INTERNATIONAL MONETARY FUND

CABO VERDE

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SECOND REVIEW UNDER THE POLICY COORDINATION INSTRUMENT AND REQUEST FOR MODIFICATION OF TARGETS—DEBT SUSTAINABILITY ANALYSIS

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Cabo Verde: Joint Bank-Fund Debt Sustainability Analysis	
Risk of external debt distress	*High*
Overall risk of debt distress	*High*
Granularity in the risk rating	*Sustainable*
Application of judgement	*No*

Cabo Verde's risk of external and overall debt distress remains high, unchanged from the joint Debt Sustainability Analysis (DSA) of April 2020. The present value (PV) of public and publicly-guaranteed (PPG) external debt-to-GDP ratio breaches its threshold during 2020–24 under the baseline, and protractedly under stress test scenarios. The PV of total public debt-to-GDP ratio is projected to breach its threshold during 2020–27 under the baseline scenario and during 2020–31 under stress test scenarios. The debt sustainability assessment is predicated on several assumptions, including a gradual recovery of economic activity in 2021, reprofiling of debt service of all official bilateral creditors under the debt service suspension initiative (DSSI), growth-friendly fiscal consolidation in the post-pandemic period as well as resumption of structural reforms, notably to restructure State-Owned Enterprises (SOEs) and improve the business environment. Prudent borrowing policies and strengthened debt management, as well as measures to enhance the functioning of the government securities market are critical to stabilizing debt dynamics over time. In view of Cabo Verde's vulnerability to exogenous shocks, sustained progress in export and output diversification are also needed for long-term debt sustainability.

PUBLIC DEBT COVERAGE

1. **The coverage of the public sector is in line with the previous DSA** (Text Table 1). Consistent with fiscal accounts, the social security fund and local governments are excluded from the DSA, while the coverage of extra budgetary funds (EBFs) is focused on government support to State-Owned Enterprises (SOEs) through onlending and capitalization operations. Government guarantees to SOEs' external borrowing are included in the baseline stock of debt, while publicly-guaranteed domestic debt and non-guaranteed debt by SOEs are excluded because of limited information on the repayment schedule. Efforts to broaden the coverage of public sector debt are ongoing, including by supporting debt transparency reforms through a World Bank Development Policy Financing Operation.[1]

Text Table 1. Cabo Verde: Coverage of Public-Sector Debt and Design of Contingent Liability Stress Test

	Subsectors of the public sector	Check box
1	Central government	X
2	State and local government	
3	Other elements in the general government	
4	o/w: Social security fund	
5	o/w: Extra budgetary funds (EBFs)	X
6	Guarantees (to other entities in the public and private sector, including to SOEs)	X
7	Central bank (borrowed on behalf of the government)	X
8	Non-guaranteed SOE debt	

Public debt coverage and the magnitude of the contingent liability tailored stress test

		Default	Used for the analysis	Reasons for deviations from the default settings
1	The country's coverage of public debt	The central government plus extra budgetary funds, central bank, government-guaranteed debt		
2	Other elements of the general government not captured in 1.	0 percent of GDP	0.3	
3	SoE's debt (guaranteed and not guaranteed by the government) 1/	2 percent of GDP	24.3	To reflect vulnerabilities associated with guaranteed domestic debt and non-guaranteed SOE debt.
4	PPP	35 percent of PPP stock	1.1	
5	Financial market (the default value of 5 percent of GDP is the minimum value)	5 percent of GDP	5	
	Total (2+3+4+5) (in percent of GDP)		30.7	

1/ The default shock of 2% of GDP will be triggered for countries whose government-guaranteed debt is not fully captured under the country's public debt definition (1.). If it is already included in the government debt (1.) and risks associated with SoE's debt not guaranteed by the government is assessed to be negligible, a country team may reduce this to 0%.

2. **The contingent liability tailored stress test is calibrated to account for the debt coverage gaps highlighted above**. First, the default shock of 0 percent of GDP for other elements of the general government not captured in the baseline stock of debt is raised to 0.3 percent of GDP to account for the size of publicly-guaranteed domestic debt of local governments.[2] Second, while the strong financial position of the social security fund (INPS) before the COVID-19 crisis has not risen concerns of immediate fiscal risks, the need to adjust the contingent liability stress test for its exclusion would need to be re-assessed in the post-pandemic period, based on the updated actuarial study (planned for 2021) to account for implications of larger unemployment benefits paid out in 2020, temporary suspension of contributions, and other measures undertaken by the government in response to the health crisis. Third, the default shock of 2 percent of GDP for SOEs' debt is raised to 24.3 percent of GDP to reflect vulnerabilities associated with: (i) publicly-guaranteed domestic debt by ELECTRA, Newco, TACV, IFH, ENAPOR and CERMI amounting to

[1] A comprehensive assessment of contingent liabilities is expected to be concluded in 2021.

[2] Government-guaranteed domestic borrowing of municipalities from the banking system stood at CVE 623.4 million (0.3 percent of GDP) at end-December 2019 (see Text Table 3 for more details).

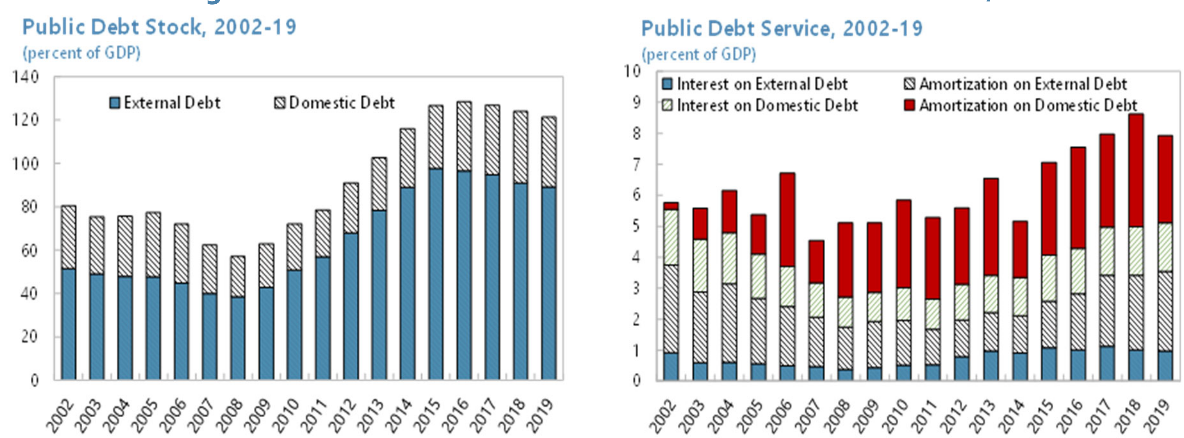
CVE 13.1 billion (6.7 percent of GDP) at end-2019 and; (ii) non-guaranteed domestic debt of loss-making SOEs totaling CVE 34.3 billion (17.6 percent of GDP) at end-2019.[3] Fourth, the default shock of 1.1 percent of GDP has been kept for public private partnerships (PPPs), in line with the previous DSA. Fifth, given that most banks are foreign-owned and well-capitalized, Cabo Verde's financial sector does not exhibit significant vulnerabilities that warrant an upward adjustment of the default minimum value of 5 percent of GDP for the financial market shock.

BACKGROUND

A. Evolution and Composition of Public Debt

3. The stock of public debt stood at 125 percent of GDP at end-2019 (Text Figure 1). It declined from its peak of 128.4 percent of GDP in 2016, reflecting the downward trend in external debt (which accounts for 73.2 percent of the total stock of public debt), consistent with improvement in the fiscal position. Domestic debt accounts for over 60 percent of debt service since most of the external debt is on concessional terms as explained below.

Text Figure 1. Cabo Verde: Profile of Public Debt and Debt Service, 2002–19



Sources: Cabo Verdean authorities and IMF staff estimates.

Note: Publicly-guaranteed external debt stock and debt service of SOEs included from 2015.

4. Cabo Verde's public external debt is highly concessional (Text Table 2). Multilateral institutions, notably the World Bank and the African Development Bank are the main creditors, while Portugal is the main bilateral creditor. The average maturity of external debt is about 30.2 years, and the average interest rate is below 1 percent.[4] More than two third of the external debt portfolio is euro-denominated, and therefore, exchange rate risks are limited since the Cabo Verdean escudo (CVE) is pegged to the euro.

[3] The total stock of non-guaranteed domestic debt stood at CVE 80.0 billion at end-2019, of which CVE 34.3 billion represented borrowing by eight SOEs that recorded negative net income in 2019 (ELECTRA, TACV, ICV, SCS, FIC, EHTCV, APN, and LEC).

[4] Commercial loans mainly consist of debt owed to Caixa Geral de Depósitos (CGD) under favorable terms: an average maturity of 20 years and an average interest rate of 1.55 percent.

Text Table 2. Cabo Verde: External Debt Profile by Type of Creditors, 2019

	Percent of external debt	Average maturity	Average interest rate
Multilateral	42.5	32.8	0.94%
Bilateral	26.1	18.6	1.00%
Commercial	31.4	17.4	1.52%

Source: Cabo Verdean authorities and IMF staff estimates.

5. **Domestic debt consists mostly of medium and long-term Treasury securities**. At end-2019, it accounted for 26.8 percent of total public debt, comprising mainly Treasury bonds (97 percent); with average maturity and interest rate of about 7.5 years, and 4.7 percent respectively. The banking sector is the main holder of government securities (60 percent), while the social security fund and households hold 38 percent and 2 percent, respectively.

6. **Publicly guaranteed debt stood at CVE 15.4 billion (7.9 percent of GDP) at end-2019** (Text Table 3). State guarantees are mainly issued for SOEs' domestic debt (85 percent of the stock), which reached 6.7 percent of GDP at end-2019. The publicly-guaranteed external debt covers TACV debt contracted with a consortium of foreign banks, while guaranteed domestic debt consists primarily of the liabilities of ELECTRA, Newco, TACV, IFH, Enapor and CERMI to the domestic banking system and Stock Exchange; and borrowing by a few municipalities (though amounts are significantly smaller). The issuance and management of State guarantees is regulated by the Decree-Law 42 of June 29, 2018, which clarifies the entities that could benefit from guarantees as well as the conditions. The law includes also an article requiring the Minister of Finance's approval for the issuance of loan guarantees. The annual guarantee ceiling is indicated in budgets submitted to parliament.[5]

Text Table 3. Cabo Verde: Publicly-Guaranteed Debt, 2016–19

	2016			2017			2018			2019		
	CVE million	Percent of GDP	Percent of debt	CVE million	Percent of GDP	Percent of debt	CVE million	Percent of GDP	Percent of debt	CVE million	Percent of GDP	Percent of debt
External Debt (A)	**882**	**0.5**	**100.0**	**2,117**	**1.2**	**100.0**	**1,674**	**0.9**	**100.0**	**1,628**	**0.8**	**100.0**
contracted by SOEs	599	0.4	67.9	1,834	1.1	86.6	1,674	0.9	100.0	1,628	0.8	100.0
contracted by private entities	283	0.2	32.1	283	0.2	13.4	0	0.0	0.0	0	0.0	0.0
Domestic Debt (B)	**10,516**	**6.3**	**100.0**	**11,778**	**6.8**	**100.0**	**12,078**	**6.6**	**100.0**	**13,773**	**7.1**	**100.0**
contracted by local governments	381	0.2	3.6	677	0.4	5.7	682	0.4	5.6	623	0.3	4.5
contracted by SOEs	10,135	6.1	96.4	11,102	6.4	94.3	11,388	6.2	94.3	13,140	6.7	95.4
contracted by private entities	0	0.0	0.0	0	0.0	0.0	8	0.0	0.1	9	0.0	0.1
Total Publicly-Guaranteed Debt (A+B)	**11,398**	**6.9**		**13,895**	**8.0**		**13,752**	**7.5**		**15,401**	**7.9**	

Source: Cabo Verdean authorities and IMF staff calculations.

[5] In addition, on December 28, 2019 Parliament passed a new Public Debt Law, which set the limits on short-term and medium-term borrowing, and specified instruments to be used.

7. Historical series of private external debt derived from international investment position (IIP) data indicate a relatively low stock of about 10 percent of GDP at end-2019. Private debt includes both bank and non-bank external debt. The central bank (BCV) compiles and publishes non-financial corporations' private debt stock statistics. Significant progress was achieved by the BCV in external sector statistics (ESS) in recent years, including the migration of BOP and IIP statistics to BPM6 and the reporting of quarterly IIP.

B. Outlook and Key Macroeconomic Assumptions

8. The baseline scenario is predicated on a gradual economic recovery starting in 2021 (Text Table 4). Real GDP growth is projected at 4.5 percent for 2021, and 6.2 percent over the medium term. The rebound assumes the gradual resumption of tourism activities and capital flows, as the global economy recovers. However, the trajectory is highly uncertain for the next two years, as the Cabo Verdean economy remains vulnerable to external shocks and dependent on export of services. Structural reforms aimed at enhancing the business environment, improving inter-island connectivity and strengthening linkages between tourism and other sectors, as well as the completion of critical infrastructure projects are expected to support growth going forward.

9. A gradual improvement in fiscal and external balances is forecasted for the medium term. By 2025, the fiscal deficit is expected to be eliminated while the external current account deficit is projected to narrow to 1.8 percent of GDP, which will facilitate the stabilization of public and external debt dynamics. A gradual fiscal consolidation will be supported by enhanced domestic revenue mobilization and strengthened expenditure management and prioritization. The gradual improvement in the primary balance, combined with progress in the restructuring of SOEs is projected to bring total financing needs to 0.2 percent of GDP over medium term. A resumption of, and expansion in tourism activities, remittances, and capital flows are expected to help strengthen the medium-term external position and the build-up of international reserves.

Text Table 4. Cabo Verde: Assumptions for Key Economic Indicators, 2020–40

(Percent of GDP)

	2017 Act.	2018 Act.	2019 Act.	2020 Proj.	2021 Proj.	2022 Proj.	2023 Proj.	2024 Proj.	2025 Proj.	2026 - 30 Proj.	2031 - 40 Proj.
Real GDP growth											
Current DSA	3.7	4.5	5.7	-6.8	4.5	4.8	5.7	6.0	6.2	5.5	5.5
2020 April DSA (RCF)	3.7	4.5	5.7	-5.5	5.0	6.4	6.0	5.7	5.5	5.1	5.0
GDP Deflator											
Current DSA	0.7	1.5	0.6	1.1	1.2	1.4	1.5	1.6	1.7	1.8	2.0
2020 April DSA (RCF)	0.7	1.5	0.6	1.7	1.7	2.0	1.9	1.9	2.0	2.1	2.2
Fiscal balance (including grants)											
Current DSA	-3.0	-2.7	-1.8	-9.7	-6.6	-3.7	-1.8	-0.8	0.0	0.1	0.3
2020 April DSA (RCF)	-3.0	-2.8	-1.8	-8.4	-4.1	-1.4	-1.1	-0.9	-0.7	-0.5	-1.0
Overall financing needs (including onlending)											
Current DSA	-3.3	-3.7	-5.1	-12.1	-6.4	-3.9	-2.0	-1.0	-0.2	0.1	0.3
2020 April DSA (RCF)	-3.3	-3.9	-5.1	-10.9	-5.1	-2.2	-1.3	-1.1	-0.9	-0.5	-1.0
Current account balance (including grants)											
Current DSA	-7.8	-5.2	0.3	-14.2	-9.2	-6.4	-4.1	-2.1	-1.8	-1.0	-0.9
2020 April DSA (RCF)	-7.9	-5.4	-0.2	-14.3	-8.6	-4.7	-2.6	-1.7	-0.5	0.8	4.7
Cv$/USD exchange rate (e-o-y)											
Current DSA	92.4	96.3	98.5	95.5	93.6	93.1	93.0	93.0	93.1	93.1	93.1
2020 April DSA (RCF)	92.4	96.3	98.5	100.3	99.5	98.9	98.3	97.8	97.8	97.8	97.8

Sources: Cabo Verdean authorities; and IMF staff estimates and projections.

10. The current shock to the Cabo Verdean economy is severe, with large uncertainties about its duration, as well as economic and social impact. A more prolonged health crisis could stall the economic recovery and become a drag on export and domestic revenue collection, as well as capital flows and private investments, leading to a deeper economic contraction in 2020, a delayed rebound, and higher balance of payments and fiscal financing needs.

11. The DSA assumes that financing needs would be covered by identified external sources, including debt service suspension under the DSSI and by net domestic borrowing up to the authorities' annual ceiling of 3 percent of GDP. Multilateral and bilateral sources for budget support of US$168 million (2.7 percent of GDP) are expected to be mobilized through 2020-22, of which 73 percent are anticipated from multilateral sources (the World Bank and the African Development Bank).[6] While projecting continued concessional foreign support in the short and medium term, the DSA assumes a slow and gradual shift toward less concessional sources in the long term, including semi-concessional loans (with a grant element of less than 5 percent) and limited non-concessional borrowing, consistent with Cabo Verde's middle-income status. With respect to domestic debt, the DSA assumes that bonds with maturities of at least 4 years would account for 97 percent of the stock in the medium term, in line with the profile of domestic debt portfolio at end-2019. The average interest rate is set to 1 percent for T-bills, and 4 and 5 percent for short-term and medium to longer-term bonds, respectively. Based on agreements secured by the authorities, debt service suspension under the DSSI amounts to US$ 8.96 million (about 0.5 percent of GDP) in 2020.

12. Tools for assessing the realism of the baseline scenario flag some deviation from historical experience, which are explained below.

- **Drivers of debt dynamics** (Figure 3). The current DSA projects similar debt accumulation in 2020-21, while slightly higher after 2022, compared to the previous DSA. The contributions of past and projected debt-creating flows to the PPG external debt and to gross public debt have also changed with the higher current account deficit and lower FDI negatively contributing to PPG external debt accumulation; and the higher primary fiscal deficit contributing to the accumulation of gross public debt relative to its historical trajectory.

- **Realism of planned fiscal adjustment** (Figure 4). The projected three-year fiscal adjustment in the primary balance stands at 1.5 percentage points of GDP between 2019 and 2022 and lies in the second quartile of the distribution of past adjustments of the primary fiscal deficit derived from the sample of LICs.

- **Consistency between fiscal adjustment and growth** (Figure 4). The projected growth path for 2020 and 2021 is revised down compared to the past DSA, and it is not in line with the multiplier-based projections. This reflects a large shock to the economy due to the pandemic and its severe impact on economic activity. Following a robust increase in the first quarter of

[6] The World Bank approved in April 2020 a COVID-19 Emergency Response operation totaling US$5 million. The Disaster Risk Management Development Policy Financing with CAT-DDO amounting US$10 million was disbursed in May 2020. The Second State-Owned Enterprise Reform and Fiscal Management Development Policy Financing, totaling US$25 million is expected to be disbursed in the third quarter of 2020.

2020 by 5.8 percent (y/y), output is forecasted to decelerate by 6.8 percent, consistent with the two-month long lockdown that was introduced in April. A slow recovery is projected for 2021 with a real GDP growth of 4.5 percent. The realism of these projections is predicated on a gradual revival in the most affected sectors (tourism, transport, and other services) which are expected to pick up in the fourth quarter of 2020, and on the authorities' commitment to accelerate structural reforms and fiscal consolidation efforts when the health crisis abates.

- **Consistency between public investment and growth** (Figure 4). The realism tool shows that like historical figures, the contribution of public investment to real GDP growth remains marginal across the previous and current DSA, mainly reflecting low multiplier for public investment, consistent with the high import content of capital spending. While public investment is expected to hover around 4-5 percent of GDP in the medium term, private investment is projected to rise gradually to about 40 percent of GDP during 2020–25.

C. Country Classification and Determination of Stress Test Scenarios

13. Cabo Verde's debt-carrying capacity is assessed as "strong" as in the previous DSA (Text Table 5). The methodology relies on a composite indicator (CI) combining the Country Policy and Institutional Assessment (CPIA) score, external conditions captured by world economic growth and country-specific factors. The latest CI score continues to be based on the October 2019 World Economic Outlook (WEO) vintage, and the 2018 CPIA. The CI score for Cabo Verde stands at 3.28, which is above the threshold of 3.05 applicable for a "strong" rating. It reflects positive contributions from the CPIA (44 percent), international reserves (30 percent), world growth (14 percent), remittances (7 percent) and country real growth rate (3 percent). Debt burden thresholds implied by the strong debt-carrying capacity under the previous and new frameworks are summarized in Text Table 6.

Text Table 5. Cabo Verde: CI Score Summary Table

Components	Coefficients (A)	10-year average values (B)	CI Score components (A*B) = (C)	Contribution of components
CPIA	0.385	3.778	1.45	44%
Real growth rate (in percent)	2.719	3.999	0.11	3%
Import coverage of reserves (in percent)	4.052	49.735	2.02	61%
Import coverage of reserves^2 (in percent)	-3.990	24.736	-0.99	-30%
Remittances (in percent)	2.022	10.814	0.22	7%
World economic growth (in percent)	13.520	3.499	0.47	14%
CI Score			3.28	100%
CI rating			Strong	

Source: IMF staff calculations. The CI cutoff for strong debt-carrying capacity is CI > 3.05.

Text Table 6. Cabo Verde: Debt Thresholds under Strong Debt-Carrying Capacity

EXTERNAL debt burden thresholds	Weak	Medium	Strong
PV of debt in % of			
Exports	140	180	240
GDP	30	40	55
Debt service in % of			
Exports	10	15	21
Revenue	14	18	23

Source: IMF staff calculations.

14. The debt sustainability analysis relies on the six standardized stress tests and the contingent liability stress test. While the former uses the default settings, the latter is customized to address potential vulnerabilities stemming from the current coverage of public sector debt as explained in paragraph 2. None of the tailored stress tests is triggered for Cabo Verde.

DEBT SUSTAINABILITY ANALYSIS

A. External Public Debt

15. Under the baseline scenario, the PV of PPG external debt-to-GDP ratio breaches its applicable threshold during 2020-24, thereby signaling a high risk of external debt distress (Figure 1, Tables 1 and 3). In addition, the PV of PPG external debt-to-export ratio breaches its threshold in 2020. The other debt burden indicators remain below the prescribed thresholds. However, both debt service-to-exports and debt service-to-revenue ratios increase throughout 2021-22 (when Cabo Verde starts repaying the principal due on loans from the Portuguese bank Caixa Geral de Depósitos) and decrease gradually from 2023 onward.

16. The PV of PPG external debt-to-GDP ratio also breaches its threshold protractedly under the stress test scenarios (Figure 1, Tables 1 and 3). Under the most extreme shock, which is a one-time 30 percent nominal depreciation, it rises to 91.7 percent in 2021 before gradually receding below the threshold of 55 percent of GDP in 2029. The threshold is also breached under the remaining five standardized bound tests, and under the tailored combined contingent liabilities test during 2020–27. The PV of PPG external debt-to-exports ratio exceeds its applicable threshold during 2020–26, rising to 395.1 percent of GDP in 2022, and gradually decreasing below the threshold of 240 percent of GDP by 2027. Likewise, both of Cabo Verde's debt service-related indicators breach their respective thresholds under the stress test scenario over the projection period. The external debt service-to-export ratio breaches its threshold during 2022-24, while the external debt service to revenue breaches its threshold during 2021–24. The projected trajectories of PPG external debt burden indicators are vulnerable to an export growth shock and to a one-time depreciation shock, stressing the need for export diversification.

B. Total Public Debt

17. The PV of total public debt-to-GDP ratio exceeds the 70 percent benchmark till 2027 under the baseline scenario (Figure 2, Tables 2 and 4).[1] The prescribed benchmark is also breached throughout the projection period under the six standardized bound tests and the tailored combined contingent liabilities test. Furthermore, the debt outlook, as shown by the public DSA indicators, is particularly vulnerable to contingent liabilities associated with SOEs' debt and one-time depreciation, which emerges as the most extreme shock. Still, despite the high public debt-to-GDP level, Cape Verde's debt is assessed to be sustainable given its high share of highly concessional external debt and moderate debt service ratios. Roll-over risks from domestic public debt are also mitigated by the maturity structure of the debt and the fact that around 40 percent of domestic debt is held by the Social Security Fund.

C. Debt Distress Ratings

18. Cabo Verde's risk of external and overall debt distress is assessed as "high" under the baseline scenario. As discussed earlier, the PV of PPG external debt-to-GDP ratio breaches its threshold till 2024 under the baseline scenario, thereby signaling a high risk of external debt distress, and is particularly sensitive to export and growth shocks. Based on the current projections, it is expected that it will gradually decline, falling below the 55 percent threshold in 2025. The "high" risk of overall debt distress is the outcome of the breach of the PV of total public debt-to-GDP ratio through 2027.

19. The outlook for public debt has deteriorated following the pandemic, and prudent borrowing policies and strengthened debt management are needed to underpin medium-term debt sustainability. The pandemic has led to a rapid deterioration of the country's external and fiscal positions, triggered a sharp contraction in economic activity, and affected medium-term economic prospects. The authorities have sought debt service suspension under the DSSI to support their response to the health crisis. As mentioned above, the DSA assumes that US$ 8.96 million of debt service (principal and interest payments) falling due in 2020 and for which agreements were secured will be reprofiled for 2021–24 in line with the terms of the Initiative.[2] In the aftermath of the health crisis, the authorities will need to refocus on policies and reforms aimed at improving the fiscal position and boosting growth to reset public debt on a declining trend over the medium term. More generally, prudent borrowing policies, adhering to the zero limit on non-concessional external borrowing in the next few years, as well as strengthened debt management strategy remain key to stabilize future debt dynamics. Ensuring medium to long-term debt sustainability will also require sustained implementation of growth-enhancing structural reforms with a focus on actions needed to diversify the production and export base, and to address critical infrastructure gaps. Measures to develop the government securities market and lower the costs of domestic borrowing will be also crucial going forward.

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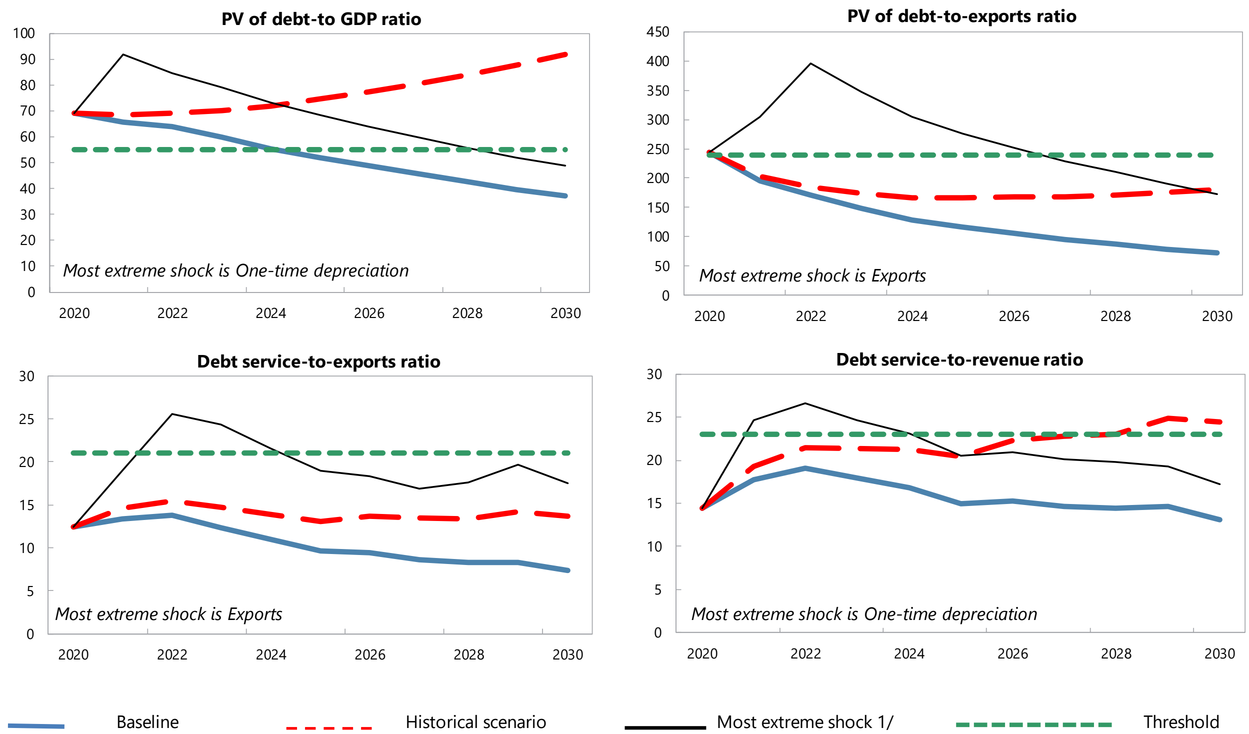
[1] While in 2028, the PV of total debt-to-GDP reaches the threshold.

[2] While debt service for May and June was eligible for suspension under the Initiative, the authorities paid these obligations while waiting for participation confirmation from creditors.

D. Authorities' Views

20. The authorities agreed with the results of the DSA and stressed their concerns about the fragility of the Cabo Verdean economy. The health crisis exposed some of the key structural challenges facing the economy, including the lack of diversification, heavy reliance on tourism, and vulnerability to exogenous shocks. The lack of natural resources combined with relatively limited fiscal space at the beginning of the health crisis, made broad-based responses to the pandemic difficult and costly, involving numerous trade-offs. The authorities reaffirmed their continued commitment to fiscal consolidation and to the goal of a public debt-to-GDP ratio lower than 100 percent over the medium term. They stressed, however, that their efforts have now been jeopardized by the pandemic. They highlighted the high uncertainties of macroeconomic assumptions and called on the IMF and the World Bank to provide them with analytical tools to inform policy discussions on debt management. At the same time, the authorities indicated that they remain committed to prudent borrowing policies, and will work towards strengthening debt management practices, and improving the functioning of the government securities market, to enhance debt sustainability in the long term.

Figure 1. Cabo Verde: Indicators of Public and Publicly Guaranteed External Debt Under Alternative Scenarios, 2020–30



Customization of Default Settings	Size	Interactions
Standardized Tests		Yes
Tailored Tests		
Combined CLs	Yes	
Natural Disasters	n.a.	n.a.
Commodity Prices [2/]	n.a.	n.a.
Market Financing	n.a.	n.a.

Note: "Yes" indicates any change to the size or interactions of the default settings for the stress tests. "n.a." indicates that the stress test does not apply.

Borrowing Assumptions for Stress Tests*	Default	User defined
Shares of marginal debt		
External PPG MLT debt	100%	
Terms of marginal debt		
Avg. nominal interest rate on new borrowing in USD	1.8%	1.8%
USD Discount rate	5.0%	5.0%
Avg. maturity (incl. grace period)	22	22
Avg. grace period	6	6

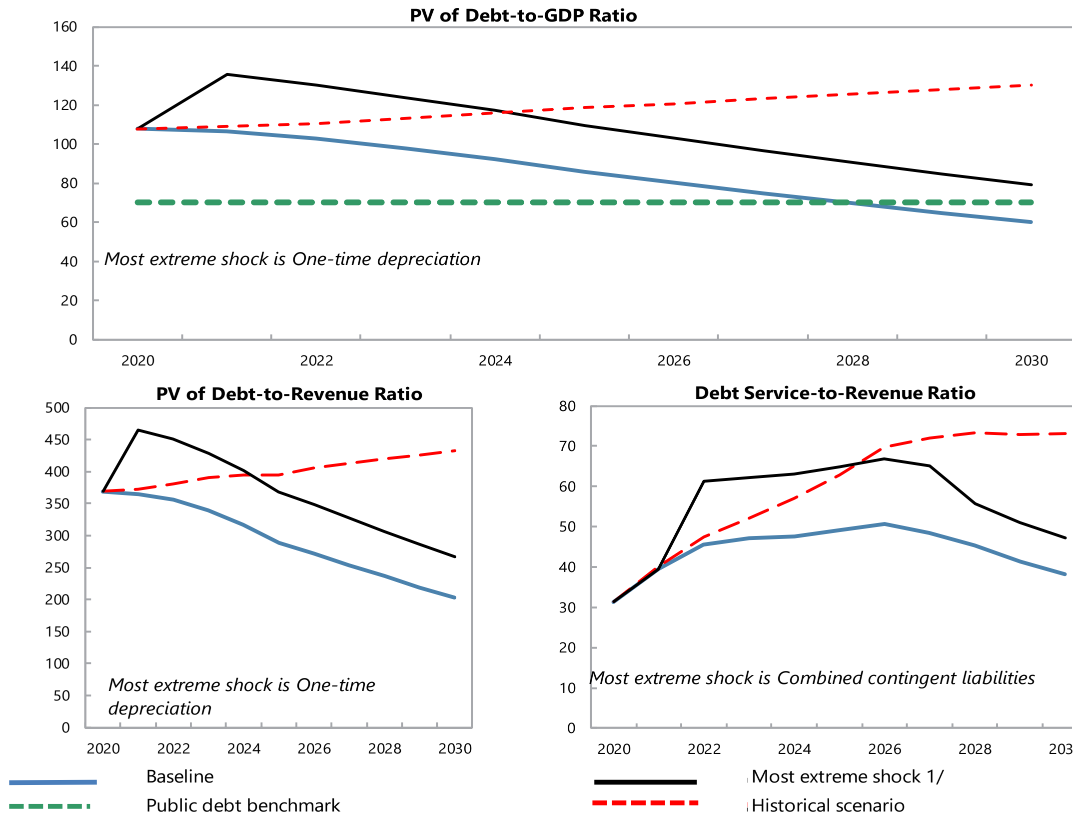
* Note: All the additional financing needs generated by the shocks under the stress tests are assumed to be covered by PPG external MLT debt in the external DSA. Default terms of marginal debt are based on baseline 10-year projections.

Sources: Country authorities; and staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio in or before 2030. Stress tests with one-off breaches are also presented (if any), while these one-off breaches are deemed away for mechanical signals. When a stress test with a one-off breach happens to be the most exterme shock even after disregarding the one-off breach, only that stress test (with a one-off breach) would be presented.

2/ The magnitude of shocks used for the commodity price shock stress test are based on the commodity prices outlook prepared by the IMF research department.

Figure 2. Cabo Verde: Indicators of Public Debt Under Alternative Scenarios, 2020–30



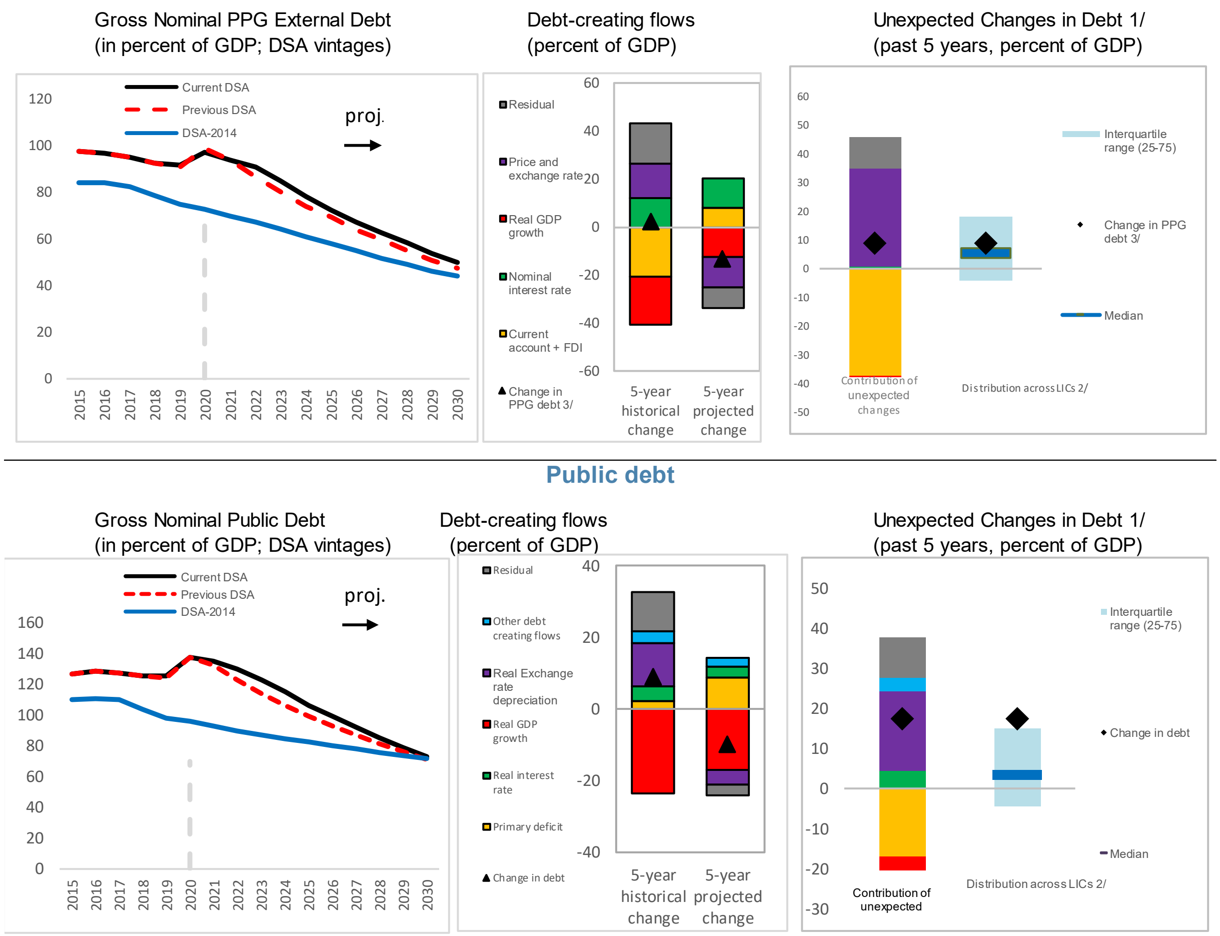
Borrowing Assumptions for Stress Tests*	Default	User defined
Shares of marginal debt		
External PPG medium and long-term	35%	35%
Domestic medium and long-term	63%	63%
Domestic short-term	1%	1%
Terms of marginal debt		
External MLT debt		
Avg. nominal interest rate on new borrowing in USD	1.8%	1.8%
Avg. maturity (incl. grace period)	22	22
Avg. grace period	6	6
Domestic MLT debt		
Avg. real interest rate on new borrowing	3.6%	3.6%
Avg. maturity (incl. grace period)	6	6
Avg. grace period	0	0
Domestic short-term debt		
Avg. real interest rate	0%	0.0%

* Note: The public DSA allows for domestic financing to cover the additional financing needs generated by the shocks under the stress tests in the public DSA. Default terms of marginal debt are based on baseline 10-year projections.

Sources: Country authorities; and staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio in or before 2030. The stress test with a one-off breach is also presented (if any), while the one-off breach is deemed away for mechanical signals. When a stress test with a one-off breach happens to be the most exterme shock even after disregarding the one-off breach, only that stress test (with a one-off breach) would be presented.

Figure 3. Cabo Verde: Drivers of Debt Dynamics - Baseline Scenario



Sources: Country authorities; and staff estimates and projections.

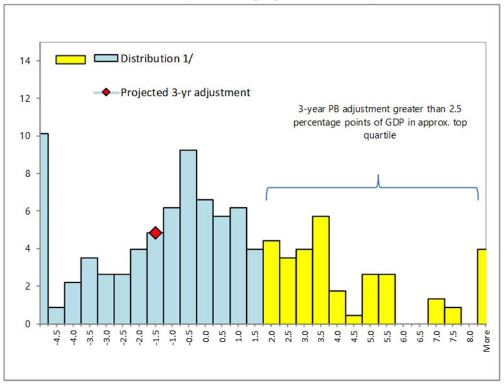
1/ Difference between anticipated and actual contributions on debt ratios.

2/ Distribution across LICs for which LIC DSAs were produced.

3/ Given the relatively low private external debt for average low-income countries, a ppt change in PPG external debt should be largely explained by the drivers of the external debt dynamics equation.

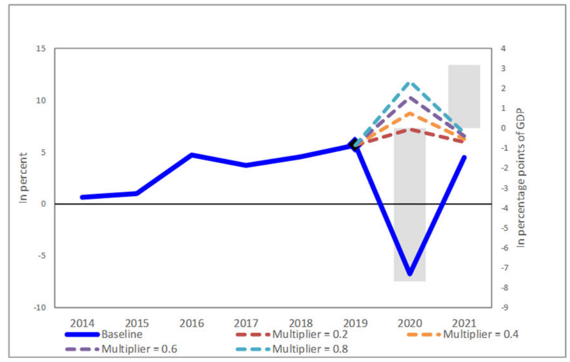
Figure 4. Cabo Verde: Realism Tools

3-Year Adjustment in Primary Balance
(Percentage points of GDP)



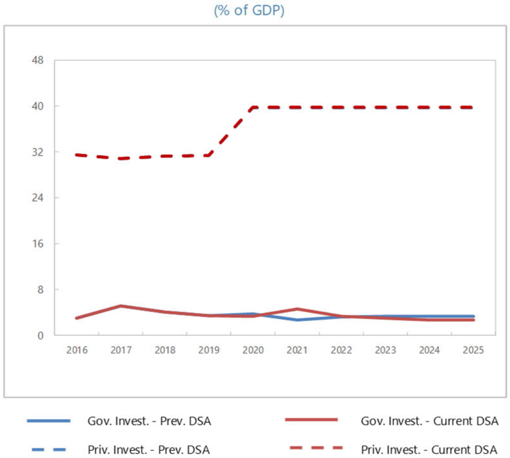
1/ Data cover Fund-supported programs for LICs (excluding emergency financing) approved since 1990. The size of 3-year adjustment from program inception is found on the horizontal axis; the percent of sample is found on the vertical axis.

Fiscal Adjustment and Possible Growth Paths 1/

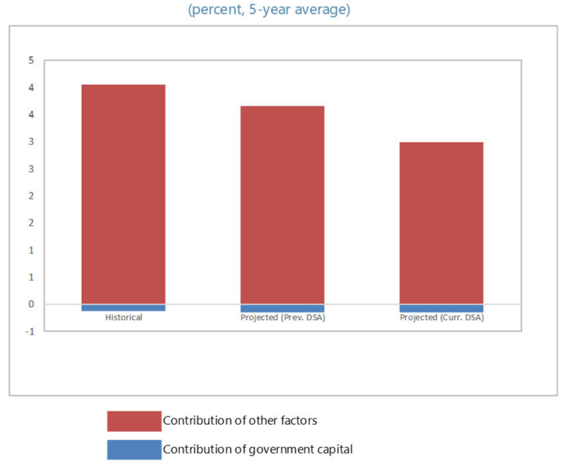


1/ Bars refer to annual projected fiscal adjustment (right-hand side scale) and lines show possible real GDP growth paths under different fiscal multipliers (left-hand side scale).

Public and Private Investment Rates
(% of GDP)



Contribution to Real GDP growth
(percent, 5-year average)



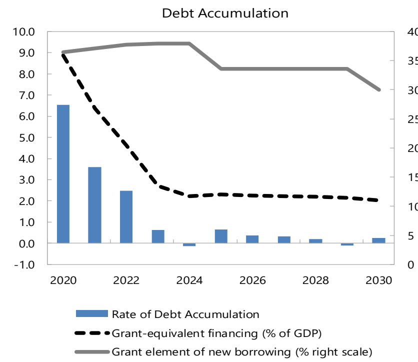
Sources: Country authorities; and staff estimates and projections.

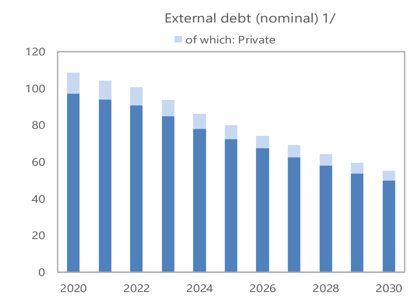
Table 1. Cabo Verde: External Debt Sustainability Framework, Baseline Scenario, 2019–40

(Percent of GDP, unless otherwise indicated)

	Actual	Projections								Average 8/	
	2019	2020	2021	2022	2023	2024	2025	2030	2040	Historical	Projections
External debt (nominal) 1/	**102.0**	**108.4**	**104.2**	**100.5**	**93.7**	**86.1**	**79.8**	**55.2**	**24.8**	**93.6**	**81.3**
of which: public and publicly guaranteed (PPG)	**91.4**	**97.0**	**93.8**	**90.8**	**84.8**	**78.0**	**72.3**	**49.9**	**24.8**	**81.6**	**73.5**
Change in external debt	-0.9	6.4	-4.2	-3.7	-6.8	-7.5	-6.3	-4.2	-5.6		
Identified net debt-creating flows	**-5.1**	**20.7**	**2.0**	**-2.0**	**-5.3**	**-7.3**	**-7.2**	**-6.4**	**-4.5**	**0.8**	**-2.9**
Non-interest current account deficit	**-2.5**	**11.9**	**6.7**	**3.8**	**1.6**	**-0.2**	**-0.4**	**-1.3**	**-0.6**	**4.9**	**1.7**
Deficit in balance of goods and services	14.0	25.5	19.7	16.6	14.4	12.2	10.9	6.6	8.2	**20.4**	**12.5**
Exports	50.7	28.3	33.8	37.3	40.2	42.9	44.7	51.0	60.7		
Imports	64.6	53.8	53.5	53.9	54.6	55.1	55.6	57.6	69.0		
Net current transfers (negative = inflow)	-16.4	-14.4	-13.3	-12.8	-12.8	-13.3	-12.2	-8.4	-9.2	**-16.6**	**-11.3**
of which: official	-3.0	-4.4	-4.4	-3.2	-2.2	-2.5	-1.9	-0.8	-0.4		
Other current account flows (negative = net inflow)	-0.1	0.8	0.2	0.1	0.0	0.9	0.8	0.5	0.4	**1.0**	**0.5**
Net FDI (negative = inflow)	**-4.0**	**-0.8**	**-2.8**	**-3.7**	**-4.0**	**-4.3**	**-4.0**	**-4.0**	**-3.8**	**-5.5**	**-3.6**
Endogenous debt dynamics 2/	**1.4**	**9.7**	**-1.9**	**-2.1**	**-2.9**	**-2.8**	**-2.7**	**-1.2**	**-0.1**		
Contribution from nominal interest rate	2.2	2.3	2.5	2.5	2.5	2.4	2.2	1.9	1.4		
Contribution from real GDP growth	-5.8	7.3	-4.4	-4.7	-5.4	-5.2	-4.9	-3.0	-1.6		
Contribution from price and exchange rate changes	5.0	...	...	...	...	...	...	...	...		
Residual 3/	**4.2**	**-14.3**	**-6.2**	**-1.7**	**-1.5**	**-0.2**	**0.9**	**2.3**	**-1.1**	**3.8**	**-1.3**
of which: exceptional financing	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Sustainability indicators											
PV of PPG external debt-to-GDP ratio	**58.8**	**69.2**	**65.8**	**63.8**	**59.9**	**55.5**	**52.0**	**37.1**	**18.6**		
PV of PPG external debt-to-exports ratio	**116.1**	**244.3**	**194.8**	**170.9**	**149.0**	**129.4**	**116.4**	**72.8**	**30.6**		
PPG debt service-to-exports ratio	**7.0**	**12.5**	**13.4**	**13.7**	**12.4**	**11.0**	**9.6**	**7.3**	**4.0**		
PPG debt service-to-revenue ratio	**13.5**	**14.4**	**17.7**	**19.1**	**17.9**	**16.8**	**15.0**	**13.1**	**8.6**		
Gross external financing need (Million of U.S. dollars)	-35.4	301.9	204.5	148.1	95.3	40.9	31.8	-13.5	-83.4		
Key macroeconomic assumptions											
Real GDP growth (in percent)	5.7	-6.8	4.5	4.8	5.7	6.0	6.2	5.5	5.5	**2.8**	**4.4**
GDP deflator in US dollar terms (change in percent)	-4.6	1.2	6.0	2.1	1.8	1.6	1.7	1.8	2.4	**-0.9**	**2.1**
Effective interest rate (percent) 4/	2.2	2.2	2.6	2.6	2.7	2.7	2.8	3.4	5.1	**3.2**	**2.8**
Growth of exports of G&S (US dollar terms, in percent)	4.3	-47.2	31.9	18.3	15.8	14.9	12.5	9.5	10.2	**6.9**	**8.9**
Growth of imports of G&S (US dollar terms, in percent)	-4.2	-21.4	10.1	7.8	9.0	8.6	9.0	9.0	9.7	**2.8**	**5.8**
Grant element of new public sector borrowing (in percent)	...	36.4	37.1	37.7	37.9	37.9	33.6	30.0	30.0	**...**	**35.0**
Government revenues (excluding grants, in percent of GDP)	26.2	24.5	25.6	26.9	27.8	28.0	28.7	28.5	27.9	**23.5**	**27.6**
Aid flows (in Million of US dollars) 5/	170.8	267.6	228.0	200.0	126.5	103.6	118.9	140.2	252.8		
Grant-equivalent financing (in percent of GDP) 6/	...	8.9	6.4	4.6	2.7	2.2	2.3	2.0	1.9	**...**	**3.5**
Grant-equivalent financing (in percent of external financing) 6/	...	54.7	57.8	51.5	51.0	55.2	49.7	49.0	52.1	**...**	**52.0**
Nominal GDP (Million of US dollars)	1,982	1,870	2,071	2,215	2,384	2,567	2,771	3,969	8,238		
Nominal dollar GDP growth	0.8	-5.6	10.7	7.0	7.6	7.7	8.0	7.4	8.0	**1.9**	**6.6**
Memorandum items:											
PV of external debt 7/	69.3	80.6	76.2	73.5	68.7	63.6	59.4	42.4	18.6		
In percent of exports	136.8	284.4	225.6	196.7	171.0	148.3	133.0	83.2	30.6		
Total external debt service-to-exports ratio	9.5	18.0	17.8	17.6	15.9	14.2	12.6	9.7	5.6		
PV of PPG external debt (in Million of US dollars)	1165.3	1294.7	1362.0	1413.5	1427.4	1424.1	1441.0	1473.3	1533.3		
(PVt-PVt-1)/GDPt-1 (in percent)		6.5	3.6	2.5	0.6	-0.1	0.7	0.3	-0.7		
Non-interest current account deficit that stabilizes debt ratio	-1.6	5.5	10.8	7.6	8.4	7.3	5.9	2.9	5.0		

Definition of external/domestic debt	**Residency-based**
Is there a material difference between the two criteria?	**No**





Sources: Country authorities; and staff estimates and projections.

1/ Includes both public and private sector external debt.

2/ Derived as [r - g - ρ(1+g) + Ɛα (1+r)]/(1+g+ρ+gρ) times previous period debt ratio, with r = nominal interest rate; g = real GDP growth rate, ρ = growth rate of GDP deflator in U.S. dollar terms, Ɛ=nominal appreciation of the local currency, and α= share of local currency-denominated external debt in total external debt.

3/ Includes exceptional financing (i.e., changes in arrears and debt relief); changes in gross foreign assets; and valuation adjustments. For projections also includes contribution from price and exchange rate changes.

4/ Current-year interest payments divided by previous period debt stock.

5/ Defined as grants, concessional loans, and debt relief.

6/ Grant-equivalent financing includes grants provided directly to the government and through new borrowing (difference between the face value and the PV of new debt).

7/ Assumes that PV of private sector debt is equivalent to its face value.

8/ Historical averages are generally derived over the past 10 years, subject to data availability, whereas projections averages are over the first year of projection and the next 10 years.

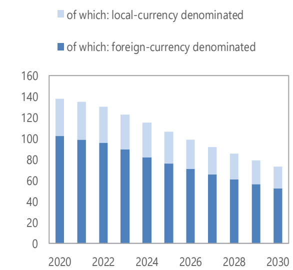
Table 2. Cabo Verde: Public Sector Debt Sustainability Framework, Baseline Scenario, 2019–40

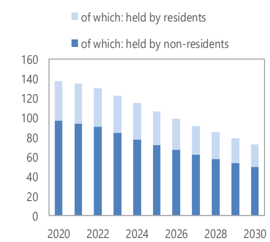
(Percent of GDP, unless otherwise indicated)

	Actual	Projections													Average 6/	
	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029		2030	2040	Historical	Projections
Public sector debt 1/	**125.0**	**137.5**	**134.8**	**130.0**	**122.8**	**114.9**	**106.3**	**98.9**	**91.8**	**85.2**	**78.8**		**73.0**	**29.8**	**109.3**	**106.7**
of which: external debt	**91.4**	**97.0**	**93.8**	**90.8**	**84.8**	**78.0**	**72.3**	**67.2**	**62.5**	**58.0**	**53.7**		**49.9**	**24.8**	**81.6**	**73.5**
Change in public sector debt	-0.6	12.5	-2.7	-4.8	-7.2	-7.9	-8.6	-7.5	-7.0	-6.7	-6.3		-5.8	-4.3		
Identified debt-creating flows	**-0.2**	**16.4**	**-3.0**	**-4.9**	**-7.4**	**-8.0**	**-8.7**	**-7.4**	**-6.9**	**-6.6**	**-6.3**		**-5.8**	**-3.1**	**5.3**	**-4.4**
Primary deficit	**-0.7**	**7.0**	**3.8**	**0.8**	**-1.0**	**-1.8**	**-2.5**	**-2.2**	**-2.2**	**-2.2**	**-2.3**		**-2.1**	**-1.2**	**3.8**	**-0.4**
Revenue and grants	29.4	29.2	29.2	28.9	28.9	29.2	29.8	29.5	29.5	29.5	29.6		29.6	29.1	**26.6**	**29.4**
of which: grants	3.2	4.7	3.6	2.0	1.1	1.1	1.1	1.1	1.1	1.1	1.1		1.1	1.1		
Primary (noninterest) expenditure	28.7	36.2	33.0	29.7	27.9	27.3	27.3	27.3	27.3	27.3	27.3		27.5	27.9	**30.4**	**28.9**
Automatic debt dynamics	**-2.8**	**7.0**	**-6.8**	**-5.7**	**-6.4**	**-6.2**	**-6.2**	**-5.2**	**-4.7**	**-4.3**	**-4.0**		**-3.6**	**-1.8**		
Contribution from interest rate/growth differential	-5.9	10.2	-5.2	-5.7	-6.7	-6.6	-6.4	-5.3	-4.8	-4.4	-4.0		-3.7	-1.7		
of which: contribution from average real interest rate	0.8	1.2	0.7	0.4	0.3	0.3	0.3	0.3	0.4	0.4	0.4		0.4	0.1		
of which: contribution from real GDP growth	-6.7	9.1	-5.9	-6.1	-7.1	-7.0	-6.7	-5.6	-5.1	-4.8	-4.4		-4.1	-1.8		
Contribution from real exchange rate depreciation	3.1	...	...	...	...	...	...	...	...	...	...		...	...		
Other identified debt-creating flows	**3.3**	**2.5**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**		**0.0**	**-0.1**	**1.1**	**0.2**
Privatization receipts (negative)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0		
Recognition of contingent liabilities (e.g., bank recapitalization)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0		
Debt relief (HIPC and other)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		0.0	-0.1		
Other debt creating or reducing flow (please specify)	3.3	2.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0		
Residual	**-0.4**	**-7.2**	**-1.3**	**0.2**	**0.5**	**0.5**	**0.4**	**0.0**	**0.0**	**0.0**	**0.0**		**0.0**	**-1.3**	**0.9**	**-0.6**
Sustainability indicators																
PV of public debt-to-GDP ratio 2/	**92.4**	**107.7**	**106.5**	**102.9**	**97.9**	**92.4**	**86.0**	**80.4**	**75.0**	**69.8**	**64.8**		**60.2**	**23.6**		
PV of public debt-to-revenue and grants ratio	**314.2**	**369.1**	**364.7**	**356.1**	**338.6**	**316.8**	**288.8**	**272.6**	**254.2**	**236.6**	**219.1**		**203.2**	**81.1**		
Debt service-to-revenue and grants ratio 3/	**26.9**	**31.4**	**39.6**	**45.6**	**47.1**	**47.6**	**49.2**	**50.7**	**48.5**	**45.4**	**41.3**		**38.2**	**15.7**		
Gross financing need 4/	7.2	18.6	15.3	14.0	12.6	12.1	12.1	12.8	12.1	11.2	9.9		9.2	3.2		
Key macroeconomic and fiscal assumptions																
Real GDP growth (in percent)	5.7	-6.8	4.5	4.8	5.7	6.0	6.2	5.5	5.5	5.5	5.5		5.5	5.5	**2.8**	**4.4**
Average nominal interest rate on external debt (in percent)	1.1	0.8	1.2	1.2	1.3	1.3	1.2	1.3	1.3	1.3	1.4		1.4	1.8	**1.2**	**1.2**
Average real interest rate on domestic debt (in percent)	4.4	3.4	3.3	3.1	3.0	3.0	2.8	2.8	3.0	3.2	3.3		3.3	2.8	**4.3**	**3.1**
Real exchange rate depreciation (in percent, + indicates depreciation)	3.6	...	...	...	...	...	...	...	...	...	...		...	...	**3.5**	**...**
Inflation rate (GDP deflator, in percent)	0.6	1.1	1.2	1.4	1.5	1.6	1.7	1.8	1.8	1.8	1.8	1.8	1.8	2.4	**0.9**	**1.6**
Growth of real primary spending (deflated by GDP deflator, in percent)	7.1	17.5	-4.6	-5.8	-0.4	3.8	5.9	5.6	5.4	5.5	5.5		6.4	5.5	**2.0**	**4.1**
Primary deficit that stabilizes the debt-to-GDP ratio 5/	-0.1	-5.6	6.5	5.5	6.3	6.1	6.1	5.3	4.8	4.4	4.1		3.7	3.1	**1.0**	**4.3**
PV of contingent liabilities (not included in public sector debt)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0		

Definition of external/domestic debt	**Residency-based**
Is there a material difference between the two criteria?	**No**

Public sector debt 1/





Sources: Country authorities; and staff estimates and projections.

1/ Coverage of debt: The central government plus extra budgetary funds, central bank, government-guaranteed debt. Definition of external debt is Residency-based.

2/ The underlying PV of external debt-to-GDP ratio under the public DSA differs from the external DSA with the size of differences depending on exchange rates projections.

3/ Debt service is defined as the sum of interest and amortization of medium and long-term, and short-term debt.

4/ Gross financing need is defined as the primary deficit plus debt service plus the stock of short-term debt at the end of the last period and other debt creating/reducing flows.

5/ Defined as a primary deficit minus a change in the public debt-to-GDP ratio ((-): a primary surplus), which would stabilizes the debt ratio only in the year in question.

6/ Historical averages are generally derived over the past 10 years, subject to data availability, whereas projections averages are over the first year of projection and the next 10 years.

Table 3. Cabo Verde: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2020–30

(Percent)

	Projections										
	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030
PV of debt-to GDP ratio											
Baseline	**69**	**66**	**64**	**60**	**55**	52	49	46	43	40	37
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2020-2040 1/	**69**	**68**	**69**	**70**	**72**	**75**	**77**	**80**	**84**	**88**	**92**
B. Bound Tests											
B1. Real GDP growth	**69**	**68**	**69**	**64**	**60**	**56**	52	49	46	43	40
B2. Primary balance	**69**	**67**	**66**	**63**	**59**	**55**	52	49	47	44	41
B3. Exports	**69**	**73**	**82**	**77**	**72**	**68**	**65**	**61**	**57**	53	49
B4. Other flows 2/	**69**	**68**	**68**	**64**	**60**	**56**	53	50	46	43	40
B6. One-time 30 percent nominal depreciation	**69**	**92**	**85**	**79**	**73**	**68**	**64**	**60**	**56**	52	49
B6. Combination of B1-B5	**69**	**75**	**76**	**71**	**66**	**63**	**59**	**55**	52	48	44
C. Tailored Tests											
C1. Combined contingent liabilities	**69**	**73**	**72**	**69**	**65**	**62**	**60**	**57**	54	52	49
C2. Natural disaster	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Threshold	55	55	55	55	55	55	55	55	55	55	55
PV of debt-to-exports ratio											
Baseline	**244**	195	171	149	129	116	106	95	87	79	73
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2020-2040 1/	**244**	202	185	174	167	167	168	167	171	175	180
B. Bound Tests											
B1. Real GDP growth	**244**	195	171	149	129	116	106	95	87	79	73
B2. Primary balance	**244**	198	178	156	137	124	113	103	95	87	80
B3. Exports	**244**	**305**	**395**	**347**	**304**	**276**	**252**	229	210	190	173
B4. Other flows 2/	**244**	202	183	160	139	126	114	103	94	86	79
B6. One-time 30 percent nominal depreciation	**244**	195	162	141	122	110	100	89	82	74	69
B6. Combination of B1-B5	**244**	**284**	192	**263**	229	207	189	171	155	141	129
C. Tailored Tests											
C1. Combined contingent liabilities	**244**	217	193	171	152	139	129	119	111	103	97
C2. Natural disaster	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Threshold	240	240	240	240	240	240	240	240	240	240	240
Debt service-to-exports ratio											
Baseline	12	13	14	12	11	10	9	9	8	8	7
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2020-2040 1/	12	15	15	15	14	13	14	13	13	14	14
B. Bound Tests											
B1. Real GDP growth	12	13	14	12	11	10	9	9	8	8	7
B2. Primary balance	12	13	14	13	11	10	10	9	9	9	8
B3. Exports	12	19	**26**	**24**	**22**	19	18	17	18	20	18
B4. Other flows 2/	12	13	14	13	11	10	10	9	9	9	8
B6. One-time 30 percent nominal depreciation	12	13	14	12	11	9	9	9	8	8	7
B6. Combination of B1-B5	12	18	**22**	20	18	16	15	14	15	15	13
C. Tailored Tests											
C1. Combined contingent liabilities	12	13	14	13	11	10	10	9	9	9	8
C2. Natural disaster	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Threshold	21	21	21	21	21	21	21	21	21	21	21
Debt service-to-revenue ratio											
Baseline	14	18	19	18	17	15	15	15	14	15	13
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2020-2040 1/	14	19	21	21	21	20	22	23	**23**	**25**	**24**
B. Bound Tests											
B1. Real GDP growth	14	18	21	19	18	16	16	16	16	16	14
B2. Primary balance	14	18	19	18	17	15	16	15	15	15	14
B3. Exports	14	18	20	19	18	16	17	16	17	19	17
B4. Other flows 2/	14	18	19	18	17	15	16	15	15	16	14
B6. One-time 30 percent nominal depreciation	14	**25**	**27**	**25**	**23**	21	21	20	20	19	17
B6. Combination of B1-B5	14	18	21	20	18	16	17	16	17	18	16
C. Tailored Tests											
C1. Combined contingent liabilities	14	18	20	19	18	16	16	15	15	16	14
C2. Natural disaster	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Threshold	23	23	23	23	23	23	23	23	23	23	23

Sources: Country authorities; and staff estimates and projections.

1/ Variables include real GDP growth, GDP deflator (in U.S. dollar terms), non-interest current account in percent of GDP, and non-debt creating flows.

2/ Includes official and private transfers and FDI.

Table 4. Cabo Verde: Sensitivity Analysis for Key Indicators of Public Debt, 2020–30

(Percent)

	Projections										
	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030
					PV of Debt-to-GDP Ratio						
Baseline	**108**	**107**	**103**	**98**	**92**	**86**	**80**	**75**	70	65	60
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2020-2040 1/	**108**	**109**	**111**	**113**	**116**	**118**	**121**	**123**	**125**	**128**	**130**
B. Bound Tests											
B1. Real GDP growth	**108**	**112**	**114**	**110**	**106**	**101**	**97**	**93**	**89**	**85**	**81**
B2. Primary balance	**108**	**110**	**113**	**107**	**102**	**95**	**89**	**83**	**78**	**73**	68
B3. Exports	**108**	**113**	**121**	**115**	**109**	**102**	**96**	**90**	**84**	**78**	**72**
B4. Other flows 2/	**108**	**109**	**107**	**102**	**97**	**90**	**84**	**79**	**73**	68	63
B6. One-time 30 percent nominal depreciation	**108**	**136**	**130**	**124**	**117**	**110**	**103**	**97**	**90**	**85**	**79**
B6. Combination of B1-B5	**108**	**111**	**114**	**109**	**104**	**98**	**92**	**87**	**82**	**77**	**73**
C. Tailored Tests											
C1. Combined contingent liabilities	**108**	**134**	**130**	**124**	**117**	**110**	**103**	**97**	**91**	**85**	**80**
C2. Natural disaster	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Public debt benchmark	70	70	70	70	70	70	70	70	70	70	70
					PV of Debt-to-Revenue Ratio						
Baseline	369	365	356	339	317	289	273	254	237	219	203
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2020-2040 1/	369	372	381	391	395	395	406	413	420	426	433
B. Bound Tests											
B1. Real GDP growth	369	380	392	381	364	339	328	313	300	286	273
B2. Primary balance	369	377	390	371	348	318	302	282	264	245	229
B3. Exports	369	388	418	399	375	343	326	306	286	263	243
B4. Other flows 2/	369	373	372	354	332	303	286	267	249	230	213
B6. One-time 30 percent nominal depreciation	369	465	451	428	402	368	349	327	306	286	267
B6. Combination of B1-B5	369	380	393	375	354	327	312	294	277	260	244
C. Tailored Tests											
C1. Combined contingent liabilities	369	459	449	428	402	369	350	328	308	288	270
C2. Natural disaster	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
					Debt Service-to-Revenue Ratio						
Baseline	31	40	46	47	48	49	51	48	45	41	38
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2020-2040 1/	31	40	47	52	57	63	70	72	73	73	73
B. Bound Tests											
B1. Real GDP growth	31	41	49	52	54	56	59	58	56	52	50
B2. Primary balance	31	40	48	52	53	54	56	54	50	45	42
B3. Exports	31	40	46	49	49	51	52	50	48	46	42
B4. Other flows 2/	31	40	46	47	48	50	51	49	46	42	39
B6. One-time 30 percent nominal depreciation	31	43	54	57	58	60	62	61	59	56	53
B6. Combination of B1-B5	31	40	48	52	53	55	58	56	54	49	47
C. Tailored Tests											
C1. Combined contingent liabilities	31	40	61	62	63	65	67	65	56	51	47
C2. Natural disaster	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.

Sources: Country authorities; and staff estimates and projections.

1/ Variables include real GDP growth, GDP deflator and primary deficit in percent of GDP.

2/ Includes official and private transfers and FDI.

Statement by Afonso Bevilaqua, Executive Director for Cabo Verde, Pedro Fachada, Alternate Executive Director, and Carla Cruz, Advisor to Executive Director

October 26, 2020

1. On behalf of our Cabo Verdean authorities, we thank the country team led by Ms. Kabedi-Mbuyi for the comprehensive and candid report. Conducting a virtual program review amid a major health crisis is not an easy task—more so for a small country with limited human resources in the public sector. The authorities are pleased with the result and grateful to the team for their dedication, diligence and perseverance.

2. As in many other small island states, the COVID-19 pandemic is having a severe economic and social impact on Cabo Verde due to its high reliance on tourism. The decline in real GDP this year is projected to be the deepest since the country's independence in 1975. Risks to the outlook remain large given the uncertainties about the duration of the pandemic and its possible long-lasting effects.

3. Despite the health crisis, performance under the Policy Coordination Instrument (PCI) has remained strong. The authorities met entirely or partially all reform targets for the second review, as well as all non-quantitative continuous targets and all quantitative targets for end-March 2020, except for the floor on tax revenues. This last target was missed by a small margin due to the early impact of the COVID-19 outbreak. The authorities remain fully committed to the objectives of the PCI and will redouble their efforts to meet all targets agreed for the third and final review, scheduled to be completed at the beginning of 2021.

Recent Economic Developments in the Aftermath of the COVID-19 Outbreak

4. The COVID-19 pandemic hit Cabo Verde in March 2020, interrupting a period of four years of strong economic and social performance. GDP grew on average close to 5 percent between 2016 and 2019, inflation remained low and stable and fiscal consolidation was initiated, putting both the fiscal deficit and the public debt on a declining trend. Further, international reserves strengthened, and poverty declined while social indicators improved in general.

5. With the spread of COVID-19 in Southern Europe and the identification of the first imported cases in one of the most touristic islands in March, the authorities acted quickly to contain community transmission and address the health and economic emergency. They declared the state of emergency, put in place social distancing guidelines, closed international borders, restricted inter-island travel and suspended non-essential activities.

6. Despite the early efforts to contain the pandemic, the number of cases has increased recently, especially after the authorities decided to ease some restrictions. By mid-October, a total of 87 deaths have occurred and 7,800 cases have been recorded, with majority in Santiago,

the largest and most populous island. Adjusted for population, Cabo Verde remains one of the most affected countries in Sub-Saharan Africa.

7. At the same time, the containment measures and the protracted halt in international travel are having a longer and more profound impact on the economy than anticipated. Recent indicators confirm a challenging economic outlook, with the pandemic taking a heavy toll on GDP in the second quarter (31.7 percent decline compared to the same quarter of 2019). Similarly, in June, consumer and business confidence recorded the lowest level in many years. Against this background, real GDP is projected to contract by 6.8 percent in 2020, comparing to a pre-COVID estimate of a 5 percent expansion.

8. The current account deficit is projected to reach 14.2 percent of GDP in 2020, as compared to a small surplus in 2019. This reversal reflects mainly the collapse in tourism receipts and remittances, although it is partially compensated by the drop in imports. Gross international reserves are estimated by staff to decline to €573 million by end-2020, as compared to €663 million in 2019. On the bright side, despite the unprecedented external shock, reserves are projected to remain at a comfortable level, equivalent to more than 7 months of prospective imports of goods and services, providing confidence about the sustainability of the peg regime, the cornerstone of Cabo Verde's monetary policy.

Policy Responses to the COVID-19 crisis

9. The authorities took significant fiscal and monetary measures to mitigate the impact of the health crisis. Priority was given to save the lives of Cabo Verdeans and support the most vulnerable segments of population. Healthcare and social protection services were expanded, while measures were also put in place to support the informal economy, provide relief to companies, ensure liquidity to the banking system, and facilitate credit creation.

10. In June, the authorities adopted a revised 2020 budget, reflecting both the decline in revenues as well as the expansion of COVID-19 related spending. The overall fiscal deficit is now expected to reach 9.7 percent of GDP, compared to 1.7 percent of GDP estimated at the time of the first PCI review in March. In parallel, the authorities have continued to advance fiscal reforms and improve fiscal monitoring to prevent the accumulation of domestic arrears and tax evasion. Regarding COVID-19 spending, the authorities remain committed to high levels of transparency and the responsible use of public resources. These expenditures are being fully disclosed on the Ministry of Finance official website and will be subject to audits in line with Cabo Verde's legal framework, as highlighted by staff in the report.

11. The banking system is facing the current crisis with strengthened capital buffers and improved operational and risk management standards, which will help mitigate the risks posed by the pandemic. Albeit remaining relatively high, legacy non-performing loans (NPLs) have continued to gradually decrease until the outbreak. The authorities remain alert and are

enhancing supervision to contain vulnerabilities stemming from the ongoing deterioration of the economic environment.

The Economic Outlook Going Forward

12. As expected, the pandemic has reversed the downward path of the public debt/GDP ratio. The authorities envisaged before the crisis a reduction in the ratio to below 100 percent by 2024, through fiscal consolidation and growth-enhancing structural reforms. The exceptional financing needs imposed by the crisis have substantially increased public sector borrowing requirements this year. As a result, the public debt is now projected to increase to 137.5 percent of GDP in 2020, compared to 118.1 percent of GDP estimated in the first PCI review. Over the medium-term, public debt is expected to resume the downward trend as the economic recovery takes hold and fiscal consolidation efforts restart. Nevertheless, it is still expected to remain elevated through 2024 given the need to promote public investment to support the recovery and encourage economic diversification.

13. Medium-term objectives will continue to drive the authorities' policies and reform efforts for the remainder of the year and in 2021. The authorities' key medium-term objectives remain to enhance domestic revenue mobilization, strengthen expenditure management, and advance SOEs reforms to support fiscal and public debt sustainability. The authorities continue to strive to improve the business environment and promote private sector development.

14. As agreed under the PCI, a Strategy Note providing a conceptual framework for the operationalization of the SPIGF (Sovereign Private Investment Guarantee Fund) was prepared by the authorities in April 2020. The SPIGF aims to support private sector investment by facilitating access to financing to capital-intensive projects. The Note and posterior revision define the SPIGF operational framework and governance structure, with particular attention to potential contingent liabilities and implications for public debt. The authorities also prepared a timeline to operationalize the SPIGF before the end of the year, in accordance with the legislation.

15. Unfortunately, the SOEs reforms program had to be delayed because of the health crisis. Considering the constraints generated by the pandemic and retrenchment among potential investors, as well as the objective to maximize revenues, the authorities have rescheduled privatizations originally planned for 2020. The authorities remain attentive to market conditions and expect to resume the program as soon as possible.

Conclusion: Cabo Verde Continues to Count on International Support in this Time of Need

16. The COVID-19 pandemic has exposed Cabo Verde's vulnerabilities to plunges in tourism revenue and lack of economic diversification. Significant risks to a sustained recovery are, on the downside, the uncertainty about the duration and trajectory of the pandemic, and, on the upside, the potential for effective and accessible vaccines that could provide confidence to

travelers. Moreover, a prolonged slowdown in the global economy would exacerbate the negative impact on tourism, remittances, and foreign investment, producing an even stronger economic contraction, as well as higher fiscal and balance of payments needs. As highlighted by staff, climate change and natural disasters also remain important long-term downside risks to the economic outlook.

17. While focusing on addressing the short-term impact of the health crisis, the authorities have been working to lay the foundation for the post-COVID recovery and enhance medium and long-term growth prospects. Despite the substantial challenges posed by the pandemic, the authorities remain committed to the key objectives set in the PCI program. Working towards medium-term fiscal and debt sustainability remains a priority. They continue to value the PCI as a fundamental instrument to support their policy framework and structural reforms agenda, as well as to catalyze external financing.

18. A key element in the authorities' strategy is the debt relief agenda. Considering that Cabo Verde's creditors are mainly multilateral institutions, the IMF's advocacy and engagement for potential debt relief negotiations would be extremely important. The authorities continue to count on international support to overcome this crisis like no other and find the path back to debt sustainability and inclusive growth.