accommodation fees. |

| **Program** | **Cost in 2012, SR Million** (share of GDP) | ***Recipients in 2012,*** *monthly ave.* | **Social need addressed and/or purpose** | **Category** | **Description** |
|---|---|---|---|---|---|
| Senior Citizens Support Scheme | 0.799 | n/a | Assistance for social housing projects. | Perm., Univ. | Provides financial assistance for the very most vulnerable to repair/renovate their house. |
| SPTC Travel Concessions | 24.63 | n/a | Free public transportation for seniors, disabled and children. | Perm., Univ. | Refund SPTC the full amount towards providing free bus fare for seniors, the disable and post-secondary students. Partial refund for Primary and Secondary students. |
| Dedicated Fund For School | 3.46 | n/a | Support to children in need at school. | Temp., Univ. | Provides non-financial support to students whom the School Head Teachers deemed to be vulnerable. Assistance varies from providing school meals to school amenities such as bags, shoes etc. |
| **Social Welfare Assistance** | **86.7** (0.6%) | Safety Net 1,647<br><br>Bursary 1,719 | Supplement household income up to the value of a basic consumption basket.<br>Covers Post-secondary student bursary which is universal and not means tested which varies from 750 for 1st year 850 for 2nd year and 950 for 3rd year students. | Temp., Means Tested | Awarded for periods of 3, 6 or 12 months and renewable if the need persists and the applicant has attempted to secure employment.<br><br>Household income thresholds: SR1,650 for the first adult; 70 percent for each additional adult and 50 per-cent for each child. In addition to benefits based on household size, benefits also include SR300 for utilities, SR300 for transportation (if needed to travel to work), SR300 for daycare for every child under 3½ years and housing expenses up to 20 percent of the wage.<br><br>Administered by Agency for Social Protection (formerly by the Social Welfare Agency). |
| **Seychelles Pension Fund programs** | **91.8** (0.7%) | | | | Administered by SPF, an independent public entity. |

| | | | | |
|---|---|---|---|---|
| Normal Retirement Benefit | 76.60 (0.5%) | 1,978 | Defined benefits scheme, mandatory for all private and public sector employees; voluntary for self employed. | Retirement age of 60 (mandatory retirement age 63); be a Seychellois citizen; have domestic residence of at least 5 years prior to retirement; and a contribution history of at least 25 years total or 10 years immediately preceding retirement. Option for early retirement without penalty at 55 years of age for government, parastatals and military.<br><br>Funded scheme (Funds inherited from predecessor, investment returns and transfers from the budget). End 2011 assets of about 7 percent of GDP. |

| | | | | |
|---|---|---|---|---|
| Normal Retirement Benefit | 76.60 (0.5%) | 1,978 | Defined benefits scheme, mandatory for all private and public sector employees; voluntary for self employed. | Retirement age of 60 (mandatory retirement age 63); be a Seychellois citizen; have domestic residence of at least 5 years prior to retirement; and a contribution history of at least 25 years total or 10 years immediately preceding retirement. Option for early retirement without penalty at 55 years of age for government, parastatals and military.<br><br>Funded scheme (Funds inherited from predecessor, investment returns and transfers from the budget). End 2011 assets of about 7 percent of GDP.<br><br>Contribution rate raised to 3.0 percent in 2012 (1.5 percent each for the employer and employee).<br><br>Replacement rate for average wage earner estimated 39 percent for vested retirees. |
| Permanent Incapacity | 9.21 | 299 | Payment to those incapable of work prior to reaching retirement age. | Paid for life after being certified by the Medical Board to be incapable of work before reaching retirement age of 60. |

| | | | | |
|---|---|---|---|---|
| Other SPF programs | 5.98 | 251 (2011) | | Include: Death Before Normal Retirement, Pre-Retirement Migration, Surviving Spouse Pensions, Children Pension, Death after Normal Retirement, Post Retirement Surviving Spouse Pension, Post Retirement Children Pension. |
| **Selected social and human capital development programs** | **140.6** (1.0%) | n/a | | Funded from Budget (other than SSF and Ministry of Education). Includes: Tertiary Education Training Fund, NIE Training Fund, NHRDC Training Fund, Children's Special Fund, and New Born Savings Scheme (through the Savings Bank). |

Prepared by A. Culiuc and C. Baker

# Annex 3. External Stability and Competitiveness

*A range of CGER-based methodologies indicates that the Seychellois rupee is broadly in line with fundamentals. A comparative analysis of external vulnerabilities, export performance and non-price indicators also suggest that Seychelles has remained competitive relative to peers.*

## A. Quantitative Analysis of External Stability

**Quantitative analysis, drawing on the IMF's CGER methodology, suggests that the real effective exchange rate is in line with equilibrium, albeit with sizable variation across methodologies.**[1]

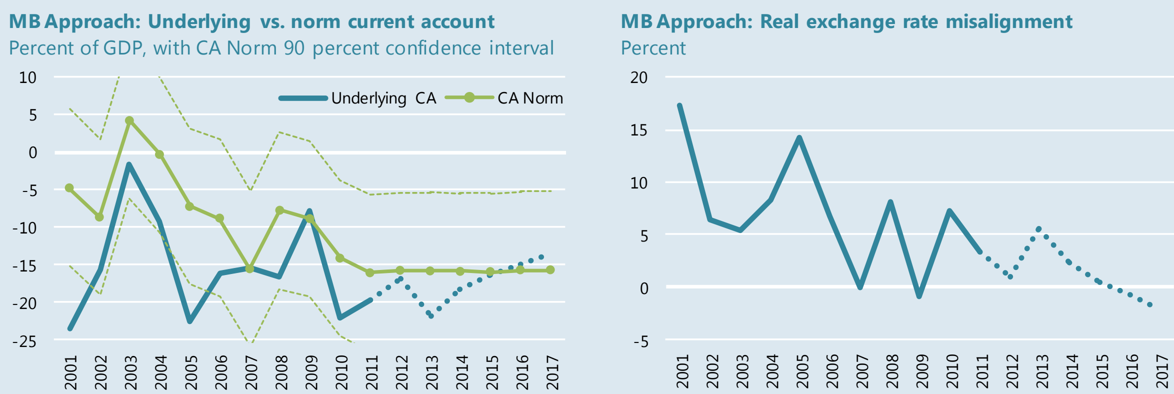
Estimated REER Misalignment [1]

| | 2012 | 2013 | 2017 |
|---|---|---|---|
| MB | 1.0 | 5.5 | -2.1 |
| ES | -0.6 | 4.2 | -3.6 |
| ERER | -20.9 | -17.1 | -16.6 |
| **Median** | **-0.6** | **4.2** | **-3.6** |

[1] Overvaluation (+); undervaluation (-)

**The Macroeconomic Balances (MB) approach shows that the underlying current account deficit has been tracking the equilibrium level (i.e., the norm) throughout most of the period, and has remained within the confidence interval since 2006**. Like most island economies, Seychelles has maintained a large current account deficit (average 16 percent of GDP 2001-12).[2] Since these large deficits have been largely driven by FDI-financed imports and some large one-off transfers, an underlying current account is estimated that strips out temporary surges in FDI and transfers. The estimated exchange rate is in equilibrium with a measured misalignment (overvaluation) of less than 6 percent in 2012–13 and a slight undervaluation over the medium term.

Figure A3.1. Macroeconomic balances approach results



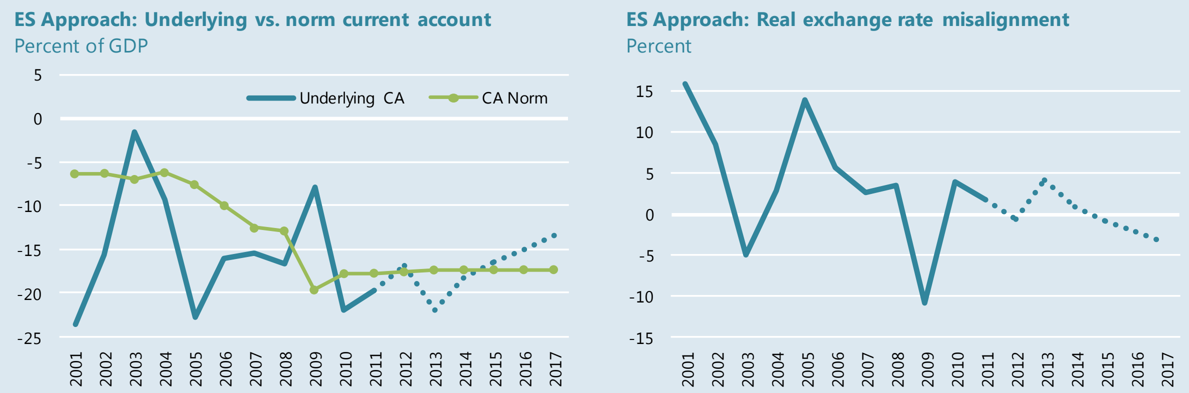

**The External Sustainability (ES) approach indicates that Seychelles' large current account deficits are in line with maintaining its highly negative NFA position at around 270 percent of**

[1] The analysis applies Seychelles-specific elasticities for calculating the relationship between current account gap and the necessary REER adjustment drawing on Tokarick, 2010 "A Method for Calculating Export Supply and Import Demand Elasticities".

[2] For more on the large current account deficits exhibited by small islands see, for example, Pineda, Cashin and Sun, 2009 "Assessing Exchange Rate Competitiveness in the ECCU".

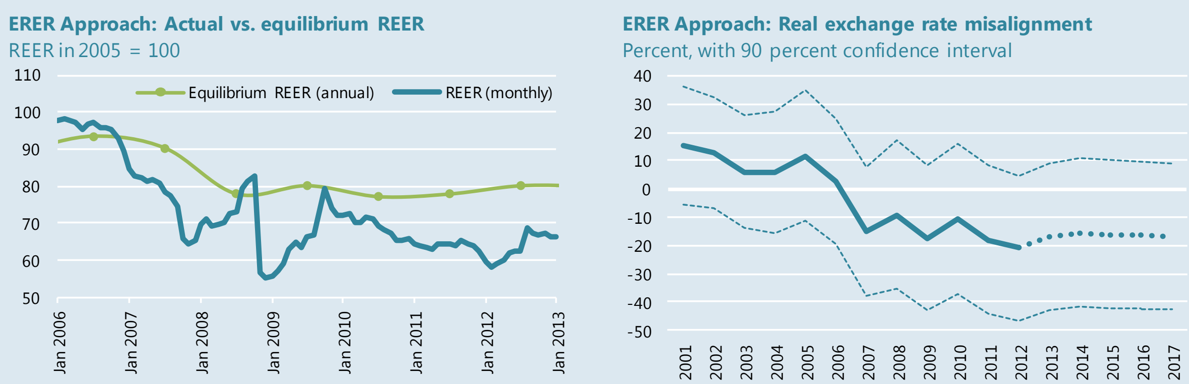
**GDP**. The measured exchange rate misalignment is modest and falls well within the confidence interval. Notwithstanding, it bears mention that there are inherent uncertainties in the measuring of NFA, especially in the case of an offshore financial center.

**Figure A3.2. External sustainability approach results**




**The Equilibrium Real Exchange Rate (ERER) results indicate that equilibrium exchange rate has remained fairly constant since 2009, resulting in a widening misalignment as the REER depreciated.** The estimated undervaluation is around 20 percent for both 2012 and 2013, although results still fall within the confidence interval. However, the methodology suffers from certain shortcomings. On the technical level, the ERER methodology relies on homogeneity assumptions across countries that are very diverse, and there are structural breaks in the series, such as Seychelles' move from a fixed to a floating exchange rate regime in late 2008. Moreover, the microstate experiences significant nominal exchange rate volatility and is subject to external shocks which quickly pass-through to inflation.

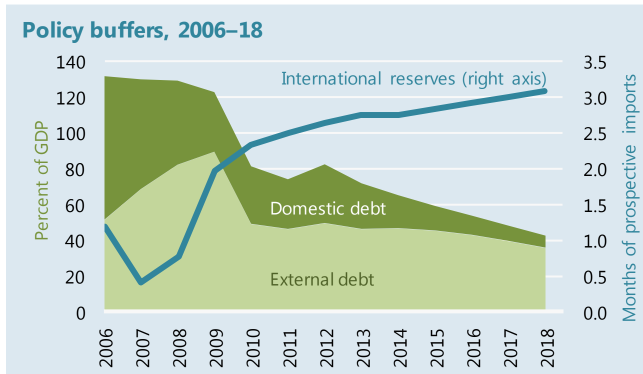
**Figure A3.3. Equilibrium real exchange rate approach results**



## B. Comparative Analysis

*In the absence of data on unit labor costs, a comparative analysis can be a useful complement to the external stability methods for assessing Seychelles' relative competitiveness. An analysis of external vulnerabilities, export performance and non-price indicators also suggests that Seychelles has remained competitive relative to peers.*

**External vulnerability is declining, but will remain high.** The large current account deficit is expected to narrow sharply over the medium-term as FDI and official grants taper off, and reserves are expected to gradually increase to 3 months of prospective imports in 2017. The projected current account is broadly in line with the estimated current account norm, and reserve coverage reaches the standard reserve metric for small states.[3] External debt has been reduced as a result of debt restructuring and is expected to fall below 50 percent of GDP as part of the government's policy to bring public debt to 50 percent of GDP by 2018 through sustained primary surpluses. However, the small and very open economy will remain vulnerable to external shocks.




**Export performance has been strong despite the challenging global environment, and prospects are supportive.**

- Goods and services export receipts grew by about 7½ percent per year (average) since 2005. Strong performance in tourism earnings and oil re-exports, averaging about 10 and 9 percent, respectively drive these findings. Export performance is expected to remain strong driven by tourism and tuna exports.

- Tourism has remained particularly robust (see annex 6), with Seychelles outperforming competitor markets despite the elimination of direct flights from Europe in early 2012 and it's branding as a high-end destination.[4] This reflects successful diversification toward non-traditional arrivals (Russia, the Gulf States, China) when traditional markets (France, Italy, Britain) faltered. There has also been some diversification of the tourism product, including through the land reclamation and development of villas, leading to an increase in the number of tourism units.

- Looking ahead, recent investments could expand export capacity. FDI and construction in the tourism sector (villas, some new hotels) may contribute to rising tourism revenues; the construction of cold storage facilities in train will support increased capacity and product

[3] Mwase, 2012 "How much should I hold? Reserve Adequacy in Emerging Markets and Small Islands" IMF Working paper WP/12/205.

[4] As a high-end destination, Seychelles ranks 120 (of 140) in terms of price competitiveness on the Travel and Tourism Competitiveness Index 2013, but remains competitive within the luxury category.

diversification by the tuna processing company (10 percent of GDP); and the recently-installed fiber optic cable could support growth in the financial services sector.

**Structural competitiveness indicators are also improving.** Seychelles climbed to 74$^{th}$ (of 185) in the 2013 World Bank' Doing Business ranking, and given structural measures underway is poised to climb further. In 2013, Seychelles took over the top spot among Sub-Saharan African countries in the Travel and Tourism Competitiveness Index and is ranked 38 (of 140) overall (Mauritius 58; Barbados 27). It also ranks favorably in Global Competitiveness and the Corruption Perception Index. However, greater effort could be made to improve other dimensions of competitiveness. Areas cited by the 2012/13 Global Competitiveness Report include access to finance, poor work ethic in national labor force and inadequate supply of infrastructure, while the Doing Business report notes challenges in starting a business, as well as access to credit and electricity.

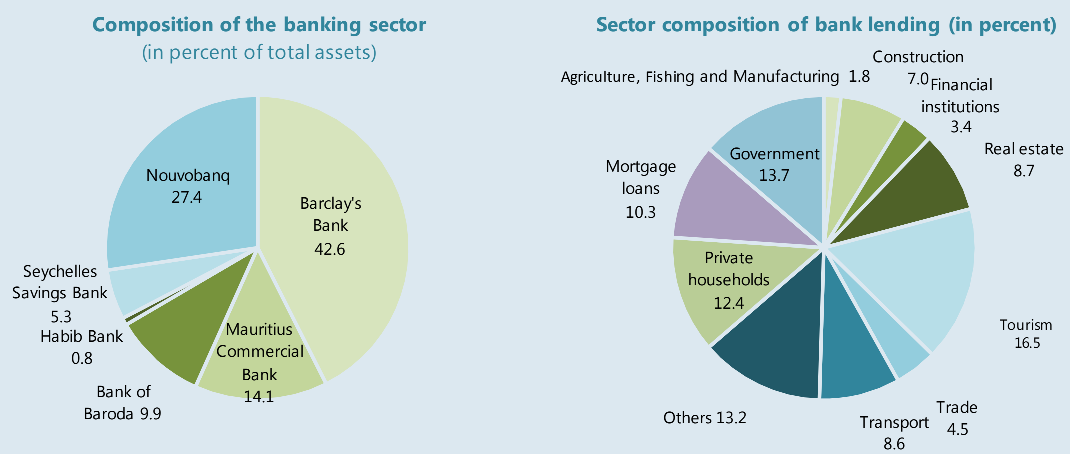
Prepared by N. Mwase and A. Culiuc

# Annex 4. Seychelles—Results of the Banking Sector Stress Tests

*The banking sector is well-capitalized, liquid and profitable. A recent uptick in nonperforming loans does not present systemic risk. Results of the stress tests show that the system is resilient to exchange rate risk, but less so to credit risk and interest-rate risk from maturity mismatches.*

**Background:** Seychelles' domestically operating banking system consists of six banks comprising total non-consolidated assets of about 104 percent of GDP. Four banks are foreign-owned and together account for 67 percent of banking system assets; two have a government-majority equity stake. The two largest banks account for 70 percent of the assets of the banking system. Banks' private-sector lending focuses on tourism, consumer credit to households, mortgage loans, real estate, transportation, and construction.

**Figure A4.1. Composition of Banking Sector and Lending**




Seychelles' banks have recovered well from the 2008 financial crisis, and their profitability and financial soundness indicators have largely improved in recent years. Since end-2011, the ratio of nonperforming loans to gross loans has hovered above 8 percent, as a consequence of two distressed loans. These claims are held by one institution, are fully collateralized, and no further provisioning is required.

**Stress tests:** The stress tests were conducted in February 2013 by the Central Bank of Seychelles' Financial Services Supervision Division using reported bank data from December 2012.[1] Three main risks were examined: *foreign-exchange risk* from exchange rate shocks; *credit risk* from a decrease in loan quality and from loan concentration through failure of the banks' largest borrowers; and

[1] In late 2010, the CBS conducted a stress test exercise in collaboration with the staff of the IMF Monetary and Capital Markets Department (Country Report No. 11/5, Appendix IV). Based on September 2010 data, the banking sector was found to be adequately capitalized, liquid and profitable. Notwithstanding a mismatch in asset/liability maturity, the banking system was deemed to be "reasonably resilient to risks".

*interest rate risk* operating through maturity mismatches of assets and liabilities.[2] A summary of the results is contained in table A3.1.

*Exchange rate shock*. Given its high degree of openness, Seychelles is vulnerable to exchange rate movements. Two types of shocks were examined: a foreign-exchange depreciation resulting from an unexpected external shock and a sharp appreciation of the Seychellois rupee.

- The depreciation scenario proved uninteresting given that banks hold long net open positions in foreign currency.[3]

- Two appreciation scenarios were then applied: (a) the maximum realized historical annual appreciation, and (b) an exchange rate shock of 2.58 standard deviations, equivalent to a 99.5 percent confidence interval of the data distribution and implying an appreciation of the rupee against the U.S. dollar by 20.3 percent. *Under no circumstances—including the most extreme shocks—did a single institution fall below the statutory capital adequacy ratio (CAR) of 12 percent.*

*Credit risk*. Three credit risk scenarios were run; all credit-default scenarios included provisioning requirements and their impact on capital and profit indicators. The first scenario covered an overall downward classification of pass loans into various lower-quality grades (special mention; substandard; doubtful; and loss), calibrated according to historical data. This scenario also assumed a 100-percent haircut on collateral values. Two additional scenarios focused on concentration risk and assumed that the largest or the five largest borrowers of each bank would default. *Under these scenarios, a few of the six banks would sink below the statutory minimum capital-to-risk weighted-assets ratio, but it would take the most extreme shock of five defaulting large borrowers to turn capital ratios negative*. Exposure to concentration risk is not unexpected for a small economy, but it underscores the importance of monitoring the financial health of large borrowers.

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[2]As Seychelles' banking system is characterized by excess liquidity, initial tests for *liquidity risk* did not yield any interesting results and were not pursued further.

[3] The indirect impact on loan portfolios operating through the balance sheet positions of borrowers could not be investigated for lack of data on net foreign-currency exposure from households and companies. Banks report that their internal risk-management guidelines prohibit lending to customers without foreign-exchange denominated income. But to the extent that such risks do exist, they would be captured by the credit-risk scenario.

**Table A4.1. Stress test results for total banking system (Q4-2012)**

(Percent, unless otherwise indicated)

| Scenario | RWCR [1] | ROE [2] | BbSCR [3] | BCAR<0 [4] |
|---|---|---|---|---|
| Actual | 26.7 | 26.0 | 0 | 0 |
| Historical exchange-rate shock | 26.4 | 25.1 | 0 | 0 |
| ER shock within 99.5 % confidence interval | 26.3 | 24.8 | 0 | 0 |
| Historically calibrated credit-default shock | 19.3 | 1.4 | 2 | 0 |
| Credit default by largest borrower | 21.1 | 6.7 | 1 | 0 |
| Credit default by five largest borrowers | 8.7 | -36.4 | 3 | 2 |
| Interest-rate shock | 18.0 | -0.8 | 2 | 0 |
| Combined shock | 1.0 | -57.9 | 4 | 3 |

[1] Risk-weighted capital ratio
[2] Return on equity (after taxes)
[3] Number of banks below statutory capital adequacy ratio
[4] Number of banks with negative capital adequacy ratio

*Interest-rate risk*. Interest-rate risk was tested by a maturity gap model which measures the differential effect of interest rate changes on the valuation of bank assets and liabilities arising from maturity mismatches. An interest shock of ten percentage points was applied on top of the actual interest rate of 10.6 percent. The results showed that *the system is somewhat vulnerable to maturity mismatches, with two banks falling below the statutory minimum CAR*.

**Combined shock.** Finally, a cumulative shock scenario was applied to combine the impacts of the 99.5 percent confidence-interval exchange-rate shock, the historically-calibrated credit-default shock, the failure of the largest borrower, and the interest rate shock. *A shock of this depth and intensity would turn capital ratios of three banks negative.* Perhaps more surprisingly, even under this extreme scenario two banks would remain (significantly) above the statutory minimum CAR.

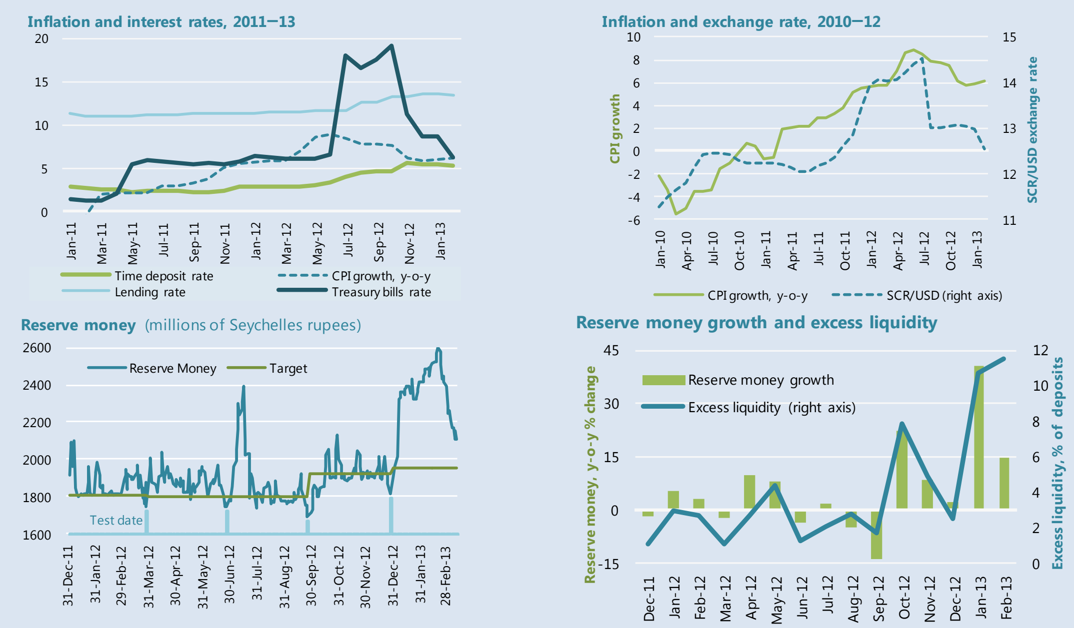
Prepared by T. Roy

# Annex 5. Monetary Framework and Challenges

*Since the adoption of a floating exchange rate in 2008, the Central Bank of Seychelles has anchored its monetary policy framework with a nominal target on reserve money (monetary base). But while monetary policy has successfully supported macroeconomic stabilization, reserve money targeting has come along with volatile interest and inflation rates.*[1]

**The link between monetary aggregates and inflation is weak, and monetary aggregates have displayed considerable volatility.** Reserve money targeting proved successful in establishing monetary discipline and bringing down inflation during the 2008 episode of high inflation. But the correlation between reserve money growth rates and inflation has been weak, particularly in the current low inflation environment, limiting the usefulness of reserve money as an indicator of future inflation or as a tool for achieving the inflation target. This is in part due to the large import share in the consumption basket and the robust pass-through from the U.S. dollar exchange rate to inflation with a relatively short lag. Moreover, the system has been characterized by rising structural excess liquidity, driven by an increase of the central bank's net foreign assets (NFA),[2] and the pass-through from short-term policy interest rates to the banking system's overall rate structure is weak. As a result, interest rates, reserve money, and bank liquidity became more volatile during 2012.[3]

**Figure A5.1 Recent monetary developments**




[1] In February 2013, a technical assistance mission by the IMF's Monetary and Capital Markets (MCM) department visited Victoria, on request by the authorities, and provided recommendations how to make the monetary policy framework both stronger and more flexible.

[2] The proportion of NFA to reserve money has increased from 43 percent (2008) to 190 percent (2012), leading to a sharp increase in sterilization costs.

[3] For more on the inflation-depreciation cycle of 2011–12, see Country Report No. 13/24, Box 1.

**Regardless of the ultimate choice of the nominal anchor, to make the monetary policy framework more effective it is first necessary to establish a functioning interest-rate channel.** This will require addressing the problem of structural excess liquidity through more durable sterilization (i.e., longer-term instruments), even if the cost ultimately needs to be borne by the central government budget. The removal of the liquidity overhang will help foster the interbank market and establish a short-term interest rate that can be targeted by the CBS to manage the supply of liquidity in the system.

**Establishing an interest rate channel should be done under the current reserve money framework, while working toward an eventual shift toward a flexible form of inflation targeting.** Key measures over the near- to medium term include:

- **Liquidity forecasts.** Enhance the CBS' capacity for liquidity forecasting along more extended time horizons.
- **Policy rate.** Establish a reference interest rate for a preferred policy instrument and decrease the number of auctions with commercial banks to achieve more market depth and to encourage interbank market operations.
- **Liquidity control.** Use the reference policy rate to target the level of bank reserves, consistent with the reserve-money target. As the interbank market develops, use central bank lending and deposit facilities to span an interest corridor for the money market rate.
- **Foreign-exchange interventions.** Given the relatively weaker policy transmission through the interest-rate channel, occasional direct interventions in the foreign-exchange markets can be a complementary tool for monetary policy. The CBS should communicate clearly that such interventions do not target a level of the exchange rate, rather are subordinated to monetary policy objectives.
- **Inflation as medium-term nominal anchor.** Clarify the operational meaning of the CBS' legal mandate for domestic price stability and formalize the inflation anchor that will replace reserve money. Decide on the most appropriate definition and measure of the CBS' target inflation rate, including the eventual use of an appropriate core index. Establish a target range for inflation to allow for flexibility against unforeseen shocks.
- **Monetary policy decisions.** Elevate the role of the CBS Board in monetary policy decisions. In the transition period, continue to target reserve money, but at a later stage, relegate reserve money to the role of an indicator for the monetary stance. Establish routines for regular communication of economic developments, their implications for inflation projections, and resulting monetary policy decisions to the general public.
- **Monetary analysis and inflation forecast.** Develop a set of high-frequency financial and real sector indicators for inflation factors. Investigate and determine the various transmission channels (exchange rate, interest rate, and credit) and corresponding time lags of monetary policy actions. Enrich the inflation forecast by including the impact of monetary policy variables and use the emergence of gaps between inflation forecast values and target values as input for monetary policy decisions.

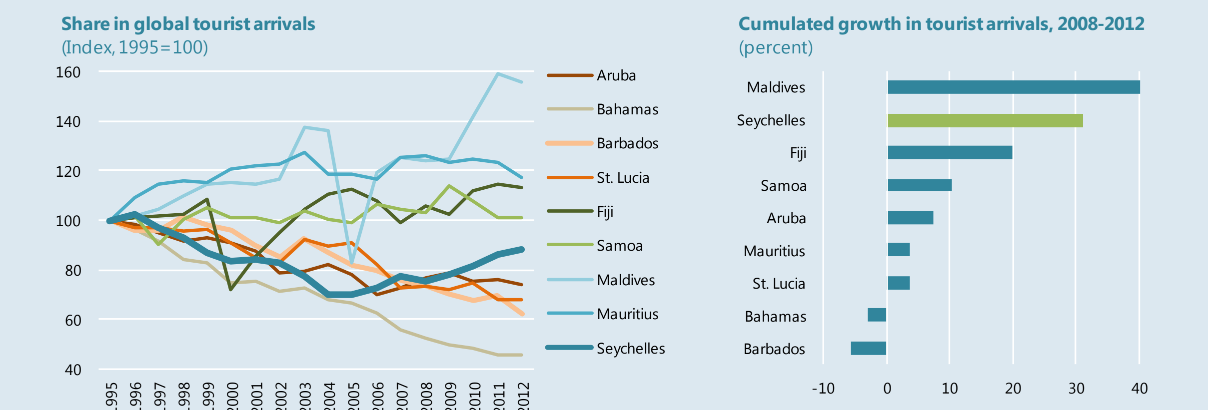
Prepared by T. Roy

# Annex 6. Tourism Competitiveness

*At around 30 percent of GDP, tourism is Seychelles' major export industry, as well as a potential channel through which external shocks affect the domestic economy. Seychelles has performed well, attracting nearly four times more tourists than predicted by a gravity-type model of tourism flows.*[1]

**Seychelles has fared better than other small island tourist destinations.** The country has been steadily rebuilding its share in global tourist arrivals over the last decade (figure A6.1, left chart), while most other small islands have seen flat (Oceania) or declining (Caribbean) shares. Seychelles' tourism industry has handled exceptionally well the years since the 2008 global crisis. Seychelles' tourist arrivals grew over 30 percent, while islands in the Caribbean have seen negative or negligible growth over the same period (figure A6.1, right chart). This success can be directly linked to Seychelles' ability to quickly diversify away from traditional European markets and its relative proximity to emerging sources of luxury destination tourists.

**Figure A6.1. Seychelles' Versus Other Small Islands: Growth and Share in World Tourism Flows**



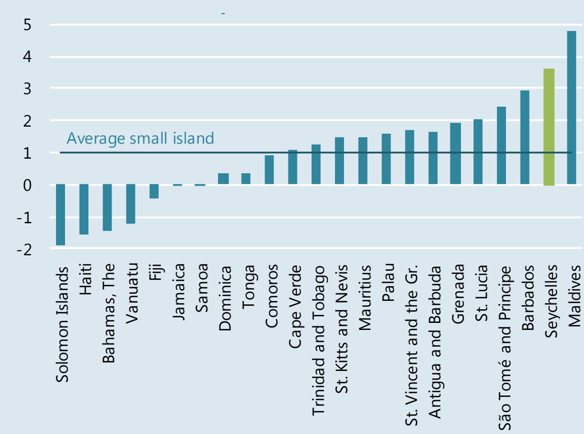

**Gravity model results show that Seychelles is highly competitive compared to other islands.** While comparing rates of growth and changes in global shares gives a useful indication of the country's tourism performance over time, comparing the *level* of tourism arrivals is complicated by the fact that tourism flows to each destination are subject to multiple objective factors, known in the traditional international trade literature as trade frictions. Some of these cannot be influenced by policies (at least not in a useful time frame), such as common borders, distances to main markets, bilateral cultural and historical ties. Accounting for and eliminating these effects allows construction of a ranking of countries' tourism competitiveness.[2] Seychelles is doing much better than most other

[1] Based on A. Culiuc "The Determinants of Global Tourism Flows", IMF Working Paper (forthcoming). The study is based on the application of the gravity model to a panel dataset containing the universe of bilateral tourism flows for 1999-2009, covering over 180 countries (underlying data from UNWTO).

[2] The computed competitiveness index is the value of the country dummy in a fixed effects regression with bilateral arrivals as explanatory variable and regressors including: GDPs of both countries, their population, areas, distances, price levels, geographical characteristics, common culture and history (language, colonial relationship).

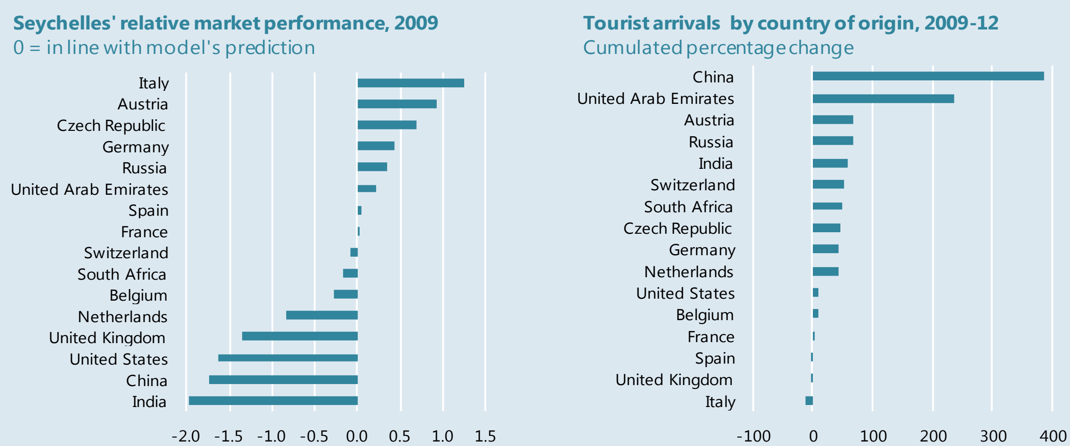
small islands with the sole exception of the Maldives (figure A6.2). Specifically, the country is receiving around 3.7 times more tourists than the model predicts for the average small island with Seychelles' characteristics.

**Figure A6.2. Relative Tourism Competitiveness Index for Small Islands**




**The results of the tourism gravity model also shed light on Seychelles' competitiveness on different markets.** The left chart in figure A6.3 plots the residuals (actual minus predicted values) for Seychelles' largest origin markets from a gravity model regression with fixed origin and destination effects. It shows that—after controlling for tourism trade frictions – Seychelles has been doing unusually well in select European markets. Interestingly, although France is Seychelles' largest market, the number of French tourists is precisely in line with the model's predictions. At the same time, the large measured underperformance in China and India helps explain the rapid growth registered on those markets since 2009 onwards (figure A6.3 right chart)—in other words, Seychelles was catching up to its potential level. However, growth was not limited to previously underperforming markets, as tourist arrivals from markets on which Seychelles already overperformed in 2009 grew by 40 to 70 percent in the three years since then (Austria, Czech Republic, Germany, Russia).

**Figure A6.3. Seychelles' Performance on top Origin Markets**



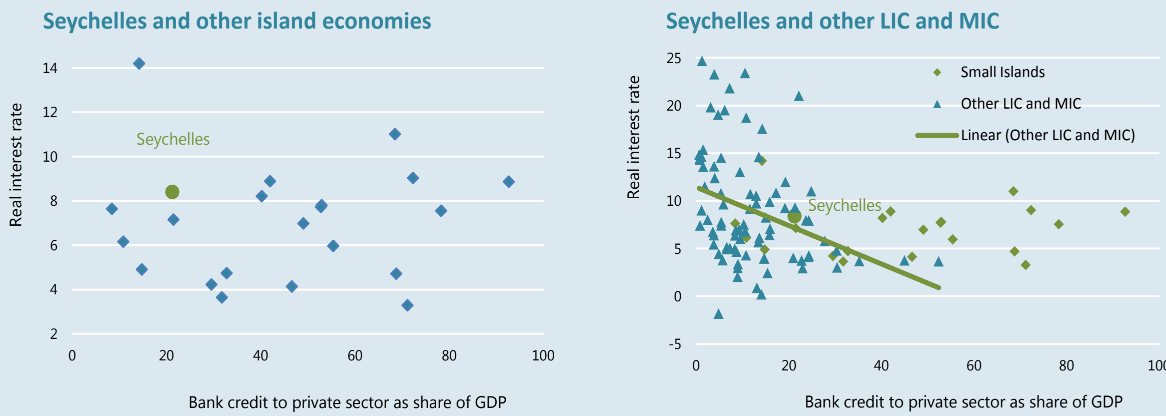
**The tourism industry represents an important channel through which Seychelles is exposed to the risks emanating from Europe.** To quantify the impact of the potential slowdown, one requires estimates of the elasticity of tourism arrival to GDP in tourist-originating countries. Using first differences regression, staff estimates the global elasticity of tourist-arrivals at around 1.3; it is however significantly lower (0.9) for small islands. Seychelles is therefore likely to see tourism demand from key European markets drop nearly one-for-one should their economies contract. Results also show that tourists are price sensitive; in response to a 1 percent appreciation in the bilateral real exchange rate arrivals and average nights-stay drop 0.11 and 0.27 percent respectively for a combined effect of 0.36 on total nights stayed. As recent experience shows, the negative impact of a short-term reduction in European arrivals could be offset by market diversification. However, if the shock were to prove protracted, maintaining high arrivals may only be possible through re-branding, involving steep discounting and lower tourist spending, which may prove detrimental in the long term to Seychelles' high-end reputation.

Prepared by A. Culiuc

# Annex 7. Cost and Availability of Bank Credit

**The financial system in Seychelles shares many characteristics with other small states, which limits its ability to support economic growth.** Some of these characteristics are a direct consequence of the limited market size, such as diseconomies of scale that hamper the supply of a broader range of financial services or shallow financial markets with few players. To some extent, these factors explain why small states are characterized by low availability of credit and high real lending rates relative to other low- and middle-income countries.[1] Among small-island economies, Seychelles' real lending interest rate is comparable to peers, although the availability of credit for the private sector—measured as bank lending to the private sector in terms of GDP—is somewhat low.[2]

**Figure A7.1. cost of Credit and Bank Lending in International Comparison**

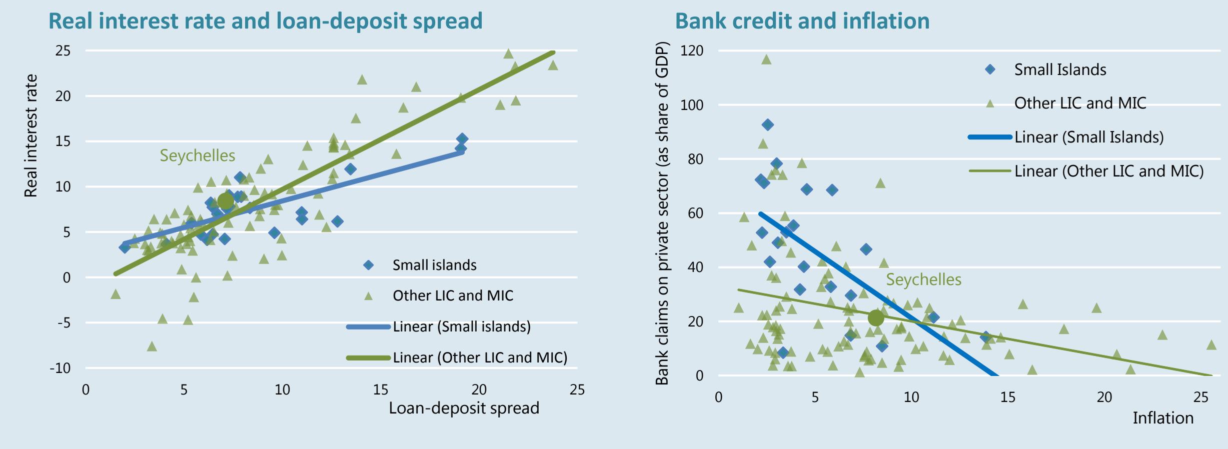



Comparing across countries, real lending rates are positively correlated with the spread between lending and deposit interest rates. Loan-deposit spreads reflect inefficiencies and costs of financial intermediation, such as limited competition in the banking sector, shallow financial markets, excess liquidity, weak banking supervision, and the level of nonperforming loans. There is also a pronounced negative correlation between the average level of inflation and bank credit to the private sector, both in small island economies and other low- and middle-income countries.

[1] In March 2013, the IMF Board discussed the paper "Macroeconomic Issues in Small States and Implications for Fund Engagement" http://www.imf.org/external/pp/longres.aspx?id=4745 .

[2] Beck, Demirgüç-Kunt, and Honohan ("Finance for All? Policies and Pitfalls in Expanding Access", 2008) include the ratio of private credit to GDP in their indicators of access to credit (table A.3, p. 194). More sophisticated indicators of access to finance are not available for Seychelles.

**Figure A7.2. Factors contributing to high costs of credit**



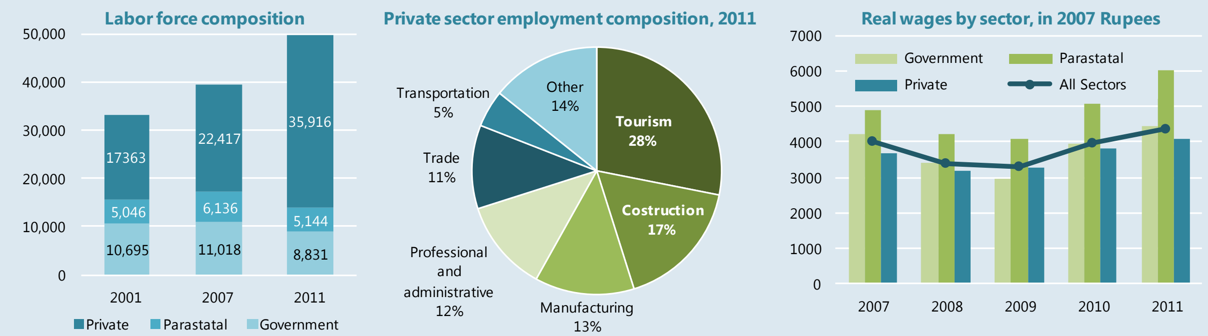

To improve access to and lower the cost of credit, policies in Seychelles should continue to counteract and mitigate some of the natural disadvantages that come with a small financial sector. For example, incentives and regulations should be geared toward fostering bank competition. There is also scope to continue to improve business conditions such as creditors' legal rights and to move bank supervision toward a forward-looking risk-based system. Taking steps to eliminate excess liquidity will lower the costs of financial intermediation, while a strengthened monetary framework that delivers on low and stable inflation is paramount to induce financial deepening and to promote access to credit.

Prepared by T. Roy

# Annex 8. Labor Market

The labor market in Seychelles is a dual market comprised of Seychellois and expatriate workers. It is characterized by high labor force participation by Seychellois (nearly 75 percent), predominantly in the formal sector. The private sector is the largest employer (tourism services, construction, tuna processing and light manufacturing) followed by government and parastatals. The government sets the minimum hourly wage (SR 21 ($1.62) in 2012). Key social partners in the labor market include the Seychelles Federation of Workers Union and the Association of Seychelles Employers. Unionization is relatively low (around 15 percent), and collective bargaining rare. In first half of 2012, the average monthly wage was SR 8,625 ($616).

**Figure A8.1. Labor Force Structure and Real Wages**




While unemployment statistics are weak, household surveys do not indicate a large unemployment problem. Survey-based data point to 2010 unemployment of 5.8 percent (2010 Census, versus 5.5 percent in the 2005 Labor Force Survey). Official estimates, which are based solely on registered job seekers on the three main islands, have historically been lower.[1] Measured youth unemployment is low, however the 2010 Census indicates that over 40 percent of all self-declared job seekers are aged 15–24. The typical job seeker is thought to be young, female, with primary and secondary education, although this may partly reflect the predominance of single mothers and the requirement to register with an employment agency in order to receive welfare and social benefits.

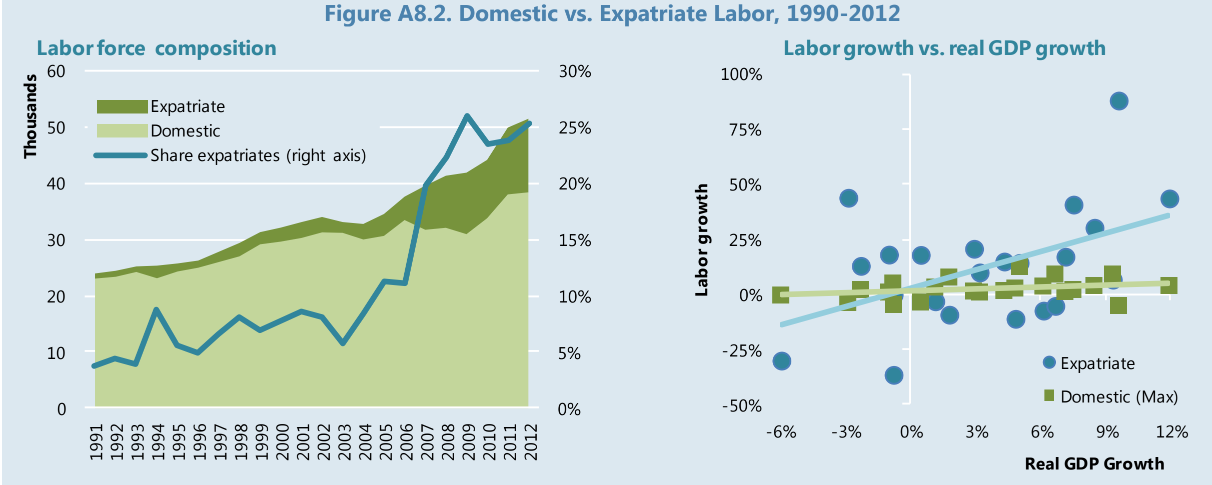
Jobs on offer exceed the number of people looking for a job in all job categories, indicating that domestic unemployment is mostly structural. A key factor is labor skill mismatch. Employment agencies report that job seekers lack qualifications, skills and experience—this is particularly the case for managerial and technical openings. The government has two programs aimed at placing participants in positions to receive on-the-job training and experience: the Skills Acquisition Program (SAP), targeted at 15–20 year olds who have dropped out of secondary school, and a Skills Development Program (SDP), targeted at post-secondary students who have dropped out of tertiary education or older job-career changers. Under both programs participants receive a monthly allowance (paid by government for the SDP and 60/40 government-employer for the SAP). Strengthening secondary education, especially in math and science, and transferring vocational training to the private sector may further serve to narrow the skills mismatch.

[1] Official statistics became highly unreliable following the 2009 transfer of the job placement service to the private sector, mostly as a result of job seekers registering with multiple agencies.

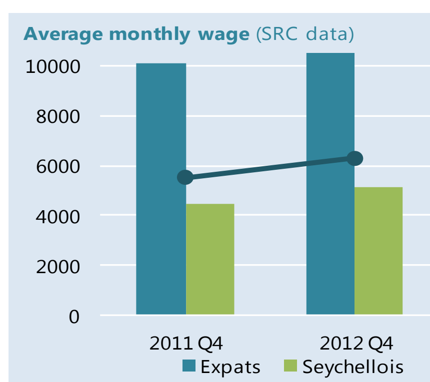
Other possible factors driving unemployment are the high reservation wage, and distaste for shift and factory work. Employers and employment agencies report that the ample social security system may provide a disincentive to enter the workforce and/or raise the reservation wage beyond the wage on offer. This is thought to be true for youth, who often prefer to rely on family networks for support than take available "undesirable" jobs (construction, fish processing, hotel shift work) and in some cases are unemployable due to substance abuse. In 2010, some 14 percent of youth aged 15–24 was neither in education nor in employment (2010 census). The labor ministry has also identified a phenomenon of "wait to work" in which labor identifies their preferred job and waits for it to become available rather than take a job presently on offer.

Data suggest that employment of Seychellois has remained stable during the recent growth episode. Between 2003 and 2011 (last year for which detailed labor data are available), the share of expatriates in total employment has increased from 6 percent to 26 percent (figure A8.2, left panel). This has been traced to a shortage of qualified local labor, especially in the construction sector (e.g., masons). Moreover, foreign labor growth is more strongly correlated with GDP growth than domestic employment growth (figure A8.2, right panel), suggesting that the private sector prefers to accommodate changes in demand by varying the number of expatriate workers.

**Figure A8.2. Domestic vs. Expatriate Labor, 1990-2012**




There are currently 13,800 expatriate workers in Seychelles. The typical expatriate worker is male (75 percent) between the age of 20 – 40 (75 percent) from Asia/Southeast Asia (India 50 percent). They work mostly in productive sectors (construction, fish processing) and tourism. Contracts are generally for two years, and extendable up to six years, provided that no Seychellois is qualified, willing and available to take up the position. A few years ago, employers in the hotel industry were given quotas for 15 years to cover their expatriate hiring needs.




According to the Seychelles Revenue Commission (SRC), the average total salary of expatriate workers is double that of Seychellois. In addition to the base salary, the employer pays all government fees related to expatriate employees, the airline ticket, and provides food and housing (or a supplement to cover these costs). Even when these additional costs are excluded from the comparison, base wages are reportedly often higher than for Seychellois workers in the same job category (no data available). Despite these higher costs, employers often prefer expatriate employees who are reportedly willing to work longer hours and may demand fewer benefits under the law.

Starting in 2013, approval of work permits has shifted from Immigration to the Ministry of Labor, with heightened vigilance over contracts and working/living conditions of non-Seychellois labor. The change in regulatory environment has led to uncertainty regarding the validity of the quota system and the ability of the tourism sector to hire needed foreign labor.

Prepared by C. Baker

**Box A8.1. Seychelles—Labor Market Legislation and Benefits**

The main acts regulating employment and industrial relations are:

- Employment Act 1995, as amended in 1999, 2006, 2007, 2008, 2009 and 2010;
- Conditions of Employment Regulations 1991, as lastly amended in 2006; and
- Industrial Relations Act.

The Ministry of Education, Employment and Human Resources (MEEHR) is responsible for labor issues through its Employment Department.

In August 2010, a tripartite Committee was formed to review the Employment Act with technical assistance from the ILO. In its Memorandum of Technical Comments on the Draft Amendments to the Employment Act of the Republic of Seychelles (February 2011), the ILO noted that the available version of the Employment Act currently in force contains some, but not all amendments adopted in previous years. Therefore, it is difficult for workers and employers to know their rights and obligations and hence comply with labor legislation.

Under the Employment Act, the same benefits and conditions apply regardless of contract type (i.e., continuous, fixed-term, part-time or casual):

- Benefits (Section 43): annual leave, maternity leave, sick leave, leave for the purpose of fulfilling or in connection with any civic duties, unpaid leave and maternity leave benefits.
- The Conditions of Employment Regulations (S.I. 34 of 1991) provide additional benefits, namely compassionate leave and education leave.
- Seychellois employees on continuous employment and fixed term contracts are entitled to 21 days paid annual leave (pro-rated if less than a year and for part-time employment).
- A casual worker who has worked for the same employer for 5 consecutive days is entitled to half of his day's pay in lieu of leave.
- Regarding compassionate leave (e.g., loss of a relative), leave in excess of 4 days in a period of 12 months may either be unpaid or, at the discretion of the employer, may be deducted from the worker's entitlement to annual leave.
- A worker shall also be allowed reasonable time off work, with or without pay at the discretion of the employer, to attend to matters which cannot normally be attended to except during the worker's working hours.

The Employment Act (Section 51) also sets out the procedures and costs related to redundancy. Employers must seek approval of MEEHR and go through a negotiation procedure. For workers under continuous employment contracts, severance pay is calculated at five-sixth of one day's wage for each completed month of service (pro-rated for part-time workers); the rate is double in the case of fixed-term contracts. Workers being made redundant shall be given one-half day leave per week during the notice period to enable them to secure employment. In the case that a worker does not agree to a change in the conditions of employment it is possible to fire the worker—the same severance payment applies. No severance is paid if the worker is fired outright.

The same terms and conditions of employment under the Employment Act apply to expatriate workers. Expatriate workers may also participate in the grievance (mediation) procedure and/or bring their case before the Employment Tribunal. However, anecdotal evidence suggests low compliance with labor laws regarding expatriates (who work longer hours and will not raise grievances), perhaps due to more limited understanding by workers of their rights under the law.

INTERNATIONAL MONETARY FUND

# SEYCHELLES

April 22, 2013

## STAFF REPORT FOR THE 2013 ARTICLE IV CONSULTATION, SEVENTH REVIEW UNDER THE EXTENDED ARRANGEMENT AND REQUEST FOR MODIFICATION OF PERFORMANCE CRITERION—INFORMATIONAL ANNEX

| Prepared By | Prepared by the African Department<br>(In consultation with other departments) |
|---|---|

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# RELATIONS WITH THE FUND

(As of February 28, 2013)

**Membership Status**: Joined 6/30/1977. Article VIII member since 01/03/1978.

| **General Resources Account** | SDR Million | % Quota |
|---|---|---|
| Quota | 10.90 | 100.0 |
| Fund holdings of currency | 36.66 | 336.35 |
| Reserve Position in Fund | 0.53 | 4.85 |

| **SDR Department** | SDR Million | % Allocations |
|---|---|---|
| Net cumulative allocation | 8.28 | 100.0 |
| Holdings | 6.37 | 76.90 |

| **Outstanding Purchases and Loans:** | | |
|---|---|---|
| Stand-by Arrangement | 6.49 | 59.54 |
| Extended Arrangement | 19.80 | 181.65 |

**Financial Arrangements**:

| | | | SDR Million | |
|---|---|---|---|---|
| Type | Arrangement | Expiration | Amount Approved | Amount Drawn |
| EFF | Dec 23, 2009 | Dec. 22, 2012 | 26.40 | 19.80 |
| Stand-By | Nov 14, 2008 | Dec. 22, 2009 | 17.60 | 11.00 |

**Projected Obligations to the Fund (SDR Million: based on existing use of resources and present holdings of SDRs):**

| | ***Forthcoming*** | | | | |
|---|---|---|---|---|---|
| | **2013** | **2014** | **2015** | **2016** | **2017** |
| Principal | 4.40 | 2.42 | 1.83 | 2.60 | 3.30 |
| Charges/interest | 0.21 | 0.22 | 0.21 | 0.19 | 0.16 |
| **Total** | 4.61 | 2.64 | 2.05 | 2.80 | 3.46 |

**Implementation of HIPC Initiative:** Not applicable

**Safeguards Assessments:**
The Central Bank of Seychelles (CBS) was subject to a safeguards assessment with respect to the Stand-By Arrangement for Seychelles. The assessment completed in 2008 found high risks in all areas of the CBS's safeguards framework, and several measures were included in the program. An update assessment in relation to the Extended Fund Facility, which was completed in July 2010, found that the authorities have implemented most of the measures recommended by the 2008 assessment. In particular, governance oversight at the CBS is now exercised by the Board and management committees, and transparency improved through application of International Financial Reporting Standards and the publication of financial statements that have been audited in accordance with international standards. The 2011 amendments to the CBS Act have strengthened the legal framework and the independence of the central bank. CBS governance has also been improved through continuous strengthening of the internal audit and control mechanisms. Given the recent augmentation of access under the EFF-supported program (approved December 17, 2012), the CBS is currently undergoing an update safeguards assessment.

**Exchange Rate Arrangement:**
The exchange market was liberalized in November 2008, which resulted in the elimination of all restrictions on the making of payments and transfers for current international transactions that are subject to Fund approval under Article VIII Sections 2, 3, and 4. The exchange rate regime is floating. On February 28, 2013 US$ 1 = SR 12.547 (mid rate).

**Article IV Consultations:**
Seychelles is currently under a 24 month consultation cycle.

**Technical Assistance (2011–March 2013):**

| Department | Head of Mission | Subject | Date |
|---|---|---|---|
| STA | Ms. Razin | External Sector Statistics | January 2011 |
| MCM | Mr. Sullivan | Central Bank Financial Reporting and Risk Management | February 2011 |
| FAD | Mr. Kloeden | Tax Reform | February 2011 |
| STA | Mr. Jones | Government Finance Statistics | March 2011 |
| MCM | Mr. Bartholomew | Central Bank Capacity Building | April 2011 |
| STA | Ms. Winston | Producer Price/Industrial Production Indices | April 2011 |

| Department | Head of Mission | Subject | Date |
| --- | --- | --- | --- |
| FAD | Mr. Ljungman | PFM Legal Framework | August 2011 |
| STA | Ms. Razin | External Sector Statistics | January 2012 |
| MCM | Ms. Radzewicz-Bak | Central Bank Capacity Building | March 2012 |
| AFS | Mr. Helis | PFM Regulatory Framework | March 2012 |
| MCM | Mr. Robotham | Payments System | April 2012 |
| FAD | Mr. Gillan | Customs administration | May 2012 |
| AFS | Mr. Panda | Basel I compliance | June 2012 |
| AFS | Mr. Ramachandran | PFM: Financial Management Information Systems and Chart of Accounts | June 2012 |
| FAD | Ms. Penfold | Revenue Commission training function | June 2012 |
| AFS | Mr. Mendes | Customs administration | July 2012 |
| AFS | Mr. Hughes | Quarterly national accounts | September 2012 |
| FAD | Mr. Le Leuch | Oil taxation regime | November 2012 |
| AFS | Mr. Hellis | PFM: Cash based IPSAS | November 2012 |
| MCM | Mr. Robotham | Payment Systems | December 2012 |
| AFS | Mr. Panda | Bank Supervision | January 2013 |
| MCM | Mr. Kovanen | Monetary Policy Framework | February 2013 |

**Resident Representative:** None

# JOINT WORLD BANK-IMF WORK PROGRAM, 2013

As of March 25, 2013

| Title | Products | Provisional timing of mission | Expected delivery date |
|---|---|---|---|
| | **A. Mutual Information on Relevant Work Programs** | | |
| **Bank** | **A. Strategy** | | |
| | Country Partnership Strategy – midterm review | To be determined | December 2013 |
| | **B. Lending Program** | | |
| | Second Development Policy Operation | May 2013 | September 2013 |
| | **C. Analytical work, Technical Assistance and Capacity Building** | | |
| | Public Expenditure Review Policy Notes: Education, Health and Public Investment Management | May 2013 | June 2013 |
| | Policy Note on Pension Reforms | May 2013 | December 2013 |
| | TA on Public Administration Reforms (PAR IDF) | March 2013 | December 2013 |
| | TA on housing finance strategy: re-defining the role of the Housing Finance Company, and designing housing subsidy and saving schemes | March 2013 | June 2013 |
| | TA on electricity tariff rebalancing and adjustment mechanism | March 2013 | June 2013 |
| | TA on Program Performance Based Budgeting | April 2013 | June 2014 |
| | TA on Financial Sector Development Strategy | To be determined | Ongoing |
| **Fund** | **A. Program and surveillance work** | | |
| | Article IV Consultations and Seventh Review under EFF | February 2013 | May 2013 |
| | Eighth Review under EFF | September 2013 | December 2013 |
| | **B. Technical assistance and capacity building** | | |
| | MCM technical assistance on reforming the monetary policy framework, strengthening technical capabilities of CBS' research and policy analysis divisions | Ongoing | Ongoing |
| | MCM/AFRITAC South technical assistance on strengthening | Ongoing | Ongoing |

| Title | Products | Provisional timing of mission | Expected delivery date |
|---|---|---|---|
| | bank supervision | | |
| | FAD/AFRITAC South technical assistance on tax and customs reform | Ongoing | Ongoing |
| | FAD/AFRITAC South technical assistance on the creation of the legal and regulatory framework for the implementation of the new Public Financial Management Act | Ongoing | Ongoing |
| | STA technical assistance on external sector statistics | Ongoing | Ongoing |
| | STA/AFRITAC South technical assistance on GDP and price statistics | Ongoing | Ongoing |
| | **B. Requests for Work Program inputs** | | |
| Bank request to Fund | Medium-term macroeconomic and fiscal framework to inform Public Expenditure Reviews and Development Policy Lending | n.a. | Ongoing |
| Fund request to Bank | Assist authorities in finalizing the tariff rebalancing plan | n.a. | March 2013 |
| | **C. Agreement on Joint Products and Missions** | | |
| Joint products | Joint mission in the context of the eighth review under the EFF to discuss a medium-term structural reform agenda focusing on: social safety net targeting; parastatal reform; and promoting private sector investment | September 2013 | December 2013 |
| | Joint technical assistance on natural resources taxation | Ongoing | Ongoing |
| | Joint Medium-Term Debt Management Strategy | n.a. | Ongoing |

# RELATIONS WITH THE AFRICAN DEVELOPMENT BANK GROUP

(As of December 31, 2012)

The African Development Bank Group commenced operations with the Republic of Seychelles in 1978 and has since approved 27 operations comprising 16 projects, seven studies, three lines of credit and one emergency assistance operation. There were no approvals between February 2000 and November 2006 when the country was under sanctions, except for an emergency assistance grant worth US$500,000 to deal with the Tsunami disaster in January 2005. Cumulative approvals as of December 2012 amounted to UA 94.51 million (about US$145 million).
An Interim Strategy Note (ISN) was approved by the Board on April 22, 2009. The ISN covered the period 2009 and 2010 and focused on a single pillar, namely supporting the Government's reform program to achieve sustainable growth. One of the successful operations implemented during the ISN was an unprecedented policy-based partial guarantee operation for US$10 million approved on December 12, 2009, in support of an exchange bond offered to external commercial creditors in the context of the public debt restructuring effort. The guarantee was instrumental in generating a high participation in the debt exchange offer. A Completion Report of the ISN undertaken in October 2010 noted that the Bank Group had maintained strategic responsiveness and flexibility, thereby ensuring success of its assistance.

Taking into account its performance, the lessons learnt and the Government strategy, the Bank prepared a full five year country strategy, which was approved by the Board in April 2011. The current Country Strategy Paper (CSP) covers the period 2011–15 and focuses on one pillar of support, "Strengthening Private Sector Development and Competitiveness", which is divided into three complementary sub-pillars; infrastructure development, enabling financing and regulatory environment, and human capacity development.

The lending program during this period includes an ICT project, the Seychelles East Africa Submarine cable amounting to US$12 million, a water and sanitation project amounting to €8 million, a mariculture development project, a line of credit, and an institutional support project. The Submarine cable project, which was financed in collaboration with the European Investment Bank (EIB), has since been successfully implemented with the project being completed in August 2012. In addition to the lending program, a non-lending program worth €2.9 million to be financed by the various Bank-managed Trust Funds and Technical Assistance Funds was proposed to be implemented during the CSP. The proposed non-lending programs are in the areas of Human Development, Regional Integration, Statistical Capacity Building, Infrastructure and Private Sector Development.

The Bank and the Government of Seychelles will undertake a mid-term review (MTR) of the CSP in 2013. The MTR will review progress made towards attaining the objectives of the CSP, assess whether the CSP pillar is still aligned with the government strategy and identify new developments in the country that might need to be incorporated in the remaining period of the CSP implementation.

# STATISTICAL ISSUES

Data provision has some shortcomings, but it is broadly adequate for surveillance. The country participates in the General Data Dissemination System (GDDS) since December 2006 and in government finance statistics modules of the Anglophone Africa project funded by the U.K. Department for International Development (DFID). Good progress has been achieved in improving statistical capacity, but sustained technical assistance and additional resources will be required for statistical development over the medium term in order to improve the quality of economic statistics. Seychelles is invited to a DFID-sponsored SDDS Workshop in Gaborone, Botswana during May 6–8, 2013, which focuses on selected Anglophone African countries that currently participate in the GDDS, but could be expected to either graduate to the Special Data Dissemination Standard (SDDS), or make significant progress toward this goal, within a three-year period.

**Real Sector Statistics**

National accounts data are prepared on a calendar-year basis with 2006 serving as the base year for constant price measures. In November 2012, the National Statistics Bureau (NSB) published new provisional national accounts estimates for 2011. There are considerable delays in compiling and disseminating volume measures of GDP estimates. The NSB is developing quarterly national accounts data for the period 2006-12; the estimates suffer from data source weaknesses, and so will continue to be produced, but not disseminated for at least the remainder of 2013. Once the annual estimates for GDP for 2012 are compiled (in the fourth quarter of 2013), annual and quarterly estimates will be reconciled for 2012; at this time experimental quarterly estimates may be published. Tourism statistics are compiled on a weekly and monthly basis. Production indicators are compiled quarterly, and both are reported to the IMF in a timely manner. Data on average earnings and employment by sector are collected on a quarterly basis by the NSB, but there are no data on unit labor costs. A new consumer price index (CPI) was introduced from October 2007. It utilizes expenditure weights derived from the household budget survey of 2006- 2007. The base period is July 2007.

**Government Finance Statistics**

Seychelles reports to STA the cash flow statements and financial balance sheet data based on the Government Finance Statistics Manual (GFSM 2001). Main recommendations of the 2011 GFS mission were: (i) establish a GFS task force among Treasury, Financial Planning and Control Division (FPC), Debt Management staff, and other relevant agencies to discuss and resolve technical and methodological issues; (ii) establish a strategic plan that specifies how to address weaknesses in terms of: (1) augmenting the cash recording of transactions in the execution of the budget with relevant accrual-based measures; (2) improving data on other economic flows for financial assets and liabilities; and, (3) addressing the lack of stock data on government holdings of nonfinancial assets, beginning with fixed assets and non-produced assets (lands).

**Monetary and Financial Statistics**

Monetary and financial sector data are reported regularly to STA for publication in the *IFS.* The analytical framework underlying the compilation of monetary statistics is generally sound. An integrated monetary database has been developed and is fully operational using the standardized report forms (SRF) for reporting monetary data to the Fund. The SRF-based monetary data have been published in the *IFS Supplement* since its March 2007 issue.

**External Sector Statistics**

The authorities have made substantial progress in adopting the methodology of the fifth edition of the *Balance of Payments Manual*. Annual balance of payments data are reported to the Statistics and African Departments nine months after the reference period, but provisional estimates are provided to missions earlier. Quarterly BOP data have been compiled since 2009, and are now publicly available. Merchandise trade data are reported on a quarterly basis. Considerable progress has been made in collecting and updating data on public sector external debt and debt-service and external payments arrears. Remaining priority areas include improving the coverage of external sector statistics and compiling international investment position.

**SEYCHELLES: TABLE OF COMMON INDICATORS REQUIRED FOR SURVEILLANCE**

(As of March 27, 2013)

| | Date of latest observation | Date Received | Frequency of data | Frequency of reporting | Frequency of publication |
|---|---|---|---|---|---|
| Exchange rate | 03/26/13 | 03/26/13 | Daily | Daily | Daily |
| International reserve assets and reserve liabilities of the monetary authorities | 03/22/13 | 03/26/13 | Weekly | Weekly | Monthly |
| Reserve money | 03/22/13 | 03/26/13 | Daily | Weekly | Monthly |
| Broad money | Dec. 2012 | 02/15/13 | Monthly | Monthly | Monthly |
| Central Bank balance sheet | 03/22/13 | 03/26/13 | Daily | Weekly | Monthly |
| Consolidated balance sheet of the banking system | Dec. 2012 | 02/15/13 | Monthly | Monthly | Monthly |
| Interest rates | Dec. 2012 | 02/15/13 | Monthly | Monthly | Monthly |
| Consumer price index | Feb. 2013 | 03/05/13 | Monthly | Monthly | Monthly |
| Revenue, expenditure, balance and composition of financing of the central government | Jan. 2013 | 03/25/13 | Monthly | Monthly | Monthly |
| Stock of central government and government guaranteed domestic debt | Jan. 2013 | 03/25/13 | Monthly | Monthly | Monthly |
| External current account balance | Dec. 2012 | 02/27/2013 | Quarterly | Quarterly | Quarterly |
| Exports and imports of goods and services | Dec. 2012 | 02/27/2013 | Quarterly | Quarterly | Quarterly |
| GDP | 2011 | Nov. 2012 | Annual | Annual | Annual |
| Gross external debt | Jan. 2013 | 03/25/13 | Monthly | Monthly | Monthly |
| International investment position | … | … | NA | NA | NA |

INTERNATIONAL MONETARY FUND
**Public Information Notice**

COMMUNICATIONS DEPARTMENT

Public Information Notice (PIN) No. 13/52
FOR IMMEDIATE RELEASE
May 15, 2013

International Monetary Fund
700 19th Street, NW
Washington, D. C. 20431 USA

**IMF Executive Board Concludes 2013 Article IV Consultation with Seychelles**

On May 8, 2013, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with Seychelles.[1]

**Background**

In the few years since the 2008 debt crisis, Seychelles has made remarkable strides, quickly restoring macroeconomic stability and creating room for private-sector activity. Macroeconomic developments in the tourism-based island economy have been favorable, despite the challenging global environment. Notably, growth held up as the tourism industry successfully attracted arrivals from non-traditional markets as European arrivals slumped, while a surge in foreign direct investment (FDI) supported construction in recent years. For the most part, inflation remained contained, and the external position improved markedly following liberalization of the exchange rate in 2008 and debt restructuring started in 2009.

In 2012, despite robust tourist arrivals, growth moderated to 2.9 percent as large investment projects were completed. Inflation spiked in July 2012 to 8.9 percent fueled by global as well as domestic developments, but has since abated as a result of successful monetary tightening. The external position continued to improve, albeit modestly. In particular, the current account deficit declined slightly, but remained high at around 22 percent of GDP, but was fully financed by FDI and external borrowing, leading to a modest rise in reserves. Debt restructuring is nearly complete, with only one loan agreement awaiting signature.

[1]Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summings up can be found here: http://www.imf.org/external/np/sec/misc/qualifiers.htm.

Fiscal policy in 2012 continued to support debt sustainability. The primary surplus is projected to have risen to 6.2 percent of GDP in part due to sizable windfall revenues which were partly saved. Buoyant revenue and grants paved the way for needed capital expenditure. Notwithstanding, public

debt increased by over 3 percentage points of GDP due mostly to currency depreciation and the government assuming liabilities of Air Seychelles.

Monetary policy was tightened sharply in 2012 in response to rising inflation and an unhinging of the exchange rate, and has since been relaxed. Starting in late-2011, rising global food and fuel prices coupled with adjustments in administered prices pushed prices higher. This was reinforced by current account pressures resulting from lower exports of transportation services in the wake of the restructuring of Air Seychelles. The looming inflation-depreciation spiral was broken in mid-2012 by two small foreign exchange market interventions by the Central Bank of Seychelles and a tightening of monetary policy. By end-2012, inflation had fallen to 5.8 percent and the exchange rate had strengthened beyond its end-2011 level.

Broad-based structural reform over the past five years has worked to improve financial performance of the public sector and increase private sector participation in economic activity. Statistical capacity continues to be strengthened. Seychelles subscribes to the IMF's General Data Dissemination Standard (GDDS) and is making progress at compiling higher frequency economic data which will support strengthened macroeconomic oversight and analysis.

**Executive Board Assessment**

Directors commended the authorities for their strong policy implementation. Macroeconomic stability has been restored and growth has remained resilient. While the outlook is favorable, the economy is vulnerable to an uncertain global environment and domestic risks. Directors called for continued commitment to sound policies and structural reforms to preserve macroeconomic and financial stability, build policy buffers, and foster strong and inclusive growth.

Directors welcomed the steps to improve financial discipline at the central government level and the recent introduction of the VAT. They agreed that strengthening the oversight and financial position of parastatals, including through adequate price mechanisms, and further progress in public financial management will be key to ensuring fiscal sustainability. For the medium term, Directors supported the authorities' fiscal policy stance which aims at targeting a primary fiscal surplus and reducing public debt to 50 percent of GDP. They welcomed that the debt restructuring is nearly complete and encouraged the authorities to exercise caution when contracting new external debt.

Directors called for continued efforts to improve the monetary framework in order to stabilize inflation expectations and policy interest rates. Absorbing excess liquidity over time will be important to strengthen the monetary anchor and monetary transmission mechanism. Directors considered that a further increase in international reserves, as market conditions permit, would provide a stronger buffer against shocks. Directors noted that the financial system is sound and welcomed the steps being taken to improve the functioning of the credit market.

Directors commended the efforts towards improving the business and investment climate, which is key to avoid a potential middle-income trap and to support broad-based growth. They encouraged the authorities to foster private sector-led growth by addressing infrastructure gaps, engendering lower cost and improved access to credit, correcting data weaknesses, and moving ahead with plans for greater workforce education and capacity building.

**Table 1. Seychelles: Selected Economic and Financial Indicators, 2010–14**

| | 2010 Actual | 2011 Actual | 2012 Est. | 2013 Proj. | 2014 Proj. |
|---|---|---|---|---|---|
| | (Percentage change, unless otherwise indicated) | | | | |
| National income and prices | | | | | |
| Nominal GDP (millions of Seychelles rupees) | 11,74 | 13,119 | 14,145 | 15,292 | 16,461 |
| Real GDP | 5.6 | 5.0 | 2.9 | 3.3 | 3.9 |
| CPI (annual average) | -2.4 | 2.6 | 7.1 | 4.5 | 3.4 |
| CPI (end-of-period) | 0.4 | 5.5 | 5.8 | 4.3 | 3.1 |
| GDP deflator average | -3.6 | 6.4 | 4.8 | 4.6 | 3.6 |
| | (Percentage change, unless otherwise indicated) | | | | |
| Money and credit | | | | | |
| Credit to the economy | 21.4 | 6.2 | 2.5 | 13.0 | ... |
| Broad money | 13.5 | 4.5 | -2.3 | 0.1 | ... |
| Reserve money | 34.7 | -2.7 | 6.9 | 12.3 | ... |
| Velocity (GDP/broad money) | 1.6 | 1.7 | 1.9 | 2.1 | ... |
| Money multiplier (broad money/reserve money) | 4.2 | 4.5 | 4.1 | 3.6 | ... |
| | (Percent of GDP) | | | | |
| Savings-Investment balance | | | | | |
| External savings | 23.0 | 22.7 | 21.7 | 23.2 | 18.4 |
| Gross national savings | 13.6 | 12.4 | 17.3 | 15.1 | 15.5 |
| *Of which*: government savings | 7.8 | 10.6 | 14.3 | 12.1 | 11.0 |
| Gross investment | 36.6 | 35.1 | 39.0 | 38.2 | 33.8 |
| *Of which*: government investment | 8.6 | 8.1 | 12.0 | 9.2 | 7.8 |
| Government budget | | | | | |
| Total revenue, excluding grants | 34.1 | 35.8 | 37.6 | 36.4 | 35.6 |
| Expenditure and net lending | 32.5 | 35.7 | 40.2 | 38.5 | 36.0 |
| Current expenditure | 27.2 | 27.6 | 28.8 | 28.8 | 27.3 |
| Capital expenditure and net lending | 5.3 | 8.1 | 11.4 | 9.8 | 8.7 |
| Overall balance, including grants | 2.5 | 2.5 | 2.4 | 1.8 | 2.0 |
| Primary balance | 8.6 | 5.4 | 6.2 | 5.1 | 4.4 |
| Total public debt | 81.6 | 74.3 | 77.3 | 72.0 | 65.3 |
| Domestic[1] | 32.5 | 28.0 | 27.7 | 25.7 | 18.6 |
| External | 49.1 | 46.2 | 49.6 | 46.3 | 46.7 |
| | (Percent of GDP, unless otherwise indicated) | | | | |
| External sector | | | | | |
| Current account balance including official transfers | -23.0 | -22.7 | -21.7 | -23.2 | -18.4 |
| Total stock of arrears (millions of U.S. dollars) | 30.3 | 9.0 | 2.7 | ... | ... |
| Total public external debt outstanding (millions of U.S. dollars) | 478 | 490 | 512 | 558 | 597 |
| (percent of GDP) | 49.1 | 46.2 | 49.6 | 46.3 | 46.7 |
| Terms of trade (= - deterioration) | -6.7 | -6.4 | -0.4 | 0.6 | 1.2 |
| Real effective exchange rate (average, percent change) | 4.4 | -7.4 | ... | ... | ... |
| Gross official reserves (end of year, millions of U.S. dollars) | 254 | 277 | 305 | 317 | 326 |
| Months of imports, c.i.f. | 2.3 | 2.5 | 2.6 | 2.7 | 2.7 |
| Exchange rate | | | | | |
| Seychelles rupees per US$1 (end-of-period) | 12.1 | 13.7 | 13.0 | ... | ... |
| Seychelles rupees per US$1 (period average) | 12.1 | 12.4 | 13.7 | ... | ... |

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

[1] Excludes debt issued in 2012 for monetary purposes (5.4 percent of GDP), as proceeds are kept in a blocked account with the Central Bank.

INTERNATIONAL MONETARY FUND EXTERNAL RELATIONS DEPARTMENT

Press Release No. 13/159
FOR IMMEDIATE RELEASE
May 8, 2013

International Monetary Fund
Washington, D.C. 20431 USA

**IMF Executive Board Completes the Seventh Review Under the Extended Fund Facility (EFF) for Seychelles and Approves US$5.0 Million Disbursement**

The Executive Board of the International Monetary Fund (IMF) today completed the seventh review of Seychelles' economic performance under a program supported by the Extended Fund Facility (EFF).[1] Completion of the review permits the immediate disbursement of SDR 3.3 million (about US$5.0 million), bringing total disbursements under the four-year arrangement to SDR 23.1 million (about US$34.9 million). At the same meeting, the Executive Board also concluded the 2013 Article IV Consultation with Seychelles, details of which will be published in due course in a Public Information Notice

The Executive Board approved a three-year EFF arrangement for Seychelles in December 2009 in an amount equivalent to SDR 19.8 million (then about US$31.1 million—see Press Release No. 09/472). The arrangement was extended by one year in December 2012 to support the country's economic reform program, with an augmentation of access of SDR 6.6 million (about US$10.0 million)—equivalent to 60.6 percent of Seychelles' quota.

Following the Executive Board's discussion of Seychelles, Ms. Nemat Shafik, Deputy Managing Director and Acting Chair, made the following statement:

"The authorities' strong commitment to macroeconomic stability has helped the economy overcome the 2008 balance of payments and debt crisis, and return to a path of continued growth, low inflation, fiscal surpluses, and declining debt. While the outlook is benign, the economy remains vulnerable to an uncertain global environment. Going forward, policies and structural reforms should aim at preserving macroeconomic and financial stability, raising policy buffers, and fostering stronger and inclusive growth.

[1] Assistance under the EFF can be provided to help countries facing serious medium-term balance of payments problems because of structural weaknesses that require time to address. Assistance under the EFF features longer program engagement—to help countries implement medium-term structural reforms—and a longer repayment period. (See http://www.imf.org/external/np/exr/facts/eff.htm). Details on Seychelles' current arrangement are available at www.imf.org/seychelles.

"The authorities have made important strides toward improving financial discipline at the central government level. To ensure fiscal sustainability, it will be critical to strengthen the oversight and financial position of parastatals and to make further progress in public financial management. For the medium term, the government is rightly targeting a primary fiscal surplus of around 5 percent of GDP in order to reach the goal of reducing public debt to 50 percent of GDP by 2018. The debt restructuring is largely completed, and caution should be exercised when contracting new external debt.

"On monetary policy, durably removing excess liquidity is the needed first step toward strengthening the monetary transmission mechanism, and will require a transparent and credible mechanism to cover the fiscal cost of sterilization. A further increase in the reserve coverage would provide a stronger buffer against shocks.

"Structural reforms should aim to deepen markets and to foster inclusive and broad-based growth. Recent improvements in the business climate are welcome. Stronger efforts towards broadening access to credit, enhancing infrastructure, addressing data weaknesses, and reducing skills mismatches in the labor market would further facilitate private sector development."

**Statement by Mr. Jong-Won Yoon, Executive Director for Seychelles and Ms. NghiLuu, Senior Advisor to Executive Director May 8, 2013**

Our Seychellois authorities' unwavering commitment to the economic reform agenda has yielded impressive results. Past reform efforts continue to bear fruit and have helped position the economy towards a strong and sustainable growth path. Seychelles, however, remains highly vulnerable to external shocks, due to its reliance on tourism and imports, which are inherent features of its economy. To ensure that macroeconomic stability is maintained, the government is determined to build adequate buffers to mitigate downside risks, address structural impediments to growth and to maintain prudent macroeconomic policies in accordance with program targets.

## Economic Development and Outlook

Despite challenging economic conditions last year, the Seychellois economy remained resilient, achieving real GDP growth of 2.9 percent in 2012. A tightening in monetary policy to cope with high inflation, coupled with a slowdown in tourism from traditional European markets led to a moderation in growth.

There are promising signs that economic activity has picked up in the first few months of 2013, underpinned by a fall in inflation and a strong recovery in tourism. Seychelles has managed to successfully diversify and expand into new tourist markets. The tropical cyclone which hit Seychelles in January is expected to have a small adverse effect on GDP, with reconstruction activity offsetting some of the impact. While the budget is expected to incur some of the recovery cost, we believe the objective of achieving a primary surplus of 5 percent of GDP can still be met this year.

Prospects for Seychelles over the near and medium term are favorable, as the economy has responded well to the economic reform program. The Seychellois economy is expected to gain momentum over the next two years as inflationary pressure abates and benefits of recent reforms begin to materialize. Real GDP growth is forecast to grow around 3.3 percent in 2013 and 3.9 percent in 2014. Investment is expected to peak over this period, and unemployment and inflation are expected to remain low.

The current account deficit is expected to narrow as FDI moderates from the strong flows experienced in recent years and international reserves are forecast to remain above the risk-weighted reserve metric over the medium term, but slightly below three months of import coverage. The Central Bank of Seychelles (CBS) will remain attune to favorable conditions for reserve accumulation, to meet the government's objective of rebuilding buffers.

## Fiscal Policy

The authorities' strong commitment to achieving fiscal surplus is an important source of stability for the economy. The good fiscal performance has also added credibility to the task of bringing public debt down to 50 percent of GDP by 2018, which remains well on track. The government's objective is to run primary surplus of around 5 percent of GDP per year over the medium term.

Our government is maintaining tight control over spending, including through the establishment of the Public Enterprise Monitoring Commission (PEMC). The PEMC will assist in strengthening the oversight of parastatals and will lead to greater compliance with reporting requirements. Our authorities share staff's assessment that improving the financial performance of parastatals will be important for fiscal sustainability.

Efforts to strengthen public financial management are being complemented by broader public sector reforms. Most notably, the preparation of the financial instructions and accounting manuals related to the Public Financial Management Act and the compilation of data under the new Chart of Accounts. The central government's decision to adopt program-based budgeting will strengthen PFM practices, and this initiative will be developed with technical assistance support from donors.

**Monetary Policy**

Inflation remained elevated in 2012, but has been on a downward trend over the past 8 months as a result of central bank intervention, rupee appreciation, and a moderation in food and commodity prices. The introduction of the VAT in January 2013 led to a temporary pick-up in inflation, which was offset by an appreciation of the rupee, which is currently at its highest level in more than three years.

Seychelles has been susceptible to bouts of liquidity overhang, with excess liquidity emerging again as a key challenge for the central bank at the start of 2013. To absorb the excess liquidity, our government is considering the possibility of issuing longer term instruments. While the adoption of reserve money target as a nominal anchor for monetary policy has played a useful stabilizing role in the period following the floating of the exchange rate in 2008, its effectiveness as a guide for inflation expectations is currently being reviewed.

The CBS recognizes the limitations with the current framework for monetary policy and that a more flexible regime is needed to achieve the central bank objective of domestic price stability. Strengthening the monetary framework and improving the monetary transmission mechanism will give the CBS more control over liquidity management and more flexibility in implementing monetary policy. Our authorities appreciate the technical assistance provided by MCM in February to strengthen the monetary policy framework and to begin work on establishing an alternative operational target. The central bank concurs with staff's recommendation that establishing a reference interest rate is an important first step. Authorities also took strong note of staff's advice that regular public communication of economic conditions and monetary policy decisions is crucial to establishing central bank credibility, transparency, and to anchor inflation expectations.

Steps are also being taken to improve the functioning of the credit market and the banking sector. The CBS is monitoring credit and price developments closely, and continues to make good use of technical assistance from the IMF. Open and frank dialogue between the Ministry of Finance and the CBS on financial reform is continuing regularly. At the same time, our authorities will continue to work with commercial banks to strengthen the financial sector and to create a competitive business environment to foster growth in small and medium enterprises. The recent establishment of the stock exchange should also support the development of the private sector.

**Structural Reform**

The Seychellois economy has achieved impressive results from extensive reforms pursued over the past few years, but the structural reform process is not yet complete. Maintaining the momentum on reform is important to the Seychellois Government and will help consolidate the recovery from the 2008 crisis. Ensuring continuity and discipline in policy making are key ingredients for the longer term success of the economy.

The government has been proactive in progressing key reforms while cognizant of the constraints faced by small, open and remote economies. As highlighted in the staff report, the unique features of microstates can make it difficult to develop significant depth and competition in the financial sector. Nonetheless, Seychelles scored well in the 2013 Doing Business indicators and investor confidence in Seychelles remains strong, as evident by the ongoing strong inflow of FDI.

The authorities' structural reform agenda is focused on: strengthening PFM, improving the financial discipline of the public sector and public enterprises, transitioning towards a more flexible monetary policy framework, and completing the implementation of utility tariffs rebalancing over seven years. Lifting institutional capacity and strengthening policy implementation capabilities will enhance the timely delivery of these reforms.

Reforming the labor market to reduce skill mismatch and to lower structural unemployment will also need to be addressed. As a middle-income microstate with full employment, an ongoing inflow of foreign workers will be needed to sustain economic growth. The integration of foreign workers into the labor force will be balanced against the need to develop the skills base of the Seychellois work force.

The Seychellois economy is in the midst of a period of extensive reform that has broad implications for the wider population. Comprehensive reforms are being pursued along many fronts, and authorities are aware that the social safety net for the most vulnerable must be protected to compensate for the social impact of reforms. Our authorities recognize that adjustments to the welfare system are required to keep pace with the broader changes in the economy. To this end, means testing will be increasingly used to determine eligibility for social welfare.

**Extended Arrangement under EFF**

Program performance throughout the life of the EFF has been exemplary. Our Seychellois authorities comfortably met all end-December quantitative performance criteria and structural benchmarks. As staff notes, authorities have a proven record of implementing past staff advice and a strong performance record under the EFF. The overperformance in the end-December 2012 Net International Reserves (NIR) target has prompted our authorities to request for modification of the end-June 2013 performance criterion, and the end-September and end-December 2013 indicative targets for NIR.

As noted in previous Buff statements on the review of the EFF, a key factor in the success of the program has been the high level of ownership by the authorities. Adherence to the targets set under the program has helped support macroeconomic stability and instilled discipline on policy formation, which coupled with intensive technical assistance, ensured that 'best practices' were being developed and implemented. With the program due to expire at the end of the year, the Seychellois authorities are keen to maintain their strong collaboration with the Fund and look forward to discussions on possible successor arrangements over the course of the year.

Finally, our Seychellois authorities would like to express their gratitude to Management, the TA mission teams, the IMF mission chief and her team for their continued hard work and dedication in helping to shape Seychelles' economic reform agenda.