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INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

PROGRAM DOCUMENT

FOR A PROPOSED LOAN

IN THE AMOUNT OF US\$5 MILLION

TO THE

REPUBLIC OF SEYCHELLES

FOR THE

SUSTAINING REFORMS FOR INCLUSIVE GROWTH
DEVELOPMENT POLICY LOAN

SEPTEMBER 25, 2015

Macroeconomic and Fiscal Management Global Practice
Africa Region

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REPUBLIC OF SEYCHELLES

CURRENCY EQUIVALENTS

CURRENCY UNIT: SEYCHELLES RUPEE (SR)

US\$1 = SR 13.28 (JULY 8, 2015)

WEIGHTS AND MEASURES

METRIC SYSTEM

FISCAL YEAR

JANUARY 1 – DECEMBER 31

ABBREVIATIONS AND ACRONYMS

AfDB	African Development Bank
AIDS	Acquired immune deficiency syndrome
ASP	Agency for Social Protection
CBS	Central Bank of Seychelles
CIS	Credit Information System
CPS	Country Partnership Strategy
DBS	Development Bank of Seychelles
DPL	Development Policy Loan
EEZ	Exclusive Economic Zone
EFF	Extended Fund Facility
EITI	Extractive Industries Transparency Initiative
EU	European Union
FDI	Foreign Direct Investment
FY	Fiscal year
GDP	Gross Domestic Product
GoS	Government of Seychelles
GRS	Grievance Redress Service
HCA	Health Care Agency
HIV	Human immunodeficiency virus
IBRD	Bank International Bank for Reconstruction and Development
IFC	International Finance Corporation
IGCSE	International General Certificate of Secondary Education
IMF	International Monetary Fund
IPSAS	International Public Sector Accounting Standards
IT	Information technology
M&E	Monitoring and evaluation
MIS	Management Information System
MoE	Ministry of Education
MoFTBE	Ministry of Finance, Trade, and the Blue Economy
MoH	Ministry of Health

MSE	Micro and Small Enterprise
MTNDS	Medium Term National Development Strategy
MTS	Medium-term Education Sector Strategy
NDS	National Development Strategy
OCR	Office of the Company Registrar
PEFA	Public Expenditure and Financial Accountability
PEMC	Public Enterprise Monitoring Commission
PER	Public Expenditure Review
PFM	Public Financial Management
PHA	Public Health Authority
PIM	Public Investment Management
PISA	Program for International Student Assessment
PPP	Public Private Partnership
PPBB	Programme Performance Based Budgeting
PSIP	Public Sector Investment Plan
PUC	Public Utilities Corporation
RAS	Reimbursable Advisory Service
SACMEQ	Southern and Eastern Africa Consortium for Monitoring Educational Quality
SADC	Southern African Development Community
SDR	Special Drawing Rights
SOE	State Owned Enterprises
SORT	Systematic Operational Risks-rating Tool
SPF	Seychelles Pension Fund
SR	Seychelles Rupee
SSI	<i>Société Seychelloise d'Investissement</i> (Seychelles Investment Society)
STC	Seychelles Trading Company
SWA	Social Welfare Assistance
UNDP	United Nations Development Program
US\$	United States Dollar
VAT	Value added tax
WTO	World Trade Organization

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REPUBLIC OF SEYCHELLES
SUSTAINING REFORMS FOR INCLUSIVE GROWTH DEVELOPMENT POLICY
LOAN

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SUMMARY OF PROPOSED LOAN AND PROGRAM
REPUBLIC OF SEYCHELLES
SUSTAINING REFORMS FOR INCLUSIVE GROWTH DEVELOPMENT POLICY LOAN

Borrower	Republic of Seychelles
Implementing Agency	Ministry of Finance, Trade, and the Blue Economy
Financing Data	Terms: A IBRD Fixed Spread Loan with a commitment-linked repayment schedule, a final maturity of 27 years including a grace period of 12 years, and level principal repayments. Amount: US\$5 million.
Operation Type	Stand-alone Development Policy Loan (DPL).
Pillars of the Operation and Program Development Objective(s)	The development objective of this DPL is to raise efficiency of public expenditure and improve the business environment. To achieve these objectives, this operation supports actions that will: (i) raise efficiency of public expenditure; (ii) facilitate access to credit; and (iii) improve public investment.
Result Indicators	<ul style="list-style-type: none"> • Reduce total spending on social assistance as percent of GDP. • Reduce spending on sickness benefit. • Increase percent of health budget allocated to prevention and promotion services. • Reduce teacher attrition as percent of total number of teachers • Increase number of credit reports issued per day • Increase number of lenders connected to collateral registry • Increase number of projects above 10 million rupees approved by the Development Committee • Increase number of SOEs under SSI's purview which have reached their financial and non-financial performance indicators as agreed between SSI, PEMC and the SOE. <p>The details on the established baselines and targets for the results indicators can be found in the results matrix annex.</p>
Overall Risk Rating	Low.
Climate and disaster risks	There are no short and long term climate and disaster risks relevant to the operation (as identified as part of the SORT environmental and social risk rating).
Operation ID	P153269.

IBRD PROGRAM DOCUMENT FOR A PROPOSED LOAN TO THE REPUBLIC OF SEYCHELLES

1. INTRODUCTION AND COUNTRY CONTEXT

1. **This program document proposes a Development Policy Loan (DPL) to the Republic of Seychelles that sustains reforms for inclusive growth.** The proposed operation is a stand-alone Development Policy Loan. The development objective of this DPL is to raise efficiency of public expenditure and improve the business environment. To achieve these objectives, this operation supports actions that will: (i) raise efficiency of public expenditure; (ii) facilitate access to credit; and (iii) improve public investment.

2. **Seychelles, a small island-state economy, has graduated to high income status this year.** With a gross national income per capita of US\$13,990 in 2014, the country has been recently graduated to high income status. It has an estimated population of 91,530 (2014), comprises 115 tropical islands spread over 45,166 hectares in the Indian Ocean, and has an exclusive economic zone (EEZ) of almost 1.4 million square kilometers in one of the world's major tuna fishing grounds. Tourism and fishing/fish processing are the major pillars of the economy, contributing 25 percent and 8 percent of gross domestic product (GDP) respectively.

3. **Seychelles has had a good performance in reducing poverty.** Seychelles has better social indicators than comparable small island countries. It has already achieved most of the Millennium Development Goals, especially for education, health, poverty eradication, and the environment.¹ The country has virtually eliminated extreme poverty and only less than 2 percent of households consumed less than US\$2 per day in 2006. The main challenges relate however to a high income disparity (the Gini coefficient increased from 0.42 to 0.65 between 2000 and 2007) and the challenges that the bottom 40 percent may have to reap the benefits of a country with a high income status, although poverty data is relatively outdated and the large Gini coefficient may stem from methodological issues at the time of calculation.² Key in this process is the need to improve the quality of public services such as education and ensure that vital services such as primary health care remain sustainable.

4. **Seychelles enjoys a stable political system and has made significant progress in improving public sector governance.** In the last election in May 2011, the incumbent, Mr. James Michel, was elected for another five-year term.³ Since 2008, the government has implemented a series of reforms to address public sector governance issues, which improved a number of governance indicators.⁴ Legislative and presidential elections are foreseen in 2016.

¹ Gross enrollment in primary and secondary education is close to 100 percent. The country's life expectancy at birth is 73 years, compared to 68.3 for Fiji and 70.7 for Cabo Verde.

² The Bank is working with the National Bureau of Statistics of Seychelles to analyze the recently finalized household survey to update poverty and inequality figures, which are expected to be published in 2015.

³ Following the September 2011 Parliamentary elections, the ruling party holds all but one seat in the National Assembly. The main opposition group boycotted this election, leading to the establishment of the Forum for Electoral Reform led by the Electoral Commission. The commission submitted a reform proposal, which is currently being studied by the authorities.

⁴ Seychelles is ranked 4th in the 2013 Ibrahim Governance indicators of African countries, in line with previous years, but there are a number of governance issues that need addressing. Seychelles is ranked at the 55th percentile on Rule of Law in the 2012 World Bank's Worldwide Governance Indicators. Also, institutional reforms have mainly focused on the supply-side, and strengthening demand side issues, such as social accountability and the role of the media, may significantly improve overall governance. On public sector reform, the government "Public Sector Administration and Reform Strategy" will be an

5. **Significant reforms have helped Seychelles to overcome the 2008 debt crisis.** After high external indebtedness and loss of competitiveness depleted foreign exchange reserves and forced a payment default in 2008, the government of Seychelles (GoS) energetically pursued reforms, with support of the International Monetary Fund (IMF) and World Bank, among others. Its economic restructuring program focused on liberalizing the exchange regime, significantly tightening fiscal policy, and reducing the state's role in the economy to boost private sector development. The public debt portfolio was restructured with the Paris Club and other private creditors. Seychelles managed to secure generous debt relief, which together with fiscal consolidation has put it on a path to fiscal and external sustainability. These positive reforms have facilitated in 2015 the approval by the Paris Club of the partial exchange of Seychelles debt in return for financing a fund for the protection and development of its marine space.

6. **The government aims to maintain solid macroeconomic policies while accelerating reforms to raise investment and promote inclusive economic growth.** A solid macroeconomic framework anchored in the IMF Extended Fund Facility (EFF) program will serve Seychelles to confront the challenges inherent to a small and remote island state that is highly vulnerable to the global economy, especially the predominance of European tourism. The authorities aim now to reorient the reforms to further accelerate economic growth by improving the investment climate to harness private sector growth,⁵ remove infrastructure bottlenecks and raise human capital.

7. **This operation supports government's reforms to accelerate inclusive economic growth.** Since poverty is so low in Seychelles, the operation focus mainly on improving inclusiveness to reduce inequality and the welfare of the bottom 40 percent of the population. First, the operation supports shared prosperity by the adoption of tools to raise the efficiency of public expenditure in human development so that quality and equity of education, health and social protection are improved. Second, reforms supported by this operation aim to facilitate access to credit, which is expected to affect positively Small and Medium Enterprises (SMEs), where presumably many of the poorer Seychellois are employed, as well as to improve the business environment with a positive impact on credit to the population at large. Third, the operation will strengthen institutions to better assess and monitor public investment, both from the public budget and SOEs, in order to provide better infrastructure to businesses and create jobs. Finally, the operation is anchored on strong fiscal discipline, necessary to attain the authorities' goal of reducing the public debt ratio to 50 percent of GDP by 2018, while building resilience to cope with external shocks.

8. **The overall implementation risk is low.** The government has a strong track record in pursuing its reform agenda and tangible results have been achieved in terms of macroeconomic policies and structural reforms. The previous engagement through a DPL series shows the positive impact that technical and financial Bank contributions had to this process. The government has requested preparation of a Systematic Country Diagnostic to inform the adoption of a new partnership with the Bank in FY16. They expect that new operations will be informed by the new partnership and requested to maintain a stand-alone DPL in the meantime

opportunity to implement second-generation reforms, including performance management in the public sector and ensuring effective internal and external public sector accountability.

⁵ Seychelles is ranked 85 in the World Bank's Ease of Doing Business Index for 2015, an improvement from 87 in 2014.

to support the on-going reforms. Acknowledging that elections may slowdown the reform process, the operation focuses on areas where consensus exist and helps to set up key tools that will be required for subsequent reforms to build upon. Other risks, such as the limited institutional capacity within sector ministries, are being overcome with substantial technical assistance, partially financed by the authorities through reimbursable advisory services. The risk that uncertain global developments may threaten Seychelles' macroeconomic stability is mitigated by the means and tools available to the government to cope with external shocks (such as the country's growing external reserves and flexible exchange rate). Furthermore, the reforms supported by this operation are also aimed at increasing Seychelles' economic resilience to cope with external shocks, by raising public sector efficiency and improving public investment. It is important however that the government continues to pursue forcefully reforms to further facilitate private sector led growth less dependent of large-scale FDI in tourism.

2. MACROECONOMIC POLICY FRAMEWORK

2.1 Recent Economic Developments

9. **Economic growth in 2014 decelerated to 3.3 percent, affected by anemic growth in Europe.** Tourism and manufacturing sector grew at a slower pace than anticipated. Tourist arrivals rose by a slim 1 percent despite concerted efforts to diversify markets, and tourism receipts fell by 8 percent due to US dollar appreciation against the Euro and the Seychelles Rupee. The manufacturing sector also performed below par, particularly the fish processing sector, following a significant decline in the international price of raw tuna and appreciation of the US dollar. This external slowdown was partially compensated by stronger domestic demand, associated to the pay rise in the public and private sector in 2014 and the 25 percent expansion of the credit to the private sector during 2014, in part due to a government SME lending guarantee program (Table 1).

10. **Fiscal policy remains anchored in reducing public debt and further reducing external vulnerabilities.** Debt reduction to complement the successful debt restructuring and build resilience continues to be the fiscal anchor. Successful tax reforms have increased efficiency while supporting tax collection and Seychelles' revenue effort compares very favorably with other middle income small states. Public expenditure has been reined in; mainly in the years after the debt restructuring was being implemented. government commitment to debt reduction continues as reflected in the 4.6 percent of GDP primary fiscal surplus in 2014. Revenue collection in 2014 was better than expected associated to growing domestic demand and robust import tax collection. Overall, public expenditure also increased in part due to salary increase granted to civil servants in 2014 and unexpected support to Air Seychelles, although it was partially compensated with a reduction in public investment due to implementation delays. Despite the primary fiscal surplus, debt valuation associated to appreciation of the US dollar, together with the issuance of more debt for monetary purposes, increased the debt to GDP ratio from 64.1 percent in 2013 to 65.3 in 2014.

11. **The current account deficit widened in 2014 putting pressure on the Seychelles rupee.** The current account deficit deteriorated to 21 percent of GDP in 2014 compared to 11.5 percent of GDP in 2013. The economy faced strong balance of payments pressures as tourism revenues, which account for more than two thirds of the country's foreign exchange

receipts, fell by about 8 percent in 2014. In addition, given Seychelles high trade openness, growing domestic demand increased imports by 7 percent in 2014, at a time when exports fell by 2 percent. Yet, Foreign Direct Investment (FDI) that stood at 14 percent of GDP, notably in the tourism and hotel sector, is behind a large part of the import growth and have to a large extent financed the current account deficit, thereby minimizing the impact on external debt.

12. The Central Bank of Seychelles (CBS) tightened monetary policy in the second half of 2014 to curb the inflationary effects of Seychelles Rupee depreciation and contain credit growth. The CBS revised downward its reserve money target and expanded its open market operations with treasury bills, raising interest rates on treasury bills from 3.5 percent (August 2014) to close to 10 percent (April 2015). The Treasury and CBS also agreed to issue medium term treasury bonds representing 4.5 percent of GDP to mop up excess liquidity. The CBS continued to build up international reserves from 3.7 months of imports in 2013 to 4.6 months in 2014, sterilizing them, and helping to resolve the excess liquidity in the financial system that undermined the monetary transmission mechanism. Overall, monetary policy supported inflation containment from 3.4 percent in 2013 to 0.5 percent in end-2014.

13. Despite rapid credit expansion, the financial sector remains strong, albeit with challenges related to high cost and financial inclusion. Overall, the financial system is small and underdeveloped and the ratio of domestic credit to GDP in 2014 is 27.2 percent compared to 24.8 percent in 2013.⁶ Limited access to credit and relatively high lending spreads continue to be serious limitations.⁷ Access is constrained, among other things, by weak capacity in the commercial banking sector to serve SMEs, an area that the Financial Sector Development Implementation Plan, prepared with World Bank support, aims to tackle. The 25 percent growth of credit to the private sector in 2014 has deteriorated some financial sector indicators such as the capital to risk-weighted although it remains well above the minimum adequacy ratio of 12 percent. Overall, the financial sector remains sound and the share of non-performing loans was 8.2 percent, still high but declining. Improvements in the credit information system and collateral registry supported by this operation are expected to improve the quality and price of credit, strengthening the soundness of the financial sector and improving access to credit.

⁶ Compared for instance to 87.8 percent of GDP in Mauritius.

⁷ The lending-deposit rate spread at end-2013 was 9 percent, below Sub-Saharan average of 11 percent but above the middle income group average of 6.3 percent. High lending spreads reflect perceived risks of lending to the private sector and high costs of operations in a small market, as well as limited competition in the banking sector.

Table 1: Selected Economic Indicators, 2013–18

Indicator	2013 Actual	2014 Est.	2015 proj.	2016 proj.	2017 proj.	2018 proj.
<i>National income and prices (annual percent growth)</i>						
Real GDP	6.0	3.3	3.5	3.7	3.6	3.5
Consumer Price Index (end-of-period)	3.4	0.5	4.9	3.8	2.5	3.3
<i>Savings and investment (% GDP)</i>						
Gross national savings	26.5	16.3	18.6	19.4	18.6	18.7
Gross investment	37.9	37.3	33.7	34.1	33.5	32.4
Credit to private sector (% growth)	4.5	25.2	12.4	-	-	-
<i>Government budget (% GDP)</i>						
Total revenues and grants	35.9	35.4	34.2	33.2	33.2	33.2
Tax revenue	31.9	32.4	31.6	31.4	31.4	31.4
Expenditure and net lending	35.9	33.0	33.9	32.2	31.7	31.7
Current expenditure	26.7	26.5	26.8	25.3	24.6	24.6
Wages and salaries	6.6	6.8	5.9	5.3	5.6	5.6
Capital Expenditure	8.9	5.6	6.2	5.4	5.0	5.0
Overall balance, accrual basis	0.0	2.4	0.3	1.2	1.5	1.5
Primary balance, accrual basis	4.6	4.6	3.8	3.8	3.8	3.8
Total external public sector debt (US\$ million)	521	505	531	537	533	541
Total public debt	64.1	65.3	63.7	59.5	54.7	49.9
Total domestic debt	27.2	29.9	25.1	23.0	20.5	17.1
Total external debt	36.9	35.5	38.6	36.5	34.3	32.8
<i>External sector</i>						
Current account balance, including official transfers (% GDP)	-11.5	-21.0	-15.2	-14.6	-15.0	-13.6
Gross official reserves (end of year, US\$ million)	425	463	463	476	505	521
Reserves in terms of months of imports	3.7	4.6	4.3	4.2	4.3	4.2
Tourism earnings (US\$ million)	430	398	380	399	423	448
Exports of Goods and Services (percent of GDP)	85	83	79	78	79	78
Imports of Goods and Services (percent of GDP)	93	98	89	87	88	86
Exchange Rate (SR/USD)-Period average	12.1	14.0	-	-	-	-
FDI, net (US\$ million)	132.6	204.9	148.5	141.2	199.1	174.8
FDI (% GDP)	9.4	14.1	10.8	9.6	12.8	10.6

Source: National Bureau of Statistics, Central Bank of Seychelles, IMF, and staff estimates.

Note: 1/ Includes debt issued by the Ministry of Finance for monetary purposes.

2.2 Macroeconomic Outlook and Debt Sustainability

14. **The economic outlook is broadly positive, although with some downside risks.** Economic growth is forecast to reach 3.5 percent in 2015 and in the medium term supported by continuous recovery in tourism, as the government continues efforts to diversify markets and new hotels become operational. The fish processing sector is also expected to recover in 2015, as ten new units for processing of demersal fish have been completed and the number of vessels has increased from 15 to 25. Inflation is expected to peak at 4.9 percent in 2015 and decline in the medium term as the rupee depreciation passes through and second round effects are expected to be limited.

15. **With limited additional gains expected in tax collection, fiscal policy will need to focus in raising efficiency of public expenditure and create fiscal space for much needed investment.** The primary budget surplus, projected to be around 3.8 percent of GDP in 2015 and in the medium term, is in line with the debt reduction target, and fiscal discipline also supports efforts to rein in domestic demand and ease pressures on the balance of payments⁸ (Table 2). No major changes are projected in tax policy and the fall in total revenue is mainly due to a projected fall in import taxes after 2014 over-performance.⁹ Government aims to increase public investment in 2015 while setting up, with support of this operation, a Development Committee to improve selection and implementation of public projects. Additional measures to contain current expenditure, raise public sector efficiency and create the needed fiscal space for public investment are supported by this operation in some of the main cost drivers of the public budget, including education, health and social protection areas.¹⁰ Key on this process will be to limit fiscal risks associated to SOEs, which in the past proved to require substantial and often unexpected public transfers. This operation continues to reinforce the capacity to monitor SOEs, particularly of the public holding company *Société Seychelloise d'Investissement* (SSI).

⁸ For instance, some government programs to promote access to finance for SMEs have been revised to ensure that imports only cover essential capital goods.

⁹ 2014 was an exceptional year where VAT receipts increased to 9.9 percent of GDP and import related taxes were 2.2 percent of GDP because of an upsurge in aggregate demand with a large import content. However, VAT collection is expected to be lower in 2015 at 9.4 percent of GDP and import taxes are expected to decline to 1.5 percent of GDP

¹⁰ Reduction of the wage bill from 6.8 percent of GDP in 2014 in 2015 to 5.9 of GDP reflects a budget reclassification from salaries to transfers to account for the new autonomous institutions created, mainly in the health sector.

Table 2: Key Fiscal Indicators (Percent of GDP)

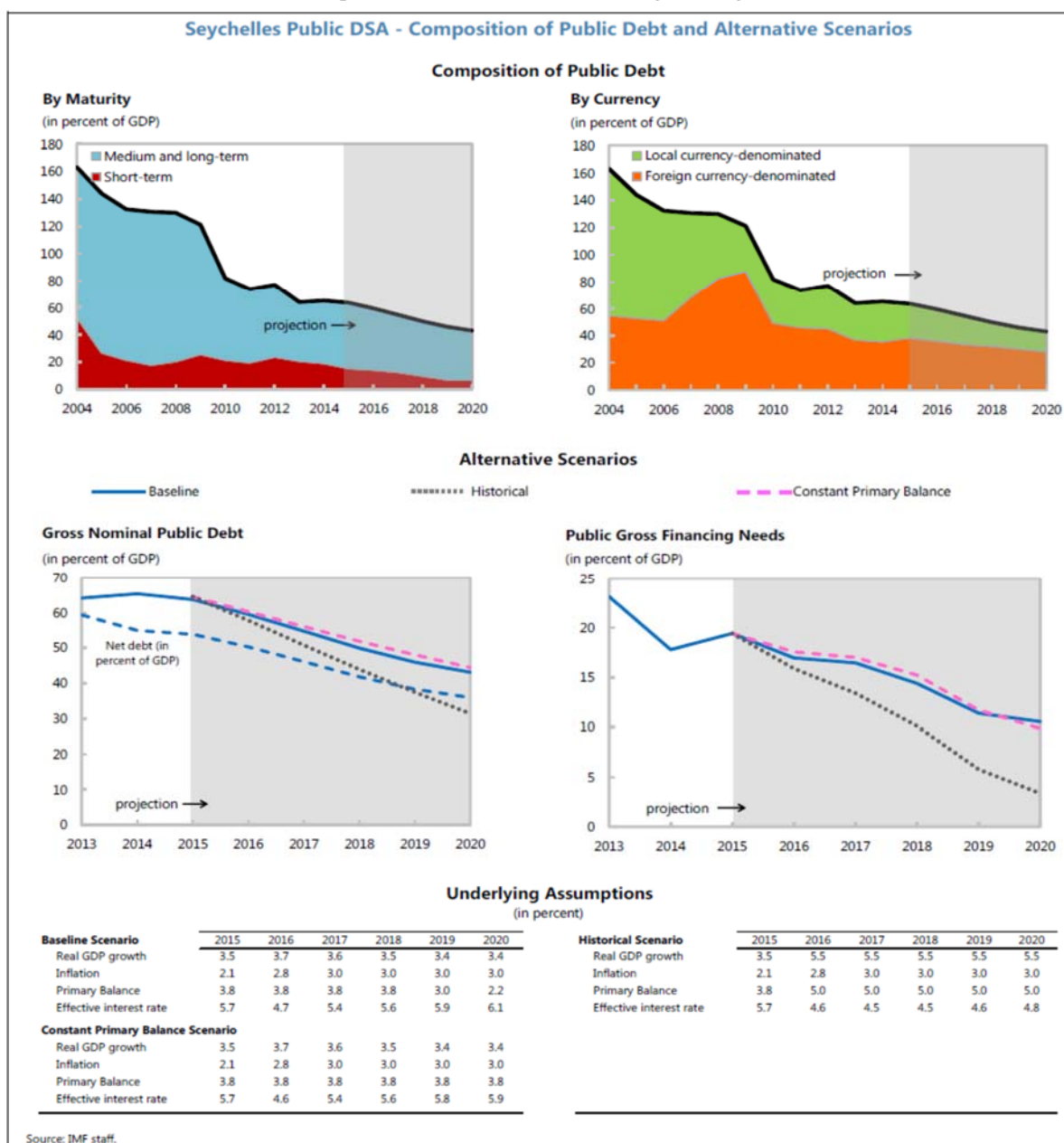
	2013	2014	2015	2016	2017	2018
	Act	Est	Proj	Proj	Proj	Proj
<i>Total Revenue (and grants)</i>	35.9	35.4	34.2	33.4	33.2	33.2
Tax Revenue	31.9	32.4	31.6	31.4	31.6	31.6
Taxes on goods and services	9.5	9.9	9.4	9.5	9.5	9.5
Personal Income Tax	4.4	4.8	4.8	4.8	4.8	4.8
Taxes on international trade	2.4	2.1	1.5	1.4	1.4	1.4
Other taxes	15.6	15.6	15.9	15.7	15.9	15.9
Non-tax revenue	4.4	3.2	3.2	3.2	3.2	3.2
Grants	4.1	3.0	2.5	2.1	1.6	1.6
<i>Total expenditure</i>	35.9	33.0	33.9	32.2	31.7	31.7
<i>Current expenditure</i>	26.7	26.5	26.8	25.3	24.6	24.6
Wages and compensation	6.6	6.8	5.9	5.8	5.6	5.6
Goods and services	7.2	7.1	5.5	5.5	5.6	5.6
Interest payments	4.6	2.2	3.4	2.6	2.4	2.4
Current transfers	8.0	10.2	11.8	11.3	11.4	11.4
<i>Capital expenditure</i>	8.9	5.6	6.2	5.4	5.0	5.0
<i>Overall Balance</i>	0.0	2.4	0.3	1.2	1.5	1.5
Primary balance	4.6	4.6	3.8	3.8	3.8	3.8
General Government Financing						
External (net)	0.7	0.0	1.8	0.1	0.0	0.0
Domestic (net)	-0.7	-2.3	-2.3	-1.3	-1.5	-1.5
of which: privatization	0.3	0.4	0.2	0.0	0.0	0.0

Source: IMF

16. **The ratio of total public debt to GDP is projected to decline to converge to 50 percent of GDP by 2018.** Public debt to GDP is expected to decline from 65.3 percent in 2014 to 63.7 percent of GDP in 2015. Public external debt is expected to be around 39 percent of GDP in 2015. However, significant risks exist given Seychelles high total and external public debt, short term debt profile, and large gross external financing needs. Based on the latest Debt Sustainability Analysis, several individual shocks¹¹ could increase the debt to GDP above the 50 percent goal in 2018 but with a declining trajectory thereafter. Major shocks to the external debt are a broadening current account and depreciation of the Seychelles rupee but both have a declining trajectory (Figure 1). Domestic roll over risks are partially offset by significant government deposits in the amount of Seychelles Rupee 1.4 billion. Also, on-going government efforts to provide more medium term monetary instruments will further reduce this risk while mopping up excess liquidity in the financial market. Also, the impact of the US dollar appreciation in debt dynamics is partially mitigated as around one third of existing debt is Euro and SDR denominated.

¹¹ These shocks include (i) 30 percent real exchange depreciation; and (ii) permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and current account balance.

Figure 1: Debt Sustainability Analysis



17. **Gross external financing needs will remain high, associated to large current account deficit and increasing debt repayments.** The current account deficit is projected to be gradually clawed back from 21 percent of GDP in 2014 to 15.2 percent in 2015 and eventually to 13.6 percent of GDP by 2018 helped by monetary policy tightening and an improvement in the terms of trade. In addition, it is expected that export of tuna will rise by about 2 percent and that tourism earnings will rise by 13 percent from 2014 to 2018, as new hotels come into operation. As a result of increasing debt repayments and income repatriation, gross external financing requirements will be around US\$225 million a year (Table 3). This is expected to be comfortably financed by substantial FDI (around 63 percent of total requirements) and minimum recourse to additional external debt (around 15 percent of total requirements). The flexible exchange rate, which is in line with fundamentals, will provide buffer

against external shocks to the economy, and CBS will continue to build up progressively international reserves, mainly through purchases on the domestic interbank market, albeit at a more moderate pace. International reserves are projected to be around 4.3 months of imports in the medium term.

Table 3: BOP Requirements and Sources (in US\$ million)

	2013	2014	2015	2016	2017	2018
Financing requirements (US\$)	-209	-307	-216	-227	-267	-263
Current Account Deficit	-162	-299	-209	-215	-233	-224
Amortization	-34	-16	-20	-28	-37	-35
Change in reserves	-116	-36	2	-12	-22	-26
Other Financial Outflows	103	44	11	28	25	22
Financing Sources (US\$)	209	307	216	227	267	263
FDI	132	201	149	142	198	175
Portfolio Investments	0	-2	0	0	0	0
Disbursements	24	21	45	34	35	9
Capital Flows	53	87	22	51	34	39

Source: IMF and World Bank calculations

18. **A number of downside risks to the economic outlook remain, which could lead to some departure from these forecasts.** The European recovery is fragile and remains vulnerable moving forward. As a result, the tourism sector may be adversely affected, further reinforced by the instability in the Russian market, which represented around 7 percent of tourist arrivals in 2014. In addition, profit margins in the tourism sector is under pressure as a result of the appreciation of the US dollar vis-à-vis the Euro since hotels in Seychelles derive their revenues from Euro whilst most of their expenses are denominated in US dollars and Seychelles Rupees. On the domestic front, the key downside risk to the economic outlook remains the ability of the government to implement its reform agenda, particularly in areas which most support economic growth in the near-term. Accelerating reforms to raise public sector efficiency and create fiscal space for public investment would have positive impact in economic growth while reinforcing debt consolidation. On the positive side, recent developments such as diminishing oil prices will have positive impact on the balance of payments, partially compensated by the dollar appreciation.

19. **Overall, Seychelles' macroeconomic framework for 2015–16 is adequate for development policy lending.** This assessment is based on the broadly favorable macroeconomic performance during the past years and on policy makers' continued commitment to sound macroeconomic management and progress on structural reforms. While substantial external uncertainty may affect the economy in 2015 and beyond, Seychelles has recently established a track record of quickly responding when confronted with economic adversity. Government growing external reserves, flexible exchange rate, high government deposits and fiscal surplus provide some means to cope with external shocks. Reforms supported by this operation, a parallel AfDB budget support operation, and the IMF EFF are expected to further reduce Seychelles' vulnerabilities and increase its resilience to cope with unexpected shocks.

2.3 IMF RELATIONS

20. **The Bank's program has been closely coordinated with the IMF program since 2008.** Building on the success of its Stand-By Arrangement and the three-year EFF in Seychelles, the IMF approved on June 4, 2014 a new three-year Extended Fund Facility for US\$17.8 million. The aim of the EFF is to reduce public debt to below 50 percent of GDP by 2018, gradually increase external reserves, implement an ambitious structural reform program to foster economic growth, and improve public financial management (PFM) and oversight of SOEs. The EFF and Bank DPL have been closely coordinated to support the overall government reform program, particularly in areas such as SOEs supervision and PFM.

3. THE GOVERNMENT'S PROGRAM

21. **The government's program is spelled out in the Medium-term National Development Strategy 2015-2019.** This operation supports some of the government's main key results areas, particularly: (i) governance (public sector reforms and public finance); (ii) economic development (small and medium enterprises and poverty and inequality); and (iii) social development (education, health and social protection and family preservation).

22. **The government continues its efforts to increase public sector efficiency by improving transparency and governance, including public financial management.** Since 2008, the government has implemented a series of reforms to improve fiscal policy and increase public sector efficiency. It continues to implement a set of reforms aimed at achieving results-based management across government. A new PFM Act was adopted in 2012 and regulations in 2014, introducing Programme Performance Based Budgeting (PPBB), the Medium Term National Development Strategy (MTNDS), Public Investment Programme (PSIP) and Asset Management. The government has also introduced a new Chart of Accounts that features a functional classification to facilitate fiscal reporting in compliance with the 2001 Government Finance Statistics Manual.¹² Government aims now to further improve the Public Investment Management system and to roll out PPBB in whole of government. The reforms also address public sector governance issues, including a review of the role of government in commercial activities, as well as improving State Owned Enterprises (SOEs) management. The adoption of the Public Enterprise Monitoring Commission (PEMC) Act in 2013 created the PEMC as an independent institution in charge of monitoring all public enterprises. Government aims now to continue strengthening PEMC capacity, efficiency in SOEs and reinforcing SSI's governance structure to better supervise government participation in commercial SOEs.

23. **The government is improving the business environment to enhance private sector-led growth.** GoS aims at reducing red tape, streamlining business processes, eliminating unnecessary procedures, and increasingly making use of IT systems to reduce processing time. As such, the government has eliminated a number of export permits, introduced an online system for applying for trade licenses, improved the framework for foreclosures, streamlined the procedures for business entry and for obtaining construction permits, and moved toward implementing online systems for registering property titles and making tax payments. The

¹² Efforts continue to increase the efficiency and improve the governance of the social protection system as well as the transparency and governance of the fisheries and petroleum sectors, including participation on the Extractive Industries Transparency Initiative (EITI).

government has also adopted a new financial sector strategy in 2015 to further develop the sector and aims now to broaden the services that the financial sector offers while deepening the efficiency of existing tools to facilitate access to credit and improve credit allocation.

24. **The government is seeking to progressively improve infrastructure services that are financed by user fees.** With the financial and technical support of the European Investment Bank and *Agence Française de Développement* as well as technical assistance from other partners, the government is increasing efficiency and sustainability in the energy sectors, and expanding the port. In the energy sector, efforts to increase energy efficiency and use of renewable energy are ongoing. The Bank has supported through a SIDS DOCK grant¹³ the preparation of grid codes, feed-in tariffs, and model energy supply purchase agreements for renewable energy technologies and is now supporting the preparation of a renewable energy policy that is expected to provide a conducive framework for private sector investment in the sector. With support from the AfDB, GoS has adopted a national Public Private Partnership (PPP) policy to further facilitate private participation in development of public infrastructure. The World Bank is also working with GoS to facilitate PPPs in the energy sector.

4. THE PROPOSED OPERATION

4.1 Links to Government Programs and Operation Description

Links to the Government's Areas of Reform

25. **The programmatic series is aligned with the government's priorities.** Within the government program, the proposed operation supports a subset of actions that will enable the authorities to: (i) improve public expenditure; (ii) facilitate access to credit; and (iii) improve public investment. The selection of these actions was guided by upstream policy dialogue with the IMF and AfDB to ensure adequate coordination in supporting the broad reform program of the government, and was underpinned by analytical work. This program takes a pragmatic approach that focuses on reforms that can be completed in the short term and can deliver immediate results, while building the foundations for broader reform over the longer term.

Lessons Learned and Reflected in Operation Design

26. **The previous DPL series provided important lessons that have informed the preparation of this operation.** These lessons included the need to ensure: (i) a strong emphasis on knowledge and technical assistance to increase institutional capacity and support reform implementation; (ii) close coordination among development partners; and (iii) strong government leadership. Given the broad reform program that is being supported and the limited capacity of the public sector in a few areas where knowledge and highly specialized skills are required, a combination of analytical work and technical assistance is critical. The Bank has produced analytical reports, often financed by the government, to inform policy reforms, including to increase efficiency and quality of health and education sectors, consolidation of social assistance programs, and implementation of the financial sector strategy. This is complemented with technical assistance, also often financed by the government, which supports the implementation of reforms considered on this program. Furthermore, donor coordination

¹³ <http://sidsdock.org/>

and the harmonization of policy dialogue with the government has proved to be essential to reduce the government's transaction costs. Joint missions between the AfDB, IMF and World Bank have taken place and there is close coordination between the three organizations. Finally, leadership and political commitment have been critical factors in the successful implementation of reforms, complemented by strong institutional capacity at the Ministry of Finance, Trade, and the Blue Economy (MoFTBE) in designing and monitoring the implementation of the reform agenda.

4.2 Prior Actions, Results, and Analytical Underpinnings

Pillar 1: Raise efficiency of public expenditure

27. **This DPL supports reforms that raise the efficiency of public expenditure.** These reforms will (i) improve monitoring and administration of social assistance system; (ii) develop a health strategy to sustain health services for the population at large; and (iii) improve teacher management.

Improve Monitoring and Administration of Social Assistance System

28. **Seychelles has a comprehensive and generous social protection system.** The system comprises universal and means-tested programs, including a targeted cash transfer (Social Welfare Assistance) and a universal pension benefit (Retirement Benefit). In addition to the universal Retirement Benefit, the Seychelles Pension Fund (SPF), financed by mandatory contributions, provides old age, disability, and survivors' pensions to formal sector workers. All social assistance is administered by the Agency for Social Protection (ASP) which was created in 2012. In the first quarter of 2014, the ASP administered 24 schemes covering 13,410 people which represented 14 percent of the population. The Seychelles Pension Fund administers contributory retirement, incapacity, and survivors benefits.

29. **The government has introduced reforms in the area of social assistance to contain cost and raise efficiency, part of which was supported by the previous DPL series.** These areas included upgrading the management information system (MIS) for Social Welfare Assistance (SWA) and establishing automated cross checks with relevant government agencies, modifying the means test for the SWA and establishing a review panel to improve targeting, consolidating the home-care and family allowance program and introducing a means test for the consolidated program, revising regulations to introduce assessment of disability based on return to work approach and shifting part of the burden on sickness benefit to the employers.

30. **Despite on-going reforms to control public expenditure in certain social programs, overall spending on social assistance has been increasing.** In 2013, spending on social assistance programs was slightly lower than 3 percent of GDP but in 2014 it increased to 3.2 percent of GDP. The universal Retirement Benefit represents the largest single program, accounting for 1.7 percent of GDP. While the spending on SWA, the main poverty targeted program, declined as a result of improved targeting and monitoring, spending on other social assistance programs increased, undermining the recent efforts to contain public expenditure.

31. **The government wants to continue reforms to control cost of social assistance and raise efficiency.** One such challenge is the significant fragmentation in the social assistance sector. Legislation for social assistance is scattered and complex and there are a number of

social assistance programs with limited coherence among them. The ASP is mandated to administer welfare, employment related benefits and approved schemes.¹⁴ Several employment related programs are divided between the ASP and the SPF.¹⁵ Finally, the ASP also manages approved programs by the government.¹⁶ While the ASP is only mandated to act as a payment agent on behalf of other government institutions, it has also been working on improvements of these programs.¹⁷

32. As prior action of this DPL, the government has clarified ASP multiple reporting lines to reinforce accountability over social security and social assistance programs. The Social Security Act gave responsibility to the Minister responsible for Finance for oversight of the Social Security Act. This was explained by the fact that, prior to the introduction of an income tax in 2010, employment related Social Security benefits were funded via contributions to the Social Security Fund. However, with elimination of contributions and the change to funding from the public budget, the rationale for MoFTBE supervision of the social security scheme has become less clear. The Agency for Social Protection Act established the ASP and mandated it to administer social security benefits (formerly contributory) and social welfare programs. The ASP Act gave portfolio responsibility for the agency and its welfare programs to the Minister in charge of Social Affairs. As a result, the ASP reports to the Minister of MoFTBE for social security benefits it administers and to the Minister responsible for Social Affairs for the operation of the agency and the implementation of the social welfare programs. To clarify this, the cabinet approved a memorandum proposing the transfer ASP ministerial responsibility to Minister responsible for Social Affairs which is a prior action to this operation.

33. Also, as a prior action of this operation, Cabinet will approve a strategic plan and action plan for the ASP. Gaps and overlaps in the legislation framework make implementation difficult without subjective interpretation. This ambiguity is an impediment for institutionalization of implementation with clear rules and guidelines. Also, there are multiple programs that may have been relevant in the past, but have lost their relevance and are putting a fiscal burden on the government budget with no clear objective. Furthermore, some benefits that identify the poor with means test have no transparent eligibility criteria. The ASP has conducted a strategic analysis to define strategic directions for core social assistance interventions. Based on this, a strategic plan and action plan for the ASP has been prepared. The action plan sets a holistic approach to social assistance to improve coherence in the legislation that has overtime become scattered and complex with the piecemeal solutions introduced to address problems as they arose.

¹⁴ The welfare and employment related benefits are administered on the basis of two main acts, the Agency for Social Protection Act (2011); and Social Security Act (2010), further developed by multiple regulations. There are multiple benefits under the Social Security Act including the non-contributory retirement pension provided to all Seychellois above age 63, sickness benefit, maternity benefit, injury benefit, invalidity benefit, disablement benefit, survivor benefit, dependent benefit, abandoned child benefit.

¹⁵ The SPF provides incapacity and survivors benefits with eligibility for SPF benefits based on contributions and eligibility for Social Security Benefits related to employment and payment of income tax, but not contributions.

¹⁶ These programs include the Home Care Allowance Program, transportation subsidies to the Seychelles Public Transport Corporation, the Post-Secondary Students Bursary Scheme, the Dedicated Fund for Education, the Skill Acquisition Programs for Youth, and Foster Care.

¹⁷ For example, the Home Care Allowance Program, the largest of the approved programs, was converted to a means tested program and the ASP conducted a census survey of beneficiaries and home carers as a basis for further improvements. The ASP also spearheaded instituting a means test for the Home Care Allowance Program. The Post -Secondary Students Bursary Scheme is provided to all students attending post -secondary institutions which mean that those students who do not need this benefit are also receiving it. As regards the Dedicated Fund, school principals determine eligibility and there are no established transparent selection criteria.

Prior Action 1: The Borrower's Cabinet has approved a strategic plan and action plan for its agency responsible for social protection and transferred the ministerial responsibility for said agency to its minister responsible for social affairs.

34. **Moving forward, implementation of the action plan will imply adoption of revised social protection legislation.** Implementation of this action plan would improve coherence and efficiency of social assistance all of which would contribute to strengthened administration of programs. The programs administered by the ASP will be reviewed to improve efficiency and effectiveness. The action plan proposes measures to reduce fraud and error and to increase automation in certain processes such as application procedures and payment systems to improve efficiency. At the same time a cost analysis will be conducted to recommend areas for improving the management of the ASP. The planned activities are expected to be conducted during 2015-2017. All in all, this is expected to translate in a reduction of total spending on social assistance from 3.2 percent of GDP in 2014 to 3 percent of GDP in December 2016.

35. **Supported by this operation, monitoring and evaluation (M&E) capacity of the ASP will be upgraded to improve control of social assistance.** The ASP currently has limited capacity to monitor and evaluate programs and to use this information for policy making. The use of information technology is limited, which undermines the capacity of the ASP to carry out M&E. For instance, reforms supported by the previous DPL series specified that the ASP will reimburse employers for only 15 of sick leave per person per year. Yet, implementation is difficult to monitor because ASP lacks an automated database of applicants and beneficiaries. As a prior action of this operation, the coverage of ASP's Management Information System (MIS) has been broadened to include the sickness benefit, which was previously not included. This is expected to facilitate implementation of the regulations related to payment of sick leave and reduce spending of sickness benefit 15 percent between 2014 and 2016, from 0.07 percent of GDP in 2014 to 0.06 percent of GDP in December 2016.

Prior Action 2: The Borrower had expanded the coverage of the agency responsible for social protection's management information system to include the data on applicants and beneficiaries of its sick leave benefits.

Develop a Health Strategy to sustain health services for the population at large

36. **Incremental reforms in the health sector in Seychelles are needed to address the new emerging needs and aspirations of the citizens.** The current health system has impressively delivered for what it is designed for – i.e. primary health care,¹⁸ and Seychelles is the first country in Africa to successfully complete the epidemiological and demographic transitions. However, aging population,¹⁹ growing non-communicable diseases, and mental health put new pressure on the health system.²⁰ In addition, Seychelles has to put in place

¹⁸ The state provides free primary and universal access to healthcare, with very good indicators of health outcomes— infant mortality at 10.9 per thousand live births in 2014, maternal mortality of zero in most recent years, all children fully immunized, 99 percent of deliveries assisted by skilled health workers, and life expectancy at birth of 73.2 years in 2014 (78.3 for women and 68.4 for men) —all of which compare favorably with other middle-income countries and some OECD countries.

¹⁹ Population above 65 years old has increased from 6.8 percent in 2010 to 7.4 percent in 2014 and is projected to reach 18.1 percent by 2040. This is already above the UN's definition of ageing society – more than 7 percent of the total population above 65 years old.

²⁰ Non-communicable diseases, in particular, have been the main causes of death in recent years and reflect changing lifestyles

strategies to contain cost as health sector spending has increased substantially in recent years²¹ and pressure will continue given the expensive tertiary care for aging population and treatments for non-communicable disease. In this context, it becomes even more critical to strengthen prevention, including multisectoral primary prevention and early detection and treatment of risk factors. Current budget allocation to prevention and education is low. Increased investment, which could be achieved through re-allocation within the existing budget, will have high return in the medium to long term to contain cost of service provision.

37. The health sector in the Seychelles is pursuing a major modernization effort to ensure its sustainability. Under the Constitution of Seychelles, the population is entitled to primary care free of charge, but what is covered under primary care is not clearly defined and the fact, GoS ends up subsidizing health care that may not be under its responsibility. To respond to the above challenges, the government has initiated multi-pronged reforms in the health sector, including an institutional reorganization aimed to separate functions and define mandates.²² The reforms aim at strengthening public health functions, making health care services more efficient, introducing a modern and integrated information system, and building a results focused accountability system. Also, GoS is developing a health sector strategy as the current health strategic framework will expire in 2016. A costed comprehensive health sector strategy will provide a framework to assess cost of service provision, which in turn will help the government to better enhance accountability, assess efficiency in use of resources, and establish standards. Also, since health services are provided free of charge, cost of service provision can be used to introduce shadow pricing and sensitize the public about the cost of health service provision.

38. The reform is expected to better protect the most vulnerable. Overall, improving the efficiency and sustainability of the health care system will have long lasting benefits to the society at large while improving the health outcomes for those most marginalized and least able to seek private care outside Seychelles. A refocused effort on primary care delivered through community care level and strengthened through outreach is expected to reach out to those most marginalized by the current system, improving equity in outcomes. Also, efforts to strengthen multisectoral actions on the public health agenda will benefit mainly the adolescents who have become one of the health groups most at risk.

39. With the support of this operation, the government will adopt a National Health Policy. As part of the implementation of the National Health Policy, GoS will adopt with World Bank support by December 2016 a clear package of health services and interventions to clarify entitlements and ensure that only most effective services aligned with the emerging disease

and diet— mainly obesity, tobacco use, alcohol abuse, and lack of physical activity. The three main causes—cardiovascular diseases, cancers, and respiratory diseases—account for about 60 percent of all deaths. Also, there is large amount of teenage pregnancies and the proportion of abortions increased in recent years. In 2014, 12 percent of all births occurred to women aged under 20 years old and between 15 to 20 percent of all pregnancies are unplanned and unwanted, resulting in rising unsafe abortion rates and premature deliveries, school dropouts and a multitude of social, medical and psychological problems. Contraceptive use remains low at 54 percent and many women still opt for illegal abortions (legal medical abortions can be obtained for very specific reasons following a review by a medical board).

²¹ Recurrent expenditure in the health sector is growing quickly from SR 273 million (2.4 percent of GDP) in 2009 to SR 615 million (3.4 percent of GDP) in 2014.

²² Following the re-organization in the health sector in Seychelles, three major autonomous entities will need to be managed in an interdependent way. The Ministry of Health (MoH) is mandated for policy development, planning, and monitoring and evaluation of program implementation; the Health Care Agency (HCA) manages the provision of health care; and the Public Health Authority (PHA) regulates the health sector and the protection of the population's health. Accountable institutions require clarity in mandate (in this case a clear definition of what is to be delivered at each level of care), strong M&E systems, and results oriented budgets.

burden in Seychelles are provided. The revised framework will also allow the government to adapt this package of services and benefits to the evolving burden of disease and new technologies over time. Furthermore, management of inputs (training, purchase of equipment and medicines) would be simplified as they are affected by the benefits delivered. The new Health policy will serve to relocate resources to most effective interventions and health prevention and promotion services are expected to increase from 6 percent of total health budget in 2014 to 9 percent by December 2016.

Prior Action 3: The Borrower's Cabinet has approved the National Health Policy.

Improve Teacher Management

40. **Seychelles has made great strides in access to education but major challenges remain with regards to quality.** Education is free and compulsory from primary to the second-to-last grade of secondary education, and enrolment rates are comparable to those in most middle-income and even some high-income countries. However, less success has been achieved in learning outcomes and completion rates in secondary education. For example, in 2012, only one-third of students in the last grade of basic education (P6) scored a grade of C or better in the National Examinations. Results of the IGCSE²³ examinations are also quite poor, particularly in science. Further, in the last two evaluations administered by the Southern and Eastern Africa Consortium for Monitoring Educational Quality (SACMEQ), students in Seychelles scored below their peers in Kenya, Mauritius, and Tanzania in mathematics. Cross-regional comparisons of outcomes for the Program for International Student Assessment (PISA+) suggest that Seychelles might also be scoring lower than Malaysia, Costa Rica, and Chile. Low learning achievements, combined with the failure of students to enter the last grade of secondary school, leave large sections of the population with insufficient mastery of basic skills.

41. **Cognizant of the challenges above mentioned the Ministry of Education (MoE) embarked on a comprehensive education reform.** A medium-term education sector strategy (MTS) for the period 2013 to 2017 was launched in August 2013. The MTS is being implemented through PPBB, as MoE is one of the two first ministries to pilot PPBB in the Seychelles. The introduction of PPBB has brought about a process of change within the MoE. The 2004 Education Act was amended and several education policies were developed, namely on inclusive education, information and communication technology, and distance education and open learning. Six education programs, based on MTS priorities, were defined with clear priorities and outcomes against which the budget is organized and disbursed.²⁴ Further, several institutional changes were introduced: (i) the Seychelles Institute of Teacher Education was incorporated into the MoE in 2014 to strengthen it and provide pre- and in-service teacher

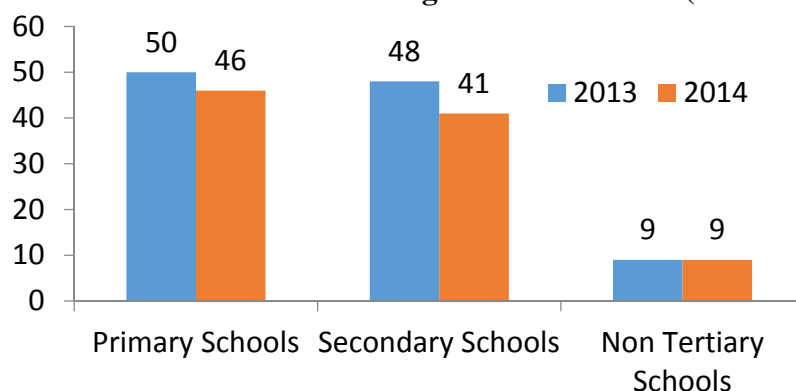
²³ Certification of secondary education is done by Cambridge International Examinations through the International General Certificate of Secondary Education (IGCSE).

²⁴ These programs are: (1) Governance, Policy and Management, which provides for the overall leadership, management and strategic policy direction of the MoE. (2) Education Development which provides support for the teaching profession, improves the standard and quality of education and promotes best practices in classrooms, schools and other centers of education. (3) Formal Early Childhood Development Care and Education which supports the development of provision of quality early childhood education. (4) Primary Education which support the development and provision of quality primary education. (5) Secondary Education which supports the development and provision of quality secondary education. (6) Tertiary Non-University Education and Training which supports the development and provision of quality tertiary education and training to meet the manpower needs of the country.

training and professional programs; (ii) the teachers' scheme of service is under revision to better define teacher career and compensation; (iii) greater schools autonomy is being promoted; and (iv) the Adult Learning and Distance Education Center was transformed into a professional center. MoE is successfully overcoming capacity challenges to successfully implement PPBB, and set a quality agenda by linking learning outcomes and quality outputs with the budget.²⁵

42. **Strengthening teacher capacity and retention with a view of improving quality is a key priority of the MTS.** Teacher attrition is a major issue affecting quality of education in the Seychelles. Difficulties to recruit and train qualified teachers are compounded by the alarming rate at which qualified teachers in primary schools, notably holders of Level 2 diplomas, are resigning (Figure 2). Although, teacher attrition has decreased in 2014, it remains very high and required that 59 teachers and lecturers were newly appointed in 2014. Many of those were expatriates, which constitute now 28 percent of the overall teaching force in Seychelles. A 2013 MoE report on teachers issues²⁶ indicates that many Seychellois teachers feel unhappy with their profession, which leads to high attrition. Teachers complain about stressful working conditions and growing administration burden that hamper effective teaching. Teacher remuneration and coverage of classes as a result of teacher shortages were also considered to negatively impact on teachers. Moreover, teachers stated that there are limited opportunities for professional and career development.²⁷

Figure 2: Number of teachers exiting State institutions (2013-14)



Source: Medium-term Strategy, Ministry of Education, Seychelles

43. **Although salary costs account for more than 90 percent of overall education spending, returns are limited due to the high attrition rates (vacancies are 30 percent on average) and low teaching performance.** This is explained by several reasons. First, compared to other upper-middle and high income countries, Seychelles allocates a relatively lower share of its national resources to education. Second, the high share of salary costs in public education is higher than in comparable countries, partly because Seychelles maintains lower pupil-teacher ratios at the primary and secondary levels than most comparable

²⁵ Examples of indicators include: percent of students in primary 6 scoring grade C and above in English and Math; and percent of teachers with minimum qualifications.

²⁶ Report resulting from meetings with teachers to discuss the challenges of their profession, 2013.

²⁷ Other factors mentioned included: (a) the need to work outside normal working hours, during weekends and public holidays to ensure that lessons are planned, find resources, prepare for classes, etc.; (b) teachers/lecturers have limited non-teaching time during school hours for preparation, marking and recording. Time outside teaching hours is used for meetings, working/training sessions, meetings with parents, and support to other classes than their own.

countries.²⁸ As a result, and despite the government's efforts to use teacher compensation as a core policy for teacher retention and quality, the education system is forced to set low standards for entry into teacher education programs, which fail to attract the adequate candidates.

44. **Monetary incentives have not been able to address the above challenge and are a source of inefficiency.** Other than their regular salaries, teachers can benefit from two types of compensation: allowances and gratuities. The allowance scheme includes: (a) inducement allowance; (b) housing allowance; (c) education performance allowance; (d) responsibility allowance; (e) free housing-accommodation allowance for teachers working in inner/outer islands; and (f) part-time allowance, which is used to pay teachers who cover extra class activities. Gratuities, which are not linked to teacher performance, represent 6.5 percent of the teacher's total earnings for continuous terms of employment, and are paid at five-year intervals. Gratuities apply to all employees on "local appointment" including those qualifying for pensions. Overall, the amount devoted to allowances and gratuities have been growing to represent 19 percent of total teachers' compensation in 2014.

45. **As a prior action to this operation, Cabinet will approve a Memorandum to establish the principles of a comprehensive teacher management policy.** Teachers have been requesting a management reform. As part of the preparation and implementation of the MTS, some ad hoc activities to improve teacher management have been introduced.²⁹ MoE aims now to develop a comprehensive teacher management policy that links teacher management to other policy development, including a revision of the teachers' scheme of service. The Memorandum establishes the key principles and targets of the teacher management policy reform, and guides further policy formulation and implementation focusing on quality and efficiency improvement. Consultations around the Memorandum have taken place with teachers, teacher trainers, school directors and MoE staff, and the content of the Memorandum reflects the views of the various stakeholders.

Prior Action 4: The Borrower's Cabinet has approved a memorandum for a comprehensive teacher management policy reform focusing on issues of teacher distribution, training, career, and performance.

46. **The comprehensive teacher management policy reform in the Memorandum is informed by international experience.** It addresses four areas: (1) teacher recruitment and selection; (2) teacher deployment and management; (3) evaluation of teachers' performance; and (4) teacher preparation and development. Implementation of the Memorandum will require a revision of the existing policies on (i) teacher recruitment and distribution; (ii) teacher career and status; and (iii) teacher compensation and incentives. The World Bank will support through a Reimbursable Advisory Service (RAS) the implementation of the memorandum during the next year. This will entail preparation of revised policies that aim to make the teaching profession more attractive. This will be achieved offering a more rewarding career path, improved training of techniques that strengthen the focus of teacher activities in the classroom, and incentives better linked to performance. Also, strategies to improve teacher

²⁸ While the geographic distribution of the population in Seychelles poses challenges to public service delivery and affect pupil-teacher ratios, other factors seem to be in place related to teacher distribution and management. Analysis of data from 2008 to 2011 indicate that while there are important geographic variations, when the smallest islands are excluded, pupil-teacher ratios in many primary and secondary schools continue to be low, indicating that there are variables other than geography in place.

²⁹ MoE has recently introduced an education performance allowance linked to teacher performance.

training (both pre- and in-service) will be adopted and implemented, along with the design and implementation of improved monitoring and evaluation mechanisms. These reforms are expected to have an impact on the decrease of teacher attrition from 11 percent in 2014 to 7 percent in December 2016.

Pillar 2: Facilitate access to credit

47. **This DPL supports reforms that are expected to facilitate access to credit through better credit information system and a collateral registry.** This program supports: (i) improve reporting of the credit information system; and (ii) create a centralized electronic collateral registry.

Improve reporting of the credit information system

48. **Incomplete credit information systems in Seychelles undermine access to credit and allocation efficiency.** Credit information systems enable lenders to view a potential borrower's financial history, improving their capacity to assess its risk. They also permit borrowers to establish a good credit history that facilitates their access to credit. In the Seychelles, the basic financial infrastructure has been created with the implementation of several payment systems operated by the Central Bank of Seychelles (CBS), the creation of the Credit Information System (CIS), and the upcoming launch of a collateral registry. The government has also adopted a new Financial Strategy in 2015 to further develop the sector. Also, with support of IFC, government has adopted a legal framework for leasing and there is a leasing program under implementation, fully funded by the Central Bank of Seychelles. Moving forward, the authorities aim to broaden the services that the financial sector offers while deepening the efficiency of existing tools to facilitate access of credit and better allocate credit. Reforms of the CIS will further facilitate the risk assessment of banks and other lenders, which may have an impact on credit access, as people that may only get loans from retailers could access cheaper bank credit based on good credit history.

49. **In 2012, the Central Bank of Seychelles launched the Credit Information System, which is the only credit reporting mechanism in Seychelles.** The CIS is an on-line system for licensed commercial banks and other regulated financial entities to access credit reports. At present, the only participants in the CIS are licensed commercial banks, the Development Bank of Seychelles, Housing Finance Company, and Seychelles Credit Union that are obliged to upload credit data to the CIS. They are also the only institutions that can request credit reports from the system. It is estimated that the CIS provides an actual credit report for 75 percent of the queries, yielding an average of 120 reports per day. No services beyond standard credit report have been developed.

50. **The information contained in CIS credit reports is useful to lenders, although it is insufficient for underpinning robust assessments of credit risk.** CIS regulations require that data providers report into the CIS all their loans to individuals and firms. Both positive and negative data is reported, and information on existing loans was updated on a monthly basis, or immediately after a loan becomes non-performing. While the introduction of credit reporting has been useful for lending as well as loan classification and provisioning, the CIS should be upgraded to improve data quality and completeness, and enable wider participation to effectively assist banks and other lenders in their credit risk assessments. In particular, the CIS

only presents financial obligations with licensed commercial banks and other regulated financial institutions. Moreover, CIS credit reports do not show specific repayment behavior and it only presents whether the credit has been classified as “pass” or in arrears.

51. With support of this operation, the CBS will improve the frequency of reporting to the CIS. The CBS has adopted regulations to ensure that institutions under its purview report more frequently to the CIS. As a result, the frequency of reporting to the CIS is enhanced, moving from monthly reporting to an event-based reporting (i.e. any time there is a change in the credit). In addition to the variables already included, CIS reports will also show specific repayment features, such as whether each individual installment or other repayment deadline was fully or partially fulfilled, or not repaid at all.

Prior Action 5: The Borrower’s central bank has promulgated regulations to ensure that credit data is reported on event-basis.

52. In the medium term, the CBS will work on other structural improvements to credit reporting in Seychelles, including a more comprehensive legal and regulatory framework for credit reporting activities. Participation in the CIS will be expanded to lenders currently not regulated by the CBS, including, among others, lending government agencies or programs (e.g. Small Business Financing Agency), as well as commercial companies and others that engage in hire-purchase activities and financial leasing, especially in light of the recently enacted Hire Purchase and Credit Sale Act and Financial Leasing Act.³⁰ To do so, the CBS will prepare with World Bank support a Credit Reporting Act before June 2016 to describe in detail the rights and responsibilities of all participants in the credit reporting system in Seychelles, including data providers, credit reporting service providers, users, data subjects, other relevant data sources and regulators.³¹ As a result of the reform supported, the number of credit reports issued per day will be expanded from 120 to 250.

Create a centralized electronic collateral registry

53. The lack of a secured lending system is a major constrain for additional lending to the private sector. Currently, there is lack of legal framework for modern secured transactions in the Seychelles and no collateral registry records secured interests over movable property. As a consequence, banks and other creditors cannot lend money using movable assets as collateral because there is no proper registry to know whether a particular movable asset is being already used as collateral or which creditor has priority over it. As a result, the banks only provide loans secured by immovable property, which excludes a significant part of the private sector from the ability to obtain credit. In addition, the lack of collateral registry prevents the banks, non-bank financial institutions and other potential creditors from using financial leasing to channel credit to the private sector. All this is partly behind of the low private sector credit in Seychelles that stands at only 25 percent of GDP.

³⁰ In a modern credit reporting system, credit data is needed from banks and other licensed financial institutions, as well as from retailers and any other real sector entity that lends money or grants any form of credit. While hire, purchase and credit sale existed in Seychelles, the new law regulates them under the Financial Services Authority and is therefore more feasible that they can become participants in the CIS.

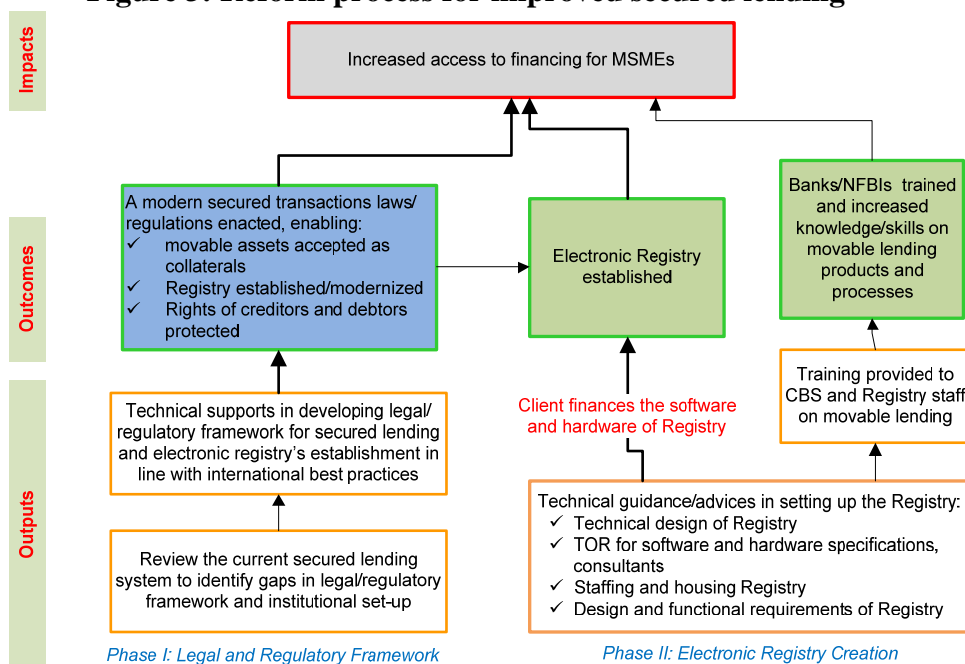
³¹ In the longer term, the CBS may also consider including other data providers, such as utilities companies, which although generally do not provide loans commercially, are involved in a form of credit relationship with their customers as they provide the underlying service in advance of payment.

54. **The Central Bank of the Seychelles (CBS) has embarked on a comprehensive reform to put in place a modern secured lending system and a collateral registry for movable property.** The GoS and the CBS have adopted, with World Bank assistance, a Cabinet Policy Paper outlining the legal reforms needed to harmonize the current commercial and financial laws with international best practice in order to have a centralized electronic collateral registry. This will require eight laws to be harmonized and enacted, starting with the amendment of the Secure Transaction Act, and followed by the Charges section of the Companies Act. In parallel, the Department of ICT and the Registry General's Office have developed and tested software for the centralized collateral registry. Making the registry operational will be done at the time the above legal reforms are implemented.

55. **As a prior action of this operation, the Cabinet has approved a Secure Transaction Bill for submission to the National Assembly.** The overall reform supported will pave the way to a modern secured transactions system by: (i) creating the underlying legal framework; (ii) creating a national collateral registry for all secured interests in movable property; and (iii) training the trainers and most important stakeholders on the use of the collateral registry. Once all three components are in place, banks and other creditors in the Seychelles will be able to use a variety of collateral (production assets, accounts receivables, etc.) and eventually provide more loans to a much needed private sector (Figure 3).

Prior Action 6: The Borrower's Cabinet has approved for submission to the Borrower's National Assembly a Secure Transaction Bill.

Figure 3: Reform process for improved secured lending



56. **Moving forward, the government intends to make the centralized collateral registry operational.** Once the Secure Transaction Act is adopted, the software for the centralized collateral registry in the Registry General's Office will be operational. Setting up a modern centralized collateral registry for movables in the Seychelles will benefit SMEs,

financial institutions (banks, leasing companies etc.) and government institutions. Financial institutions will be able to expand their lending operations against movable collateral and enterprises will have greater access to finance, as they will be able to use their movable assets, inventory and accounts receivable as collateral. Overall, these reforms are expected to raise the number of lenders connected to collateral registry to 15 by December 2016, compared to none as it is the case today. This is expected to have a positive impact both in terms of the number of companies that receive loans secured with movable property as well as the value of loans guaranteed by movable collateral.

Pillar 3: Improve Public Investment

57. **This DPL supports reforms to improve public investment through better public investment management systems and improved government supervision of commercial SOEs.** This program supports: (i) improving public investment management; and (ii) enhance SSI capacity to monitor public by SOEs.

Improve Public Investment Management

58. **The government has made considerable progress in PFM.** Since 2008, Seychelles has substantially improved its PFM system, as evidenced by the improved rating in the Public Expenditure and Financial Accountability (PEFA) in 2011. The government adopted a new PFM Act in 2012 and regulations in 2014 that introduced PPBB, the Medium Term National Development Strategy (NDS), the Public Sector Investment Programme (PSIP) and asset management. The government has also introduced a new chart of accounts that features a functional classification to facilitate fiscal reporting in compliance with the 2001 Government Finance Statistics Manual. A policy framework that sets out the benefits of adopting PPBB and implementation guidelines for the PPBB was adopted, and PPBB is being rolled out with assistance of the World Bank.

59. **Although there has been some progress, the public investment management (PIM) process in Seychelles is still uncoordinated and lags behind other PFM areas.** In 2012, the government published a guidance document for the development of public investment proposals. It introduced the PSIP and requirements for submitting investment projects for screening and approval. As a result, the system prevents any project to be implemented unless it is included in the public budget and the PSIP. However, too many projects are included in the PSIP despite the fact that only 20 percent of them are implemented annually, which undermines its credibility. There is still limited efficiency in the public investment process as manifested in project delays, incomplete projects, and lengthy procurement procedures that translate in failures to fully execute the capital expenditure budget.³² The proposed reform also seeks to reduce the procurement thresholds to ensure that adequate procurement review is focused on most relevant purchases.

60. **There is not yet systematic approach to capital budgeting and most areas and components of the capital expenditure process need to be developed further.** There is a lack of project selection criteria and, in the absence of a national development plan, projects are

³² Execution rates for capital expenditures between 2007 and 2011 ranged from 79 to 93 percent of the budget, during this period on average only an estimated 87 percent of capital appropriations have been spent.

selected in an ad-hoc basis. Also, lack of formal guidelines for preparation of feasibility studies of public projects and project appraisal undermines gate-keeping functions and the connection between project financing and recurrent expenditures. Furthermore, lack of an institutionalized and centralized unit for assessment of projects translate into inadequate project verification in terms of its social and economic impacts. Finally, there is overall lack of economic skills in government, which translate into limited planning and appraisal capacity across government. Government currently reviews a large number of projects, typically in a formal way but with little analysis.

61. **As a prior action of this operation, the government will make operational a Development Committee and Secretariat to appraise large projects and adopt guidelines for public investment and maintenance.** The Development Committee has been created and staff appointed by presidential decision on October 10, 2014. It is formed by representatives from line ministry and/or SOEs, regulatory authority and MoFTBE. It will approve all screening criteria for development projects, with the Secretariat to review the screening conducted by ministries and agencies. As part of the implementation of PPBB, ministries and agencies, during their medium term expenditure strategy planning process, will be responsible of determining capital projects required to achieve their objectives. Such planned projects will be submitted to the Secretariat for consideration. The Secretariat will also review technical quality of project preparation and appraisal on a selective basis and approve all large, complex and PPP development projects as well as all small projects in batches.³³ It will also review and approve all major cases of project adjustment. With World Bank support, GoS as prepared detailed guidelines on project appraisal methods and standards to facilitate the assessment of the financial viability of projects, which for particularly large or complex projects would also require comprehensive cost-benefit analysis. Major adjustments to project design or cost outside of planned agreements would be reassessed and reapproved by the Development Committee. Large and complex projects and new projects (even if small) that will be repeated should be subjected to full appraisal, whereas small and repeated projects can use key indicators to ensure consistency with sector strategies and adequacy of demand.³⁴

Prior Action 7: The Borrower has established a committee for independent review and selection of public investment projects, appointed the relevant staff for the purpose of said committee's operations and the Borrower's Cabinet has approved the guidelines for preparation and appraisal of public investment projects.

62. **A strengthened PIM system will ensure adequate assessment of all investment projects in the PSIP.** As a result of this reform, it is expected that the PSIP will ingrain a control mechanism that ensures that all approved and budgeted projects have been through appropriate screening, preparation and approval processes. To track progress in this reform, the government expects that all projects above 10 million rupees in the 2017 public budget will be assessed and approved by the Development Committee.

³³ The Secretariat is expected to be formed by a Project Appraisal Unit that develop methods and standards for project appraisal, direct capacity building efforts across the GoS (including the capacity of the Development Committee members themselves), and review project documents and feasibility studies in conjunction with the sponsoring organization before they are presented to the Development Committee.

³⁴ Between 25 to 50 percent of all projects presented annually are asset renovation, rehabilitation or replacement to sustain service delivery capacity. Budget and authority to implement these projects should be delegated to sector ministries as part of their sector budget, with some ex-post control carried out by the Development Committee.

63. **The government, supported by the previous DPL series, has made progress in addressing SOE governance.** The legal framework for oversight of 24 SOEs was created with the adoption of the Public Enterprise Monitoring Commission Act in 2013. The Act sets up the Public Enterprise Monitoring Commission (PEMC), originally established in the MoFTBE, as an independent oversight body for SOEs. SOE reporting and disclosure has been improved and made more timely with, institutional arrangements clarified, and a performance monitoring function established. As a result, most audited financial statements are now publicly available on PEMC's website. However, PEMC still does not produce a complete report on the SOE portfolio. Also, salaries of public enterprise employees have been delinked from civil service wages.

64. **Efficiency is being increased but efforts need to continue to keep fiscal risks under control.** Key public entities such as the Public Utilities Corporation (PUC) and the Development Bank of Seychelles (DBS) have regained profitability in the past five years, and Air Seychelles' marginal profitability today shows improvements made since steep losses a few years back. Yet, more needs to be done to improve enterprise efficiency and delivery of public services, to enhance SOE creditworthiness and investment returns while minimizing contingent and implicit liabilities to the state.³⁵ For instance, while Seychelles Trading Company (STC) does not depend on government budget outlays, its contemplated expansion could represent contingent liabilities if losses occur, and may undermine competition in the retail sector.

65. **SOEs supervision needs to be clarified and reinforced.** In 2013, eight SOEs were transferred to the *Société Seychellois d'investissement* (SSI), itself an SOE falling under the PEMC Act, which manages the state's shareholder rights in commercial SOEs with social or developmental goals. Government is planning to transfer another six SOEs to SSI which intends to hold this portfolio and provide strategic guidance, ensuring that shareholder policies reflect government priorities. The turnover of the SSI portfolio SOEs was approximately 740 million USD in 2014, equal to approximately 50% of GDP. Net profit was just over 17.4 million USD, but this result includes some public transfers, grants or unpaid/deferred taxes, which if taken into account would have worsened the results. Only 3 companies have paid dividends over the years 2012-13-14 (Indian Ocean Tuna, Land Marine, IDC). In 2014 total Dividends received by SSI were 45 million SR (approx. 2.8 USD Million or 0.5% of GDP), but taxes owed by these SOEs far outweighed the dividends received. The companies are generally solvent and most have sufficient liquidity to cover current liabilities. Hence the fiscal risk from contingent liabilities is probably low or moderate in the short to medium term. The new role of SSI should be to better manage such risks by close monitoring and independent analysis of companies in the portfolio. The original mandate of SSI delineated the roles of the SSI board, the SOE boards and SOE management under its purview and the relationship of SSI with other agencies such as PEMC.

³⁵ Key SOEs such as SEYPEC, Air Seychelles or the Seychelles Trading Company (STC) do not transfer any dividends to the State and a few SOEs still receive sizable subventions, grants and net lending for their operations. For instance, PUC and SPTC receive public transfers, for capital expenditure in the case of PUC and to cover SPTC operating losses associated to low average tariffs. There have also been significant public transfers in connection with the restructuring of Air Seychelles.

66. **While SSI's new mandate takes the first steps in putting important governance structures in place, a number of areas required greater clarify, particularly in areas which could increase fiscal risk.** Firstly, the mandate went beyond management of the SOE portfolio, stating that SSI would be the GoS's investment vehicle. Secondly, the mandate allowed SSI to retain SOE dividends for future investment and to borrow commercially as well as to borrow against SOE shares. The latter may have significant fiscal consequences, even if the investment is not explicitly guaranteed by the state. Moreover, SOE dividends have provided a major source of public finance in the Seychelles, accounting for around 5 percent of government revenue a year, and constitute a major component of the medium term fiscal framework going forward. Finally, in terms of governance, there is conflict of interest of SSI board directors that can also head SOEs that SSI holds.

67. **With the support of this operation, the government has clarified the mandate of SSI.** The mission statement now takes into account the macroeconomic situation of the country, including limited savings, high public debt level, and high opportunity cost of new investments by SOEs. The method of selection and the composition of SSI's board of directors has been revised to improve transparency in line with international good practices. As a result, board governance will be improved, particularly the director nomination process, which is expected to strengthen boards.

Prior Action 8: The Borrower has approved a revised mandate for Société Seychelloise d'Investissement, in a manner that clearly defines the unique objectives and activities of the institution in relation to the Borrower's other similarly-situated institutions, all in line with good international practice on corporate governance of state-owned enterprises.

68. **Moving forward, the government will further focus SSI's mandate through a shareholder policy for SSI and an investment strategy and operating guidelines.** This will clarify transfer of dividends and retained earnings, portfolio objectives and define when investment have public interest. It will also determine the criteria to apply concerning risk, minimum projected financial and economic rates of return, and performance benchmarks, as well as the due diligences for project selection to minimize fiscal risk and impact on competition. Policy implementation will help SSI to play an important role to identify and provide guidance to each board on SOE operational weaknesses, with support from an improved monitoring function. It can also help improve board governance, particularly the director nomination process, which would help strengthen boards by leading to the nomination of more qualified directors. Also, SSI can play a role to ensure that SOEs remain focused on their core mandates and avoid unnecessary risks by expanding beyond those core mandates.

69. **Effective implementation of SSI's mandate and policies will largely depend on an improved monitoring function.** PEMC will continue its role as monitoring institution of all SOEs, as mandated in the PEMC Act. It will also carry out governance audits of three selected SOEs by June 2016 and three more by June 2017. The World Bank, funded by GoS, will support PEMC to build capacity in its performance monitoring unit to identify, early on, signs of impending difficulties in SOEs. Also, SSI will work with PEMC and the SOEs under SSI's purview to develop a set of financial and non-financial performance indicators for each SOE.³⁶

³⁶ Performance indicators for monitoring SOEs performance will include financial and non-financial indicators. Among the latter they will be turnover/revenue, administrative costs/costs of sales, operating profit, net profit/loss, return on assets, dividend payments, retained earnings, debt levels (ST/LT borrowings, payables), subsidies/transfers from budget (including loans from government) and deferred taxes/tax liabilities. Among the non-financial indicators there will be staffing levels and

These indicators would be the result of an annual strategy exercise and be continually monitored by PEMC to assess progress. As a result, it is expected that at least two-thirds of SSI portfolio companies will meet or exceed their respective indicators by December 2016.

Analytical Underpinnings

Table 4: Analytical Underpinnings Informing this DPL

Prior action	Analytical underpinnings
Pillar 1: Raise efficiency of public expenditure	
<p>Prior Action 1: The Borrower's Cabinet has approved a strategic plan and action plan for its agency responsible for social protection and transferred the ministerial responsibility for said agency to its minister responsible for social affairs.</p> <p>Prior Action 2: The Borrower had expanded the coverage of the agency responsible for social protection's management information system to include the data on applicants and beneficiaries of its sick leave benefits.</p>	<p>Strategic Analysis of the Agency for Social Protection (ASP) prepared by the Agency for Social Protection in 2014 identifies challenges to improve the effectiveness of the social assistance sector and the Agency for Social Protection. Also, Seychelles: Legislative, Regulatory and Policy Note on Social Protection prepared in 2015 identifies gaps and overlaps in the social assistance regulation and recommends ways to address these challenges moving forward, including clarification of ministerial responsibility over ASP and the need to continue improving M&E of existing social assistance programs..</p>
<p>Prior Action 3: The Borrower's Cabinet has approved the National Health Policy.</p>	<p>Special health task force report “strengthening and modernizing Seychelles’ health systems to improve health outcomes” sets out a number of policy and reform actions; and PER Policy Notes of 2014 “adapting the health sector to emerging challenges” examined issues of financial sustainability, efficiency in the allocation of funds, and productivity. They present challenges related to growing NCDs and make recommendations in terms of improved management of health system and need to update the health strategy to raise efficiency and confront them.</p>
<p>Prior Action 4: The Borrower's Cabinet has approved a memorandum for a comprehensive teacher management policy reform focusing on issues of teacher distribution, training, career, and performance.</p>	<p>Education Medium Term Strategy 2013-2017 calls for a comprehensive reform of teacher issues (performance, salary, career, training, retention). Also PER Policy Note on Education 2014 sets out a number of policy reforms for the education sector including on improving efficiency of teacher management.</p>

staffing costs, capacity building (i.e. qualified local staff in managerial/technical positions), quality of services – as measured by customer satisfaction.

Prior action	Analytical underpinnings
Pillar 2: Facilitate access to credit	
Prior Action 5: The Borrower's central bank has promulgated regulations to ensure that credit data is reported on event-basis.	The Seychelles' Financial Sector Development Implementation Plan (approved by Cabinet in November 2014) focuses on the development of the National Payment System and other relevant financial sector infrastructure. The report recognizes that the introduction of the credit information system in 2012 has been extremely useful, but a number of upgrades are necessary to improve data quality (more often reporting) and completeness (more institutions reporting) and ensure that the system effectively assists banks and other lenders in their credit risk assessment.
Prior Action 6: The Borrower's Cabinet has approved for submission to the Borrower's National Assembly a Secure Transaction Bill.	The Seychelles' Financial Sector Development Implementation Plan (approved in 2014) also focuses on the development of the collateral registry and proposes legislation changes, and institutional and capacity strengthening to make operational a collateral registry.
Pillar 3: Improve public investment	
Prior Action 7: The Borrower has established a committee for independent review and selection of public investment projects, appointed the relevant staff for the purpose of said committee's operations and the Borrower's Cabinet has approved the guidelines for preparation and appraisal of public investment projects.	PER Policy Notes of 2014 "Strengthening Public Investment Management" identified critical weaknesses in public investment management and proposed an action plan for improvement, including the creation of the Development Committee. A World Bank commissioned report in 2015 "Strengthening Public Investment Management: Strengthening the Roles of the Public Sector Investment Program, Development Committee and Project Implementation" provides guidance about the mandate of the Development Committee and the guidelines to adopt.
Prior Action 8: The Borrower has approved a revised mandate for Société Seychelloise d'Investissement, in a manner that clearly defines the unique objectives and activities of the institution in relation to the Borrower's other similarly-situated institutions, all in line with good international practice on corporate governance of state-owned enterprises.	The World Bank prepared in 2015 a Review of SOE holding and Investment Companies worldwide , a brief note that reviewed good practices in the mandates of holding companies worldwide. It summarized these good practices into specific recommendations to guide the revision of SSI's mandate.

4.3 Link to CPS and Other Bank Operations

Link to Country Partnership Strategy

70. **This DPL and the World Bank's Country Partnership Strategy (CPS) for 2012-16 are closely linked to each other and to the government's program.** The CPS presented to the World Bank's Executive Board in April 2012 was updated and extended by the CPS Progress Report of November 2014. It is organized around two pillars and one foundation: competitiveness and employment; vulnerability and resilience; and governance and public sector capacity. The CPS Progress Report reaffirmed the important role of this DPL as the Bank's main vehicle for further supporting the government's broad reform program. The DPL supports the CPS as follows: (i) inclusiveness, through the improvement of education, health and social protection services; (ii) public sector efficiency, through the improvement of public investment management and monitoring of SOEs; and (iii) access to finance and business environment, through expanded services relate to credit information and collateral registry.

71. **The DPL complements other World Bank Group assistance that supports regional integration, public sector efficiency, private sector development, social protection, and renewable energy.** Through reimbursable advisory services, the Bank is providing technical assistance to support improvements in social protection legislation, implementation of Programme Performance Based Budgeting (PPBB), and institutional development and training to reinforce public investment management. Parallel trust-funded technical assistance has been provided to help develop the Financial Sector Implementation Strategy as well as the development of the credit information management system and collateral registry. Additional World Bank assistance is being provided to strengthen the national bureau of statistics to analyze households' survey information. Also, support is provided to the ministry of environment and energy to develop a renewable energy policy to expand energy capacity. An Extractive Industries Technical Advisory Facility is supporting implementation of the EITI. Finally, Seychelles is a member of the Accelerated Program for Economic Integration (APEI), a group of like-minded African countries aiming at speeding up reforms and learn from each other's experiences through South-South exchanges, a process that is being supported by the World Bank through technical assistance and a regional DPL.

4.4 Consultation and Collaboration with Development Partners

Consultation

72. **The government uses a participatory approach in its reform program to gain maximum cooperation from all stakeholders in its implementation.** During his State of the Nation Address, the President of the Republic of Seychelles outlines the measures to be implemented in the coming years. Consultations involve a wide range of stakeholders, including the National Economic Council that draws members from the public sector, private sector, and civil society to advise the government on economic policy for sustainable development. Also, the Minister of Finance uses public budgets to announce budgetary measures that could affect the population in advance of their implementation. Wide consultations have been held with stakeholder groups for reforms in areas supported. On the health sector, for example, the Taskforce report and the WBG's policy note and assessment were based on extensive consultations as well as the collection of two databases: a patient exit survey and a census and survey of health workers.

Collaboration with Other Development Partners

73. **This program supports reform areas that complement programs being implemented by other development partners in Seychelles.** This operation is closely coordinated with a parallel budget support operation by the African Development Bank (AfDB). The AfDB operation is a one year single tranche program of US\$10 million that aims to address key constraints for competitiveness and strengthen resilience in Seychelles through public sector efficiency, financial sector and business development. World Bank, AfDB and IMF programs have been closely coordinated, including through joint missions, to avoid overlapping areas and ensure adequate support to the broad reform program of the government. The United Nations Development Programme (UNDP) is providing the government with support to develop and strengthen the institutional capacity to promote environmental protection, biodiversity conservation, energy efficiency, and climate change adaptation. The EU provides technical assistance to mitigate global climate impact, in coordination with UNDP, as well as budget support operations through a regional integration program and a Fisheries

Agreement. Coordination is ensured by the MoFTBE, which allocates responsibilities to the development partners in different sectors.

5. OTHER DESIGN AND APPRAISAL ISSUES

5.1 Poverty and Social Impact

74. **The proposed operation is expected to have a favorable impact on poverty and social indicators.** The policy focus of the operation addresses poverty and inequality in the following three ways: (i) raising the efficiency of public expenditure in human development will serve to better protect the poor and increase the quality in education and health to further reduce inequalities; (ii) a more conducive access to credit will help to increase investment and create jobs; and (iii) enhanced efficiency in public investment is likely to remove supply side constraints and facilitate investment and employment creation. The actions supported by the operation are not expected to have any direct distributional impact on the poor. With regard to the reform in social protection, it seeks at this point to clarify the mandate and the tools to better monitor its implementation. The health reform will serve to ensure that adequate primary health care is institutionalized in the system, ensuring that those more vulnerable enjoy sustainable health services.

5.2 Environmental Aspects

75. **Policy actions supported by this DPL are unlikely to have any negative effects on the country's environment and natural resources.** Reforms supported by the proposed operation are not directly or indirectly linked to environmental aspects.

5.3 PFM, Disbursement, and Auditing

76. **Seychelles' fiduciary framework is adequate for supporting the proposed operations.** Seychelles' fiduciary framework is strong, and is reflective of improvements in the country's PFM system, as noted in the latest PEFA report (2011) and results of implementation of the PFM Action Plan (2012-2014); and the overall fiduciary risk is assessed to be low. Seychelles' budget information is transparent and access to key fiscal information, such as budget documents, is freely available to the public on a timely basis. To address the weaknesses identified in the report, the government designed and has been implementing a 2012-2014 PFM action plan. Some of the achievements include: (a) The Public Finance Management Act was revised in 2012 to further strengthen budget processes including design, execution, and reporting; (b) implementation of PPBB to improve allocation of resources to priority areas and focus on results; and (c) preparation of the 2013 financial statement using cash-based International Public Sector Accounting Standards (IPSAS) which enhances the quality of financial information. To continue improving PFM systems, a new action plan is being developed. The IMF 2013 safeguard assessment report of the CBS concluded that the CBS's internal controls, financial reporting, and external audit and internal audit systems were adequate and aligned with international standards.³⁷ The report called for CBS to pay further

³⁷ The assessment found that the CBS has implemented the recommendations of the 2010 assessment, namely, it has strengthened its: (i) external audit mechanism (by approving a new auditor independence policy and proactively implementing external auditor's management letter issues); (ii) financial reports, which are now prepared in line with International Financial Reporting Standards and audited by an independent audit firm using international standards of auditing; and (iii) legal framework.

attention to developing and implementing a risk-based internal audit methodology and filling vacant staff positions. The CBS has committed itself to addressing the identified weaknesses in order to improve the safeguard environment. The CBS's operations are reflected transparently in its audited financial statements.³⁸

77. Loan disbursement will follow the World Bank's disbursement procedures for development policy lending. Specifically, the loan will be disbursed in a single tranche upon effectiveness of the Loan Agreement and subject to the satisfactory implementation of the program and to the appropriateness of the country's macroeconomic policy framework. The loan proceeds will be credited to an account that forms part of the country's official foreign exchange reserves at the Central Bank of Seychelles (CBS). The CBS will credit the Seychelles rupee equivalent to the MoFTBE treasury Account to finance government budgeted expenditures. The CBS will not impose any charges or commission on the government for these transactions. The government, through the MoFTBE, will provide written confirmation to the World Bank within 30 days of disbursement that: (i) the loan proceeds were received into an account of the government that is part of the country's foreign exchange reserves, indicating the date and the name/number of the government's bank account in which the amount has been deposited; (ii) an amount equivalent to the credit proceeds from the World Bank has been credited to the treasury account along with an indication of the exchange rate applied; and (iii) the Seychelles rupee equivalent of the credit proceeds was recorded as financing the government budget (including the CoA name/account number, the date, and the exchange rate used). The conversion from US dollars to Seychelles rupees will be based on the prevailing exchange rate on the date that the funds are credited to the treasury account. The loan proceeds shall not be used to finance excluded expenditures as defined in the Appendix of the Loan Agreement. If any portion of the loan is used to finance ineligible expenditure as so defined, the World Bank shall require the government to promptly refund the amount upon notice from the World Bank. Amounts refunded to the World Bank upon such a request shall be cancelled. The accounting of the loan proceeds will be the responsibility of the Comptroller General at the MoFTBE. Government procedures will be followed to administer, record, and audit transactions relating to the loan proceeds and related payments. Upon the Bank's request, the Borrower shall: (i) have the Deposit Account audited by independent auditors acceptable to the Bank, in accordance with consistently applied auditing standards acceptable to the Bank; (ii) furnish to the Bank as soon as available, but in any case not later than four months after the date of the Bank's request for such audit, a certified copy of the report of such audit, of such scope and in such detail as the Bank shall reasonably request; and (iii) within thirty (30) days of such deposit, the Recipient shall provide a written report to the Association of the amount deposited in the Deposit Account and credited to the Recipient's budget-management system. Since the control environment in the CBS is considered to be adequate, no additional fiduciary requirements shall apply. The closing date of the Loan is December 31, 2016.

5.4 Monitoring and Evaluation

78. The results framework presented in Annex 1 of this document will be used as a monitoring tool by the Government of Seychelles and the World Bank. The government and the World Bank will review the progress of the DPL program twice a year, and Aide

³⁸ Since the 2009 financial year, the CBS's financial statements have been prepared in accordance with international financial reporting standards, and they are available on the CBS website up to December 31, 2013.

Memoires will be prepared to monitor progress. The MoFTBE will be responsible for the overall coordination and monitoring of the reform program supported by the DPL and will furnish information to the World Bank, as required, to monitor outcomes in the results framework. The MoFTBE will liaise with focal points in the other ministries, departments, and agencies involved as needed. Periodic monitoring and dialogue with the relevant line ministries and other stakeholders involved in implementing the reforms will take place through World Bank field missions.

79. **Grievance Redress.** Communities and individuals who believe that they are adversely affected by specific country policies supported as prior actions or tranche release conditions under a World Bank Development Policy Operation may submit complaints to the responsible country authorities, appropriate local/national grievance redress mechanisms, or the WB's Grievance Redress Service (GRS). The GRS ensures that complaints received are promptly reviewed in order to address pertinent concerns. Affected communities and individuals may submit their complaint to the WB's independent Inspection Panel which determines whether harm occurred, or could occur, as a result of WB non-compliance with its policies and procedures. Complaints may be submitted at any time after concerns have been brought directly to the World Bank's attention, and Bank Management has been given an opportunity to respond. For information on how to submit complaints to the World Bank's corporate Grievance Redress Service (GRS), please visit <http://www.worldbank.org/GRS>. For information on how to submit complaints to the World Bank Inspection Panel, please visit www.inspectionpanel.org.

6. SUMMARY OF RISKS

80. **Table 5 summarizes the ratings for 9 risk categories according to the Systematic Operational Risks-rating Tool (SORT).** The overall risk rating of this operation is "low" in light of the risks and mitigating factors. The following discusses the most relevant risks that could impede the achievement of the intended outcomes as stated in the program development objective, include the following: (a) political and governance, (b) macroeconomic, and (c) institutional capacity for implementation and sustainability.

81. **Political and Governance (moderate):** The government has shown remarkable leadership in pursuing the reform agenda, and substantial results have already been achieved as part of the implementation of the previous DPL series and IMF EFF. Risks associated to upcoming elections in 2016 are mitigated as the new cabinet appointed in January 2015 has committed to maintaining a stable macroeconomic framework and continue the structural reforms.

82. **Macroeconomic (moderate):** Macroeconomic risk is moderate. Seychelles has relatively high debt levels, small size, dependency on the global environment, and limited risk diversification options. The major risk is related to the uncertain developments in the euro zone to which Seychelles is highly exposed through tourism and FDI, which present a threat on economic growth and the fiscal position and financing the current account deficit. The government has a reasonable number of tools to cope with these external economic uncertainties and to maintain a stable macroeconomic environment for the implementation of this program. In the short term, the current level of international reserves (4 months of imports) provides some buffer against any potential deterioration in the balance of payments. In the

medium term, the floating exchange rate facilitates the correction of external imbalances. On the fiscal front, significant treasury deposits in the central bank could sustain public expenditure in the short term as needed.

83. **Institutional capacity for implementation and sustainability (moderate):** Risks associated with limited capacity to implement the reforms, especially in sector ministries, is being overcome by substantial technical assistance provided in parallel, including through reimbursable technical assistance.

Table 5: Seychelles - The Systematic Operational Risks-rating Tool (SORT)

Risk Categories	Rating (H, S, M or L)
1. Political and governance	M
2. Macroeconomic	M
3. Sector strategies and policies	L
4. Technical design of project and program	L
5. Institutional capacity for implementation and sustainability	M
6. Fiduciary	L
7. Environment and social	L
8. Stakeholders	L
9. Other	-
Overall	L

Annex 1: Policy and Results Matrix

Prior action	Results
Pillar 1: Raise efficiency of expenditure	
Prior Action 1: The Borrower's Cabinet has approved a strategic plan and action plan for its agency responsible for social protection and transferred the ministerial responsibility for said agency to its minister responsible for social affairs.	Indicator: Total spending on social assistance as % of GDP. Baseline (2014): 3.2% of GDP Target (December 2016): 3% of GDP
Prior Action 2: The Borrower had expanded the coverage of the agency responsible for social protection's management information system to include the data on applicants and beneficiaries of its sick leave benefits.	Indicator: Spending on sickness benefit Baseline (2014): 0.07 % of GDP Target (December 2016): Spending on sickness benefit decreases by 15 % to 0.06 % of GDP
Prior Action 3: The Borrower's Cabinet has approved the National Health Policy.	Indicator: Percent of health budget allocated to prevention and promotion services. Baseline (2014): 6 percent; Target (December 2016): 9 percent
Prior Action 4: The Borrower's Cabinet has approved a memorandum for a comprehensive teacher management policy reform focusing on issues of teacher distribution, training, career, and performance.	Indicator: Teacher attrition as percent of total number of teachers Baseline (2014): 11 percent Target (December 2016): 7 percent
Pillar 2: Facilitate access to credit	
Prior Action 5: The Borrower's central bank has promulgated regulations to ensure that credit data is reported on event-basis.	Indicator: Number of credit reports issued per day Baseline (2014): 120; Target (December 2016): 250
Prior Action 6: The Borrower's Cabinet has approved for submission to the Borrower's National Assembly a Secure Transaction Bill.	Indicator: Number of lenders connected to collateral registry Baseline (2014): 0; Target (December 2016): 15
Pillar 3: Improve Public Investment	
Prior Action 7: The Borrower has established a committee for independent review and selection of public investment projects, appointed the relevant staff for the purpose of said committee's operations and the Borrower's Cabinet has approved the guidelines for preparation and appraisal of public investment projects.	Indicator: Number of projects above 10 million rupees approved by the Development Committee Baseline (2014): 0 Target (2017 public budget): All
Prior Action 8: The Borrower has approved a revised mandate for <i>Société Seychelloise d'Investissement</i> , in a manner that clearly defines the unique objectives and activities of the institution in relation to the Borrower's other similarly-situated institutions, all in line with good international practice on corporate governance of state-owned enterprises.	Indicator: Number of SOEs under SSI's purview which have reached their financial and non-financial performance indicators as agreed between SSI, PEMC and the SOE. Baseline (2014): none; Target (December 2016): Two-thirds of SSI portfolio companies

Annex 2: Letter of Development Policy



Republic of Seychelles Ministry of Finance, Trade and the Blue Economy

The Minister

7th September, 2015

Mr. Jim Yong Kim
President
The World Bank Group
Washington DC

Dear Mr. Kim,

1. On behalf of the Government of Seychelles, I hereby write to request the approval for the Sustaining Reforms for Inclusive Growth Development Policy Loan to the Republic of Seychelles. The objective of this development policy loan is to raise efficiency of public expenditure and improve the business environment. To achieve these objectives, this operation supports actions that will: (i) raise efficiency of public expenditure; (ii) facilitate access to credit; and (iii) improve public investment.
2. In 2008 we started the reform process and it is encouraging to see that seven years later the broad based support for the process still exists and continues to be strengthened. The private sector and the civil society on their part continues to play an important role in the process, thereby keeping our progress on the right trajectory. The international community, especially our development partners continues to equally extend their support to us through budget support and technical assistance in various areas.

I. SEYCHELLES REFORM PROGRAM

I.1 Overview

3. The core aim of Seychelles development remains the need to reduce its vulnerability and ensure long-term sustainable and inclusive development. In order to maintain the gains we have achieved so far the overarching goal of Seychelles' fiscal policy remains to put public finances on a sustainable path, while creating the fiscal space to raise public investment and support targeted social safety nets.

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4. 2014 has been a very challenging year for us especially with regards to the macroeconomic performance, principally in the balance of payments area. An increase in public sector wage coupled with the acceleration in credit to private sector contributed to an increase in import in the third quarter while a decline in tourism earnings further contributed to the pressures in the foreign exchange market. The Central Bank of Seychelles (CBS) tightened its monetary policy during the second half of 2014, to mitigate some of the foreign exchange pressure. The 2014 real GDP growth rate, at 3.3 %, was to some extent higher than projected, while the decline in international petroleum prices resulted in an almost stable consumer price index in the 12 month to end- December 2014.
5. On the budget side, we achieved a higher primary surplus target than programmed (4.6% of GDP as against 4.4% programmed), driven by strong revenue collection.
6. We remain committed to our strategy of reducing public debt to build the country's resilience. Due to the strong fiscal performance and GDP growth forecast in the medium term, public debt is expected to be reduced below 50% of GDP in 2018. One of the key debt management goals is to smooth out the external debt service profile and shift public borrowing to local currency wherever possible.
7. In February 2015, Paris Club creditors with the participation of South Africa agreed to an early repayment scheme for the debts of Seychelles rescheduled by the Paris Club in 2009, in support of marine conservation efforts. The transaction will enable Seychelles to buy back a portion of the debt maturities falling due to the Paris Club between 2015 and 2021 at a 5% discount to face value.
8. We are pleased to report that the implementation of the program supported by the Extended Fund Facility approved by the Executive Board of the IMF in June 2014 is on track as we continue to perform well on our agreed reform program.

II. MAIN ELEMENTS OF POLICY REFORMS

9. To sustain the achievements of the economic reform program and address the remaining challenges we will continue strengthening the institutional and governance framework in critical areas such as public finance management, public enterprise monitoring, and the investment climate among others.

1. Fiscal Policy

10. The 2015 budget aims at achieving a primary surplus target of SR 720 million which is equivalent to 3.7% of projected GDP. Following the strong performance of consumption taxes in 2014, we aim to strengthen revenue performance in 2015, particularly in the area of business tax, and to that end we are taking a number of measures which include: (i) on line submission of tax returns and expanded e-payment facilities; (ii) strengthening capability to analyze transfer pricing; (iii) conducting 60 audits of large businesses, with the assistance of externally recruited auditors, and using a risk management

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process to prioritize audits (SB); (iv) improve collection of tax arrears; (v) improving customs compliance; (vi) simplifying procedures of excise tax collection at customs.

11. The Seychelles Revenue Commission (SRC) is undertaking a wide-ranging action plan for the improvement of compliance level and to enhance revenue collection for 2015. This includes the introduction of online submission of Business Tax Returns and expanding e-payment facilities, which became operational in April 2015.

2. Public Financial Management Reforms

Since 2008, when we started the reform process strengthening the Public Financial Management Framework and the budgetary process has been and remains one of our key objectives.

MTFF (Medium Term Fiscal Framework)

In November 2014, the Medium Term Fiscal Framework benchmark was approved by the Cabinet of Ministers and the 2015 budget was formulated on this basis for the first time. This will assist in establishing the indicative Budget ceilings over a five year period. A Fiscal working group has been established, comprising of members from the Ministry of Finance, Trade & the Blue Economy to ensure the consistent updating of the MTFF variables.

PPBB (Program Performance Based Budgeting)

In 2015, the Program Performance Based Budgeting (PPBB) has been adopted for the first two pilot Ministries. In addition three other pilot ministries and their related agencies have also joined the piloting process with continued technical assistance from the World Bank.

PFM Action Plan (Public Financial Management)

The government has adopted a new PFM Action plan for the period 2015-2018. The updated plan is targeting improvement in capital project, cash and asset management and aid to an improved medium term budget framework (MTBF). One of the key objectives of the PFM Action plan is to enhance transparency and governance, enhance the efficiency of State Owned Enterprises in the delivery of public services, strengthen SOE credit worthiness and returns on investment and reduce SOE contingent liabilities on the state budget. A Public Expenditure and Financial Accountability (PEFA) also is also expected to be carried out in the second half of 2015.

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PIM

Although we have made considerable progress in the PFM area since 2008, we still lacked a systematic approach to capital budgeting and most areas and components of the capital expenditure process needed to be developed further. There has been a lack of project selection criteria, formal guidelines for preparation of feasibility studies of public projects and project appraisal.

In March 2015, a Development Committee was appointed in to ensure that all public sector capital projects over R10 m in the Public Sector Investment Program (PSIP) are coordinated and appraised before final Government approval and funding is catered. In addition to the establishment of the Development Committee we have adopted guidelines for public investment and maintenance (*prior action 7*). To improve service delivery, all project officers and decision makers will be given the appropriate training to ensure that there is a coordinated approach to capital project management.

Cash Management

The government will further re-enforce the Treasury single account (TSA) by improving the reporting of all balances of commercial bank accounts outside of the TSA. This will allow comprehensive reporting of all commercial bank balances held by the MDAs and subordinate agencies through Quarterly reconciliation of all government's budget dependent entities commercial bank accounts which is to be submitted to Treasury. This will facilitate annual reporting of the government financial statement as all such accounts will be captured and account balances disclosed.

Public Private Partnership (PPP)

Development of a Public Private Partnership Framework

The Government remains committed to putting in place a comprehensive Public Private Partnership (PPP) framework to support the transition of the Seychelles economy towards greater private sector participation and economic contribution. The framework also aims at ensuring value for money from PPPs as well as limiting fiscal risks. The first phase for the development of the framework which is the preparation of a PPP policy has been completed with the assistance of the Investment Climate Facility for Africa (ICF) in collaboration with the African Development Bank. The policy sets clear country definition of PPP, sectoral coverage as well as clear guidelines and principles for the implementation of PPP projects in Seychelles. The next phase is the development of the PPP Legal Regulatory and Operational framework with technical assistance from the Bank.

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3. Efficiency of Public Expenditure

12. In order to sustain the reforms implemented so far and achieve our target of 50% of GDP in 2018 we recognize the work that needs to be done to ensure efficiency of public expenditure. Since 2008 the Bank has assisted us on various occasions to carry out public expenditure reviews in the social sector more specifically focusing on education, health and social protection. Going forward the government will be focusing on public investment management which is one area of PFM which is still lagging behind and needs to reform. Currently there is weak budgeting that impacts the quality of overall PIM. There is low efficiency of public investment that has manifested in a number of dimensions including delays and incompleteness of projects.
13. In the area of social assistance, the Government remains committed to reforms which will contain cost and improve efficiency, in line with the engagements made in the previous DPL series the World. Going forward, we note that the overall spending on social assistance has been on the increase and the government is committed to controlling such cost and raise the efficiency of social assistance.

Further to technical assistance from the World Bank we have been able to identify the cost drivers and challenges. One such challenge is the significant fragmentation in the social assistance sector. There are numerous legislations and social assistance programs. In order to address this issue of fragmentation, the government has clarified ASP multiple reporting lines to reinforce accountability over social security and social assistance programs. The Social Security Act gave responsibility to the Minister responsible for Finance for oversight of the Social Security Act. The Agency for Social Protection Act established the ASP and mandated it to administer social security benefits (formerly contributory) and social welfare programs. The ASP Act gave portfolio responsibility for the agency and its welfare programs to the Minister in charge of Social Affairs. To clarify and streamline this and to improve the coherence and efficiency of social protection, the ASP ministerial responsibility has been transferred to the Minister responsible for Social Affairs and the Government has approved a strategic plan (2015-2018) and action plan for the ASP (*prior action 1*). The strategic plan will be implemented in broad areas (immediately, short term, long term arrangements) and operationalized through annual operational plans. A set of core indicators will be agreed for required monitoring and reporting.

14. In continuing to improve control of social assistance the monitoring and evaluation (M&E) capacity of the ASP will be upgraded. The ASP currently has limited capacity to monitor and evaluate programs and to use this information for policy making. As you will recall, one reform supported by the past DPL series is the reduction in the number of sick leave days reimbursed by ASP. The implementation process has been challenging due to the fact that ASP lacked an automated database of applicants and beneficiaries. I am pleased to confirm that the coverage of ASP's Management Information System (MIS) has been broadened to include the sickness benefit, which will facilitate monitoring of the sick leave program (*prior action 2*).
15. To date the World Bank has assisted us with two public expenditure review exercises in the health sector. While the review exercises shows that the health system has delivered for what it is designed (i.e. primary health care), further reforms to address the new emerging needs are required. In addition, there

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is a need to put in place strategies to contain cost as health sector spending continues to substantially increase and pressure will continue given the expensive tertiary care for aging population and treatments for non-communicable disease.

16. To address these challenges and ensure sustainability there is a major modernization effort in the health sector and to this end government has adopted a National Health Policy (*prior action 3*).
17. Similarly in the education sector substantial progress has been made over the years although major challenges remain with regards to quality. In order to address this challenge it is imperative that we address the issue of teacher capacity and retention. This is also a key priority in the medium term strategy for the education sector. As a first step the government has approved a Memorandum establishing the principles of a comprehensive teacher management policy (*prior action 4*). The policy framework once developed will detail priority measures and interventions to address the many inter-related dimensions in the teaching profession in a more coherent and systematic manner. It will also consider other emerging issues and internal instruments that have a bearing on the teaching profession. The policy framework will be implemented over a 3 year period, 2015-2017.
18. SOE governance remains a priority on our agenda of reforms. We have received support from the World Bank in previous DPL and I am pleased to advise that we have made progress in addressing SOE governance. However we recognize the need to further clarify and reinforce SOE supervision. The mandate of the Société Seychellois d'investissement (SSI) has now been clarified through its mission statement (*prior action 8*). With a revised mandate SSI will now be able to better manage fiscal risks by close monitoring of and independent analysis of companies in the portfolio.
19. Going forward the Government will further focus SSI mandate by developing a shareholder policy, an investment strategy and operating guidelines.

4. Private Sector Developments

20. The promotion of competition and increased private sector involvement in key sectors remain one of our key priorities, in line with the government's commitment to sustained and inclusive growth and improvement in the investment climate. The development of e-services remains high on our agenda as we keep striving to improve the investment climate, increase efficiency and improve service delivery. One of the measures identified to assist in the process is the creation of a centralized electronic collateral registry. The absence of a secured lending system and the necessary legal framework is a major constrain for additional lending to the private sector.
21. The Central Bank of the Seychelles (CBS), with the assistance of the World Bank, has embarked on a comprehensive reform to put in place a modern secured lending system and a collateral registry for movable property. The government has recently approved a Secure Transaction Bill which will now be submitted for submission to the National Assembly (*Prior Action 6*).
22. In pursuing the improvement of the investment climate, we note that access to credit has been one of

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the most challenging issues. In 2012, the Central Bank of Seychelles launched the Credit Information System, which is the only credit reporting mechanism in Seychelles. The on-line system provides for licensed commercial banks and other regulated financial entities to access credit reports. However the CIS is still incomplete and only caters for the introduction of credit reporting. While this is useful for lending as well as for loan classification and provisioning, there is the need to upgrade it to improve data quality and completeness, and enable wider participation to effectively assist banks and other lenders in their credit risk assessments.

23. In order to address some of the limitations of the current system, the CBS has adopted regulations to ensure that institutions under its purview report more frequently to the CIS. Reports is now event-based rather than monthly (*prior action 5*) and the reports will also show specific repayment features.

Conclusion

24. As the above indicate, the Government of the Republic of Seychelles is strongly committed to undertaking necessary reforms to promote economic growth modernize our country and raise efficiency of public expenditure and improve the business environment. In this context, the support of The World Bank through approval of the Development Policy Loan would be important to successful implementation of the government's continued reform agenda and its quest to become more resilient.
25. Accordingly, the Government of the Republic of Seychelles requests that Development Policy Loans be approved.

Yours sincerely



Jean Paul Adam

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Annex 3: Fund Relations Annex

IMF Executive Board Concludes 2015 Article IV Consultation with Seychelles

Press Release No. 15/294

June 23, 2015

On June 17, 2015, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with Seychelles.

Macroeconomic outcomes remain solid, and most of the external pressures experienced in 2014 have abated. Weakness in the main exports combined with strong domestic demand in 2014 led to depreciation pressures on the exchange rate. Beginning in late 2014, tighter monetary policy, a recovery in tourism, and falling global fuel prices, together with the effects of the depreciation on imports, helped to contain the external pressures. The combination of spending discipline and buoyant fiscal revenues—driven by strong imports—resulted in a primary surplus of over 4½ percent of GDP in 2014, exceeding the target. However, disappointing tourism arrivals ensured that growth remained subdued in 2014. Financial sector soundness indicators remain in the comfortable range; the Central Bank of Seychelles had to take management control of a small off-shore bank in October 2014 after it lost its correspondent relationship, but there should be no significant repercussions on Seychelles' economy.

With a continuing recovery in tourism and the effect of lower fuel prices, projected growth for 2015 is slightly higher than earlier envisaged at 3½ percent; the exchange rate has recovered modestly against the dollar. The depreciation began to pass through to inflation, reaching 4.0 percent in May 2015 (year-on-year). The large current account deficit in 2014 is expected to contract sharply in 2015, helped by monetary policy tightening and lower fuel prices. In addition to a decline in FDI-related imports, import demand will be restrained by the depreciation, continued tight monetary policy, and a tight public sector wage round.

Executive Board Assessment

Executive Directors agreed with the thrust of the staff appraisal. They commended the authorities for the strong implementation of their Fund supported economic program, notwithstanding a difficult external environment. The growth outlook is favorable, but the economy remains vulnerable to global developments while domestic risks are linked to state owned enterprises. Against this background, Directors underscored the importance of continued sound policies and structural reforms to strengthen macroeconomic and financial stability, build policy buffers, and foster sustained and inclusive growth.

Directors welcomed the authorities' commitment to reducing public debt below 50 percent of GDP by 2018. They observed, however, that achieving this target while continuing to address critical infrastructure needs will require improving revenue mobilization and spending efficiency in the context of a sound medium term budget framework.

Directors considered that the authorities' tight monetary stance has been appropriate in light of the recent external pressures and the rapid credit growth. Noting the risks to financial and macroeconomic stability that continued credit expansion would entail, Directors welcomed the authorities' commitment to develop macro prudential tools and stressed the need for a determined implementation of reforms in this area.

Directors welcomed plans to develop a more forward looking monetary policy framework, based on liquidity and inflation forecasting and a strong coordination with the fiscal authorities. Directors encouraged the authorities to further strengthen international reserves while maintaining appropriate exchange rate flexibility, which has served the economy well.

Directors noted that the fragile financial situation of some state owned enterprises represents a significant fiscal risk. Accordingly, they encouraged the authorities to push ahead with their strategy to strengthen governance and performance of public enterprises. Directors also stressed that any new expansions of state owned enterprise operations or mandates should be carefully vetted and based on a strong and clear rationale for public sector involvement.

Directors agreed that further reforms are necessary to promote a dynamic private sector. They supported measures to further improve the business and investment climate, including by opening up key sectors so far protected from competition. Addressing skills mismatches in the labor market remains an important policy priority.

Directors welcomed Seychelles' subscription to the IMF's Special Data Dissemination Standard and its recent accession to the World Trade Organization.

Seychelles: Selected Economic and Financial Indicators, 2012–18

	2013		2014		2015		2016	2017	2018
	Prel.	Est.	1 st Rev.	Est.	1 st Rev.	Proj.	Proj.	Proj.	Proj.
National income and prices									
Nominal GDP (millions of Seychelles rupees)	15,544	17,015	18,342	18,133	19,539	19,168	20,434	21,796	23,233
Real GDP	6.6	6.0	2.8	3.3	3.0	3.5	3.7	3.6	3.5
CPI (annual average)	7.1	4.3	2.3	1.4	5.2	4.3	2.9	3.0	3.0
CPI (end-of-period)	5.8	3.4	4.8	0.5	2.5	4.9	3.8	2.5	3.3
GDP deflator average	10.5	3.2	2.5	3.1	3.4	2.1	2.8	3.0	3.0
Money and credit									
• Broad money	-0.6	23.7	12.0	17.5	5.3	5.7	...	...	...
• Reserve money (end of period)	6.9	15.4	16.5	13.9	5.6	8.0	...	...	...

Seychelles: Selected Economic and Financial Indicators, 2012–18

• Reserve money (average of last quarter)	...	...	-17.4	-14.5	5.6	2.1	...	...	...
• Velocity (GDP/broad money)	2.1	1.8	1.8	1.7	1.8	1.7	...	...	...
• Money multiplier (broad money/reserve money)	4.2	4.5	4.3	4.6	4.3	4.5	...	...	...
• Credit to the private sector	8.5	4.5	15.2	25.2	3.3	12.4	...	...	...
Savings-Investment balance									
External savings	19.9	11.5	22.5	21.0	20.5	15.2	14.6	15.0	13.6
Gross national savings	17.5	26.5	14.7	16.3	15.2	18.6	19.4	18.6	18.7
<i>Of which:</i> government savings	8.6	5.2	6.1	6.6	6.1	5.4	7.5	7.9	9.5
Gross investment	37.4	37.9	37.2	37.3	35.8	33.7	34.1	33.5	32.3
<i>Of which:</i> public investment ¹	10.4	8.9	6.2	6.3	6.8	6.7	6.8	6.6	7.0
Government budget									
Total revenue, excluding grants	34.2	31.9	31.6	32.4	31.0	31.6	31.4	31.3	31.4
Expenditure and net lending	36.1	36.0	32.3	32.7	32.6	33.6	32.0	31.6	31.2
Current expenditure	25.7	26.7	26.1	26.5	25.8	26.8	25.3	24.9	24.2
Capital expenditure	10.4	9.3	6.2	6.3	6.8	6.7	6.8	6.6	7.0
Overall balance, including grants	2.2	0.3	2.1	2.0	0.3	0.3	1.2	1.4	1.5
Program primary balance	5.7	4.6	4.3	4.6	3.7	3.8	3.8	3.8	3.8
Total public debt	77.1	64.1	64.9	65.3	62.3	63.7	59.5	54.7	49.9
Domestic ²	32.0	27.2	28.2	29.9	23.8	25.1	23.0	20.5	17.1
External	45.1	36.9	36.7	35.5	38.5	38.6	36.5	34.3	32.8
External sector									
Current account balance including official transfers	-19.9	-11.5	-22.5	-21.0	-20.5	-15.2	-14.6	-15.0	-13.6
Total external debt outstanding (millions of U.S. dollars) ³	1,556	1,583	...	1,670	...	1,788	1,881	2,010	2,123
(percent of GDP)	137	112	...	117	...	130	128	129	129

Seychelles: Selected Economic and Financial Indicators, 2012–18

Terms of trade (- =deterioration)	-0.1	-0.2	-0.6	2.0	0.8	12.0	-3.4	-1.5	-0.6
Real effective exchange rate (average, percent change)	-0.8	17.9	0.0	-2.8	...	...	...	...	...
Gross official reserves (end of year, millions of U.S. dollars)	307	425	452	463	453	463	476	505	521
Months of imports, c.i.f.	2.8	3.7	4.1	4.6	4.0	4.3	4.2	4.3	4.2
Exchange rate									
Seychelles rupees per US\$1 (end of period)	13.0	12.1	13.3	14.0	...	...	...	...	...
Seychelles rupees per US\$1 (period average)	13.7	12.1	12.6	12.7	...	...	...	...	...

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

¹Includes onlending to the parastatals for investment purposes.

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

³ Includes private external debt.

