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Seychelles: Letter of Intent, Memorandum of Economic and Financial Policies, and Technical Memorandum of Understanding

December 3, 2009

The following item is a Letter of Intent of the government of Seychelles, which describes the policies that Seychelles intends to implement in the context of its request for financial support from the IMF. The document, which is the property of Seychelles, is being made available on the IMF website by agreement with the member as a service to users of the [IMF](#) website.

SEYCHELLES: LETTER OF INTENT

Mr. Dominique Strauss-Kahn

Managing Director
International Monetary Fund

December 3, 2009

Dear Mr. Strauss-Kahn:

1. The attached Memorandum of Economic and Financial Policies for 2009–12 (MEFP) describes Seychelles' performance in the third quarter of 2009, policies for the remainder of 2009, as well as our policies for the 3 year period 2010–12.
2. **We request completion of the third review under our Stand-By Arrangement (SBA) and the release of the fourth tranche of SDR 2.2 million (25 percent of quota) there under.** All the quantitative performance criteria (PCs) at end-September 2009 were met and all three structural benchmarks at end-September were observed.
3. **Following completion of the third review, and associated purchase, we request that the SBA be cancelled and replaced with a 3-year arrangement under the Extended Fund Facility (EFF)** in amount of SDR 19.8 million (225 percent of quota) and disbursement of the first tranche of SDR 0.88 million (10 percent of quota). We expect to meet all quantitative PCs and structural benchmarks for end-December 2009.
4. **The EFF will support our public debt restructuring process** aimed at reestablishing external sustainability; **accompany a comprehensive medium-term structural reform strategy** aimed at securing macroeconomic stability and raising growth performance; and **guide our macroeconomic policies** over the next three years.
5. **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 remain committed to full implementation of the recommendations of the Fund's safeguards assessment of the Central Bank of Seychelles (CBS).

6. **In line with our commitment to transparency, we request that the IMF publish this letter, the MEFP, the technical memorandum of understanding (TMU), and the staff report.** We will simultaneously publish these documents in Seychelles.

Sincerely yours,

/s/

James Alix Michel
President,
Republic of Seychelles
Attachments: MEFP and TMU

ATTACHMENT 1

SEYCHELLES: MEMORANDUM OF ECONOMIC, FINANCIAL
AND STRUCTURAL REFORM POLICIES FOR 2009–12

1. INTRODUCTION

1. This document:
 - a. Reviews macroeconomic and financial performance under our current Stand-By Arrangement (SBA) through end-September 2009.
 - b. Updates the MEFP of June 16, 2009 for the second SBA program review, detailing our policy commitments through the remainder of 2009 to support completion of the third SBA review.
 - c. Describes our macroeconomic policies and reform commitments for the three year period 2010–12 under a successor Extended Fund Facility (EFF) arrangement.

II. RECENT ECONOMIC DEVELOPMENTS AND PERFORMANCE UNDER THE PROGRAM

2. **The key objectives of our SBA—to stabilize the macroeconomy and initiate the first generation structural reforms—have been achieved.** The functioning of our economy has improved significantly following the reforms launched in late 2008. In particular, with the removal of all exchange restrictions has catalyzed substantial improvements in economic efficiency. After a period of turbulence immediately following exchange rate liberalization, the rupee stabilized and has appreciated significantly from its lows early in the year. Inflation has continued at near zero levels since March 2009 and nominal interest rates on short-term T-bills declined to under 5 percent at end-October, consistent with tight fiscal policy and exchange rate trends. The reconstitution of gross international reserves has progressed strongly to US\$136 million (1.3 months of imports) at end-October, in part due to the general SDR allocation (US\$10 million). All quantitative PCs at end-September 2009 were met with margins (Table 1) and we have implemented the measures included in the MEFP for the second SBA review (Table 2).

3. **The decline in real GDP growth in 2009 will be less than earlier projected, as the reduction in tourism earnings and related construction activity is attenuating.** As a small open economy, Seychelles was hard hit by the global recession and piracy in the Indian Ocean, but there are now early signs of a revival of business activity and employment creation. We now project real GDP to contract by 7½ percent in 2009, an improvement on the 10.7 percent contraction projected in June.

4. **The government has consistently exceeded its fiscal targets this year with a primary surplus of 13.4 percent of GDP recorded in the first nine months of 2009.** Expenditure has been tightly controlled and revenue has held up well despite the difficult

domestic and external environment. The Public Procurement Act has induced needed discipline in expenditure commitments and the repayment of budget arrears has continued. Social assistance outlays have risen during the year, but have remained well within budget allocations.

5. **The Central Bank's (CBS) reserve money targeting framework is achieving its objectives and the CBS gained additional flexibility with the introduction of new indirect policy instruments.** In addition to weekly deposit auctions and a standing credit facility, the CBS's portfolio of treasury bills have been actively used in open market operations. In line with best international practices, repo and reverse repo transactions are gradually becoming the main policy tools for liquidity management. The rapid disinflation in 2009 has provided room for a measured easing of monetary policy. Reserve requirements have been reduced from 13 percent of deposits to 10 percent as of October 1, 2009 and the local asset ratio abolished. While benchmark interest rates on government securities fell sharply from the peak of 30 percent in January to 5 percent in October, credit growth has been slow to recover due to the contraction in the real economy.

6. **The floating exchange regime has contributed to the rapid stabilization of the economy and has eased the burden on monetary policy.** Following a period of overshooting after the float, the rupee has steadily appreciated as banks have unwound large open foreign exchange positions and real interest rates remained strongly positive through early October. The CBS's partly sterilized interventions have been limited to smoothing excessive market volatility and ensuring the sound functioning of the market. The nominal exchange rate appreciated sharply in early October, in part due to continued buildup of the government's cash balances through T-bill sales, which proved unnecessary. In response, treasury cash surpluses were sharply reduced in early October and the foreign exchange market has since stabilized.

7. **Our structural reform agenda is gaining momentum, with all structural benchmarks implemented as planned** (Table 3). A new Public Enterprise Monitoring and Control Act was approved by the National Assembly in September, legislating financial reporting obligations and corporate governance guidelines for all public entities. The introduction of a treasury single account has produced major improvements in cash and expenditure management. External financial audits of the seven largest public enterprises have been completed and management audits of major public entities have also progressed, catalyzing major changes in business practices in some key public enterprises (notably, the utilities company (PUC), the public transport company (SPTC) and Air Seychelles). New Central Bank and Financial Institutions Acts have been put in place, strengthening the framework for monetary policy and financial sector regulation and development.

8. **The CBS has made considerable progress implementing the recommendations of the 2008 Safeguards assessment report.** During 2009 the CBS Board approved a policy that will ensure adequate external audit quality in future years. It also has adopted an internal audit charter. The internal control framework was strengthened by: (i) the reorganization of

the Banking Services Division to allow for the segregation of the accounting and foreign reserves management functions and reporting; (ii) the establishment of an Investment Committee and adoption of an asset-liability management framework for strategic allocation of reserves; and (iii) the appointment of an Operational Risk Committee to oversee the development and maintenance of the CBS' operational risk management framework. The CBS is in the final stages of adopting IFRS-based financial reporting for the 2009 accounts.

9. **The CBS strengthened the capital requirement for banks and adopted a system of prompt-corrective action.** The system is driven by the CAMELS bank rating system and includes triggers for strong and aggressive action for banks that fail to meet the required capital levels. The CBS' Financial Services Supervision Division was reorganized with separate onsite, offsite, policy and foreign exchange sections.

10. **We have made good progress in normalizing relations with external creditors and restructuring our unsustainable external debt.** We successfully negotiated a debt restructuring with the Paris Club in April 2009, signed a bilateral rescheduling agreement with Malaysia on comparable terms and have also made good progress with private creditors. Following active discussions with all creditor groups, we are close to launching a debt exchange offer for Eurobond and amortizing note holders on terms compatible with Seychelles' limited payments capacity, and comparable to those agreed with Paris Club creditors. The offer will be supported by a US\$10 million policy-based Guarantee Operation from the African Development Bank, reducing the coupon on the exchange bond and providing additional comfort to creditors. We expect the debt exchange with commercial bondholders to be completed by mid-January 2010. Discussions with commercial banks have proceeded in parallel and restructuring terms agreed on a few loans. Some banks may participate in the exchange bond offer.

III. POLICIES FOR THE REMAINDER OF 2009

11. **We remain committed to implementing the policies and meeting the structural and quantitative targets for end-December 2009 described in our previous MEFP.** Our forecasts are for inflation to remain in the low single digits, allowing further measured easing of monetary policy. The external current account deficit is expected to narrow, with exports of tourism services expected to increase as the global economy recovers and additional hotel accommodation comes on line. Gross reserves are expected to rise further to US\$153 million by end-2009 (1.4 months of imports).

12. **We will meet the 2009 program primary surplus target, adjusted for foreign financing of 13.4 percent of GDP.** The government's over performance in the first 3 quarters has provided the fiscal space for a supplementary appropriation of about 2 percent of GDP to meet emergency expenditure needs, the most notable components of which are emergency financing for Air Seychelles (0.3 percent); departure payments for workers whose jobs are being outsourced in 2010 (0.3 percent); enhanced cofinancing of private sector tourism marketing (0.2 percent); the rehabilitation of PUC (0.4 percent); a targeted voluntary

13. departure scheme (0.1 percent); and strengthening the capacity of the Seychelles Revenue Commission (SRC) to deliver tax reform (0.1 percent). Our overall fiscal performance, coupled with falling interest rates and increased external financial assistance, will allow us to reduce domestic debt by 5½ percent of GDP in 2009. We are continuing to strengthen our treasury management capacity in close collaboration with the CBS.

14. **The CBS will closely monitor the impact of recent monetary easing.** Inflation has remained near zero for some time and the exchange rate appreciation of the past few months is still working its way through domestic prices. While the reserve money target for December has been raised moderately, the CBS stands ready to tighten monetary policy at the first signs of a pick up in inflation.

15. **Our structural reform efforts are progressing apace and we expect to meet the structural benchmarks set for end-December 2009 under our SBA.** Business tax reforms are being finalized for introduction from January 1, 2010 and we are working towards preparation of more comprehensive budget documentation for 2010. Further expenditure reforms and rationalization, bolstered oversight and monitoring of the public entities and enterprises, and strengthened financial sector supervision are being implemented. We have prepared a medium-term debt strategy and annual borrowing plan to accompany the 2010 Budget.

IV. MEDIUM-TERM MACROECONOMIC AND STRUCTURAL REFORM POLICIES

16. **The major objectives of our EFF-supported program will be to:**

- a. preserve macroeconomic stability;
- b. achieve external sustainability; and
- c. improve economic efficiency and durably raise growth through the implementation of a second generation of structural reforms.

17. **Our ambitious structural reform agenda aims to transform the economy by institutionalizing higher governance standards, rationalizing the public sector and improving the business environment.** We will continue to remove distortions, modernize economic laws and regulations, and reduce and refocus the role of the state in the economy from operator to facilitator and regulator. We will pursue a significant reinforcement of monitoring and control over parastatal bodies to address major financial risks to the stability of public finances and choke-points to growth. Some of the key reforms—public enterprise restructuring, tax reform, strengthened public financial management—were initiated under our current SBA.

18. **This reform strategy serves as a coordinating function for donors and stakeholders.** Our reform program is supported by contributions from several multilateral (AfDB, IBRD, EU, UNDP) and other development partners through development policy

loans, public expenditure reviews, related programs and technical assistance. Most notably, we are working with the World Bank to elaborate a strategy for improving the business climate and modernizing the labor law.

19. **The EFF provides a macroeconomic framework to guide fiscal and financial policies over the next three years.** After the shocks of 2008–09, we expect the economy to start a sustained recovery from 2010. There are positive signs that tourism and related services—the main drivers of growth—commenced a gradual recovery in the second half of 2009, and FDI is expected to rebound in 2010 with several large projects in the pipeline. The investment would be supported by a successful public external debt restructuring in late-2009/early-2010 that would reduce country credit risk. Real GDP growth is projected to recover to 4 percent in 2010 and to 5 percent in 2011–12, while inflation is expected to remain in the low single digits. The external current account deficit is expected to widen again in 2010, due to higher growth and FDI, but narrow over the medium term as tourism earnings recover. Foreign exchange reserves are projected to rise gradually to about 2½ months of import coverage by end-2012.

A. Fiscal Policy

20. **The overarching goals of fiscal policy are to put public finances on a sustainable path, while creating the fiscal space to raise public investment and support our targeted social safety net.** Primary fiscal surpluses will be targeted at 7 percent of GDP in 2010, declining to about 4½ percent by 2012, levels that are consistent with achieving our medium-term sustainability objective, assuming full external debt restructuring. This profile will allow us to reduce domestic public debt significantly, releasing resources to support private sector development.

2010 budget

21. **Following the sharp tightening in 2009, an easing of the fiscal stance to a 7 percent primary surplus is targeted for 2010.** We will implement the first phase of the medium-term tax reform with the 2010 Budget. The tax reforms are broadly revenue neutral in 2009 but overall revenue will be lower on account of significant one-off revenues and the exchange rate appreciation effect totaling almost 4 percent of GDP. We will also continue to strengthen the revenue commission and its tax administration functions to improve governance, efficiency, and effectiveness. A conservative revenue forecast is assumed in the program as there are uncertainties regarding the underlying tax base, the response to the tax reform, and the large nominal appreciation of the rupee in 2009, which are expected to result in realized revaluation losses primarily for the financial sector. Should overall revenue exceed projections in 2010, we intend to save a portion and use the rest for additional urgent infrastructure spending; the appropriate savings/spending balance would be determined in consultation with IMF staff at the time of the first program review under the EFF, determined in the context of the macroeconomic situation then prevailing.

22. **On the expenditure side, rationalizing the size of the public sector and reinforcing control over public finances will create the space for higher capital investment.** Building on our tight control of government expenditures in 2009, recurrent expenditures will be reduced further as a percentage of GDP in the 2010 Budget. This will allow us to increase capital expenditure to 7.7 percent of GDP in 2010 (including the spending contingency), directed primarily at urgent rehabilitation of the electricity and water infrastructure that was curtailed in the past by foreign exchange restrictions and, if left unaddressed, would threaten our projected growth recovery. The budget will also include an expenditure contingency of about 1 percent of GDP, which has been earmarked for investment projects that will proceed as long as the primary fiscal position remains on track.

Tax reform

23. **A fundamental medium-term reform of the tax system will be launched with the 2010 Budget.** Our objective is to have a simple, fair, and equitable system, which will promote growth, improve self-compliance, and level the playing field for investors. We will launch a communication campaign to explain tax system changes and consult extensively with stakeholders before design features are settled. The reform is aimed to be broadly revenue neutral over the medium term, with a phased reduction in business tax rates compensated by a broadened direct and indirect tax base, including through the elimination of exemptions. The reform has three pillars:

- Broadening the **business tax base** by removing exemptions and sectoral preferences (tourism and fishing), eliminating thresholds for corporations and reducing the threshold for noncorporate entities, addressing accelerated capital depreciation, introducing a thin capitalization norms. Business tax rates will be lowered in steps from 2010 through to 2012 to promote competitiveness and achieve harmonization across sectors. The revised Business Tax Act will be introduced with the 2010 Budget and will come into effect on January 1, 2010.
- A withholding-based **personal income tax** (PIT) on domestic sourced revenue for nationals and resident expatriates will also be introduced with the 2010 Budget, replacing the social security contribution from July 1, 2010. This will broaden the income tax base from withholding on wages to include domestic-sourced income, dividends, and some fringe benefits, not captured under the Business Tax Act. The new PIT will also include a rebate for low income earners.
- Introduction of a single rate **VAT** from January 1, 2012, replacing the current multiple rate GST, broadening the indirect tax base and improving both the efficiency of the indirect tax system and external competitiveness. Important steps in this direction will be taken in the 2010 Budget, including expanding the GST base to a broader range of services and the reduction of cascading effects through the levying of GST once—on either imports or sales.

We aim to have a level playing field on taxation in place by January 2012. The granting of new tax incentives under the Tourism Incentive Act, Agriculture and Fisheries Incentive Act, and the Investment Promotion Act will be strictly limited and any new incentives, or extensions to existing ones, granted after October 1, 2009 will lapse on December 31, 2011. In addition, we are in discussions with established operators under these incentive regimes with a view to bringing them into the new tax regime as soon as possible. It is our aim to phase out these concessions by January 2012, concurrent with the introduction of the VAT.

24. We are also modernizing and reinforcing revenue administration in line with recommendations by the IMF's Fiscal Affairs Department.

Action	Timing
Revenue Administration-General	
SRC Governance Reform: <ul style="list-style-type: none"> • Implement an integrated function based structure for domestic tax operations, with an audit group that is specifically focused on large taxpayers. • Create a dedicated project reform office. • Establish corporate-level staff affairs and internal audit units. 	December 2009
<ul style="list-style-type: none"> • Introduce new Revenue Administration and Business Number Acts. 	January 2010
Customs Administration	
<ul style="list-style-type: none"> • Develop a customs reform strategy and implementation plan. 	March 2010
<ul style="list-style-type: none"> • Migrate to ASYCUDA World. 	2 nd half of 2010
<ul style="list-style-type: none"> • Create two new headquarters-type units in the customs division for program development/planning and enforcement/investigations. 	March 2010
<ul style="list-style-type: none"> • Introduce new Customs Management Act, including HS codes. 	June 2010
<ul style="list-style-type: none"> • Develop trade administration expertise and develop a WCO strategy. 	2010

Tax policy

Action	Timing
Business Tax	
• Introduce new Business Tax Act	January 2010
• Eliminate retail shops from the International Trade Zone (ITZ)	July 2010
Personal Income Tax (Pay as you go withholding)	
• Introduce new PIT legislation to replace Social Security contribution.	July 2010
Indirect taxation	
• Extend full GST to all consultancy and corporate service provider service fees.	January 2010
• Reintroduce phased rise in GST on tourism to 15% with initial rise to 12%	November 2010
• Reduce cascading by eliminating GST on imports for all business that are liable for GST on their sales	January 2010
• Eliminate the retail mark-up to calculate the GST and raise rates to 15%	January 2010
Trade Taxes and Excises	
• Launch an excise regime to identically tax imported and domestically produced excisable commodities.	July 2010
• Partial conversion of trade taxes on petroleum, cigarettes, and alcohol to excise duties consistent with commitments under the COMESA.	January 2010
• Extend partial excises on petroleum to PUC and on domestic aviation fuel	January 2010
• Reduce by one-half rebates on fuel, except for registered artisanal fishermen.	January 2010

Public financial management and expenditure reform

25. **We will continue to strengthen the public financial management framework.** Modernizing and strengthening the treasury function will be important to consolidate and optimize the use of government cash balances and improve oversight by the Ministry of Finance of spending units. The introduction of a Treasury Single Account represents a major step forward in our capacity to both monitor and control public expenditure and manage the government's cash balances, with related benefits to the central bank's liquidity management operations. This measure has also revealed the need for a new chart of accounts, which we are aiming to introduce with the 2011 Budget.

26. **We will implement expenditure rationalization measures recommended in the World Bank's Public Expenditure Review (PER), starting in 2010.** In 2009 government employment was reduced by some 2,500 employees (about 15 per cent of the public sector workforce) through a voluntary departure and early retirement scheme. We are now in the process of articulating strategic plans for each government sector, initially focusing on health and education, which will inform further efforts to improve the efficiency of government

service provision. Based on the findings of a high-level government task force, the functions of the civil service are being progressively streamlined with a view to eliminating inefficiencies and duplication, overstaffing in ministries and public entities, and outsourcing ancillary services to the private sector. Initial measures in this regard are the outsourcing of 650 noncore support staff, the removal of vacant posts from the government payroll and a targeted voluntary departure scheme for the security forces. Public sector wage policy is also being reformed through the introduction of a new wage grid that will consolidate allowances, establish a clearer link between remuneration and performance, realigning incentives, while containing growth in the overall public sector wage bill.

27. **Our social safety net will continue to strike a balance between targeted income support and retaining incentives to work.** Following the elimination of universal subsidies in 2008, the government introduced a means-tested social safety net to ensure that low-income households are able to meet a basic standard of living. Reflecting the new targeted approach to social assistance, we are preparing a merger of Social Security Fund administration into the Social Welfare Agency by July 1, 2010 with the view to securing administrative efficiencies and savings. We are also working, with World Bank assistance, to fine-tune the targeting of our social safety net and to establish linkages to the minimum wage so as to preserve the incentive to work. We are also expanding training programs for the unemployed and those exiting the public service through the voluntary departure scheme to ensure that any period of unemployment is transitory.

28. **We will also improve transparency and strengthen institutional capacity in the area of fishing licenses, recognizing the importance of this sector to our economy.** In the interests of transparency and public accountability, we will start to disclose the details of all fishing license agreements in 2010. Commensurately, we will work with the World Bank to build an economic and financial model to support more informed fishing licensing and natural resource management policies.

Action	Timing
<ul style="list-style-type: none"> • Introduce a new public sector wage grid. 	January 2010
<ul style="list-style-type: none"> • Fine-tune targeting of social safety net with World Bank assistance. 	2010
<ul style="list-style-type: none"> • Complete the merger of the administrations of Social Security Fund into the Social Welfare Agency. 	July 2010
<ul style="list-style-type: none"> • Systematic disclosure of the fishing license fees, details of all fishing agreements and payments, industry related agreements signed by government and fish catch statistics. 	March 2010
<ul style="list-style-type: none"> • Develop an economic and financial model, with World Bank assistance, of the fisheries to support more informed licensing and natural resource management policies 	2010
<ul style="list-style-type: none"> • Reform the Pension Fund funding formula with the assistance of the World Bank to link with wage levels and provide adequate and sustainable funding. 	2010

Budget preparation and presentation

29. **Our fiscal policy objectives will be supported by strengthened budget processes and improved budget documentation, as recommended by the IMF's Fiscal Affairs Department.** Starting with the 2011 Budget, we will move to a medium-term budgeting framework, presenting the government's fiscal and economic projections over a three-year period. The 2011 Budget process will commence in March 2010 with Cabinet's discussion of a budget strategy document, setting the fiscal context and establishing the government's priorities for the budget. Ministries and other budget dependent entities will then submit their recurrent and capital expenditure proposals to the Ministry of Finance using a standard template that will require detailed costings to be produced over the three-year budget estimates period. The Ministry of Finance's capacity to scrutinize these expenditure proposals will also be enhanced through increased resourcing, the introduction of formal expenditure review procedures and detailed reconciliation of budget estimates with quarterly and year-end outcomes. The recently created financial analysis unit at the SRC will be

Action	Timing
Budget	
<ul style="list-style-type: none"> Extend budget coverage for 2010 to full presentation of revenues, expenditure and financing, and include discussion of macroeconomic assumptions and objectives, fiscal targets and objectives, and an annual borrowing plan, supported by a medium-term debt strategy. 	December 2009
<ul style="list-style-type: none"> Include a full break down of the revenue and expenditures of budget dependent agencies as an annex to the 2010 Budget tables 	December 2009
<ul style="list-style-type: none"> Determine budget treatment of all budget-dependent agencies for 2011 budget 	June 2010
<ul style="list-style-type: none"> Build capacity in the Ministry of Finance to analyse expenditure proposals 	2010–11
<ul style="list-style-type: none"> Transfer financial analysis unit from SRC to Ministry of Finance 	June 2010
<ul style="list-style-type: none"> Cabinet approval of 2011 Budget strategy. 	June 2010
<ul style="list-style-type: none"> The Ministry of Finance to circulate a standard template requiring all ministries and budget dependent bodies to submit an analysis of mid-year expenditure outcomes relative to budget and updated forecasts. 	July 2010
<ul style="list-style-type: none"> Introduce budget submission protocols and procedures for spending ministries and budget dependent agencies for the 2011 budget 	July 2010
<ul style="list-style-type: none"> Produce a consolidated fiscal table for general government, incorporating all budget dependent agencies. 	June 2010
<ul style="list-style-type: none"> Adopt a new chart of accounts for the 2011 budget 	November 2010
<ul style="list-style-type: none"> Revise the Financial Instructions and Accounting Manual 	March 2011
<ul style="list-style-type: none"> Introduce a new Public Finance Law 	September 2011

transferred to the Ministry of Finance in 2010 and we will work to increase its capacity.

30. **We are also working towards a more complete presentation of the budget for 2010.** We will publish a full breakdown of the revenue and expenditures of budget dependent agencies as an annex to the 2010 Budget tables, increasing the transparency of the government's financial commitments. We will determine the budget treatment of all other budget-dependent agencies—moving from reduced form to full presentation in the fiscal tables where applicable—for the 2010 Mid-Year Budget Review. We will then prepare consolidated general government accounts for the 2011 Budget.

B. Public Enterprise Reform

31. **The government has adopted a public enterprise reform strategy aimed at making the sector more efficient, transparent and accountable.** It includes a detailed work plan for the new Public Enterprise Monitoring Division (PEMD) directed at reinforcing the monitoring and control of public enterprises, strengthening governance, reducing dependence on public funding and minimizing financial risks to the state. The legal basis for this work was established with the recent approval of the Public Enterprise Monitoring and Control Act (the Act) by the National Assembly, mandating strengthened reporting arrangements for public enterprises and setting uniform governance rules (e.g. appointment of the Chief Executive Officer, establishment of the Board of Directors and the role of supervisory Ministries). The Act also requires each public enterprise to prepare a statement of corporate intent to ensure that the objectives of Management, the Board of Directors and the government as shareholder are in full alignment. Performance targets will also be established, where possible, against which the public enterprise will be assessed.

32. **We are also taking steps towards further rationalization of public sector ownership.** The government has privatized a number of state-owned enterprises over the last two years, but there is scope to go further. The Public Enterprise Monitoring Division is finalizing strategic assessments for each public entity—drawing on recently concluded external financial audits and management audits—evaluating the case for public ownership and making recommendations to the government. We have also tendered for expert services to conduct an efficiency review and strategic assessment of the options for the future of the national airline and its ancillary services.

33. **The government, together with the CBS, is developing an exit and consolidation strategy for publicly-owned financial institutions.** Privatization of Seychelles Savings Bank and Nouvobanq would bring new technology, strengthen management and fresh capital to our banking system, stimulate competition and enhance the quality of bank services. The process will commence in December 2009 with the contracting of specialist privatization expertise through an open international tender with the objective of bringing both institutions to the market before end-September 2010, market conditions permitting. We have sought the assistance of the FIRST initiative to assess the government's strategic options with regard to three nondeposit taking institutions – the Development Bank of Seychelles, Housing Finance

Company, and the Concessional Credit Agency with a view to their consolidation and/or privatization. The CBS and PEMD have already started to lay the groundwork for this assessment.

Action	Timing
<ul style="list-style-type: none"> • Cabinet approval of a public enterprise reform strategy and work plan for the PEMD 	December 2009
<ul style="list-style-type: none"> • Begin establishing performance benchmarks for public enterprises 	December 2009
<ul style="list-style-type: none"> • Engage IFC or launch a tender for an advisor for the privatization of Nouvobanq and Seychelles Savings Bank 	December 2009
<ul style="list-style-type: none"> • Prepare a strategic assessment and reform action plan for each major public enterprise. 	2010–11
<ul style="list-style-type: none"> • Elaborate strategy to consolidate and/or privatize the Development Bank of Seychelles, Housing Finance Company, and the Concessional Credit Agency. 	2010
<ul style="list-style-type: none"> • Air Seychelles: 	
<ul style="list-style-type: none"> • Implement management audit action plan 	November 2009
<ul style="list-style-type: none"> • Launch tender for strategic options assessment and efficiency review 	November 2009
<ul style="list-style-type: none"> • Adopt an action plan to implement the recommendations of the strategic assessment and efficiency review 	June 2010
<ul style="list-style-type: none"> • Complete management audits of additional public entities: <ul style="list-style-type: none"> • Seychelles Tourism Board (STB) • Seychelles Fishing Authority (SFA) • National Arts Council (NAC) • Seychelles Trading Company (STC) • Seychelles Civil Aviation Authority (SCAA) • Seychelles International Business Authority (SIBA) • Nouvobanq • Seychelles Savings Bank (SSB) • Development Bank of Seychelles (DBS) 	2010
<ul style="list-style-type: none"> • Formalize all government loans to public entities 	January 2010

C. Public Debt Restructuring and Management Strategy

34. **We are committed to continuing our good faith efforts to achieve a comprehensive public external debt restructuring, consistent with our medium-term payments capacity and the Fund’s lending into arrears policy. We will ensure**

information transparency, inter-creditor equity, and dialogue with all creditor groups. As was recognized by Paris Club creditors, immediate and sizable cash flow relief in the short- to medium-term, and a sustained reduction of our debt service burden are necessary. This needs to be supplemented by significant balance of payments support from our international partners.

35. **The principal objective of our medium-term debt management strategy is to place public debt on a sustainable path.** The strategy approved by Cabinet in November is a commitment to achieving this through the pursuit of prudent fiscal and monetary policies and securing a restructuring of public external debt that is consistent with Seychelles' limited payments capacity. We will also ensure that the government's financing needs and payment obligations are met on a timely basis, at the lowest possible cost consistent with a prudent degree of risk. We will update our debt management strategy annually, or following major events that impact public debt, notably after the debt restructuring is completed. We will also implement the annual borrowing plan for 2010 as approved with the 2010 Budget.

36. **An updated debt sustainability analysis (DSA) produced by IMF staff indicates that our medium-term fiscal targets and the securing of public external debt restructuring will place our external debt position on the path to sustainability.** However, bound tests show that Seychelles will remain highly vulnerable to shocks and demonstrate the importance of adhering to the fiscal path defined by our macroeconomic framework.

D. Foreign Trade Regime

37. **We intend to implement the COMESA common external tariff within the 5 year period from our admission this year (2013), as per our market access offer made under the interim EPA signed in August 2009.** We have also reactivated our application to join the WTO and are actively pursuing discussions to that end.

E. Monetary, Exchange Rate, and Financial Sector Policies

38. **Price stability will remain the primary objective of monetary policy.** Our success in containing inflation over the past year and significant appreciation of the rupee provided scope to loosen monetary policy in the third quarter of 2009 and raise the reserve money target for December 2009. We are monitoring credit and price developments closely and stand ready to tighten monetary policy should inflationary pressures re-emerge. In line with our policy to abolish all direct monetary instruments, we will continue to gradually reduce the reserve requirement as conditions permit.

39. **Monetary policy will continue to be based on reserve money targeting through the use of indirect instruments.** The CBS has recently added repurchase agreements (repos) and credit auction arrangements (CAA) to its range of monetary instruments. Beginning in 2010, we will introduce a Standing Deposit Facility (SDF) to complement the current

overnight credit facility. Once this is in place, the CBS will use repos to guide short-term interest rates. In addition, foreign exchange swaps and forwards will also be put in place to diversify and further deepen the foreign exchange market.

40. **Development of money markets is an important priority.** 91-day T-bills have been established as the benchmark reference rate for the pricing of securities. However, there is no secondary market and the primary market remains shallow. Direct nonbank participation in Treasury bill auctions will continue until the infrastructure for a properly functioning secondary market is in place. Once this is achieved, we will introduce a primary dealer system whereby participation in Treasury bill auctions will be restricted to banks, who will bid on their own behalf and on behalf of their customers.

41. **Coordination between monetary and fiscal policy will remain key to an efficient liquidity management framework.** To this end, we will continue to make extensive use of the recently established liquidity forecasting and reserve money programming framework. The CBS and Ministry of Finance will work closely on the T-bill issuance profile—and subsequent communication to market participants—to promote the smooth functioning of the market. The CBS will also formalize the arrangements for its use of government securities as a monetary policy instrument through a memorandum of understanding with the Ministry of Finance.

42. **We remain committed to a floating exchange rate regime, which has served Seychelles well during the initial phase of our economic reforms.** The CBS will only intervene in the foreign exchange market to smooth out excessive volatility and ensure orderly market conditions. The establishment of the foreign exchange interbank market has provided a platform for a more efficient allocation of foreign currency among banks. To date, institutional factors coupled with market conditions, notably a surplus of foreign exchange in the system, have held back the efficient functioning of the interbank market. Therefore, the CBS will continue to work closely with banks, and make use of technical assistance from the IMF, to improve the efficiency of the interbank foreign exchange market.

Financial sector supervision and development

43. **The CBS will continue to strengthen the supervision and regulation of the financial sector.** The decision of the government to transfer supervision of state-owned nonbank financial institutions to the CBS in late 2009 will allow for a more effective oversight of these institutions. During 2010, we will continue to implement our 18-month action plan for strengthening risk-based supervision. We intend to increase the minimum paid-up capital requirement for holders of a domestic banking license and will promote the use of the net tangible capital ratio as an added measure of capital adequacy. We will seek technical assistance from the IMF to further refine prudential regulations and build domestic supervisory capacity. One of our key objectives is to enhance trust of the public in the banking system and to this end we are considering the possibility of introducing a deposit insurance scheme in 2011/12 and will study its feasibility and optimal operational modalities.

We also intend to develop guidelines for a crisis preparedness program for the banking system that could be extended to nonbank financial institutions and other financial intermediaries as warranted.

44. **We will intensify our efforts to promote transparency in our offshore financial sector through enhanced coordination between the Seychelles International Business Authority, which supervises the offshore sector, the CBS, and the Financial Intelligence Unit.** Furthermore, we will continue to co-operate with international bodies like OECD and the FATF and have sought technical assistance from the Fund for a diagnostic assessment of the offshore sector.

45. **The CBS will continue to modernize the national payment system.** Several important steps were taken during 2009, including the establishment of a complete requirements and standards document for electronic funds transfers that replaced the manual settlement system. We intend to introduce an Electronic Clearing House, a National Payment System; a National Clearing and Settlement System Bill; promote the use of plastic cards; and implement a real time gross settlement system in 2010/11.

CBS governance and capitalization

46. **The CBS will press forward with its program of improving internal control and audit systems.** An updated safeguards assessment is required for the EFF. Building on the measures taken in response to the first safeguards assessment, the CBS will implement the recommendations of the updated assessment in 2010–11.

47. **To improve the efficiency of its operations and in line with the modernization of the banking services activities, the CBS is working to introduce a core banking system in 2011.** A complete needs analysis and requirements definition for the CBS Core Banking System has been completed with the assistance of the IMF's Monetary and Capital Markets Department and our external auditors.

48. **The CBS is undercapitalized, which if left unaddressed, could constrain its ability to implement prudent monetary policies.** As prescribed by the CBS Act, our intention was to gradually increase the central bank's capital base through the retention of 50 percent of annual profits until the target level of 10 percent of monetary liabilities is reached (up from 4 percent in 2008). However, significant valuation losses, due to the significant appreciation of the rupee, has eroded CBS's operating profits. If the external auditors determine that capital of the CBS is further impaired following closure of the 2009 annual accounts in early 2010, the government will promptly fully replenish the CBS' capital base, as required by the law, through a direct securitized injection. This would strengthen the balance sheet of the CBS and enhance its portfolio of tradable securities to be used in open market operations.

Action	Timing
• Complete CBS procedures manual	December 2009
• Publish commercial bank supervision report	December 2009
• Gradually raise minimum capital requirements for domestic banks.	2010–11
• Progressively raise capitalization of CBS to full level of 10 percent of monetary liabilities	2010–12
• Introduce an integrated IT-based accounting framework at CBS (core banking system).	September 2010
• Adopt IFRS for 2009 CBS accounts	March 2010
• Present a National Electronic Clearing and Settlement System Bill to the National Assembly	June 2010
• Implementation of the real time gross settlement system.	2010–11
• Introduce a business continuity plan at CBS	September 2010
• Adopt a crisis preparedness plan for financial system	December 2010
• Produce a financial survey encompassing both bank and nonbank financial institutions	September 2010
• Introduce a new methodology for calculating application and annual license fees for domestic and offshore banks	March 2010

F. National Statistics

49. **We are committed to improving the quality, periodicity, and timeliness of macroeconomic statistics.** We are moving to address deficiencies in key macroeconomic data – especially GDP estimates, and external sector statistics –to improve their usefulness for economic analysis and policy formulation. The Ministry of Employment will reinforce their efforts to produce high-frequency labor market data. We are also strengthening the National Statistics Bureau (NSB) and will implement recommendations of the management audit by end-2009. We have requested technical assistance from the IMF Statistics Department (on fiscal accounts) and from the World Bank (to strengthen the NSB). We will bring Seychelles into line with international best practice, by aiming to implement the IMF's Special Data Dissemination Standard (SDDS) and the Balance of Payments and International Investment Position Manual 6. We will set up a central coordination unit at the NSB that acts as a databank and a hub for data distribution, and monitors the timeliness of submission of the data by various agencies.

Action	Timing
• Adopt a strategic plan to upgrade national statistics	April 2010
• Implement Balance of Payments and International Investment Position Manual 6	2011
• Publish General government fiscal statistics	April 2010
• Implement SDDS	2011

IV. PROGRAM FINANCING

50. **For the remainder of 2009, the external nonproject financing requirement will be covered by** disbursements from the IMF under the SBA (25 percent of quota; SDR 2.2 million) and under the prospective EFF (10 percent of quota; SDR 0.88 million); from the World Bank and African Development Bank development policy loans (US\$19 million); from the EU Vulnerability Flex (€8 million); and from external debt relief (US\$83 million, including on the US\$55 million in arrears accumulated in the first three quarters). For 2010, a financing gap of US\$68 million is expected to be closed by debt relief under the second tranche of the Paris Club agreement; the restructuring of the remainder of public external debt, notably with commercial creditors and non-Paris Club creditors; and disbursements under the EFF. For 2011–12, the financing gaps will be closed by external debt relief and disbursements under the EFF. We have also assumed a follow-up operation by the World Bank at the conclusion of the current Development Policy Loan.

V. PROGRAM MONITORING

51. **The EFF-supported program will be monitored by semi-annual program reviews, with quarterly quantitative performance criteria and disbursements.** The quarterly quantitative performance criteria (QPCs) for end 2009 and for 2010 are shown in Table 4. The structural benchmarks for end-2009 and 2010 are shown in Table 3. The non zero ceilings on the contracting or guaranteeing of external debt are to allow for budgeted public project finance and program support from multilateral institutions exclusively.

52. **The completion of the first review under the EFF will be based on meeting the QPCs at end-March 2010.** The first review will focus on further strengthening operations at the CBS, reinforcing public financial management, bolstering the financial system, progress on normalizing relations with external creditors, implementing the tax reform, and the stance of fiscal policy. The first program review is expected to be completed by late June 2010. The second program review will be based on meeting the end-September 2010 QPCs and is scheduled to be completed by end-December 2010. It will focus on the 2011 Budget, progress in implementing the tax reform, and in strengthening public financial management. Quarterly financing assurance reviews will continue as long as public debt arrears remain outstanding.

53. **The attached Technical Memorandum of Understanding (TMU) defines the quantitative performance criteria, indicative targets and adjusters under the program.** Seychelles will avoid introducing new exchange restrictions, multiple currency practices, or bilateral payments agreements in contradiction with Article VIII of the IMF's Articles of Agreement and imposing any import restrictions for balance of payments reasons. We stand ready to adopt any additional measures, in consultation with IMF staff, which may become necessary to ensure program success.

Table 1. Seychelles: Quantitative Performance Criteria Under the Stand-By Arrangement, 2009
(Millions of Seychelles rupees; end-of-period)

	2009											
	March			June			September			December		
	EBS/09/32	Adjusted	Actual	EBS/09/92	Adjusted	Actual	EBS/09/92	Adjusted	Prel.	EBS/09/92	Adjusted	Projected
Performance criteria												
Net international reserves of the CBS, millions of U.S. dollars (floor) ¹	20	25	76	70	66	81	83	60	117	94	85	130
Reserve money (ceiling)	1,146		1,051	1,266		1,119	1,311		1,169	1,351		1,480
Primary balance of the consolidated government (cumulative floor) ^{2,3,4}	73	173	678	858	849	995	1,006	1,022	1,381	1,173	1,302	1,375
The contracting or guaranteeing of new external debt by the public sector (Millions of U.S. dollars; cumulative ceiling) ²	10	...	0	10	...	0	34	...	0	39	...	24
The contracting or guaranteeing of new short-term external debt by the public sector (Millions of U.S. dollars; cumulative ceiling) ²	0.0	...	0.0	0.0	...	0.0	0.0	...	0.0	0.0	...	0.0
The accumulation of external payments arrears by the public sector (ceiling) ⁵	0.0	...	0.0	0.0	...	0.0	0.0	...	0.0	0.0	...	0.0
The accumulation of domestic payment arrears by the public sector (ceiling)	0.0	...	0.0	0.0	...	0.0	0.0	...	0.0	0.0	...	0.0
Memorandum items:												
External non project financing (millions of U.S. dollars; cumulative) ²	-10.0	-5.3	-5.3	-26.0	...	-29.5	-7.3	...	-30.8	-8.9	...	-17.2
Program financing support ²	0.0	0.0	0.0	0.0	...	0.0	19.0	...	0.0	19.0	...	19.6
Cash payments on foreign debt service ²	10.0	5.3	5.3	26.7	...	29.5	28.4	...	30.8	30.4	...	48.1
External budget grants ²		0.0	0.0	0.6	...	0.0	2.1	...	0.0	2.5	...	11.3
Budget contingency ³	100	...	0.0	0.0	...	0.0	50	...	2.8	100	...	100
Program accounting exchange rates												
SR/US\$ (end-of-quarter)	16.00	16.00	16.09	14.65	...	14.65	14.65	...	14.65	14.65	...	14.65
US\$/Euro (end-of-quarter)	1.46	1.46	1.33	1.33	...	1.33	1.33	...	1.33	1.33	...	1.33
US\$/UK pound (end-of-quarter)	1.84	1.84	1.48	1.48	...	1.48	1.48	...	1.48	1.48	...	1.48
US\$/SDR (end-of-quarter)	1.56	1.56	1.50	1.50	...	1.50	1.50	...	1.50	1.50	...	1.50
Reserve requirement (percent of deposits)	13	13	13	13	...	12	12	...	12	12	...	12

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

¹ The floor will be adjusted downwards (upwards) for any shortfall (excess) in external nonproject financial support from that assumed in the program.

² Cumulative flows from the beginning of the calendar year.

³ The floor will be adjusted upwards for any unused amounts of the contingency in the budget for the recapitalization of the banking sector assumed in the program.

Amounts of the contingency in excess of programmed amounts need to be funded within the program limits.

⁴ The floor on the primary fiscal surplus will be adjusted upwards (downwards) by any excess (shortfall) of external budget grants from that assumed in the program.

⁵ The non-accumulation of new external payment arrears constitutes a continuous performance criterion. Excludes arrears for which a rescheduling agreement is sought. Some external arrears were accumulated in December 2008, but cleared before end-December.

⁶ The floor on the primary surplus of the consolidated government will be adjusted upwards by the cumulative amount of the contingency for recapitalizing the state-controlled financial institutions which is not used for that purpose.

Table 2. Seychelles: Principal Reform Measures Implemented

June-October 2009

Action	Timing
<i>Fiscal policy</i>	
Adopted a tax policy strategy with FAD TA	June
Developed corporate governance guidelines for public entities	August
Adopted a single treasury account	September
Introduced legislation to mandate that all revenue collected by the SRC be posted to the Government's consolidated revenue account.	September
<i>Monetary policy</i>	
Made operational new lending facilities to commercial banks	June
Introduced repo and reverse-repo facilities	June
Adopted modernized and strengthened Financial Institutions Act	June
Updated and strengthened credit concentration and connected lending regulations	June
Eliminated the local asset ratio	August
Initiated a measured reduction in reserve requirements	August
Improved liquidity forecasting and strengthened monetary targeting	Ongoing
<i>CBS governance and safeguards</i>	
Launched a tender to upgrade CBS's IT system to introduce an integrated accounting framework	September
<i>Public enterprise reforms</i>	
Completed external audits of the 2008 accounts of seven major public enterprises in accordance with international audit standards	September
Prepared a strategic assessment for each major public enterprise	September
Conducted management audits of major public enterprises	Ongoing
Adopted a Public Enterprise Monitoring and Control Act	September
Established a public enterprise monitoring division in Ministry of Finance	September
<i>Foreign exchange regime and reserves management</i>	
Approved a modernized Foreign Exchange Act	June
Established a Foreign Reserves Management Committee at the CBS	June
Adopted foreign reserves management guidelines	September
<i>Financial sector reforms</i>	
Adopted a modernized and strengthened Financial Institutions Act	June
In consultation with IMF technical experts:	
◦ Introduced documentation on the acquisition of substantial interests	June
◦ Updated credit concentration regulations and connected lending	June
◦ Introduced CBS manual on prompt and corrective actions	September

Table 3. Seychelles: Structural Benchmarks for 2009–10

Measure	Target date	Status
• Introduce a treasury single account.	End-September 2009	Met. The TSA is leveraging progress on PFM.
• Adopt foreign reserves management investment guidelines.	End-September 2009	Met. The CBS Board adopted guidelines on September 25, 2009.
• Adopt Public Enterprise Monitoring and Control act.	End-September 2009	Met. Parliamentary approval secured on September 28, 2009.
• Complete CBS procedures manual (MEFP, ¶46).	End-December 2009	In progress.
• CBS to publish commercial bank supervision report (MEFP, ¶46).	End-December 2009	In progress.
• Amend the Business Tax Act in line with the tax reform strategy (MEFP, ¶22).	End-December 2009	In progress.
• Cabinet approval of customs reform strategy and implementation plan (MEFP, ¶23).	End-March 2010	
• Publish general government fiscal statistics (MEFP, ¶29).	End-April 2010	
• Submit to National Assembly a new customs management act (MEFP, ¶23).	End-June 2010	
• Introduce Personal Income Tax (MEFP, ¶22).	July 1, 2010	
• Introduce budget submissions protocols and procedures (MEFP, ¶28).	End-July 2010	
• Adopt a new chart of account for the 2011 budget (MEFP, ¶29).	End-November 2010	
• Submit to National Assembly a bill creating a national clearing house and settlement system (MEFP, ¶44).	End-December 2010	

Table 4. Seychelles: Quantitative Performance Criteria Under the EFF, December 2009 - December 2010
(Millions of Seychelles rupees; end-of-period)

	2009		2010		
	December	March	June	September	December
	Prog.	Prog.	Prog.	Prog.	Prog.
Performance criteria					
Net international reserves of the CBS, millions of U.S. dollars (floor) ¹	130	133	128	142	168
Reserve money (ceiling)	1,480	1,537	1,592	1,676	1,753
Primary balance of the consolidated government (cumulative floor) ^{2,3}	1,375	261	437	659	761
The contracting or guaranteeing of new external debt by the public sector (Millions of U.S. dollars; cumulative ceiling) ²	39	2	3	13	37
The contracting or guaranteeing of new short-term external debt by the public sector (Millions of U.S. dollars; cumulative ceiling) ²	0.0	0.0	0.0	0.0	0.0
The accumulation of external payments arrears by the public sector (ceiling) ³	0.0	0.0	0.0	0.0	0.0
The accumulation of domestic payment arrears by the public sector (ceiling)	0.0	0.0	0.0	0.0	0.0
Memorandum items:					
External non project financing (millions of U.S. dollars; cumulative) ²	-17.2	1.7	1.8	9.0	31.8
Program financing support	19.6	0.0	0.0	0.0	19.6
Cash payments on foreign debt service	48.1	1.8	5.8	6.9	9.2
External budget grants	11.3	3.5	7.6	15.9	21.4
Program accounting exchange rates					
SR/US\$ (end-of-quarter)	11.00	11.00	11.00	11.00	11.00
US\$/Euro (end-of-quarter)	1.48	1.48	1.48	1.48	1.48
US\$/UK pound (end-of-quarter)	1.65	1.65	1.65	1.65	1.65
US\$/SDR (end-of-quarter)	1.59	1.59	1.59	1.59	1.59

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

¹ The floor will be adjusted downwards (upwards) for any shortfall (excess) in external nonproject financial support from that assumed in the program.

² Cumulative flows from the beginning of the calendar year.

³ The non-accumulation of new external payment arrears constitutes a continuous performance criterion. Excludes arrears for which a rescheduling agreement is sought.

ATTACHMENT 2**SEYCHELLES: TECHNICAL MEMORANDUM OF UNDERSTANDING**

1. This technical memorandum of understanding presents the definitions of variables included in the quantitative performance criteria and indicative targets set out in the memorandum of economic and financial policies (MEFP), the key assumptions, and the reporting requirements of the Government and the Central Bank of Seychelles (CBS) needed to adequately monitor economic and financial developments. The quantitative performance criteria and indicative targets, and the benchmarks for 2009-10 are listed in Tables 1 and 3 of the MEFP, respectively.

I. QUANTITATIVE PERFORMANCE CRITERIA**A. Net International Reserves of the CBS (Floor)****Definition**

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

Calculation method

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

Monitoring and reporting

4. At each program test date (through end-December 2009), the quarterly net international reserves data submitted by the CBS to the IMF will be audited by the CBS external auditors in accordance with International Standards on Auditing, to ensure conformity with the program definition and calculation methods. Subsequent to end-December 2009, quarterly audits will be conducted by the internal audit division. Audit

reports will be submitted to the CBS, with a copy to the IMF, no later than two months after each test date.

Adjusters

5. The floor on the CBS's NIR will be adjusted upward (downward) by the amount by which the external nonproject loans and cash grants exceeds (falls short of) the amounts assumed in the program (MEFP Table 1). The floors will also be adjusted upwards (downwards) by the amount that external debt service payments fall short (exceed) the amounts assumed in the program.

B. Reserve Money (Ceiling)

Definition

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

Monitoring and reporting

7. For each program test date (through end-December 2009), the quarterly reserve money data submitted by the CBS to the IMF will be audited by the CBS' external auditors in accordance with International Standards on Auditing, to ensure conformity with the program definition. Subsequent to end-December 2009, quarterly audits will be conducted by the internal audit division. Audit reports will be submitted to the CBS, with a copy to the IMF, no later than two months after each test date.

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

8. The consolidated government primary balance from above the line on a commitment basis is defined as total consolidated government and social security fund revenues (excluding privatization and long-term lease income receipts) less all noninterest (primary) expenditures of the government and social security fund.

D. Public External Debt (Ceiling)

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

U.S. dollars at program exchange rates. A zero subceiling on short-term external debt applies continuously to the contracting or guaranteeing of short-term external debt by the public sector, with an original maturity of up to and including one year.

10. For the purpose of this performance criterion, the term “debt” has the meaning set forth in point No. 9 of the Executive Board’s Guidelines on Performance Criteria with Respect to Foreign Debt (Decision No. 12274-(00/85)). Debt is understood to mean a current, non contingent liability, created under a contractual arrangement through the provision of value in the form of assets (including currency) or services, and which requires the obligor to make one or more payments in the form of assets (including currency) or services, at some future points in time; these payments will discharge the principal and/or interest liabilities incurred under the contract. The ceiling on contracting official and officially guaranteed external debt includes all form of debt, including:

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

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

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

(iv) Arrears, penalties, and judicially awarded damages arising from the failure to make payment under a contractual obligation that constitutes debt are debt.

E. External Arrears of the Public Sector

11. The nonaccumulation of arrears to external creditors will be a continuous performance criterion under the program. External payments arrears for program monitoring purposes are defined as the amount of external debt service due and not paid within the contractually agreed period, including contractual and late interest. Arrears resulting from the nonpayment of debt service for which a clearance framework has been agreed or a rescheduling agreement is sought are excluded from this definition.

F. Budget Expenditure Arrears

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

II. DATA AND INFORMATION

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

The CBS will report

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

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

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

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

The Ministry of Finance will report

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

- Consolidated government operations on a commitment basis and cash basis in the IMF-supported program format.
- The detailed revenues and expenditures of the central government and social security fund.
- Monthly accounts of the public nonbank financial institutions.

- Import and export data from the customs department.
- Monthly public debt report.

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.