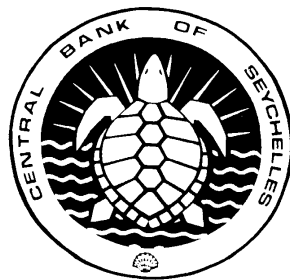




CENTRAL BANK OF SEYCHELLES

ANNUAL REPORT 2004

CENTRAL BANK OF SEYCHELLES



ANNUAL REPORT

2004

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Letter of Transmittal

Central Bank of Seychelles
P.O. Box 701
Victoria

March 15, 2005.

President J. A. Michel
State House
Victoria

Dear Mr. President,

I have the honour to submit for your approval the First Annual Report of the Central Bank prepared in accordance with Section 47(4) of the Central Bank of Seychelles Act, 2004, together with a copy of the Annual Accounts for 2004 certified by the Auditors.

Yours faithfully,

A handwritten signature in blue ink, appearing to read 'F. Chang Leng', with a horizontal line underneath.

F. Chang Leng
Governor

CENTRAL BANK OF SEYCHELLES

Board of Directors

(as at 27th December 2004)

Francis Chang Leng	-	Governor & Chairman
Errol Dias	-	Member
Francis Chang-Sam	-	Member
Ronny Govinden	-	Member
Vivianne Fock-Tave	-	Member

Secretary to the Board

Jean-Claude d'Offay

Board of Directors

(as at 31st December 2004)

Francis Chang Leng,	-	Governor & Chairman
Errol Dias	-	Member
Francis Chang-Sam	-	Member
Jean Weeling-Lee	-	Member
Wilfred Jackson	-	Member

Secretary to the Board

Jean-Claude d'Offay

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Technical Note

Owing to rounding of figures, the sum of separate items may not always add up to the total shown. Abbreviations used in this Report are:

R = Seychelles Rupee

CBS = Central Bank of Seychelles

n.a = Figure not available

.. = Negligible

-/0 = Nil

SECTION ONE

Highlights of the Seychelles Economy

Overview

Strong recessionary conditions continued to persist in the domestic economy during 2004. As a result, economic activity slackened, particularly in the productive sectors of tourism, fisheries and manufacturing, leading to a further contraction of 2.0 per cent in real GDP. Whilst concrete gains were made in fiscal consolidation, the depth of the underlying macroeconomic imbalances were such that no visible relief was reported in the external sector, which continued to be hamstrung by shortages in foreign currency.

The overall balance of payments deficit for the year widened from R181 million in 2003 to R345 million, financed by a R181 million draw down on reserve assets and a build-up in external arrears of R164 million. In general, developments in the external environment were unfavourable for the country; soaring oil prices caused a 49 per cent hike in the country's oil import (f.o.b.) needs to R455 million whilst the continued strength of the euro adversely affected the competitiveness of the tourism sector¹ relative to the Caribbean

and other similar jurisdictions, which traditionally price their products in US dollars. Towards the end of December, economic activity was further disrupted by the considerable damages inflicted by the Tsunami and ensuing floods.

Notwithstanding the decline in real GDP, M2(p), the broadest measure of the monetary aggregate, posted a growth of 1.1 per cent to reach a record R4,274 million. Still, this constitutes a welcome deceleration in the growth of money and is just under the 1.8 per cent expansion in nominal GDP and well short of the reported 3.9 per cent increase in the Retail Price Index (RPI).

Against the above backdrop, the year closed with the gross official external reserves declining to R190 million (US\$35 million); on a net basis however, reserves strengthened appreciably from minus R323 million at end-December 2003 to minus R304 million reflecting in some measure the sizeable repayments made on the Tokyo-Mitsubishi Syndicated loan contracted by the Central Bank in 2002.

¹ Seychelles depends predominantly on the European markets for its tourists and the practice in the trade is to fix the prices of tourism packages a year in advance (normally October/November) in euros. In contrast to Seychelles, the tourism currency for Caribbean destinations is usually the US dollar; thus a weakening of the dollar relative to the euro, improves the competitiveness of these countries relative to Seychelles.

Important Policy Initiatives during 2004

Business confidence, which was at historic lows, strengthened somewhat in the year as government ratified its commitment to fundamental economic reforms, privatisation, trade liberalisation, improved governance and enhanced dialogue with the private sector. Two joint government-private sector economic forums were created, the first of which, is the Economic Committee, a technical body set up to study the economic state of the country and to recommend appropriate policy responses; and the second, the Joint Economic Council, a high-level consultative committee of government officials and the business fraternity, designed to promote greater dialogue and understanding on national economic and financial affairs.

In parallel to these important initiatives, various institutional reforms were implemented to improve the business climate and to unshackle businesses from excessive regulations and bureaucracy; an important development in this regard was the streamlining of investment approval process through the creation of the Seychelles Investment Bureau (SIB) under the direct authority of the President's Office. As a major comfort to investors, one of the SIB's first pronouncements was to introduce an Investment Code for Seychelles, as an instrument to safeguard investors' interests and provide robust mechanisms for arbitration in case of disputes.

In the interest of instilling greater transparency in government procurements and privatisation initiatives, a National Tender Board was established. In addition, the authorities declared their plan to move away from direct controls and regulation of trade. Effectively, as of July 1, the monopoly right of SMB was reduced to only seven categories of commodities. This was followed by the announcement that from the same date, imports of goods for personal use would not require an import permit, provided the items do not fall in the category of offensive, restricted or illegal goods.

After months of deliberations, the government enacted legislations to set up a Port Authority with the clear mandate of commercialising the activities of Port Victoria in order to maximise business potential. It is understood that the concept will be extended to the International Airport and in 2005 a Civil Aviation Authority is to be set up.

In the tourism sector, government intends to merge the activities of the Ministry of Tourism and those of the Seychelles Tourism Marketing Authority (STMA) in one body, the Seychelles Tourism Board. The new body will be headed by a board with strong private-sector representation and will focus at re-positioning Seychelles as a unique island destination offering value for money in accommodation and service quality levels.

Financial Sector Reforms

To further enhance and complement the other structural reforms that were being put in place, the government put forth new legislation for the financial system. The National Assembly repealed the Central Bank of Seychelles Act 1982 and replaced it with the Central Bank of Seychelles Act 2004, thus formally bestowing the institution with a high degree of autonomy in the conduct of its operations. At the same time, a new Financial Institutions Act was passed.

Under the new legislations, the Board of the Central Bank assumes full policy responsibility for the attainment of a number of macroeconomic objectives, amongst which is “to promote price stability and the maintenance of both domestic and external value of the Seychelles Currency”. Taking stock of the depth of the prevailing macroeconomic distortions, in particular the official domestic and external debt burden and the stock of commercial arrears, the Central Bank has a formidable task at hand.

To enhance the effectiveness of monetary policy instruments, the Bank’s immediate priority is to rapidly rebuild confidence in the domestic currency and ensure that economic agents willingly hold it as a store of value - and not as is presently the case, simply a medium for facilitating transactions. This will require a radical re-assessment of interest rate policy and the prevailing foreign exchange controls within the overall framework of the government’s economic restructuring programme. In parallel, there is an urgent

need to reduce the high costs of financial intermediation in the banking sector, a situation that has admittedly arisen out of past Central Bank prescriptions on banks’ lending portfolios and the stringency in the foreign exchange situation promulgated by adherence to a non-market clearing exchange rate.

In January 2004, the Central Bank reversed its earlier policy on the issuance of Seychelles government treasury bills through a tap arrangement, in favour of a tender system. Within the scope of significant money market rigidities elsewhere in the financial system, this development was admittedly a small step in reinstating market forces in the determination of domestic interest rate; but symbolically, it gave strong signals of the Central Bank’s future policy direction in monetary management. In the same vein, the re-introduction of the Foreign Exchange Pipeline Payments Scheme backed by a 100 per cent cash margins for foreign exchange applications by all parties, except designated small businesses, signalled the institution’s seriousness at regaining effective control over the growth of monetary aggregates.

With regards to external policy, the Central Bank is of the conviction that any new initiative in this domain must be taken in a measured and cautious way in view of the “macroeconomic overhang” associated with past policies; it continues to call for a balanced approach to economic adjustment, using all available policy instruments in a consistent, coherent and well-articulated manner.

The above stated and in acknowledgement of the economy's strong dependence on tourism, the Central Bank strongly believes that safeguarding social cohesion must be an important and integral part of any economic adjustment programme; as such, it will give its best endeavours to ensure that in the pursuit of its policy objectives, social costs are minimised.

Fiscal Developments

On the fiscal side, the Central Bank has carefully monitored the progress made in fiscal consolidation. It is of the view that the Macroeconomic Reform Programme (MERP) launched in July 2003 has successfully arrested the deterioration in the state of government finances. An overall surplus of R270 million was reportedly achieved in 2003 and another of R143 million in 2004. Even though in 2004, the outcome fell short of the budgeted level, the MERP has nonetheless stabilised the economy and set the platform for economic recovery, although somewhat paradoxically, it has done so by first unleashing recessionary forces in the productive sectors.

An analysis of the 2004 fiscal accounts clearly shows that fiscal consolidation was achieved on the strength of revenue from the Goods & Services Tax (GST) - introduced in July 2003 as the centrepiece of the MERP – even if the amount collected fell far short of budget. On the expenditure side, slippages under various cost centres amounting to R225 million were incurred, suggesting a need for stronger financial control. Overall however, the state

of government finances, as measured by the “primary balance”, which excludes interest service cost from the overall balance, appears relatively healthy with a surplus of R398 million, equivalent to 10 per cent of GDP. However, it is of consequence to note that this commendable outturn can be overwhelmingly eroded if domestic interest rates were to rise substantially next year with money market liberalisation.

External Sector Developments

In many ways, 2004 was a poor year insofar as export performance in goods and services is concerned. Following the introduction of the GST, all economic sectors, notably tourism, fisheries and industries, experienced significant increases in their operating cost base. This coupled with the maintenance of the existing foreign exchange regime, resulted in a marked decline in the international competitiveness of domestic goods and services. Tourism, the mainstay, recorded another consecutive year of decline in arrivals to about 121,000 visitors, although tourism income expressed in the amount converted into Seychelles rupees through the banking system, rose by 11 per cent to R756 million on account of the depreciation of the rupee against the euro, the principal tourism currency.

The Tourism Incentives Act 2003 (TIA), which came into force late last year, went some distance to compensate for the costs disadvantages of operating tourism business in the archipelago. However, the costs savings associated with its various concessions on

trades tax, business tax, gainful occupation permits (GOP) and employers' social security, were largely eroded by the cascading effects of the GST. In response to representations made by the trade, government amended the TIA in 2004, with the aim of improving concession levels and changing the GST base such that it applies on the concessionary trades tax level and excludes the statutory mark-up of 30 per cent. In December 2004, the President pledged to extend the concessions to the Agriculture and Fisheries sectors in 2005, an announcement that has been welcomed by operators, especially in the wake of the disruptions to activity caused by the tsunami and flood events towards the close of the year.

With regards to merchandise exports, 2004 was again a disappointing year with total proceeds falling by R82 million to R1,099 million, explained in large measure by declines in fresh/frozen fish and canned tuna exports. In contrast, merchandise imports grew by 9.7 per cent to R2,158 million, thus resulting in a wide trade deficit of R1060 million. Much of the increased imports can be attributed to the rise in petroleum prices, which caused fuel imports to escalate from R305 million last year to R455 million.

Real Sector Developments

The continued stringency in the foreign exchange situation and the GST had overall an adverse impact on manufacturing activity during 2004. In the case of the manufacturing sector, output of beers and soft drinks declined by 11 and 20 per cent respectively; whilst canned tuna production fell by about 5.0 per

cent. In other sectors, a mixed picture emerges with increases recorded in bottled water, juices, milk products, sauces and jams; and decreases in cigarette production, paints and allied products, processed meat and pasta.

In aquaculture, prawn production reached a high-point of 1,164 tonnes, representing a further increase over last year's bountiful harvests. Likewise, agricultural production of vegetables, fruits & root crops rose by 7.7 per cent to 4,581 metric tonnes whilst livestock output expanded by 6.0 per cent to 2,170 tonnes. In the fisheries sector, the tonnage of tuna fished in the country's EEZ amounted to 356,352 tonnes, an average annual outcome; more positively, the artisanal fishing sector posted a 14 per cent increase in catch to 4,374 metric tonnes.

With the economy in recession, employment levels witnessed a fall of 1.2 per cent to 41,1169 persons, the first decline in five years. All sectors – government, parastatal and private – recorded cutbacks in staffing, but the largest redundancies were recorded by the private sector. Overall however, the economy's wage bill increased as concurrently average monthly earnings rose by 3.8 per cent to R3,740 per month.

During the year, domestic inflation as measured by the Retail Price Index (RPI) surged by 3.9 per cent largely on account of the GST. Against the backdrop of declining real output, the emergence of inflationary tendencies suggests that the economy is drifting dangerously towards a state of

“stagflation” – to reverse the trend, immediate policy responses are called for.

Outlook for 2005

From various perspectives, the medium term prospects for the economy are highly encouraging. Yet, the Central Bank remains cautious in its assessment of the economic outlook for 2005. With the government’s continued commitment to fundamental economic adjustments, restructuring and liberalisation, steady gains are expected in critical economic aggregates.

On the whole, the Central Bank is satisfied that after years of fiscal and monetary lassitude, economic stabilisation is being steadily achieved. However, as the facts stand and despite recent fiscal gains, economic fundamentals, such as domestic and external public debt, monetary aggregates and domestic prices are still well outside prudent and/or sustainable levels. On the policy front therefore, despite the best intentions of policy, it is unrealistic to expect a radical improvement in the economic landscape, notably in the foreign exchange situation, in 2005.

Still, compared with previous years, it must be said that the economy is on the right adjustment track and following the submission of the findings of the Economic Commission and the regular visits of foreign economic missions, the authorities are now well briefed on the economic state of the country. This

places them in an informed position to make decisions regarding economic policy.

As the authority on economic and fiscal affairs, the Central Bank has an important responsibility to disseminate its know-how to the government and all economic stakeholders. In the course of 2005, the Bank must endeavour to extend its knowledge base by investing resources in researching areas of national significance, such as the growth dynamics of small island developing states (SIDs); the long-term viability of the tourism and fisheries sector; the economic consequences of trade liberalisation in the context of COMESA/WTO/LOME; and the welfare costs of protecting local industries.

In the course of 2004, the government took a bold supply-side policy initiative in regard to its civil aviation policy; it announced its agreement to liberalise air traffic to Seychelles by allowing Emirates and Qatar Airways to make high-frequency scheduled flights to the country despite the commercial concerns of Air Seychelles. As a result, the tourism industry will enjoy a 50 per cent expansion in seat capacity over Europe in 2005 and as the new services will hub over Dubai and Doha, improved connections for Eastern European tourists - especially Russians - to the country can be expected. On the downside, the increased airline capacity is unlikely to be matched by a corresponding expansion in arrivals overnight and as such, intense competition is expected in the airline business.

The adoption of a more open sky policy was welcomed by the tourism trade, although concerns remained about the lack of direct flights to key European cities, considered vital for the five-star market segments, and the financial future of the domestic carrier in a significantly deregulated environment.

The government has also demonstrated foresight in diversifying its foreign exchange revenue base through an offshore “tanker fleet” project, involving construction of three modern double-hull tankers by the German-based Lindenau Shipyard. The first vessel, “Seychelles Pride”, was launched in 2002 and is now in active and successful service with

the second tanker “Seychelles Pioneer”, due for delivery in April 2005. In that same month, the third tanker “Seychelles Progress” will be launched with commissioning scheduled for August 2005. Both new vessels have been designed to International Maritime Organisation (IMO) Class 2 standard, implying that they will have the capability of carrying both oils and certain chemical products. The fleet comes at a most opportune time when single-hull tankers are rapidly being phased out by international safety regulators, causing a major shortfall in the tonnage of tanker capacity globally. Against this background, the success of the Seychelles tanker fleet is almost certainly guaranteed.

SECTION TWO

Financial Survey

1. Overview

The year 2004 was marked by important developments in the monetary sector. Within the scope of the new approach to economic management, consensus was reached that in the interest of fundamental reforms, monetary policy must not be subordinated to fiscal policy; accordingly, a new Central Bank Act was passed which modernises the roles and functions of the Central Bank and extends a high degree of policy autonomy to the Board of the institution. In parallel, a revised version of the Financial Institution Act was enacted.

In early January, the Central Bank reversed its earlier policy of issuing government treasury bills on tap, in favour of a tender system. Within the context of serious market rigidities in the financial system, the impact of the changeover in reinstating market forces in the determination of interest rates was largely insignificant; symbolically however, it gave strong signals of the Bank's future direction in regard to monetary management. Of equal importance was the introduction of a revised Foreign Exchange Payment Pipeline Scheme, which compulsorily requires all requests for foreign exchange be backed by a 100 per cent

cash margin, except for requests lodged by small business operators. The objective of the measure was to tighten domestic liquidity, and more importantly, demonstrate to the market, the Central Bank's seriousness at regaining control over the movement of monetary aggregates.

With regards to the actual movements in the main monetary aggregates – namely credit and money supply – these were not, unlike earlier years, dominated by the financing operations associated with the fiscal accounts (*See Government Finance*). In 2004, the main impetus for monetary expansion came from private sector and parastatal credit which in combination surged by R211 million; reflecting the gains in fiscal consolidation, net claims on government actually fell by R172 million, thus partially neutralising the credit expansion of the other sectors. A strengthening in the country's net external asset position from minus R516 million to minus R415 million contributed positively to monetary growth, thus resulting overall in a 1.1 per cent expansion of the broad money aggregate M2(p), to R4,275 million.

Following the implementation of the revised Pipeline Scheme, the liquidity situation of the commercial banks tightened measurably as evident from an increase in their credit/deposit ratio from 109.2 in 2003 to 113 in 2004. Faced with this situation, the banks resorted to frequent use of short term borrowing facilities at the Central Bank to support their daily operations.

Paradoxically, despite the observed tightening in domestic liquidity, on a volume weighted basis, the average rates on time deposits declined whilst the savings rate remained administratively set at 2.50 per cent. With regards to the lending rate, a decline of almost 1.0 percentage point was observed.

2. Monetary Policy Instruments

In the recent past, economic management has relied heavily on fiscal policy with monetary policy relegated to an accommodating role. This is set to change with the enactment of the Central Bank of Seychelles Act 2004.

The objectives of the Bank as stipulated by the Act are:

- to regulate the issue, supply and availability of money and its international exchange;
- to promote price stability and the maintenance of both domestic and external value of the Seychelles currency;
- to advise the government on banking, monetary and financial matters, and in particular on the monetary implications of proposed fiscal or

credit policies or operations of the government;

- to promote internal and external monetary stability;
- to promote a sound financial structure;
- to foster financial conditions conducive to the orderly and balanced economic developments of Seychelles; and
- to perform such other functions as may be assigned to the Bank by any law.

In discharge of the above, it is of critical necessity that the Central Bank rebuilds confidence in the domestic currency as a store of value and not simply as a medium of exchange; unless this is done, the transmission mechanism of monetary policy – and therefore the effectiveness of monetary instruments – would be seriously compromised. Of late, concerns have been expressed at the high costs of financial intermediation in the banking sector, a situation promulgated largely by certain policy measures and compounded by the acute shortage in foreign exchange. Whilst this will equally need to be addressed as a matter of priority, the process must be carried out with care and utmost objectivity so as not to damage confidence and affect the stability of the banking system.

In line with international norms, the Central Bank aspires to pursue an independent monetary policy in the attainment of its objectives. Within the current institutional and macroeconomic policy framework, it has limited scope of exerting control on monetary

aggregates with any degree of precision. For example within the confines of a fixed exchange rate regime, considerable external arrears and no cushion of reserves, the Central Bank is not in a position to influence the level of monetary aggregates in response to large movements in external flows. Consequently for the time being, monetary targeting is not a viable policy proposition.

2.1 Minimum Reserve Requirement¹

One of the statutory requirements on the commercial banks is the minimum cash reserve ratio which obliges financial institutions to hold deposits with the Central Bank. It is also a monetary tool that can be used by the Bank to control liquidity.

At the end of the period under review, this ratio remained at 2.5 per cent. During the course of the year, all banks were able to maintain that requirement and on average, it stood at 5.6 per cent for the year.

2.2 Local Asset Ratio²

The local assets ratio is an instrument that is used by the Central Bank to influence commercial bank lending portfolio and ensure that the banks dedicate a minimum share of their resources to the financing of government

borrowing needs. In September 1998, the Bank adjusted the local asset ratio to 70 per cent from 50 per cent. However, in 2001, the Bank again reduced this ratio to 50 per cent, and this has remained unchanged until to date. At the end of 2004, all commercial banks except one, notably for a short period of time, remained within the ratio of 50 per cent. As for the other banks, they held more than the required level.

2.3 Central Bank Advances to Commercial Banks³

Given their tight liquidity position throughout the year, the banks had to resort frequently to the Central Bank for short term advances, a facility that is repayable within fourteen days of disbursements.

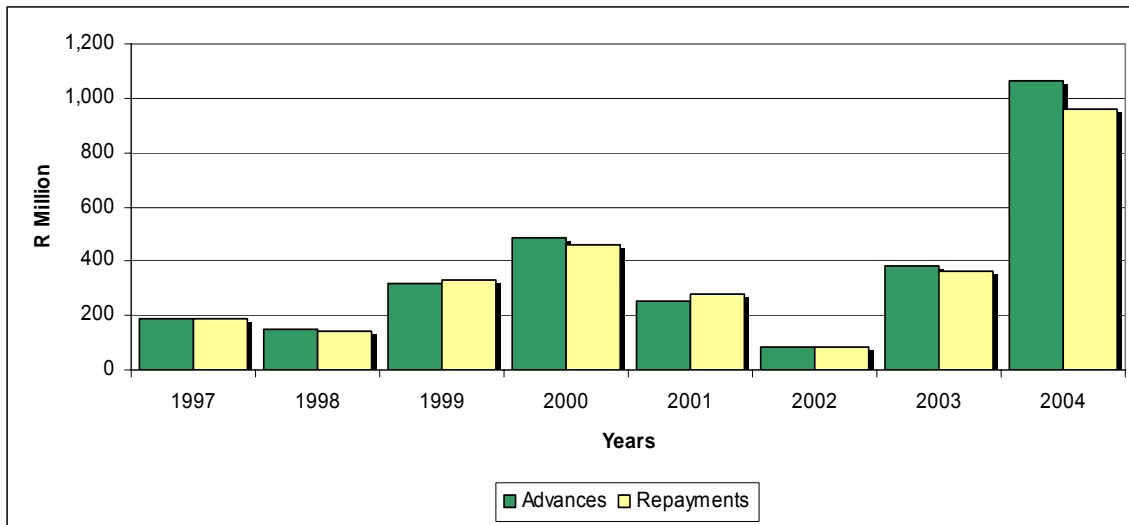
Total advances made to commercial banks in the year amounted to R1,064 million, showing an increase of 180 per cent relative to the previous year (*Chart 2.1*). The average outstanding stock of such advances stood at R45 million at the end of 2004. The increased resort to this temporary facility was mostly caused by liquidity squeeze imparted by the new Pipeline Scheme introduced in April and the implementation of the new tender system for treasury bills.

¹ The minimum reserve requirement is a minimum ratio of cash reserves to eligible deposits that commercial banks are required to hold at the Central Bank. The higher is this ratio, the lower is the money multiplier, thus the monetary impact of new injections of liquidity. The minimum reserve requirement was set at 20 per cent on 16 November 1992. As from 15 September 1998, this ratio was lowered to 2.5 per cent

² With effect from 15 September 1998, the local assets ratio was raised from 50 per cent to 70 per cent. This ratio was lowered to 50 per cent in November 2001.

³ This is the sole standing facility offered by the Central Bank of Seychelles. Since September 1993, the rate on advances has been set at 50 basis points above the average of the last tender rate, rounded to 1/8 of 1 per cent.

Chart 2.1: Central Bank advances to Commercial Banks (1997 –2004)



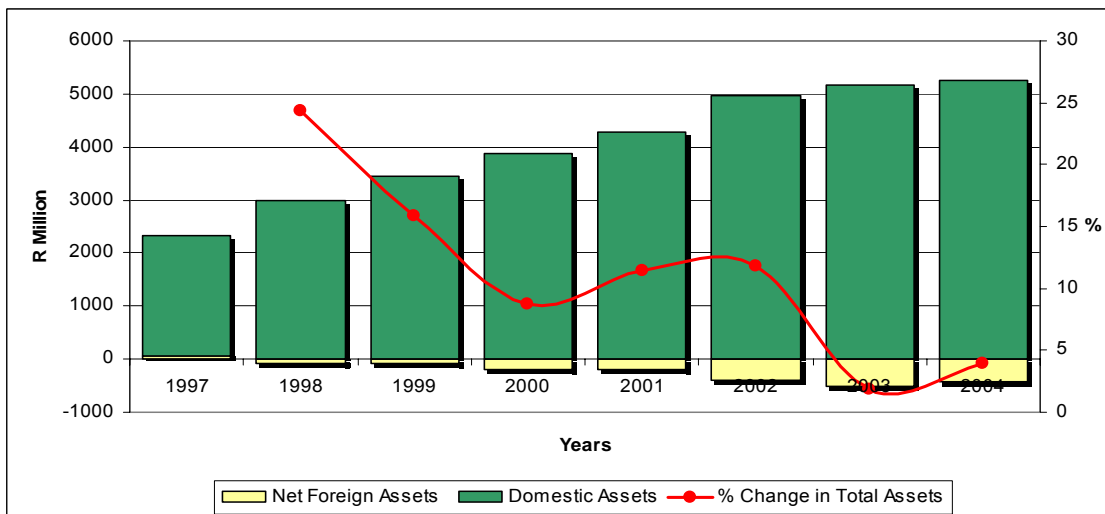
Source: Central Bank of Seychelles

3. Net Foreign and Domestic Assets

In 2004, there was a marked improvement in the country’s net foreign assets position relative to the previous year. Although it remained negative, net foreign assets improved from minus R517 million to minus R415 million (Chart 2.2). The improvement in the Central Bank’s net reserves position was mostly on the liabilities side where a drop (of

R199 million) was recorded. On the other hand, commercial banks’ recorded improvements on both assets and liabilities sides, with an increase in the former and a decline in the latter. As such, the banks were mostly responsible for the overall improvement in the country’s net foreign assets position.

Chart 2.2: Net Foreign and Domestic Assets (1997 – 2004)



Source: Central Bank of Seychelles

Developments in domestic assets followed a similar pattern to last year. As in 2003, they grew at a much reduced pace compared to 2002 and earlier years when the trend was strongly upwards. The main source of credit expansion has been in respect of claims on government; such claims only began to decline in mid-2003 when the government introduced its MERP programme. In 2004, claims on government (net) plummeted by a further R172 million after declining by R131 million in 2003.

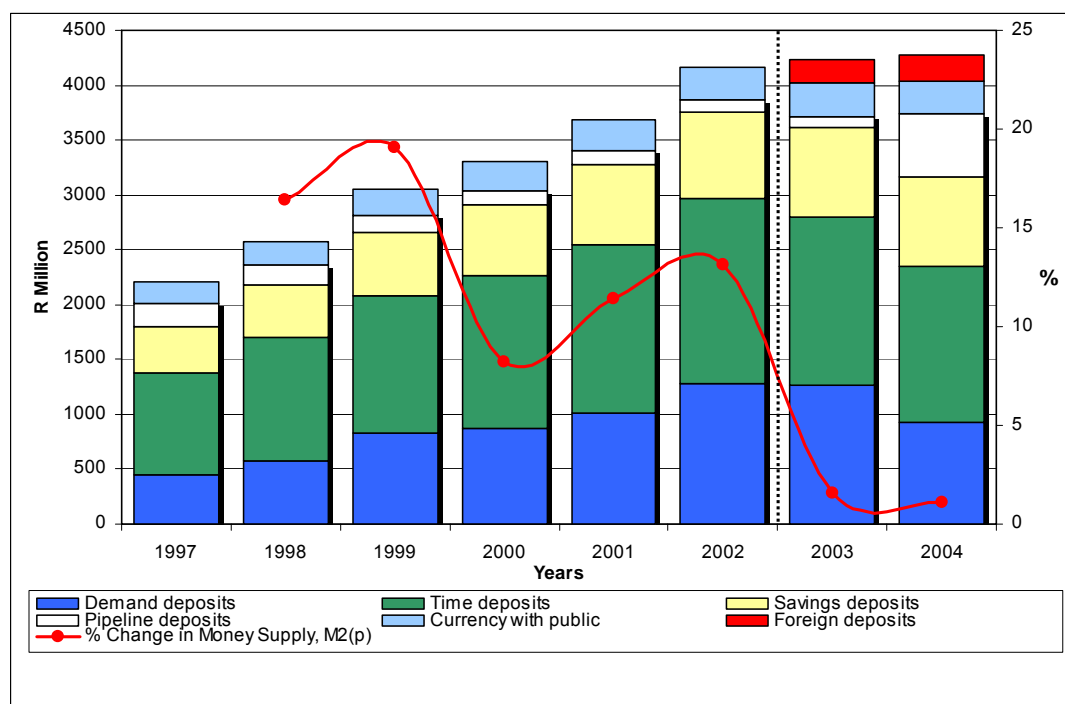
4. Money Supply

In 2004, the broad money aggregate M2(p) grew by R45 million or by 1.1 per cent (*See Chart 2.3*). This moderate rise was mostly underpinned by an expansion in private and

parastatal credit with contractionary movements being recorded from the external sector (negative R102 million) and central government (negative R172 million)

It is of importance to note that monetary data for 2003 and 2004 includes foreign exchange deposits in the banking sector and as such are not strictly comparable with data for earlier years. This stated one can safely assume that such balances were not highly significant in prior years. However, if as a matter of conjecture, foreign currency deposits at the end of 2002 were around R200 million, then there would have been a decline in M2(p) at the end of the year 2003 (of about 3.1 per cent).

Chart 2.3: Money Supply (1997 – 2004)



Source: Central Bank of Seychelles

By the end of December 2004, M2(p) totalled R4,275 million, showing an increase of R45 million, compared to R4,230 million at the end of 2003 (See Table 2.1). An analysis of the M2(p) aggregate shows that all components of money supply declined, except for 'foreign

currency deposits' and the aforementioned pipeline deposits. Foreign currency deposits, which constitute a component of quasi money, rose by R19 million (9.1 per cent) to R213 million relative to 2003.

Table 2.1
Monetary Survey;¹ 2000-2004

	2000	2001	2002	2003	2004
	(R million)				
Net Foreign Assets²	-194.6	-190.5	-394.1	-516.4	-414.5
Central Bank (net)	-132.3	-162.6	-450.3	-324.2	-306.2
Commercial banks	-62.3	-27.8	56.2	-192.3	-108.3
Domestic Assets	3864.3	4280.9	4965.1	5171.8	5250.4
Claims on private sector	565.6	643.5	753.5	993.8	1164.1
Claims on parastatals	20.2	10.8	5.4	102.8	183.3
Claims on government (net)	3278.5	3626.6	4206.3	4075.2	3903.0
Total Assets	3669.7	4090.4	4571.0	4655.3	4835.9
Money Supply, M2(p)	3306.5	3682.5	4165.4	4230.2	4274.8
Money Supply, M2	3174.2	3554.8	4062.1	4128.0	3685.4
Money, M1	1137.5	1290.6	1576.9	1570.9	1226.9
Currency with public	264.4	279.9	301.0	305.9	295.8
Demand deposits	873.1	1010.7	1275.9	1265.0	931.1
(of which parastatals)	182.7	232.7	354.7	477.2	283.9
Quasi-money	2036.7	2264.2	2485.2	2557.1	2458.5
Time deposits	1394.0	1540.0	1693.8	1537.8	1420.9
(of which parastatals)	177.5	183.9	223.3	227.5	152.2
Savings deposits	642.7	724.2	791.4	806.7	805.6
Foreign Currency deposits ³	-	-	-	212.6	232.0
Pipeline deposits	132.3	127.7	103.3	102.1	589.5
Other items, net	363.2	407.9	405.6	425.1	561.0

Figures do not necessarily add up due to rounding.

¹ End-of-period data.

² Excludes government balances abroad.

³ Newly incorporated into money supply as of 2003

Source: Central Bank of Seychelles

As for narrow money (M1), it recorded a sharp decline over last year. It fell by R344 million or 22 per cent, on account of combined contractions in 'demand deposits' and 'currency with the public', which dropped by R334 million (26 per cent) and R10 million (3.3 per cent) respectively. The movement out of demand deposits is explained by the fact that depositors shifted their deposits into the pipeline scheme. The less liquid component of money supply, quasi money, also decreased

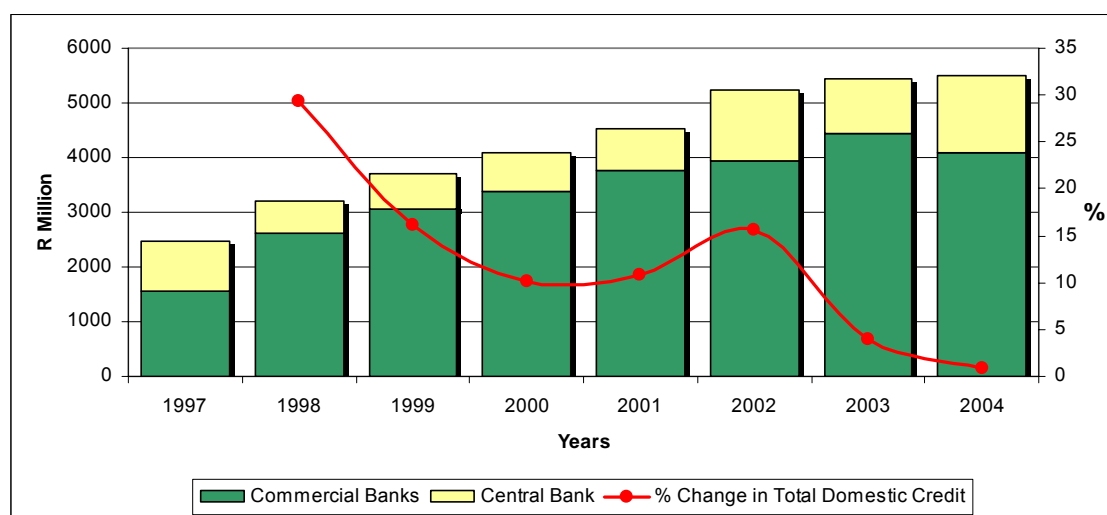
at the end of 2004, by R99 million or 3.9 per cent, mostly on account of time deposits.

5. Domestic Credit

5.1 Central Bank and Commercial Bank Credit

From a monetary survey perspective, movements in domestic credit (*Chart 2.4*), unless neutralised by a contraction in net external assets, are directly reflected in changes in domestic monetary aggregates.

Chart 2.4: Total Domestic Credit (1997 – 2004)



Source: Central Bank of Seychelles

At the end of 2004, total domestic credit in the banking sector amounted to R5,495 million compared to the year 2003 when it totalled R5,444 million. This change represented an increase of R51 million or 0.9 per cent. Although on a net basis, government reduced its liabilities to the banking sector, it significantly increased its reliance on Central Bank resources. In 2004, Central Bank credit

to government, (*Chart 2.5*) rose by R389 million or 38 per cent to R 1,401 million. As this occurred in parallel to a R589 million drop in government borrowings from banks, it is not a cause for immediate concern. However such a development is not in conformity with the stated objective of the MERP, which aimed to reduce government's reliance on the Central Bank's advances.

Table 2.2
Credit;^{1/2} 2000-2004

	2000	2001	2002	2003	2004
	(R million)				
Total Credit	4090.3	4529.9	5234.5	5443.7	5494.6
Commercial banks	3391.5	3755.9	3941.2	4432.1	4054.1
Claims on private sector	565.6	643.5	753.5	993.8	1124.1
Claims on parastatals	20.2	10.8	5.4	102.8	183.3
Claims on government	2805.7	3101.6	3182.4	3335.5	2746.6
Of which:					
Dev. Fund Stocks	(100.7)	(139.7)	(139.7)	(140.0)	(147.1)
Treasury bonds	(903.6)	(940.4)	(794.3)	(1167.4)	(1079.4)
Treasury bills	(1777.1)	(1771.0)	(1784.4)	(1003.9)	(1511.6)
Central Bank	698.8	773.9	1293.2	1011.7	1400.6
Claims on government	698.8	773.9	1293.2	1011.7	1400.6
Of which:					
Advances	(395.9)	(472.4)	(1092.0)	(811.0)	(1316.6)
Treasury bonds	(300.7)	(300.7)	(200.0)	(200.0)	(84.0)
Treasury bills	(2.3)	(1.0)	(1.2)	(0.7)	(0.0)

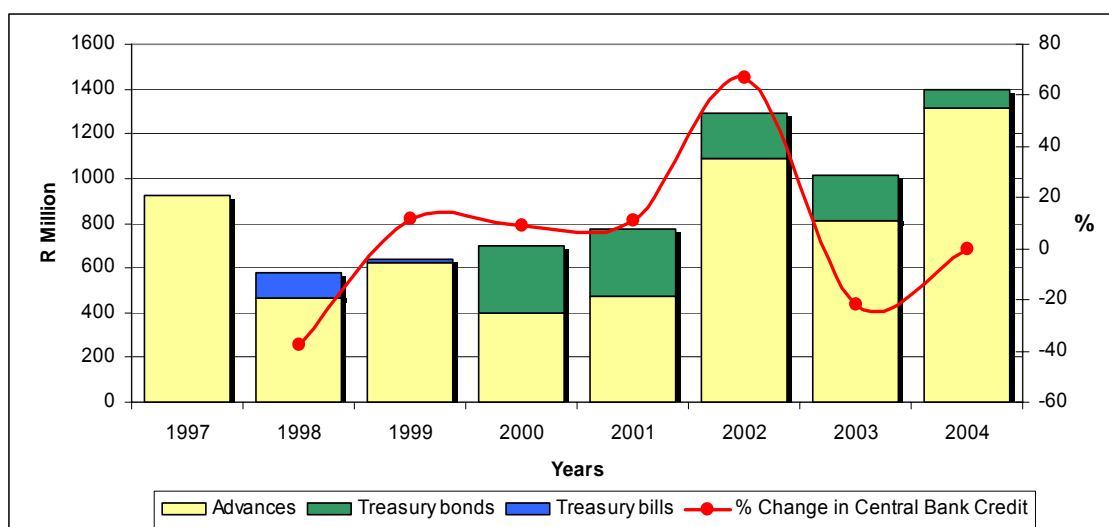
Figures do not necessarily add up due to rounding.

¹ End-of period data.

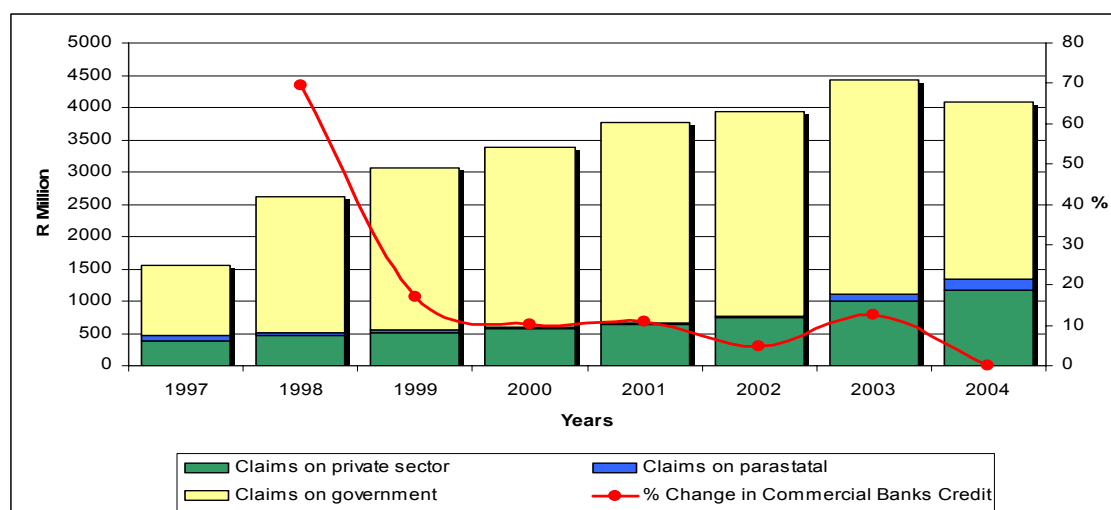
² All figures for stocks, bonds and bills are at cost value.

Source: Central Bank of Seychelles

Chart 2.5: Central Bank Credit (1997 – 2004)



Source: Central Bank of Seychelles

Chart 2.6: Commercial Banks' Credit (1997 – 2004)

Source: Central Bank of Seychelles

5.2 Sectoral Development of Credit to Private Sector and Parastatals

As mentioned above, there was an increase in commercial banks claims on both the private sector and the parastatals. At the end of the period under review, the non-government sector accounted for R1,347 million worth of credit. This represented a rise of R251 million or 23 per cent compared to the previous year. The surge was mostly on account of the private sector which increased its borrowings by a significant R170 million or 17 per cent. As can be observed in *Chart 2.6* above, commercial banks credit to private sector has been on an increasing trend. In the case of the parastatal sector, an increase in credit of R81 million or 78 per cent was recorded compared to the year 2003.

An in-depth assessment of the broad economic sectors reveal that there was an increase in advances in most sectors despite some showing declines, such as 'agriculture and fishing', 'manufacturing', and 'transportation' (See *Chart 2.7 & Table 2.3*). Notwithstanding

the overall increases in advances, it was observed that there was a decrease in the rate of growth of such advances to 'other businesses' and 'tourist facilities'. These registered much lower increases of 29 per cent and 14 per cent respectively. In absolute terms, they grew by R85 million and R44 million, compared to the year 2003 when they increased by R195 million and R110 million. There was a significant pick up in activities in the 'construction' sector which reflected heightened private sector's interest in that area; credit to this sector increased by over 100 per cent. Nonetheless, some sectors' performance continued to be hampered by the foreign exchange shortage. For instance, 'manufacturing', which is dependent on imported inputs, posted a decline of R2.5 million or 24 per cent compared to the year 2003. It is interesting to note that some classes witnessed some major increases in their use of bank resources; notably, 'mortgage loans' and 'wholesale & retail trade', the latter increasing by R54 million or by 78 per cent.

Table 2.3
Commercial Banks – Loans and Advances
To Non-Government Sector by Economic Sectors;¹ 2000-2004

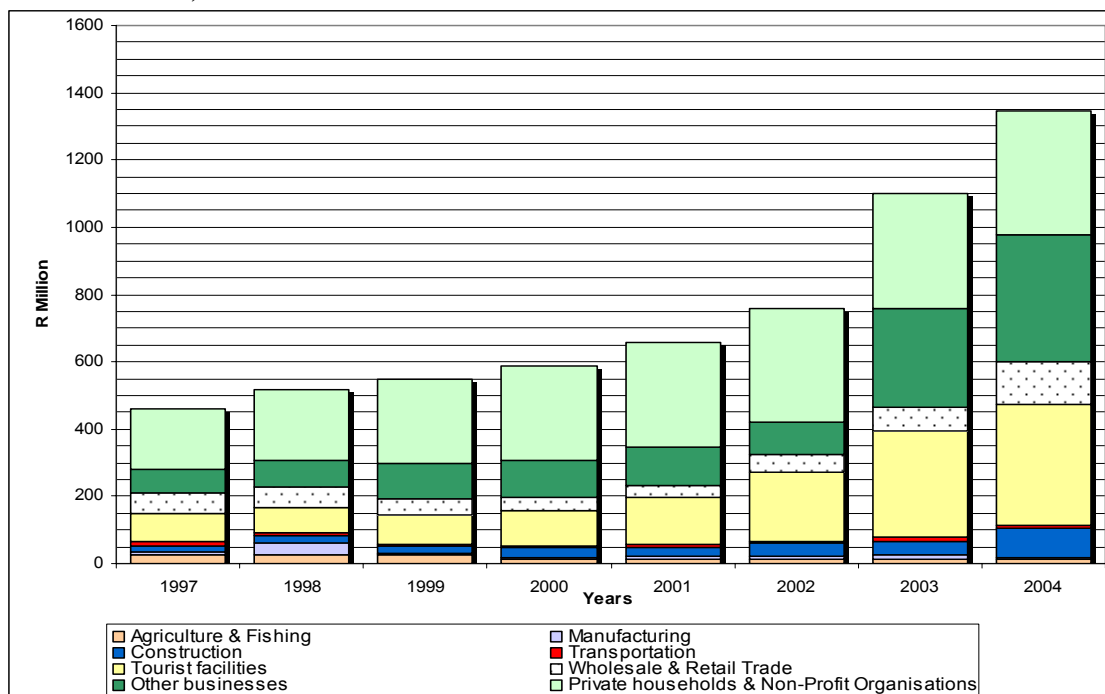
	2000	2001	2002	2003	2004	2000	2001	2002	2003	2004
	(R million)					(per cent)				
Total Advances	588.9	655.8	760.3	1098.5	1347.4	100.0	100.0	100.0	100.0	100.0
Of which:										
Foreign currency loan	17.8	12.2	20.4	73.1	121.9	3.0	1.9	2.7	6.7	9.1
Agriculture & fishing	11.6	13.9	13.4	14.3	11.6	2.0	2.1	1.8	1.3	0.9
Of which:										
Refinance scheme	3.1	1.5	1.5	2.0	0.0	0.5	0.2	0.2	0.2	0.0
Manufacturing	4.8	6.1	9.0	10.4	7.9	0.8	0.9	1.2	0.9	0.6
Of which:										
Refinance scheme	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Construction	29.8	30.3	38.2	43.2	87.0	5.1	4.6	5.0	3.9	6.5
Transportation	4.9	4.5	3.5	10.6	6.6	0.8	0.7	0.5	1.0	0.5
Tourist facilities	107.7	140.8	207.0	317.4	361.5	18.3	21.5	27.2	28.9	26.8
Wholesale & Retail trade	38.7	37.7	53.3	70.1	124.4	6.6	5.7	7.0	6.4	9.2
Other businesses	111.0	114.2	97.2	291.7	377.2	18.8	17.4	12.8	26.6	28.0
Private households & Non-profit organisations	280.4	308.2	338.8	340.9	371.3	47.6	47.0	44.6	31.0	27.6
Of which										
Mortgage loans	148.1	167.5	174.2	189.1	223.8	25.1	25.5	22.9	17.2	16.6

Figures do not necessarily add up due to rounding.

¹ End-of-period data.

Source: Central Bank of Seychelles

Chart 2.7: Commercial Banks' Loans and Advances to the Non-Government Sector (1997 – 2004)

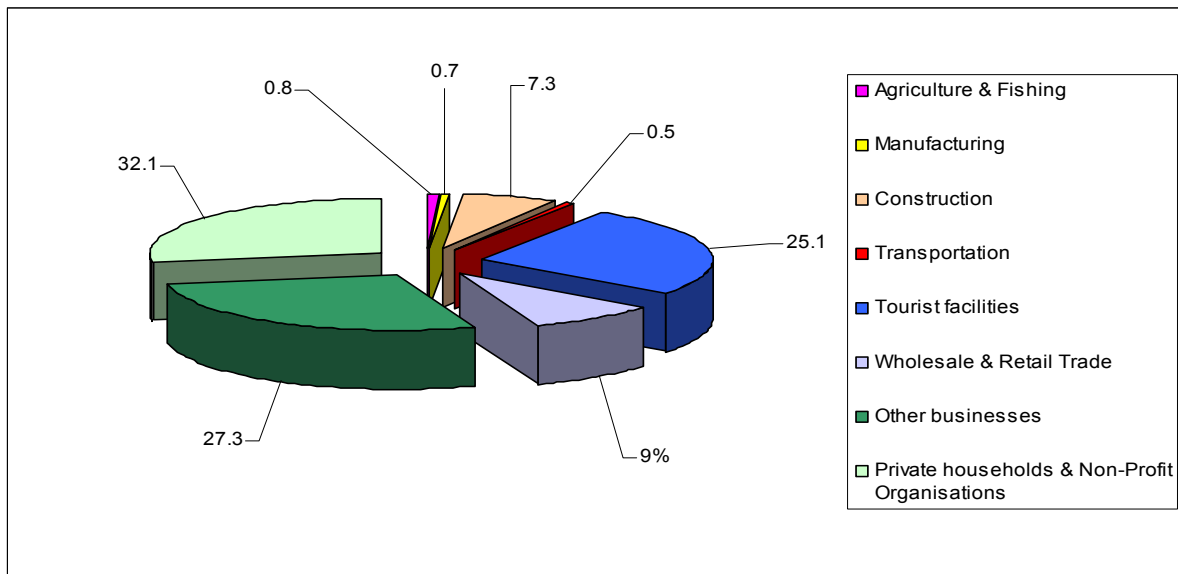


Source: Central Bank of Seychelles

Chart 2.8 below illustrates the distribution of commercial banks' loans and advances to the non-government sector in 2004. The sectoral allocation of credit differed slightly from the

previous year, when 'private households & non-profit organisation' held the largest share of 31 per cent (R341 million).

Chart 2.8: Commercial Banks Loans and Advances to the Non- Government Sector percentage share (2004)



Source: Central Bank of Seychelles

In 2004, 'other businesses' accounted for the biggest share of total credit with 28 per cent (R377 million). The second main borrower was 'private households & non-profit organisations' with 28 per cent (R371 million), followed by the tourism sector with 27 per cent (R362 million). These developments were broadly in line with trends in the estimates for GDP for 2004.

5.3 Development Bank's Credit⁴

The Development Bank of Seychelles (DBS) finances development projects that do not

always meet normal banking criteria in terms of risks or structure of finance required. DBS offers a better alternative as it lends for a longer period than commercial banks. In 2004, it invested in sectors such as agriculture, fishing and tourism as well as others shown in Table 2.4.

In 2004, loans extended by DBS increased by R40 million or 15 per cent compared to R 7.5 million or 2.9 per cent in 2003. One of the underlying factors affecting this growth was the various reforms that were undertaken in

⁴ From January 17, 1994, the Development Bank of Seychelles provides credit to Seychellois investors at concessionary rates. To qualify as "Seychellois", nationals must own at least 50 per cent of the investment. Currently, DBS charges 7.5 per cent p.a. on loans up to R250,000 and 9.0 per cent p.a. on loans above R250,000. The minimum contribution for the investor has remained constant for the past 10 years ranging from 25 per cent to 40 per cent of the total project cost. The Development Bank does not provide credit for purposes of working capital.

the economy throughout the year. For example, the implementation of the Tourism Investment Act 2004 (TIA) offering various

fiscal concessions to the trade appeared to have stimulated some investment activity in the tourism sector.

Table 2.4
Loans by Development Bank by Economic Sectors;* 2000-2004

	2000	2001	2002	2003	2004	2000	2001	2002	2003	2004
	(R million)					(per cent)				
Total Advances	223.3	230.8	260.2	267.7	307.5	100.0	100.0	100.0	100.0	100.0
Agriculture	6.2	5.1	6.1	8.1	12.5	2.8	2.2	2.4	3.0	4.1
Fishing	21.2	18.8	22.2	21.9	22.1	9.5	8.1	8.5	8.2	7.2
Industry	18.2	15.6	13.5	13.8	14.9	8.1	6.7	5.2	5.2	4.8
Tourism	89.9	87.6	93.6	85.0	103.2	40.3	37.9	36.0	31.8	33.6
Other services	87.8	103.8	124.8	138.9	154.8	39.3	45.0	48.0	51.9	50.3

Figures do not necessarily add up due to rounding.

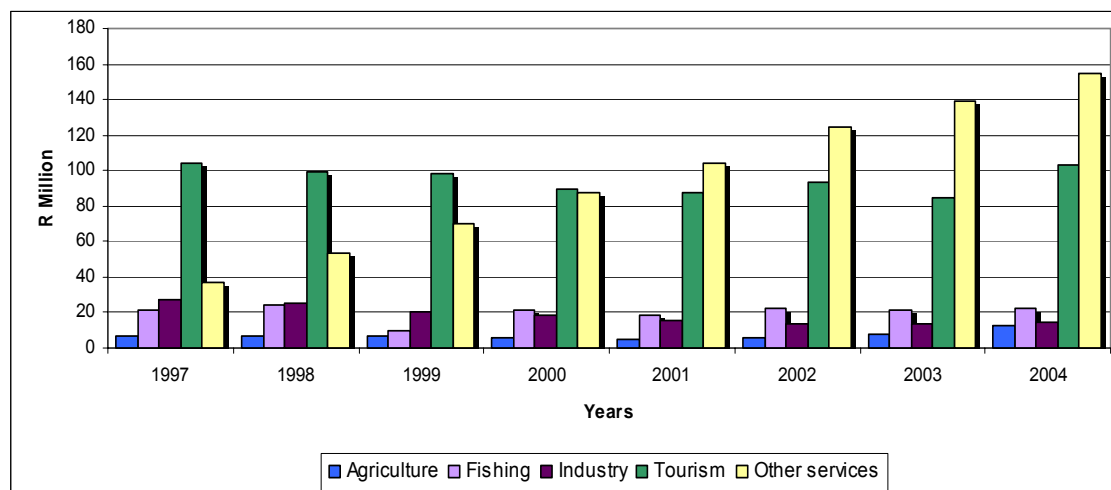
* End-of-period data.

Source: Development Bank of Seychelles

Although all sectors registered an increase in loans in 2004, the most remarkable developments came from 'tourism' and 'other services', with increases of R18 million and R16 million respectively. The other sectors

which experienced increases were 'agriculture', 'industry' and 'fishing', which posted credit growths of R4.4 million, R1.1 million and R0.3 million respectively.

Chart 2.9: Loans by Development Bank by Economic Sectors (1997 – 2004)



Source: Central Bank of Seychelles

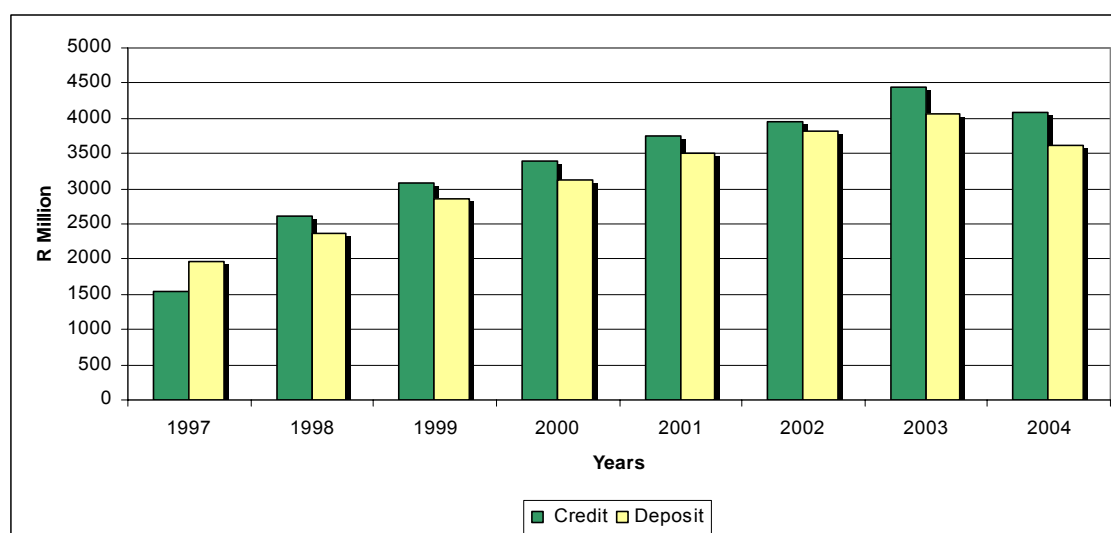
6. Liquidity of Commercial Banks

The liquidity of banks was affected by two major events in the year, specifically in the second quarter. In the first quarter, commercial banks did not approach the Bank for short term credit, but instead relied on inter-bank financing to raise the necessary liquidity at short notice. Nonetheless, the re-introduction of the tender system for the issue of government paper in January, and that of the foreign exchange pipeline scheme in April exerted some adverse effects on the cash flows of banks. This was to the point that in the second quarter of the year, banks were faced with a tight liquidity constraint as their deposit base declined on a month to month basis. Banks' liquidity position, which is measured by the credit to deposit ratio, fell particularly from the end of March. This was illustrated by an increase in the credit to deposit ratio, which moved from 106.7 per cent at the end of March to 111.6 at the end of June.

The shock on deposits which came when the Pipeline Scheme was introduced, originated from the fact that (with the exception of small businesses) it required all bank customers to place rupee deposits upfront against their foreign exchange requests. In this context, the inter-bank market was not able to sustain the liquidity requirements of the banks, which meant that they had ultimately to resort to the Central Bank for relief.

Furthermore, the issuing of treasury bills on a tender basis had a major impact on the banks' cash flow as their major clients shifted their funds directly into the 91-day treasury bills in search of higher yields. With these two major developments, the deposits at commercial banks fell between the end period of December 2003 and that of December 2004.

Chart 2.10: Credit and Deposits of Commercial Banks (1997 – 2004)



Source: Central Bank of Seychelles

Table 2.5
Liquidity Indicators of Commercial Banks;¹ 2000-2004

	2000	2001	2002	2003	2004
	(R million)				
Credit	3391.5	3755.9	3941.2	4432.1	4094.1
Deposits ²	3114.3	3505.1	3824.2	4059.1	3618.8
	(per cent)				
Credit-deposit ratio	108.9	107.2	103.1	109.2	113.1

Figures do not necessarily add up due to rounding.

¹ *End-of-period data.*

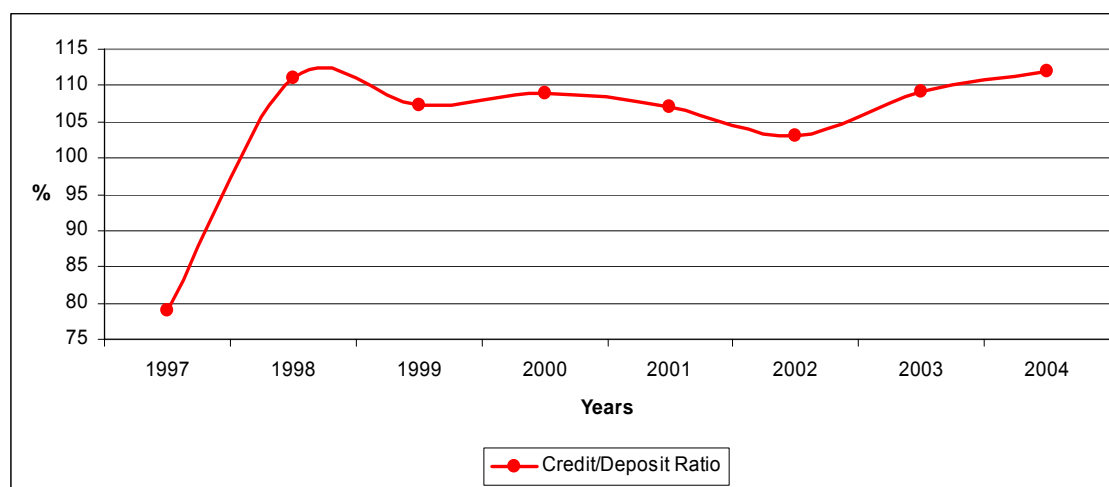
² *Excludes Pipeline deposits.*

Source: Central Bank of Seychelles

During the year, total credit at banks dropped by 7.6 per cent, whilst deposits fell by 11 per cent; thus yielding a 3.9 per cent growth in the

credit/deposit ratio. This suggests a significant tightening in the state of banks' liquidity position relative to earlier years.

Chart 2.11: Credit/Deposit Ratio of Commercial Banks (1997 – 2004)



Source: Central Bank of Seychelles

7. Interest rates

An important development in interest determination took place during the year. On January 13, the government re-introduced the issue of treasury bills on tender, a move which underlined its policy of a gradual liberalisation of the economy. This development attracted mostly commercial banks and large companies which responded positively. With treasury

bills on tender, the cost of borrowing for the government on such instruments was determined by the market. However, given the upward trend of the average tender rate of treasury bills, this entailed a higher interest rate bill for the government. Since interest rates were market determined, there was a more optimum allocation in the pricing of short term government papers.

In general however, money market rigidities remain prevalent in the financial system. The upward pressure on treasury bill rates had no observable impact on the structure of other interest rates in the expected direction.

Compared with the last tap issue, when treasury bills were offered with a rate of 2.0 per cent, the average 91-day treasury bill rose to 2.34 per cent under the tender system, whilst that on the 365-day bill reached, 3.84 per cent.

The minimum savings rate, which is set by the Central Bank, remained unchanged at 2.50 per

cent. However, in 2004 the general movement in interest rates on most deposits, in line with past trends, maintained its downward path that started in 1997. Except for the movement in the savings rate (*Table 2.6 & Chart 2.12*), which increased slightly by 14 basis points, a decline was observed in the rates of other deposit instruments. The most significant declines were 71 basis points and 66 basis points, for the maturities in brackets of '12 months' and '6 to 12 months' respectively.

On the lending side, the volume weighted average lending rate fell by 95 basis points to 10.13 per cent.

Table 2.6
Interest Rates;¹ 2000-2004

	2000	2001	2002	2003	2004
	(per cent)				
Volume-weighted average deposit rates:					
Savings rate	3.02	3.03	3.03	2.85	2.99
Time deposits					
7 days	2.79	2.89	2.78	2.39	2.28
> 7 days ≤ 3 months	4.77	4.92	4.93	3.99	3.55
> 3 months ≤ 6 months	4.76	4.98	4.98	4.22	3.78
> 6 months ≤ 12 months	4.29	4.31	4.34	3.98	3.32
> 12 months	6.33	4.80	4.26	3.75	3.04
Volume-weighted					
Average lending rate	11.45	11.14	11.09	11.08	10.13
91-day treasury bill rate ²	4.50	4.50	4.50	4.50	-
91-day treasury bill rate ³	-	-	-	2.02	-
91-day treasury bill rate ⁴	-	-	-	-	2.34
365-day treasury bill rate ⁵	-	-	-	-	3.84

¹ Annual and quarterly rates are averages of monthly data, compiled on an end-of-period basis.

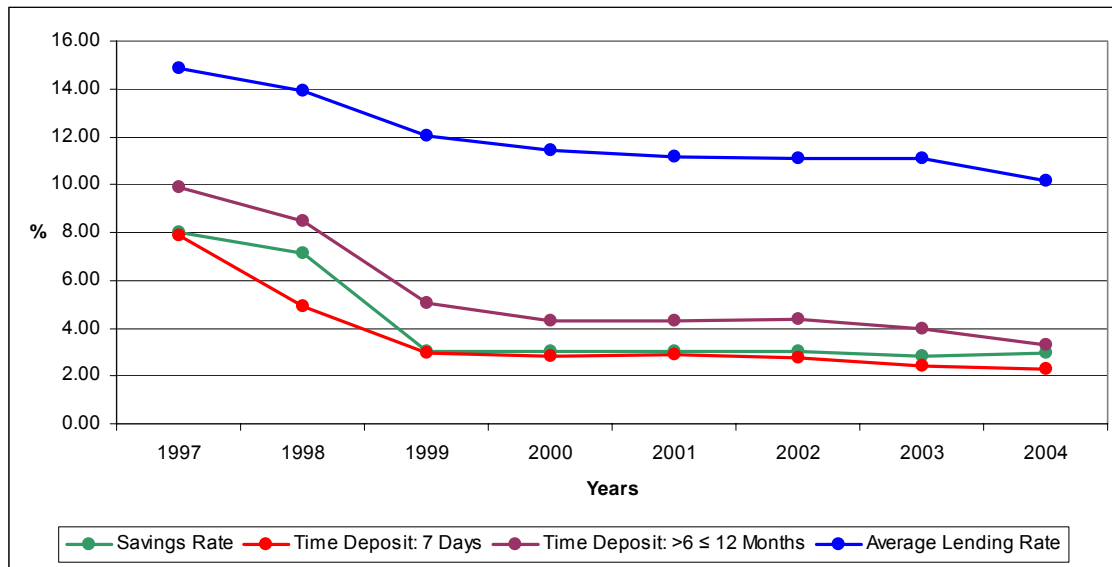
² With effect from September 15, 1998, new issues of 91-day bills were issued on tap.

³ With effect from July 15, 2003, new issues of 91-day bills were issued on tap, available to commercial banks only.

⁴ With effect from January 13, 2004, new 91-day bills were issued on tender.

⁵ With effect from December 20, 2004, new issues of 365-day bills were issued on tender.

Source: Central Bank of Seychelles

Chart 2.12: Interest Rates (1997 -2004)

Source: Central Bank of Seychelles

SECTION THREE

Government Finance

Overview

Developments in the government accounts in 2004 were generally not as anticipated. Within the Macroeconomic Reform Programme (MERP) framework, an overall R593 million surplus was projected. In the event, this was not remotely achieved. Nevertheless the overall budget surplus of R143 million posted in 2004 was a notable achievement.

With strong recessionary forces, soaring oil prices and political instability internationally, a tighter fiscal outcome would have undoubtedly plunged the domestic economy deeper into recession. Indeed the adverse effects of the GST on the domestic manufacturing base and tourism industry continued to be felt in 2004, leading to another year of declining real growth.

With the exchange rate currently assigned to an inflation target and monetary policy in a passively accommodating role, fiscal policy has the twin role of controlling domestic absorption and maintaining external balance. As experience has shown, there are inherent

conflicts when one instrument is targeted at multiple objectives. In both 2003 and 2004, the GST has proved its potency at promoting rapid fiscal adjustments, but it did so at heavy costs in terms of output losses and inflation, leading to further deterioration in the country's external competitiveness.

In recognition of these shortcomings, the government sought to reduce the impact of MERP, more specifically GST, on the tourism sector. This came in the form of the Tourism Incentives Act in 2003, further amended in 2004, embodying a number of fiscal concessions aimed at promoting new investments and reducing operational costs in the industry. In consequence of this, government traded off some of the GST revenue gains.

To contain the inflationary impact of the GST on consumer welfare, government implemented a general trades tax reduction on a range of essential commodities.

Notwithstanding these significant concessions, government revenue remained buoyant during

the year. Total receipts amounted to R1,885 million, R18 million higher than in the previous year. However this fell short of the MERP target of R2,111 million.

On the expenditure side, MERP had proposed a cap of R1,517 million on outlays. Significantly, this was exceeded by R226 million, suggesting the need either for more realistic budgeting, or a reinforcement of fiscal discipline.

The overall surplus translated in an improvement in the public debt situation; this can be substantiated from the monetary survey, which shows a R172 million decline in net claims on government by the financial system to R3,903 million in 2004.

However, following certain institutional policy changes, notably the introduction of the revised Pipeline Scheme and the tender issue for treasury bills, the banking sector experienced massive outflow of deposits, reducing their ability to support government debt. In consequence, government resorted back to the Central Bank for its financing requirements. At the end of 2004, government liabilities to the Central Bank reached R1,401 million. This development runs contrary to the objective of MERP, but was clearly unavoidable under the circumstances.

As a newly independently institution, the Central Bank has now the mandate to pursue an independent monetary policy course. In regard to its relationship with government, its immediate priority is to refrain from further undesirable monetisation of fiscal deficits. As such, it will be expedient for limits to be placed on total accommodation to government and to ensure that both parties respect them.

1. Outcome for 2004

As stated earlier, the government budget for 2004 missed its target by a wide margin. At R143 million (*Chart 3.1 and Table 3.1*), the overall surplus was R450 million short of the MERP target.

At the end of 2004, current expenditure aggregated to R1,628 million. At this level, it represented an excess spending of R160 million or 11 per cent over budget. The other category of government spending - capital expenditure, was projected at R50 million. This amount was insufficient to sustain the costs of unfinished projects of 2003, let alone those that were undertaken in 2004. As such, the year closed with capital expenditure at R114 million.

Table 3.1
Government Budget; 2002- 2005
Summary

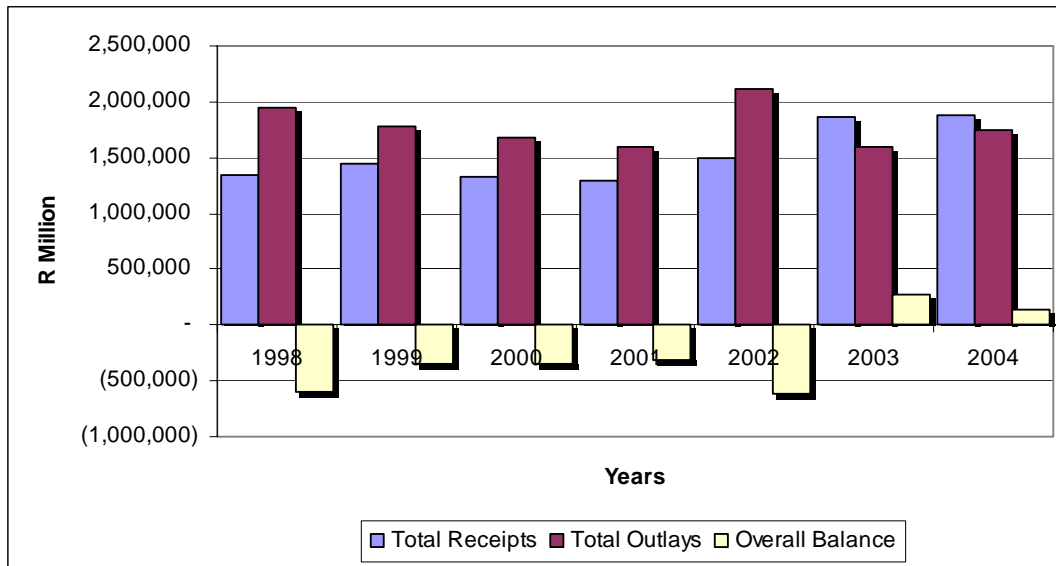
	2002 Revised Budget	2002 Actual ¹	2003 Original Budget	2003 MERP Budget	2003 Actual ¹	2004 MERP Budget	2004 Actual ¹	2005 Budget
R million								
Total Receipts	1516	1498	1512	1898	1868	2111	1885	2004
Current receipts	1488	1473	1502	1893	1857	2110	1882	1999
Of which:								
Trades tax	[305]	[360]	[304]	[353]	[394]	[362]	[351]	[306]
Transfers from Social Security	[110]	[110]	[120]	[120]	[120]	[110]	[110]	[125]
Business/income tax	[240]	[253]	[222]	[274]	[277]	[274]	[297]	[317]
Grants	28	25	10	5	11	1	3	5
Total Outlays	1974	2121	1693	1648	1597	1517	1743	1725
Current outlays	1780	1720	1625	1579	1511	1467	1628	1507
Appropriation items	1457	1380	1363	1331	1283	1234	1360	1196
Of which:								
Ministries/departments	[852]	[832]	[813]	[839]	[824]	[811]	[846]	[794]
Social Security contributions	[131]	[131]	[138]	[138]	[148]	[133]	[143]	[143]
Current outlays to parastatals	[142]	[170]	[101]	[82]	[61]	[30]	[36]	[30]
Charges	323	326	261	284	228	233	268	312
Of which:								
Interest payments	[307]	[326]	[250]	[272]	[216]	[222]	[256]	[301]
Capital outlays	274	358	68	69	86	50	114	200
Net lending	-80	43	0	0	1	0	1	0
Of which:								
Parastatals	[-80]	[37]	[0]	[0]	[0]	[0]	[0]	[0]
Primary Balance²	-151	-297	69	522	486	815	398	580
Overall Balance	-458	-623	-180	250	270	593	143	279
Financing (net)	458	623	180	-250	-270	-593	-143	-279
Foreign loans (net)	552	-414	-73	69	13	-46	-11	-116
Domestic loans (net)	-94	974	253	-319	-241	-547	-103	-163
Cash movements	0	63	0	0	-42	0	-28	0
Memorandum Items:								
Amortisation of loans	526	757	1028	793	1667	4562	1548	2034
Of which								
Foreign loans	306	371	109	62	15	88	15	199
Domestic loans	219	386	919	731	1652	4474	1533	1835

Figures do not necessarily add up due to rounding.

¹ These series are subject to audit and might be revised accordingly.

² The primary balance is obtained by excluding interest payments from the overall balance.

Source: Department of Finance

Chart 3.1 - Government Finance Outcome for 1998-2004

Source: Department of Finance

On the revenue side, total receipts amounted to R1,885 million. At this level, it was short of expectations by R225 million. However, this was a more favourable performance compared to 2003, when total revenue amounted to R1,868 million. In absolute terms, it represented a R17 million increase. As with 2003, the main revenue earner in 2004 was the 'other indirect taxes' category, which recorded an inflow of R612 million. The 'trades tax' category also performed modestly, with an inflow of R351 million. Nonetheless, some categories registered shortfalls and the most significant of which was registered under the 'dividends/interest' category.

It was encouraging to note, however, that the tax category performed comparatively better than in 2003. It showed an increase in revenue of R88 million. The non-tax categories also generated a substantial inflow of R512 million,

of which the most significant came from 'administrative fees & charges'. However, this stood below the outcome for 2003, which amounted to R564 million. The government also received more grants than it had budgeted for in that year. Compared to the expected R1.0 million, revenue from grants amounted to R3.5 million.

With regards to net lending, the authorities projected a nil disbursement in 2004. However, this target was missed by R1.0 million. Nonetheless, the government continued to enforce repayments on the advances made during the course of the year.

2. Revenue

In 2004, current receipts alone amounted to R1,882 million, a record level. The other component of total revenue, namely grants,

amounted to R3.5 million. This brought total receipts for the year under review to R1,885 million, but still R225 million short of budget.

Slippages in revenue were broad-based. The biggest underperformance was recorded under 'dividends & interest', amounting to R94 million due to the non receipt of dividend payments from some parastatals. Other significant shortfalls came from 'other indirect taxes', 'miscellaneous receipts', 'reimbursements', 'trades tax', and 'administrative fees/charges'. They fell below their targets by R90 million, R56 million, R14 million, R11 million and R10 million respectively.

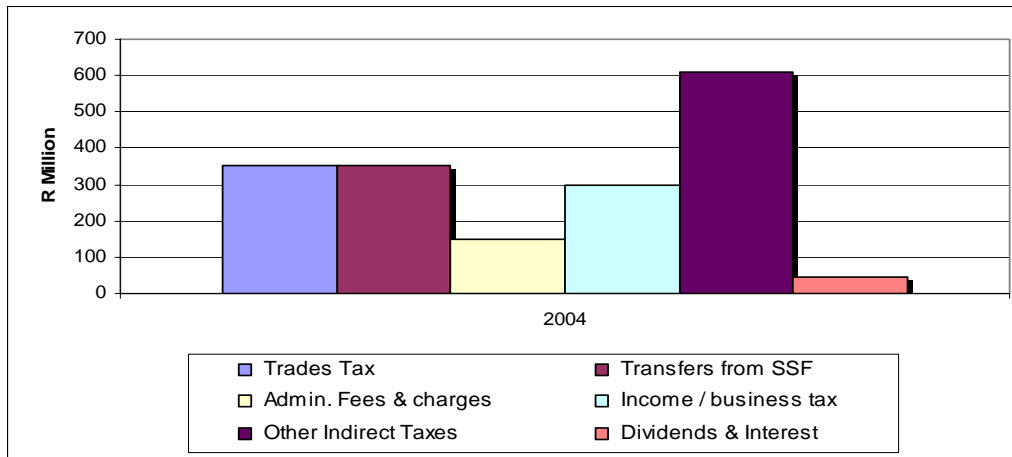
With regards to the 'other indirect taxes', the Goods and Services Tax (GST) on 'locally manufactured goods' missed the budget target by R48 million. In spite of this, some R239 million was collected from this revenue source. In addition, GST of R197 million was collected in respect of domestic 'services' and a further R126 million on 'imported goods'.

Revenue from 'trades tax' fell largely due to the increase in the c.i.f. price of petroleum

products, which under the prevailing trades tax mechanism, has an inverse relationship to revenue.

On a more encouraging note, certain categories performed better than expected. The 'income/business tax' head contributed R297 million to revenue. At this level, it was R23 million or 8.5 per cent above budget. Other positive performances came from 'fees & fines' and 'rents & royalties' which were in excess of their budgets by R20 million and R4.8 million respectively. With regards to 'fees & fines', the favourable outcome was linked to a remarkable growth in 'fishing license fees', which amounted to R61 million.

Overall, the 'tax' categories continued to be the main source of budget revenue in 2004 (See Chart 3.2). In aggregate, they accounted for a 67 per cent share of current receipts, or R1,260 million in nominal terms. It is to be noted that 'trades tax' revenue fell in 2004, even though a growth in imports was recorded. This reflects the general reduction in the trades tax regime for various commodities and the exemption/concession schemes embodied in the TIA.

Chart 3.2 - Major Revenue Flows in Current Receipts in 2004

Source: Department of Finance

Table 3.2
Government Budget; 2002-2005
Revenue

	2002 Revised Budget	2002 Actual ¹	2003 Original Budget	2003 MERP Budget	2003 Actual ¹	2004 MERP Budget	2004 Actual ¹	2005 Budget
	(R million)							
Total Receipts	1516	1498	1512	1898	1868	2111	1885	2004
Current receipts	1488	1473	1502	1893	1857	2110	1882	1999
Transfers from social security fund	110	110	120	120	120	110	110	125
Trades tax	305	304	304	353	394	362	351	306
Income/business tax	240	253	222	274	277	274	297	317
Other indirect taxes	344	325	373	502	502	702	612	628
Of which GST:								
Locally manufactured goods	-	-	-	238	215	287	239	232
Services	-	-	-	169	158	187	197	197
Imported goods	-	-	-	91	72	169	126	120
Fees and fines	97	92	97	103	103	102	121	128
Administration fees and Charges	130	136	130	137	137	160	149	119
Rent and royalties	18	16	18	23	23	20	25	89
Income – public service	10	8	10	8	8	10	9	10
Dividends and interest	122	76	122	150	150	141	47	156
Reimbursements	40	33	45	33	33	42	28	30
Miscellaneous	72	65	62	111	111	188	132	91
Grants	28	25	10	11	11	1	3	5

Figures do not necessarily add up due to rounding.

¹ These series are subject to audit and might be revised accordingly.

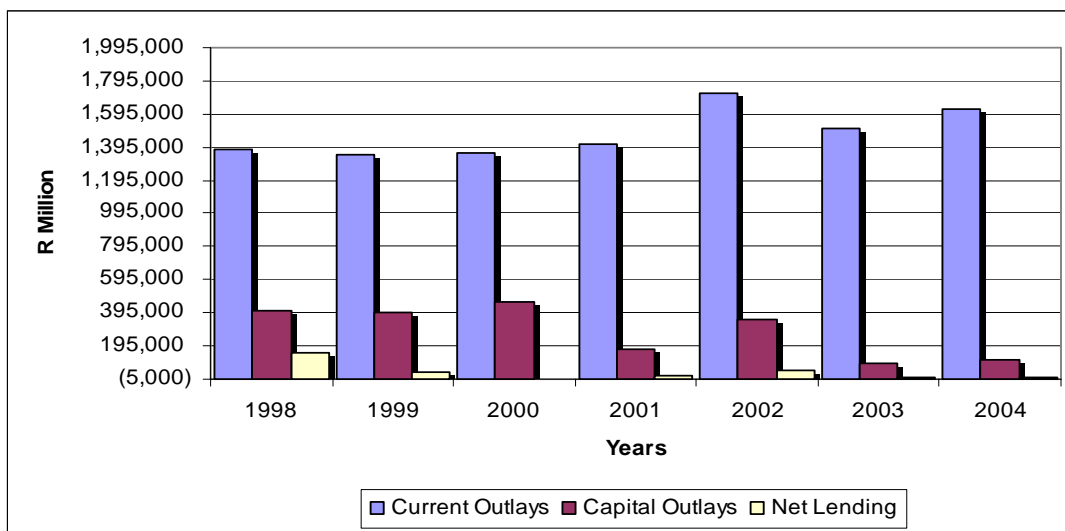
Source: Department of Finance

3. Expenditure

In 2004, the government failed to restrain its expenditure within the target set by MERP. Statistics show that it made overruns on all three main categories of expenditure, namely, 'current expenditure', 'capital expenditure' and 'net lending'. Total actual spending for the year aggregated to R1,743 million (*See Chart 3.3*), to stand higher than planned by R225 million or 15 per cent. On balance, it could be argued that the MERP target was too optimistic and against the backdrop of recessionary tendencies, could have driven the economy deeper into recession.

Current outlays, totalled R1,628 million in 2004, some R160 million above the planned R1,467 million. The other category of expenditure, namely capital outlays, amounted to R114 million. This was on account of capital projects, which exceeded its planned limit by R64 million. The higher than planned expenditure was the result of unfinished projects in 2003 that had to be carried out during 2004, as well as an increase in the price of construction materials. The third component of outlays, namely net lending, did not post a major overrun.

Chart 3.3 - Government Expenditure by main headings; 1998-2004



Source: Department of Finance

3.1 Current Outlays

Most components under this heading posted overruns, with the most significant overspending coming from 'appropriation items', notably R126 million. In turn, this performance was driven by significant overruns under 'centralised payments', 'development grants',

'ministries/departments', 'social security contribution' and 'current outlays on parastatals'. These categories spent in excess of their allocation by R43 million, R39 million, R35 million, R10 million and R6.4 million respectively. As such, they required additional funding, which amounted to R112 million for the period under review.

In the 'centralised payments' category, additional funding was granted to 'general contingencies', 'provision for arrears' (which represented payments made in foreign currency for purchases that were committed in the previous year for certain ministries) and the 'overseas training fund'. These amounted to sums of R50 million, R40 million and R14 million respectively. As for the 'ministries/departments' category, certain ministries spent remarkably higher than their budgets, and thus had to seek additional funding. These were the Ministry of Health, (R10 million), the Police Department, (R9.4 million), and the Defence Department (R8.7 million). Faced with a reduced MERP budget, the Ministry of Health could not contain its spending owing to increases in the price of medicine and overseas medical treatments. As for the police department, additional expenditure was undertaken to strengthen the logistic base, through the procurement of new vehicles and other essential equipment.

Consistent with past trends, overspending was less pronounced in respect of 'charges'. At R268 million, this category posted an excess spending of 15 per cent, or of R35 million. The bulk of this amount was attributed to payments made in 'public debt interest', which was R256 million in the year. Expenditure on this item, which is the second largest next to 'ministries/departments', surpassed its budget by R34 million.

Nonetheless, it is worth noting that two categories registered savings, albeit minimal. These were the 'pensions/gratuities' and 'pension scheme contribution' category, which

made savings of R12 million and R0.5 million respectively.

3.2 Capital Outlays

Capital expenditure for 2004 comprised of spending on capital projects, which represented government investment in infrastructure as well as in other public goods and services. The essence of capital expenditure is that it provides for future consumption, and as such it is an influential element in economic growth. In the year, the government reiterated the need for more private sector involvement in the economy, and the private sector was deemed as the engine for economic growth. Nonetheless, compared to past trends (*See Chart 3.4*), and despite exceeding its budget, the government's spending on capital investment remained on a low end in 2004. This was due to the authority's efforts at curtailing expenditure in order to generate budget surpluses.

At R114 million, capital outlays stood higher than its planned limit, which was projected at R50 million. This more than twofold increase was attributed to spending on 'capital projects', which exceeded its budget by R64 million. Of the R114 million, the bulk of expenditure was in the last quarter of the year, notably a sum of R51 million.

In 2004, most of the unbudgeted capital expenditure was on services such as 'housing', 'public sector management' and 'education', (*See Table 3.4*). The movement in capital expenditure can be seen in *Chart 3.4* below.

Table 3.3
Government Budget; 2002-2005
Expenditure

	2002 Revised Budget	2002 Actual ¹	2003 Original Budget	2003 MERP Budget	2003 Actual ¹	2004 MERP Budget	2004 Actual ¹	2005 Budget
	R million							
Total Budget Outlays	1974	2121	1693	1648	1597	1517	1743	1726
Current Outlays	1780	1720	1625	1579	1511	1467	1628	1508
Appropriation items	1457	1380	1363	1331	1283	1234	1360	1214
Ministries/departments ²	852	832	813	839	824	811	846	794
Tourism & Transport	75	71	75	74	75	72	73	67
Education & Youth	159	157	160	159	162	157	156	151
Health	143	139	164	162	158	159	169	155
Defence	74	79	64	63	67	74	82	69
Internal Affairs	71	70	72	72	75	14	16	16
Pension & Gratuities	38	37	38	37	36	40	28	33
Subventions	196	220	180	154	133	77	87	85
Regulatory bodies ³	54	50	53	47	49	46	50	53
Parastatals	142	170	101	82	61	30	36	30
Other bodies	-	-	26	26	22	1	1	1
Social Security Contributions	131	131	138	138	148	133	143	143
Pension Scheme Contributions	7	7	7	7	6	7	6	7
Land Acquisitions ⁴	(-)	(-)	(-)	(-)	(-)	5	6	7
Development Grants to								
Parastatals ⁴	(-)	(-)	(-)	(-)	(-)	8	47	11
Other appropriations ⁵	234	149	188	156	136	154	197	135
Charges	323	340	261	284	228	233	268	312
Public debt interest	307	326	250	272	216	222	256	300
Other charges ⁶	15	15	12	12	12	12	12	12
Capital Outlays	274	358	68	69	86	50	114	200
Development grants to								
parastatals	66	66	11	12	9	(-)	(-)	(-)
Land acquisitions	8	8	7	7	11	(-)	(-)	(-)
Capital projects	200	283	50	50	65	50	114	200
Net Lending	-80	43	0	0	1	0	1	0
BTL advances – parastatals	-80	37	0	0	0	0	0	0
BTL advances – others	0	6	0	0	1	0	1	0
Capital subscriptions	0	0	0	0	0	0	0	0
Equity participation	0	0	0	0	0	0	0	0

Figures do not necessarily add up due to rounding.

¹ These series are subject to audit and might be revised accordingly.

² Due to a reclassification, there is a break in the series of this item. Road and building maintenance, contributions to political parties, and housing improvement grants are examples of items that were recorded under "other current transfers" in previous Reports, but are now included in various "ministries/departments" or "other charges" in this Report.

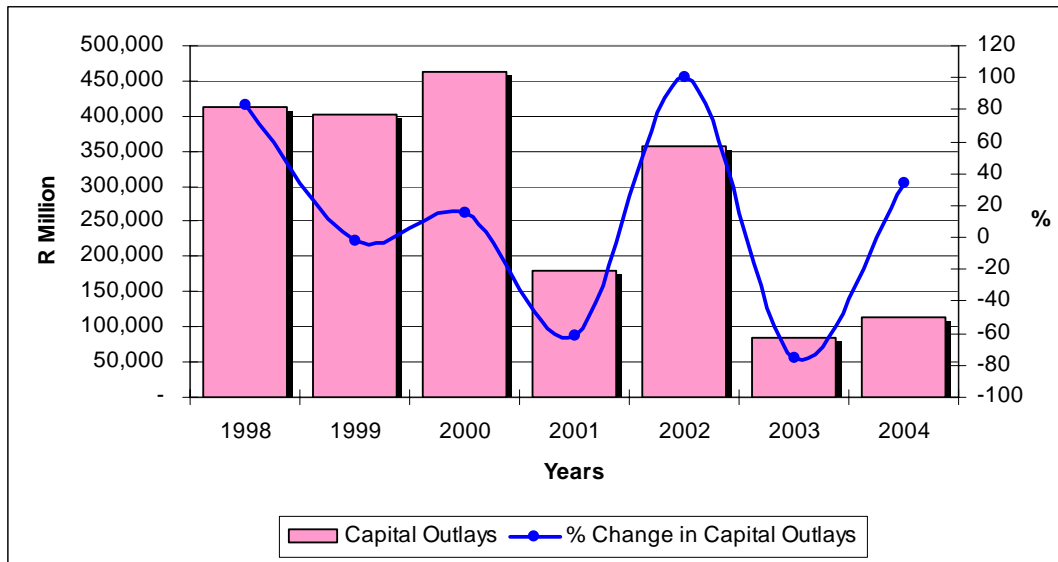
³ Regulatory bodies are Seychelles Licensing Authority, Seychelles Fishing Authority and Seychelles Bureau of Standards. For 1995 Seychelles International Business Authority is also regulatory body.

⁴ Land acquisitions and development grants to parastatals have been reclassified from capital outlays to current outlays.

⁵ Examples of "other appropriations" are contributions to a training fund and international organisations.

⁶ "Other charges" consist of: salaries of constitutional appointees; contribution to political parties; and execution of elections.

Source: Department of Finance

Chart 3.4 - Government Capital Expenditure 1998- 2004

Source: Department of Finance

3.2.1 Public Sector Capital Project Expenditure

As mentioned earlier, capital expenditure in 2004 aggregated to R114 million, to stand higher than the previous year by R29 million. A breakdown of this category showed that all three sectors namely the 'economic sectors', 'infrastructure & utilities' and 'services' recorded a surge in activities as compared to 2003. This outcome was representative of some unfinished projects in 2003 that the government had not budgeted for, which had to be carried out in 2004, in addition to projects that were planned for the year.

3.2.1.1 Economic Sectors

There was a significant growth under 'economic sectors' in 2004, when compared against the previous year. Expenditure

escalated to R5.5 million, an increase of more than 600 per cent over 2003. Three items under this category registered a rise in spending, with the biggest recorded under 'agriculture'. In relation to 2003, tourism also posted a meaningful increase of R1.6 million, whilst 'trade & commerce' recorded the smallest growth.

Spending on 'agriculture' was mainly for the financing of the 'tuna quay project', and this totalled R2.4 million. With regards to 'tourism', the increase was associated with expenditure on the Seychelles Hospitality and Tourism Training College (SHTTC) refurbishment, which amounted to R1.2 million. No spending was made on 'fisheries', 'other island development', and 'craft & home industries'.

3.2.1.2 Infrastructure and Utilities

Outlays on 'infrastructure and utilities' totalled R26 million. As such, it showed a remarkable increase of 18 per cent or R4.0 million compared to 2003, when it amounted to R22 million. This increase was accounted for by most items under this category. In terms of magnitude, the item which accounted for the most significant spending was 'transport' and this was for a sum of R14 million. The most significant movement or change in spending came under the 'land bank' project, notably by R5.0 million. This reflected the fact that no expenditure was carried out under this expenditure item in 2003. Another increase was also registered under 'electricity, water supply & sanitation', and this was to the extent of R0.1 million. Spending on 'land reclamation' decreased from R8.6 million to R6.9 million, whereas 'communications' fell from R0.5 million to R0.1 million.

Of the total expenditure for 'infrastructure and utilities', the largest share was accounted for by spending on 'transport', with a sum of R14 million, of which the most important project was the Mahé secondary road rehabilitation at a cost of R10 million.

3.2.1.3 Services

Of the three sectors, 'services' registered the largest increase in expenditure. Compared to the year 2003, where spending was curtailed at

R42 million, R83 million was spent in 2004. 'Public sector management', which amounted to R26 million, posted the largest increase in spending relative to 2003, when it amounted to R7.9 million. In addition, considerable resources were spent on construction works for SPDF; the repair of the coast guard vessel 'Andromanche'; trades tax office renovations; remedial works & amenities in schools; new roof for Liberty House; national library air conditioning; and furniture for primary schools. These projects amounted to R6.9 million, R3.7 million, R3.4 million, R2.4million, R1.4 million, R1.3 million and R1.2 million respectively.

Expenditure on projects categorised as 'environment' amounted to R9.7 million in the year, half of which was absorbed by the 'gorilla rock' demolition project. Compared to 2003, other subgroups of 'education', 'internal affairs', 'housing', 'social development', 'youth & sports' and 'culture' registered cost increases of R4.7 million, R4.4 million, R2.2 million, R 2.1 million, R0.9 million and R0.7 million respectively. Expenditure under 'public sector management' was the highlight of this category, as it accounted for 31 per cent of total sector outlays.

Table 3.4
Public Sector Capital Expenditure; 2000-2004

	2000	2001	2002	2003	2004
	(R thousand)				
Total	400,986	185,981	254,297	65,417	114,084
Economic Sectors	3,930	26,588	2,994	849	5,450
Agriculture	1,112	1,070	738	745	3,777
Fisheries	18	24,980	1,382	-	0
Tourism	2,674	477	851	104	1,664
Outer island development	-	-	-	-	-
Craft & home industries	-	-	23	-	-
Trade & commerce	126	62	-	-	9
Infrastructure and Utilities	268,694	63,608	101,719	22,090	26,121
Transport	49,267	14,663	13,624	12,826	13,860
Water supply & sanitation	64,805	1,374	411	152	275
Communications	4,581	6,650	7,621	491	122
Land Reclamation	137,317	32,532	65,232	8,621	6,880
Land Bank	12,725	8,388	14,830	-	4,984
Services	128,362	95,785	149,584	42,478	82,513
Education	13,057	18,504	16,355	12,741	17,424
Health	6,726	9,379	1,376	377	2,245
Housing	58,826	21,725	64,017	1,868	4,088
Social development	8,934	6,830	24,622	10,870	12,921
Culture	908	96	1,923	920	1,613
Sports	1,915	15,324	14,884	2,847	3,765
Information & media	4,157	924	-	-	-
Internal affairs	4,226	677	-	644	4,998
Public sector management	17,910	13,656	18,971	7,908	25,790
Environment	11,704	8,670	7,436	4,302	9,668

Source: Department of Finance

3.3 Net Lending

The government's policy towards net lending in 2004 did not change. As with the last year, it continued to aim towards a nil balance at the end of the year, as compared to past trends where the government lent substantially in the form of advances to 'parastatals', as well as 'others', the latter which are advances made under 'general purpose loans' to public servants. Although the nil balance was not achieved, it was encouraging to note that the overrun was a minimal amount of R1.0 million, which consisted of loans under 'others'.

A comparison with the outcome of 2003 indicated that there was a better performance in 2004, as the government managed to reduce net lending by R0.2 million. It is important to highlight that preceding the Macroeconomic reform programme in 2003, 'advances to parastatals' and 'advances to others' were quite significant. In 2002, for instance, these two categories were the main contributors to the net lending heading which cumulated to R43 million. Thus, the government's efforts in containing this component of expenditure were commendable.

4. Financing

Developments under government financing were satisfactory. On the domestic front, gross domestic loans amounted to R1,430 million, whereas amortisation level stood higher at R1,533 million. This meant that on a net basis, the government was able to map out repayment on its loans, such that the net domestic indebtedness fell by R103 million. This financial outcome was encouraging given that in the past the government relied heavily

on domestic funding to finance its budgetary operations.

The outcome on the international markets was even more encouraging. On a net basis, the government made repayment on its foreign loans, and this amounted to R11 million. The financing gap was bridged by an increase of R28 million in government cash balances, which was held principally with the Central Bank.

SECTION FOUR

The External Sector

1. Overview

This section provides a general review of the external sector using Balance of Payments (BOP) statistics, which record Seychelles' transactions with the rest of the world. In general, the BOP outcome would mirror the economic characteristics of the compiling country.

As a typical small island developing state (SID), the Seychelles economy is highly open and heavily dependent on imports for consumption, investment, production and even, re-exports. For over two decades, the government has pursued an ambitious social programme which has successfully propelled the country to the rank of 35th in the UN's Human Development Index (HDI), the highest in the region. Increasingly however, it has become difficult to maintain this tempo of growth, which was financed from borrowed internal and external resources.

More fundamentally, as a deliberate policy, Seychelles has maintained an exchange rate regime that is assigned to an inflation target with the objective of protecting consumers; with the stock of external debt now at a high

level, the exchange rate is now becoming a critical issue in the management of public debt as a currency depreciation would lead to corresponding exchange losses on the stock of such debt with serious budgetary consequences.

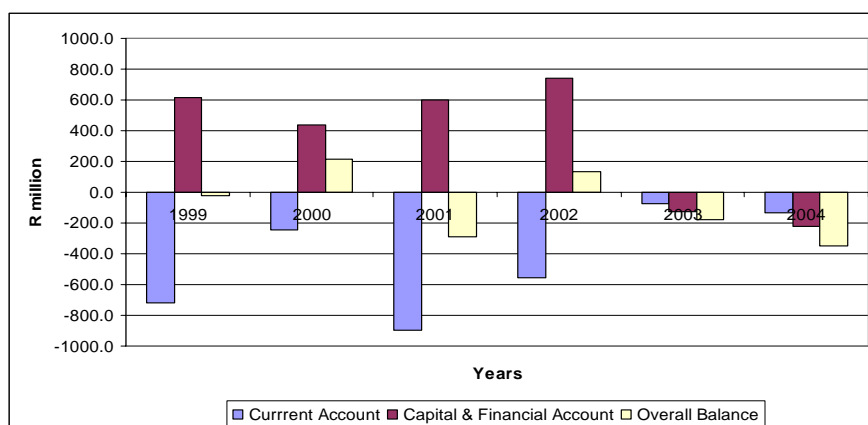
Until recently, the adherence to a non-competitive exchange rate has not been a major constraint to economic growth. In fact, both the fisheries and tourism sectors have prospered in spite of it. Today, the situation is fast changing. With both the monetary and external sectors in marked disequilibria, there is an urgent need to re-assess policy options and re-orient policy priorities in line with the economic situation. As covered elsewhere, the Macroeconomic Reform Programme (MERP) introduced in July 2003, has stabilised the economy and set the platform for a resumption of growth; in its current state, MERP is essentially deflationary and has to rely on concessionary schemes such as the Tourism Investment Act and the forthcoming Agriculture & Fisheries Investment Act, to promote competitiveness and stimulate economic growth.

Of late, the country's imports needs have increased significantly but in the absence of a corresponding growth in external receipts, this has led to large payment deficits that have been financed through borrowings and the build-up of commercial arrears.

During 2004, the external accounts continued to face payment difficulties, exacerbated in part by the government policy to liberalise

trade in preparation for participation in the Free Trade Agreement (FTA) of COMESA as well as to reduce operating costs and enhance consumer welfare. To this end, the monopoly rights of the Seychelles Marketing Board (SMB) were restricted to only seven categories of commodities; trades tax applicable to some key sectors of the economy reduced; and import permit for most goods imported for personal use abolished.

Chart 4.1: The overall balance, current account and capital & financial account of the BOP from 1999 – 2004



Source: Central Bank of Seychelles

The provisional BOP estimates for the year 2004 showed an overall deficit. This amounted to R345 million or 8.9 per cent of nominal GDP, which compares less favourably to a shortfall of R181 million recorded in 2003. The year's overall balance was financed by a drawdown of R181 million in reserves, coupled with an increase of R164 million in the total stock of arrears.

As anticipated, the current account which portrays the difference between domestic demand and supply recorded a deficit. This

stood at R136 million or 3.5 per cent of nominal GDP and was a worse outcome compared to a shortfall of R71 million in 2003. The wider current account deficit was the result of a deterioration in the goods account, specifically the trade balance, due a contraction in exports earnings, coupled with an increase in imports. Whilst the reduction in exports revenue is a cause for concern, the rise in imports associated largely with higher costs of mineral fuel imports is an even more worrisome development. In 2004, disruptions in supply amid rising global demand resulted

in periods of price hikes in the oil market, pushing the price of this important commodity to record highs.

As for the services account, which captures earnings from tourism, this was as usual in surplus in 2004. At R618 million, the surplus represented an improvement of R13 million or 2.1 per cent above the previous year's level. Notwithstanding this outcome, the tourism sector was adversely affected by the prevailing high prices of jet fuel which forced the national airline to increase its air fares and in doing so affected the country's competitiveness in the global tourism market. This, added to the adverse GST impact on operational costs, led to a decline in arrivals. Faced with this situation, the authorities intervened and introduced new incentives in support of activities in that industry.

With regards to the development under the capital and financial account, this showed a net capital outflow for the second consecutive year and at an increased magnitude. From a deficit of R127 million in 2003, the accrued net outward movements of capital increased to R224 million. The aggregate bilateral and multilateral capital transfers to the domestic economy contracted to a mere R5.4 million. In addition, the country recorded a fall in direct investment as well as a decline in re-invested earnings in Seychelles. As expected, most of the investment inflows were directed to the tourism sector. Under "other investments", the account showed further reduction in the country's overall liabilities with the rest of the world. From an accrued

net repayment of R445 million in 2003, the year 2004 showed a shortfall of R400 million.

At the end of the year 2004, the gross official reserves, which comprises of Central Bank (R188 million) and government (R2.4 million), amounted to R190 million or US\$35 million. In terms of import cover, this was equivalent of 3.9 weeks of 2004's c.i.f. imports. At the end of the year 2003, such ratio was reported at 8.6 weeks of c.i.f. imports.

In terms of exchange rate development, there was no change in the regime and the level at which the Rupee is anchored. In general, the domestic currency weakened relative to most of the world's major currencies. However, the depreciation was at a reduced range of 1.8 per cent to 18 per cent compared to the year 2003. Similar to the preceding year, the domestic currency depreciated most strongly against the South African rand (18 per cent). The smallest movement of 1.8 per cent in the exchange value of the rupee was relative to the US dollar, a development which was within the fluctuation limit permitted under the MERP.

Looking ahead, no immediate overall improvement is anticipated in the external sector. Any potential for an improved performance would require a significant increase in foreign exchange inflows. As the situation stands, the country's large stock of external liabilities and accumulated commercial would continue to pose major adjustment challenges to policymakers.

2. Current account

2.1 Trade in goods

Following the revisions in trade policies set out under the economic reform programme introduced in mid-2003, the year 2004 witnessed further changes in the trade regime. With the aim to gradually remove control measures in the economy and move away from regulations of trade, effective July 1, 2004, goods being imported for personal use no longer require an import permit. In addition, government implemented a general reduction in trades tax rates for various goods.

In 2004, the current account posted a goods deficit of R641 million. This outcome which showed an increase in net outflow relative to the previous year was brought about by a widened trade deficit. The shortfall under “general merchandise” expanded by a significant R272 million. The worsened

deficit was explained by a growth in imports which was compounded by a contraction in exports.

As for the remaining sub-accounts under “goods”, the outcome under “repairs on goods” saw a deficit of R23 million. This represented a significant increase in net outflows as compared to a shortfall of only R2.9 million recorded in 2003. There was similarly a remarkable growth of R20 million in outflows in respect of repairs on resident ships and aircrafts. Conversely, as in the preceding year, a surplus was registered under “goods procured in ports by carriers”. For the year under review, this amounted to R442 million and represented mostly growth in credit from the sales of petroleum products to foreign ships and aircrafts, influenced by the high oil prices.

Chart 4.2: Trade in Goods; 1999 – 2004



Source: Management and Information Systems Division, Central Bank of Seychelles

Table 4.1
Balance of Payments;^{1/2} 1999-2004

	1999	2000	2001	2002	2003	2004
	(R million)					
						<i>Provisional</i>
CURRENT ACCOUNT	-721.3	-245.3	-896.5	-554.7	-70.980	-136.1
Goods,	-1197.2	-679.5	-1251.9	-796.3	-492.3	-640.6
Credit (of which)	778.2	1112.9	1267.9	1297.1	1546.9	1652.6
Merchandise exports (f.o.b)	596.6	740.8	954.7	992.2	1180.3	1098.6
Debit (of which)	1975.4	1792.4	2519.8	2093.4	2039.2	2293.2
Merchandise imports (f.o.b)	1905.1	1713.4	2447.3	2028.3	1968.2	2158.3
Services	550.8	564.5	469.4	539.9	605.0	617.9
Credit (of which)	1449.6	1639.5	1723.0	1716.8	1784.4	1785.6
Tourism income converted into rupees	596.2	600.0	648.8	706.4	680.5	756.4
Debit	898.9	1075.0	1253.6	1176.9	1179.4	1167.7
Income	-127.6	-190.2	-171.2	-372.6	-233.3	-183.2
Compensation of employees	-0.5	-13.5	-12.1	-17.5	-25.5	-23.3
Credit	1.0	1.0	1.0	1.1	0.9	0.9
Debit	1.5	14.5	13.1	18.6	26.4	24.1
Investment income	-127.1	-176.7	-159.1	-355.1	-207.8	-159.9
Credit	44.2	56.8	47.3	39.7	63.9	55.8
Debit	171.3	233.5	206.5	394.7	271.6	215.8
Current transfers	52.6	60.0	57.3	74.4	49.6	69.8
General government	89.2	86.1	67.5	72.8	56.9	70.5
Credit	89.3	86.6	69.6	73.8	59.0	72.0
Fishing license fees	32.8	24.8	38.4	35.0	42.6	53.2
Overseas grants	40.6	49.6	14.0	25.2	10.7	3.5
Educational grants	15.9	6.7	9.5	6.8	0.8	6.7
Other grants		5.6	7.7	6.8	4.8	8.5
Debit	0.1	0.5	2.1	1.0	2.1	1.5
Other sectors	-36.6	-26.1	-10.2	1.6	-7.2	-0.6
Credit	21.1	17.1	9.5	9.8	5.9	8.2
Debit	57.7	43.2	19.7	8.2	13.1	8.9
CAPITAL AND FINANCIAL ACCOUNT	611.1	437.2	603.6	743.0	-126.9	-224.2
CAPITAL ACCOUNT	88.0	5.1	55.3	27.5	40.1	5.4
FINANCIAL ACCOUNT	523.1	432.1	548.4	715.5	-167.0	-229.7
Direct investment	246.9	79.0	329.2	213.6	271.5	164.2
Abroad	48.1	60.0	50.0	47.9	44.0	41.8
In Seychelles (of which)	295.0	139.0	379.2	261.5	315.5	206.0
Sale of Assets (Privatised enterprises)	0.0	0.0	0.0	0.0	85.0	0.0
Equity capital	275.0	114.0	331.7	205.8	181.7	172.8
Re-invested earnings	20.0	25.0	47.5	55.7	48.8	33.1
Portfolio investment	2.9	5.4	6.0	5.7	6.1	5.9
Assets	0.1	0.5	-0.4	-0.4	-0.1	-0.2
Liabilities	3.0	6.0	6.4	6.1	6.2	6.1
Other investment	273.3	347.7	213.1	496.1	-444.6	-399.8
Assets	69.3	84.9	51.3	58.6	80.0	67.5
Liabilities	342.6	432.6	264.5	554.8	-364.6	-332.3
Net errors and omissions	85.2	19.8	6.6	-55.3	16.9	14.8
OVERALL BALANCE	-25.0	211.8	-286.3	133.0	-181.0	-345.5
Financing of overall balance	25.0	-211.8	286.3	-133.0	181.0	345.5
Reserve assets ³	-42.0	-110.9	60.5	-141.7	-16.9	181.3
Arrears	67.0	-100.9	225.8	8.6	197.9	164.1
Memorandum items:						
Current account (percentage of GDP)	-20.0	-5.6	-22.8	-13.0	-1.9	-3.5
Trade Balance (f.o.b.)	-1308.5	-972.5	-1492.7	-1036.1	-782.7	-1059.7
Stock of Reserves (Gross)(R million)	160.2	271.1	210.6	352.3	369.2	187.8
Stock of Reserves (Gross) (Weeks of c.i.f. imports)	3.7	7.2	3.9	8.0	8.6	3.8

¹ Contrary to the exchange record, this series is recorded on an accrual basis.

² Data series differ from previous publications due to revisions.

³ (-) sign indicates increase in reserves.

Source: Central Bank of Seychelles

2.1.1 Merchandise exports

The provisional estimate for the year 2004 showed that foreign exchange generated by the country from exports of goods amounted to R1,099 million. This represented a contraction of R82 million or 6.9 per cent and is not favourable news for the authorities. In the previous year, a laudable growth rate of 19 per cent in exports was recorded. In 2004, the reduced exports earning was explained by a contraction under two categories; namely “canned tuna” and “fresh and frozen fish”.

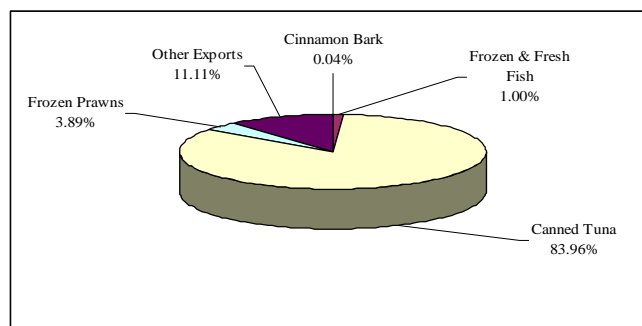
In 2004, sale of canned tuna to overseas markets – which has been on an increasing trend since 1996 – contracted by R101 million or 9.8 per cent in value terms. This suggested a fall in the level of production, which amongst other factors could have been associated with the shortage of water supply experienced during the dry season. The drop in production and exports of canned tuna was not a positive outcome given that in 2003, “canned tuna” accounted for more than 86 per cent of the country’s total export proceeds.

Moreover, this commodity was the driving factor behind 2003’s expansion in earnings with a growth of 21 per cent. Nonetheless, despite the recent decline, the tuna canning factory (Indian Ocean Tuna (IOT)) remains the country’s main single manufacturing and exporting entity.

Exports of “fresh & frozen fish” fell from R28 million in 2003 to R11 million or by a significant 61 per cent. The decline could partly be explained by the ban on exports of certain pelagic species to the European Union (EU) on account of allegedly high cadmium levels. It is understood that this ban will be lifted in 2005 following a review of EU regulations regarding fish imports.

With regards to exports of one of the country’s traditional crops, namely cinnamon bark, this continued to decline and at the end of the period, a mere R0.5 million worth of foreign exchange inflows was earned from this commodity compared to R1.0 million in 2003.

Chart 4.3: Exports 2004



Source: Management and Information Systems Division

As for the remaining categories of exports, the observed movement was a growth, with a maximum of R35 million or 40 per cent posted under “other exports”. Within this subgroup, exports of “other processed fish”, declined from R27 million to R16 million and this again suggested a reduced level of income generated in the fisheries sector.

Nevertheless, exports of frozen prawns, which soared to R41 million in 2003, maintained its growth trend with a total of R43 million exported during 2004. This was underpinned by another year of bountiful harvest for this valuable export commodity.

Table 4.2
Domestic Exports; 1999-2004

	1999	2000	2001	2002	2003	2004 <i>Prov.</i>
	(R million)					
Total	596.6	740.8	954.7	992.2	1180.3	1098.6
Copra	0.0	0.0	0.3	0.0	0.0	0.0
Cinnamon bark	2.2	1.3	1.3	1.2	1.0	0.5
Frozen and fresh fish	28.3	20.7	17.3	18.2	28.0	11.0
Canned tuna	531.9	606.2	771.2	843.7	1023.1	922.4
Shark Fins (Dried)	0.3
Crustaceans	7.7	18.3	12.1	8.7	41.2	42.7
of which:						
Frozen Prawns	7.7	18.3	12.1	8.7	41.2	42.7
Other exports	26.2	94.3	151.4	114.9	87.0	122.0

Source: Management and Information Systems Division

2.1.2 Merchandise imports

Being a small island state with limited economic resources, the level of aggregate demand that can be satisfied from domestic supply is restricted. Under such circumstances, many of the merchandises that are imported are of necessity.

For the year 2004, the provisional estimate showed that total imports (f.o.b.) was valued at R2,158 million. This implied that following a contraction of 3.0 per cent at the end of 2003, imports grew by R190 million or 9.7 per cent, on account of an increase under most of its categories. The main remarkable development was observed under “mineral fuels”. From

R305 million in 2003, imports of this commodity grew to R455 million or by a significant 49 per cent. This brought its share of total imports to 21 per cent. As stated earlier, one important factor behind this development was the movement in oil prices. During the year 2004, the price of oil was hovering at record highs based on concerns for fear of oil production and supply disruptions in the major oil-producing countries amidst soaring global demand.

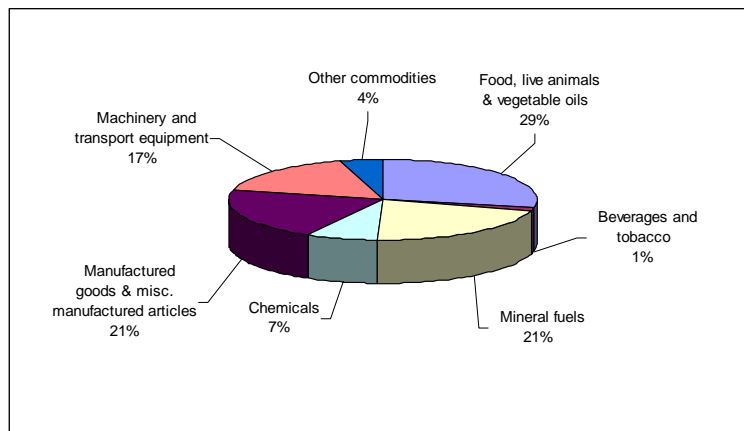
Debit under “food, live animals & vegetable oils”, which accounted for 28 per cent of total imports stood at R607 million. This was R38 million or 6.7 per cent above its previous

year's level. Such increases could have been influenced by the changes in trade policies. As mentioned elsewhere, from July 1, 2004, the Seychelles Marketing Board (SMB) retained import monopoly on only seven categories of commodities, down from its original eleven. From that same date, imports for personal use could be freely imported, except for a short list of restricted/dangerous items. In the second half of the year alone, following these changes, the value of imports under the heading "food, live animals & vegetable oils" grew by 9.9 per cent above that of the corresponding period of the previous year.

Accrued payments under "beverages and tobacco", with a share of 1.3 per cent of aggregate imports showed a slight expansion of R0.4 million or 1.4 per cent in 2004 to stand at R28 million.

Another category of imports which observed an increase relative to the previous year was "machinery and transport equipment". The growth under this entry amounted to R23 million or 6.8 per cent and accounted for 17 per cent of total imports. This mainly represented an increase in imports of electrical machinery and mechanical appliances.

Chart 4.4: Imports (f.o.b.) 2004



Source: Management and Information Systems Division, Central Bank of Seychelles

The remaining growths in import were R2.8 million (9.0 per cent) and R1.7 million (0.4 per cent), being accrued payments under "other

commodities" and "manufactured goods & miscellaneous manufactured articles".

Table 4.3
Imports (c.i.f.) – by HS¹ Sections; 1999-2004

	1999	2000	2001	2002	2003	2004
	<i>Prov.</i>					
	(R million)					
Description						
Total imports	2241.3	1948.9	2776.0	2294.9	2230.6	2466.9
Food and live animals	484.2	517.8	645.6	673.8	669.3	714.0
Beverages & tobacco	29.9	27.1	21.9	36.5	32.8	32.8
Mineral fuels	198.5	422.7	409.6	327.9	358.3	535.6
Chemicals	138.3	128.7	144.9	152.0	207.0	188.5
Manufactured goods &						
Misc. manufactured articles	714.4	472.9	459.2	520.4	533.6	535.6
Machinery & transport equipment*	638.7	332.4	1056.5	542.5	394.4	421.0
Other commodities	37.3	47.3	38.3	41.9	36.2	39.4

¹ Harmonised System

* Include the value of the Boeing 767-300 acquired by Air Seychelles in April 2001 under a financial lease agreement.

Source: Management and Information Systems Division

Amongst the commodities which observed a drop in import levels, the most significant decrease was recorded under importation of “chemicals” with a contraction of R16 million or 8.9 per cent.

The drop in imports under “other unrecorded shipment (shuttle trade)” was R7.6 million or 12 per cent. This fall in the estimates of “unofficial” imports could ostensibly be linked to the reduced number of residents who travelled abroad during the year. The drop in overseas travel by residents can be attributed to the combined effect of GST on incomes and the increase in air fares by the national airline following the rise in the price of jet fuel.

2.1.3 Goods procured in ports

As mentioned earlier, the account under “goods procured in ports by carriers” remained

in surplus. For the period, a remarkable expansion of R143 million (48 per cent) was observed in such net inflow. This was particularly explained by an increase under the ‘credit’ entry which outweighed the growth in debit.

On the credit side, the most prominent observation was related to the gross inflow originated from transactions with foreign ships and aircrafts. In aggregate, these rose by a noteworthy R188 million or 52 per cent, which mirrored the growth in payments under “petroleum products”. The latter increased from R353 million in 2003 to reach a peak of R531 million in 2004. As in the case of petroleum payments, the growth in “re-exports” of fuel reflected price effects as opposed to quantity changes.

Table 4.4
Goods procured in Ports; 1999-2004

	1999	2000	2001	2002	2003	2004 Prov.
	(R million)					
Goods procured in port, net	114.2	304.4	246.8	242.7	298.5	441.8
Credit	178.8	368.2	309.1	300.7	362.2	549.9
Petrol	169.5	356.8	296.6	290.9	352.7	531.0
Food and beverages	6.9	8.5	7.1	7.4	7.8	6.6
Others	2.4	2.9	5.4	2.4	1.6	12.3
Debit	64.6	63.8	62.3	58.0	63.7	108.1
Petrol	54.6	54.3	53.0	47.1	50.7	94.4
Food and beverages	10.0	9.5	9.3	10.9	13.0	13.7

Source: Management and Information Systems Division; Central Bank of Seychelles' estimates

On the debit side, the increase was R44 million or 70 per cent. Debit in respect of petroleum products purchased abroad by residents - accounting for 87 per cent of gross outflows under this account – increased by R44 million or a significant 86 per cent.

2.1.4 Repairs

As in 2003, the overall outcome under “repairs on goods” remained in deficit. However, net outflows were significantly higher at R23 million compared to R2.9 million recorded in 2003. The estimated credit towards repairs on foreign goods stood at R4.1 million, a drop of R0.3 million relative to the previous year. A review of the credit side entry revealed that from R3.6 million in 2003, the estimated inflows classified under “repairs on foreign aircrafts” fell to R3.4 million. This could be associated with the reduction in the number of flights to the country by foreign airlines. During the year, credit in respect of non-resident ships, moved from R0.8 million to R0.6 million, and similarly, this suggests a

reduced number of foreign vessels using Port Victoria.

With regards to repairs on local goods abroad, the period observed a significant R19 million increase, explained largely by costs incurred in the maintenance of resident aircrafts abroad.

2.2 Services

In recent years, the contribution of the services sector to the Seychelles economy has increased in importance; as such, the tourism sector has established itself as one of the most important industries in the country in terms of foreign exchange contributions. In the context of BOP, the contribution of the services account is vital in view of its recurring surpluses and thus its positive net contribution to the current account.

As expected, the estimated outcome under the services account for the year 2004 was a surplus and this amounted to R618 million.

Table 4.5
Services;¹ 1999-2004

	1999	2000	2001	2002	2003	2004 <i>Provisional</i>
	(R million)					
SERVICES, NET	550.8	564.5	469.4	539.9	605.0	617.9
Transportation	218.2	300.0	231.8	178.7	222.5	155.5
Passenger	345.0	378.5	332.9	344.7	373.7	350.0
Credit	381.6	491.6	437.2	455.0	472.4	463.4
Ticket sales to non-residents by Air Seychelles	351.6	469.4	417.0	451.0	472.4	463.4
Others	30.0	22.2	20.2	4.1	0.0	0.0
Debit (tickets to foreign airlines by residents)	36.7	113.2	104.3	110.3	98.7	113.3
Freight	-209.6	-156.0	-170.6	-257.9	-244.0	-272.4
Credit	70.6	87.6	112.9	28.9	34.8	36.0
Debit	280.2	243.6	283.5	286.9	278.8	308.4
Other transportation services	82.9	77.6	69.6	91.9	92.8	77.9
Credit (of which)	134.0	128.3	124.5	148.1	166.5	150.0
Marine and port charges	27.9	28.3	27.0	30.8	34.0	33.0
Income from stevedoring	53.4	49.2	44.9	61.8	68.4	58.8
Agency service income	16.2	16.0	15.0	10.6	21.5	19.3
Airport (ground) handling fees	14.3	15.7	14.2	15.5	16.0	15.2
Aircraft landing fees	14.6	14.2	13.1	14.6	15.1	12.2
Others	7.6	4.9	10.2	14.7	11.6	11.5
Debit of aircraft landing Fees abroad	51.1	50.7	54.9	56.3	73.7	72.1
Travel	611.3	670.8	732.3	731.4	739.1	767.8
Credit	724.0	795.6	856.2	900.5	924.2	944.4
Tourism earnings (converted into rupees)	717.9	788.8	848.7	893.9	918.1	938.3
Others	596.2	600.0	648.8	706.4	680.5	756.4
Others	6.1	6.7	7.4	6.6	6.1	6.0
Debit	112.7	124.7	123.8	169.1	185.1	176.6
Foreign travel expenditure	95.0	100.0	92.9	131.2	129.2	109.0
Training of residents abroad	17.7	24.7	30.9	30.4	24.5	38.4
Others	0.0	0.0	0.0	7.6	31.4	29.1
Insurance, net	-74.3	-67.8	-81.1	-79.8	-81.1	-83.6
Royalty Debit	-2.5	-2.5	-2.5	-3.0	-3.0	-3.0
Financial and Business Services	-147.1	-190.4	-261.3	-194.1	-244.4	-210.4
Credit (of which)	46.4	52.0	92.7	79.3	72.4	83.9
Telecommunications Seychelles	39.6	49.9	54.8	56.0	56.2	60.1
Debit	193.5	242.4	354.0	273.3	316.8	294.3
Construction service	-119.8	-196.7	-208.3	-143.2	-92.2	-82.4
Government services	64.8	51.1	58.4	49.9	64.1	73.9
Credit	86.9	77.7	82.0	90.1	105.7	100.1
Foreign embassies in Seychelles	3.0	3.0	3.0	3.0	3.0	2.7
Licences and other fees	83.9	74.7	79.0	87.2	102.7	97.4
Debit	22.0	26.7	23.5	40.2	41.6	26.2
Expenses by Seychelles embassies	6.7	6.8	6.5	6.7	6.1	3.3
Tourism promotion	15.3	19.8	17.1	13.6	15.2	12.7
Government others	-	-	-	19.9	20.3	10.2

Source: Central Bank of Seychelles

A detailed review of the main headings under the services account showed mixed results. Under “transportation”, the outcome continued to be in surplus, however, the magnitude was reduced by R67 million or 30 per cent. This followed a worsened performance under all of the main components under this account. For once, net passenger credit contracted from R374 million to R350 million or by 6.3 per cent, attributable to a fall in credit associated with a reduction in the number of visitors to the country during the year.

Payments to foreign airlines by residents showed a growth of R15 million or 15 per cent. This increase came despite the decline in the number of residents who travelled abroad in 2004. Such outcome could have been influenced by the rise in prices payable per resident, which could partly be associated with the depreciation of the domestic currency against most major currencies.

With regards to freight transactions, the account continued to be in deficit. In 2004, the shortfall amounted to R272 million. Such development is explained by the growth in insurance payable for goods imported, which was directly related to the increase in (c.i.f.) imports.

As for the outcome under “other transportation services”, this remained in surplus and maintained its positive net contribution to its main account. However, from its most recent peak of R93 million in 2003, the surplus contracted by 16 percent to R78 million. This

was explained by a drop of R17 million in credits with decline evident under all categories of inflows under this entry. However, in magnitude, this was more prominent under “income from stevedoring” which was R9.5 million less than the amount registered in 2003 following a reduction in fishing activities during the year. Due to related factors, inflows from “marine and port charges” stood at R1.0 million below that of the previous year.

A contraction of R2.9 million was also recorded under “aircraft landing fees”. Such development was influenced by the reduced number of foreign aircraft services to Seychelles. British Airways replaced its Boeing 747 plane with one of lesser capacity in 2004, before suspending the service altogether. The estimated contraction in inflows under “airport handling fees” was 4.9 per cent.

As for the value for “agency service income” and that under “others”, the amount reduced by R2.2 million and R0.1 million respectively.

In terms of its size and its positive net inflows, transactions under the subgroup “travel” account for the largest share of the services account. Since 1999, the outcome of the former account has been on a general increasing trend. In 2004, such net inflow stood at R768 million, representing an increase of R29 million (3.9 per cent). This was due to an improvement on the credit side, as well as the drop in gross outflows. The growth in

credits amounted to R20 million or 2.2 per cent, somewhat slower than in the previous year.

The aggregate accrued payments effected by the Seychelles economy relating to travel was R177 million, representing a contraction of R8.5 million or 4.6 per cent. This is explained by a drop of R20 million in foreign travel expenditure by residents as a result of a 12 percent drop in overseas travel by residents. A drop of 29 per cent was also recorded in debits in respect of "health services" whilst that in respect of "training of residents abroad" grew by a significant 57 per cent.

The balance under "insurance", continued to be in deficit in 2004. Influenced by payments associated with importation of goods items, and the earlier-mentioned increase in imports, the shortfall increased by R2.5 million to stand at R84 million. On a gross basis, credit contracted by R0.5 million whilst debit grew by R2.0 million. With regards to the net outcome under royalty, this remained somewhat constant and showed net outflows worth R3.0 million.

Another sub-account under "services" which recorded a deficit was "financial and business services". In 2004, the estimated shortfall was R210 million. This was an improvement of R34 million relative to the previous year.

Gross services inflows amounted to R84 million, representing an increase of R11 million. This was associated with an

expansion in credits under both of the accounts' main components, namely "telecommunications" and "other business services" which grew by R3.9 million and R7.6 million respectively. However, on the debit side, the estimated amount with respect of services offered by non-residents contracted by a significant R23 million and was influenced by the drop under "others" which was R25 million less than the amount recorded in 2003.

For "construction services", the account remained in deficit. Owing to a reduced level of gross inflow, the estimated net outflow contracted by 9.8 per cent to stand at R82 million. The drop is mainly on account of services provided by non-residents associated with construction works in tourism establishments.

As for transactions under "government services", the account showed an outcome that was rather positive. It not only remained in surplus but its net contribution increased. From R64 million in 2003, this net inflow grew to R74 million. This 15 per cent net improvement was triggered by a contraction in the amount payable to non-residents given that on the credit side, a slight decline was observed. From R106 million in 2003, the aggregate credits moved to R100 million. This was explained by a lower level of inflows under "licenses and other related fees" which fell by R5.3 million. Influenced by the drop in visitor arrivals, the entry under "immigration fees and stamps" contracted by R2.0 million.

However, the most remarkable decline on the credits side was R15 million under “other licence fees”, offsetting the growth in receipts of R9.8 million and R1.8 million reported under “flight information region” and “radio broadcasting licence fees”.

2.3 Income

As has been traditionally the case, the income account registered a deficit. However, the year 2004 observed a further reduction in the magnitude of the shortfall which consequently improved the account’s net contribution to the current account. From R233 million in the preceding year, the shortfall contracted to R183 million in 2004. This was particularly associated with the development under “other investment” where a fall in net payable income was observed. Consequently, the outcome under “investment income” showed a deficit which contracted by R37 million or 18 per cent to end with a net outflow of R171 million.

The balance under “compensation of employees”, which is a sub-account under “income” recorded a shortfall of R23 million, an improvement of R2.3 million relative to the previous year. On the credit side, the gross inflow of income was R0.9 million and remained rather constant in comparison with the previous year. This represented mainly the estimated income to residents’ staff at foreign embassies. On the debit side, the aggregate amount stood at R24 million, which was in respect of accrued payments for the value of services offered by expatriate employees to

resident companies, including some state-owned companies.

2.4 Transfers

In Seychelles, the transfers account records the smallest level of current transactions. Nevertheless, for the year 2004, the account not only remained in surplus but its net contribution increased in relation to the previous year. The growth in net inward transfers followed a positive development under both of the accounts’ main subgroups; namely “general government” and “other sectors”.

From R57 million in 2003, the surplus under “general government” increased to R70 million, of which gross inward transfers were R72 million. Similar to the preceding year, the bulk of these credits originated from fishing licence fees, which grew by R11 million to R53 million. Its share to gross inflows under “general government” was 74 per cent. On the debits side, the estimated outward transfers effected by the government to non-residents was R0.6 million lower than what was registered in the previous year.

With regards to the “other sectors”, which is a compilation of the flows relating to workers’ remittances, the account remained in deficit. Nevertheless, the size of the net outflow reduced considerably from R7.2 million in 2003, down to a mere R0.6 million for the period under review. Such development is explained by a reduction in outflows of

remittance outside the economy and also a drop in transfers of workers' remittances to residents.

3. Capital and financial account

From the BOP compilation, the outcome under this account gives an indication of capital movements, as well as provides an idea of the net financial and investment position of the compiling economy.

In an environment of limited resources such as the Seychelles economy, capital inflows from abroad are required in order to support economic growth and many other socioeconomic objectives. For the year 2004, the provisional estimated outcome under the "capital and financial account" was a deficit for the second consecutive year. This amounted to R224 million and represented an increase in net capital and financial outflows relative to the previous year. Whilst the capital account showed a significant contraction in capital transfers into the domestic economy compared to the previous year, the financial account portrayed an increase in net capital outflows.

3.1 Capital account

For the year 2004, the aggregate amount of capital inflow was R5.4 million. This was a significant contraction of R35 million compared to the preceding year when the sum of bilateral and multilateral capital inflows amounted to R40 million. The total contribution from bilateral donations was

R2.5, million whilst R3.0 million was received from multilateral agreements.

3.2 Financial account

Following a deficit last year, provisional estimates for the year 2004 showed another shortfall of R230 million in the financial account. The outcome was greatly influenced by the country's transactions under "other investment" which was likewise in deficit for a second year.

"Other investment" which represented the largest value of transactions under this account, was in shortfall of R400 million in 2004. This represented a contraction of R45 million in net liabilities in comparison to the previous year. On the asset side, the estimated movement was from R80 million in 2003, down to R67 million in 2004. Such development suggested that residents were drawing down on their assets abroad. On the liability side, which mostly shows loan transactions, the decrease was from R365 million in 2003 to R332 million in 2004. The loan component showed an accrued net repayment position of R259 million or a reduction in net liabilities from R345 million recorded in the previous year. Therefore, in comparison with the preceding year, the estimated combined accrued net repayment of loans by the monetary authority, government, parastatals, commercial banks, and private companies contracted in 2004 as compared to 2003.

As for foreign direct investment, the period continued to record a positive net inflow. However, from R272 million in 2003, the figure fell by R107 million to R164 million. The gross inflow of investments in Seychelles fell by R110 million or 35 per cent. As in the preceding year, this mainly represented investment in the tourism sector which was less than in 2003. Moreover, for the year being reviewed, most of these inflows were with respect to renovation of existing establishments rather than investments of new businesses. The drop in gross direct investment inflows was linked to the lower level of investments under all main components under this head. For once, total funds of equity investment registered a drop of R8.9 million or 4.9 per cent. In addition, re-invested earnings in Seychelles fell by R16 million or 32 per cent and unlike the year 2003, in 2004, no sale of government assets to non-residents took place.

Outward direct investment was estimated at R42 million, representing a reduction of R2.2

million below the year 2003's level. This figure comprised of R25 million worth of equity and a reduction of R17 million in amounts re-invested abroad by residents.

With regards to portfolio investments, this stood at an estimated net inflow of R5.9 million, which was a slight drop of 2.8 per cent compared to the level registered in 2003.

4. External reserves

In the past few years, the country has observed fluctuations in its stock of reserves. At the end of the year 2004, gross official reserves, which comprise of Central Bank and government amounted to R190 million (US\$35 million). With regards to Central Bank reserves which stood at R188 million (US\$34 million), this represented a reduction of R181 million or 49 per cent from R369 million (US\$67 million) recorded in 2003. In terms of reserves adequacy, gross official reserves were in total equivalent of 3.9 per cent weeks of 2003's c.i.f. imports value.

Table 4.6
External Reserves;¹ 1999-2004

	1999	2000	2001	2002	2003	2004
	(R million)					
Gross official reserves	162.7	274.2	213.4	352.7	370.6	190.2
Central Bank	160.2	271.1	210.6	352.3	369.2	187.8
Government	2.5	3.1	2.8	0.5	1.4	2.4
Central Bank's short-term						
Borrowings	211.2	403.4	373.2	802.6	693.3	494.0
Net official reserves	-48.5	-129.2	-159.8	-449.8	-322.7	-303.8

¹ End-of period data.

Source: Central Bank of Seychelles

5. Exchange rates

In 2004, the rupee continued to be pegged against the Seychelles Trade and Tourism Weighed Basket (STTWB) of currencies. In line with the reform programme introduced in July 2003, the exchange value of the rupee per US dollar was not allowed to fall below 5.50 per unit of US dollar. Therefore, it followed that despite the development in the international market where the US dollar was exchanged at record lows against most commonly traded currencies, especially the euro, the value of the rupee/ US dollar remained stable.

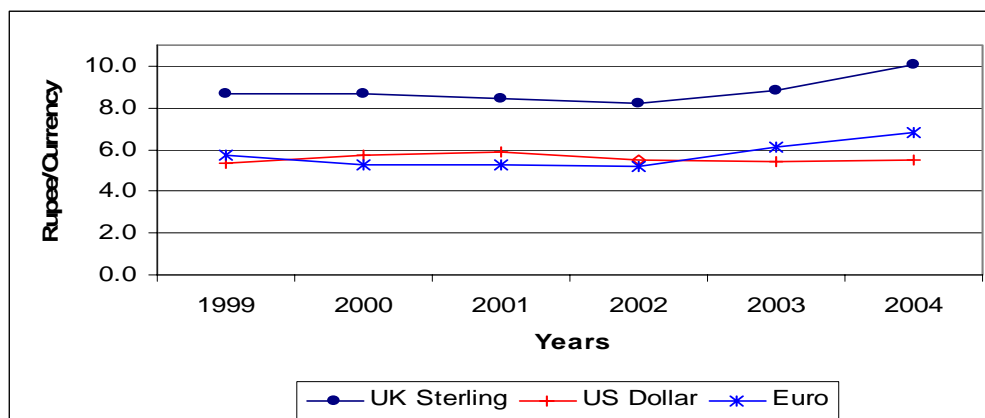
Nevertheless, during the year 2004, the Seychelles rupee observed a general weakening in its trading value against most of the world's major currencies. This followed the trend observed in the previous year when the only gain in strength of the domestic currency was 1.6 per cent to the US dollar. However, the range of depreciation narrowed to between 1.8 and 18 per cent. The lower end

corresponded to the movement of the rupee to the US dollar.

The weakening of the domestic currency was greatest relative to the South African rand. Nonetheless, this was at a reduced level of 18 percent compared with 38 per cent in 2003. It is of significance to note that since 2003, the rand has strengthened remarkably against most international currencies.

As for the remaining movements in exchange rates, the domestic currency depreciated by 15 per cent against the Australian dollar and 14 per cent against the UK pound sterling. Against the euro and the Swedish krona, the rupee weakened by 12 per cent. With regards to the Swiss franc the rupee lost 10 per cent of its value. The remaining depreciation of the rupee against some of the major currencies published by the Central Bank of Seychelles were 9.4 per cent (Canadian dollar), 8.9 per cent (Japanese yen), and 5.0 per cent (Singapore dollar).

Chart 4.5: Exchange rate movements of the three main currencies in the STTWB;1999 – 2004



Source: Central Bank of Seychelles

In view of the persisting foreign exchange shortages, as illustrated by the size of the pipeline deposits, evidence suggest that hard currencies were being traded in the unofficial foreign exchange market. This implied that

over the period and similar to the preceding year, foreign currencies were bought and sold at a premium above the official exchange rate. Unfortunately, this report cannot substantiate the quantum of such premium during the year.

Table 4.7
Exchange Rates;¹ 1999-2004

	1999	2000	2001	2002	2003	2004
(Seychelles Rupees per currency unit)						
Euro	5.6980	5.2650	5.2516	5.1751	6.1154	6.8378
US dollar	5.3418	5.7132	5.8585	5.4883	5.4013	5.5000
Pound sterling	8.6415	8.6446	8.4397	8.2329	8.8292	10.0747
Deutsche mark	2.9217	2.6917	2.6851	-	-	-
Japanese yen	0.0471	0.0530	0.0483	0.0438	0.0467	0.0509
French franc	0.8710	0.8026	0.8004	-	-	-
Italian lira	0.0030	0.0027	0.0027	-	-	-
South African rand	0.8742	0.8248	0.6925	0.5225	0.7211	0.8532
Singapore dollar	3.1515	3.3132	3.2714	3.0633	3.1001	3.2539

¹ *Period averages.*

Source: Central Bank of Seychelles

SECTION FIVE

The Real Sector: Production, Employment and Prices

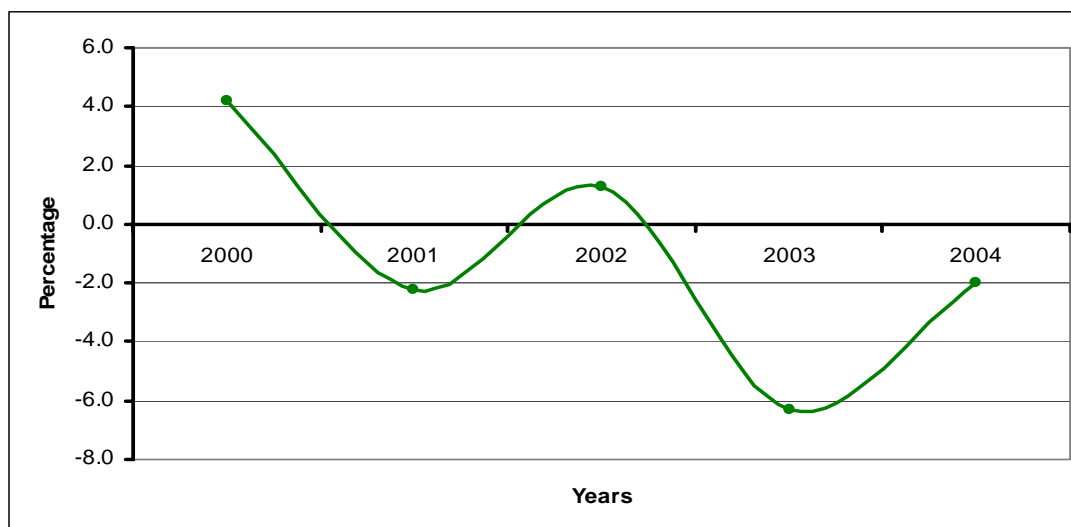
1. National Income and Production

The Seychelles economy which is dominated by a few industries experienced a decline in domestic output throughout the year 2004. Various factors were responsible for the slowdown. Most industries continued to operate sporadically on account of acute shortages of hard currency necessary to import raw materials, equipment and spare parts. Moreover, the introduction of the GST increased their operating cost base and on the demand side, led to a general contraction in consumer demand. Further production disruptions were caused by an acute water shortage in 2004.

The policy priority in 2005 is to arrest the decline in domestic output. This is a challenging task and prospects ahead are mixed. Measures taken by government to stimulate activity in tourism, agriculture and

fisheries can be expected to raise output but on the other hand, the anticipated slowdown in the Euro Zone economies (*which account for at least 65 per cent of our tourist arrivals*) could delay the recovery in the tourism sector which would in turn impede recovery in the overall economy. In addition, no significant improvement in foreign exchange availability can be expected in 2005 to ease the plight of the manufacturing sector.

According to the 2004 provisional estimates of national income produced by the Management and Information System Division (MISD) of the Ministry of Economic Planning, real GDP dropped by 2.0 per cent as shown in Chart 5.1. Recessionary tendencies were broad-based and most sectors registered downturn compared to 2003, notably 'manufacturing' and the 'services' sector.

Chart 5.1: Percentage change in Real GDP; 2000 – 2004

Source: Management & Information Systems Division

The rate of inflation rose from 3.3 per cent in the preceding year to 3.9 per cent, mainly on account of the effect of the GST. Partly in

consequence, nominal GDP registered a growth of 1.8 per cent.

Table 5.1
Gross Domestic Product by Kind of Economic Activity; 2000 – 2004
at constant (1986) market prices

	2000	2001	2002	2003 ¹	2004 ²
Percentage Change	4.2	-2.2	1.3	-6.3	-2.0
	(R million)				
GDP at market value	2615.4	2557	2589.3	2425.4	2376.4
Agriculture, forestry and fishing	78.6	74.7	76.1	69.9	69.4
Mining, manufacturing and Handicrafts	455.1	441.1	452.4	400.7	365.4
Electricity and water	106.9	112.2	133.4	135.7	137.4
Building and construction	199.6	202.2	210.6	168.1	225.3
Transport, distribution and Communications	1005.8	959.7	938.2	833.0	808.9
Hotels and restaurants	71.1	78.2	77.5	68.4	67.0
Financial and business services	230.7	229.0	216.7	207.5	210.0
Government services	193.6	191.2	207.1	184.7	177.3
Other services	274.0	268.7	277.3	357.4	315.7

¹ Provisional

² Preliminary Estimates

Source: Management & Information Systems Division

Table 5.2
Gross Domestic Product by Kind of Economic Activity; 2000 - 2004
 at current market prices

	2000	2001	2002	2003¹	2004²
	(R million)				
GDP at market value	3513.3	3622.5	3825.5	3797.2	3867.0
Agriculture, forestry and fishing	99.4	103	110.3	100.5	100.7
Mining, manufacturing and Handicrafts	674.9	654.8	698.0	623.2	645.0
Electricity and water	47.8	61.5	74.7	78.7	61.1
Building and construction	296.8	307.4	384.2	342.5	379.8
Transport, distribution and Communications	1032.9	1069.8	1110.6	1088.9	1173.1
Hotels and restaurants	324.2	383.7	379.8	350.5	389
Financial and business services	362.4	364.4	376.3	378.5	381.2
Government services	433	443	458	488.8	492.5
Other services	241.9	234.9	233.6	345.6	244.6

¹ Provisional

² Preliminary Estimates

Source: Management & Information Systems Division

During the year, economic activity continued to be dominated by the services sector which accounted for 66 per cent of the total value added. However, in relation to 2003, this represented a contraction of 1.6 percentage

points in its share of GDP. On the other hand, the distribution of the primary and secondary sectors increased by 0.04 percentage points to 2.9 per cent and 1.6 percentage points to 31 per cent, respectively.

Table 5.3
Gross Domestic Product by Broad Productive Sectors; 2000 – 2004
 at current market prices

	2000	2001	2002	2003¹	2004²
	(R million)				
GDP	3513.3	3622.5	3825.5	3797.2	3867.0
Agriculture, forestry and fishing	99.4	103.0	110.3	100.5	100.7
Industries	995.7	997.5	1128.4	1018.1	1055.5
Tourism	630.8	697.8	707.0	660.2	725.8
Government	433.0	443.0	458.0	488.8	492.5
Other services	1354.4	1381.2	1421.8	1529.6	1492.5

¹ Provisional

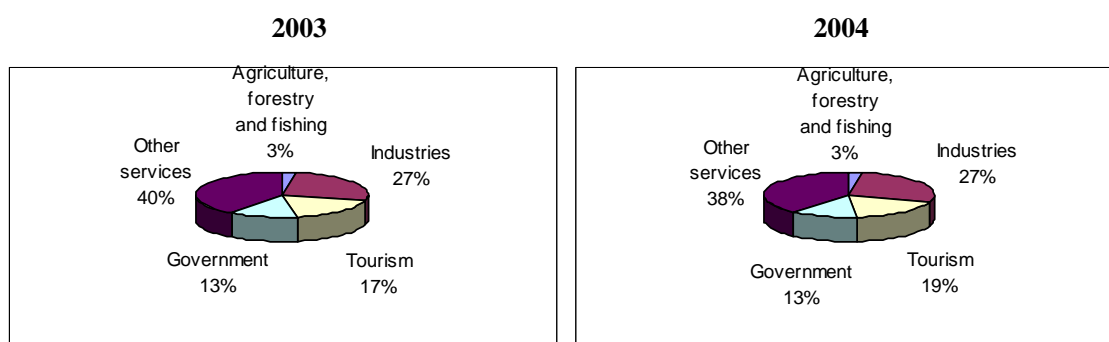
² Preliminary Estimates

Source: Management & Information Systems Division

A comparison of the nominal value added contribution by the broad sectors, as illustrated in Table 5.3, reveals a similar pattern to the corresponding constant GDP data. The share of GDP of the primary and secondary (industries) sectors remained at 2.6 per cent and 27 per cent respectively. There was a slight change in the share of the three main services items namely 'tourism', 'government'

and 'other services'. The 'tourism' share, led by the rise in prices within this sector, rose by 1.4 percentage points to 19 per cent. Conversely, 'government' share of GDP fell by a minimal 0.1 percentage points to 13 per cent. The share of the 'other services' similarly declined from 40 per cent in 2003 to 38 per cent in the year under review.

Chart 5.2: Share of nominal GDP by broad sectors



Source: Management & Information Systems Division

1.1 Primary sector

According to the provisional national income figures, output in the primary industry was driven by the performance of the fisheries sector. In the year under review, the contribution of the primary sector fell by 0.7 per cent in real terms. Yet, the production figures recorded for this sector showed a better outcome compared to 2003. This suggests that either available production indicators do not fully cover the full spectrum of activities in the sector, or further reconciliation of data is required.

1.1.1 Fisheries

As showed by the provisional catch figures issued by the Seychelles Fishing Authority

(SFA), there was an increase in the local sub-sector fishing activity. By the end of the year under review, the volume of fish landed by the artisanal fleet improved by 14 per cent to 4,374 metric tonnes. (See Table 5.4). On a similar note, the semi-industrial long-line fishery which continued to suffer the consequences of the restriction on export of swordfish to the EU market due to the level of cadmium, posted an increase in its total landed catch to 122 metric tonnes. Even though this compared better to the 92 metric tonnes recorded in 2003, it stood relatively low relative to the years 2000- 2002.

Table 5.4
Estimates of Fish Landed by Fishing Method; 2000 – 2004

	2000	2001	2002	2003	2004
	metric tonnes				
Artisanal	4,764	4,290	4914	3853	4374
Semi-industrial (long-line)	290	238	247	92	122
Industrial (1)					
- Caught	330,340	296,141	379,253	407,684	356,352
- Trans-shipped	269,673	255,551	332,860	359,136	306,274

¹ The industrial statistics for 2004 are CBS estimates.

Source: Seychelles Fishing Authority

In view of the above, export estimates showed a significant decline of 46 per cent and 61 per cent in the volume and value of 'fish and frozen fish' exported, respectively. However, as the ban on export of swordfish to the EU market is expected to be removed in 2005 with a higher permissible level of cadmium, catch is expected to increase with a resultant rise in export.

With regards to development financing, the total amount of funds pledged for investment stood at R13 million, indicating a fall of 15 per cent over the previous year. The Development Bank of Seychelles (DBS) approved a total of 30 'fisheries' loans for a value of R3.2 million as compared to 34 for R4.5 million in the previous year. Total lending by the commercial banks amounted to R10 million. In relation to the previous year, this represented a fall of 9.1 per cent. Under the re-finance scheme there was no disbursement during the year.

For the year 2005, investment in this sector is expected to be boosted on account of an

Agriculture and Fisheries Incentives Bill which is expected to be enacted in early 2005. This bill would include several fiscal incentives to promote investment and reduce costs in these two important sectors. Consequently, a higher level of production should be achieved in 2005.

Further investments in infrastructure are also likely to be undertaken upon the approval of the fisheries grant aid project from the government of Japan. The project will consist of the development of a new fishing port at the Providence Industrial Estate and an ice plant for Bel Ombre district. Government is also contemplating constructing small fishing harbours at district level in the manner of Bel Ombre as a way to decentralise the fishing activity away from Victoria.

At the industrial fisheries level, government will implement a downward revision in the tuna transshipment tax in 2005 in order to enhance the competitiveness of Port Victoria as a transshipment hub. This should in turn encourage the foreign fishing vessels to trans-

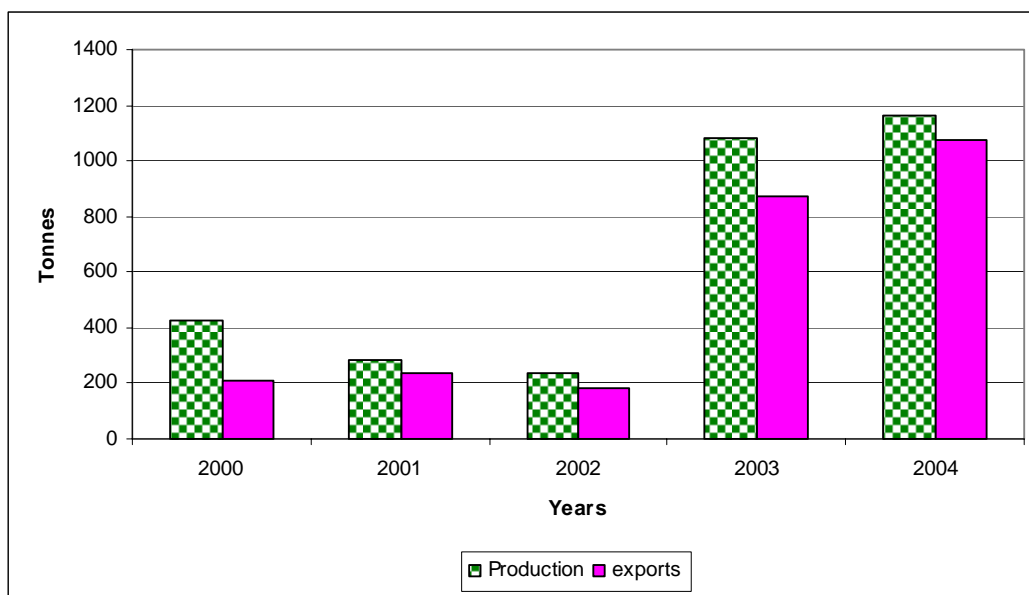
ship a higher proportion of their catch in Seychelles.

Contrary to the rise in the catch in the local fishing sub sectors, the performance of the industrial tuna fishing activity was not as good as in the previous year. The estimated total turnover for the tuna fishing fleet pointed to a reduction of 13 per cent to 356,352 metric tonnes as compared to the record 407,684 metric tonnes in 2003. Likewise, the estimated transshipment dropped by 15 per cent relative to 2003 to 306,274 metric tonnes. This was despite the completion of the project to repair and re-align the tuna quay in the fishing port during the year.

1.1.2 Aquaculture

The production of prawns which made a remarkable recovery in 2003, maintained its level of performance throughout 2004 (See Chart 5.3). This reflected the latest investment made in the industry. By the end of the year under review, its total yield stood at 80 tonnes above the 1,084 tonnes registered in 2003. According to the figures from the industry, prawns exported amounted to 1,078 tonnes, representing 93 per cent of the total 1,164 tonnes produced. In turn, higher export earnings were posted.

Chart 5.3: Prawns Production Indicators; 2000 – 2004



Source: SMB's Prawns Industry

1.1.3 Agriculture

The real value added contribution of 'agriculture' remained at the same level as in the previous year. In contrast, an increase of

3.0 per cent was recorded in nominal terms. Yet, the production estimates pointed to an improvement in the agricultural products, thanks in part to the range of continued

technical assistance and institutional support provided to the sector by the Ministry of Environment and Natural Resources throughout the year.

The production of vegetables and fruits posted an increase (9.7 per cent and 2.3 per cent, respectively) in 2004 though at slower rate than in the previous year. As for the production of the traditional cash crops (cinnamon and copra), this remained particularly low and geared for domestic

consumption rather than exports. Similarly, the overall livestock production in 2004 was better than in 2003. This was despite the significant rise in the cost of animal feed which caused a few smaller farms to cut down on production and others to report losses. Meat production posted a 6.0 per cent increase to 2,170 tonnes (See Table 5.5). On account of the increase in domestic output, the imports of the respective farm products fell during the year.

Table 5.5
Production of Crops and Livestock product; 2002 - 2004

	2002	2003	2004 ¹
	tonnes		
Crops	3698	4253	4581
Vegetable	2152	2556	2796
Fruits	1088	1137	1163
Root crops and spices	458	560	622
Livestock product	1980	2047	2170
Poultry meat	1274	1433	1504
Pork	692	601	649
Beef	14	13	17

¹ Crops production for 2004 are CBS estimates

Source: Ministry of Environment and Natural Resources

The strong performance of the agricultural sector during the year was achieved against the backdrop of unfavourable weather conditions. The prevalence of drought spells and occasional short heavy rainfalls eroded the soil and flooded some farms on the coastal areas. Another major setback was the continued difficulty to access foreign exchange to import critical inputs. This brought about many undesirable effects such as an inconsistent and

inadequate supply of materials and equipment, especially for crop development. In consequence, several investments especially in new farming techniques were delayed, pending the availability of foreign exchange.

Notwithstanding the above, new developments were observed in this sector. Farmers in 2004 benefited from 18 loans (8 to support the livestock sector and 10 for crop development)

for small agricultural development under the Agricultural Development Fund¹. These were for a total sum of R1.2 million and were approved to assist 18 farmers. An additional 18 loans were approved by the Development Bank of Seychelles (DBS) valued at R6.9 million. In the following year, investors in the agricultural sector will continue to benefit from loans from both sources. Further external assistance to the sector is likewise expected.

In addition, as mentioned above, the Agriculture and Fisheries Incentives Bill will provide additional benefits to all registered farmers. These will include trades tax and GST exemptions on capital equipment and a flat 5.0 per cent trades tax on imported raw materials. Moreover, as from January 1, 2005, farmers will be exempted from payment of business taxes on profits below the threshold of R240,000 per annum. Although this will have a negative impact on government revenue, it would help to improve the value added contribution of the agricultural sector.

Hence, 2005 is expected to be a better year for this sector in terms of output. Along with all the projects planned for 2005, the Ministry responsible for agriculture will continue its effort in the livestock sector, so as to attain 100 per cent self-sufficiency in poultry and pork during the next decade. Similar efforts would be geared towards meeting 80 per cent of the country's consumption of fruits and

vegetables. Further attempts will also be made to promote organic crops and floriculture along with the exploitation of spices, essential oils and traditional plantation crops in order to expand and diversify the agricultural base.

1.2 Industries

The 'industries' was the only large sector which posted an increase (3.3 per cent) in real output in 2004 relative to the preceding year. This was spurred by vigorous activity in the construction sector and not the manufacturing sector, which remained comparatively sluggish.

Despite the disappointing outcome of most manufacturing businesses in 2004, it is hoped that there would be a turnaround in the level of such activities in 2005. This would be on account of new government initiatives to modernise the economy and provide a better business environment for local companies. To this end, the number of monopoly items imported by the SMB was reduced in 2004. Effective January 2005, the monopoly rights of the SMB will be removed completely. This would allow the private sector to compete with SMB on a more level playing field. The government also intends to implement a privatisation programme to extend the role of the private sector and promote competition. Additionally, it is expected that the trades tax will be removed or reduced significantly on most imported inputs throughout 2005.

¹ The Agricultural Development Fund is a low interest loan scheme facilitated by the Ministry of Environment and Natural Resources (MENR), with grace periods extending to at least six months.

Construction activity was significantly up in 2004, thanks mostly to investments in the tourism sector and real estate. Construction activity is expected to remain strong in 2005 on account of reparation works on the infrastructures and buildings which were damaged by the tsunami in late 2004. However, without an improvement in the foreign exchange situation, growth in the 'industries', including construction, would continue to be hindered and business plans to improve earnings potential could be adversely affected.

1.2.1 Construction

In real terms, output of the construction sector made a remarkable recovery of 34 per cent in the year, after contracting by 20 per cent in 2003. Over the past years, the demand for construction services has been linked to a large extent to government's capital projects and new tourism investments. In 2004, construction activities were mainly private-sector driven, notably by the tourism industry. Two major non-tourism private sector's projects were the construction of the Caravel House and the Dockland complex, of which the latter was completed in the year. On the whole, activity in this highly import-dependent industry was heavily constrained by the shortage of the foreign exchange, causing acute difficulties in sourcing building materials.

1.2.2 Manufacturing

On a less positive note, output of the manufacturing industries remained subdued in 2004. The foreign currency shortage remained the dominant factor for this deterioration in

real output. This caused many businesses to close down while others experienced reductions in output. Additionally, the higher cost of production, especially following the imposition of the GST, and the weakening of the rupee against the major currencies, reduced the sector's competitiveness and profitability. In real terms, the contribution of manufacturing, including handicrafts, fell by 8.8 per cent although in nominal terms, a rise of 3.5 per cent was recorded. The rise in current prices was due to the increase in import prices which also contributed to the slump in output.

Given the size of the economy, the manufacturing sector is dominated by a few large entities, namely the Indian Ocean Tuna Canning factory and the Seychelles Breweries Ltd (SEYBREW), with the rest being small to medium sized enterprises. The output of these two industries, stood below the level recorded in 2003.

The production of total canned tuna by the Indian Ocean Tuna Canned factory recorded a decline (*5.0 per cent*) in 2004 compared to 2003. To some extent, this would be due to the water shortage towards the middle of the year, which caused a halt in production activity. Yet, the quantity of this product exported grew by 2.7 per cent to 36,711 tonnes, although in value terms a contraction was observed.

Similarly, the total production of the SEYBREW compared less favourably relative to the three previous years. In 2004 relative to 2003, its overall volume of production

plummeted by 15 per cent, mostly affected by the fall in ‘soft drinks’. However, total sales receipts increased by 1.3 per cent. This reflected the higher-priced products of the company following the introduction of GST, which also influenced the consumers to shift to other available substitutes, notably fruit juices and imported beers.

As for ‘electricity and water’, it experienced an expansion in real output (*1.3 per cent*) despite the water shortage experienced during the year. This rise was associated with the increase in electricity production on account of a continued rise in demand. In current terms however, output declined from R79 million to R61 million.

1.3 Services

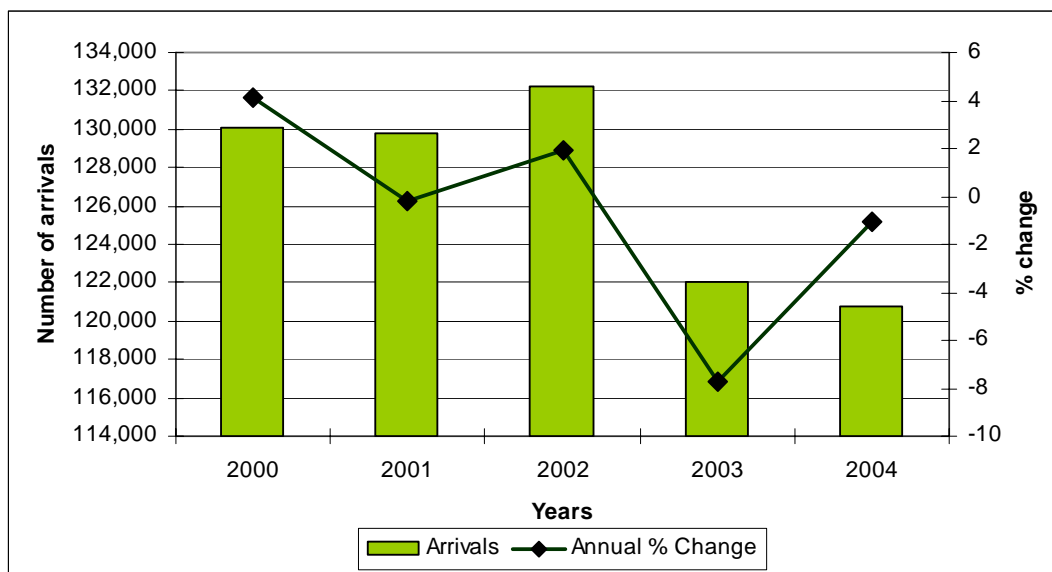
Overall, the tertiary sector, experienced a contraction of 4.4 per cent in real output. The

decline was largely due to the lacklustre performance in tourism and its affiliated services. ‘Tourism’, which forms the backbone of the services sector, fell by 2.4 per cent in 2004 as compared to 2003. This was due to the lower visitor arrivals. In nominal terms however, tourism output rose by 9.9 per cent, reflecting the impact of higher prices in the business.

1.3.1 Tourism

The tourism industry which is the main industry of the Seychelles economy, contributed a share of 19 per cent to GDP at current prices during the year under review. This sector directly employed 20 per cent of the labour force and generated R756 million worth of foreign exchange in 2004.

Chart 5.4: Visitor Arrivals; 2000 – 2004



Source: Management & Information Systems Division

There are increasingly serious concerns that tourism is fast losing its competitiveness. This worries all stakeholders because of the downstream repercussions on other economic sectors. In 2004, visitor arrivals declined by 1.0 per cent. (See Chart 5.4). Though this was not a significant fall, it brought the tourist figure down to the lowest point recorded over the past nine years. The total 120,765 arrivals recorded in the year under review stood at only 45 visitors above the corresponding 1995 total.

An analysis of the data reveals that in relation to the previous year, arrivals were worst in the first half of 2004 as opposed to the second half. For the first six months of the year, in relation to the same period of 2003, the number of visitors declined by 7.2 per cent, but in the second half of the year, this increased by 5.6 per cent. This turnaround may perhaps be attributed to the initial success of the Tourism Incentives Act (TIA) at re-energising the sector. If sustained, this is a most encouraging trend for Seychelles.

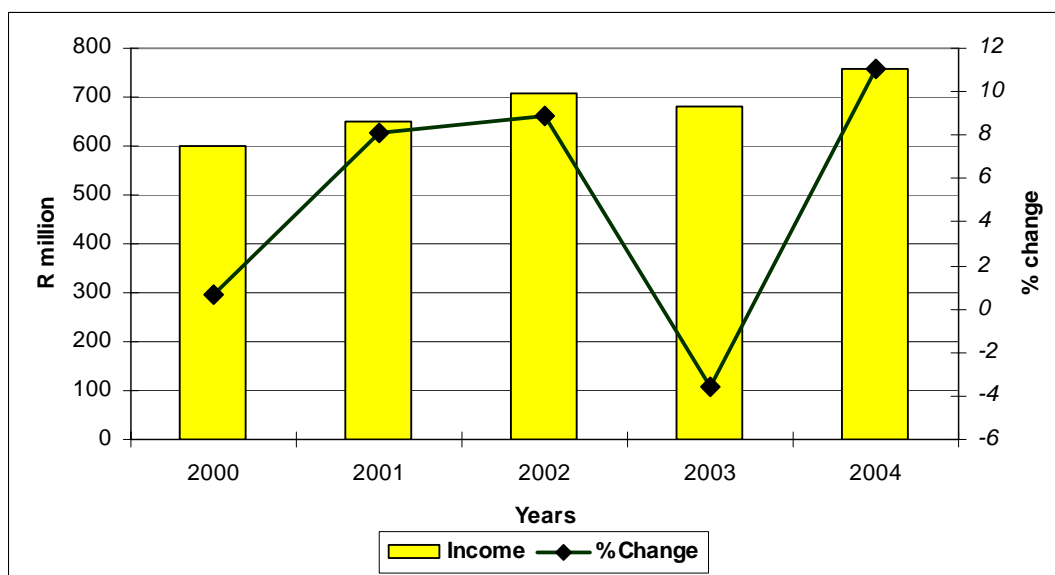
Table 5.6
Tourism; 2000 - 2004

	2000	2001	2002	2003	2004 ¹
Visitors nights- thousands	1352	1350	1331	1239	1210
Visitors arrivals - thousands	130	130	132	122	121
Average length of stay (nights)	10.4	10.4	10.4	10.1	10.0
Tourism income - R million	600	649	706	681	756
Average expenditure per diem	445	480	527	550	624
Memorandum					
Hotel bed occupancy rate (%)	52	51	52	46	44

¹ Visitor nights and hotel bed occupancy rate are CBS estimates
Sources: Management & Information Systems Division (except tourism income which is from Central Bank data)

On another positive note, notwithstanding the relatively unsatisfactory outcome in arrivals, tourism income converted into local currency through the local banking system recorded a significant increase. One influential factor was the fall in the value of the rupee against the euro throughout the year. Another was the prevailing higher prices in the average room rate charged by the sector on account of an

increased number of high-end properties. For the second time in the last five years, income exceeded R700 million and amounted to a record high of R756 million (See Chart 5.5). This represented an improvement of 11 per cent compared to the amount of income generated in 2003. The average expenditure per diem per visitor rose to R624 compared with R550 in the previous year.

Chart 5.5: Tourism Income; 2000 – 2004

Source: Central Bank of Seychelles

For the year 2004, Europe remained the top market, despite a fall of 1.3 per cent to 98,387 in the number of visiting tourists. However, three of the four most important countries (*in terms of share in arrivals*), namely the UK & Eire, Italy and Germany recorded declines in arrivals. Visitors arriving from these fell by 0.8 per cent, 0.4 per cent and 0.2 per cent respectively. On the other hand, France, which remained the leading market with a share of 22 per cent, posted a slight increase of 0.2 per cent. The second most important market, UK & Eire, accounted for 15 per cent of total arrivals.

The number of African tourists to Seychelles declined by 7.2 per cent in 2004 whilst visitors arriving from the other continents, recorded increases. The largest increase was from Oceania, from 502 to 713 visitors which represented 0.6 per cent of the total market.

Asian and American visitors increased by 4.4 per cent and 16 per cent to 4,981 and 4,030 respectively. Consequently, as in the case for Oceania, they experienced a rise in their market shares.

Total bed capacity in the country increased from 4,980 to 5,025 in 2004. As a result, the average bed occupancy rate fell further below the benchmark of 50 per cent. For the year 2004, it stood at an estimated 44 per cent compared with 46 per cent in 2003. As was the case in the previous year, the 'other islands' continued to enjoy better occupancy rate than the main island, Mahe. Similarly, occupancy rates were higher in the 5-star establishments compared to the lower-class establishments. In terms of average length of stay, this declined slightly to 10.0 nights in 2004 compared to 10.1 nights in the preceding year.

In view of difficulties in the sector, the government met with the trade during the year, to assess the existing state of the industry and to discuss possible solutions. Some of the main problems identified were low value for money as compared to similar products in the region and high costs of operations, leading to an uncompetitive product. For this reason, revisions were made to the TIA 2003 to lessen the adverse effects of the Macro Economic Reform Program (MERP) on tourism business. The revised Act became effective on July 1 and granted further benefits and concessions to all tourism related activities. It must be noted that these incentives were aimed at helping the operators to upgrade their products, improve service delivery and also to encourage new investment in the industry.

Notwithstanding the declining arrivals, interests in this industry remained high reflecting exciting long-term prospects. During the year, several projects were approved and one of them was a 5-star hotel at Port Launay by Corvina/Constance Group estimated at around US\$100 million. Other leading groups, such as Four Seasons, Southern Sun, and Hilton are also expected to start their projects in 2005. In addition to these new investments, there was also a number of renovation/extension works undertaken, such as the extension of the Banyan Tree resort. Other hotel establishments, like the Barbaron hotel managed by Le Meridien, started refurbishment during the year under review. Its 'sister' hotel, Le Meridien Fisherman's Cove, re-opened for business on June 1,

2004 as a 5-star resort and spa following a complete refurbishment with additional rooms. These developments should create additional employment opportunities and improve the scope for generating additional revenue in the future.

With regards to air services, British Airways made its last flight to the Seychelles in June 2004. The main reasons for this were the difficulties in repatriating rupee earnings and declining sales. In the second half of the year, the government took a bold step towards liberalising air access to the country. Two well-known airlines namely, Emirates and Qatar showed strong interests. The Emirates Airlines will commence operation in the first quarter of 2005 and as for Qatar Airways, it started its four weekly services to the Seychelles in late 2004.

As 2004 closed, the government and operators in the trade are increasingly optimistic of a turnaround in the industry. The vision 21 strategy: Tourism Development in Seychelles 2001 – 2010 envisages reaching a reasonable and achievable 180,000 of inbound tourists by the year 2010. This would mean an increase of almost 50 per cent over the 120,765 recorded in 2004, a target that can easily be achieved once the competitiveness of the industry is restored.

In conformity with the above aim, government announced that from January 2005, Trades Tax will be reduced on a wide variety of essential items feeding into the sector. Several operators will also benefit from Trades Tax

and GST exemptions on the services they offer. Therefore, an improvement in the products on offer as well as the quality of service is expected in 2005. To uphold product standards, the government will put in place a Tourism Standard Board. All these measures should go some way to enhance the competitiveness of the tourism industry.

Nonetheless, the slower growth rates which have been forecasted for the Euro zone could have a negative impact on the performance of tourism, where most of our visitors are originated.

2. Employment

For the first time in the past five years, estimates point to a fall in employment during

2004. The figure computed for end of December 2004 represented a decline of 1.2 per cent in the amount of employees to 41,169. Consistent with the last five years half of the total number of employment was recorded in the private sector. By the end of December 2004, estimated employment in the private sector stood at 20,590. Yet, as compared to 2003, the share of private employees fell by 0.5 percentage points. Similarly, employment from the public sector fell following some restructuring in that sector during the year. The number of jobs in 'government' declined by 0.7 per cent to 14,674. On the other hand, the parastatals recorded a rise in employment, though at the slowest rate (*1.1 per cent*) posted over the past five years, to 5,905.

Table 5.7
Employment; 2000 - 2004

	2000	2001	2002	2003	2004 ¹
Total	39381	40263	41687	41675	41169
Private Sector	19753	20944	21715	21060	20590
Parastatals	5550	5872	5957	5841	5905
Government	14078	13447	14015	14774	14674

¹ CBS estimates

Source: Social Security Fund

In the economic sectors, 'public administration and defence' remained the largest employer with an estimated share of 17 per cent of total workforce. The top job creation activity was in the 'fishing' sector whilst job losses were highest in 'real estate, renting and business activities'. The latter fell by 15 per cent

compared to 2003, partly reflecting the difficult conditions faced by private businesses in the year.

3. Earnings

The year 2004 estimates show that the average monthly earnings for all sectors rose by 3.8 per

cent in relation to 2003. This increased average earnings was from R3,603 to R3,740 at current prices with all sectors posting gains (Table 5.8). On average, the private workers

observed a rise of 6.4 per cent in monthly earnings, but even at this level, earnings still lagged behind those of the public sector.

Table 5.8
Average Monthly Earnings; 2000 – 2004

	2000	2001	2002	2003	2004 ¹
	(Rupees - current prices)				
All sectors	3343	3417	3465	3603	3740
Private Sector	3208	3303	3269	3297	3507
Parastatals	3693	3648	3865	3984	4027
Government	3561	3581	3593	3918	3997

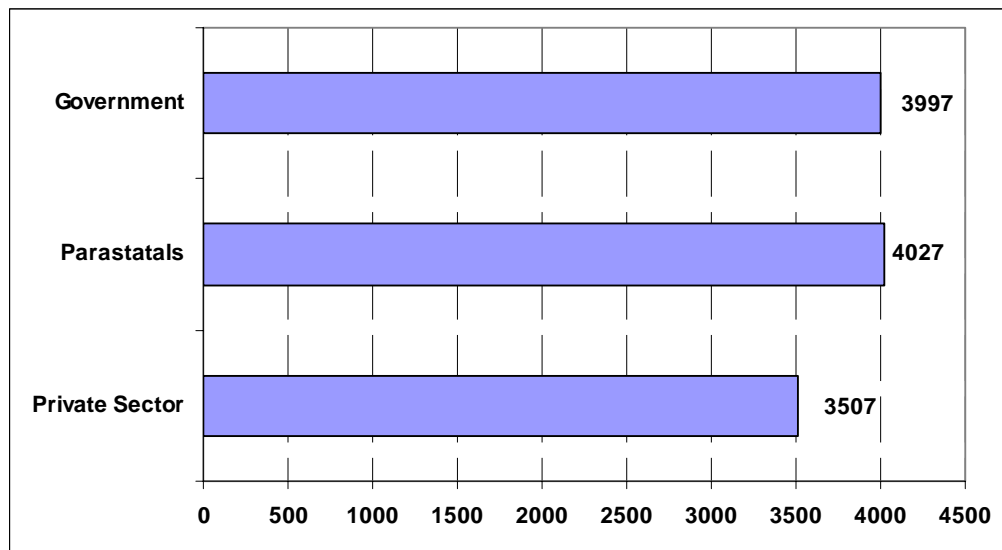
¹ CBS estimates

Source: Management & Information Systems Division

Although parastatal average earnings posted the slowest growth in 2004, they stood at the highest in the economy at R4,027. (See Chart

5.6). By comparison, average monthly earnings for the government sector increased by R79 or 2.0 per cent to R3,997.

Chart 5.6: Average Monthly Earnings for 2004



Note: CBS estimates²

Source: Management & Information Systems Division

² Based on the figures provided by MISD.

An analysis by industrial group showed that the highest average monthly earnings was recorded under 'transport, storage and communication' at R5,148. As for the lowest, this was posted under 'wholesale and retail trade'. Employees within the 'fishing' sector recorded the fastest increase of 18 per cent to R3,341, followed by the construction sector

(15 per cent). As for 'mining & quarrying' which recorded the fastest increase in the previous year, it continued to rise quite significantly at 9.5 per cent to R5,066. Other strong increases were recorded under, 'restaurants and hotels' and 'education' at 7.4 per cent and 6.9 per cent respectively.

Table 5.9
Average Monthly Earnings by Kind of Economic Activity; 2003 – 2004

	2003	2004(1)	
	(Rupees - current prices)		% change
Agriculture & forestry	2909.9	3067.4	5.4
Fishing	2826.0	3340.6	18.2
Manufacturing	2986.2	3136.6	5.0
Electricity & water	3780.1	3695.2	-2.2
Mining and quarrying	4625.2	5066.3	9.5
Construction	2667.8	3071.6	15.1
Wholesale and retail trade	2756.9	2845.8	3.2
Restaurants & hotels	3307.9	3551.6	7.4
Transport, storage & com	4723.2	5147.8	9.0
Public administration and defence	4115.5	4137.4	0.5
Financial intermediation	4990.7	5030.1	0.8
Real estate, renting and business activities	4189.8	3573.9	-14.7
Education	3390.8	3625.3	6.9
Health and social work	4126.5	4178.5	1.3
Other community, social and personal svcs	3804.8	3772.3	-0.9
	3602.6	3739.7	3.8

(1) CBS estimates

Source: Management & Information Systems Division

Nevertheless, a few declines were registered during the year. This mainly affected the employees within the 'real estate, renting and business activities services'. For the year 2004 as compared to 2003, they witnessed a 15 per cent drop in their average monthly earnings. There were also declines in average earnings in 'electricity and water' and 'other

community, social and personal services'. These two sectors registered a fall of 2.2 per cent to R3,137 and 0.9 per cent to R3,772 respectively.

4. Prices

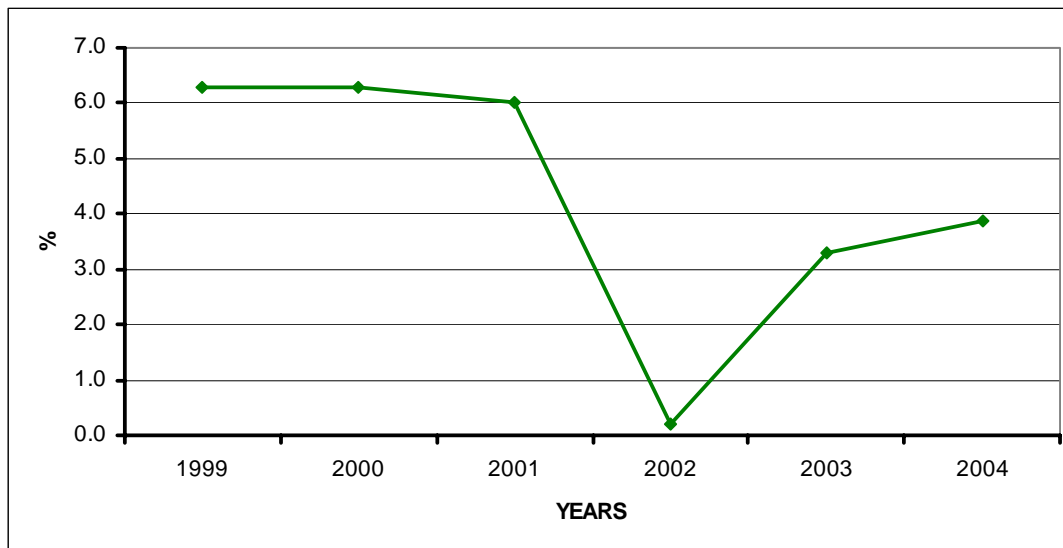
Inflation as measured by the movements in the Retail Price Index (RPI) has been relatively

high over the past few years. The only effective drop was in 2002 (*See Chart 5.7*), following the authorities' effort to curb the upward movement in prices. However, in 2003, following the introduction of the Goods and Services Tax (GST) as part of the MERP, there was a sudden upward shift in prices. The rate for the GST was set at 12 per cent with an effective rate of up to 15 per cent. Hence, by

the end of 2003, inflation had risen to 3.3 per cent compared to 0.2 per cent in 2002.

As expected, the effects of the GST continued to be felt in 2004, especially in the first six months. Thus, prices appeared more volatile in the year compared to 2003. By the end of the twelve months under analysis, the rate of inflation had picked up 56 basis points to stand at 3.9 per cent.

Chart 5.7: Yearly Inflation Rate; 1999 – 2004



Source: Management & Information Systems Division

A review of the movement of the inflation rate over 2004 revealed that on average, prices remained unstable. During the first six months of the year, the twelve-month inflation rate accelerated from 3.8 per cent in January to 6.4 per cent in June. However, exactly one year

after the GST was imposed and for the first time since January 2003, the rate of inflation slowed down slightly in July. (*See Chart 5.8*) Thereafter, as the impact of the GST faded, the general price level grew at progressively decreasing rates.

Table 5.10
Composition of the Retail Price Index; 2000 – 2004

		2000	2001	2002	2003	2004
	Weights					
			percentage change			
All Items	1000	6.3	6.0	0.2	3.3	3.9
Local	656	7.2	4.7	0.6	4.0	3.4
Imported	344	4.4	8.4	-0.5	2.2	4.6
Fish	32	-6.5	15.6	4.9	9.0	-7.1
Other Food	234	2.9	3.2	0.2	1.8	1.9
Local	119	4.5	2.7	2.0	3.4	2.8
Imported	115	0.7	3.0	-1.0	0.5	1.1
Non-Food Items	734	7.7	6.3	0.0	3.6	5.0
Local	505	8.6	4.6	0.1	3.8	4.1
Imported	229	5.5	9.9	-0.2	3.2	6.8

Source: Management & Information Systems Division(MISD)

In 2004, , much of the growth in the overall price level originated from the increase in the prices of the imported items as opposed to the domestically produced goods. This was despite the series of price reductions on a host of imported monopoly items by the SMB and the downward revision of trades tax. The import price index increased by 4.6 per cent in 2004 compared to 2.2 per cent in 2003. This change in the index of the imported items was partly influenced by the depreciation of the rupee against the major currencies. On the

other hand, the index of the local items dropped from 4.0 per cent to 3.4 per cent.

Except for the price of fish, all other components of the RPI observed an upward movement in their respective price index in 2004. Fish prices dropped by 7.1 per cent due to the high supply experienced throughout the year, the first decline in over four years. In 2004, the inflation rate of the 'non-food' index was 5.0 per cent whereas for 'other food', it amounted to 1.9 per cent, almost unchanged from the year 2003.

Table 5.11
Inflation rates of the components of the other food and the non-food for 2004

	weight	inflation rate		weight	inflation rate
OTHER FOOD	25.5	1.9	NON FOOD ITEMS	71.9	5.0
Bread and Cereals	8.7	1.7	Alcoholic beverages	10.7	8.4
Meat (Fresh, chilled, frozen)	3.3	4.5	Tobacco	0.5	2.0
Fish (frozen, smoked, salted)	0.2	7.6	Clothing and footwear	6.7	11.4
Milk, cheese and eggs	1.9	6.6	Housing, water, electricity and gas	14.8	1.3
oils and fats	1.0	-2.3	Furniture and household equipment	9	5.8
fruits	0.9	-5.0	health	1.3	4.7
vegetables	3.8	-3.9	transport	5.8	3.0
sugar, jam, honey & confec.	3.0	4.8	communication	4.5	7.2
food product n.e.c.	0.2	2.5	recreation and culture	5.5	3.6
non-alcoholic beverages	2.6	4.2	education	1.4	10.8
			restaurants and hotels	0.1	22.8
			misc. gds and svcs	11.7	2.0

Source: Management & Information Systems Division

A further analysis of the 'non-food' prices revealed that the influential item for the rise in its inflation rate was the development in the price increase of 'furniture and household equipment'. This subgroup of the 'non-food' increased by 5.8 per cent, 4.4 percentage points higher than in 2003. Likewise, the 'clothing and footwear' index rose by an average of 11 per cent compared to 5.9 per cent in 2003 which contributed considerably to the acceleration in the overall inflation rate of the 'non-food'. Yet, the largest acceleration in price growth was posted in the average price of education which swung from a negative 1.6 per cent to a positive 11 per cent. In terms of the inflation rates of the subgroups of the 'non-food', the most rapid rise in prices was posted under the tourism related item. During the year under review, the prices of

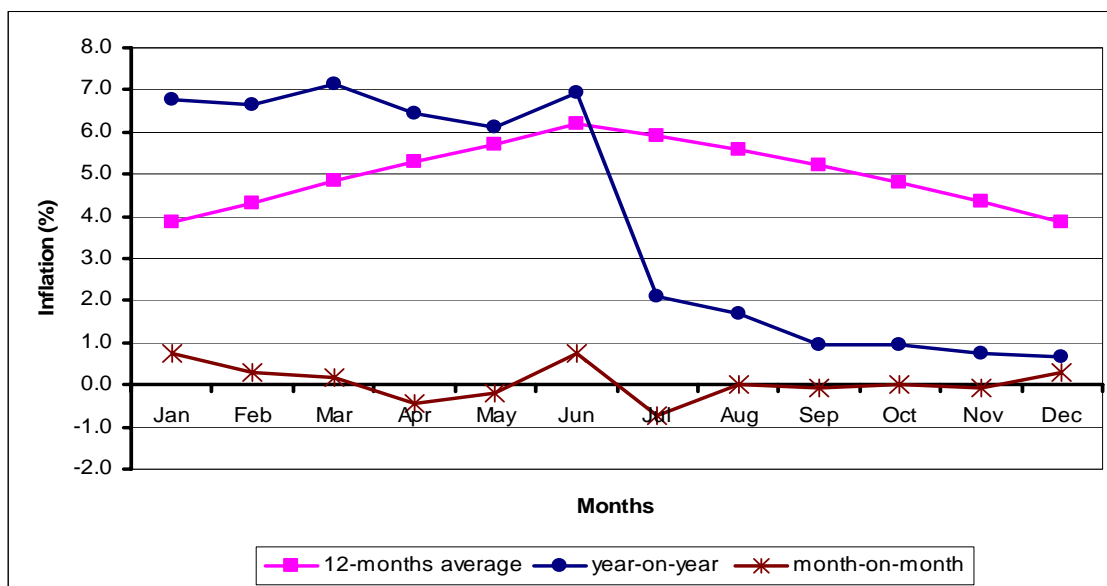
'restaurants & hotels' increased by 23 per cent compared to 14 per cent in the preceding year. However, the significance of this item in the basket is relatively low. As for the relatively high inflation rate of 'alcoholic beverages' (8.4 per cent), this played a key role on the overall rate for the 'non-food', despite a slight decline with respect to 2003.

As mentioned above, the rate of growth of the 'other food' prices remained almost constant in 2004 compared to 2003. The most substantial price increase was posted under 'fish (frozen, smoked, salted)' with an annual average growth rate of 7.6 per cent during the year under review. This represented an acceleration of 4.1 percentage points in relation to 2003. Similarly, the general price growth of 'milk, cheese and eggs' increased to

6.6 per cent. The acceleration in the price increase posted under ‘bread and cereals’ (from 0.3 per cent to 1.7 per cent) had the greatest impact on the growth in the inflation rate of the ‘other food, although its effect was greatly offset by the development in ‘vegetables’ prices. Compared with 2003 when the general price for ‘vegetables’ grew by 2.7 per cent, it fell by 3.9 per cent during the year being reviewed. As for the inflation rate for meat products, this climbed from 3.0 per cent to 4.5 per cent.

Taking into account the year-on-year price movement, this dropped from 6.8 per cent in January 2004 to 0.7 per cent by the end of the year. (See Chart 5.8). The largest monthly difference was from June to July, given that the GST was introduced in July 2003. Thus, in the second half of the year 2004, the year-on-year price gaps were narrower as compared to the first six months.

Chart 5.8: Inflation Rates for the months of 2004



Source: Management & Information Systems Division

The increase in prices in the months of 2004 as compared to the corresponding months of 2003 was greater for the imported items. During the first half of the year, the general price of imports grew by an average 7.6 per cent relative to the corresponding period of the previous year. The highest rate was posted in June, when prices relative to June 2003 rose

by 8.2 per cent. In the second half of the year, prices remained closer to those posted in the same period of the previous year, with an average rise of 1.7 per cent. The local price index also followed a similar pattern, albeit at slower rates. On average, in the first half of 2004, the prices of locally produced goods stood at 6.1 per cent above those recorded in

the same period of the preceding year. As expected, in the second half of the year, the average fell significantly to only 0.9 per cent.

In view of the major elements of the RPI, the year-on-year overall price movements were mainly associated with the changes in the average price of the 'non-food'. The price index of the 'non-food' remained above that

prevailing in 2003 all through the year. This was more apparent in the first six months as may be seen from Table 5.12. With regards to the general price of the 'other food', this moved at a slower pace than that for the non-food for each month compared with 2003. In the last six months of the year, its prices actually fell below those posted in the corresponding months of the previous year.

Table 5.12
relative changes in prices in 2004 compared to the same months in 2003

	all items	imports	local	fish	other food	non - food
weight	100.0	37.5	62.5	2.6	25.6	71.9
January	6.8	7.4	6.5	5.1	5.3	7.4
February	6.6	7.6	5.9	1.2	5.0	7.4
March	7.1	7.7	6.8	5.1	5.4	7.8
April	6.4	7.1	6.0	-12.3	5.4	7.5
May	6.1	7.7	5.2	-22.3	4.9	7.7
June	6.9	8.2	6.3	4.5	4.7	7.8
July	2.1	3.2	1.4	-4.9	-0.7	3.2
August	1.7	2.7	1.0	-5.7	-1.7	3.1
September	0.9	1.8	0.5	-19.5	-0.7	2.4
October	0.9	1.2	0.8	-8.9	-1.8	2.3
November	0.8	1.1	0.5	-13.9	-1.9	2.2
December	0.7	0.3	0.9	-9.1	-0.9	1.5

Source: Management & Information Systems Division

As for the year-on-year price of fish, this assumed a faster declining trend. On average, the recorded prices in the months of 2004 mostly fell below those which prevailed in the same period of 2003. The largest decrease in fish prices was posted in May at 22 per cent compared to May 2003, as a result of exceptionally higher catches compared to the previous year. Similarly, the decrease in the price of fish, especially in the second half of the year, followed the large supply of fish throughout these months. One other plausible explanation could be the fact that immediately

after the GST was imposed, fish prices rose considerably and subsequent to then, are now steadily normalising.

Outlook for 2005

Prices are expected to stabilise further in 2005, once the effects of the GST has fully filtered through the economy. The reduction in trades tax on a wide range of commodities should likewise keep price pressures at bay. However, given the openness of the economy, all this may be totally eroded by adverse movements in the exchange rate.

SECTION SIX

Operations and Administration of the Central Bank¹

1. Overview

The year under review, saw a continuation of the government's economic reform programme aimed at correcting the severe macroeconomic imbalances that have plagued the Seychelles economy during the past years. The reforms are predominantly centred on fiscal consolidation, but in addition involve a gradual scaling down of government involvement in economic activity and a move towards a more liberal economy with the State acting as regulator and facilitator.

Accordingly, the year 2004 saw the re-introduction of a tender system for the issue of treasury bills, under which, the interest rate of bills are market determined. The re-introduction of the tender system for the issue of treasury bills was conducted as a pilot project and the intention is to extend it to the issue of other government securities. The tender system would allow for a more efficient allocation of funds from surplus agents in the economy to government. As a matter of policy and in an effort to limit Central Bank credit to government, the former did not

participate in the tender for treasury bills in 2004.

An important institutional component of the reform programme is the decision to grant the Central Bank full administrative and operational independence from government. This was first announced by the President in July and the administrative order was followed by the enactment of the Central Bank Act in late December. Under the previous legislation, the Governor of the Bank also held the position of Principal Secretary in the Ministry of Finance. This may have led to a certain degree of ambiguity in economic policy decision-making as the Bank and government have different agendas. Under the new Act, the Governor of the Bank will no longer be allowed to hold the post of Principal Secretary of Finance. A new board of directors of the Bank was appointed, constituting of directors from both the private and public sector. The new Act also explicitly sets out the objectives of the Bank. The Act will enhance the credibility of the Central Bank both domestically and internationally, and

¹ All the data presented in this section is actual.

strengthen its role as financial watchdog of the economy.

Two IMF technical assistance teams visited the Seychelles during 2004. The first mission was to assist in the formulation of a more robust Anti-Money Laundering Act which is expected to be passed early in 2005. The subsequent mission conducted a multi-sector assessment of the compilation of statistics in the country and provided guidance on statistical practices and development in the areas of national accounts, prices, foreign trade, fiscal, monetary, balance of payments, external debt and selected socio-demographic statistics. The Bank also received the customary IMF Article IV team for their evaluation of the economy, although during 2004, the Article IV team split their mission into two visits, with the first concentrating on the 2003 Macro Economic Reform Programme (MERP) results and the second focussing on the usual Article IV assessment.

During the year, the Central Bank continued to perform its role as regulator of the financial sector, thus ensuring a sound financial system.

2. Banking Services

2.1 Currency and Banking Operations

The Banking Services Division has the responsibility of issuing currencies and managing accounts held with the Bank on behalf of the government, commercial banks, other local financial institutions, foreign governments and international agencies. It is also accountable for the daily financial transactions of the Bank and administers

temporary advances made to government, whilst closely monitoring external reserves. The sale of the numismatic coins and dealings in coins and notes with dealers abroad is yet another responsibility of the division.

2.1.1 Government accounts

Despite assurances given by government that it will limit its use of Central Bank credit as a source of financing, the year 2004 not only saw the continued usage of the Bank's advances by government but also a marked increase relative to the previous year. On a yearly average of monthly data basis, a 34 per cent increase in Central Bank advances was recorded, from R938 million in 2003 to stand at R1,262 million in 2004.

Similarly, on an end of period basis, Central Bank advances recorded a significant increase of 62 per cent to stand at R1,317 million in 2004 from a total of R811 million in 2003. This is shown in *Table 6.1* and *Chart 6.1* below. It must be noted that total advances is composed of two elements; short-term advances and foreign loans borrowed by the Central Bank which it on-lends to the government in the domestic currency. In 2004, short-term advances totalled R858 million, an alarming increase of 366 per cent over the previous year's total of R184 million. Back-to-back facilities of two loans amounted to R426 million, a fall of 32 per cent relative to the R627 million of 2003. The sharp increase in short-term advances reflects the difficulties that Government faced in managing its day to day cash flow.

With the new Central Bank Act in place, definite caps have been imposed on the amount of advances that the Bank can disburse to government; in future, government may

have no choice but to re-look at its whole operation so as to either find other sources of financing or to reduce its expenditure.

Table 6.1
CBS Advances to government; 1999-2004

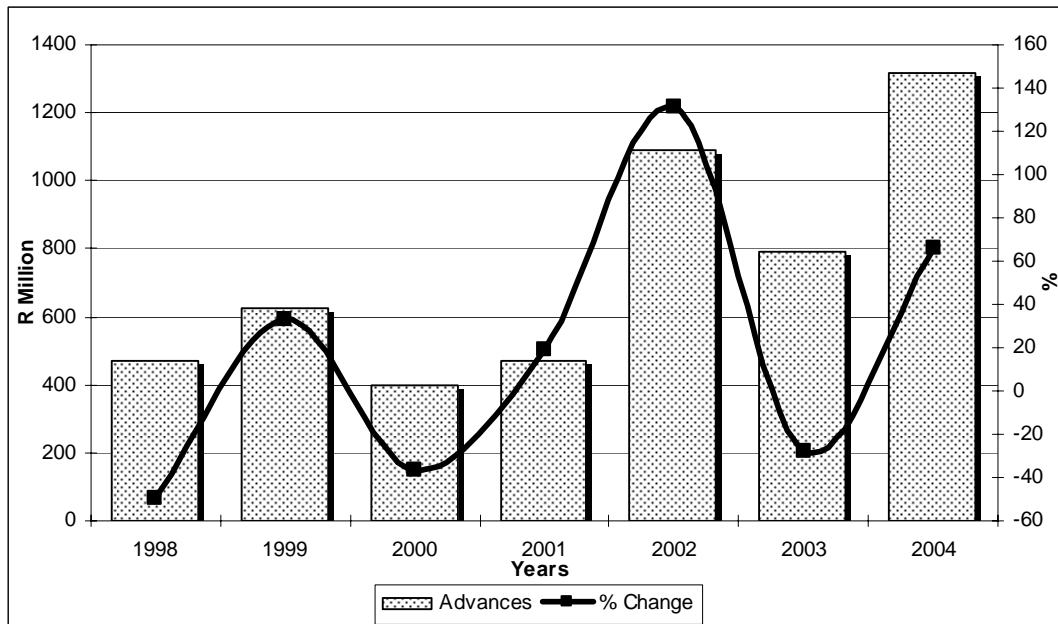
	1999	2000	2001	2002	2003	2004
	(R million)					
Advances ¹	547.2	58.3	493.9	650.8	938.3	1261.6
Advances ²	623.9	395.9	472.4	1092.0	811.0	1316.6
Growth ¹	-37.45	-89.35	747.22	31.77	44.17	34.46
Growth ²	33.03	-36.55	19.33	131.18	-25.73	62.34

¹ Yearly averages of monthly data compiled on an end-of-period basis.

² End-of-period data.

Source: Central Bank of Seychelles

Chart 6.1: CBS Advances (End-of-period) (1998 – 2004)



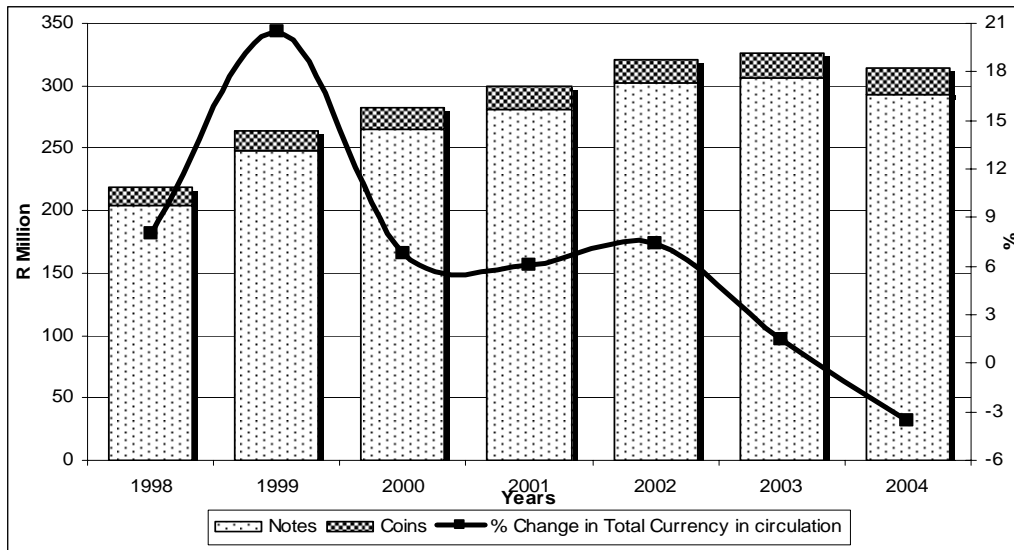
Source: Central Bank of Seychelles

2.1.2 Currency issues

Total currency in circulation at the end of the year stood at R315 million. This represents a 3.5 per cent decrease in 2004 relative to the previous year's total of R326 million. This is shown below in *Chart 6.2 and Table 6.2*.

Out of the total of currency in circulation, R294 million were in notes while the remaining R21 million were coins.

Chart 6.2: Notes and Coins in circulation (1998-2004)



Source: Central Bank of Seychelles

Table 6.2
Circulation of Notes and Coins;¹ 1999-2004

	1999	2000	2001	2002	2003	2004
(R million)						
Total	264.27	282.23	299.24	321.35	326.06	314.56
Notes	247.94	265.27	280.94	301.66	305.65	293.50
Coins	16.33	16.96	18.30	19.69	20.41	21.06
(per cent)						
Share						
Notes	93.8	94.0	93.9	93.9	93.7	93.3
Coins	6.2	6.0	6.1	6.1	6.3	6.7

¹ End-of-period data

Source: Central Bank of Seychelles

2.1.3 Numismatic issues

During 2004, the sale of numismatic coins, on both local and international markets recorded a 92 per cent drop, from a total of R25,997 in 2003 to a sum of R2,144. There were no new issues of such coins during the year.

2.1.4 Accounts of commercial banks

The Financial Institution Act, 2004, makes it a statutory requirement for commercial banks to hold a minimum percentage of their eligible deposits as cash reserves at the Central Bank. This provision is also a monetary policy tool that can be used by the Bank to regulate the

liquidity level of the economy. For the year under review this requirement remained unchanged at 2.5 per cent and all commercial banks were able to meet this condition.

The activities of the banker's clearing house remained under the ambit of the Central Bank. The total number of items cleared during 2004 was, 586,068 a 2.1 per cent rise relative to the 598,907 items cleared in the previous year. This amounted to R2.4 billion worth of claims cleared during 2004 and is an increase of 19 per cent relative to the R2.0 billion of 2003 (*Table 6.3*).

Table 6.3
Bankers' Clearing House Activities; 1999-2004

	1999	2000	2001	2002	2003	2004
	(Total)					
Number of items cleared	644,593	620,492	609,284	606,193	598,907	586,068
Amount (R'000)	1,641,388	1,861,626	1,676,372	1,662,604	2,007,938	2,386,481
	(Daily average)					
Number of items cleared	2,568	2,533	2,447	2,454	2,405	2,327
Amount (R'000)	6,539	7,598	6,732	6,731	8,064	9,501

Source: Central Bank of Seychelles

2.1.5 Other accounts

During the year under review, the Bank continued in its administration of two other groups of accounts on behalf of the government in addition to the main accounts of government and those of commercial banks.

The first set of account includes those of local and international financial institutions, foreign

government agencies and accounts in respect of the Pipeline Scheme.

The second group of accounts consisted of several interest bearing "special funds" of government (labelled special deposits). For the financial year ending December 2004, the balance on these accounts was R941,069, a 2.0 per cent increase relative to the 2003 total of R922,476.

2.1.6 Annual balances

For the year ending December 31, 2004, the Bank recorded an aggregate of R51 million as net operating profits. This represents a 136 per cent increase relative to the previous year's net operating profit of R21 million.

For the year under review, total income increased by 48 per cent from R67 million in 2003 to R99 million. Total expenditure also increased slightly to stand at R48 million in 2004, a rise of 6.0 per cent from the R45 million of 2003.

2.1.7 External reserves

At the end of the financial year of 2004, gross external reserves of the Bank stood at R188 million, a decrease of 49 per cent relative to the year ending of 2003. This was in spite of a fall of R16,000 in the SDR holdings (from R23,347 in 2003 to R6,972 in 2004) due to changes in the valuation of the Seychelles Rupee. The allocation of SDR by the IMF to the Seychelles increased marginally by 5.0 per cent to stand at R3.5 million.

2.2 Administration and Public Debt

The main functions of the Administration and Public Debt Division remained carrying out the administrative duties of the Bank and the management of domestic public debt instruments on behalf of the government.

As noted earlier, the year 2004 saw the re-introduction of the tender system for the issue of treasury bills. The previous tender system was deemed inconsistent with government's fiscal strategy and was abolished in 1998. The present economic strategy recognises the benefits of a tender system in the determination of domestic interest rates and proposes to extend it to the issue of other government papers.

2.2.1 Treasury Bills

During 2004, there were eight issues of treasury bills, with seven being for 91-day bills and one for 365-day bills. The response to these issues was generally positive, with a mixture of commercial banks, private companies and individuals participating in the tenders (although, as expected, the dominant players were the big commercial banks).

A total of R5.3 billion worth of 91-day bills was issued under the new system during the year. The average tender rate for the initial tender stood at 2.13 per cent and remained constant for the following couple of tenders. However, with the introduction of the new foreign exchange pipeline in April, the average tender rate gradually increased as the squeeze on liquidity took effect. The last tender for 91-day bills produced an average tender rate of 2.64 per cent, 0.51 percentage points higher than the rate in the initial tender.

Table 6.4
Treasury Bills;¹ 1999-2004

	1999	2000	2001	2002	2003	2004
	(R million)					
Stock outstanding ^{1/3}	1388.8	1889.8	1933.9	1940.5	1780.5	1232.8
91-day bills (tap issue)	-	-	-	-	-	-
91-day bills (new tap issue) ⁵	-	-	-	-	335.0	38.9
91-day bills (tender issue) ⁶	-	-	-	-	-	1147.4
91-day bills ⁴	599.8	679.3	689.5	691.1	431.5	-
182-day bills ⁴	474.9	606.6	630.5	633.6	509.2	-
365-day bills ⁴	314.1	603.8	614.1	615.8	504.8	30.5
365-day bills (tender issue) ⁷	-	-	-	-	-	16.1
Stock outstanding ^{2/3}	1424.7	1945.7	1991.1	1997.9	1827.4	1241.3
91-day bills (tap issue)	-	-	-	-	-	-
91-day bills (new tap issue) ⁵	-	-	-	-	336.7	40.0
91-day bills (tender issue) ⁶	-	-	-	-	-	1154.2
91-day bills ⁴	606.6	687.0	697.2	698.9	436.3	-
182-day bills ⁴	486.7	621.7	646.0	649.4	521.9	-
365-day bills ⁴	331.4	637.0	647.9	649.6	532.5	30.5
365-day bills (tender issue) ⁷	-	-	-	-	-	16.7
Held by						
Central Bank	59.5	18.6	6.3	0.6	2.1	0.0
Commercial banks	1180.2	1709.5	1813.8	1823.3	1696.7	1179.2
Other financial institutions	8.5	18.0	10.4	11.5	7.3	1.5
Others	176.4	199.7	160.7	162.6	121.3	60.6
Non-residents	-	-	-	-	-	-

¹ At cost value.

² At face value.

³ Annual and quarterly data are averages of monthly data, compiled on an end-of-period basis.

⁴ With effect from September 15, 1998, new issues of 91-day, 182-day and 365-day bills were placed on tap.

⁵ With effect from July 15, 2003, new issues of 91-day bills available to commercial banks only.

⁶ With effect from January 2004, there was the reintroduction of tender for treasury bills; for now only applicable to 91-day bills.

⁷ Tender for 365-day bills was introduced in December 2004.

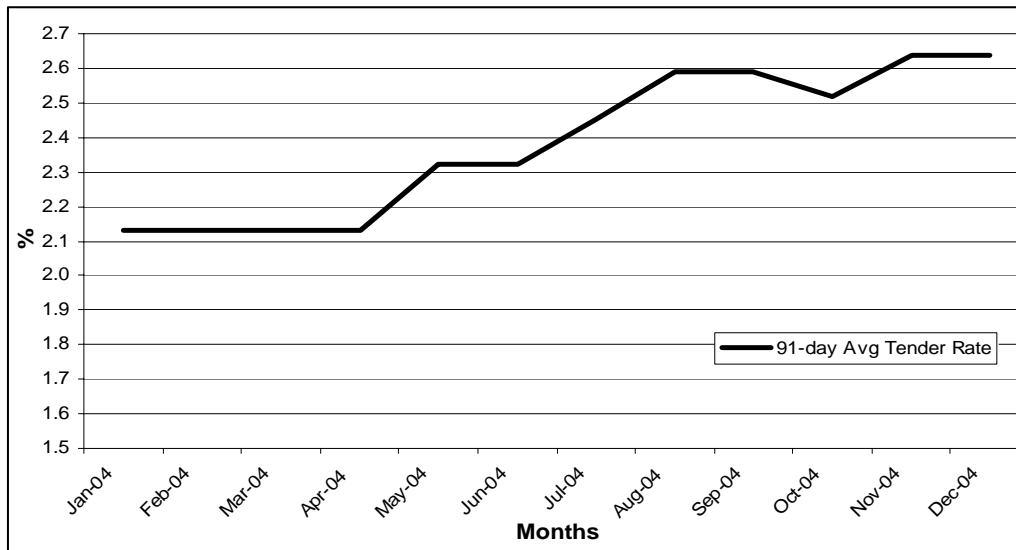
Source: Central Bank of Seychelles

A total of R200 million worth of 365-day bills was issued on tender in 2004. The average tender rate of this issue was 3.83 per cent.

It is expected that interest rates for treasury bills in 2005 continue to follow the upward

trend set during 2004 but the rate of increase will depend on a number of factors in the economy, such as the movements of exchange rates and the budgetary outcome.

Chart 6.3: Average Tender Rate for 91-day treasury bills during 2004



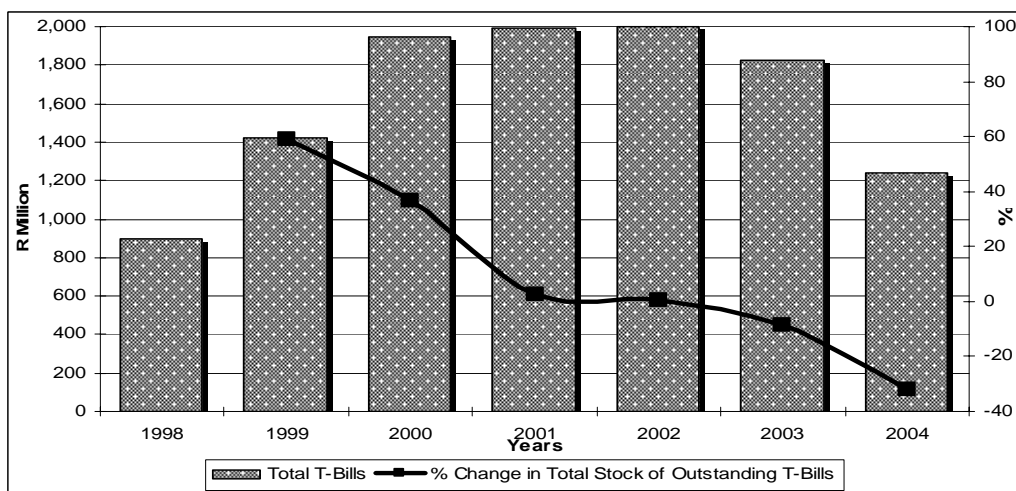
Source: Central Bank of Seychelles

The total value of bills sold for the year under review was R5.5 billion, showing an increase of 41 per cent relative to the previous year.

Total discount paid for 91-day bills which were issued in 2003 was R4.0 million, for 365-

day treasury bills issued prior to 2004 was R8.0 million, for 182-bills issued prior to 2004 was R2.0 million and for 91-day bills issued on tender in 2004 was R20 million. As a result, for the year 2004, total discount paid for treasury bills stood at R34 million.

Chart 6.4: Total Stock of Outstanding Treasury Bills (1998 – 2004)



Source: Central Bank of Seychelles

The total stock outstanding of treasury bills, at face value, stood at R1,241 billion for 2004, a decline of 32 per cent relative to the 2003 total. This is shown in *Chart 6.4 and Table 6.4* above.

2.2.2 Treasury Bonds

The year under review saw no introduction of new treasury bonds. Total sales of treasury bonds in 2004 stood at R668 million. This represents a decline of 45 per cent over the previous year's total.

Total redemption of treasury bonds in 2004 stood at R650 million. This represents an

increase of R108 million from the R542 million redeemed in the previous year. A total of R30 million was paid out as interest, a decrease of 42 per cent over the previous year.

The stock outstanding of bonds for the year averaged R1.79 billion. This is a 58 per cent increase relative to the average of R1.12 billion of 2003. As with preceding years, the bulk of the bonds was held by the commercial banks. Commercial banks held 64 per cent of the stock of treasury bonds outstanding, whilst the remaining 36 per cent was held by other entities.

Table 6.5
Treasury Bonds;¹ 1999-2004

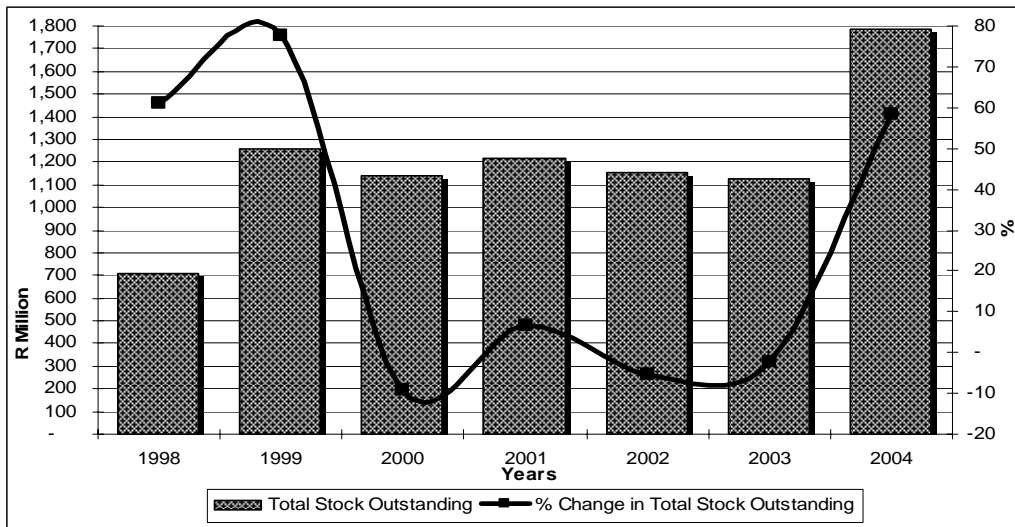
Date Issued	Authorised Limit	1999	2000	2001	2002	2003	2004
		(R million)					
Stock outstanding		1255.8	1141.2	1218.7	1153.7	1127.8	1787.0
15/07/03 ² 2.25%, 1-yr	200.0	-	-	-	-	91.7	108.3
15/07/03 ² 4.0%, 3-yr	600.0	-	-	-	-	169.5	625.0
15/07/03 ² 5.0%, 5-yr	500.0	-	-	-	-	129.2	400.9
03/09/01 7.5%, 3-yr	450.0	-	-	146.3	450.0	450.0	303.7
25/09/00 6.75%, 2-yr	200.0	-	38.2	277.0	261.8	23.0	-
15/07/03 ² 7.0%, 7-yr	200.0	-	-	-	-	66.4	200.0
07/02/00 7.5%, 3-yr	300.0	-	210.1	300.0	300.0	89.9	-
09/09/99 6.75%, 2-yr	250.0	83.3	250.0	166.7	-	-	-
01/09/98 6.0%, 1-yr	500.0	360.4	-	-	-	-	-
01/09/98 6.75%, 2-yr	200.0	199.6	157.3	0.4	-	-	-
01/09/98 7.5%, 3-yr	150.0	149.1	150.0	132.5	0.9	-	-
01/09/98 8.0%, 5-yr	50.0	34.6	50.0	50.0	50.0	47.7	15.0
15/07/03 ² 8.0%, 10-yr	100.0	-	-	-	-	41.1	134.2
01/02/97 11.0%, 3-yr	200.0	200.0	180.2	40.4	-	-	-
01/02/97 11.5%, 5-yr	150.0	105.5	105.5	105.5	91.0	19.3	-
01/10/95 12.0%, 3-yr	250.0	123.3	-	-	-	-	-
01/09/93 12.5%, 2-yr	250.0	-	-	-	-	-	-
15/11/92 12.0%, 5-yr	150.0	-	-	-	-	-	-
01/08/90 16.5%, 3yr	10.0	-	-	-	-	-	-
01/08/90 16.5%, 5yr	10.0	-	-	-	-	-	-
Held by:							
Central Bank		0.1	0.0	-	-	-	6.6
Commercial banks		1040.1	903.7	930.8	880.6	830.7	1137.5
Other financial institutions		-	-	-	-	-	3.0
Others		215.7	237.4	287.9	273.2	297.1	639.9

¹ Annual data are averages of monthly data, compiled on an end-of-period basis.

² New issue introduced in July 2003.

Source: Central Bank of Seychelles

Chart 6.5: Total Stock of Outstanding Treasury Bonds (1998 – 2004)



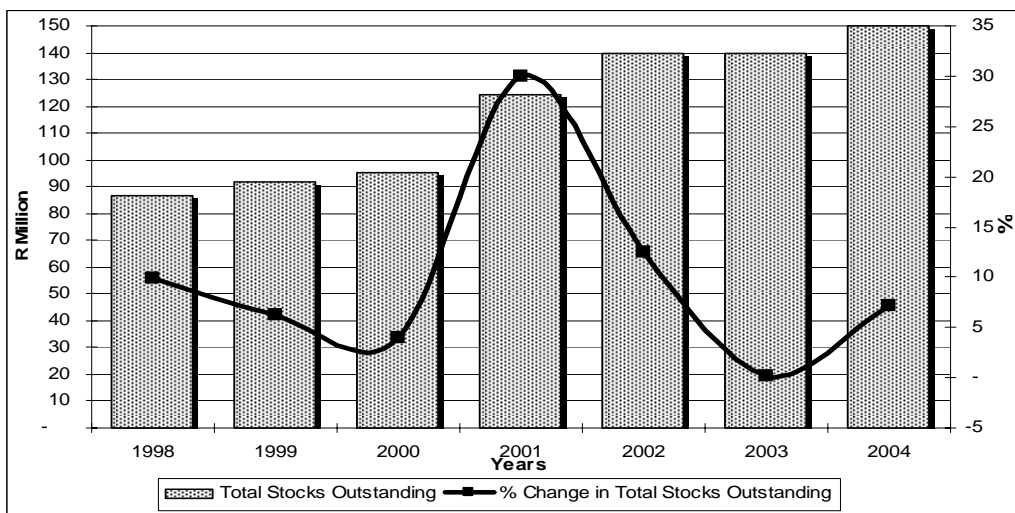
Source: Central Bank of Seychelles

2.2.3 Seychelles Government Stocks

For the year under review, R70 million worth of a new 8.0 per cent, 10-year government stock was offered for sale. This was to counteract the redemption of the previous 8.0 per cent, 10-year stock which was redeemed during the year. The average total stock

outstanding for 2004 was R150 million, an increase of 7.0 per cent relative to the previous year’s average. This total was being held primarily by commercial banks (98 per cent), with the remaining 2.0 per cent held by “others”.

Chart 6.6: Total Stock of Outstanding Government Stocks (1998 – 2004)



Source: Central Bank of Seychelles

Table 6.6
Government Stocks;^{1/2/} 1999-2004

Authorised Limit	1999	2000	2001	2002	2003	2004
	(R million)					
Stock outstanding	91.9	99.9	124.2	139.7	140.0	150.0
8.00%, 2009	50.0	2.1	9.9	34.2	49.7	50.0
8.50%, 2005/07	30.0	29.8	30.0	30.0	30.0	30.0
8.00%, 2004	60.0	60.0	60.0	60.0	60.0	-
8.00%, 2014	70.0	-	-	-	-	70.0
Central Bank	-	-	-	-	-	-
Commercial banks	92.0	99.9	124.2	139.7	140.0	147.1
Other financial institutions	-	-	-	-	-	-
Others	-	-	-	-	-	2.9

¹ Yearly averages of monthly data, compiled on an end-of-period basis.

² At cost value.

Source: Central Bank of Seychelles

2.3 Bank Supervision

During 2004, the Bank Supervision Division carried out business as usual, upholding its responsibilities with the aim of ensuring a sound banking system. It carried out 3 inspections of bank institutions; of which all three were full inspections. All banks were seen to be meeting the criteria set by legislation except for one which failed to meet the Local Asset Ratio requirement on three occasions. Local Asset Ratio (LAR) is a requirement that all commercial banks must hold a portion of their assets as government debt. This ratio is determined by the Central

Bank. It is to be noted that the practice of using the LAR as a financing tool for government may be inherently inefficient as it can distort the natural pattern of bank lending; under certain conditions, it could even affect the solvency of banks and puts the banking system at risk of collapse.

2.3.1 Minimum required capital and investment of capital funds

No alterations were made in 2004 regarding the minimum required capital of commercial banks. All of them complied with this statutory requirement.

Table 6.7
Capital Fund Ratios of Commercial Banks;¹ 1999-2004

	1999	2000	2001	2002	2003	2004
	(R million)					
Capital Funds	188.48	205.16	210.60	215.37	218.16	220.31
Assigned capital	104.45	110.75	110.80	110.95	110.75	110.75
Reserve fund	84.03	94.41	99.80	104.624	107.41	109.56
Minimum required capital (5% of A) ^{2/3}	124.10	-	-	-	-	-
Memorandum item						
Eligible deposit liabilities (A)	2482.05	-	-	-	-	-

¹ Annual averages of monthly aggregates compiled on a monthly basis.

² Figures for 1999 relate to the first four months only.

³ As of May 1999, the Minimum required capital was replaced by a new requirement known as the Risk Weighted Capital Adequacy Ratio (RWCAR) set at a minimum of 8.0 per cent.

Source: Central Bank of Seychelles

2.3.2 Minimum reserve requirements and local asset ratio

There were no alterations made to the minimum reserve requirements of the commercial banks during the year, this

remained fixed at 2.5 per cent. The outcome at the end of the financial year 2004 was 5.6 per cent, a slight improvement to the outcome of the previous year. This is shown in *Table 6.8 and Chart 6.7* below.

Table 6.8
Minimum Reserves and Local Assets Ratio;¹ 1999-2004

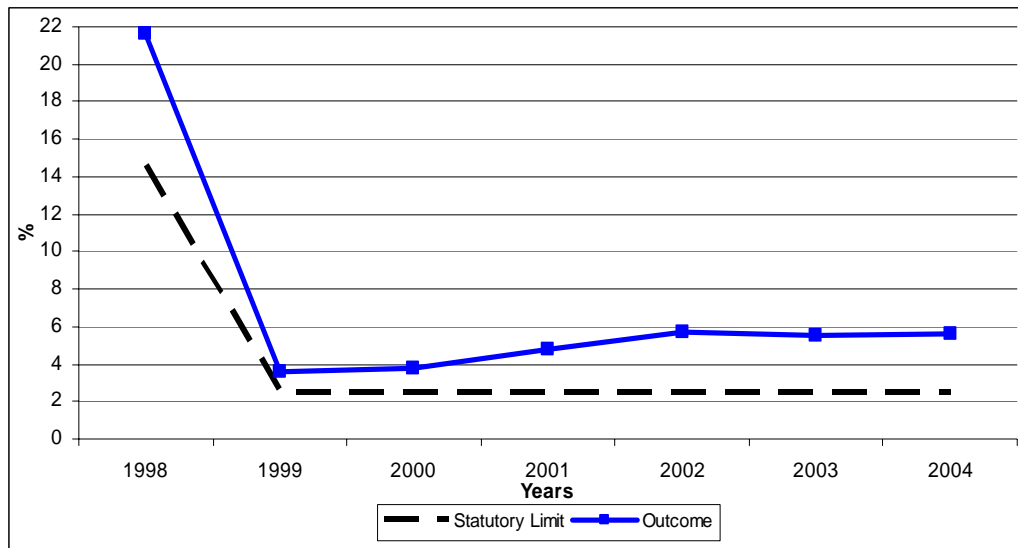
	1999	2000	2001	2002	2003	2004
	(per cent)					
Minimum reserve requirement						
Statutory limit	2.50	2.50	2.50	2.50	2.50	2.50
Outcome	3.56	3.79	4.76	5.70	5.50	5.60
Minimum local assets						
Statutory limit	70.00	70.00	66.54	50.00	50.00	50.00
Outcome	97.11	95.83	95.03	81.50	79.46	70.00

¹ Yearly averages of weekly data.

Note: Minimum local assets ratio was reduced to 50 per cent in November 2001.

Source: Central Bank of Seychelles

Chart 6.7: Minimum Reserve Requirement (1998 – 2004)

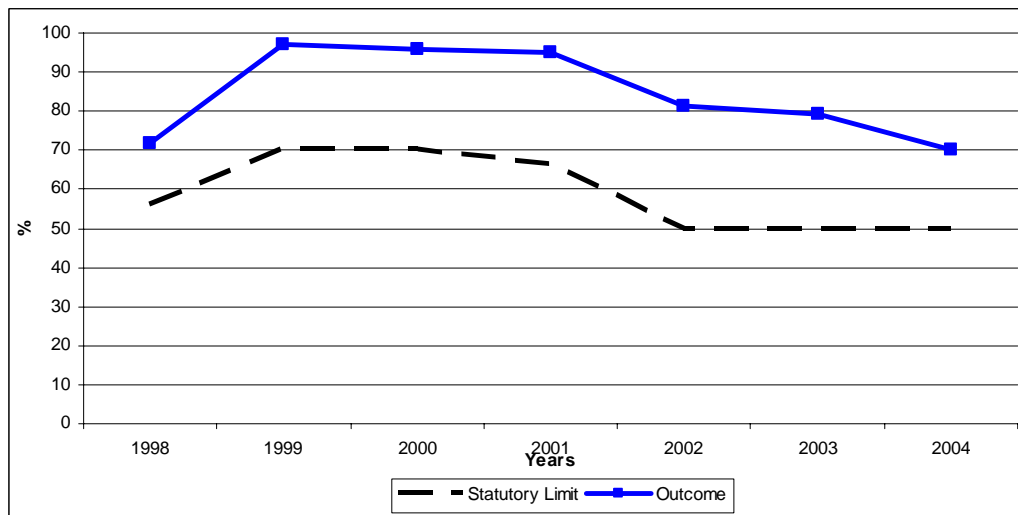


Source: Central Bank of Seychelles

The statutory limit of the local asset ratio in 2004 remained at 50 per cent, with all banks

combining to give an actual outcome of 70 per cent. This is shown below in *Chart 6.8*.

Chart 6.8: Minimum Local Assets (1998 – 2004)



Source: Central Bank of Seychelles

2.3.3 Central Bank advances to commercial banks

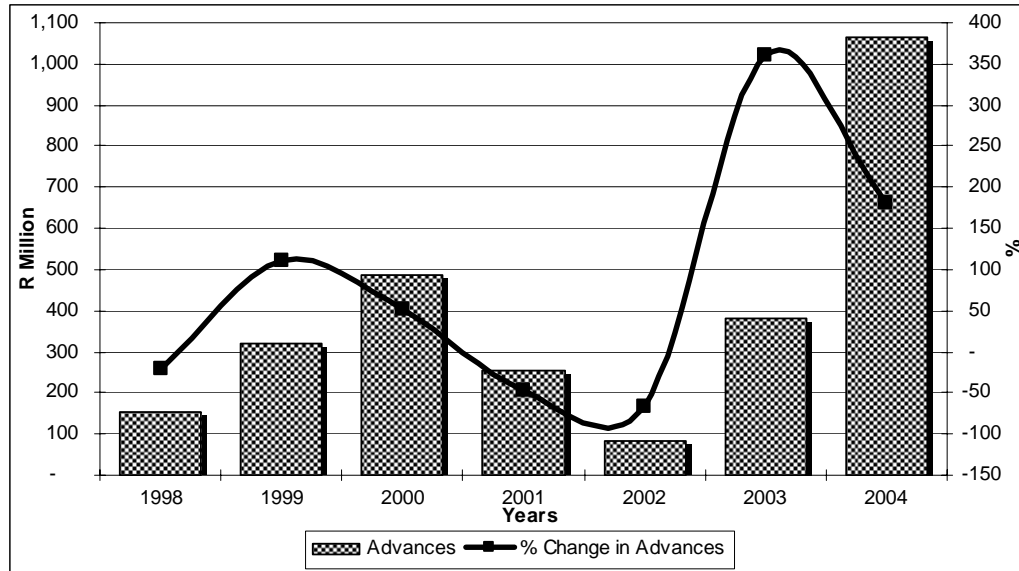
The Central Bank offers temporary advances to the commercial banks when they face

liquidity shortages. For the year under review, total advances increased considerably, by 180 per cent, from R380 million in 2003 to R1,064 million in 2004. This is shown in *Chart 6.9*

and Table 6.9 below. One of the reasons for the increase in advances to commercial banks was the shock on the daily cash flows of banks

caused by the re-introduction of the foreign exchange pipeline system.

Chart 6.9: Central Bank advances to commercial banks (1998 – 2004)



Source: Central Bank of Seychelles

**Table 6.9
CBS Advances to Commercial Banks; 1999-2004**

	1999	2000	2001	2002	2003	2004
	(R million)					
Advances	318.0	485.4	254.7	82.5	379.5	1063.5
Repayments	328.0	463.4	276.7	82.5	360.5	962.5
Stock of credit ¹	6.6	6.1	4.0	0.0	9.0	44.5

¹ Yearly data are averages of monthly data, compiled on an end-of-period basis.

Source: Central Bank of Seychelles

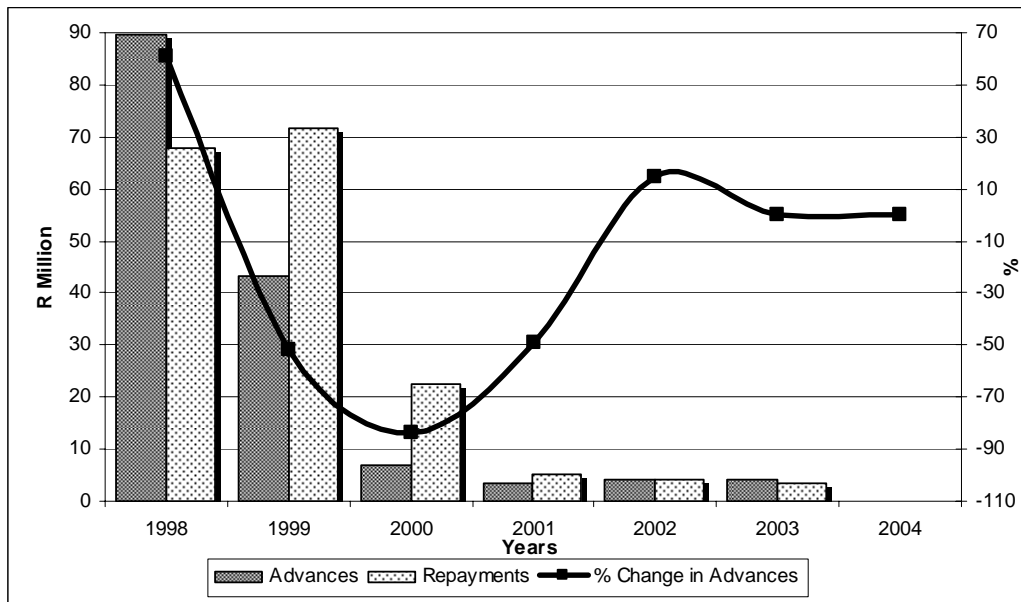
2.3.4 Government of Seychelles

Concessionary Re-finance Scheme

The scheme offers financing to export-oriented and import-substitution industries and is administered by the Bank on behalf of the Department of Finance. During 2004, no new line of finance was approved by the latter.

Consequently, no advances were made during 2004. Repayments totalling R0.1 million were also made during the year. This is shown in *Chart 6.10 and Table 6.10* below.

Chart 6.10: Advances and repayments of Government concessionary re-finance scheme (1998 – 2004)



Source: Central Bank of Seychelles

**Table 6.10
Government Concessionary Re-finance Scheme; 1999-2004**

	1999	2000	2001	2002	2003	2004
	(R million)					
Stock of credit¹	21.3	4.9	2.2	1.9	1.8	0.7
Of which:						
Export-oriented:						
Private sector	6.3	3.7	2.2	1.9	1.8	0.7
Public sector	15.0	1.3	0.0	0.0	0.0	0.0
Advances	43.1	6.9	3.5	4.0	4.0	0.0
Repayments	71.6	22.6	5.1	4.0	3.5	0.1

¹ Yearly data are averages of monthly data, compiled on an end-of-period basis.

Source: Central Bank of Seychelles

2.3.5 Commercial bank advances to non-Seychellois

The year 2004 saw total advances made by commercial banks to non-Seychellois investors and private individual stand at R89

million, a 197 per cent increase relative to the total of the previous year.

Table 6.11
Commercial Bank Advances to Non-Seychellois;¹ 2002-2004

	2 0 0 2		2 0 0 3		2 0 0 4	
	Limit	Outstanding	Limit	Outstanding	Limit	Outstanding
	R million	%	R million	%	R million	%
Advances	46.7		30.0		89.1	
Tourism	39.4	(84.4)	19.5	(65.0)	29.5	(33.1)
Wholesale/retail	0.0	(0.0)	0.2	(0.7)	0.2	(0.2)
Building and construction	0.5	(1.1)	1.6	(5.3)	0.0	(0.0)
Manufacturing	0.9	(1.8)	0.2	(0.7)	0.4	(0.5)
Agriculture	0.0	(0.0)	0.0	(0.0)	0.0	(0.0)
Fishing	0.0	(0.0)	0.6	(2.0)	0.5	(0.6)
Real estate	0.0	(0.0)	2.5	(8.3)	0.0	(0.0)
Individuals & households	2.7	(5.8)	4.6	(15.3)	2.6	(2.9)
Other businesses	3.2	(6.9)	0.8	(2.7)	55.8	(62.6)

¹ End-of-period data

Source: Central Bank of Seychelles

2.3.6 Commercial bank advances to parastatals

The Central Bank and the Department of Finance jointly controls credit offered to parastatal organisations. For the year under review, a limit of R243 million was set. This is compared to the R242.5 million ceiling of 2003. The balance outstanding showed a

massive increase relative to the previous year, to stand at R159.2 million. It must be noted that 87 per cent of the total advances made went to parastatals in the building and construction sector, 11 per cent going to parastatals in the Wholesale/retail sector and the remaining 1.4 per cent going to the tourism sector.

Table 6.12
Commercial Bank Advances to Parastatals;¹ 2002-2004

	2 0 0 2			2 0 0 3			2 0 0 4		
	Limit	Outstanding		Limit	Outstanding		Limit	Outstanding	
	R million	%		R million	%		R million	%	
Advances	7.5	5.2		242.5	78.9		243.0	159.2	
Tourism	7.5	5.2	(100.0)	7.5	3.9	(4.9)	7.5	2.2	(1.4)
Wholesale/retail	0.0	0.0	(0.0)	0.0	0.0	(0.0)	0.0	17.1	(10.7)
Building and construction	0.0	0.0	(0.0)	235.0	75.0	(95.1)	235.0	138.0	(86.7)
Manufacturing	0.0	0.0	(0.0)	0.0	0.0	(0.0)	0.0	0.0	(0.0)
Agriculture	0.0	0.0	(0.0)	0.0	0.0	(0.0)	0.5	0.3	(0.2)
Fishing	0.0	0.0	(0.0)	0.0	0.0	(0.0)	0.0	0.0	(0.0)
Transport	0.0	0.0	(0.0)	0.0	0.0	(0.0)	0.0	1.6	(1.0)
Communications	0.0	0.0	(0.0)	0.0	0.0	(0.0)	0.0	0.0	(0.0)

¹ End-of-period data

Source: Central Bank of Seychelles

2.3.7 Advances to wholesale and retail trade

Credit to wholesale and retail traders from commercial banks continued to be monitored by the Bank. As it has been the case with the past couple of years, all activities occurred on the accounts of the private sector. At the year ending December 31, 2004, the balance stood at R33 million, R16 million below the set limit of R48 million.

2.3.8 Banking licences

During the year under review, Barclays Bank was issued a new banking license for the establishment of an offshore banking unit.

3. Research and Statistics

With the introduction of the MERP in 2003, the role the Research and Statistics Division became crucial, as it took on the task of monitoring the performance of the economic indicators and provide timely updates of the data through its publications. This role continued during 2004 as the reforms of government carried through. To carry out this responsibility, it had to work in close collaboration with the Department of Finance, the Ministry of Economic Planning and the national statistics office – the Management Information Systems Division (MISD).

The Division remained as the liaison office with international organisations for which the Bank has to provide statistical information. It helped provide the IMF Article IV missions with the necessary information on their visit.

4. Administrative matters

4.1 Higher education, training and courses

Mr. Christophe Edmond, Assistant Accountant, attended the 35th International Central Banking Course being held in Islamabad, Pakistan. The course started on March 8 and to April 16.

Mrs Jenifer Vital, Bank Supervision Officer, attended a 2 weeks attachment programme on supervision of offshore Banks at Bank of Mauritius during the period August 2 to 13, 2004.

Mrs Nella Souris, Banking Supervisor and Mrs Christine Hitie, Bank Supervision Officer, attended the ESAF Banking Supervisors Intermediate training course in Banking Supervision which was held in Pretoria, South Africa, during the period August 16 to 27, 2004.

Miss Brigitte Valmont, Research Officer, attended a course on Financial Programming and Policies which was held in Pretoria, South Africa during the period August 2 to 13, 2004. The course was fully funded by the Joint Africa Institute.

Miss Caroline Abel, Director Research & Statistics is presently in UK, at the University of Glasgow where she is pursuing a course leading to a Masters of Philosophy (M.Phil) in Monetary and Finance. The course started in September 2004 and will end in September 2005.

Miss Danielle Robert, Senior Bank Clerk, is pursuing a 3-year course leading to a BA (Hons) in Accounting and Finance at the Brighton University. The course started in September 2004 and will end in June 2007.

Mr Francis Lebon, Senior Bank Clerk, is pursuing a 3-year course leading to a BA (Hons) in Economics, Finance and Banking at the University of Portsmouth. The course started in September 2004 and will end in June 2007.

Mr Norman Lucas, Director Banking & Currency Operations, attended a course on Management of Foreign Reserves. The course was held in London during the period October 11 to 15, 2004.

Miss Dorothea Michel, Research Officer attended the Monetary and Financial Statistics course held in Washington from October 12 to November 5, 2004. The course was organised by the IMF.

Mr Alain Chang-Sam, Research Officer participated in the Residential Segment of the IMF Institute Distance Learning Course on Financial Programming and Policies held in Washington from November 29 to December 10, 2004.

4.2 Workshop and seminars

Miss Caroline Abel, Director Research and Statistics, and Mrs Jennifer Vital, Bank Supervision Officer, attended a workshop on Financial Stability and Monetary Policy which

was held in Mauritius during the period March 22 to 24. The workshop was organised by the Bank of England and Bank of Mauritius.

Miss Jennifer Morel, Director General Bank Supervision, attended a seminar on International Accounting and Auditing for Banks which was held in Basel, Switzerland during the period March 30 to April 2.

Mr Brian Commettant, Research Officer, attended a course on Banking and Finance in Small States which was held in Malta during the period May 3 to 14.

Mr Norman Lucas, Director Banking & Currency Operations attended the Perago User Conference 2004 which was held in Pretoria, South Africa from May 12 to 14.

Mr Philip Moustache, Bank Supervision Officer, attended the AML/CFT Strategy Development Workshop which was held in Cape Town, South from May 25 to 27.

Mr Christophe Edmond attended a Seminar on Payment Systems which was held in Tunis, Tunisia from September 6 to 10, 2004. The seminar was funded by the Joint Africa Institute.

Miss Jennifer Morel, D.G. Bank Supervision attended the 13th International Conference of Banking Supervisors (ICBS) which was held in Madrid, Spain during the period September 22 to 23, 2004.

Miss Jennifer Morel, D.G. Bank Supervision attended the Financial Stability Institute (FSI) High Level Meeting on Practical Application of Basel II for the Africa Region in Pretoria, South Africa from November 16 to 17, 2004.

Mrs Jenifer Vital, Bank Supervision Officer attended the Barclays Africa and Middle East Financial Crime Conference held at the Gold

Reef City in South Africa from November 20 to 30, 2004.

Mr Brian Commettant, Research Officer attended a Seminar on Monetary and Financial Statistics: Compilation and Reporting Issues which was held in Tunis, Tunisia from December 6 to 10, 2004. The seminar was organised by the Joint Africa Institute.

**OFFICERS OF THE CENTRAL BANK OF SEYCHELLES
IN 2004**

Francis Chang Leng	-	Governor
Peter Larose	-	General Manager
Patrick Stravens	-	Monetary and Banking Advisor
<i>Vacant</i>	-	Director General Banking Services
Jennifer Morel	-	Director General Bank Supervision
<i>Vacant</i>	-	Director General Research and Statistics
Jean-Claude d'Offay	-	Director General Administration & Public Debt
Norman Lucas	-	Director Banking and Currency Operations
Caroline Abel	-	Director Research and Statistics
Phillip Moustache	-	Senior Bank Supervision Officer
Guyliane Joubert	-	Bank Supervision Officer
Christine Hitié	-	Bank Supervision Officer
Jenifer Vital	-	Bank Supervision Officer
<i>Vacant</i>	-	Senior Research Officer
Dorotha Michel	-	Research Officer
Phillip Pierre	-	Research Officer*
Brian Commettant	-	Research Officer
Alain Chang Sam	-	Research Officer

OFFICERS OF THE CENTRAL BANK OF SEYCHELLES (*Cont'd*)
IN 2004

Moyra Alexis	-	Research Officer
Brigitte Valmont	-	Research Officer
Jeannette Payet	-	Accounts Manager
Christophe Edmond	-	Assistant Accountant
Mike Tirant	-	Assistant Accountant
Terry Adrienne	-	Public Debt Officer
Levina Françoise	-	Administration Officer
Juliette Bertin	-	IT Officer

** No longer in service with the Central Bank prior to 31st December 2004*