



SEYCHELLES

January 2022

FIRST REVIEW UNDER THE EXTENDED FUND FACILITY ARRANGEMENT—PRESS RELEASE; STAFF REPORT; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR THE SEYCHELLES

In the context of the First Review under the Extended Fund Facility Arrangement, the following documents have been released and are included in this package:

- **Press Release.**
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on December 17, 2021, following discussions that ended on November 5, 2021, with the officials of the Seychelles on economic developments and policies underpinning the IMF Request for a Staff-Monitored Program. Based on information available at the time of these discussions, the staff report was completed on December 3, 2021.
- A **Statement by the Executive Director** for the Seychelles.

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

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IMF Executive Board Completes First Review Under the Extended Fund Facility Arrangement for Seychelles

FOR IMMEDIATE RELEASE

Washington, DC – December 17, 2021: The executive Board of the International Monetary Fund (IMF) completed today the first review of Seychelles' economic performance under the 32-month Extended Fund Facility (EFF) arrangement that was approved on July 29, 2021. The completion of the review allows the authorities to draw the equivalent of about \$33.6 million (SDR 24 million), bringing total disbursements under the current EFF to about \$67 million (SDR 48 million).

The expected macroeconomic recovery has materialized. Seychelles remains a leader in vaccine coverage at home, and the widespread availability of vaccines in Seychelles' key tourist markets, particularly Europe, is contributing to a strong rebound in tourism. The economic outlook, while positive, remains subject to the uncertain evolution of the COVID-19 pandemic globally, including the omicron variant.

The authorities kept expenditures below program, reflecting mostly lower capital expenditures resulting from a reduction in expected external financing. As a result, public debt is on a faster downward trajectory. Yields on government securities have fallen markedly, supported by improved investor confidence and monetary policy accommodation. The combined effects of the liability management operation successfully implemented in July 2021 and deeper fiscal consolidation have substantially reduced rollover risks.

At the conclusion of the Executive Board's discussion, Mr. Bo Li, Deputy Managing Director and Chair stated:

"Driven by a swift recovery of the tourism sector, the Seychellois economy has rebounded strongly from the severe contraction in 2020 and program implementation is strong. The authorities have made substantial strides in restoring macroeconomic stability and are committed to the structural reform agenda.

"Front-loaded fiscal adjustment is appropriate to reduce debt vulnerabilities and fiscal risks. Measures to enhance revenue performance and the unwinding of COVID-related support measures are welcome. The authorities are taking steps to develop a medium-term fiscal framework and improve spending efficiency.

"The liability management operation (LMO) implemented in 2021 and deeper fiscal consolidation have substantially reduced rollover risks and laid the foundation for further easing of domestic financial conditions. Prudent debt management remains essential to further reduce vulnerabilities. Further improvements to public debt management capacity would be welcome.

"The accommodative monetary policy stance remains appropriate and continued efforts to strengthen the transmission mechanism are welcome. The authorities are monitoring inflationary pressures and are committed to maintaining a market-determined exchange rate.

“Continued efforts are needed to safeguard financial sector stability. A well-planned strategy for unwinding the COVID-19 related support measures and continued efforts to enhance the AML/CFT framework are important priorities.

“The authorities are taking steps to improve transparency and public efficiency. Further efforts to pursue governance reforms are encouraged. It will be important to advance structural reforms to promote private sector development, support diversification, and build resilience to climate change.”



SEYCHELLES

FIRST REVIEW UNDER THE EXTENDED FUND FACILITY ARRANGEMENT

December 3, 2021

EXECUTIVE SUMMARY

Macroeconomic developments and outlook. The expected macroeconomic recovery has materialized. Seychelles remains a leader in vaccine coverage at home, and the widespread availability of vaccines in Seychelles' key tourist markets, particularly Europe, is contributing to a strong rebound in tourism. The economic outlook, while positive, remains subject to the uncertain evolution of the COVID-19 pandemic globally.

Program performance: Program implementation has been strong and all quantitative program targets (QPCs) at end-July 2021 and ITs at end-September 2021 were met, some with wide margins; appropriate progress was made toward structural benchmarks. The authorities kept expenditures below program, reflecting mostly lower capital expenditures resulting from a reduction in expected external financing. As a result, public debt is on a faster downward trajectory. Seychelles' debt remains sustainable, albeit with significant risks. Capacity to repay the Fund remains adequate.

Liability Management Operation: A pre-COVID legacy of reliance on short-term domestic borrowing, coupled with the 2020 fiscal expansion to finance COVID support measures, significantly increased the gross financing needs (GFNs) of the government by end-2020. In early July 2021, the authorities successfully implemented a liability management operation (LMO), extending the average maturity of existing treasury-bill debt by several years by exchanging treasury bills for longer-term bonds. The authorities also began unwinding COVID-related spending measures. As a result, yields on government securities have fallen markedly, supported by improved investor confidence and monetary policy accommodation. The combined effects of the LMO and deeper fiscal consolidation have substantially reduced rollover risks.

Focus of discussions. Discussions focused on recent economic developments, fiscal performance and the 2022 budget, reductions in external financing and offsetting policies, monetary policy transmission mechanism to revive bank credit, financial sector stability as COVID-support measures are planned to be withdrawn, and progress on governance reforms.

Recommendation. Staff recommends completion of the first review, given the authorities' robust actions to meet program targets and commitments, notwithstanding difficult pandemic circumstances.

Approved By
Vivek Arora (AFR) and
Maria Gonzalez (SPR)

The hybrid mission took place during October 22 – November 5 and consisted of Boriana Yontcheva (head), Aissatou Diallo, Erin Nephew (all AFR), Hanife Yesim Aydin and Arindam Roy (both MCM), and Kyungsuk Lee (SPR). Danielle Bieleu and Tebo Molosiwa provided excellent assistance with the preparation of this report.

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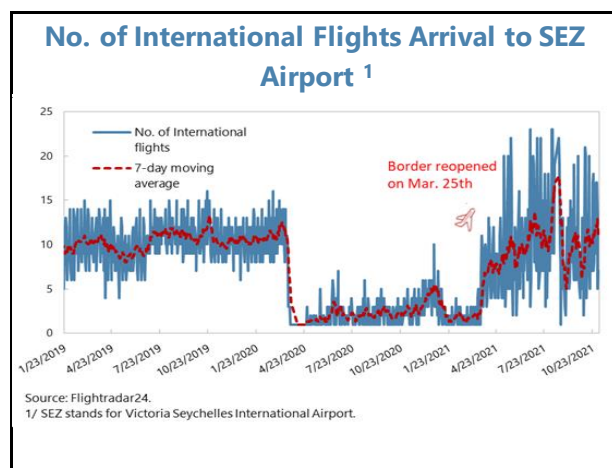
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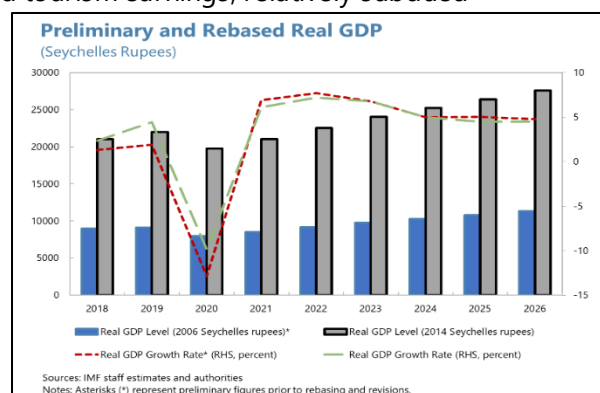
RECENT DEVELOPMENTS, OUTLOOK, AND RISKS

1. The post pandemic economic recovery is expected to be V-shaped and driven by tourism. Market sentiment has improved, fiscal deficits have narrowed, and debt ratios have been put on a decisively downward trajectory. (MEFP ¶11-13)

2. Growth is driven by a swift recovery of the tourism sector. Since July 2021, tourist arrivals have continued apace and real GDP growth is projected to reach 6.1 percent in 2021, in line with expectations at the time of EFF approval. In October, the authorities released revised and rebased GDP data for 2014-2019. As a result, swings in the real growth rate associated with the tourism-driven contraction in 2020 and the tourism-driven recovery in 2021 appear smaller in amplitude in the rebased and revised figures but remain in line with prior estimates (see chart)¹. Given widespread vaccine coverage, COVID infections are down significantly, with the 7-day average of new cases below 100 per 100,000, from September 2021. Forecasts for the upcoming holiday season are strong and tourist arrivals for 2021 as a whole are projected to reach 70 percent of the 2019 level.



3. The external position has begun to strengthen. Gross international reserves (GIR), which fell in early 2021, began to grow again due to increased tourism earnings, relatively subdued imports, and support from the IMF, including the SDR allocation. GIR increased from USD 529 million at end-March 2021 to USD 651 million as of end November 2021. Reserves are expected to reach USD 675 million as of end-2021 or 4.6 months of prospective imports. The current account deficit is projected to narrow to 20 percent of GDP in 2021 from 25 percent of GDP in 2020.- The nominal exchange rate between the Seychelles rupee and the US dollar has recovered to its pre-COVID level, as



¹ The rebasing of GDP had been planned for several years and was undertaken with IMF technical assistance. In these new estimates, GDP is larger than previously estimated. Tourism is a smaller share of the economy relative to other sectors, like finance and insurance and real estate, than previously estimated. As a result, the tourism-led contraction in 2020 was not as deep as initially estimated, and the tourism-led recovery in 2021 was not as steep as initially forecast. Although both the initial and current numbers reflect a roughly 70 percent decline in tourism in 2021 and a roughly 40 percent recovery in tourism in 2021, the overall GDP growth numbers are slightly different. The 6.1 percent growth number is now on a larger base, reflecting a nominal amount of economic activity that is roughly similar to the 6.9 percent growth initially forecast on the smaller base.

foreign exchange supply has exceeded demand. The REER appreciated by 47 percent from March 2021 to September 2021, mainly driven by a 50 percent NEER appreciation. Foreign currency deposits in the banking system increased by USD280 million during January–September 2021.

4. Price rises have accelerated in 2021 but inflation peaked in May. Annual average inflation is expected to reach 10 percent in 2021, up from 1.2 percent in 2020 mostly due to second-round effects of the 2020 exchange rate depreciation, combined with pandemic related cost-push factors.² However, inflation has been receding since its peak in May 2021, reflecting the pass-through effect from the exchange rate appreciation in April 2021. Inflation is expected to continue to ease in 2022 mainly due to the lagged impact of the exchange rate appreciation on food prices and the planned reduction in electricity tariffs but oil prices could pose further risks.

5. Despite ample liquidity, private sector credit growth decelerated by 7.9 percent (y-o-y at end-September 2021) mostly due to the impact of currency appreciation.³ Limited risk appetite of banks for lending amid the rise in NPLs and uncertainty also contributed to the credit slowdown. The strong projected economic recovery indicates prospects of improving risk appetite for bank lending in the near future. Monetary policy rates have been on hold since July 2021. Notwithstanding the appropriately accommodative monetary policy stance and abundant liquidity, lending rates have remained sticky (Annex II).⁴

6. The 2021 budget set the stage for a decisive decline of public debt, after the pandemic-related surge in 2020. The 2021 primary deficit is expected to decrease to 6.6 percent to GDP. In addition to unwinding COVID-related spending measures, both current and capital expenditures have been curtailed to offset in part a reduction in external bilateral financing. The 2022 budget proposal aims at a primary balance of -0.8 of GDP reflecting the authorities' multi-year plan to reduce debt-related vulnerabilities.

7. Public debt burden indicators have improved, reducing debt sustainability risks. The debt-to-GDP ratio is expected to decline from 92.2 of GDP at end 2020 to around 81 percent of GDP by end-2021 and to around 54 percent by end-2026. Interest rates for one-year Treasury bills have declined by more than 450 basis points since the LMO implementation in July 2021 reflecting a reduction in sovereign risk perceptions. Better economic prospects, a stronger fiscal outlook, and improved investor confidence resulted in an upgrading of Seychelles' sovereign ratings in November 2021.⁵

8. Banks continue to remain well capitalized and highly liquid. Deposit levels are stable and new loan extensions are low owing to limited risk appetite. The regulatory capital ratio

² The sharp currency appreciation that began in April 2021 has only partially offset the increase in global commodities prices, and shipping and transportation costs given the lag in exchange rate pass-through.

³ Without exchange rate appreciation, private sector credit would have declined only by 1.5 percent.

⁴ Supportive monetary policy caused aggregate reserves held at the central bank in excess of the reserve requirement to swell to 8 percent of GDP as of October 28, 2021.

⁵ Fitch upgraded Seychelles' sovereign ratings from B to B+ on November 19, 2021.

increased to 22 percent as of September 2021, from 17.1 percent at end-2020, stemming from a reduction in risk-weighted assets following the appreciation of the rupee in April 2021. Asset quality has been reportedly stable, and the average non-performing loan ratio (NPL) remains low although it has increased from 3.3 percent in December 2020 to 4.9 percent in September 2021. The Central Bank of Seychelles (CBS) is expected to start unwinding the temporary COVID-mitigating measures in 2022. Full exit from these measures and recognition of COVID-impacted loans could lead to an increase in the overdue loans and NPL ratios.

9. The outlook remains positive but with downside risks. The substantial recovery in tourist arrivals is expected to continue even though a renewed COVID-19 outbreak – whether in Seychelles or in its partner countries – could slow tourism growth again. Risks related to a tightening of monetary policy and financial conditions in the United States and Europe could limit Seychelles’ external financing ability. Higher NPLs in the banking sector from the COVID-19 impact also remain a risk. However, contingent liability risks to the government from Air Seychelles have been reduced, as the remaining debts of Air Seychelles will be managed through a process of administration. The domestic banking system is not exposed to Air Seychelles. The country remains vulnerable to climate change.

PROGRAM PERFORMANCE

10. Program implementation has been strong. All quantitative program targets (QPCs) at end July 2021 and ITs at end September 2021 were met, some (such as the primary deficit) by a wide margin (Table 1 of the MEFP). Progress on the structural reform agenda has been good (Table 2 of the MEFP). The cabinet has approved all the necessary legislation to ensure that Seychelles is fully compliant with EU and OECD international tax frameworks (*structural benchmark for end-September 2021*), in recognition of which Seychelles has been removed from the EU list of non-cooperative jurisdictions. Risks to debt sustainability from Air Seychelles have been reduced as Air Seychelles has gone into administration. The authorities worked with the World Bank and identified the least costly scenario, which was approved by the cabinet in September (*structural benchmark for end-September 2021*; (MEFP ¶150)). In early October 2021, the government appointed two administrators for Air Seychelles as per the requirement of the Insolvency Act. More than eighty percent of international business companies had submitted information to the centralized database of beneficial owners kept by the Financial Intelligence Unit as of October 2021, with full compliance expected by January 2022. The Financial Services Authority (FSA) and Financial Intelligence Unit (FIU) will assess accuracy of the ownership information by June 2022 (MEFP ¶174). The authorities could not meet the structural benchmark for submitting the Policy Paper on the Financial Stability Act due to capacity constraints and requested IMF assistance to peer review the policy paper. This structural benchmark is revised for March 2022 (MEFP 65). All other structural benchmarks for end-September were met and progress toward achieving end-December benchmarks is on track.

POLICY DISCUSSIONS

A. Fiscal Policy

The authorities are committed to reducing debt vulnerabilities and fiscal risks by frontloading the fiscal adjustment and returning to a primary surplus of 2.9 percent as early as 2023 (compared to a deficit of 0.4 percent at EFF approval).

11. The 2021 primary balance is projected to outperform original program projections by 2.5 percent of GDP. It is expected to reach 6.6 percent of GDP, compared with 9.1 percent of GDP expected during program approval (a reduction of 631 bn rupees or about 30 percent lower than the original deficit target). Revenues outperformed the EFF projections by 1 percent of GDP but a significant reduction in grants reduced total revenues and grants by 0.4 percent of GDP compared to the EFF projection. On the expenditure side, the unwinding of COVID related support measures reduced related expenditures from 6 percent in 2020 of GDP to 0.9 percent of GDP in 2021. The authorities also implemented other current expenditure-saving measures and offset the reduction in grants and project loans by under-executing capital expenditures in 2021 (4.9 percent of GDP versus planned 7.2 percent of GDP).

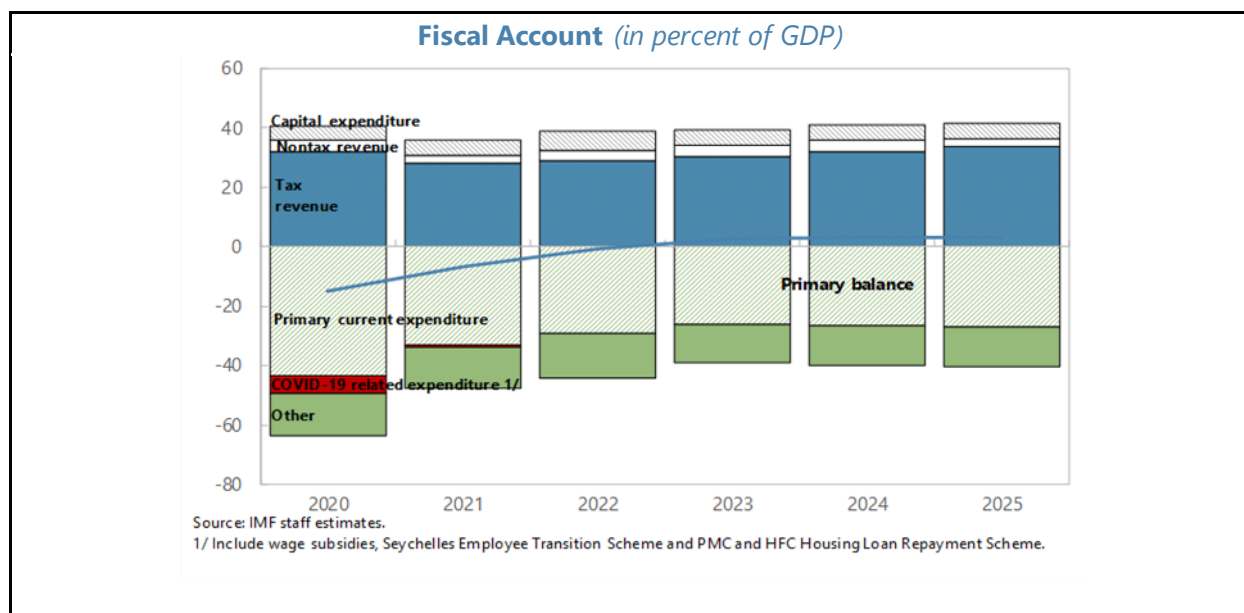
12. The draft 2022 budget sets a more ambitious primary deficit target than the fiscal framework agreed at the time of the EFF. The authorities are committed to a primary deficit of 0.8 percent of GDP in 2022 (compared to 4.7 percent of GDP at EFF approval) (MEFP ¶129). Tax revenue as a percent of GDP would increase from 26.7 percent of GDP in 2021 to 28.2 percent in 2022 based on the recovery and measures to strengthen revenue administration (*structural benchmark for end-September 2023*; (MEFP ¶127). The business tax rate reform is expected to generate some revenue losses in 2022, but such losses would be more than offset in 2023 and beyond thanks to savings expected from (1) the reform in taxation to include all securities dealers, (2) digital economy taxation, and (3) the increase in profit tax to 3 percent (MEFP ¶127). Total revenues are expected to increase by 2.1 percent of GDP between 2021 and 2022.

Text Table. Seychelles: List of Fiscal Measures Incorporated in the 2021 Budget

	SR'million	% of GDP
Revenue Side		
Tax Reform; Amnesty Program July to Dec 2021	20.0	0.09%
Abolishment of CSR Tax from April 2021	-58.6	-0.25%
Sub-Total	-38.6	-0.16%
Expenditure Side		
Public Sector Reforms	279.1	1.19%
Abolishment of the FA4JR Scheme from 1st April 2021	1082.0	4.62%
Abolishment of the SETS program from 1st March 2021	7.0	0.03%
Abolishment of the Unemployment Relief Scheme from 1st April 2021	29.6	0.13%
Sub-Total	1397.7	5.97%
Sources: Authorities and IMF staff calculations.		

Fiscal Measures in the Medium – Term 2022-26 (in Percent of GDP)					
	2022	2023	2024	2025	2026
Revenue Side					
Business tax rate reform	-0.2	-0.2	-0.2	-0.2	-0.2
Reform in taxation to include all securities dealers		0.7	0.1	0.08	0.08
Digital economy taxation		0.1	0.0	0.04	0.04
Transfer pricing reforms			0.0	0.03	0.03
Increase in PT to 3%		0.0	0.0	0.03	0.03
VAT Reforms (Review exemptions and deferred VAT, Review VAT threshold, Improved compliance wholesale/retail sector)			0.0	0.04	0.05
Taxation of Super Yachts			0.1	0.06	0.05
Sub-Total	-0.2	0.7	0.07	0.06	0.05
Expenditure Side					
Public Sector Reforms	0.9	0.80	0.03	0.03	0.03
Abolishment of wage subsidies	0.69	0.0	0.0	0.0	0.0
Abolishment of Seychelles Employee Transition Scheme	0.05	0.0	0.0	0.0	0.0
Abolishment of the Unemployment Relief Scheme	0.08				
Abolishment of PMC and HFC Housing Loan Repayment Scheme	0.09	0.0	0.0	0.0	0.0
Sub-Total	1.80	0.80	0.17	0.03	0.03
Sources: Authorities and IMF staff calculations					

13. The government has set lower targets for current expenditures (wages and salaries, goods and services and transfers), supported by structural reforms (wage bill, pension fund, and social protection system reforms) and some discretionary restraints (capping of salaries and allowances). A Public Service Salary Review Committee has been set up chaired by the Minister of Finance, Economic Planning & Trade. The Committee will conduct an analysis that will support the wage bill reform (MEFP ¶130). These measures would allow a reduction in current expenditure by 4 percent of GDP between 2021 and 2022, while capital expenditures would rise by 1.2 percent of GDP due to some new grant-financed projects and the postponement of some planned projects in 2022. Seychelles has demonstrated a strong track record in implementing ambitious fiscal consolidation programs. The 2021 realization (expected primary deficit of 6.6 percent of GDP versus 9.1 at the program approval) along with the planned revenue and expenditures measures reinforce the feasibility of the current fiscal consolidation path. Should downside risks materialize, the authorities are committed to reaching their consolidation targets. They will identify non-priority spending and investment infrastructure projects that could be dropped while protecting education, health, and social spending.



14. Risks to debt sustainability from Air Seychelles have been reduced now that Air Seychelles has gone into administration. The task of the administrators will be to consider the optimal ways of restructuring Air Seychelles and settling its debts. For the 2022 budget, the government has allocated \$5 million previously agreed for the repayment of the Etihad Airways debt that Government purchased at a discount, and \$1.4 million for a liability from 2015. Contingent liability risks to the government have been reduced, as remaining debts of Air Seychelles will be managed through the process of administration and are expected to be paid from Air Seychelles' assets (*structural benchmark for end-September 2021*; MEFP ¶150).

15. Progress was made on the implementation of a Medium-Term Fiscal Framework (MTFF). A recent IMF technical assistance (TA) mission (September 2021) delivered hands-on training on the principles of fiscal sustainability and public debt dynamics aimed at strengthening debt management. For FY23, additional support in strengthening the credibility of the MTFF through improving costing methodologies, including the estimation of binding expenditure ceilings is scheduled. Also, the authorities have started technical discussions with IMF staff on strengthening fiscal forecasting, reporting, budget institutions, fiscal risk analysis, and enforcement of budget ceilings.

16. Improving the efficiency of government spending will be key to ensuring fiscal sustainability and enhancing growth prospects over the medium term. A Public Investment Management Assessment (PIMA) planned for FY23 will help identify opportunities to increase the efficiency of public investment including the scope for the procurement system to support PPPs (MEFP ¶144). To ensure the transparency of COVID-related spending, the government is carrying out an audit, which will include information on awarded companies (MEFP ¶144).

17. The authorities are implementing projects for climate-change adaptation, digitalization, and the reform of the social safety net. Climate change adaptation investments

remain as critical as ever. The authorities intend to mainstream climate adaptation in Seychelles' post-pandemic recovery plan (MEFP ¶17,18,25). Staff are working closely with the World Bank and AfDB in this area and will continue to work with the authorities on necessary reforms to social protection (MEFP ¶24, 41, 42).

18. Reductions in external financing in 2021 will be compensated for by greater policy adjustment than the EFF envisaged, and by more domestic financing. Budget support from two of Seychelles' key bilateral partners is now expected not to materialize in 2021. In addition, a planned World Bank health and nutrition project has not yet been approved by its Board. The reduction in external financing relative to the original EFF is expected to be USD 79 million (USD 68 million from the bilateral partners and USD 11 million from the World Bank). However, fiscal adjustment is larger than envisaged by USD 42 million in 2021 and the remaining financing need of USD 37 million is being met by domestic financing, helped by favorable domestic financial conditions (MEFP ¶32).

B. Monetary and Exchange Rate Policy

19. The Central Bank of Seychelles (CBS) stands ready to act if inflationary pressures persist. The lagged impact of the rupee appreciation, particularly on food prices, combined with lower electricity tariffs is expected to reduce inflationary pressures starting early-2022⁶. Should inflation remain at double-digit levels—including due to the materialization of downside risks—CBS will act swiftly to keep expectations well anchored. The authorities intend to expand the survey of inflation expectations in order to support their policy response capacity. The planned TA support by AFRITAC South on updating the Producer Price Index will help improve the inflation forecasting framework (MEFP ¶53, 54).

20. The authorities are working to ensure a well-functioning, interest-rate-based monetary policy framework. The ongoing reforms to the monetary policy framework include development of an interbank market and fine-tuning of communications policy. As lending rates have been sticky, the interest rate transmission channel needs to be strengthened within the context of rising NPLs and risk aversion of the banking sector (MEFP ¶53). At the same time, greater recourse to net external financing vis-a-vis domestic financing during 2021-22 will require sterilization by the CBS. Resumption of repo operations based on a Master Repurchase Agreement will strengthen CBS' liquidity management capacity. To strengthen monetary policy implementation, including the transmission mechanism, IMF TA is planned in the fourth quarter of 2021.

21. The authorities are managing exchange rate policy challenges. The CBS intends to continue to allow the market to determine the exchange rate, with interventions only to limit disorderly market conditions and to build external buffers ((MEFP ¶55). Although banks generally do not extend foreign currency credit to entities with no foreign exchange earnings, the banking regulations do not provide sufficient guidance. Greater exposure to foreign currency liabilities of

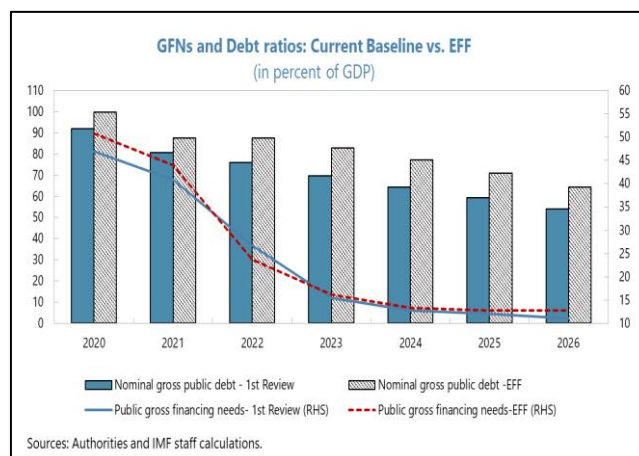
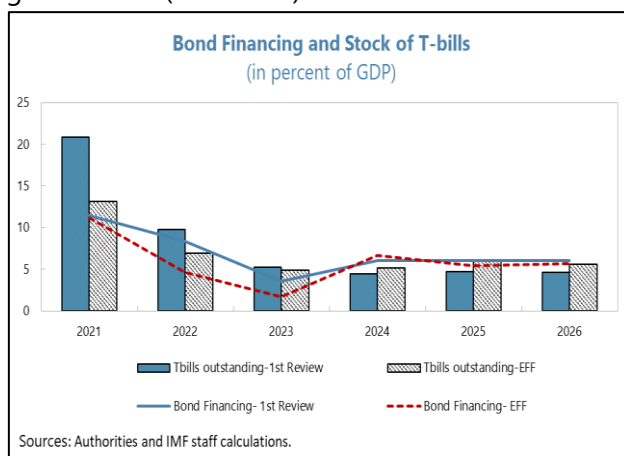
⁶ Electricity tariffs are updated in line with international fuel prices, which are expected to decline in 2022.

banks from foreign currency deposits would also warrant better risk management capabilities for the banking sector.

C. Debt Reduction Strategy

22. The authorities' successful liability management operation (LMO) has helped to mitigate the heightened refinancing risks associated with a heavy reliance on short-term domestic financing (Annex III). By reducing sovereign risks and the supply of short-term debt issuance, the LMO has contributed to a further easing of sovereign yields since its execution. Gross financing needs (GFNs), which rose to 47 percent of GDP in 2020, are projected to decline to 41 percent in 2021, and further to 11 percent by 2026 (compared with 12 percent by 2026 envisaged last July), mainly because of the successful LMO and strong fiscal consolidation. One-year T-bill yields declined by 461 basis points during July-October 2021.

23. The authorities plan to tap the domestic market and use the recently allocated SDRs to offset the reduction in external financing for 2021 and 2022. In August 2021, Seychelles received SDR 21.9 million as part of the Fund's general SDR allocation to members. In the current domestic low-yield and surplus liquidity context, domestic financing can replace some foreign financing.⁷ The issuance of bonds rather than T-bills would prevent the re-emergence of rollover risks. The authorities completed the bond issuance program for 2021 by issuing bonds amounting to 1.6 percent of GDP (SCR 400 million) in November 2021. The 2022 financing gap is further planned to be met through utilization of SDR allocation (1.6 percent of GDP) (MEFP ¶32). The CBS will be proposing amendments to the CBS Act to on-lend proceeds from SDR utilization to the government (MEFP ¶32).



⁷ Bond issuance for 2021 will remain at around 11 percent of GDP as estimated during EFF approval. This will include bond issuance for the remaining part of 2021 amounting to 1 percent of GDP. At the end of 2021, the overall exposure of the banking sector to government securities is projected to remain unchanged at 16 percent of bank total assets compared to the previous year, but the shares of T-bills will fall and that of bonds will rise to be roughly even. Annual bond issuance during 2022-2026 is projected to decline from 2021 level and average at around 6.0 percent of GDP (compared to 4.6 percent during EFF approval). The reduction in T-Bills (annual average of 2.4 percent of GDP) during the same period, partly supported by external financing would provide room to absorb the bond issuance and accommodate a possible future pick up in bank credit.

24. The authorities have made steady progress on structural benchmarks related to debt management. They have met the structural benchmark for the first review (*end-September 2021*) on publishing a debt bulletin on the Ministry of Finance website. Two quarterly debt bulletins have been published in 2021 that would help to bolster debt transparency. IMF TA on updating and publishing a debt management strategy, an annual borrowing plan (ABP), and an auction calendar (*structural benchmark for end-March 2022*) is scheduled for early 2022. Given previous challenges to implementing a debt management strategy, the authorities are working to strengthen the planning process for debt management through the active involvement of the high-level National Public Debt Management Committee (chaired by the Principal Secretary, Ministry of Finance) to approve the quarterly borrowing plan on a recurring basis (*new structural benchmark for end-March 2022*); and through enhanced coordination between cash and debt management. Given the limitations of the core banking system used by the CBS, which currently cannot handle bond auctions, the authorities are working to develop the process required to adopt an auction mechanism for future issuance of bonds instead of the previous practice of tap issuances. With a shift to a regular bond issuance strategy, it would be imperative to develop a plan for a government securities trading framework, approved by the government in consultation with the CBS by end-2022 to initiate trading in government securities, (*new structural benchmark for end-December 2022*). Staff also urged the authorities to undertake legal reforms required to make domestic bond issuance a regular operation without requiring issuance-specific legal approval. (MEFP ¶151,52).

D. Financial Stability

25. The banking system appears well capitalized and highly liquid, with limited impact of COVID-19 on loan portfolios, backed by the ongoing recovery and remaining support measures. The banks experienced a reduction in interest income in 2021 stemming from payment holidays, the impact of local currency appreciation on value of FX loan portfolios, and the reduction in prime lending rates. Loan-loss provisions are lower in 2021 compared to 2020 due to the recovery, resulting in a positive adjustment of macroeconomic variables in IFRS 9 models and a reversal in provisions. With the economic recovery, firms under moratoria started to repay their loans and the supply for new loans -- both working capital and project loans -- increased in recent months, reflecting improved but still low risk appetite for lending (MEFP 60).

26. By the end of 2021, the CBS will submit to its Board a plan for unwinding the package of various COVID-19 related support measures including the withdrawal of the private sector credit relief scheme, provisions for central bank advances to the government and the payment holiday for bank customers.⁸ In the context of finalizing its unwinding plans, the CBS

⁸ The Private Sector Credit Relief Facility aimed to provide working capital loans with partial government guarantee on capital and subsidized interest rates by 400 bps. At the end of September, it accounted for 4.5 percent of the total bank credit. The government has not availed fresh advances from the CBS in 2021.

should urge banks to differentiate viable borrowers with liquidity shortages from non-viable ones in order to support credit growth and asset quality in the banking system (MEFP ¶62).

27. The recovery and increasing willingness of banks starting from October 2021 to extend loans underscores the significance of a well-designed strategy for unwinding COVID-19 related support and forbearance measures. Staff underlined the necessity of undertaking a prudent bank-level analysis regarding the impact of unwinding these measures on banks' asset quality. The CBS is assessing the impact of all COVID-19 related borrower support measures, including relief schemes, moratoria and regulatory forbearance measures, and is committed to basing its assessment on granular, bank-level data. Based on preliminary assessments, the CBS does not expect a significant negative impact of unwinding the COVID-19 measures on banks' asset quality. A proposal for unwinding some measures in their entirety while replacing some others with more targeted versions will be submitted to the CBS Board by end-2021 (MEFP ¶63).

28. The CBS remains committed to ensuring a stable and well-capitalized banking system that can support the recovery and is standing ready to take early intervention measures where necessary. If any bank becomes undercapitalized, the CBS will use the set of relevant early intervention measures, including suspension of dividend payments. Staff further urged the CBS to enhance the effectiveness of the supervisory framework including regular monitoring of the health of the banking system by collecting more granular information and ensuring that banks' loan classification correctly reflects their asset quality⁹ and loans are adequately provisioned. The CBS remains committed to monitoring the relevant classification of loans and providing guidance on prudential treatment of moratoria and NPL management strategies (MEFP ¶64). To preserve the stability of the financial system while supporting growth, the CBS will encourage banks to engage in restructuring of loans for firms that are viable but have temporary liquidity shortages.

29. The authorities are committed to keeping the progress on structural benchmarks related to financial stability. To ensure that the legal basis and the mandate of the Financial Stability Commission (FSC) are strengthened, the CBS prepared in April 2021 a draft policy paper outlining various considerations for the drafting of a Financial Stability Act in April 2021. After requesting IMF TA, the CBS will submit the Policy Paper to the Cabinet for approval by March 2022 (*revised structural benchmark for March 2022*; (MEFP ¶65).

30. The authorities continue to pursue their efforts to enhance the legislative framework for a National Payment System, adopt innovative financial services in line with the national Fintech strategy, promote digital financial literacy, and enhance financial consumer protection. Staff welcomes the CBS' commitment to implementing an enhanced credit information system and the supporting legal framework to extend the coverage of credit information. Nonetheless, given the intense reform agenda and capacity constraints, staff advised the authorities to prioritize the actions to be taken towards modernizing the financial system and deepening the financial sector while preserving the efforts on financial stability, such as the draft legislation for

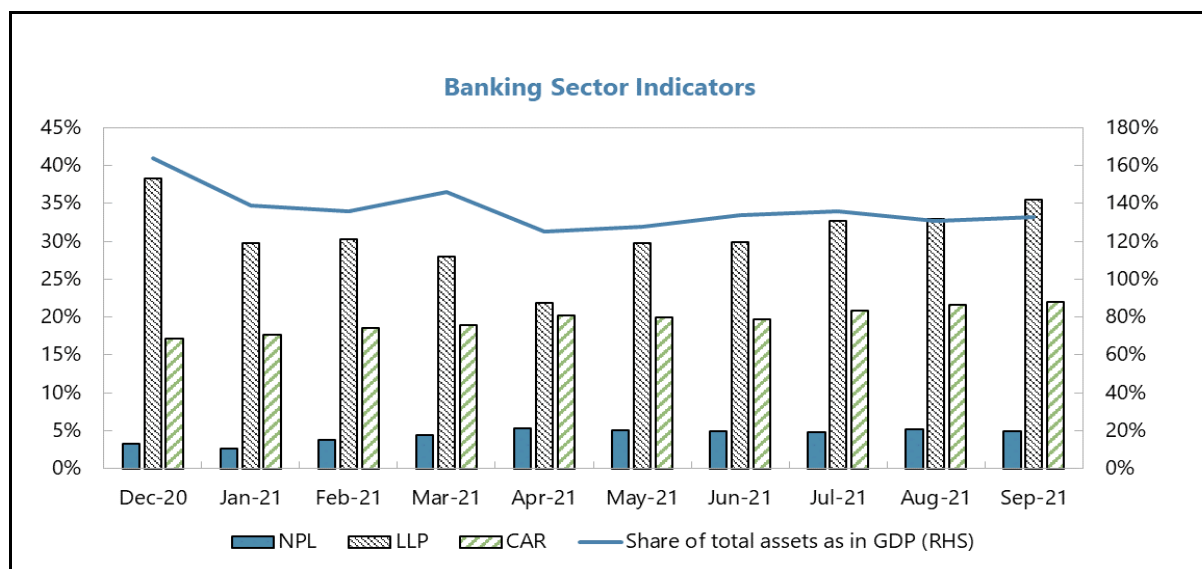
⁹ Such granular data should include, inter alia, data on restructured and rescheduled loans and FX placements and exposures.

crisis management and bank resolution and the Financial Stability Act and remain on track with the agreed timing for structural benchmarks (MEFP ¶66,67, 68, 69, 70, 71). Staff will assess the progress in enhancing the legislative framework for payments and digital finance in Article IV mission.

E. Governance and Transparency

31. The authorities are implementing transparency and accountability measures related to COVID-19 spending. The authorities have met their commitments under the RFI, with the exception of the audit of emergency spending. The audit of emergency spending that was initially planned to be published in September 2021 was delayed due to staffing shortages related to COVID; it is now scheduled to be sent to the Ministry of Finance in November 2021 and to be made public in December 2021 (MEFP ¶144).

32. The reform on beneficial ownership transparency is on track. In August 2020, the new Beneficial Ownership Act and Regulations came into force. The Act provides for identification and verification of beneficial ownership of legal persons and legal arrangements, in addition to the requirements to establish and maintain an up-to-date register of beneficial owners by resident agents, and a centralized database to be kept by the Financial Intelligence Unit (FIU). The centralized database became operational in July 2021. Eighty-two percent of the more than 53,000 international business companies in good standing had submitted information to the beneficial ownership database as of October 2021, with full compliance expected by January 2022. The FSA and FIU will, by June 2022, publish an assessment report on the accuracy of the beneficial ownership information of the international business companies in the database (MEFP ¶174).





F. Data Issues

33. Data issues in key macroeconomic aggregates are being addressed. IMF TA has supported the National Bureau of Statistics (NBS) to rebase annual GDP estimates at current and constant prices as well as to improve quarterly GDP estimates, while addressing the large inconsistencies in the GDP series. IMF TA was also provided to the CBS to improve external sector statistics, in particular an estimation of tourism earnings (MEFP ¶158). The mission underlined that sustainable capacity improvements require adequate resources at the NBS and the CBS.

PROGRAM MODALITIES AND FINANCING

34. The program remains fully financed. There are firm commitments for financing for the next 12 months and good prospects for the remainder of the program period. The much steeper than planned fiscal consolidation (savings of USD 71 million from the primary balance in 2022) will partly offset the reduction in bilateral financing. Nevertheless, the reductions in external financing in 2021 and 2022 will require the authorities to rely on more domestic financing (at a moderate pace due to the significant fiscal savings) and to use their SDR allocation. GIR both in percent of ARA metric and months of imports are projected to remain at an appropriate level.

35. Seychelles' capacity to repay the Fund remains adequate but subject to high risks. The return of tourists to the country is likely to generate significant repayment capacity. The authorities have embarked on a successful vaccination campaign and re-opened the border to tourists as of end-March 2021. Their tourism capacity remains intact, with few hotels having closed, and growth is rebounding without apparent scarring effects, as guest workers are returning, and labor shortages do not appear to be constraining the tourism recovery. The authorities' commitment to the program and their solid repayment history following previous Fund programs also provide comfort. The Fund credit-to-GDP ratio will peak at 8.6 percent in 2021, higher than in most recent EFF cases (excluding European exceptional access cases) and reflects Seychelles' small GDP size. The Fund credit to GIR ratio is projected to peak at 19.5 percent in 2022. Obligations to the Fund relative to exports of goods and services will peak at 1.1 percent in 2024. At the same time, the program involves significant risks, which include uncertainties around tourism and the extensive structural reform agenda.

36. The CBS remains committed to implementing the safeguards assessment recommendations. - While slightly delayed, the CBS, in consultation with the IMF, will submit amendments to the CBS Act to the Cabinet in March 2022 which would strengthen governance and oversight, enhance institutional and personal autonomy, and safeguard financial autonomy. Moreover, the CBS is expected to start unwinding the temporary COVID-mitigating measures in 2022 (MEF164)

STAFF APPRAISAL

37. The economy has rebounded strongly from the severe 2020 pandemic-related contraction, and the outlook is favorable. Growth is driven by a swift recovery of the tourism sector and expected to reach about 6 percent of GDP. Market sentiment has improved, fiscal deficits have narrowed, and debt ratios have been put on a decisively downward trajectory. This recovery was aided by the authorities' substantial strides in restoring macroeconomic stability and structural reforms set in motion during the ongoing EFF-supported program.

38. Price rises accelerated in early 2021 but inflation is expected to ease in 2022. As a small open economy Seychelles fully felt the impact of pandemic-related cost-push factors combined with

the lagged second-round effects of the steep 2020 currency depreciation. Inflation has however been receding since its peak in May 2021 as the exchange rate recovered to its pre-pandemic level and is expected to continue to ease in 2022. and The CBS is monitoring inflation expectations and stands ready to act if inflationary pressures persist.

39. The authorities are committed to reducing debt vulnerabilities and fiscal risks by frontloading the fiscal adjustment.

- **The 2021 primary balance is projected to outperform the projection at the time of the EFF by 2.5 percent of GDP.** The primary deficit in 2021 is expected to reach 6.6 percent of GDP compared to 9.1 percent envisaged at the time of the EFF approval. Revenues outperformed the EFF projections and the unwinding of COVID-related support measures reduced related expenditures from 6 percent of GDP in 2020 to 0.9 percent in 2021.
- **The 2022 budget similarly sets a more ambitious primary deficit target than previously envisioned of 0.8 percent of GDP.** Tax revenues are expected to rise on the back of the economic recovery, tax reforms, and measures to strengthen revenue administration. The government has identified structural reforms to allow a substantial reduction in current expenditures as a share of GDP while increasing capital expenditures.

40. The authorities have addressed the heightened refinancing risks associated with the heavy reliance on short-term domestic financing during the COVID period. The successful implementation of the liability management operation (LMO) has significantly mitigated rollover risks and laid the foundation for further easing of domestic financial conditions.

41. The banking system weathered the crisis well, underscoring the significance of a well-designed strategy for unwinding COVID-19 related support and forbearance measures. The CBS is appropriately assessing the impact of all COVID-19 related borrower support measures. The CBS intends to undertake a prudent bank-level analysis of the impact of these measures on banks' asset quality, which will strengthen the unwinding strategy.

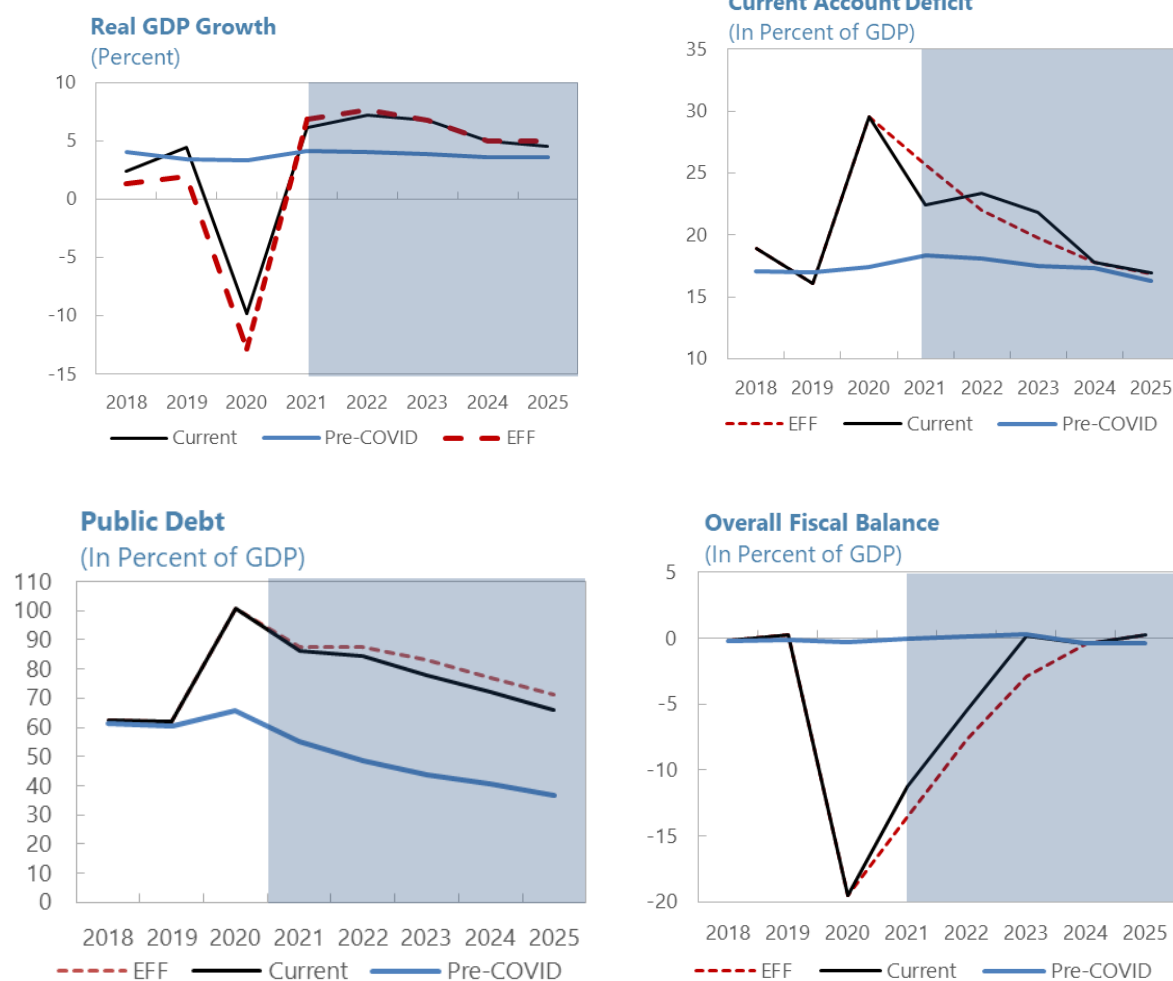
42. Staff welcomes the authorities' continued efforts to improve governance and stresses the need to strengthen implementation and enforcement going forward. The authorities have taken important steps to strengthen the legal and institutional framework to fight corruption. The beneficial ownership database is a welcome tool to enhance transparency of international business companies. Ensuring accuracy of and appropriate access to the ownership information, including the assessment report expected in June 2022, will be critical moving forward. Consolidating improvements in the PFM system's integrity and transparency are also important to the authorities' efforts.

43. The Seychellois economy faces risks. The main risk to the outlook and the EFF-supported program arises from COVID-related risks to the outlook owing to the economy's high dependence on tourism. The authorities would need to be prepared to reallocate budgetary resources to cover priority needs while protecting the public finances. Seychelles is vulnerable to climate related risks.

Risk mitigation would include sound fiscal policies and policies to diversify Seychelles' economy as a medium-term priority.

44. Staff supports the authorities' request for completion of the first review under the Extended Arrangement. The attached Letter of Intent and Memorandum of Economic and Financial Policies set out appropriate policies to pursue the program's objectives. The capacity to repay the Fund is adequate but subject to high risks, and risks to program implementation are manageable.

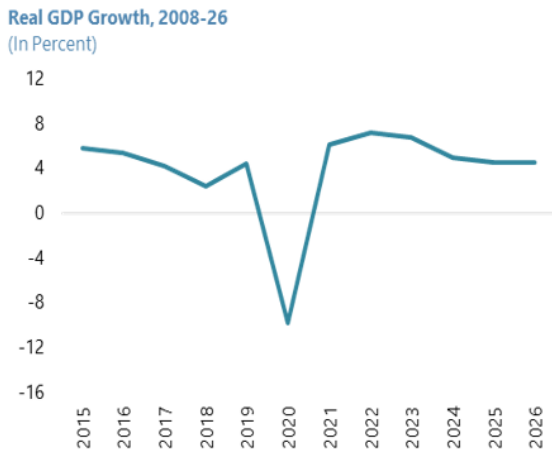
Figure 1. Seychelles: Indicators of Economic Activity



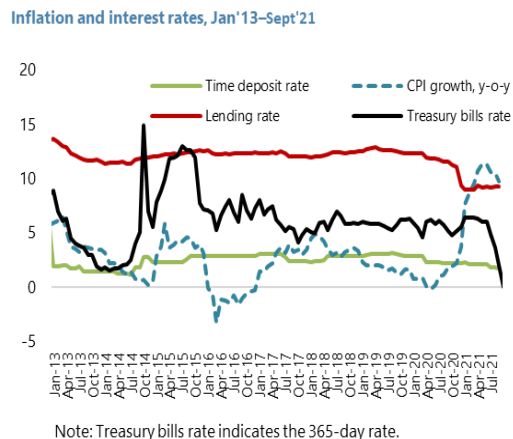
Sources: Seychelles authorities, and IMF Staff calculations.

Figure 2. Seychelles: Macroeconomic Indicators – 2008-26

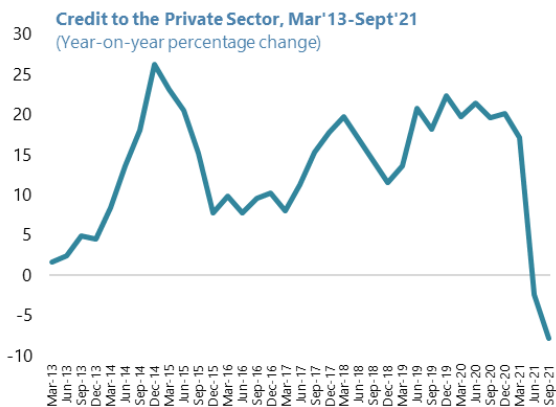
The economy is projected to experience a V-shape recovery...



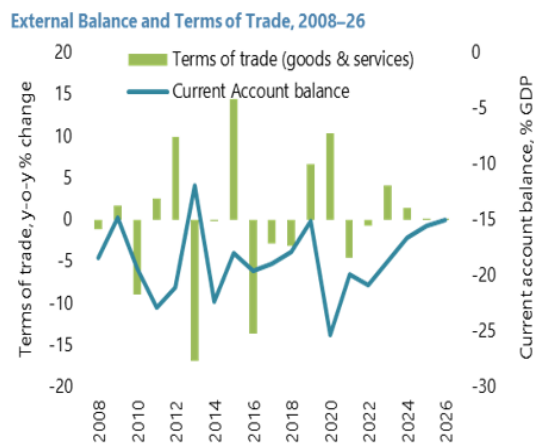
Interest rates are stable, and inflation is picking up...



Private sector credit has declined mainly due to the exchange rate appreciation...



External deficit is improving...



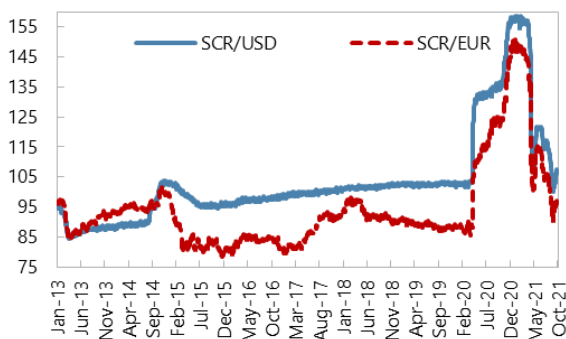
Sources: Seychelles authorities, and IMF Staff calculations.

Figure 3. Seychelles: Macroeconomic Developments and Projections

Recent appreciation partly offset the 2020 depreciation....

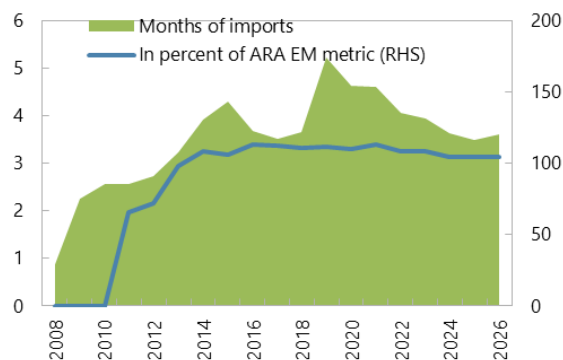
Daily exchange rates index, Jan'13-Oct'21

(December 31, 2011 = 100)



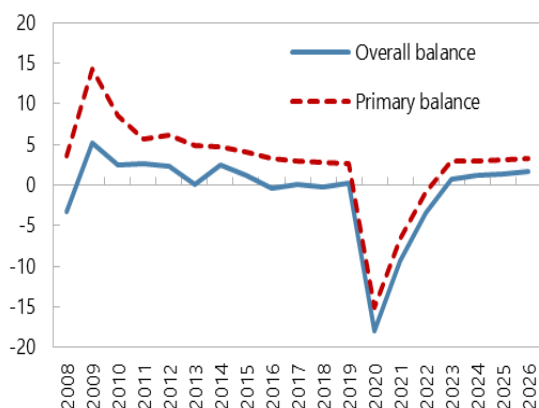
Reserves remained strong....

Reserves Adequacy, 2008-26¹



Ambitious fiscal consolidation...

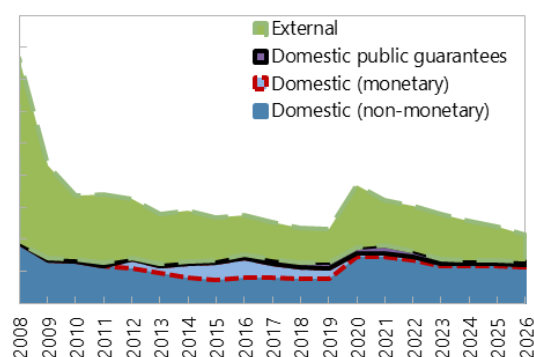
Fiscal balances, 2008-26



...will preserve debt sustainability....

Stock of public debt, 2008-26

(Percent of GDP)



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

Sources: Seychelles authorities, and IMF Staff calculations.

Table 1. Seychelles: Selected Economic and Financial Indicators, 2019-26

Nominal GDP (2017): US\$1,498 million

Per capita GDP (2017): US\$15,735

Population, end-year (2016): 94,677

Literacy rate (2015): 95.3 percent

Main products and exports: Tourism, Canned Tuna

	2019	2020	2021		2022		2023	2024		2025		2026		
	Act.	Prel.	EFF 1st review	EFF 1st review	EFF 1st review	EFF 1st review	EFF 1st review	EFF 1st review	EFF 1st review	EFF 1st review	EFF 1st review	EFF 1st review	EFF 1st review	
(Annual percent change, unless otherwise indicated)														
National income and prices														
Nominal GDP (millions of Seychelles rupees)	23,603	21,664	23,585	25,034	26,219	27,841	28,889	30,595	31,235	33,087	33,781	35,611	36,464	38,328
Real GDP (millions of Seychelles rupees)	21,959	19,795	...	21,005	...	22,518	...	24,049	...	25,251	...	26,388	...	27,575
Real GDP growth	4.5	-9.9	6.9	6.1	7.7	7.2	6.8	6.8	5.0	5.0	5.0	4.5	4.8	4.5
CPI (annual average)	1.8	1.2	10.0	10.0	3.7	3.7	3.2	3.2	3.0	3.0	3.0	3.0	3.0	3.0
CPI (end-of-period)	1.7	3.8	8.6	8.6	3.9	3.9	3.5	3.5	3.2	3.2	3.0	3.0	3.0	3.0
GDP deflator average	-0.3	1.8	10.2	8.9	3.2	3.7	3.2	2.9	3.0	3.0	3.0	3.0	3.0	3.0
Money and credit														
Broad money	13.9	29.2	...	...	...	...	...	...	...	...	...	...	...	...
Reserve money (end-of-period)	22.7	40.4	...	...	...	...	...	...	...	...	...	...	...	...
Velocity (GDP/broad money)	1.2	1.2	...	...	...	...	...	...	...	...	...	...	...	...
Money multiplier (broad money/reserve money)	4.3	3.9	...	...	...	...	...	...	...	...	...	...	...	...
Credit to the private sector	22.3	20.2	9.1	-11.9	16.6	16.0	17.7	16.2	18.7	15.9	16.5	15.5	15.6	15.0
(Percent of GDP, unless otherwise indicated)														
Savings-Investment balance														
External savings	15.2	25.4	25.7	20.0	22.0	20.9	19.8	18.8	17.8	16.6	16.9	15.5	15.5	15.0
Gross national savings	12.3	-3.2	2.3	5.3	5.7	5.6	8.1	5.8	8.8	8.4	9.5	9.3	10.8	9.7
Of which: government savings	5.6	-13.3	-6.1	-5.5	-1.1	0.8	2.6	4.0	3.7	5.1	5.3	5.7	5.8	6.3
private savings	6.7	10.1	8.4	10.8	6.7	4.8	5.4	1.8	5.1	3.3	4.2	3.6	5.0	3.4
Gross investment	27.4	22.3	28.0	25.2	27.7	26.8	27.8	25.8	26.6	26.0	26.4	25.8	26.3	25.8
Of which: public investment ¹	4.9	4.8	9.0	4.9	8.7	6.4	7.3	5.3	6.1	5.5	5.9	5.2	5.5	5.2
private investment	22.5	17.5	19.0	20.3	19.0	20.4	20.5	20.5	20.5	20.5	20.5	20.6	20.8	20.6
Private consumption	54.1	50.4	54.9	54.8	56.1	58.9	54.8	60.8	52.7	58.7	53.4	57.7	52.1	57.0
Government budget ⁵														
Total revenue, excluding grants	35.3	33.0	29.0	30.0	31.2	32.1	32.4	32.5	34.2	33.5	34.9	34.4	35.4	35.2
Expenditure and net lending	36.7	52.8	45.6	41.7	41.1	38.1	37.0	33.9	36.0	34.6	36.0	35.1	36.0	35.4
Current expenditure	31.8	46.3	36.6	35.5	33.3	31.5	31.2	28.5	31.2	28.6	30.4	28.6	30.4	28.8
Capital expenditure ¹	4.9	4.8	7.2	4.9	7.0	6.4	5.9	5.3	5.2	5.5	5.3	5.2	4.7	5.1
Overall balance, including grants	-0.8	-18.0	-12.8	-9.3	-7.3	-3.4	-2.7	0.6	-0.4	1.1	0.2	1.4	0.6	1.7
Primary balance	2.6	-15.0	-9.1	-6.6	-4.7	-0.8	-0.4	2.9	2.6	3.0	2.8	3.1	3.0	3.2
Total government and government-guaranteed debt ²	58.1	92.2	82.7	80.7	82.8	75.9	79.2	69.7	73.3	64.3	68.1	59.5	62.1	53.9
External sector														
Current account balance including official transfers (in percent of GDP)	-15.2	-25.4	-21.1	-20.0	-22.0	-20.9	-19.7	-18.8	-17.7	-16.6	-16.8	-15.5	-15.3	-15.0
Total external debt outstanding (millions of U.S. dollars) ³	4,885	5,048	5,446	5,494	5,816	5,769	6,131	6,056	6,330	6,236	6,547	6,427	6,802	6,635
(percent of GDP)	290.7	410.1	386.2	401.8	330.7	310.2	316.4	294.3	302.1	277.1	288.9	262.0	389.8	246.8
Terms of trade (=deterioration)	6.6	10.2	-3.6	-4.5	-4.1	-0.8	-0.4	4.0	0.9	1.3	0.9	1.3	0.0	0.0
Real effective exchange rate (average, percent change)	...	...	...	...	...	...	...	...	...	...	...	...	...	...
Gross official reserves (end of year, millions of U.S. dollars)	581	559	672	675	743	673	815	720	816	720	824	751	848	778
Months of imports, c.i.f.	5.2	4.6	4.6	4.6	4.4	4.1	4.4	3.9	4.0	3.6	3.8	3.5	3.9	3.6
In percent of Assessing Reserve Adequacy (ARA) metric	111.6	109.9	114.5	113.4	115.9	108.0	117.4	108.5	111.1	104.2	107.0	104.6	104.6	104.2
Exchange rate														
Seychelles rupees per US\$1 (end-of-period) ⁴	14.1	21.6	...	...	...	...	...	...	...	...	...	...	...	...
Seychelles rupees per US\$1 (period average) ⁴	14.0	17.6	...	...	...	...	...	...	...	...	...	...	...	...

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

¹ Includes onlending to the parastatals for investment purposes.² Includes debt issued by the Ministry of Finance for monetary purposes.³ Includes private external debt.⁴ As to 2020, exchange rate measured as of July 14, 2020.⁵ The fiscal program targets at the approval of the EFF are now presented in percent of the new GDP.

Table 2. Seychelles: Balance of Payments, 2019-26

	2019		2020		2021		2022		2023		2024		2025		2026	
	Act.	Prel.														
	Proj.															
			1st	1st	1st	1st	1st	1st	1st	1st	1st	1st	1st	1st	1st	1st
			EFF	review	EFF	review	EFF	review	EFF	review	EFF	review	EFF	review	EFF	review
(In millions of US dollars, unless otherwise indicated)																
Current account balance (+ surplus; - deficit)	-255	-313	-331	-273	-386	-388	-384	-386	-378	-375	-393	-381	-397	-404		
(percent of GDP)	-15.2	-25.4	-21.1	-20.0	-22.0	-20.9	-19.7	-18.8	-17.7	-16.6	-16.8	-15.5	-15.3	-15.0		
Balance of goods and services (+ surplus; - deficit)	-189	-234	-262	-213	-313	-309	-277	-287	-251	-274	-260	-275	-252	-285		
Exports of goods	483	420	479	447	506	479	565	503	600	520	651	558	706	591		
Of which: oil re-exports	153	96	133	116	122	125	151	129	158	130	166	136	175	140		
Of which: tuna exports	203	252	267	286	283	300	303	315	322	328	345	344	369	358		
Imports of goods	1,120	853	964	908	1,122	1,109	1,246	1,218	1,390	1,336	1,537	1,461	1,677	1,616		
Of which: oil imports	204	164	189	188	208	203	248	230	259	238	272	252	301	258		
Exports of services	1,126	683	743	789	937	975	1,168	1,203	1,353	1,394	1,506	1,552	1,653	1,705		
Of which: tourism earnings	590	221	247	275	378	390	525	532	610	618	696	705	787	797		
Imports of services	678	483	520	541	635	654	763	775	814	852	880	924	934	965		
Balance on primary income (+ surplus; - deficit)	-59	-66	-68	-63	-77	-88	-104	-94	-126	-99	-135	-108	-147	-120		
Of which: interest due	30	33	34	30	38	31	39	29	56	27	54	25	61	32		
transfers of profits and dividends	17	11	4	4	20	20	20	20	20	20	20	20	20	20		
Balance on secondary income (+ surplus; - deficit)	-6	-14	-1	3	5	8	-3	-5	-1	-2	3	2	2	1		
Of which: general government, net	28	18	9	15	14	19	11	13	11	12	11	13	10	12		
Capital and financial account	324	265	377	326	445	374	449	426	398	394	412	422	434	445		
Capital account	38	21	53	31	52	44	54	36	54	54	42	59	43	59		
Financial account	286	244	325	295	393	329	395	391	344	340	369	364	391	387		
Direct investment, net ¹	236	186	182	172	208	208	259	259	297	297	335	335	356	356		
Abroad	-8	-7	-7	-7	-7	-7	-7	-7	-7	-7	-7	-7	-7	-7		
In Seychelles	228	179	175	165	201	201	251	251	290	290	328	328	350	350		
Of which: offshore sector	0	0	0	0	0	0	0	0	0	0	0	0	0	0		
Portfolio investment, net	-11	-105	7	-38	3	-12	3	-12	3	-12	6	-12	6	-12		
Other investment, net	61	163	136	161	182	133	133	144	43	55	28	41	29	43		
Government and government-guaranteed	11	-3	137	29	137	34	103	60	-21	-24	-26	-37	-25	-35		
Disbursements	43	35	179	71	190	86	156	111	35	32	32	19	31	19		
Project loans	43	4	38	7	55	28	51	35	32	25	32	19	31	19		
Program loans	0	31	141	64	135	58	105	77	3	7	0	0	0	0		
World Bank		21	53	44	32	28	40	22	3	7	0	0	0	0		
African Development Bank		10	20	20	30	20	30	20	0	0	0	0	0	0		
Bilateral Budget Support			68	0	73	10	35	35								
Amortization	-32	-38	-42	-42	-53	-52	-52	-52	-56	-55	-57	-56	-56	-55		
Others	49	167	-1	132	45	100	30	84	64	79	54	78	53	78		
Net errors and omissions	0	0	0	0	0	0	0	0	0	0	0	0	0	0		
Overall balance	69	-48	46	53	60	-15	65	40	20	19	19	41	37	41		
Financing	-69	48	-46	-53	-60	15	-65	-40	-20	-19	-19	-41	-37	-41		
Change in net international reserves (increase: -)	-69	48	-46	-53	-60	15	-65	-40	-20	-19	-19	-41	-37	-41		
Change in gross official reserves (increase: -)	-62	23	-110	-116	-73	1	-71	-47	-1	0	-9	-31	-23	-27		
Change in liabilities to IMF, net	-7	25	64	63	14	13	7	7	-19	-19	-10	-10	-14	-14		
Purchases/drawings	0	32	69	69	19	19	19	19	0	0	0	0	0	0		
Repurchases/repayments	7	7	6	6	5	5	12	12	19	19	10	10	14	14		
Other net foreign assets (increase: -)	0	0	0	0	0	0	0	0	0	0	0	0	0	0		
Exceptional financing	0	0	0	0	0	0	0	0	0	0	0	0	0	0		
Financing gap	0	0	0	0	0	0	0	0	0	0	0	0	0	0		
<i>Memorandum items:</i>																
Exports G&S growth, percent	-4.2	-31.5	12.2	12.1	18.0	17.6	20.1	17.4	12.7	12.2	10.4	10.2	9.3	8.8		
Tourism growth, percent	5.5	-62.5	11.5	24.3	53.0	41.7	39.1	36.4	16.2	16.2	14.1	14.1	13.0	13.0		
Exports of goods volume growth, percent	-8.0	4.5	-1.7	-16.6	2.3	5.3	11.4	10.9	6.4	4.6	8.7	8.4	6.8	4.3		
Imports G&S growth, percent	-3.6	-25.7	10.3	8.4	18.3	21.7	14.4	13.1	9.7	9.8	9.7	9.0	8.0	8.2		
Imports of goods volume growth, percent	-3.7	-16.9	0.9	-12.7	17.6	21.0	11.2	11.5	10.7	9.5	9.8	9.1	8.2	10.4		
Exports G&S, percent of GDP	96	90	95	90	82	78	89	83	92	85	93	86	92	85		
Imports G&S, percent of GDP	107	109	115	106	100	95	103	97	104	97	104	97	102	96		
FDI, percent of GDP ¹	14.1	15.1	11.6	12.6	11.9	11.2	13.2	12.6	13.9	13.2	14.3	13.6	13.8	13.2		
Gross official reserves (stock, e.o.p.) ²	581	559	670	675	743	673	815	720	816	720	824	751	848	778		
(Months of imports of goods & services)	5.2	4.6	4.6	4.6	4.4	4.1	4.4	3.9	4.0	3.6	3.8	3.5	3.9	3.6		
Percentage of IMF reserve adequacy metric	112	110	114	113	116	108	117	108	111	104	107	105	105	104		
Government and government-guaranteed external debt	443	488	714	595	882	660	992	728	950	684	912	635	871	583		
(Percent of GDP)	26.4	48.7	45.4	43.5	50.2	35.5	50.8	35.4	44.5	30.4	38.9	25.9	33.7	21.7		
GDP (Millions of U.S. dollars)	1,681	1,231	1,572	1,368	1,755	1,860	1,953	2,058	2,138	2,250	2,343	2,453	2,588	2,689		

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

¹Per STA recommendations, renewals of off-shore licenses are excluded.²The level of GIRs computed from the BOP includes the budget support

Table 3a. Seychelles: Consolidated Government Operations, 2019-26¹
(Millions of Seychelles Rupees)

	2019	2020	2021		2022		2023		2024		2025		2026	
	Act.	Prel.					Proj.							
			1st	1st	1st	1st	1st	1st	1st	1st	1st	1st	1st	1st
			EFF	review	EFF	review	EFF	review	EFF	review	EFF	review	EFF	review
(Millions of Seychelles rupees)														
Total revenue and grants	8,435	7,543	8,209	8,120	9,422	9,663	10,506	10,578	11,779	11,835	12,901	12,992	14,048	14,202
Total revenue	8,341	7,156	7,252	7,514	8,677	8,923	9,899	9,953	11,307	11,085	12,430	12,251	13,580	13,474
Tax	7,425	6,369	6,601	6,692	7,688	7,863	8,739	8,908	10,070	9,999	11,419	11,329	12,466	12,493
Personal income tax	975	1,023	1,014	996	1,163	1,162	1,328	1,292	1,536	1,455	1,639	1,606	1,806	1,777
Trade tax	313	260	285	233	345	289	431	352	570	512	648	588	746	676
Excise tax	1,385	1,268	1,317	1,226	1,549	1,554	1,778	1,672	2,009	1,838	2,247	2,094	2,437	2,359
Goods and services tax (GST) / VAT	2,594	2,117	2,618	2,320	2,950	2,951	3,394	3,242	3,646	3,340	3,965	3,698	4,278	3,992
Business tax	1,397	1,204	1,002	1,433	1,189	1,437	1,389	1,845	1,662	2,146	2,027	2,419	2,220	2,651
Corporate Social Responsibility Tax (CSR)	109	102	82	58	0	0	0	0	0	0	0	0	0	0
Marketing Tourism Tax (MTT)	71	62	27	62	61	68	67	74	122	187	172	241	190	293
Other	580	334	215	324	432	353	352	380	526	520	721	682	789	745
Nontax	916	787	652	822	989	1,060	1,160	1,046	1,237	1,086	1,011	922	1,114	981
Fees and charges	340	263	291	365	457	325	504	396	545	408	499	420	539	402
Dividends from parastatals	477	414	285	321	341	590	445	590	481	618	301	442	365	519
Other	99	110	76	136	191	61	210	60	210	60	210	60	210	60
External grants	94	387	957	607	745	740	607	625	473	750	471	741	467	728
Expenditure and net lending	8,379	11,440	11,411	10,443	11,441	10,607	11,333	10,380	11,911	11,459	12,824	12,498	13,809	13,564
Current expenditure	7,509	10,037	9,166	8,887	9,284	8,783	9,537	8,708	10,331	9,447	10,821	10,189	11,647	11,040
Primary current expenditure	6,950	9,397	8,254	8,222	8,569	8,071	8,839	8,012	9,333	8,827	9,886	9,577	10,717	10,451
Wages and salaries ²	2,507	2,845	2,962	2,930	3,137	3,097	3,158	3,100	3,442	3,359	3,717	3,628	4,015	3,918
Goods and services ²	2,793	2,915	3,148	3,067	3,268	3,030	3,361	2,969	3,525	3,214	3,697	3,446	3,991	3,709
Transfers ²	1,612	3,607	2,108	2,174	2,129	1,897	2,281	1,903	2,255	2,040	2,351	2,182	2,582	2,338
Social program of central government	162	1,512	449	486	190	303	193	298	201	357	209	441	242	508
Transfers to public sector from central government	92	435	224	248	344	149	468	140	409	55	443	59	478	63
Benefits and programs of Social Security Fund	1,358	1,660	1,436	1,440	1,595	1,445	1,620	1,465	1,645	1,628	1,699	1,682	1,861	1,766
Other	39	31	35	51	35	47	38	41	112	214	121	321	130	486
Interest due	559	640	912	665	715	711	698	696	998	620	935	612	930	590
Foreign interest	237	292	355	228	309	199	340	184	589	157	567	142	544	126
Domestic interest	322	348	557	438	406	512	359	512	409	462	367	470	386	463
Capital expenditure	671	1,032	1,797	1,238	1,946	1,696	1,719	1,613	1,724	1,754	1,790	1,869	1,813	1,973
Domestically financed	225	599	606	597	748	730	895	602	967	721	1,048	849	1,090	971
Foreign financed	446	432	1,191	641	1,198	966	825	1,011	757	1,033	742	1,020	723	1,002
Net lending	149	222	397	266	161	78	27	9	-194	108	164	300	295	400
Contingency	50	149	50	53	50	50	50	50	150	150	50	140	54	151
Primary balance	615	-3,257	-2,289	-1,658	-1,304	-232	-129	893	866	995	1,012	1,106	1,168	1,227
Overall balance, commitment basis ³	56	-3,897	-3,201	-2,323	-2,019	-943	-827	198	-132	376	77	494	238	638
Change in float	-252	-189	0	0	0	0	0	0	0	0	0	0	0	0
Overall balance, cash basis (after grants)	-196	-4,086	-3,201	-2,323	-2,019	-943	-827	198	-132	376	77	494	238	638
Financing	196	4,086	3,201	2,323	2,019	943	827	-198	132	-376	-77	-494	-238	-638
Foreign financing	-45	652	3,669	1,535	2,251	705	1,632	987	-594	-635	-522	-687	-551	-702
Disbursements	352	1,176	4,546	2,132	3,125	1,566	2,596	1,938	519	465	459	279	441	274
Project loans	352	46	704	116	828	424	752	518	475	362	459	279	441	274
Program/budget support	0	1,130	3,842	2,016	2,297	1,142	1,844	1,420	44	103	0	0	0	0
Of which RFI	0	535	0	0	0	0	0	0	0	0	0	0	1	1
Scheduled amortization	-397	-523	-878	-597	-873	-862	-964	-952	-1,114	-1,100	-981	-966	-993	-976
Of which Paris Club buy-back	...	...	...	...	...	...	...	...	...	...	...	...	...	...
Domestic financing, net	237	3,176	-555	788	-334	155	-932	-1,270	726	172	445	194	313	65
Bank financing	110	2,700	-500	709	-300	139	-1,000	-1,338	653	154	401	174	282	58
CBS	185	1,071	0	0	0	450	0	0	0	0	0	0	0	0
Commercial banks	-75	1,629	-500	709	-300	-311	-1,000	-1,338	653	154	401	174	282	58
Nonbank financing	126	476	-56	79	-33	15	68	68	73	17	45	19	31	6
Privatization and long-term lease of fixed assets	0	0	88	0	101	84	127	86	0	88	0	0	0	0
Statistical discrepancy	5	257	0	0	0	0	0	0	0	0	0	0	0	0
<i>Memorandum item:</i>														
External debt service due	634	816	1,233	825	1,182	1,061	1,304	1,136	1,702	1,258	1,549	1,108	1,537	1,103

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

¹ The fiscal program targets at the approval of the EFF are now presented in percent of the new GDP. Data include the central government and the social security system.

² From 2015 onwards, wage and salaries and goods and services (to be) spent by government agencies other than Ministries are reclassified into these items from transfers.

³ Only interest payments on foreign debt are on a commitment basis. Other expenditures are recorded when checks are issued or transfers initiated.

Table 3b. Seychelles: Consolidated Government Operations, 2019-26¹
(Percent of GDP)

	2019	2020	2021		2022		2023		2024		2025		2026	
	Act.	Prel.	1st		1st		1st		1st		1st		1st	
			EFF	review	EFF	review	EFF	review	EFF	review	EFF	review	EFF	review
Total revenue and grants	35.7	34.8	32.8	32.4	33.8	34.7	34.3	34.6	35.6	35.8	36.2	36.5	36.7	37.1
Total revenue	35.3	33.0	29.0	30.0	31.2	32.1	32.4	32.5	34.2	33.5	34.9	34.4	35.4	35.2
Tax	31.5	29.4	26.4	26.7	27.6	28.2	28.6	29.1	30.4	30.2	32.1	31.8	32.5	32.6
Personal income tax	4.1	4.7	4.1	4.0	4.2	4.2	4.3	4.2	4.6	4.4	4.6	4.5	4.7	4.6
Trade tax	1.3	1.2	1.1	0.9	1.2	1.0	1.4	1.2	1.7	1.5	1.8	1.7	1.9	1.8
Excise tax	5.9	5.9	5.3	4.9	5.6	5.6	5.8	5.5	6.1	5.6	6.3	5.9	6.4	6.2
Goods and services tax (GST) / VAT	11.0	9.8	10.5	9.3	10.6	10.6	11.1	10.6	11.0	10.1	11.1	10.4	11.2	10.4
Business tax	5.9	5.6	4.0	5.7	4.3	5.2	4.5	6.0	5.0	6.5	5.7	6.8	5.8	6.9
Corporate Social Responsibility Tax (CSR)	0.5	0.5	0.3	0.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Marketing Tourism Tax (MTT)	0.3	0.3	0.1	0.2	0.2	0.2	0.2	0.2	0.4	0.6	0.5	0.7	0.5	0.8
Other	2.5	1.5	0.9	1.3	1.6	1.3	1.2	1.2	1.6	1.6	2.0	1.9	2.1	1.9
Nontax	3.9	3.6	2.6	3.3	3.6	3.8	3.8	3.4	3.7	3.3	2.8	2.6	2.9	2.6
Fees and charges	1.4	1.2	1.2	1.5	1.6	1.2	1.6	1.3	1.6	1.2	1.4	1.2	1.4	1.0
Dividends from parastatals	2.0	1.9	1.1	1.3	1.2	2.1	1.5	1.9	1.5	1.9	0.8	1.2	1.0	1.4
Other	0.4	0.5	0.3	0.5	0.7	0.2	0.7	0.2	0.6	0.2	0.6	0.2	0.5	0.2
External grants	0.4	1.8	3.8	2.4	2.7	2.7	2.0	2.0	1.4	2.3	1.3	2.1	1.2	1.9
Expenditure and net lending	35.5	52.8	45.6	41.7	41.1	38.1	37.0	33.9	36.0	34.6	36.0	35.1	36.0	35.4
Current expenditure	31.8	46.3	36.6	35.5	33.3	31.5	31.2	28.5	31.2	28.6	30.4	28.6	30.4	28.8
Primary current expenditure	29.4	43.4	33.0	32.8	30.8	29.0	28.9	26.2	28.2	26.7	27.8	26.9	28.0	27.3
Wages and salaries	10.6	13.1	11.8	11.7	11.3	11.1	10.3	10.1	10.4	10.2	10.4	10.2	10.5	10.2
Goods and services	11.8	13.5	12.6	12.3	11.7	10.9	11.0	9.7	10.7	9.7	10.4	9.7	10.4	9.7
Transfers	6.8	16.6	8.4	8.7	7.6	6.8	7.5	6.2	6.8	6.2	6.6	6.1	6.7	6.1
Social program of central government	0.7	7.0	1.8	1.9	0.7	1.1	0.6	1.0	0.6	1.1	0.6	1.2	0.6	1.3
Transfers to public sector from central government	0.4	2.0	0.9	1.0	1.2	0.5	1.5	0.5	1.2	0.2	1.2	0.2	1.2	0.2
Benefits and programs of Social Security Fund	5.8	7.7	5.7	5.8	5.7	5.2	5.3	4.8	5.0	4.9	4.8	4.7	4.9	4.6
Other	0.2	0.1	0.1	0.2	0.1	0.2	0.1	0.1	0.3	0.6	0.3	0.9	0.3	1.3
Interest due	2.4	3.0	3.6	2.7	2.6	2.6	2.3	2.3	3.0	1.9	2.6	1.7	2.4	1.5
Foreign interest	1.0	1.3	1.4	0.9	1.1	0.7	1.1	0.6	1.8	0.5	1.6	0.4	1.4	0.3
Domestic interest	1.4	1.6	2.2	1.7	1.5	1.8	1.2	1.7	1.2	1.4	1.0	1.3	1.0	1.2
Capital expenditure	2.8	4.8	7.2	4.9	7.0	6.1	5.6	5.3	5.2	5.3	5.0	5.2	4.7	5.1
Domestically financed	1.0	2.8	2.4	2.4	2.7	2.6	2.9	2.0	2.9	2.2	2.9	2.4	2.8	2.5
Foreign financed	1.9	2.0	4.8	2.6	4.3	3.5	2.7	3.3	2.3	3.1	2.1	2.9	1.9	2.6
Net lending	0.6	1.0	1.6	1.1	0.6	0.3	0.1	0.0	-0.6	0.3	0.5	0.8	0.8	1.0
Contingency	0.2	0.7	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.5	0.1	0.4	0.1	0.4
Primary balance	2.6	-15.0	-9.1	-6.6	-4.7	-0.8	-0.4	2.9	2.6	3.0	2.8	3.1	3.0	3.2
Overall balance, commitment basis ²	0.2	-18.0	-12.8	-9.3	-7.3	-3.4	-2.7	0.6	-0.4	1.1	0.2	1.4	0.6	1.7
Change in arrears	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	0.0
Change in float	-1.1	-0.9	0.0	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)	-0.8	-18.9	-12.8	-9.3	-7.3	-3.4	-2.7	0.6	-0.4	1.1	0.2	1.4	0.6	1.7
Financing	0.8	18.9	12.8	9.3	7.3	3.4	2.7	-0.6	0.4	-1.1	-0.2	-1.4	-0.6	-1.7
Foreign financing	-0.2	3.0	14.7	6.1	8.1	2.5	5.3	3.2	-1.8	-1.9	-1.5	-1.9	-1.4	-1.8
Disbursements	1.5	5.4	18.2	8.5	11.2	5.6	8.5	6.3	1.6	1.4	1.3	0.8	1.2	0.7
Project loans	1.5	0.2	2.8	0.5	3.0	1.5	2.5	1.7	1.4	1.1	1.3	0.8	1.2	0.7
Program/budget support	0.0	5.2	15.3	8.1	8.3	4.1	6.0	4.6	0.1	0.3	0.0	0.0	0.0	0.0
Of which RFI	0.0	2.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Scheduled amortization	-1.7	-2.4	-3.5	-2.4	-3.1	-3.1	-3.2	-3.1	-3.4	-3.3	-2.8	-2.7	-2.6	-2.5
Of which Paris Club buy-back														0.0
Domestic financing, net	1.0	14.7	-2.2	3.1	-1.2	0.6	-3.2	-4.2	2.2	0.5	1.3	0.5	0.8	0.2
Bank financing	0.5	12.5	-2.0	2.8	-1.1	0.5	-3.5	-4.4	2.0	0.5	1.2	0.5	0.7	0.2
CBS	0.8	4.9	0.0	0.0	0.0	1.6	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Commercial banks	-0.3	7.5	-2.0	2.8	-1.1	-1.1	-3.5	-4.4	2.0	0.5	1.2	0.5	0.7	0.2
Nonbank	0.5	2.2	-0.2	0.3	-0.1	0.1	0.2	0.2	0.2	0.1	0.1	0.1	0.1	0.0
Privatization and long-term lease of fixed assets	0.0	0.0	0.4	0.0	0.4	0.3	0.4	0.3	0.0	0.3	0.0	0.0	0.0	0.0
Statistical discrepancy	0.0	1.2	0.0	0.0	0.0	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)	23,603	21,664	23,585	25,034	26,219	27,841	28,889	30,595	31,235	33,087	33,781	35,611	36,464	38,328

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

¹ The fiscal program targets at the approval of the EFF are now presented in percent of the new GDP. Data include the central government and the social security system. into these items from transfers.

² Only interest payments on foreign debt are on a commitment basis. Other expenditures are recorded when checks are issued or transfers initiated.

Table 4. Seychelles: Depository Corporations Survey and Central Bank Accounts, 2016-2021

	2016	2017	2018	2019	2020	2021	2021
	Act.	Act.	Act.	Act.	Act.	Mar. Act.	Jun. Act.
(Millions of Seychelles rupees)							
Depository corporations survey							
Net foreign assets	9,817	10,754	11,948	12,647	18,612	17,957	16,710
Central bank	6,550	6,982	7,248	7,807	11,685	10,661	8,370
Deposit money banks	3,267	3,771	4,700	4,841	6,927	7,296	8,340
Net domestic assets	3,831	5,134	5,166	6,847	6,566	6,249	8,417
Domestic credit	7,110	8,476	8,620	10,562	14,609	13,810	13,700
Net claims on the government	1,791	2,209	1,699	1,882	4,175	3,522	4,381
<i>Of which</i> : Government deposits at the Central Bank	-3,355	-3,355	-2,829	-2,513	-1,638	-2,382	-1,875
<i>Of which</i> : Change in monetary debt ¹	-191	670.0	394.1	219.2	149.0	0.0	0.0
Credit to the economy	5,319	6,267	6,921	8,680	10,434	10,289	9,319
<i>Of which</i> : credit to the private sector	5,122	6,032	6,727	8,229	9,888	9,779	8,898
Other items, net	-3,279	-3,342	-3,453	-3,715	-8,043	-7,562	-5,284
Broad money	13,648	15,888	17,115	19,494	25,179	24,206	25,127
Currency in circulation	1,026	1,116	1,169	1,228	1,460	1,463	1,440
Foreign currency deposits	5,029	6,115	7,060	7,987	11,810	11,300	11,704
Local currency deposits	7,592	8,657	8,886	10,278	11,909	11,443	11,983
Central bank							
Net foreign assets	6,550	6,982	7,248	7,807	11,685	10,661	8,370
Foreign assets	7,059	7,560	7,731	8,191	12,144	11,118	8,830
Foreign liabilities	508	578	483	384	458	457	460
Net domestic assets	-3,558	-3,423	-3,528	-3,242	91	-83	1,420
Domestic credit	-2,855	-2,629	-2,651	-2,318	4,247	3,820	3,260
Government (net)	-2,170	-1,731	-1,644	-1,328	-453	-1,197	-662
Commercial banks	-610	-705	-845	-873	4,865	5,149	4,036
Other (parastatals)	-75	-192	-162	-117	-166	-132	-114
Other items, net	-703	-794	-877	-925	-4,156	-3,903	-1,840
Reserve money	2,992	3,559	3,720	4,564	6,408	5,502	6,097
Currency in circulation	1,026	1,116	1,169	1,228	1,460	1,463	1,440
Commercial bank reserves (includes cash in vault)	1,966	2,443	2,551	3,336	4,947	4,039	4,657
<i>Of which</i> : vault cash	193	212	...	...	...	...	...
<i>Of which</i> : excess reserves (excl. bank vault cash)	9	182	...	...	...	...	...
<i>Of which</i> : required reserves in foreign currency	703	841	924	924	924	924	924
required reserves in domestic currency	1,061	1,208	1,346	1,595	1,844	1,907	1,967
Memorandum items:							
Gross official reserves (millions of U.S. dollars)	523	546	548	580	559	588	617
Foreign currency deposits (millions of U.S. dollars)	372	442	503	567	638	618	648
Broad money growth (12-month percent change)	12.1	16.4	7.7	13.9	29.2	...	...
Credit to the private sector (12-month percent change)	10.3	17.8	11.5	22.3	20.2	...	...
Reserve money (end-of-period; 12-month percent change)	14.5	18.9	4.5	22.7	40.4	...	...
Reserve money (daily average over quarter; 12-month percent change)	10.4	19.0	...	...	...	...	...
Money multiplier (broad money/reserve money)	4.6	4.5	4.6	4.3	3.9	...	...
Velocity (GDP/broad money; end-of-period)	1.5	1.4	1.3	1.2	1.2	...	...
Sources: Central Bank of Seychelles; and IMF staff estimates and projections.							
¹ Negative shows accumulation, positive shows retiring (debt that is not rolled over)							

Table 5. Seychelles: Financial Soundness Indicators for the Banking Sector, 2013 – 2021Q2

	2016	2017	2018	2019	2020	2021 Q1	2021 Q2
	(Percent, end-of-period)						
Capital adequacy							
Regulatory capital to risk weighted assets	26.6	23.5	20.5	19.5	17.1	18.8	19.7
Regulatory tier 1 capital to risk weighted assets	20.4	18.1	16.8	16.2	14.1	14.5	17.2
Capital to assets (net worth)	11.8	11.0	10.1	9.9	8.4	8.2	9.0
Net tangible capitalization ¹	12.0	11.2	10.1	10.0	8.5	8.3	9.1
Asset quality							
Foreign exchange loans to total loans	25.0	27.7	24.2	26.0	36.4	35.0	30.0
Non-performing loans to gross loans	6.8	7.1	3.5	2.7	3.3	4.4	5.0
Provision as percentage of non-performing loans	37.4	31.9	19.2	25.1	38.3	28.0	29.9
Provisions as percentage of total loans	2.5	2.3	0.7	0.7	1.3	1.2	1.5
Earnings and profitability							
Return on assets (annualized)	3.8	3.9	3.7	2.5	1.0	1.9	1.5
Return on equity (annualized)	32.7	35.1	35.7	24.0	11.5	22.8	17.0
Interest margin to gross income	62.7	53.1	54.5	62.6	58.3	67.3	74.9
Noninterest expense to gross income	45.5	49.7	55.9	57.7	55.3	62.1	69.9
Net interest margin (annualized) ²	4.6	4.1	4.2	9.4	7.4	1.8	3.7
Net noninterest margin (annualized) ³	-1.0	-0.2	-0.8	-3.1	-1.7	-0.8	-2.2
Expense to income	55.2	54.2	61.4	63.7	60.7	66.5	74.0
Interest expense to gross income	10.7	12.5	14.4	16.6	13.6	13.4	15.7
Liquidity							
Core liquid assets to total assets ⁴	28.6	38.2	45.2	44.1	44.1	38.1	41.0
Broad liquid assets to total assets ⁵	47.9	55.4	58.2	55.3	57.3	52.5	57.7
Liquid assets (broad) to short term liabilities	55.0	62.4	63.7	60.6	62.3	58.0	64.4
Liquid assets (broad) to total liabilities	54.3	62.2	64.7	61.6	62.5	57.2	63.2
Liquid assets to deposit liabilities	57.8	65.7	68.5	65.3	67.8	61.3	68.2
Foreign exchange exposure							
Net open foreign exchange position to capital	3.0	0.0	3.4	2.4	-0.1	14.3	-4.1

Source: Central Bank of Seychelles.

¹ Defined as: equity capital/(assets-interest in suspense-provisions).² Defined as: (Interest income - interest expense)/average assets.³ Defined as: (Noninterest income - noninterest expense)/average assets.⁴ Core liquid assets include cash, balances with CBS, and deposits with other banks.⁵ Broad liquid assets include core liquid assets plus investments in government securities.

Table 6. Seychelles: Schedule of Purchases Under the EFF Arrangement

Date Available	Amount	% of Quota	Conditions Necessary for Disbursement
July 29, 2021	SDR 24 million	104.8	Executive Board approval of the EFF arrangement.
December 1, 2021	SDR 24 million	104.8	Observance of end-July 2021 performance criteria, and completion of the first review under the arrangement.
June 1, 2022	SDR 6.5 million	28.4	Observance of end-December 2021 performance criteria, and completion of the second review under the arrangement.
December 1, 2022	SDR 6.5 million	28.4	Observance of end-June 2022 performance criteria, and completion of the third review under the arrangement.
June 1, 2023	SDR 6.5 million	28.4	Observance of end-December 2022 performance criteria, and completion of the fourth review under the arrangement.
December 1, 2023	SDR 6.5 million	28.4	Observance of end-June 2023 performance criteria, and completion of the fifth review under the arrangement.
Total	SDR 74 million	323	

Source: IMF staff estimates.

Table 7. Seychelles: Indicators of Fund Credit, 2016-2032

	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032
	(Millions of SDR)																
Existing Fund credit																	
Stock ¹	28.0	29.3	24.8	19.7	37.6	33.6	29.9	21.4	8.2	1.2	0.4	0.0	0.0	0.0	0.0	0.0	0.0
Obligation	2.9	4.0	5.1	5.6	5.5	4.5	4.0	8.8	13.4	7.0	0.8	0.4	0.0	0.0	0.0	0.0	0.0
Principal (repayments/repurchases)	2.6	3.6	4.5	5.1	5.0	4.1	3.7	8.5	13.2	7.0	0.8	0.4	0.0	0.0	0.0	0.0	0.0
Charges and interest	0.3	0.4	0.5	0.5	0.5	0.4	0.3	0.3	0.2	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Disbursements	...	4.9			22.9	...	...	...	...	...	...	...	...	...	...	...	...
Prospective Fund credit																	
Disbursement	0.0	0.0	0.0	0.0	0.0	48.0	13.0	13.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Stock ¹	0.0	0.0	0.0	0.0	0.0	48.0	61.0	74.0	74.0	74.0	65.5	54.8	42.4	30.1	17.8	5.4	1.6
Obligations ²	0.0	0.0	0.0	0.0	0.0	0.4	1.4	1.8	1.8	1.5	10.2	12.0	13.1	12.7	12.6	12.5	3.8
Principal (repayments/repurchases)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	8.5	10.7	12.3	12.3	12.3	12.3	3.8
Charges and interest	0.0	0.0	0.0	0.0	0.0	0.4	1.4	1.8	1.8	1.5	1.6	1.2	0.8	0.4	0.3	0.2	0.1
Stock of existing and prospective Fund credit¹																	
	28.0	29.3	24.8	19.7	37.6	81.6	90.9	95.4	82.2	75.2	65.9	54.8	42.4	30.1	17.8	5.4	1.6
In percent of quota	122.2	128.0	108.2	86.0	164.3	356.2	396.8	416.6	358.9	328.5	287.6	239.1	185.2	131.4	77.6	23.7	7.2
In percent of GDP	2.6	2.6	2.2	1.7	4.4	8.6	7.1	6.7	5.3	4.4	3.5	2.7	2.0	1.3	0.7	0.2	0.1
In percent of Government Revenues					12.5	26.6	20.4	19.4	14.8	12.2	9.6	7.4	5.3	3.5	1.9	0.5	0.2
In percent of exports of goods and services	2.9	2.7	2.1	1.8	4.9	9.5	9.0	8.1	6.2	5.2	3.7	2.8	2.0	1.3	0.7	0.2	0.1
In percent of gross reserves	7.6	7.6	6.5	4.9	9.6	17.5	19.5	19.2	16.5	14.5	12.2	9.4	6.8	4.4	2.4	0.7	0.2
Obligations to the Fund from existing and prospective Fund arrangements																	
Disbursements	0.0	4.9	0.0	0.0	22.9	48.0	13.0	13.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Obligations	2.9	4.0	5.1	5.6	5.5	4.8	5.4	10.5	15.2	8.5	11.0	12.4	13.1	12.7	12.6	12.5	3.8
Principal (repayments/repurchases)	2.6	3.6	4.5	5.1	5.0	4.1	3.7	8.5	13.2	7.0	9.4	11.1	12.3	12.3	12.3	12.3	3.8
Charges and interest	0.3	0.5	0.5	0.5	0.5	0.8	1.7	2.1	1.9	1.6	1.6	1.2	0.8	0.4	0.3	0.2	0.1
In percent of quota ³	12.7	17.6	22.1	24.5	23.9	21.2	23.5	45.9	66.2	37.1	48.0	54.0	57.2	55.6	55.1	54.5	16.8
In percent of GDP	0.3	0.4	0.4	0.5	0.6	0.5	0.4	0.7	1.0	0.5	0.6	0.6	0.6	0.5	0.5	0.5	0.1
In percent of Government Revenues					1.8	1.6	1.2	2.1	2.7	1.4	1.6	1.7	1.6	1.5	1.3	1.2	0.4
In percent of exports of goods and services	0.3	0.4	0.4	0.5	0.7	0.6	0.5	0.9	1.1	0.6	0.6	0.6	0.6	0.6	0.5	0.5	0.1
In percent of gross reserves	0.8	1.1	1.3	1.4	1.4	1.0	1.2	2.1	3.0	1.6	2.0	2.1	2.1	1.9	1.7	1.6	0.4

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

¹ End-of-period.² Repayment schedule based on repurchase obligations. Obligations to the Fund from Existing and Prospective Fund Arrangements includes charges.³ Effective February 2016, the new quota of SDR 22.9 million is applied.

Table 8. Seychelles: Decomposition of Public Debt and Debt Service by Creditor, 2020-22¹

	Debt Stock (end of period)			Debt Service					
	2020			2020	2021	2022	2020	2021	2022
	(In US\$ million)	(Percent total debt)	(Percent GDP)	(In US\$ million)			(Percent GDP)		
Total	924.5	100	75.1	358.7	583.5	286.4	29.1	42.7	15.4
External	489.2	52.9	39.7	55.3	55.8	60.4	4.5	4.1	3.2
Multilateral creditors ^{2,3}	255.5	27.6	20.8	16.7	18.5	19.9	1.4	1.4	1.1
IMF	54.1	5.9	4.4						
World Bank	69.7	7.5	5.7						
AfDB	64.3	7.0	5.2						
Other Multilaterals	67.3	7.3	5.5						
o/w: EIB	37.1	4.0	3.0						
o/w: BADEA	19.5	2.1	1.6						
Bilateral Creditors ²	107.1	11.6	8.7	10.4	10.3	14.7	0.8	0.8	0.8
Paris Club	56.5	6.1	4.6	2.2	2.3	6.0	0.2	0.2	0.3
o/w: France	30.8	3.3	2.5						
o/w: UK	6.5	0.7	0.5						
Non-Paris Club	50.6	5.5	4.1	8.2	8.1	8.8	0.7	0.6	0.5
o/w: China	18.3	2.0	1.5						
o/w: Saudi Arabia	13.8	1.5	1.1						
Bonds	107.9	11.7	8.8	26.3	25.0	23.6	2.1	1.8	1.3
Commercial creditors	18.7	2.0	1.5	2.0	2.0	2.2	0.2	0.1	0.1
o/w: Nedbank	10.0	1.1	0.8						
o/w: Habib Bank	4.6	0.5	0.4						
o/w: MCB	4.1	0.4	0.3						
Domestic	435.4	47.1	35.4	303.4	527.6	226.0	24.7	38.6	12.1
Held by residents, total	435.4	47.1	35.4	303.4	527.6	226.0	24.7	38.6	12.1
Held by non-residents, total	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
T-Bills	260.3	28.2	21.2	300.7	518.6	207.6	24.4	37.9	11.2
Bonds	92.5	10.0	7.5	0.0	5.0	14.3	0.0	0.4	0.8
Loans	82.5	8.9	6.7	2.7	4.1	4.1	0.2	0.3	0.2
Memo items:									
Collateralized debt ⁴	0.0								
o/w: Related									
o/w: Unrelated									
Contingent liabilities									
o/w: External public guarantees	9.7								
o/w: Domestic Public guarantees	39.4								
o/w: Other explicit contingent liabilities ⁵									
Nominal GDP	1230.9								

1/As reported by Seychelles authorities according to their classification of creditors, including by official and commercial. Debt coverage is the same as the DSA.

2/Some public debt is not shown in the table due to [confidentiality clauses/capacity constraints].

3/Multilateral creditors² are simply institutions with more than one official shareholder and may not necessarily align with creditor classification under other IMF policies (e.g. Lending Into Arrears)

4/Debt is collateralized when the creditor has rights over an asset or revenue stream that would allow it, if the borrower defaults on its payment obligations, to rely on the asset or revenue stream to secure repayment of the debt. Collateralization entails a borrower granting liens over specific existing assets or future receivables to a lender as security against repayment of the loan. Collateral is "unrelated" when it has no relationship to a project financed by the loan. An example would be borrowing to finance the budget deficit, collateralized by oil revenue receipts. See the joint IMF-World Bank note for the G20 "Collateralized Transactions: Key Considerations for Public Lenders and Borrowers" for a discussion of issues raised by collateral.

5/Includes other one-off guarantees not included in publicly guaranteed debt (e.g. credit lines) and other explicit contingent liabilities not elsewhere classified (e.g. potential legal claims, payments resulting from PPP arrangements).

Annex I. Risk Assessment Matrix (RAM)¹

Source of Risks	Relative Likelihood/ Time Horizon	Excepted Impact if Realized	Recommended Policy Response
External Risks			
Protracted delay in tourism recovery-from traditional markets.	Medium	High	Develop a contingency plan that would lower the impact of a delayed economic recovery: Authorities could consider further fiscal consolidation and reliance on concessional financing in case such risk materialize.
	Short to Medium term	A protracted delay in tourism arrivals from the main European countries could hamper the planned tourism and economic recovery during the first half of 2021.	
Protracted delay in tourism recovery-from new markets.	Medium	High	Develop a contingency plan that would lower the impact of a delayed economic recovery: Authorities could consider further fiscal consolidation and reliance on concessional financing in case such risk materialize.
	Short to Medium Term	An unexpected drop in tourism arrivals from new markets (Israel, Russia) could hamper the planned tourism and economic recovery during the first half of 2021.	
Shortfall of external financing	Medium	High	Develop a contingency plan that would lower the impact of a shortfall in external financing: Authorities could consider further fiscal consolidation and debt restructuring.
	Short Term to Medium Term	A shortfall of external financing could imply high GFNs for several years.	
Domestic Risks			
Vaccines could prove less effective than expected	Low	Medium	Rely predominantly on concessional financing; optimize debt portfolio; adjust public investment level to reduce borrowing needs, if necessary
	Short to Medium Term	Low effectiveness in vaccines could further disrupt domestic activity and tourism recovery.	
Natural disasters related to climate change could happen.	Low	Medium	Prioritize the implementation of projects related to climate change.
	Short to Medium Term	The materialization of risks related to natural disasters could trigger further public expenditures and alter the planned reduction of public debt.	
Higher NPA levels in the banking sector	Medium	Medium	Encourage and facilitate prudent restructuring of loans and enhance management and monitoring of NPLs: Authorities should provide guidance on prudential treatment of moratoria and NPL management strategies, assess their implementation, and monitor the relevant reclassification of loans. Authorities should further develop detailed reporting templates for restructured and rescheduled loans and for monitoring the impact of COVID-19 measures on the asset quality of banks.
	Short to Medium Term	Higher NPA levels in the banking sector which is currently not recognized due to the regulatory forbearance could escalate further in case the economic recovery falls short of expectations.	
Materialization of contingent liabilities from Air Seychelles	Low	Medium	Implement the least costly scenario identified by the World Bank, which is the liquidation of Air Seychelles through the judicial process, which is ongoing
	Short to Medium Term	The materialization of contingent liabilities from Air Seychelles could alter the planned reduction of public debt.	

¹The Risk Assessment Matrix (RAM) shows events that could materially alter the baseline path (the scenario most likely to materialize in the view of IMF staff). The relative likelihood is the staff's subjective assessment of the risks surrounding the baseline ("low" is meant to indicate a probability below 10 percent, "medium" a probability between 10 and 30 percent, and "high" a probability between 30 and 50 percent). The RAM reflects staff views on the source of risks and overall level of concern as of the time of discussions with the authorities. Non-mutually exclusive risks may interact and materialize jointly. "Short term (ST)" and "medium term (MT)" are meant to indicate that the risk could materialize within 1 and 3 years, respectively.

Annex II. Monetary Policy Transmission Mechanism and Credit Growth

1. The effectiveness of the transmission mechanism through the interest rate channel has diminished in recent months. Between January 2020 and June 2021, in response to the reduction in the monetary policy rate by 200 basis points, the average lending rate on private sector credit declined by 312 basis points compared to a reduction in deposit rates by 75 basis points. Since July 2021, the monetary policy rate has been reduced by another 100 basis points. At the same time, in July 2021, through a structural shift of the interest rate corridor, the spread on interest rates between the Standing Credit Facility and the Standing Deposit Facility was reduced by 200 basis points. However, the average lending rate on private sector credit remained unchanged between end-June and end-September 2021.¹ In contrast, average rates on saving deposits, which were already low, declined by 37 basis points during the same period. Consequently, the average spread between lending and deposit rates, which was already high, has increased further by 36 basis points to 7.5 percent as of end-September 2021. This reflects the longstanding high wedge between deposit and lending rates in Seychelles.

2. Notwithstanding an accommodative monetary policy, bank credit to the private sector has been on a declining trend in 2021, mainly due to exchange rate effects and risk aversion for lending. Private sector credit in local currency terms declined by 7.9 percent (y-o-y at end-September 2021) mainly due to the impact of currency appreciation. Local currency credit contracted by 1.3 percent (y-o-y at end-September 2021) while foreign currency credit in US dollar terms declined by 1.8 percent. Without the impact of exchange rate appreciation, the decline in private sector credit stood lower at 1.5 percent. Credit in local currency terms declined significantly for the household sector, tourism, real estate, telecommunications and manufacturing, largely reflecting the rising incidence of NPLs in these sectors except real estate. In contrast, credit for building and construction increased sharply, while it increased moderately for mortgage lending, both of which helped offset part of the credit contraction.

3. As banks' net income has come under stress in 2021, banks may be adopting a risk-averse strategy by curtailing credit and managing NPLs through lower provisions and higher recovery of bad debt to maintain their profitability. The banking system experienced a reduction in interest income in 2021 due to payment holidays for bank borrowers, the impact of local currency appreciation on the FX loan portfolio, and the reduction in prime lending rates. Despite the reluctance of banks to extend new loans, a sentiment which prevailed during the COVID-19 outbreak through September 2021, discussions with the banks reveal that there is now a greater appetite for extending new loans, provided that the banks can preserve their asset quality.

¹ Net of the Private Sector Credit Lending Facility which provided subsidized interest rates, the average lending rates increased by 5 basis points between end-June and end-September 2021.

Annex III. Sovereign Debt Exchange Under Stressed Conditions

Introduction

1. **The Government of Seychelles on July 14, 2021, successfully executed a liability management operation (LMO) on its domestic debt through a market-based exchange.** The exchange operation involved replacing Treasury Bills (T-bills) in the domestic market with longer-term bonds and was undertaken against the backdrop of significant debt sustainability risks, including refinancing risks, and increased borrowing costs.
2. **LMOs are widely used by sovereign debt managers as part of their risk management framework, mainly for managing refinancing risks of the sovereign debt portfolio¹.** Buybacks and exchanges (or switches) are the most common tools of LMOs used to mitigate short- to medium-term refinancing risks while attempting to enhance market liquidity for cost reduction in the context of benchmark bond issuance. Advanced economies (AEs) and emerging markets (EMs) with relatively developed debt markets undertake LMOs in the domestic market as a voluntary operation by adopting market-based pricing and are part of normal debt management operations.
3. **This Annex attempts to delineate the key issues involved in implementing a domestic debt exchange under conditions of sovereign stress with elevated risks to debt sustainability.²** Section 2 provides a summary of the recent LMO implemented in Seychelles in respect of its design, performance, and impact on relevant macro-financial considerations. Section 3 briefly discuss the role of buybacks and exchanges in domestic debt markets under stressed sovereign debt conditions, setting out the key considerations involved. Section 4 concludes with some key takeaways on LMOs in domestic markets for sovereigns under stress.

Debt Exchange in Seychelles – Design and Impact

4. **Seychelles was hit hard by the COVID-19 global pandemic, resulting in elevated debt sustainability risks.** Following an economic slump due to the sudden halt in tourist arrivals, higher borrowing requirements from the fiscal shock and a sharp exchange rate depreciation, public debt spiraled to over 92 percent of GDP at the end of 2020 from 58 percent in 2019.³
5. **A legacy of reliance on short-term financing along with the COVID-19 induced fiscal shock led to heightened refinancing risks.** Gross financing needs, which were already high in 2019 at 28 percent of GDP increased sharply to 47 percent in 2020, a large part of which was financed through T-Bills. In the absence of regular bond issuance, T-Bills had been extensively issued for both

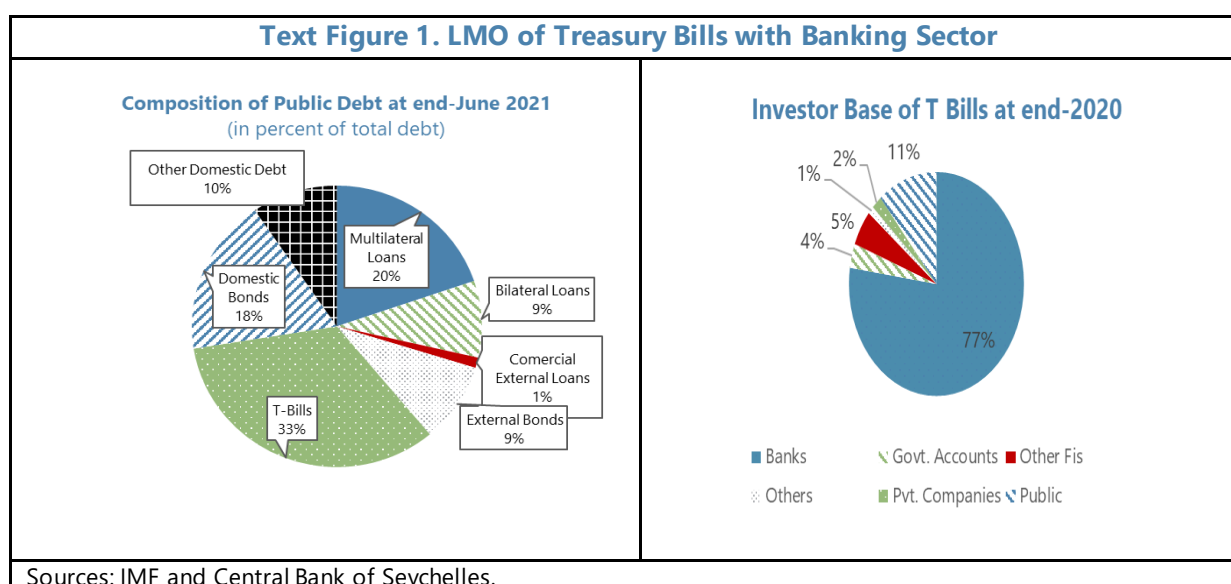
¹ Although LMO comprise other risk management tools, this paper will limit its discussion on market-based exchanges (switches) and buybacks in the domestic market which will be interchangeably used with the term LMO.

² Domestic debt in this Annex refers to debt issued under “domestic jurisdiction” and may differ with other definitions: debt denominated in local currencies or held by domestic residents, although there may be a significant overlap.

³ All debt ratios expressed as percentage of GDP are based on the revised GDP series released by the authorities in October 2021 and may therefore differ from figures reported in the EFF report in July 2021.

fiscal financing and monetary policy operations.⁴ However, with the COVID-19 induced fiscal shock and an accommodative monetary policy, T-bills were used for financing purpose only. At the end of June 2021, T-Bills accounted for one-third of the entire public debt stock (Figure 1).

6. Escalation in debt sustainability risks, particularly high refinancing risks, led to an increased risk premium on government debt along with reduced market demand. Despite the accommodative monetary policy, T-bill yields increased between December 2020 and March 2021 reflecting increased sovereign risk.⁵ Investor demand for T-bills also declined during this period with the bid-offer ratio down to 50 percent in February 2021, compared to ratios in excess of 100 percent in the preceding period. Recognizing the need to reduce the rollover risks, the authorities issued bonds through a tap mechanism in 3, 5 and 7-year maturities amounting to SCR 1.1 billion in February 2021.



Design of the LMO

7. In order to reduce refinancing risks, a multi-pronged strategy as part of the IMF program was devised to extend debt maturity and reduce costs that included a “one-off” LMO. The policy framework included: (i) a market-based operation that exchanged T-Bills into bonds amounting to 5 percent of GDP and one-fourth of T-bills stock at end-June 2021; (ii) increased recourse to concessional external loans with longer maturities by another 5 percent of

⁴ T-bills were issued in 91-day, 182-day and 365-day tenors.

⁵ Although policy rates were reduced by 200 bps during 2020, the 365-day T-Bill rates increased by 27 bps between end-December 2019 and end-March 2021.

GDP over the program period to replace relatively expensive short-term domestic debt;⁶ and (iii) a shift towards a regular domestic bond financing strategy from reliance on T-bill issuance. The LMO remained a core part of the program design since GFN would have still prevailed above 16 percent of GDP by 2026 in the absence of the LMO, although solvency risks would have been attenuated. With the reduction in sovereign risks, the LMO also had the potential to pave the way for a yield correction as the real yield on Seychelles' debt instruments exceeded the average peer country level with similar ratings ("B" for Seychelles).

8. The LMO was designed within an overall debt reduction strategy as part of the program that aimed to reduce solvency risks through economic recovery, a backloaded fiscal adjustment, and the ensuing exchange rate appreciation. With the return of tourists, the local currency appreciated sharply by more than 30 percent in April 2021, thereby regaining its pre-COVID level. The program envisaged a V-shaped recovery with subsequent stable growth.

9. The LMO benefited from monetary policy accommodation along with improved investor confidence through a reduction in yields. Policy rates were reduced by 100 basis points two days before the announcement of the LMO along with a structural downward shift in the central bank's short-term corridor rates and narrower width by 200 basis points.⁷ Reserve requirements were also reduced by 300 basis points on Seychelles rupee deposit liabilities. The sharp currency appreciation in April 2021 and early signs of economic recovery led to a decline in yields on one-year T-bills by 43 basis points before the LMO was implemented, compared to its peak level in March 2021, indicating an improvement in sovereign risk perception.

10. To take advantage of improving investor confidence, the authorities announced the LMO to exchange one-fourth of outstanding T-Bills into long-term bonds with tenors of 3, 5 and 7 years. The LMO was announced on July 2, 2021, offering to exchange SCR 1.5 billion of T-bills (face value) into bonds.⁸ The exchange covered 182-day and 365-day T-bills but excluded 91-day T-bills since its stock was significantly smaller than the other tenors, and it constitutes a reference rate for interbank operations, thereby avoiding any potential market distortions. Surplus liquidity conditions along with weakening credit growth pushed the banks to search for yields to maintain their interest income. As debt sustainability risks were gradually easing, investing in long-term government bonds in exchange for T-bills appeared to be an attractive alternative for the investors.

11. The dominance of the banking sector as an investor base for T-Bills warranted the LMO to be targeted to banks. Banks held more than three-fourths of the stock of T Bills at end-2020 (Figure 1). The LMO therefore required around 30 percent of the T-Bills holdings of the

⁶ Substitution of T-bills with external financing would require some sterilization measures which would reduce the net savings.

⁷ In July 2021, through a structural shift in interest rate corridor, the interest rate on the Standing Credit Facility was reduced by 250 basis points from 6 percent to 3.5 percent, while the rate on the Standing Deposit Facility was reduced by 50 basis points from 1 percent to 0.5 percent.

⁸ Bids for the exchange were accepted during July 7-14, 2021.

banking sector at the end of June 2021 to be exchanged into bonds. To meet the banking sector preferences, issuance of 3, 5 and 7-year were planned that could provide them flexibility to choose tenors according to their liquidity management requirements. Since these bond tenors were issued in January 2021, it would also help to provide a pricing reference. Liquidity constraints for the banks from bond financing were expected to be offset by an increase in core liquidity resulting from retirement of T-Bills through external financing. The impact of the LMO on bank balance sheets was carefully analyzed to ensure that observance of regulatory requirements was not impacted. The provision of contingency measures, if required, through an adequate liquidity backstop by the central bank was also planned.

12. The LMO was designed to be undertaken through a market-based voluntary operation that would avoid its characterization as an event of default which could have triggered negative externalities. The LMO therefore adopted an auction-based mechanism for debt exchange while keeping it voluntary for existing holders. A multiple price auction format was adopted which allowed competitive bidding exclusively for the banking sector while allowing non-competitive bids for all investor types, including the banks.⁹

13. Operational constraints were carefully analyzed to develop solutions and prepare for the execution of the LMO. Since the existing practice of ad-hoc issuance of bonds required a legal enactment, the necessary timeframe was utilized for the legal process. The Core Banking System used by the Central Bank of Seychelles for auctions of T-bills did not have the functionality to cater for bond auctions and non-competitive bids. As a result, the entire LMO had to be processed outside the Core Banking System through a manual process that was resource intensive, including its settlement. For this purpose, issuance of T-bills was not undertaken for two auctions during July 14 -21, 2021.

14. The authorities upgraded their communications strategy to bolster investor confidence in their proposed policies, including the LMO. To obtain the buy-in of the banks for the LMO, the authorities undertook extensive consultation with the banking sector two months before its execution and explained their debt reduction strategy, including the implementation of the LMO. Overall, both the Ministry of Finance and Central Bank of Seychelles adopted an active coordination framework to deal with the economic crisis and for public communication purposes.

15. On July 14, 2021, the authorities successfully implemented the LMO which helped extending the maturity of the participating debt portfolio from less than a year to 4.8 years. Overall, bid participation (amounting to SCR 1.2 billion) represented 80 percent of the offered amount and was fully allocated. The majority of the bids were received from 365-day T-bills, amounting to 75.1 percent of total bids. Investor demand for T-bonds issued in the exchange was evenly distributed across the tenors with a relative preference towards shorter tenors (Table 1).

⁹ Bids were allowed for the destination bonds while prices of the source T-bills were fixed through the prevailing spot curve.

Given that the banking sector held the bulk of the T-bills, it contributed to 98 percent of the overall exchange. Competitive bidding accounted for 85 percent of the total exchange.

Table 1. Debt Exchange Result				
	Exchange Instruments			Total Amount (SCR billion)
Offered Volume (SCR bn.)				1.5
	Source: Treasury Bills			
Tenor	182-days	365-days		1.24
Face Value of Bids Received (percent of total)	24.9	75.1		
	Destination: Treasury Bonds			
Tenor	3-year	5-year	7-year	1.22
Market Value of Bids Allocated (percent of total)	38.0	32.7	29.4	
Coupon Rate (percent)	5.25	7.00	8.25	
Weighted Average Yields (percent)	5.76	7.09	8.43	
Weighted Average Price	99.96	99.65	99.11	
Source: Central Bank of Seychelles				

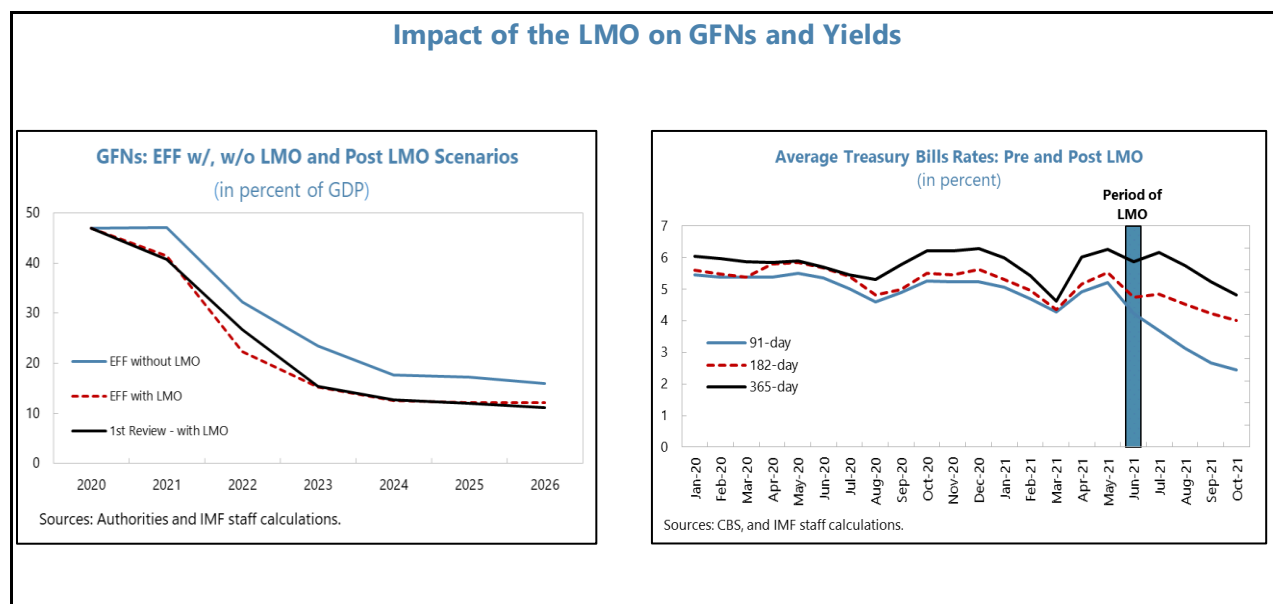
Impact of the LMO

16. The successful implementation of the debt exchange significantly mitigated rollover risks and strengthened debt sustainability. GFNs are projected to drop sharply from 47 percent of GDP in 2020 to 41 percent in 2021 and further to 11 percent by 2026 (Figure 2). The reduction is higher than expected at the time of program approval (12 percent in 2026).

17. The exchange operation laid the foundation for lower long-term borrowings costs, thereby preserving debt sustainability. The cost of long-term issuance declined in the LMO exchange supported by monetary accommodation. As a response, bond yields issued in the exchange were lower by 91 – 157 bps for the different tenors compared to the rates issued in early February 2021. The LMO contributed to further easing of domestic financing conditions from a reduced sovereign risk premium. Although no further monetary support was provided, yields on T-bills dipped more than 340 bps up to end-October 2021 for the 182-day and 365-day tenors since the LMO was undertaken. The decline in yields also stemmed from the reduced supply of T-bills offered to the market due to the impact of the LMO and the unwinding of COVID-related spending measures, resulting in smaller fiscal deficits than anticipated at program approval.

18. Bank balance sheets were not constrained by the LMO along the liquidity dimension largely thanks to monetary support and risk aversion towards private credit. Following the LMO, banks' exposure to government securities remained unchanged at 16 percent of its assets between end-June 2021 and end-September 2021. The LMO, however, resulted in a change in its composition with the share of bonds increasing by 4.2 percent of total assets between the same period at the expense of T-Bills. Higher exposure to bonds had a marginal impact on banks' core

liquidity, declining from 19 percent of total assets at end-June 2021 to 18 percent at end-September 2021. Banking system liquidity remained abundant at the end of October 2021 (8 percent of GDP) mainly due to monetary accommodation and a recent decline in private sector credit.



LMOs on Domestic Debt Under Stressed Conditions

19. Public debt sustainability risks include both solvency and liquidity risks. Sovereign stress can manifest itself in the form of high/rising borrowing spreads, loss of market access, and default, among others (IMF, 2021). There is a thin line between solvency and liquidity risks given the two-way feedback mechanism between them. At the same time, there is a two-way movement between rollover risks and market risk perception in the run up to a debt distress. For assessing risks on public debt sustainability, the IMF's DSA framework includes an upper threshold on rollover risks, for which Gross Financing Needs (GFN) is used as a measure.¹⁰

20. For sovereigns with continued access to markets but facing high risks of debt distress, an LMO can help mitigate sovereign risks. Since an LMO taking place under debt distress conditions with elevated yields (and depressed market prices) keep the net present value (NPV) of the debt unchanged, an LMO involves a trade-off between liquidity and solvency risks. Exchanging short-term (by remaining maturity) debt into longer maturities will typically increase the nominal value of debt, thereby aggravating solvency risks. An LMO, by itself, may not be sufficient to restore debt sustainability without supporting macro-fiscal measures which could ultimately ease solvency problems. However, sovereigns facing heightened stress while retaining market access may find

¹⁰ Based on the DSA frameworks for low-income countries (LIC) and Market Access Countries (MAC), thresholds on GFN are set at 14 percent, 15 percent, and 20 percent of GDP for LICs, EMs and AEs; respectively.

LMOs aimed at changing the debt portfolio structure able to help calm market concerns and reduce (credit/risk premium) spreads (Jonasson, T and M. Papaioannou, 2018).¹¹

21. The feasibility of undertaking a market-based debt exchange depends on the scale of debt distress, debt portfolio vulnerabilities, risk perception, macroeconomic prospects, debt market structure and financial stability considerations. A pragmatic approach is required to determine the extent of portfolio adjustment feasible, particularly where investor sentiment remains fragile (IMF, 2011). Investors may not be interested in a voluntary LMO where market perception of sovereign risk runs high, and any proposed macroeconomic adjustment is not considered credible enough or not adequate to reduce the risks significantly. Where issuance of securities has been limited to short-term tenors, the prospects of bond issuance in longer-term maturities as part of the debt exchange will be severely constrained.¹² A fragile domestic banking sector with underlying vulnerabilities may prove to be a major constraint for banks to participate in the LMO, especially where domestic banks constitute a sizeable investor base.

22. Episodes of domestic debt exchanges have been observed that were undertaken under debt distress with high refinancing risks stemming from domestic debt, notably Argentina (2001), Russia (1998), and Turkey (2001).¹³ There were some similarities in the prevailing macro-financial challenges when such exchanges took place. In all three countries, the debt exchange was executed when sovereigns faced significant rollover risks from domestic debt with rising borrowing costs and faced an external shock under pegged exchange rates. The sovereign debt distress was exacerbated by banking sector vulnerabilities (Russia, Turkey), and real sector shocks (Argentina).

23. Domestic debt exchanges undertaken under stressed conditions differed in their design and had mixed success in mitigating debt sustainability risks. Countries facing banking sector vulnerabilities exchanged domestic debt denominated in local currencies into foreign currency denominated debt – either domestically issued (Turkey) or in the international market (Russia) which enabled the domestic banks to close their foreign exchange position.¹⁴ In contrast, Argentina maintained in the exchange its exposure to foreign currency denominated debt. Higher yields on local currency bonds in all three countries were also a key factor for issuance of foreign currency debt as part of the debt exchange to contain interest costs. All the three countries undertook an LMO under an IMF program. The LMO in Russia was significantly undersubscribed

¹¹ This has been demonstrated during episodes of domestic market stress that spilled over to EMs during the global financial crises and more recently following the impact from the COVID-19 global pandemic.

¹² This is mainly due to investor aversion to assume new credit risks with longer duration and to the attendant uncertainty on pricing of new tenors. A pre-condition for undertaking a LMO therefore requires an embryonic secondary market activity for the securities and tenors involved in the LMO which provides a pricing reference.

¹³ After losing market access for more than one year following the global financial crisis, in an effort to regain market access for long-term instruments, Ireland undertook a series of LMO in 2012 as an opportunistic transaction with the easing of sovereign risks.

¹⁴ Turkey also exchanged part of the debt into local currency floating rate debt due to the prevailing uncertainty on interest rates and exchange rate pressure.

while high interest rates involved in the debt swap for Argentina led to a deterioration in its solvency position - with both the countries eventually defaulting on their debt.

Conclusion

24. LMOs on domestic debt under sovereign stress can be a useful tool to mitigate refinancing risks in particular for cases where most of the refinancing risks are emanating from domestic debt. Pricing of the LMO should be carefully analyzed to ensure the trade-offs between liquidity and solvency risks does not aggravate sovereign risk. The feasibility of an LMO would crucially depend on investor risk perception, macroeconomic prospects, depth of the debt market and financial stability implications. Feasibility of the LMO in Seychelles benefitted from a sharp trajectory for restoration of debt sustainability backed by its V-shaped recovery as well as a risk aversion of the banking sector to extend credit to the private sector thereby providing a source of demand for government bonds. Market communications by the authorities about the design and purpose of the LMO is integral to the success of a LMO under sovereign stress. Finally, as a tactical decision, the timing of an LMO under sovereign stress is key to its success, as it needs to be implemented well before the slide in investor confidence becomes an irreversible process.

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Appendix I. Letter of Intent

Victoria, Seychelles
December 2, 2021

Ms. Kristalina Georgieva,
Managing Director,
International Monetary Fund
700 19th St, NW
Washington, DC 20431 USA

Dear Ms. Georgieva:

Seychelles has been hard hit in 2020 by the international effects of the Covid-19 pandemic, which brought tourism, the mainstay of our economy to a halt. Nonetheless, the strong effort to vaccinate the population in the first months of 2021 have allowed us to reopen the country to tourism from mid- March 2021 and since then tourist flows have progressively picked up, resulting in a strong pick up of economic activity so far. The government was thus able to put an end in February 2021 to the financial assistance for job retention scheme previously put in place in March 2020 to support income of furloughed workers. Tax and non-tax revenue recovered significantly in 2021 so that the primary budget deficit performance criterion for July 2021 under the Fund supported program was met with a significant margin, and we expect to end the year with a primary balance deficit substantially lower than envisaged under the program. All other quantitative performance criteria for end July 2021 were also met.

In the policy area, we are implementing with the determination the action plan we have presented when requesting the 32- month arrangement under the EFF. Our main objectives are to strengthen the resiliency of the economy to external shocks, achieve a primary budget surplus position so as to contain the burden of public debt, extend its time profile, rationalize the tax regime, improve expenditure management, and enhance financial sector stability and compliance with international financial standards.

Risks to debt sustainability from Air Seychelles have been reduced now that Air Seychelles has gone into administration. In early October 2021, the government appointed two administrators as per the requirement of the Insolvency Act and the task of the administrators will be to consider the optimum ways of restructuring Air Seychelles and settling its debts.

The policies we are pursuing now and that will be carried out in the coming months are presented in the attached Memorandum of Economic and Financial Policies, which updates the Memorandum of July 2021.

We believe that the economic and financial policies set forth in the MEFP are sufficient to ensure that the objectives of the program will be met. 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, in accordance with the Fund's policies on such consultations. We will supply the Fund with timely and accurate data that are needed for program monitoring.

We authorize the publication of this letter of intent, the attached MEFP, the technical memorandum of understanding, and the forthcoming staff report.

Sincerely yours,

/s/

Naadir Hassan,
Minister of Finance, Economic Planning and Trade

/s/

Caroline Abel
Governor Central Bank of Seychelles

Attachment I. Memorandum of Economic and Financial Policies

I. Background and Macroeconomic Outlook

1. Seychelles is making significant progress in recovering from the impact of Covid -19 pandemics thanks to an early start in the vaccination campaign in February 2021 which made possible the reopening of the country to tourism in March; by end- March 60% of the population was vaccinated which allowed the country to fully reopen the border for tourist arrivals in late March, eliminating the restriction on tourist movements in the country that were introduced in mid-2020. In the initial months, the tourist inflow originated from nontraditional markets in the Middle East and Eastern Europe and picked up further since July with a resumption of tourism arrivals from the traditional markets in Western Europe as those countries relaxed pandemic border controls. Prospects are favorable for the last quarter of the year. Tourist arrivals in the second quarter were 50% of the level in 2019, and in the third quarter 65%; in the last quarter they could attain 70% of the 2019 level, and total arrivals in the year could reach 170,000 persons, compared with 114,000 in 2020, when they were concentrated in the first quarter.

2. Economic activity was also supported by expansion in agriculture and fisheries sector, although the transformation of fishing products declined. Information and communication showed a strong increase. The construction sector remains weak, with only few major projects underway, and some government construction projects delayed, while building of individual new houses is very limited. In all GDP is expected to increase by 6.1 % in 2021, after a decline of 9.9% in 2020.

3. In 2022 real GDP is expected to increase by 7.2 per cent driven by further improvement in tourism, and by a pick-up in construction activity, as a few large hotel resorts projects are scheduled to start, together with some renovation of existing hotels; private housing construction could also gradually recover. Value added in fishing and agriculture is expected to increase by 3%, and information and communication will show a strong increase, driven by the offering of new services.

4. The exercise to rebase the GDP in 2014 has been completed and has resulted in an upward revision of the 2020 GDP by 4 %.

5. The reopening of the economy and the return of confidence led to a reversal of the strong depreciation of the exchange rate Following the significant depreciation of the rupee in 2020, the exchange rate has strengthened over the past months, supported by stronger inflows from the tourism sector. However, in line with the improvement in economic activity, demand for foreign exchange is expected to increase which, combined with the supply-side

constraints, may imply that annual average inflation will remain elevated at around 9.8% in December 2021, but is forecasted to drop to 3.3% at end-2022.

6. Budgetary performance in 2021. In light of improved economic prospects and the need to protect public finances, between January and March 2021 the government decided to end the job retention financial assistance scheme introduced in March 2020. The budget revenue performance improved in the second and third quarter with the pick-up of tourism, that strengthened VAT receipt. Business tax receipt in 2021 are expected to exceed both the budget forecast and the forecast under the EFF-supported program. Despite some shortfall in excise revenues in relation to program forecast, the total tax revenue forecast for the year under the program is expected to be exceeded by a small margin, and the total revenue target will be met by a significant margin, owing to a good performance of non-tax revenue. The total revenue target for July 2021, a quantitative performance criterion, was exceeded, and the primary deficit target was met with a significant margin.

7. On the budget expenditure side, the measures to contain the wage bill in 2021 were executed as planned, with no wage increases, no increase in long term allowances and no new scheme of services. Savings have been carried out as planned in the outlays for goods and services, including the renegotiations of rents, and the cut in traveling costs. Outlays for the social programs of the Agency of Social Protection are in line with the budget, and so are transfers to public enterprises; transfers to Air Seychelles remains within the budget limits, they include mainly support for wage payments. Capital expenditure is expected to remain below program projections.

8. The primary balance target for the end of the year is expected to be met with a significant margin. The 2021 primary deficit is now expected to fall to 6.6 percent of GDP, significantly below the program target of 9.7%. Without the upward revision of GDP, the primary deficit would reach 7.0 % of GDP. Because of delays in securing bilateral budget support loans, which under the program were forecast at US\$ 68 million or 5 % of GDP, the government will have to rely on more domestic financing than programmed; to that end a bond was issued in late November, with tenor of 4 to 6 years, taking advantage of the low-rate environment.

9. In July the authorities successfully conducted the planned liability management operation, switching SR 1.2 billion of Treasury bills into bonds with tenors of 3, 5, and 7 years, with an average maturity of 4.8 years and bond yields about 125-150 bps below the previous issues. This operation reduced considerably refinancing risks, and cut by 5% of GDP the stock of Treasury bills outstanding, which had reached 20% of GDP at end-2020. Following this operation, weekly issues of T bills were modest in August, September and October, and interest rates on T bills which had ranged between 3.7% and 6 % in early June in the three tenors (90, 180 and 360 days) fell to the range of 0.5% to 1.5% in October. The decline in rates reflects the abundant liquidity in the banking system, which is faced with a weak demand for credit from the private sector. In November-December a further decline in weekly Treasury bills issues is planned, accompanied by a Treasury bond issue. The stock of Treasury bills that stood at SR 5.6 billion at end 2020 (26% of GDP) is

projected to decline by end – year to SR 3.8 billion (15.2% of GDP). Total government and government guaranteed debt, which stood at 92.2% of revised GDP at end 2020 is forecast to decline to 81.2 percent at end 2021.

10. Prices remained elevated for the most part of 2021, with the year-on-year Consumer Price Index (CPI) standing at 10.0 per cent and the 12-month average inflation at 8.8 per cent in October. The average price of goods and services increased in 2021 in line with the depreciation observed in 2020. In addition, the impact of higher international commodity prices, increased freight costs and other supply-side constraints filtered through the domestic prices.

11. Monetary policy has remained accommodative since the second quarter of 2020 with the aim of supporting domestic economic activity. At the beginning of 2021, the Monetary Policy Rate (MPR) stood at 3.0% and that stance was maintained until the third quarter of 2021, when it was revised to 2.0%. This was accompanied by a structural shift in the interest rate corridor, with the interest rates on the Standing Deposit Facility and Standing Credit Facility set at 0.5% and 3.5%, respectively. The adjustment was necessary to realign market interest rates with prevailing macroeconomic fundamentals and was maintained for the fourth quarter of 2021.

12. The current account balance is showing signs of improvement relative to 2020, with a projected deficit of 20 percent of GDP in 2021 compared to 25.4 per cent the previous year. Exports of goods picked up during the year, driven by higher demand for canned tuna. In terms of services, tourism revenue is expected to amount to US\$276 million, an increase of 25 per cent relative to 2020, supported by the relaxation of travel restrictions and increasing tourist arrivals. However, imports also rose, but mainly on account of more expensive commodity prices on the international market and higher cost of transportation. Similar to 2020, private sector financial inflows, in particular trade credits, have remained an important source of financing in 2021.

13. The central bank established in March 2020 a long-term lending instrument for banks and other financial institutions to provide working capital support to businesses impacted by the COVID-19 pandemic. Accordingly, the Private Sector Relief Credit Line Facility (PSRCLF) was established – for a sum of R 500 million to support micro, small and medium enterprises (MSME) with an annual turnover below R25 million. Participating financial institutions then on-lend funds borrowed from the PSRCLF at an interest rate of 1.5 per cent to MSMEs. A second fund, the Private Sector Large Enterprise Credit Line Facility (PSLERCLF) worth R750 million, for larger businesses with an annual turnover above R25 million, was established in June 2020 for participating financial institutions to on-lend at an interest rate of 4.5 per cent were set up. At the point of establishment, the banks and other financial institutions had until December 2020 to request for advances from the CBS, but after assessing the economic situation, engagement with key relevant stakeholders, the deadline was extended to December 2021. In terms of support to businesses under the schemes, initially they were to cover a period of 6 months of expenses, but this period has been revised to 12 months, following an internal assessment and consultation with the private sector. Revisions also included an increase in the tenor from 3 years to a maximum of 8 years and moratorium period from 12 months to 18 months. As of November 30, 2021, 23.28% (R116,394,565.61 out of R500

million) has been used under the PSRCLF for MSMEs and 37.21% (R279,046,183.00 out of R750 million) has been used under the PSLERCLF.

I. Program Objectives and Policies

A. Real Sector Reforms (Diversification, Digitization, Climate Change Adaptation)

14. The government objective is to enhance the prospects for sustainable and inclusive medium-term growth, relying on actions to diversify tourism services, and to make better use of the potential of the fisheries sector. The latter can benefit from the diversification of the production chains and the activity of new operators, along the line envisaged in the World Bank supported SWIOFISH 3 project.

15. In the tourism sector, the adoption of an updated Tourism Master Plan is a key step for tackling structural bottlenecks on an island-by-island basis. It aims to widen the offer of services with the balanced objectives of economic empowerment, environmental preservation, and socio-cultural integration. Important progress has been achieved in recent months in reaching new markets and better promoting local content. Continued efforts will be needed to develop skilled local labor, increase the supply of local agricultural products to the sector, and support small businesses, based on the recent Tourism Value Chain Analysis.

16. In the fisheries sector significant progress has been achieved to diversify the value chain, with the completion in mid- 2021 of the cold storage facilities in the new industrial zone in Iles du Port. New fish processing units with medium size factories are expected to enter into operation soon, which will expand export and local employment.

17. The Government remains committed to accelerate the drive for energy transition. Renewables will be at the center of economic recovery strategies to advance economic, social and climate priorities for a Sustainable Post-COVID Recovery. The long-term commitment is to achieve a decarbonized economy by 2050 and to boost electricity generation from renewable energies, including marine energy technologies, bio-energies, such as biomass and waste-to-energy, and the use of environment friendly intermittent energy storage technologies.

18. With its updated Nationally Determined Contribution (NDC) submission, Government is re-iterating and improving upon its commitments towards increasing the reduction of greenhouse gas emissions. Economy wide absolute GHG emissions will be reduced by 293.8 ktCO₂e in 2030 (26.4%) compared to business as usual (BAU) scenario. Ambitious targets set for the energy sector are: 30% of gasoline private vehicles to be electric by 2030, and Energy Efficiency improvement level of 15% by 2030. Key implementation targets focus on modernize the entire electricity sector, increased electricity generation from renewable sources, improved energy efficiency across sectors, the shift from fossil fuel-engineered transport to electrified transport and individual active mobility, enhanced resource rehabilitation and land mitigation measures. To plan,

manage and track progress, Seychelles has to build a national climate governance system centered on inclusive consultations, institutional coherence and scientific excellence. The Energy policy is currently being reviewed. The objective is to have an updated Energy Policy Document, with realistic targets for Intermittent and non-intermittent renewable energy sources by last quarter 2022. The Government is currently in discussion with African Development Bank for potential assistance to develop an integrated resource plan (IRP) for the power sector.

19. The Covid-19 pandemic has shown the vulnerability of a country highly dependent on the tourism industry and shown the need to diversify, while maintaining the attractiveness of the country as a tourism destination. As tourism remains a key the pillar of the economy it is necessary to expand the offering of the tourism experience and diversify the products that we have to offer our visitors. Certain new products such as 'cultural tourism' is being developed, so that our visitors may experience our heritage, our culture, and our cuisine amongst others. This will also help to bring about more development in our communities, which will enrich the experience of our visitors. A review of our tourism attractions is also being undertaken so as to make them more interesting for visitors. As an island state, we have to make better use of our ocean, and create more water sport activities and other leisure activities.

20. Government is also encouraging more local participation in this sector. For this to materialize, we must ensure that the supply chain is well established. This will create the opportunity for the other two key sectors, fisheries and agriculture, to also contribute to the recovery of our tourism industry.

21. In the agricultural and fisheries sectors continued efforts are needed to widen the productive capacity and to attract new entrepreneurs. The fisheries sector remains a key one in our quest for economic transformation with the various potential it offers. After many years of research and investment, the Seychelles Aquaculture sector has now officially been launched.

22. The government has promulgated the first Aquaculture Regulations and its accompanying standards. The regulations were developed based on global best practices to ensure that the sector develops in a well-coordinated and regulated manner with the highest compliance levels. The Aquaculture Standards would serve to guide the private sector operators and always ensure that the best practices are being observed. The regulations also make for provision for the establishment of the Aquaculture Regulatory Committee. The committee is responsible for the effective and efficient development of the sector and consist of the key ministries, departments, agencies, Ceps (Citizens Engagement Platform Seychelles) and SCCI (Seychelles Chamber of Commerce and Industry) to better represent the mandate of the committee. Their mandate is to provide an inter-departmental focus to coordinate policy, align legislative and institutional structures, drive and track aquaculture development progress and make recommendations throughout the development of the sector.

23. In the agricultural sector the Government's objective is to transform the local food and nutrition production landscape to a more self-sufficient system. This will be achieved by

increasing the volume of local production in relation to total consumption of livestock to 80%, local fruits & vegetables to 90%. In doing so particular attention will also be paid to strengthening the ability of our local food producers to adapt to climate change. The authorities are also working towards building the national capacity and capability to improve the country's strategic food reserve for a minimum period of six months

24. The Ministry of Investment, Entrepreneurship and Industry is taking actions to facilitate business start-ups improve the business climate. Priority is given to the online registration of businesses. Actions are being taken to helping small and medium enterprises to expand and promote local production to reduce dependence on imports. This ministry will create a framework to support research and development activities, and the proper protection of intellectual property, with the aim of increasing our capacity for exporting in the region and internationally.

25. The effects of COVID-19 pandemic have further reinforced the need to embrace the digital economy agenda going forward. The Digital Economy Diagnostic Report coupled with the Seychelles Fintech Strategy have identified key pillars that need to be established so that Seychelles can progress on moving forward the digital economy agenda. The Government has given due attention to the digital transformation of the economy and the creation of an enabling environment for the uptake and usage of Digital Financial Services. These pillars include a robust regulatory framework, efficient and reliable digital infrastructures as well as enhanced digital skills and literacy. The digital action plan for the medium term will therefore focus on the following:

- Improve relevant digital infrastructure. A new Communications Bill which aims to address anti-competitive practices and provide a better legal framework for the telecom sector is expected to come into force during the first half of 2022. This will also be accompanied by the regulations on the number portability. The second submarine cable PEACE will become operationalized by April 2022. This will be followed by the operationalization of 3rd submarine cable the mid-year 2023.
- Enhance the level of digital skills to ensure inclusion and equal access to opportunities and promote use of digital platforms in public service delivery. During the first half of 2022 key platforms will come online, mainly the digital ID system, the online Business, Company & association registration and the online License Application. The full implementation of the Health Information System is also expected by end 2022.
- Increase financial inclusion through digitalization of payment systems.
- Develop digital entrepreneurial ecosystems in order to diversify and strengthen the economy

26. Priority climate change adaptation investments have been identified in critical infrastructure, tourism and coastal management, food security, biodiversity, water security, and the blue economy. Furthermore, there are planned projects under the umbrella of disaster risk reduction management, such as establishing early warning systems and improving coastal resilience that are worth considering. The Government plans to mainstream climate adaptation in Seychelles'

recovery post-pandemic plan. Also, a careful cost-benefit analysis of climate change related projects is being undertaken as the government prioritizes its spending. Seychelles is recognized -- and receives the support of other countries and international organizations -- for its program of adaptation to climate change and the management of the challenges associated with it. Severe erosion, waves crashing on coastal roads, and inundations during the annual rainy seasons have shown that our environment, our economic resources, and even our social life, remain vulnerable, and there is an urgent need to seriously address these challenges.

B. Fiscal Policies, and Fiscal Structural Reforms

The budget for 2022 and beyond

27. The keystone of our reform program is a large, upfront fiscal adjustment leading to the attainment of sustainable fiscal surpluses over the medium term with the aim to reduce public debt sustainability risks. The sharp recovery in the exchange rate in April 2021, together with the GDP growth, contributed to the strong reduction in the ratio of public debt to GDP in 2021, but significant risks to debt sustainability continue to exist. A policy of fiscal consolidation and prudent debt management, accompanied with a steady economic recovery, is expected to reduce public and publicly guaranteed debt from 92 percent of GDP at end- 2020 to 51 percent at end 2026. The government is committed to achieve its pre-COVID objective of reducing debt to around 50 percent of GDP by 2026.

28. The government is committed to stronger revenues; therefore, we expect an improvement of the primary balance by 4 percent of GDP in 2022, bringing the expected deficit to 0.8 percent. This compares with an initial program target of a deficit of 5 percent in 2022; in 2023 we aim at a surplus of 3 percent instead of a deficit of 0.4 percent under the initial program. These results will be achieved by pursuing a prudent expenditure policy while widening the tax base with revisions of the exemptions under the VAT and a rationalization of the business tax limiting deductibility provisions and uniformizing the tax rates among sectors. By 2024 we aim at achieving a revenue/GDP ratio excluding grants of 33.8 percent close to the one achieved in 2019. On the expenditure side we plan to rationalize the wage bill as well as goods and services expenses, and containing transfers, including through reviewing the programs to make them better targeted and financially sustainable. We will also undertake a comprehensive review of the procurement environment in Seychelles to rationalize procedures and increase efficiency of spending.

29. The budget target for 2022, of a deficit of 0.8 percent of GDP, is to be achieved by raising revenue to 32.2% of GDP, up from 30.0 per cent in 2021, mobilizing grants for 2.8 per cent of GDP, up from 2.4 per cent in 2021, and by lowering considerably expenditure as a ratio to GDP. Wage and salaries and goods and services will be maintained flat in nominal terms, while transfers will decline, given the end of subsidies for wage maintenance in effect in the first 2 months of 2021.

30. On the revenue side, value added tax receipts are expected to rise as a share of GDP by about 1.5 percentage points, reflecting stronger tourism activity, and business tax receipts would also rise modestly as a share of GDP. A new tax schedule for the business tax will enter into effect in 2022 (see below). Excise receipts and customs revenue will increase in line with GDP. External grants for capital expenditure are expected to rise as a share of GDP by 0.5 percentage points.

31. On the expenditure side, outlays wage and salaries will remain close to the level of 2021 with no salary increase and recruitment limited to the priority health and education sector.

The forecasted savings will be SR 500.0 million equivalent to 1.8 percent of GDP. Government has to allocate an additional SR 63.2 million under wages and salaries or 0.2 percent of GDP based on the increase of employers' pension fund contribution from 3% to 5% in January 2022. This is part of the reform for sustainability of the pension fund. The effort to rationalize expenditure on goods and services will continue, and their level will remain flat in nominal terms. Rental agreements are being renegotiated and savings achieved with reduction in foreign traveling. Government will start investing in construction of offices through a public private partnership so that the expenditure under rental vote can be used to pay for a building on an annual basis with the intention of transferring the building to Government over the long term. The first one will be for Seychelles Revenue Commission and the construction will start in 2022. Outlays on social programs will decline, as 2021 level reflected subsidies for employment retention by the private sector in the first two months of the year. Capital expenditure will increase because of some new projects financed by grants (drug rehabilitation center, La Digue hospital). Net lending to PUC for its capital projects will remain stable.

32. Financing of the budget deficit will rely on external budgetary support from the World Bank, and the African Development Bank, respectively US\$ 27.5 and 20 million, and bilateral loans under negotiations, for US\$10 million. The SDR allocation is available as a buffer; the authorities are making preparations to amend the CBS Act to allow for its use. The government will confirm the bilateral financing before the Board meeting. This external financing will exceed the overall deficit, allowing for a reduction of the stock of short-term domestic government securities, and a lengthening of average maturity of the debt.

Revenue Measures

33. Reforms in tax administration in 2022 will focus on digitalization initiatives, stronger compliance monitoring, and improving our performance in terms of international obligations.

34. Enhance the ASYCUDA system at customs, with the aim to moving to online service and reduce paper transactions. There will be new developments in terms of creation of data warehouses, creation of a platform for Single Window and the system will be upgraded to accommodate new modules, such as Excise, Government Warehouse, Bonded Warehouse and Courier Services. Furthermore, ASYCUDA will be integrated with an online payment gateway. The project is expected to be completed by June 2023, however the different modules will be deploy for

use as and when they are ready. The first two modules are expected to be completed within 6 months from now and that is for courier services and excise tax management.

35. Increase the number of services offered online such as business registration, e-payment and the submission of returns and other forms required for registered businesses, including International Business Companies (IBCs). The project is expected to be completed by June 2023, however the different modules will be deploy for use as and when they are ready. We have already implemented e-payment using credit/debit card and we expect to implement payment using SEFT platform before the end of 1st quarter 2022.

36. Review and implement structural reform of the Tax Division with the aim of improving tax collection and ensuring that businesses meet their obligations. Voluntary compliance through self- assessment will be encouraged by making it easier for taxpayers to file and pay on- time. However, the Examination and Assessment Unit has been created to implement more effective and targeted measures and compliance programs to identify and deal with non-compliance. The Unit will complement the functions of Audit by conducting desk audits and raising default assessments for non-lodgment of tax returns.

37. Utilize information received from reporting jurisdictions that exchange tax information with Seychelles, under the 'Global Forum's Automatic Exchange of Information', enhance sourcing and utilization of third-party information to identify risk of non-compliance; including use of information received from reporting jurisdictions under the 'Global Forum's Automatic Exchange of Information', since 2017. SRC has acquired a system for Automatic Exchange of Information. This will allow SRC to be more efficient in exchanging information and in meeting OECD standards. The testing phase has been completed and work is progressing to go live with the system. It is expected to be further updated in 2022 to cater for Foreign Account Tax Compliance Act (FATCA). The system will also include a case management function to manage Exchange of Information upon Request.

38. Redevelopment of the SRC's Tax Management System. The Cabinet of Ministers has approved for a new taxation management system to be developed and completed by 2023. Financing is provided by the EU under an agreement signed in April 2019. The aim is to increase the functionalities of the current Client Management System (CMS), to close significant gaps, which hinder a modern tax management system. Several procedures in the system are not fully automated and are implemented as manual steps. The system is not fully integrated with E-Services, and does not include key functions like case management, debt management, business intelligence, and data warehousing. The interface will be redeveloped in web-based form and the system will be upgraded to make use of modern IT technologies. The initial phase of business process reengineering has started, and the registration module is expected to be completed by December 2021. The key deliverables are to develop a modern Tax Management System that will result in increased revenue collection, increased use of digital services to lower compliance costs for taxpayers and subsequently improve voluntary compliance, increase the taxpayer registration and offer additional

opportunities for taxpayer education. The project is expected to be completed by June 2023; however, the different modules will be deployed for use as and when they are ready.

39. SRC will strengthen capacity for managing international taxation risk and has received technical assistance from OECD Tax Inspectors Without Borders (TIWB) to build its tax audit capacity in Transfer Pricing. The one-year programme was launched virtually early October 2021. Over the next 12 months, the Government of India will be providing a tax expert to assist the SRC to build capacity in handling transfer pricing cases in the tourism and financial services sectors.

40. Legislation will be adopted to reform the business tax effective January 1, 2022 with the view to unify the tax rate for different productive sectors at 25% (currently tourism, fishery and agriculture benefit of a lower 15% profit tax rate), reduce the accelerated depreciation provisions for tourism, agriculture and fishery, and revise the taxation of security dealers. Taking into account the objective to develop the agricultural sector over the medium term, this sector will have a grace period of 3 years and during the period an assessment will be done on the best modalities for a tax structure for this sector. In addition, we will get Cabinet approval of legislative amendments to streamline VAT exemptions, in consultation with IMF staff (structural benchmark for end-September 2022).

Expenditure Management and Efficiency of Public Spending

41. The GOS is taking steps to adopt a Medium-Term Fiscal or Budget Framework to bolster the sustainability of public finances. The **following** step would consist of defining the contours of the implementation of a multi-year budget. An AFRITAC mission is expected early in 2022 to work with the authorities in reviewing the current processes in place and advise on the best structure to put in place. The Ministry of Finance is currently working with the Ministries, Departments and Agencies in improving the Public Sector Investment Plan (PSIP) over the medium term to be consistent with the budget framework. Currently the MDAs are able to plan their investment plan over two years. The authorities are also working on the result-based management to ensure there is synergy between Government strategies with budget planning. Government has also appointed a Public Service Salary Review Committee to conduct an analysis of the current salary structure in line with international best practices. In addition, the committee will conduct a wage bill analysis and will develop an appropriate sustainable salary structure taking into account performance management in public sector. The aim is to ensure the wages and salaries are maintained at 11 percent of GDP over the medium term.

42. With the support of the World Bank budget support of US\$ 9 million in 2021, reforms will be introduced in the social protection system in the form of a “Program for Results” (PforR). The aim is to reform the social protection **system** to ensure its sustainability, as well as promoting the insertion in the labor force of current working-age beneficiaries. The Program covers the five largest cash transfer programs managed by the Agency for Social Protection (ASP): Retirement Pension (RP), Homecare Program (HCP), Invalidity Benefit (IB), Disability Benefit (DB), and Social Welfare Assistance (SWA).

43. The Program development objectives are to improve the efficiency and effectiveness of social protection programs in the Seychelles, while remaining above the floor on social expenditure established under the program. The focus in 2022 will be to:

- Improve fiscal sustainability of Retirement Pension through the enactment of the law increasing the retirement age for the Retirement Pension to 65 years old beginning in January 1, 2023
- Improve efficiency and transparency of social protection programs through the following measures.
- ASP will adopt a revised socioeconomic needs assessment based on non-income dimensions of poverty.
- Comprehensive Review of ASP internal controls and payroll systems to check adequacy and adherence to the established country systems and controls
- Trained caregivers within HCA, ASP, and MOH are providing home care to at least 60% of new high-need HCP beneficiaries

Increase Efficiency of Public Spending

44. The GOS is committed to improve the efficiency of government spending. Following a July 2019 FAD- AFS mission which recommended a comprehensive review of the legal framework for public procurement in Seychelles, a review of the structural, legal, and operational factors of Seychelles' procurement system is being conducted and is expected to be completed by end 2022. A Public Investment Management Assessment (PIMA) will take place in the first half of 2023 to help identify opportunities to increase the efficiency of public investment, including the scope for the procurement system to support PPPs. In addition, with the assistance of the World Bank, Public Expenditure Reviews (PER) are being conducted in education and health sector, and is expected to be completed in June 2022. To ensure the transparency of COVID-19 emergency-related spending, government is carrying out an audit, which will include information on awarded companies. The audit of emergency spending that was initially planned to be published in September 2021 was delayed due to staffing shortages related to COVID-19; it is scheduled to be sent to the Ministry of Finance in November 2021 and to be made public in December 2021.

45. In order to improve PFM, it was decided that a new IFMIS platform should be installed by January 2024. This should strengthen capacities to manage public finance business processes and also link up with the emerging national payments platform prepared by the central bank. This will be done with the assistance of AFS which fielded a remote technical assistance (TA) mission to Seychelles in early 2021. A budget for the new IFMIS will be included in the 2022 budget.

Results-Based Management

46. The government is committed to pursue a result- based management approach to public spending. The aim is to strengthen the results-focus across government to enhance public sector **efficiency**, effectiveness, transparency, and accountability with the ultimate objectives to enhance growth, economic diversification, and social inclusion across sectors. As we journey towards economic recovery, RBM thus plays a critical role in ensuring that our limited resources are sufficient to not only sustaining the financial needs of the country, but also in achieving the much-needed transformational change for our country.

47. The Government will have a whole rollout of RBM, with preparatory work beginning immediately and ready for the 2023 budget process. An integrated RBM calendar will be issued by end 2021 to kick start the process.

48. The full rollout of RBM will thus improve operational and allocative efficiency in the public sector and create greater fiscal space for the provision of essential public services. This will mean:

- More services to bridge existing deficiencies in health, education, natural resources management, water and sanitation, energy, infrastructure and other basic services, together with more effective fiscal and social impact assessment; thus giving rise to:
- Better services to improve the quality of life across large segments of the population.

49. Additionally, the full RBM rollout will be based on a portfolio planning approach whereby the portfolio takes the lead and guides its departments and public bodies in the process, through integrated portfolio-wide strategic planning, budgeting and monitoring and evaluation, and performance management systems. This will ensure that clear accountability exists to individual Ministers and senior management and to institution budgets. Furthermore, each portfolio will be able to produce a comprehensive strategic plan and annual performance plans that are of good quality. In doing so, this will ensure that all government entities are indeed planning for results and leading towards a participative, performance-driven work culture focused on continuous improvement, better service delivery and the achievement of national outcomes.

C. Minimizing Risks of SOEs

50. The Cabinet has approved the new Public Enterprise Monitoring bill to strengthen management of state-owned enterprises. The legislature will consider it in 2022. With the passage of the bill, the Public Enterprise Monitoring Commission (PEMC) would become the only authority to oversee public enterprises. In collaboration with the ministries concerned, and their boards, the PEMC will establish targets for these enterprises to ensure that they generate revenue for government and for the people of Seychelles, that they are fully accountable to government, and that the decisions they take are aligned with national plans.

51. Risks to debt sustainability from Air Seychelles have been reduced now that Air Seychelles has gone into administration. The GOS worked with the World Bank and identified that

the least costly scenario would be the liquidation of Air Seychelles. This was presented to and approved by cabinet in September (*SB met*). In early October 2021, the government appointed two administrators as per the requirement of the Insolvency Act. The task of the administrators will be to consider the optimum ways of restructuring Air Seychelles and settling its debts. Separately, in August 2021, EA Partners bondholders presented a petition before the Supreme Court in Seychelles for the winding down of Air Seychelles. For the 2022 budget, Government has allocated only the \$5 million previously agreed for the repayment of the Etihad Airways debt that Government purchased at a discount and \$ 1.4 million previous liability from 2015. Contingent liability risks to the government have been reduced, as remaining debts of Air Seychelles will be managed through the process of administration and are expected to be paid from Air Seychelles' assets.

D. Public Debt Management Strategy

52. Following the successful liability management operation in July, the government continues to assess the options to refinance short-term debt, namely treasury bills, and to lengthen their maturity through the issuance of bonds. A medium-term debt management strategy (MTDS; *structural benchmark for end-March 2022*) will be updated and published with technical support from the IMF to guide future borrowing decisions that would adequately consider cost-risk tradeoffs. AFRITAC south provided technical assistance in August 2021 on asset and liability management concentrating on specific public debt dynamics tools and the link to macro framework. Further, implementation of the MTDS will be supported by publishing an Annual Borrowing Plan (*structural benchmark for end-March 2022*) along with an auction calendar for all government securities to help market participants plan their liquidity management and reduce uncertainty. There will be stronger interagency coordination at a high level, between the Ministry of Finance and the Central Bank through the existing National Public Debt Management Committee to determine the quarterly borrowing plan on a recurring basis (*new structural benchmark for end-March 2022*). The Ministry of Finance has started publishing quarterly reports on debt management operations and outstanding debt position on its website (*structural benchmark for end-September 2021*).

53. In 2022 the government intends to regularly issue bonds through the auction mechanism. Bond issuance will be supported by improving their liquidity through repo operations and initiating trading reforms in government securities. Initial discussion has started with the relevant stakeholders in order to have the necessary frameworks in place to make available such facility. A plan for a government securities trading framework will be approved by the government in consultation with the CBS by end-2022 (*new structural benchmark for December 2022*). The IMF will provide necessary technical assistance for this purpose.

E. Monetary and Exchange Rate Policy

54. Mindful of potential short-term domestic inflationary pressures that may arise due to external developments, continued support to the economy remains crucial. As such, monetary policy is expected to remain accommodative in the short term to foster a conducive environment, that would stimulate credit and encourage economic activity. The Central Bank remains vigilant to monitor inflationary developments and take appropriate measures. The CBS plans to monitor

inflation expectations through a survey with the assistance of National Bureau of Statistics. The Monetary Policy Rate (MPR) remains the main policy signal, and is complemented by an interest rate corridor, as a part of an interest rate based monetary policy framework.

55. The downward shift in the interest rate corridor which became effective in July 2021, led to the expectation of a general reduction in interest rates in the domestic debt market.

However, thus far, limited transmission of monetary policy to the banking sector, has been observed through the interest rate channel. As at October 2021, the effective savings rate stood at 1.69%, declining by 62 basis points, from a rate of 2.31% in December 2020. As for the average lending rate, it fell by 21 basis points over the same period to stand at 9.13%. This was mainly on account of the low interest rates applicable on credit provided to MSMEs and Large Enterprises, which stand at 1.5 per cent and 4.5 per cent, respectively. To strengthen implementation of monetary policy, including its transmission mechanism, technical assistance from IMF has been scheduled before end March 2022.

56. The CBS remains committed to a floating exchange rate and will only intervene to facilitate orderly conduct of the market. As the tourism sector is recovering at a faster-than-anticipated pace and the general outlook appears optimistic, it is expected that market-clearing conditions will prevail.

57. Gross International Reserves (GIR) increased from US\$ 559 million end of 2020 to US\$ 651 million as of November 30, 2021. The increase was primarily driven by a pick-up in tourism sector and supported by the IMF first disbursement of US\$34.3 million under the programme. The increase in the GIR was also attributed to the SDR allocation equivalent to US\$31.2 million, in August 2021. If required, international reserves will be used to support the market through foreign exchange interventions to ensure orderly market conducts without compromising the floating exchange rate regime.

58. Through the Reserves Advisory Management Partnership (RAMP) of the World Bank which was signed in January 2019 for a period of three years, the CBS remains committed to enhance capacity building of the staff in the areas of reserves management. The engagement as part of the partnership also includes an investment management mandate, whereby RAMP manages US\$100 million worth of reserves.

F. Efforts to Improve External Statistics

59. Work on the alternative tourism earnings estimation framework is progressing well and this method is expected to be implemented as of next year. Necessary backward adjustment will be incorporated. In addition, CBS received TA from the IMF Statistics Department, with the aim to improve the quality of external sector statistics by identifying and collecting offshore data, which remains a major challenge. A detailed action plan has been prepared for the implementation of the mission's recommendations.

G. Modernizing the Financial System and Ensuring Financial Stability

60. CBS remains committed to ensuring a stable and well-capitalized banking system that can support the recovery by effectively monitoring and supervising the health of the financial system. To ensure effectiveness of the supervisory process, CBS stands ready to take relevant and timely enforcement actions where necessary. If any bank becomes undercapitalized, the CBS will use the set of relevant early intervention measures, including further suspension of dividend payments. Within CBS 'usual regulatory framework, viable but undercapitalized banks would be required to submit capital plans while nonviable financial institutions would be resolved using the appropriate resolution tools. Borrower support measures should be gradually unwound, and the remaining ones will be targeted and time bound. CBS will ensure that banks' loan classification correctly reflects the asset quality of the banking system and regulatory forbearance measures will be withdrawn.

61. CBS has made its supervisory framework more risk-sensitive, objective, forward-looking and continuous. For that purpose, CBS had initiated a project in 2018 for the adoption of a risk-based supervision (RBS) framework, which integrates Basel II Pillar 2 requirements. During 2020, CBS successfully completed the second phase of the project which entailed the design and development of the RBS framework and associated data models, guidelines/circulars, manuals, and policies, as well as capacity building for supervisors and supervised entities. The initial roll out of the RBS framework has started in 2021.

62. Throughout 2020, work remained ongoing to finalize a policy paper for adoption of Basel II Pillar 1. The paper was endorsed by the Cabinet of Ministers in late 2020 and is now with the Attorney General's Office for drafting. As regards to Basel II Pillar 3, the CBS anticipates finalizing its set of disclosure guidelines by May 2022. Furthermore, the policy paper for the amendment in the Financial Institutions (Capital Adequacy) Regulations, 2010 to adopt the Basel III capital definition will be approved by the Cabinet by May 2022, with the assistance of technical advisors (*structural benchmark for end-May 2022*).

63. The CBS has since September 2021, initiated work in drafting a paper on unwinding of policy measures that were implemented in light of COVID-19. Thus far, work has been focused on the gathering of disaggregated data from commercial banks, Development Bank of Seychelles and Seychelles Credit Union on COVID-19 related forbearance measures, moratoria and borrower support measures. Following this, CBS shall analyze the data and perform stress tests to assess the resilience of the banking sector. Results of the analysis and stress tests, along with research on the impact of these measures and unwinding them on banks' asset quality shall assist in putting forth recommendations on how and when best to unwind these measures. CBS is targeting to present the results to the IMF Board for consideration at its meeting set for December 2021.

64. In order to boost financial sector resilience, CBS will enhance the monitoring of the banking system by collecting additional information including for restructured and rescheduled loans and FX placements and exposures. CBS will closely monitor and assess the asset quality of banks and take early intervention measures where necessary. To preserve the

stability of the financial system while supporting growth, banks will be encouraged to engage in restructuring of loans for firms that are viable but have temporary liquidity shortages. CBS will monitor the relevant reclassification of loans and proactively provide guidance on prudential treatment of moratoria and NPL management strategies.

65. The CBS focuses on strengthening the legal basis of the Financial Stability Committee (FSC). Following the establishment of the FSC in March 2016, work remains ongoing in ensuring that the legal basis of the FSC and its mandate are strengthened. In that regard, CBS prepared a draft policy paper outlining various policy considerations for the drafting of a financial stability bill in April 2021. CBS has requested the IMF's assistance to peer review the policy paper on Financial Stability Act. Hence, CBS will submit the Policy Paper to the Cabinet for approval by March 2022 (*revised structural benchmark*).

66. The CBS remains committed to having a robust crisis management and resolution framework. We will take the necessary steps to enhance our macroprudential toolkit as well as the crisis management and bank resolution framework. A policy paper supporting the drafting of an effective resolution framework, aligned with the BCBS recommendations and FSB Key Attributes of Effective Resolution Regimes, was presented to the Cabinet of Ministers and endorsed in December 2018. However, due to capacity constraints on the legislative drafting, the policy paper has not yet been turned into a draft bill. The policy paper is currently being reviewed in view of recent developments, necessitating changes to further enhance the powers of resolution authorities in respect of co-ordination and co-operation mechanisms, as well as instruments to deal with evolving types of crises, such as the recent pandemic whereby aspects of business continuity and operational resilience have received due attention. By end June 2022, CBS will submit a Policy Paper to the Cabinet of the proposed bank resolution framework in alignment with international best practices and tailored to the financial system of Seychelles (*structural benchmark for end-June 2022*). The draft Bank Resolution Bill will be approved by the Cabinet by end June 2023 (*structural benchmark for end-June 2023*).

67. The CBS pursues its effort in ensuring that its legislative framework for the National Payment System remains aligned with international standards and best practices. A review of the National Payment System Act, 2014, along with supporting regulations, is being undertaken to ensure that deficiencies identified while administering the Act are addressed and its regulatory framework is aligned with international standards and best practices. Policy proposals for amendments to the legal framework are anticipated to be finalized in March 2022. In addition, the CBS is in the process of finalizing its oversight framework and, with the technical assistance received from AFS in May-June 2021. This work is expected to be completed by December 2021.

68. The CBS pursues the quest to have a resilient and inclusive national payment system. The Policy Paper on the Modernization of the National Payment System was presented to the new Cabinet of Ministers in September 2021 alongside the National Fintech Strategy. While discussions are ongoing with the private sector to establish an entity to manage payment system infrastructures, in October 2021, the Request for Information for the Core Banking project was released. A new core

banking system is deemed critical to meet the perceptible needs associated to the developments in the national payment system. The CBS has further engaged with VISA, to reduce fees on card transactions. VISA has introduced interchange modifications and lower segment rates for education, fuel, quick service restaurants, small retail, telecommunications and utilities. The interchange modification that will be introduced in Seychelles will be effective as of February 2022.

69. The CBS is committed to collaborate with the Government and the private sector to implement the Seychelles Fintech Strategy. The implementation of the Strategy, that was approved by the Cabinet of Ministers in September 2021, is underway with sectoral meetings being undertaken to present the strategy to stakeholders. The Central Bank has sought support from the Alliance for Financial Inclusion for the formulation of a Regulatory Sandbox that has as ultimate objective to embrace innovative financial products or services. The Regulatory Sandbox is expected to be in place by the end of 2022.

70. The competent authorities are cognizant that a robust financial consumer protection legal framework coupled with an aggressive digital financial literacy campaign are crucial given the developments in the financial sector. Digital financial literacy remains at the forefront of CBS' efforts with emphasis being placed on cyber security as well as the consumers' roles and responsibilities on the digital journey. Furthermore, the revised policy decisions as regards to the Financial Consumer protection bill was approved by Cabinet in October 2021. The Bill is expected to be approved by the National Assembly in the first quarter of 2022.

71. The Central Bank is committed to enhancing access to affordable and sustainable finance. Work is therefore ongoing to implement a comprehensive Credit Information System accompanied by the supporting legal framework. The enhanced Credit Information System will include credit information from non-financial firms in addition to banks. This is essential for an inclusive economic growth. The contract to implement an enhanced Credit Information System has already been awarded and the project is tentatively scheduled to be completed by the end of 2022.

72. Seychelles continue to show progress on its AML/CFT framework. Based on the significant reforms done by Seychelles, the Eastern and Southern Africa Anti-Money Laundering Group (ESAAMLG) have approved 9 re-ratings for Seychelles so far out of the 20 recommendations which have deficiencies. This was after the 21st Council of Ministers and 42nd ESAAMLG Task Force of Senior Officials Virtual Meetings held in September 2021. Seychelles intend to request for another re-rating for another 10 recommendations by the end of January 2022 after enactment of a number of legislations by the end of 2021.

73. Having a robust AML-CFT regulatory and supervisory framework remains high on the agenda. In August 2020, the new AML/CFT Act and Regulations came into force. These have been formulated to cater to deficiencies identified by the Mutual Evaluation undertaken by ESAAMLG and the weaknesses identified through the National Risk Assessment which was finalized in 2018. One of the major changes to the Act was the allocation of the supervisory aspect of ML and TF, to three supervisory authorities; FIU, FSA and CBS, in order to ensure effectiveness in the supervision of the entities regulated by the respective supervisory authorities. A tripartite Memorandum of

Understanding was signed between the aforementioned authorities in 2020 to further foster collaboration in the discharge of their regulatory and supervisory functions vis-à-vis the new AML/CFT legislation.

74. In August 2020, the new Beneficial Ownership Act (“BO Act”) and Regulations came into force. The BO Act provides for identification and verification of beneficial ownership of legal persons and legal arrangements, in addition to the requirements to establish and maintain an up-to-date register of beneficial owners at the principal place of its resident agent, and a centralized database to be kept by Financial Intelligence Unit. In 2021 amendments of the International Business Companies (IBCs) Act required accounting records of IBCs to be kept in the registered office in Seychelles.

- The centralized database became operational in July 2021. Eight two per cent of the international financial services sector legal persons and legal arrangements (i.e. International Business Companies, Trust, Foundations etc.) submitted information to the beneficial ownership database by October 2021. The FIU is working closely with the remaining legal persons and legal arrangements, through their resident agents, to ensure their compliance by December 2021. The Non-compliant legal persons and legal arrangements will be sanctioned as per the provisions of the BO Act.
- The Financial Services Authority (“FSA”) has as of October 2021, initiated a series of inspections at the premises of resident agents so as to gauge the level of compliance of the legal persons and legal arrangements with the relevant provisions of the BO Act.
- Based on the outcome of the 2021 inspections, the FSA will, by the start of January 2022 submit a risk-based action plan on its intended supervisory activities, specifically with regards to compliance inspections for the calendar year 2022. The FSA and Financial Intelligence Unit (FIU) will consequently publish, by June 2022 an assessment report detailing, inter alia, an assessment of the level of compliance of the legal persons and legal arrangements vis-à-vis the applicable provisions of the BO Act including whether the information being populated on the registers and the centralized database is accurate and up to date.
- The FSA will as part of its onsite and offsite activities impose the relevant sanctions for cases of non-compliance observed with respect to the provisions of the BO Act.
- The authorities have also been working closely with the domestic entities for the submission of related information to the beneficial ownership database by end-January 2022. The BO Act and Regulations will be amended to address deficiencies and concerns in relation to certain provisions in the legislation, and the amendments to the Act is expected to be gazetted by End-November 2021.

75. The Republic of Seychelles has been removed from Annex I of the European Union’s (EU’s) list of non-cooperative jurisdictions for tax purposes (the “EU blacklist”) following the Economic and Financial Affairs Council of the EU meeting on the 5th October 2021. This follows key steps taken in reforming Seychelles’ territorial tax regime to address the concerns of the

EU, in conjunction with addressing concerns of the Global Forum on Transparency and Exchange of Information for Tax Purposes (the Global Forum).

76. The Seychelles has been moved to Annex II of the list of non-cooperative jurisdictions (the “EU grey list”) for criterion 1.2 (tax transparency), with removal from Annex II pending the positive outcome of a Global Forum supplementary review. Moving to the EU grey list suspends sanctions (“Defensive Measures”) invoked as a result of being on the EU blacklist.

A. Refining the Territorial Regime to Deliver on the Needs of the Seychelles whilst Allaying EU Concerns

77. On 16th September 2021, following engagement with both the EU and the private sector, the Business Tax (Amendment) (Commencement) Notice, 2021 and Business Tax (Amendment of Seventh Schedule) Regulations, 2021 were published in the Gazette. This brought into effect refinements in the Seychelles territorial tax system, such that the exemption from tax for foreign income is suitably targeted. It amended the Business Tax Act (Cap 20) to ensure that the following applies for companies that are members of a multinational group:

- Activities performed abroad by a permanent establishment of a Seychelles company will be exempt from tax in the Seychelles, with foreign income from activities that are not sufficient to qualify as a permanent establishment remaining taxable.
- Foreign income received on Seychelles based intellectual property will be taxable in the Seychelles, with a territorial exemption for income from patents (and equivalent rights) related to the level of research and development undertaken in the Seychelles connected to the creation of that patent.
- Foreign passive income will be exempt under the territorial regime where the Seychelles company receiving the passive income has adequate economic substance in the Seychelles.

Any foreign income that is subject to tax in the Seychelles, such as companies with insufficient economic substance or on non-patent intellectual property, will be taxed in the Seychelles, with a credit for foreign taxes incurred.

In addition, the Act updates the definition of “permanent establishment” to align with the latest model definitions of the Organisation for Economic Cooperation and Development (OECD) and the United Nations.

H. Meeting Global Forum Standards

- Seychelles’ request for an Exchange of Information on Request supplementary review was presented and approved at a meeting of the Peer Review Group (PRG) on 17th September 2021.

- The request for supplementary review followed the Seychelles' implementation of an extensive programme to ensure the framework for exchange of information is in place, focusing on:
 - legislative reform underpinning availability and access to information,
 - strengthening supervision (reporting requirements) and monitoring,
 - strengthening enforcement and penalties,
 - streamlining exchange of information processes,
 - implementing a tracking system, building a statistics database,
 - focusing on capacity building both in the administration and of taxpayers, and
 - extending the exchange network to include all relevant jurisdictions.
 The Seychelles submission was done after the enactment of five key pieces of legislation in 2020 and 2021 as follows:
 - Legislation enacted in 2020
 - Beneficial Ownership Act, 2020

The Beneficial Ownership Act, 2020 came into operation on the 28th August 2020 and has ensured that the definition of beneficial owners satisfies the Financial Action Task Force (FATF) and OECD requirement.

- Legislation enacted in 2021
 - Limited Partnerships (Amendment) Act, 2021
 - International Business Companies (Amendment) Act, 2021
 - Foundations (Amendment) Act, 2021
 - Trusts Act, 2021

All entities will need to keep accounting information in Seychelles together with the supporting transaction documentations. These requirements will also apply to entities that are struck off and dissolved. All such data need to be kept up to date and must be kept for at least seven years.

The PRG members concurred that the Seychelles qualified for a supplementary review, and that the review would require an on-site visit.

H. Next Steps

The only remaining step needed to enable Seychelles to be removed from Annex II is obtaining a Largely Compliant status in the forthcoming Supplementary Review, and thereby satisfying criterion 1.2. With the new rules on availability of information now passed, Seychelles is building a track record under the new system, ready to demonstrate the success of the new regime in the on-site visit of the Global Forum (scheduled in 2022).

78. Program monitoring. Program implementation will continued to be monitored through semi-annual reviews, quantitative performance criteria and indicative targets, continuous

performance criteria, and structural **benchmarks**. The second review is set for June 2022 based on end-December 2021 quantitative targets and the third review is set for December 2022 based on end-June 2022 quantitative targets. The quantitative targets and structural benchmarks are set out in Tables 1 and 2 of the MEFP respectively. Detailed definitions and reporting requirements for all performance criteria are contained in the Technical Memorandum of Understanding (TMU) attached to this memorandum, which also defines the scope and frequency of data to be reported for program monitoring purposes. During the program period, the government will not introduce or intensify restrictions on payments and transfers for current international transactions or introduce or modify any multiple currency practice without the IMF's prior approval, conclude bilateral payments agreements that are incompatible with Article VIII of the IMF's Articles of Agreement, or introduce or intensify import restrictions for balance of payments reasons.

Table 1. Seychelles: Proposed Quantitative Program Targets, 2021-2022 ¹
(In millions of Seychelles Rupees)

	July 31, 2021			September 30, 2021			December 31, 2021			March 31 2022			June 30, 2022			September 30, 2022			December 31, 2022			
	Performance Criteria			IT			Performance Criteria			IT			Performance Criteria			IT			IT			
	Prog.	Actual	Status	Prog.	Adjusted targets	Actual	Status	Prog.	Actual	Status	Prog.	Actual	Status	Prog.	Actual	Status	Prog.	Actual	Status	Prog.	Actual	Status
A. Quantitative performance criteria²																						
Net domestic financing of the government (ceiling) ³	2034.0	1521.7	Met	-109.0	1385.0	917.5	Met	-555.0		25.0		100.0		120.0		155.0						
Primary balance of the consolidated government (floor)	-1726.0	-723.4	Met	-2026.0		-696.9	Met	-2289.0		-700.0		-178.0		-198.0		-232.1						
Total revenue (floor) ⁴	2217.4	3969.6	Met	3626.0		5242.4	Met	7252.0		1735.5		3470.9		5206.4		8923.1						
Net international reserves of the CBS, millions of US dollars (floor) ⁵	359.0	396.0	Met	374.0	329.0	455.0	Met	394.0		407.0		410.0		415.0		420.0						
B. Continuous quantitative performance criteria (ceilings)																						
Accumulation of new external payments arrears	0.0	0.0	Met	0.0		0.0	Met	0.0		0.0		0.0		0.0		0.0						
Accumulation of new domestic payments arrears	0.0	0.0	Met	0.0		0.0	Met	0.0		0.0		0.0		0.0		0.0						
C. IT																						
Net change in CG guaranteed domestic and external debt	502.0	-1880.0	Met	604.0		-2141.0	Met	753.0		990.0		1226.4		1532.9		1839.5						
Priority social expenditure (floor) ²	475.2	826.9	Met	712.8		1058.2	Met	1425.5		287.0		574.1		861.1		1483.6						
Sources: Seychelles authorities; IMF staff estimates and projections.																						
¹ The terms in this table are defined in the Technical Memorandum of Understanding (TMU).																						
² The performance criteria are cumulative from the beginning of the calendar year.																						
³ If the amount of disbursed external budgetary assistance net of external debt service obligations falls short of the program forecast, the ceiling on net domestic financing will be adjusted pro-tanto. If the amount of disbursed external budgetary assistance net of external debt service obligations exceeds the program forecast, the ceiling will be adjusted downward by the excess disbursement unless it is used to reduce domestic payment arrears. The NDF refers to the central government.																						
⁴ If growth fall short of targets the revenues floor will be adjusted accordingly.																						
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. The floor will also be adjusted upwards (downwards) by the amount that external debt service payments fall short of (exceed) the amounts assumed in the program. The floors will also be adjusted upwards by the amount of the new SDR allocation to Seychelles if the IMF makes a new allocation of SDRs to its membership.																						

Table 2. Seychelles: Actual and Proposed Structural Benchmarks Under the EFF, 2021–2023

Actions	Timing	Objective	Status
Fiscal and Public Financial Management Policy			
Cabinet approval of all the necessary legislation to ensure Seychelles is fully compliant to be removed from the EU list of non-cooperative jurisdictions.	End-September 2021	Ensure Seychelles is fully compliant with EU and OECD harmful preferential tax regimes (BEPS Action 5).	Met
Ministerial Approval of Circular to reduce the deviation between the forecast and the outcome in the monthly cashflow plan consistent with the 2022 budget, in consultation with IMF staff.	End-June 2022	Strengthen Treasury cash management.	
Cabinet approval of legislative amendments to streamline VAT exemptions, in consultation with IMF staff.	End-September 2022	Strengthen revenue mobilization.	
Cabinet approval of revisions to business tax laws to streamline exemptions, in consultation with IMF staff.	End-November 2021	Strengthen revenue mobilization.	Met
Completing the customs automation project, in consultation with IMF staff.	End-September 2023	Strengthen revenue mobilization.	
Debt Management			
Publish a new domestic debt management strategy document.	End-March 2022	Mitigate foreign currency and rollover risks, optimize issuance decisions, and strengthen benchmark pricing through extension of the yield curve. The debt management strategy will guide future borrowing decisions based on cost-risk trade-offs related to the debt portfolio.	
Publish an Annual Borrowing Plan along with an auction calendar to help market participants plan their liquidity management and reduce uncertainty.	End-March 2022	Implement the debt management strategy.	
The Ministry of Finance will publish quarterly reports on debt management operations and outstanding debt position as published in the debt bulletin on its website.	End-September 2021 and quarterly thereafter	Enhance debt management and transparency.	Met
The Ministry of Finance, in consultation with the CBS will approve a plan for government securities trading framework	End-December 2022	Implement the debt management strategy.	
The National Public Debt Management Committee chaired by the Principal Secretary Ministry of Finance will approve a quarterly borrowing plan on a recurring basis	End-March 2022 and quarterly thereafter	Implement the debt management strategy.	

**Table 2. Seychelles: Actual and Proposed Structural Benchmarks Under the EFF, 2021–2023
(concluded)**

State-Owned Enterprises (SOEs)			
Cabinet approval of (1) least cost structure for Air Seychelles, as part of the 2022 budget process; and (2) long-term strategy that lays out long-term options for Air Seychelles, in consultation with IMF/WB staff.	End- September 2021	Minimize the fiscal impact on the 2022 budget.	Met
Cabinet approval of Amendments on the Public Enterprise Monitoring Committee (PEMC) Act to strengthen the enforcement power of the PEMC, in consultation with IMF staff.	End-November 2021	Reduce contingent fiscal risks.	Met
Financial Sector Stability			
Cabinet approval for policy paper for the draft Financial Stability Bill for empowering the relevant authorities to use macroprudential tools and providing the legal basis for the Financial Stability Committee.	End-November 2021-Revised deadline March 2022	Enhance financial stability powers with the aim of safeguarding the stability of the financial system	“Not Met – Reset: End- March 2022”
Cabinet approval of the policy paper for the amendment in the Capital Adequacy Regulation for the CBS to adopt the Basel III Capital Definition	End-May 2022	Buttress banking sector soundness and financial sector stability	
Submit policy paper for the draft Bank Resolution Bill to the Cabinet	End-June 2022	Address shortcomings from previously approved cabinet policy paper for bank resolution and to align with ongoing revisions to the Financial Institutions Act, 2004 as amended and Insolvency Law, as well as cater recent developments stemming from the current crisis. Includes identification of consequential amendments in subsidiary legislations, with the objective of providing the regulators the necessary powers to effectively resolve troubled financial institutions.	
Cabinet approval for draft Bank Resolution Bill in alignment with international best practice	End-June 2023	Address shortcomings from previously approved cabinet policy paper for bank resolution and to align with ongoing revisions to the Financial Institutions Act, 2004 as amended and Insolvency Law, as well as cater recent developments stemming from the current crisis. Includes identification of consequential amendments in subsidiary legislations, with the objective of providing the regulators the necessary powers to effectively resolve troubled financial institutions.	

Attachment II. Technical Memorandum of Understanding

This Technical Memorandum of Understanding (TMU) defines the performance criteria, quantitative benchmarks, and structural benchmarks of the Republic of Seychelles' economic and financial program supported by the Extended Fund Facility (EFF). It also specifies the frequency and deadlines for data reporting to the staff of the International Monetary Fund (IMF) for program monitoring purposes.

I. Definitions

- Unless otherwise indicated, “government” is understood to mean the central government of the Republic of Seychelles and does not include any political subdivisions (such as local governments), the central bank, or any other public or government-owned entity with autonomous legal personality not included in the government’s budget.
- Consolidated government debt is understood to mean central government plus public guarantees.
- “External debt” is defined as debt denominated in any currency other than the Seychellois rupee (SCR). (1) The performance criterion or indicative target will include all forms of debt. The definition of “debt” is set out in paragraph 8 (a) of the Guidelines on Public Debt Limits in Fund-Supported Programs attached to the Executive Board Decision No. 16919-(20/103), adopted October 28, 2020. For the purpose of these guidelines, the term “debt” will be understood to mean a current, i.e., not contingent, liability, created under a contractual arrangement through the provision of value in the form of assets (including currency) or services, and which requires the obligor to make one or more payments in the form of assets (including currency) or services, at some future point(s) in time; these payments will discharge the principal and/or interest liabilities incurred under the contract. Debts can take a number of forms, the primary ones being as follows:
 - loans, i.e., advances of money to the obligor by the lender made on the basis of an undertaking that the obligor will repay the funds in the future (including deposits, bonds, debentures, commercial loans and buyers’ credits) and temporary exchanges of assets that are equivalent to fully collateralized loans under which the obligor is required to repay the funds, and usually pay interest, by repurchasing the collateral from the buyer in the future (such as repurchase agreements and official swap arrangements);
 - suppliers’ credits, i.e., contracts where the supplier permits the obligor to defer payments until sometime after the date on which the goods are delivered or services are provided; and
 - leases, i.e., arrangements under which property is provided which the lessee has the right to use for one or more specified period(s) of time that are usually shorter than the total expected service life of the property, while the lessor retains the title to the property. For the purpose of these guidelines, the debt is the present value (at the inception of the lease) of

all lease payments expected to be made during the period of the agreement excluding those payments that cover the operation, repair, or maintenance of the property.

(2) 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.

II. Quantitative Performance Criteria

A. Ceiling on Net Domestic Financing of the Government

1. Net domestic financing (NDF) of the government is defined as the sum of: (i) net bank credit to the government, defined below; and (ii) net nonbank financing of the government, including the proceeds of the sale of government assets, which includes proceeds from the divestiture of shares of public enterprises, that is privatizations, Treasury bills, and other securitized obligations issued by the government and listed in rupees in the domestic financial market, and any Central Bank of Seychelles (CBS) credit to the government, including any drawings on the rupees counterpart of the Special Drawing Rights (SDR) allocation.
2. The data deemed valid within the framework of the program will be the amounts for net bank credit to the government and for the net amount of Treasury bills and bonds issued in rupees on the domestic financial market, calculated by the CBS, and the amounts for nonbank financing calculated by the Treasury of Seychelles.
3. Gross external budgetary assistance is defined as grants, loans, and non-earmarked debt relief operations (excluding project-related loans and grants, use of IMF resources, and debt relief under the Heavily Indebted Poor Countries (HIPC) and Multilateral Debt Relief (MDRI) Initiatives. Net external budgetary assistance is defined as the difference between gross external budgetary assistance and the sum of total debt service obligations on all public external debt (defined as the sum of interest payments and amortizations on all external loans, including interest payments and other charges to the IMF and on project-related loans, but excluding repayment obligations to the IMF), and all payments of external arrears.
4. Adjustors: Net domestic financing of the government will be adjusted downward (upward) if net external budgetary assistance exceeds (falls short of) the program projections.
5. For the purpose of monitoring, data will be provided to the Fund by the authorities on a monthly basis with a lag of no more than four weeks from the end-of-period.

B. Floor on the Primary Balance

6. The primary balance is defined as total revenues and grants minus primary expenditure and covers non-interest government activities as specified in the budget. The primary balance will be measured as cumulative over the fiscal year and it will be monitored from above the line.

- Revenues are recorded when the funds are transferred to a government revenue account. Tax revenues are recorded as net of tax refunds. Revenues will also include grants. Capital revenues will not include any revenues from non-financial asset sales proceeding from divestment operations.
- Central government primary expenditure is recorded on a cash basis and includes recurrent expenditures and capital spending. Primary expenditure also includes transfers to State-Owned Enterprises (SOEs). All primary expenditures directly settled with bonds or any other form of non-cash liability will be treated as one-off adjustments and recorded as spending above-the-line, financed with debt issuance, and will therefore affect the primary balance.

7. Adjustors: The primary balance target will be adjusted upward (downward) by the surplus (shortfall) in disbursements of grants relative to the baseline projection.

8. For the purpose of monitoring, data will be provided to the Fund by the authorities monthly with a lag of no more than four weeks from the end-of-period.

C. Floor on Total Revenue

9. Total government revenue includes tax and nontax revenue, as shown in the fiscal table, but excludes external grants, revenue of autonomous agencies, and privatization receipts.

10. The government revenue floor will be adjusted downward by the amount equivalent to the shortfall in gross domestic product compared to the program projections.

11. For the purpose of monitoring, data will be provided to the Fund by the authorities on a monthly basis with a lag of no more than four weeks from the end-of-period.

D. Floor on Net International Reserves

12. Net International Reserves (NIR) of the CBS are defined as the difference between reserve assets and reserve liabilities with a maturity of less than one year.

13. Reserve assets are defined as readily available claims on nonresidents denominated in foreign convertible currencies. They include the CBS's holdings of monetary gold, SDRs, foreign currency cash, foreign currency securities, deposits abroad, and the country's reserve position at the Fund. Excluded from reserve assets are any assets that are pledged, collateralized, or otherwise encumbered, claims on residents, claims in foreign exchange arising from derivatives in foreign

currencies vis-a-vis domestic currency (such as futures, forwards, swaps, options et cetera), precious metals other than gold, assets in nonconvertible currencies, and illiquid assets.

14. Reserve liabilities are: (1) all foreign exchange liabilities to residents and nonresidents with maturity of less than one year, including commitments to sell foreign exchange arising from derivatives (such as futures, forwards, swaps, options, et cetera); and (2) all liabilities outstanding to the IMF (only the total outstanding use of Fund Credit and loans is included in reserve liabilities).

15. Adjustors: The floor on the CBS's NIR will be adjusted upward (downward) by the amount by which the external non-project loans and non-project cash grants exceeds (falls short of) the amounts assumed in the program. The floor will also be adjusted upwards (downwards) by the amount that external debt service payments fall short of (exceed) the amounts assumed in the program. The floors will also be adjusted upwards by the amount of the new SDR allocation to Seychelles if the IMF makes a new allocation of SDRs to its membership.

16. For the purpose of monitoring, the data will be reported by the CBS on a daily basis, with a lag of no more than one week from the end-of-period.

E. Non-Accumulation of New Domestic and External Arrears (continuous)

17. Domestic payments arrears are defined as domestic payments due but not paid by the government after a 90-day grace period, unless the payment arrangements specify a longer payment period. The Ministry of Finance records and updates the data on the accumulation and reduction of domestic payments arrears.

18. The government undertakes not to accumulate any new domestic payments arrears. The non-accumulation of new domestic payments arrears will be continuously monitored throughout the program. The accumulation of any new domestic payments arrears will be reported immediately by the government to Fund staff.

19. The government undertakes not to accumulate any new external public payments arrears, with the exception of arrears related to debt that is the subject of rescheduling. External public payments arrears are defined as payments due but not paid by the government as of the due date specified in the contract, taking into account any applicable grace periods, including contractual and late interest, on the external debt of the government or external debt guaranteed by the government. The performance criterion on the non-accumulation of new external public payments arrears will be continuously monitored throughout the program. The accumulation of any new external payments arrears will be reported immediately by the government to Fund staff.

20. Standard continuous performance criteria include: 1) prohibition on the imposition or intensification of restrictions on making of payments and transfers for current international transactions; 2) prohibition on the introduction or modification of multiple currency practices; 3) prohibition on the conclusion of bilateral payments agreements that is inconsistent with Article VIII;

and 4) prohibition on the imposition or intensification of import restrictions for balance of payments reasons.

III. Indicative Targets

A. Net Change in Consolidated Government Guaranteed Domestic and External Debt

21. The government guaranteed domestic and external debt is defined as the public debt and includes the central government debt plus domestic and external guarantees provided by the government.

B. Floor on Government Social Spending

22. The indicative floor on social spending will apply to the expenditures incurred by the government on the following plans and programs that are intended to have a positive impact on education, health, social protection, housing and community services and recreational activities:

- Social Programs of Government Benefits and approved programs of ASP (Invalidity benefits, disability benefits, post-secondary students bursary, sickness benefits, maternity benefits, orphans' benefits, injury benefits, semi-orphan benefits, apprenticeship scheme, home careers schemes, vulnerable home repair scheme, SPTC travel concessions, inter island transport etc.)

IV. Program Reporting Requirements

23. Performance under the program will be monitored from data supplied to the IMF by the authorities. The authorities will transmit promptly to IMF staff any data revisions as well as other information necessary to monitor the arrangement under the EFF.

V. Data and Information

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

The CBS will report

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

- Daily reserve money data.
- Foreign exchange reserves position.
- A summary table on the foreign exchange market transactions.

- The results of the liquidity deposit auction, 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 and in GFSM2001 format.
- The detailed revenues and expenditures of the central government and social security fund.
- Import and export data from the customs department.
- Public debt report reconciled with the cash operations to minimize any statistical discrepancy.
- Consolidated creditors schedule on domestic expenditure arrears of the government.

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

- Accounts of the public nonbank financial institutions.

25. 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.

**Statement by Chang Huh,
Executive Director for Seychelles
Gantsogt Khurelbaatar, Advisor for Seychelles,
and Jinhyuk Yoo, Advisor for Seychelles
December 17, 2021**

The Seychellois authorities thank the IMF Executive Board, Management, and staff for the continued support. They also appreciate the constructive and candid policy dialogue they had with Fund staff during the first review discussions on the Extended Credit Facility (EFF). They consider that the staff report to the Executive Board provides an accurate account of the discussions.

Recent developments, COVID-19, Outlook

Since the approval of the program in July of this year, the economy has continued to recover quickly as most restrictions on tourist movements were lifted and the number of tourist arrivals has steadily increased. GDP is projected to grow at 6.1 percent in 2021, a big turnaround from a decline of 12.5 percent last year. The external position has strengthened, with foreign reserves accumulated, the current account deficit projected to narrow, and the exchange rate strongly appreciating. The public debt level relative to GDP is expected to decline by 11.2 percentage points from 92.2 percent at the end of 2020 to around 81 percent by the end of 2021. Interest rates for one-year Treasury bills have lowered by more than 450 basis points due to the successful implementation of a liability management operation (LMO) in July and improved investor confidence.

A majority of the population has been fully vaccinated and the number of infected cases is currently low, thanks to the successful vaccination campaign. The authorities are starting to administer booster shots for the adult population and vaccines for the youth.

The outlook is positive with growth of 7.2 percent projected for 2022 and around 5 percent over the medium term. However, significant downside risks remain as a small open tourism-dependent country. Global travel restrictions and new variants of COVID-19 could pose high risks to the tourism and economic recovery.

Program performance

Program performance has been strong. All quantitative program targets for the end of July have been met, with the primary budget deficit performance criterion met with a high margin. The structural reform agenda under the program is well underway and all structural targets were met except one. Due to capacity constraints, the authorities could not help postponing submitting the Policy Paper on the Financial Stability Act to the cabinet for approval early next year. They have already requested technical assistance from the Fund and are confident in completing this benchmark by the next review. On contingent liability issues arising from Air Seychelles, Air Seychelles has gone into administration. In early October 2021, the government appointed two administrators as per the requirement of the Insolvency Act and they will explore the optimal ways of restructuring it and settling its debts from its assets.

Fiscal policy

The key pillar of the Seychelles' EFF program is to frontload fiscal adjustment to reduce the debt sustainability risks. Despite a reduction in expected external financing, the authorities were able to relieve fiscal and debt rollover risks, with the successful debt exchange in July and the positive revenue performance. As a result, the primary fiscal deficit in 2021 is expected to reach 6.6 percent of GDP, significantly lower than the projection of 9.1 percent of GDP at the program approval. Going forward, the authorities are determined to further reduce the primary fiscal deficit, thereby reducing public debt to around 50 percent by 2026. The primary deficit in 2022 is ambitiously set to 0.8 percent of GDP which is lower by 3.9 percentage points compared to the earlier benchmark.

The authorities have pursued a prudent expenditure policy, supported by structural reforms to rationalize inflexible outlays including wage and salaries. On the revenue side, they are seeking to widen the tax base with revisions of the exemptions under the VAT, rationalize business tax, limit deductibility provisions, and uniformize tax rates among sectors. Also, efforts to improve customs tax collection by moving to online services and reducing paper transactions and costs are planned in 2022. In addition, the authorities are working to adopt a medium-term budget framework and improve the Public Sector Investment Plan (PSIP).

External bilateral financing planned for 2022 is delayed, but the authorities are working with partners to secure financing next year. Thanks to the more positive fiscal outturn, the financing gap is reduced, and should external financing fall short, the authorities will consider using more domestic financing or the proceeds from SDR allocations.

Monetary and financial sector policies.

Monetary policy has remained accommodative since the second quarter of 2020 to support domestic economic activity. Inflation is expected to be elevated at 9.8 percent in 2021, but it

is forecast to slow to 3.3 percent by the end of 2022. However, increased economic activity and supply-side constraints related to the global disruption in shipments may sustain inflation and negatively affect inflation expectations. The Central Bank of Seychelles (CBS) is monitoring inflation dynamics and stands ready to act if inflationary pressures persist.

CBS is committed to the flexible exchange rate regime and will intervene only to limit disorderly exchange rate movements. CBS also remains committed to ensuring a stable and well-capitalized banking system that can support the recovery by effectively monitoring and supervising the health of the financial system.

Structural reforms

The current pandemic is a reminder that the Seychelles economy is highly vulnerable and largely dependent on two sectors - tourism and fisheries. Under the program, the authorities plan to undertake reforms to diversify the economy and deepen economic linkages among sectors and support the agricultural sector to improve self-sufficiency in food supply. In addition, the authorities aim to strengthen and improve the country's resilience to climate change, with plans to reduce greenhouse gas emissions, increase investment to improve climate change resilience, and boost power generation from renewable resources. The long term vision is to achieve a decarbonized economy by 2050. Improving the business environment and governance are also key priorities, with the authorities planning to create an enabling environment for entrepreneurship by digitizing most government services, improve the country's digital capacity and support domestic production to reduce import dependence.