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CABO VERDE

July 2022

REQUEST FOR AN ARRANGEMENT UNDER THE EXTENDED CREDIT FACILITY—PRESS RELEASE; STAFF REPORT; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR CABO VERDE

In the context of the Request for an Arrangement Under the Extended Credit Facility, the following documents have been released and are included in this package:

- A **Press Release** including a statement by the Chair of the Executive Board.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on June 15, 2022, following discussions that ended on April 26, 2022, with the officials of Cabo Verde on economic developments and policies underpinning the IMF arrangement under the Extended Credit Facility. Based on information available at the time of these discussions, the staff report was completed on June 3, 2022.
- A **Debt Sustainability Analysis** prepared by the staff of the IMF and the International Development Association.
- A **Statement by the Executive Director** for Cabo Verde.

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

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International Monetary Fund
Washington, D.C.

IMF Executive Board Approves US$60 Million Extended Credit Facility Arrangement for Cabo Verde

FOR IMMEDIATE RELEASE

- IMF Board approves SDR 45.03 million (about US$60 million) three-year ECF arrangement for Cabo Verde, with SDR 11.26 million (about US$15 million) available for immediate disbursement.
- The financing package will help mitigate the lingering impact of the COVID-19 pandemic and the spillover effects of the war in Ukraine; reduce the fiscal deficit and preserve debt sustainability; protect vulnerable groups; and support a reform agenda that leads to higher and more inclusive growth.
- Key policy actions under the program include measures to boost revenue and improve the efficiency of spending, strengthen state-owned enterprises to mitigate fiscal risks, as well as measures to continue modernizing the monetary policy framework and safeguarding financial stability.

Washington, DC – **June 15, 2022:** On June 15, 2022, the Executive Board of the International Monetary Fund (IMF) approved a 36-month arrangement under the Extended Credit Facility (ECF) for Cabo Verde in an amount equivalent to SDR 45.03 million (190 percent of quota or about US$60 million). The ECF arrangement will help shore up international reserves, preserve debt sustainability, increase resilience to shocks, including from climate change, and make growth more inclusive. The program will help fill financing gaps together with the support of continued financing from Cabo Verde's development partners.

Approval of the ECF arrangement enables immediate disbursement of SDR11.26 million (47.5 percent of quota, about US$15 million), fully usable for budget financing, in order to support the implementation of the reforms. This follows Fund emergency support to Cabo Verde in April 2020 under the Rapid Credit Facility (100 percent of quota, SDR 23.7 million, equivalent to US$32.3 million at the time of approval).

Cabo Verde's economy is facing significant challenges associated with the lingering effects of the global pandemic, as well as rising food and fuel prices due to the war in Ukraine and the impact of the ongoing five-year drought. The economy rebounded strongly in 2021 following the COVID-19 induced sharp recession in 2020 (about 15 percent contraction), and recorded growth of 7 percent, which was supported by the easing of international travel restrictions, and the country's highly successful vaccination program (one of the most successful in Africa). However, the spillover effects of the war in Ukraine are expected to weaken the economic recovery and the growth forecast has been revised downward from 6 percent to 4 percent in 2022. Higher commodity prices and weaker than earlier expected prospects for the tourism sector are projected to result in a significant widening of the current account deficit to about 14.1 percent of GDP in 2022, as well as lower international reserves. The overall fiscal deficit is expected to continue to improve to 6.3 percent of GDP in 2022, from 7.3 percent of GDP in 2021.

The ECF arrangement has four main objectives that are aligned with the government's medium-term economic development plan (PEDS). First, strengthening public finances to preserve public debt sustainability and expand social safety nets. Second, reducing fiscal risks from public enterprises and improving their financial management and transparency. Third, modernizing the monetary policy framework and improving the resilience of the financial system. Fourth, raising growth potential and building resilience to shocks through structural reforms and economic diversification.

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

"Cabo Verde showed a strong track record of commitment to reforms and macroeconomic stability before and during the pandemic, which contributed to a strong rebound of the economy following the COVID-19 induced recession. However, the spillover effects of the war in Ukraine, the lingering effects of the pandemic, and the impact of the ongoing five-year drought have weakened economic recovery and resulted in increasing financing needs.

"The new Fund-supported arrangement will support the authorities' priorities to preserve debt sustainability, shore up international reserves, increase resilience to shocks, including from climate change, and make growth more inclusive. The reform agenda will be supported by a well-tailored capacity development strategy which is aligned with the program.

"The key strategy focuses on gradual and growth-friendly fiscal consolidation to place public debt on a decisive downward path and maintain debt sustainability. Fiscal policy will also be guided by the need to increase social spending to protect vulnerable groups. Implementing fiscal structural reforms, including strengthening the tax administration, enhancing public financial management, and reforming state-owned enterprises, will help boost revenue, enhance the efficiency of public spending, and reduce fiscal risks. The authorities' initiatives to further enhance fiscal transparency and governance should continue.

"Modernizing the monetary framework and strengthening the financial sector will help safeguard financial stability and the peg. Bolstering international reserves, carefully unwinding crisis-related support measures, closely monitoring non-performing loans, and further strengthening the AML/CFT framework, will be critical measures in this regard.

"Steadfastly implementing the authorities' development plan will improve the business environment and help support private sector-led growth. Considering Cabo Verde's high vulnerability to the effects of climate change, the planned bold steps to climate adaptation will be key to boost the economy's resilience and growth potential."

Cabo Verde: Selected Economic Indicators, 2019–27

	2019	2020	2021	2022	2023	2024	2025	2026	2027
				Proj.	Proj.	Proj.	Proj.	Proj.	Proj.
				(Annual percent change)					
National accounts and prices 1/									
Real GDP	5.7	-14.8	7.0	4.0	4.8	5.7	5.5	5.0	4.5
GDP deflator	0.6	-0.9	1.8	4.5	2.6	2.0	2.0	2.0	2.0
Consumer price index (annual average)	1.1	0.6	1.9	6.5	3.5	2.0	2.0	2.0	2.0
Consumer price index (end of period)	1.9	-0.9	5.4	6.5	3.5	2.0	2.0	2.0	2.0
External sector									
Exports of goods and services	10.2	-58.7	39.3	11.2	32.6	11.0	9.6	9.0	9.3
Of which: tourism	9.4	-69.1	48.4	14.2	22.2	18.7	11.8	8.7	5.5
Imports of goods and services	1.6	-23.2	11.0	14.4	5.8	7.1	6.4	7.3	6.4
			(Change in percent of broad money, 12 months earlier)						
Money and credit									
Net foreign assets	7.8	-6.6	6.0	-10.6	2.7	1.6	2.1	2.3	1.3
Net domestic assets	0.6	10.3	-4.0	12.2	5.0	5.3	4.6	4.3	4.3
Net claims on the central government	-4.8	-1.3	0.6	1.8	1.6	0.7	0.3	-0.1	-0.4
Credit to the economy	2.3	2.9	1.8	5.1	1.3	2.7	2.1	4.3	3.2
Broad money (M2)	8.4	3.8	2.0	1.6	7.7	6.8	6.7	6.6	5.6
				(Percent of GDP, unless otherwise indicated)					
Savings and investment									
Domestic savings	37.3	20.7	31.0	30.0	35.2	33.9	35.3	34.7	34.7
Government	0.1	-7.4	-4.5	-2.6	-1.8	-0.1	1.7	2.9	2.5
Private	37.2	28.1	35.5	32.6	37.0	34.1	33.6	31.8	32.3
National investment	37.1	35.7	42.3	44.1	41.4	39.8	39.9	39.3	39.0
Government	3.6	3.3	2.2	3.4	3.1	3.1	3.0	3.0	3.0
Private	33.6	32.4	40.1	40.7	38.2	36.7	36.9	36.3	36.0
Savings-investment balance	0.2	-15.0	-11.3	-14.1	-6.2	-5.9	-4.7	-4.6	-4.2
Government	-3.4	-10.7	-6.7	-5.9	-4.9	-3.2	-1.3	-0.1	-0.5
Private	3.6	-4.3	-4.5	-8.1	-1.3	-2.7	-3.4	-4.5	-3.7
External sector									
External current account (including official transfers)	0.2	-15.0	-11.3	-14.1	-6.2	-5.9	-4.7	-4.6	-4.2
External current account (excluding official transfers)	-2.5	-17.6	-14.2	-16.1	-8.1	-7.2	-5.7	-5.6	-5.2
Overall balance of payments	6.8	-4.6	-1.0	-5.2	2.6	1.5	1.9	2.1	1.2
Gross international reserves (months of prospective imports of goods and services)	9.0	7.1	6.3	5.0	5.1	5.1	5.1	5.3	5.2
Government finance									
Revenue	26.8	24.7	22.6	25.4	24.8	25.5	25.9	26.3	26.5
Tax and nontax revenue	23.9	21.4	20.6	23.5	23.6	24.4	24.9	25.4	25.7
Grants	2.9	3.2	2.0	1.9	1.2	1.1	1.0	0.9	0.8
Expenditure	28.5	33.8	29.9	31.7	30.4	29.5	28.1	27.3	27.3
Primary balance	0.7	-6.4	-5.1	-3.6	-2.6	-1.3	0.0	1.0	1.0
Overall balance (incl. grants)	-1.7	-9.1	-7.3	-6.3	-5.6	-4.0	-2.1	-0.9	-0.8
Net other liabilities (incl. onlending)	-3.0	-1.2	0.9	-0.7	-0.5	-0.2	-0.2	-0.2	0.0
Total financing (incl. onlending and capitalization)	4.6	14.0	6.4	7.0	6.2	4.2	2.3	1.1	1.2
Net domestic credit	1.3	2.8	1.6	3.5	3.0	1.3	0.6	-0.3	-0.8
Net external financing	3.3	11.2	4.8	3.5	3.2	2.9	1.7	1.4	1.6
Public debt stock and service									
Total nominal government debt	114.0	142.6	143.0	145.9	139.7	132.5	124.0	116.2	109.6
External government debt	82.6	103.1	101.5	103.6	97.7	93.1	88.4	83.7	79.6
Domestic government debt	31.4	39.5	41.5	42.3	42.0	39.4	35.5	32.4	30.0
External debt service (percent of exports of goods and services)	5.4	14.8	13.4	17.7	14.7	11.0	10.3	9.5	9.0
Present value of PPG external debt									
Percent of GDP (risk threshold: 55%)	55.8	70.3	60.3	55.9	53.4	51.4	49.3	47.3	45.6
Percent of exports (risk threshold: 240%)	119.9	335.9	208.1	188.4	145.8	136.3	128.4	121.0	113.7
Present value of total debt									
Percent of GDP (benchmark: 70%)	92.4	105.4	104.7	97.9	95.0	90.5	84.7	79.7	75.5
Memorandum items:									
Nominal GDP (billions of Cabo Verde escudos)	213.9	180.7	196.8	213.8	229.8	247.7	266.6	285.5	304.2
Gross international reserves (€ millions, end of period)	666.1	582.4	591.3	491.0	544.3	577.6	623.3	677.5	710.3

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

1/ The Cabo Verdean exchange rate has been pegged to the Euro since 1999, at a rate of 110.265 CVE/€.

INTERNATIONAL MONETARY FUND

CABO VERDE

June 3, 2022

REQUEST FOR AN ARRANGEMENT UNDER THE EXTENDED CREDIT FACILITY

EXECUTIVE SUMMARY

Context. Cabo Verde's economy is facing significant economic challenges associated with the lingering effects of the pandemic, as well as rising food and fuel prices triggered by the war in Ukraine. Climate change is also creating new difficulties after a fourth consecutive drought year. The economy rebounded strongly in 2021 following the COVID-19 induced recession in 2020, due in part to the authorities' effective policy response, including one of the most successful vaccination programs in sub-Saharan Africa. However, the spillover effects of the Ukraine war are likely to weaken the economic recovery, worsen the fiscal and external positions, lead to higher inflation, and result in a substantial decline in international reserves. As a result, strong policy measures are needed to shore up international reserves, preserve debt sustainability, increase resilience to shocks, including climate change adaptation and mitigation, and make growth more inclusive.

Program Objectives and Modalities. The authorities have requested a new Extended Credit Facility (ECF) to help bolster reserves and support their economic reform program which is anchored on four key pillars: (i) fiscal consolidation to place public debt on a decisive downward path and preserve debt sustainability; (ii) public finance management (PFM) reforms to improve the efficiency of public spending and reduce fiscal risks from state-owned enterprises (SOEs); (iii) improvements to modernize the monetary policy framework and strengthen the financial system; and (iv) structural reforms to raise potential growth and increase resilience to external shocks. Staff support the authorities' request for a 36-month ECF arrangement with semi-annual reviews and access at 190 percent of quota (SDR45.03 million, about US$63.37 million). The authorities would use the ECF to shore up reserves and for budget support. Overall public debt remains at high risk of distress but there is adequate capacity to repay the Fund.

Program Policies. Strong fiscal adjustment is needed to boost policy credibility and set public debt on a decisive downward path. Protecting social spending to mitigate the impact of the pandemic and the war in Ukraine is essential. The program also supports the authorities' fiscal reform agenda, with an emphasis on domestic revenue mobilization, improvements in public finance management and efforts to contain possible fiscal risks from SOEs – especially Cabo Verde Airlines. The program also includes steps to contain risks from non-performing loans (NPLs) and the possible erosion in banks' asset quality at the expiration of the exceptional COVID-19 support measures.

Staff views. The Letter of Intent and Memorandum of Economic and Financial Policies signal strong program ownership with the set of policies to attain the objectives of the authorities' program. The main risk to the program is from uncertainty regarding the duration and impact of the Ukraine war, however, strong commitment and the track record of implementing reforms, program ownership, capacity development support and continued engagement by development partners will provide the impetus for success.

Approved By
Costas Christou (AFR) and Johannes Wiegand (SPR)

Discussions took place during three separate missions between January 31-April 26, 2022, virtually, in-person in Praia, and in-person in Washington DC. The staff team comprised Alex Segura-Ubiergo (head), Charles Amo-Yartey, Reginald Darius, Nombulelo Gumata, and Tomas Picca (all AFR). Ms. Carla Cruz and Mr. Ricardo Velloso (both OED) participated in most of the meetings. The mission met with Prime Minister Silva, Vice Prime Minister and Minister of Finance and Economic Development Correia, Central Bank Governor Santos, members of the Economic and Finance Committee of the National Assembly, other government and central bank officials, representatives of the private sector, and development partners. Mr. Lester Magno (AFR) assisted in the preparation of this report.

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CONTEXT

1. **The Cabo Verde economy was severely impacted by the COVID-19 pandemic**. The country entered the crisis with sound macroeconomic fundamentals, though high debt levels remained a serious vulnerability. In particular, economic growth averaged 5 percent during the pre-pandemic years (2018-19), international reserves were at comfortable levels, and the fiscal deficit and government debt were on a downward trajectory. When the crisis hit, the authorities took policy measures that helped mitigate the impact of the pandemic. Nevertheless, GDP contracted by close to 15 percent in 2020—the largest decline in the country's post-colonial history and one of the largest in sub-Saharan Africa. While the Omicron variant initially created new challenges, the health environment has improved substantially since January 2022.

2. **The nascent economic recovery has been disrupted by the external shock triggered by the war in Ukraine**. The shock is leading to higher fuel and food prices and lower demand for tourism. Cabo Verde has very limited policy space to respond to the shock, which is intensifying economic pressures and compounding the scarring from the pandemic shock.

3. **Over the medium term, further structural reforms are needed to put the country on a stronger and more inclusive growth trajectory**. Within this context, the 2019-2021 Policy Coordination Instrument (PCI) supported the government's ambitious reform program to rein in public debt and promote the development of the private sector. While the program produced some positive results (Annex I), the pandemic has eroded some of the gains and had a particularly negative impact on the authorities' efforts to pursue fiscal consolidation and SOE reforms. The Ukraine war is also likely to have an adverse impact on debt vulnerabilities and induce a significant fall in reserves, which in the absence of additional external financing, could impact the stability of the fixed exchange rate regime.

4. **Against this backdrop, the authorities have requested a new program to support the implementation of their strategic plan for sustainable development (PEDS)**. The objective of the authorities' three-year economic program is to reduce macroeconomic vulnerabilities and create conditions for inclusive growth through a significant reduction in the fiscal deficit and public debt, and improvement in the business environment.

5. **Cabo Verde's political environment is expected to remain stable, with some of the highest scores on governance in Sub-Saharan Africa**.[1] The pro-business *Movimento para Democracia* (MpD) won the April 2021 parliamentary elections while the opposition African Party for

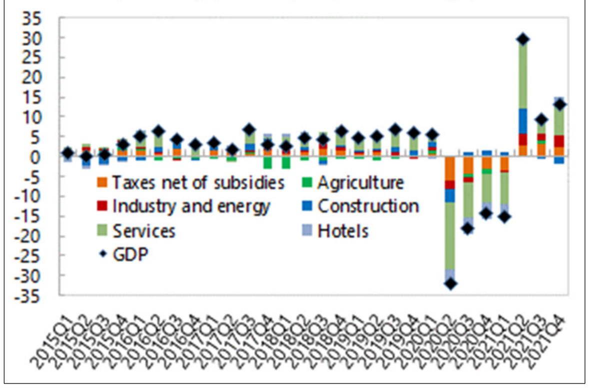
[1]Cabo Verde has a robust democracy with a tradition of peaceful political transitions for nearly four decades. The country continues to score at the top of Africa in measures of governance and transparency.

the Independence of Cabo Verde (PAICV), which ruled Cabo Verde when it was a one-party state, won the October 2021 presidential elections. José Maria Neves was sworn in as the new president of Cabo Verde on November 9, 2021.[2]

RECENT ECONOMIC DEVELOPMENTS

6. The economic rebound in 2021 was broad-based with economic growth reaching 7 percent (Text Figure 1). The rebound in economic activity was supported by the easing of international travel restrictions, strong private sector credit growth (5.8 percent y/y) and the successful vaccination program. Inflation picked up at 7.6 percent in March 2022 due to higher food, clothing, and transportation costs reflecting the impact of the Ukraine war. The authorities have finalized the rebasing of the national accounts statistics to 2015 from 2007. The published data indicates that the rebased nominal GDP is about 10 percent higher than previous estimates, reflecting a more acurate measure of the services sector (Annex II).

Text Figure 1. Cabo Verde: Contributions to Growth
(Quarterly, year-on-year percent change)

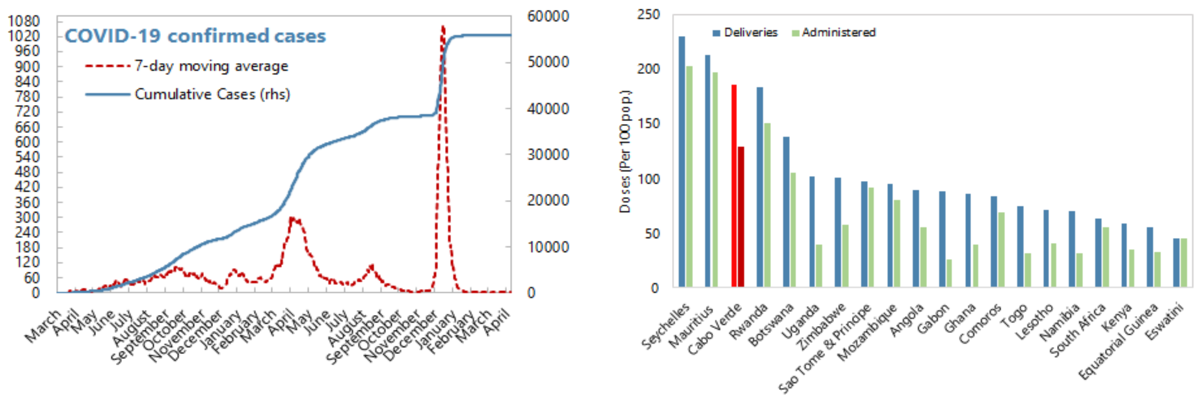


7. Cabo Verde has one of the fastest COVID-19 vaccine rollouts in sub-Saharan Africa. More than 90 percent of the adult population have received at least one vaccine dose with vaccination rates close to 100 percent in some of the tourism islands (Text Figure 2). The successful COVID-19 vaccination campaign limited the impact of the Omicron variant. The January 2022 surge in COVID-19 cases was short-lived and did not lead to a tightening of restrictions or delay the planned easing of some economic support measures. The average number of daily COVID-19 cases is currently in the single digits compared with about 1,000 cases in December 2021; while total COVID-19 infections stood at 55,886 at end-April 2022, and hospitalizations remain low.

8. External sector developments in 2021 were favorable. The current account is estimated to have narrowed from 15 percent of GDP in 2020 to 11.3 percent in 2021 on account of a strong recovery in goods exports and higher tourism receipts. Imports of goods and services increased by 10 percent during the same period as the recovery gained traction and supported domestic demand. Gross international reserves increased from €582.4 million in 2020 to €591.3 million in 2021 (about 6.3 months of prospective imports) supported by the SDR allocation (SDR 22.72 million; about 1.5 percent of GDP), and external loan disbursements.

[2]Under Cabo Verde's semi-parliamentary political system, the prime minister is head of the government, and the president has a more ceremonial role as head of state with veto powers.

Text Figure 2. Cabo Verde: Covid-19 Cumulative Daily Cases & SSA Vaccination Rates



Sources: OWID; Johns Hopkins CSSE; and IMF staff calculations.

9. **The external position in 2021 was substantially stronger than the level implied by fundamentals and desirable policy settings (Annex IV)**. The high and negative net international investment position is a source of vulnerability, but risks are partly contained by the structure of Cabo Verde's external liabilities, largely composed of FDI and long-term debt. The reserve adequacy model based on the IMF LIC/MIC framework suggests reserves of about 3.7 months of imports. However, given the small size of Cabo Verde's economy, the undiversified economic structure and high vulnerability to external shocks, staff recommends reserves in the range of 5 to 5½ months of imports. Cabo Verde's business environment has improved in recent years, but continued structural reforms remain critical to enhance competitiveness.

10. **The financial system has remained resilient**. Data for end 2021 suggest that the financial system is highly liquid, profitable, and well capitalized. The banking sector entered the pandemic with strong capital buffers and improving profitability that helped contain risks. Regulatory capital to risk weighted assets (CAR) was 21.1 percent at end-December 2021, well-above the regulatory minimum of 12 percent, while the return on assets was relatively low at 1.5 percent. Non-performing loans (NPLs) declined from 9.5 percent at end 2020 to 7.2 percent of total loans at end December 2021 reflecting the moratorium on loan repayments and write-off of legacy loans.[3]

11. **Fiscal performance improved in 2021**. The overall deficit declined to 7.3 percent of GDP and was financed through external disbursements (about 70 percent) and domestic financing (about 30 percent). (Text Table 1). Lower public investment and current expenditure restraint helped achieve the authorities' budget objectives. Public debt stood at 143 percent of GDP at end-2021.

[3]The Banco de Cabo Verde introduced a moratorium on loan repayment as part of the measures to mitigate the economic impact of the COVID-19 pandemic in April 2020. The moratorium on loan repayment is expected to expire at the end of June 2022.

Text Table 1. Cabo Verde: Quarterly Fiscal Performance[1]
(Millions of Cabo Verde Escudos)

	2020	2021				
	Q4	Q1	Q2	Q3	Q4	Q4'21 vs Q4'20
	Act.	Act.	Act.	Act.	Proj.	(Percent Change)
Revenue	44,626	8,328	17,885	28,681	44,530	-0.2
Tax revenues	32,900	7,017	14,957	23,680	33,542	2.0
Taxes on income and profit	9,990	1,769	4,404	6,678	9,149	-8.4
Taxes on goods and services	15,632	3,415	6,867	11,007	15,824	1.2
Taxes on international trade	6,593	1,675	3,374	5,509	7,894	19.7
Grants	5,866	158	690	1,146	3,985	-32.1
Other revenues	5,861	1,153	2,239	3,855	7,002	19.5
Expenditure	61,052	11,964	25,536	41,799	58,898	-3.5
Expense	55,119	11,545	25,034	38,660	54,544	-1.0
Net acquisition of nonfinancial assets	5,933	419	502	3,139	4,354	-26.6
Primary balance	-11,598	-2,661	-5,595	-10,030	-10,112	-12.8
Overall balance	-16,426	-3,636	-7,651	-13,118	-14,368	-12.5
Net other liabilities	-2,104	-514	-858	1,919	1,691	-180.4
Financing needs	18,530	4,150	8,509	11,199	12,677	-31.6

Sources: Cabo Verdean authorities and IMF staff projections.
1/ Includes budgetary central government (BCG) and extra budgetary central government (ECG), but excludes social security funds.

12. The COVID-19 pandemic has made critical SOE reforms more challenging. In particular, the authorities had to postpone the privatization program to 2022, after renationalizing the airline company (CVA) citing misuse of pandemic support. Preliminary estimates suggest that CVA will need about €30 million (1.7 percent of GDP) during 2022-23 to support its operations pending its re-privatization. The sharp increase in international oil prices over the last six months, coupled with sticky electricity tariffs, is also having a negative impact on the financial performance of the electricity company (ELECTRA), which had losses of CVE 1.5 billion (0.8 percent of GDP) in 2021. The company is likely to suffer an additional CVE 1 billion (about 0.5 percent of GDP) of losses in 2022 due to the authorities' decision to limit tariff adjustments in a context of rising food and fuel prices.

13. The authorities are implementing the governance commitments on crisis-related spending made in the context of the RCF and have also developed a framework for the use of the recent SDR allocation. In this regard, they continue to monitor COVID-related expenditures, including through the publication of key spending data on the website of the Ministry of Finance. In addition, the 2020 audited financial accounts, including COVID-related expenditures, have been submitted to parliament (MEFP, ¶18). The transfer of the SDR resources from Banco de Cabo Verde (BCV) to the government was completed in 2021 and the amount has already been included in public debt. A memorandum of Understanding (MoU) detailing the framework for the use of SDRs was signed between the Ministry of Finance and BCV (MEFP, ¶18).

MACROECONOMIC OUTLOOK AND RISKS

14. **The near-term outlook has deteriorated due to the war in Ukraine**. Real GDP growth has been revised downwards from 6 percent to 4 percent in 2022 as the war in Ukraine is expected to be a drag on tourism. Higher commodity and fuel prices and the weaker prospects for the recovery in the tourism sector are projected to result in a significant widening of the current account deficit (to about 14.1 percent of GDP in 2022) and lower international reserves. Near-term inflation is likely to remain elevated reflecting international oil and food price developments.

Text Table 2. Cabo Verde: Medium-Term Macroeconomic Indicators[2]

(Percent of GDP, unless otherwise indicated)

	Ukraine War Assumptions							
	2020	2021	2022	2023	2024	2025	2026	2027
Real GDP growth (percent)	-14.8	7.0	4.0	4.8	5.7	5.5	5.0	4.5
Primary balance	-6.4	-5.1	-3.6	-2.6	-1.3	0.0	1.0	1.0
Fiscal balance	-9.1	-7.3	-6.3	-5.6	-4.0	-2.1	-0.9	-0.8
Total financing needs	14.0	6.4	7.0	6.2	4.2	2.3	1.1	1.2
Current account balance	-15.0	-11.3	-14.1	-6.2	-5.9	-4.7	-4.6	-4.2
Gross reserves (millions of euros) 1/	582.4	591.3	491.0	544.3	577.6	623.3	677.5	710.3
Gross reserves (months of prospective imports)	7.1	6.3	5.0	5.1	5.1	5.1	5.2	5.2
Public debt	142.6	143.0	145.9	139.7	132.5	124.0	116.2	109.6
Nominal GDP (billions of Cabo Verde escudos)	180.7	196.8	213.8	229.8	247.7	266.6	285.5	304.2
	Pre-war Assumptions							
Real GDP growth (percent)	-14.8	6.9	6.0	6.1	5.7	5.5	5.0	4.5
Primary balance	-6.2	-5.8	-3.0	-2.0	-1.0	0.0	1.0	1.3
Fiscal balance	-9.1	-8.8	-7.2	-5.2	-4.1	-2.6	-1.2	-0.9
Total financing needs	9.4	8.3	9.5	5.6	4.3	2.8	1.4	1.2
Current account balance	-15.9	-12.5	-9.9	-6.8	-5.0	-4.5	-4.2	-4.0
Gross reserves (millions of euros)	582.4	591.3	606.7	603.9	621.8	636.9	661.4	688.4
Gross reserves (months of prospective imports)	7.1	6.3	6.7	6.2	6.0	5.7	5.6	5.4
Public debt 3/	156.3	155.2	157.0	148.2	140.7	131.9	123.2	115.8
Nominal GDP (billions of Cabo Verde escudos) 4/	164.9	181.4	196.3	212.2	228.7	246.2	263.7	281.2

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

1/Includes prospective ECF disbursments

2/The medium-term assumptions include the effect of the Fund disbursements that would allow the authorities to maintain a level of reserves in the range of 5 to 5½ months of imports.

3/Ratio calculated with non-rebased GDP series

4/ Non-rebased nominal GDP

15. **Medium-term prospects remain broadly positive provided the authorities implement their reform program (Text Table 2)**. The planned fiscal consolidation, a successful restructuring of the major SOEs, and structural reforms are expected to lead to faster growth of credit to the private sector, boost investor confidence, accelerate medium-term growth, and place public debt on a sustained downward path. Real GDP growth is anticipated to remain robust at about 5½ percent reflecting the continued recovery of the tourism sector toward pre-pandemic levels, including through an increase in hotel room capacity, and the implementation of reforms under the

authorities' strategic plan for sustainable development (PEDS). The current account deficit is projected to narrow to about 4 percent of GDP in the medium term supported by fiscal consolidation, strong tourism performance, and higher remittances reflecting labor market improvements in advanced economies. This will help international reserves recover and stabilize at slightly above 5 months of prospective imports. The primary fiscal balance would improve by about 1 percentage point of GDP per year over the medium-term reflecting revenue mobilization and expenditure restraint. This would contribute to a substantial decline in the stock of public debt from 143 percent of GDP in 2021 to about 110 percent of GDP by 2027. Over the long term, GDP growth is projected at about 4½ percent, broadly in line with potential growth.

16. **However, the medium-term outlook is also subject to substantial risks**. The main downside risk relates to the evolution of the pandemic and its impact on the external sector through a possible decline in tourism (Annex III), as well as significant increases in fuel and food prices and tighter financial conditions owing to the Ukraine war. Other external risks include the de-anchoring of inflation expectations in advanced economies and vulnerability to natural disasters (including those associated from climate change). Domestic risks could stem from insufficient progress in fiscal consolidation and SOE reforms, and possible delays in implementing structural reforms to increase productivity and diversify the economy. On the upside, faster than expected global containment of the pandemic could support a faster recovery of tourism and strengthen the pace of the economic recovery.

17. **The authorities agreed with staff's assessment of Cabo Verde's medium-term outlook and risks (MEFP, ¶12)**. They stressed uncertainties regarding the impact and duration of the Ukraine war as a significant risk to the medium-term outlook. Within this context, the BCV viewed the projected gross international reserves cover as an important buffer. On the medium term, they stressed that the economy's growth potential is high, and idle resources remain as the economy returns to pre-pandemic level of output. In that regard, they saw significant upside risk to the medium-term growth projections supported by targeted growth enhancing structural reforms.

THE EXTENDED CREDIT FACILITY

A. Program Objectives and Policies

18. **The objectives of the program are aligned with the government's medium-term economic development plan (PEDS) and include**:

- Strengthening public finances to preserve public debt sustainability and expand social safety nets.
- Reduce fiscal risks from public enterprises and improving their financial management and transparency.
- Modernizing the monetary policy framework and improving the resilience of the financial system.

- Raising growth potential and building resilience to shocks through structural reforms and economic diversification.

19. Strong ownership, continued support from development partners, and timely implementation of reforms is critical. Cabo Verde has a robust track record of reform implementation, and an impressive tradition of good governance and transparency. The program has a carefully selected set of reforms necessary to achieve the overall objectives of the three-year program. The program will support the authorities' reform objectives over three years and will bolster policy credibility to help preserve Cabo Verde's strong relations with the donor community and facilitate continued strong financial support from other donors. The program will seek complementarity with other development partner programs whenever possible, and the implementation of reforms will be supported by IMF technical assistance. Tables 9 and 10 provide an overview of the conditionality under the program.

B. Strengthening Public Finances to Preserve Public Debt Sustainability

20. Fiscal consolidation to reduce public debt is an important aspect of the government's economic program. The fiscal strategy is anchored by the objective of reducing the debt-to-GDP ratio from the current 143 percent to below 110 percent by 2027. This is based on a multiyear fiscal consolidation effort to improve the primary fiscal balance from a deficit of 5.1 percent of GDP in 2021 to a surplus of 1 percent of GDP by 2026 (MEFP, ¶14). The adjustment is significant, and initially revenue driven, with limited expenditure reduction in 2022 due to the need to support the economy to mitigate the impact of the Ukraine war.[4] This adjustment would be associated with a reduction in the PV of external debt-to-GDP ratio from 60.3 percent in 2021 to 45.9 percent in 2027.

21. The program targets a 1.5 percent of GDP improvement in the primary balance for 2022 to be achieved mainly through higher revenues (Text Table 3; Table 3a and 3b). The primary deficit would decline to 3.6 percent of GDP—about 0.4 percent of GDP lower than in the authorities' original budget. This reflects the need to mitigate the economic impact of the war in Ukraine and the need for additional spending to support vulnerable groups (MEFP¶15).

- Revenue mobilization measures are expected to yield about 1 percent of GDP (Text table 3) (MEFP ¶17). These measures include the imposition of a 5 percent import duty on previously exempted imports,[5] and an increase in the excise tax on tobacco products (Text Table 3). These tax measures will be supported by efforts to reduce tax arrears on VAT, personal, and corporate income taxes. The completion of the concession for airport management is expected to generate one off revenues of about 1.8 percent of GDP and the airport security tax is expected to yield 0.3 percent of GDP.

[4]The authorities intend to unwind COVID-19 related spending measures (1.8 percent of GDP in 2021; 1.6 percent of GDP in 2022). Factoring out these and the initial large correction in 2022, the adjustment would be equivalent to about 1 percent of GDP per year between 2023-26.

[5]Including business furniture and other equipment.

- Expenditure restraint will be achieved through streamlining of non-essential public investment projects, and through prudent policies to contain the growth of the wage bill, transfers, and subsidies (MEFP, ¶19). Fiscal consolidation is designed to protect social spending, with an additional 0.3 percent of GDP allocated to targeted social safety net programs, in part to increase the number of vulnerable households that would receive cash transfers to help cushion the economic impact of the Ukraine war (MEFP, ¶20).

- These measures will help reduce the overall deficit from 7.3 percent of GDP in 2021 to 6.3 percent in 2022, and the primary balance from 5.1 percent to 3.6 percent.

- The fiscal position could be negatively affected by the war in Ukraine, including through lower growth, weaker revenue collections and the impact of higher fuel prices on the operations of Cabo Verde Airlines. Should these risks materialize, further expenditure restraint (especially reducing non-priority public investment projects or slowing down their rate of execution) may be needed to maintain a prudent fiscal position in line with program objectives.

Text Table 3. Cabo Verde: Primary Balance Improvements, 2022
(Staff Projection, Percent of GDP)

Primary balance 2021	**-5.1**
Adjustments, including one off revenue items	0.0
Change in tax revenues	**0.8**
New tax policy measures in 2022	0.7
Electronic invoicing	0.2
Turnover tax	0.1
Implementation of 5 percent import duties on previously exempted goods	0.2
Increase in tobacco tax	0.2
Reduction in VAT on electricity	-0.2
Other income taxes	0.1
Tax administration measures	0.4
VAT arrears collection	0.2
Personal income tax arrears collection	0.1
Corporate income tax arrears collection	0.1
Change in other revenues	**2.1**
Completion of concession for airport management	1.8
Airport security tax	0.3
Change in grants	**-0.2**
Change in primary expenditures	**-1.2**
Expense	-0.1
Net acquisition of non-financial assets	-1.1
Primary balance in 2022	**-3.6**

Sources: Cabo Verdean authorities and IMF staff estimates.

22. **Medium-term fiscal consolidation will be supported by the implementation of additional fiscal policy measures**. Ongoing tax administration reforms, including the implementation of electronic invoicing as well as other reforms to improve compliance will support revenue mobilization and are expected to yield an additional 2 percent of GDP over the medium term (MEFP ¶18). The implementation of the ECOWAS common external tariff—delayed due to the COVID-19 outbreak—is projected to yield about 1 percent of GDP over the medium term. The government will submit to parliament the budget for 2023 that will be in line with commitments under the program **(Structural Benchmark (SB), 2nd review)**.

Text Table 4. Cabo Verde External Borrowing Program, 2022

PPG external debt contracted or guaranteed	Volume of new debt, US million	Present value of new debt, US million 1/
Sources of debt financing	149.9	94.3
Concessional debt, of which 2/	149.9	94.3
Multilateral debt	107.1	68.5
Bilateral debt	42.8	25.8
Non-concessional debt, of which	0.0	0.0
Semi-concessional debt 3/		
Commercial terms 4/		
Uses of debt financing	149.9	94.3
Infrastructure	98.5	63.1
Budget financing	51.4	31.2

Sources: Cabo Verdean Authorities; IMF Staff calculations

1/ Contracting and guaranteeing of new debt. The present value of debt is calculated using the terms of individual loans and applying the 5 percent program discount rate

2/ Debt with a grant element that exceeds a minimum threshold. This minimum is typically 35 percent, but could be established at a higher level. Some of the loans are packaged with grants, such that the overall financing package meets the 35 percent concessionality threshold

3/ Debt with a positive grant element which does not meet the minimum grant element.

4/ Debt without a positive grant element. For commercial debt, the present value would be defined as the nominal/face value.

23. **The program supports a well targeted fiscal structural reform agenda—with revenue mobilization, SOE and public financial management reforms (MEFP ¶22-26)**. Key measures include putting in place an electronic invoicing system for the VAT that will cover at least 50 percent of taxpayers by end-2022 **(SB, 2nd review)**. The fiscal program also focuses on reducing fiscal risks stemming from public enterprises (Annex V), including through the preparation of quarterly fiscal risk assessment reports (**SB, 1st review)**; as well as quarterly monitoring reports on the SOEs' budget execution **(SB, 2nd review),** and improving the consolidated annual SOEs reports **(SB, 3rd review)**. The program will also broaden the coverage and transparency of the government accounts including the compilation and publication of the historical series of government financial statistics for the general government **(SB, 3rd review)**; and the publication of annual budget execution reports for the general government **(SB, 3rd review)**. In addition, the authorities will finalize a business plan for Cabo Verde Airlines to minimize losses and eventually return the company to profitability ahead of its re-privatization.

24. **Prudent borrowing policies will focus on moderate external borrowing on concessional terms and containment of domestic borrowing to prevent possible crowding out effects and preserve debt sustainability (Text table 4)**. In that regard the program includes a zero ceiling on non-concessional borrowing as a performance criterion given the high risk of overall debt distress. The debt sustainability analysis shows that the risk of overall debt distress is high due to high external debt levels (Annex VII and DSA). However, overall public debt is assessed as

sustainable given that debt service requirements remain manageable thanks to: (i) the high degree of concessionality of external debt with an average interest rate below 1 percent, (ii) a debt structure based largely on fixed rates and hence providing protection from the ongoing tightening cycles, and (iii) the fixed exchange rate and still adequate reserve levels that neutralize the negative impact of exchange rate trends on debt dynamics that is currently being observed in other countries with flexible rates. Within this context, the present value (PV) of public and publicly guaranteed (PPG) external debt-to-GDP ratio breaches its threshold in 2022 under the baseline (a shorter duration breach than previously expected due to the recent GDP rebasing), and more protractedly under stress test scenarios. Preserving debt sustainability is predicated on the authorities' commitment to implementing the reforms agenda.

C. Monetary Policy and Financial Stability

25. Monetary policy will continue to prioritize the need to safeguard the peg and strengthen the policy framework (MEFP ¶33). In the near term, the monetary policy stance seems appropriate, carefully balancing the need to support the fledging economic recovery with the importance of protecting the peg. Over the medium term, the BCV should target reserves in the range of 5-5½ months of imports to support the peg given the country's small size and vulnerability to exogenous shocks.

26. The BCV is gradually unwinding COVID-19 related support. The accommodative monetary and financial measures implemented in 2020 helped to support credit and provided liquidity to households and firms (MEFP ¶10). However, with the end of pandemic-related restrictions, the resumption of economic activity, and considering the high levels of liquidity in the banking system, the authorities have appropriately started unwinding some of these measures. The central bank also confirmed that it will closely monitor reserves and inflation developments and will stand ready to adjust policy settings as required.

27. A preliminary assessment by the central bank suggests that the banking sector is well placed to withstand the effects of the projected increase in non-performing loans (MEFP ¶35). The BCV agreed to carry out a comprehensive study of loan losses and provisions at the expiration of the credit moratorium (end June 2022) ***(SB, 2nd review)***, encourage and facilitate prudent restructuring of loans, and proactively provide guidance on the prudential treatment of moratoria and NPL management strategies. In addition, the BCV proposed developing a common framework[6] for the resolution of crisis-related NPLs **(SB, 2nd review)**. The central bank will also guide the development of detailed reporting templates for the restructured and rescheduled loans and for monitoring the impact of COVID measures on the asset quality of banks **(MEFP ¶35)**.

28. Steps will also be taken to enhance the effectiveness of the AML/CFT regime (**MEFP ¶35)**. This will be implemented based on the Inter-Governmental Action Group against Money Laundering (GIABA)'s recommendations of the 2019 Mutual Evaluation Report (including the

[6]The common framework is being developed jointly by the BCV and the World Bank.

establishment in 2020 of a national AML/CFT committee and strengthening of risk-based supervision, including for designated non-financial businesses and professions). Cabo Verde's recent exit from the EU list of non-cooperative jurisdictions for tax purposes has helped preserve correspondent banking relationship (CBR).

29. Structural reforms will focus on further strengthening the monetary policy transmission mechanism and enhancing analytical capacity to track developments in the economy (MEFP ¶34-38). To support the development of the money market, a preannounced schedule for TIM (Títulos de Intervenção Monetária—Monetary Intervention Securities (MIS)) and TRM (Títulos de Regularização Monetária—Monetary Regularization Securities (MTS)) auctions will be instituted **(SB, 1st review)**. The auction schedule and related information will be pre-announced on the BCV website. Other reform areas include strengthening the payment systems, introduction of composite indicators of economic activity **(SB, 2nd review)** and strengthening near-term forecasting, implementation of central bank digital currency, and developing a framework for the provision of emergency liquidity assistance.

30. An updated safeguards assessment of the BCV is substantially complete. Progress has been made in enhancing external audit and financial reporting at the BCV since the 2008 safeguards assessment. However, legal amendments are needed to strengthen the BCV's decision-making structure, autonomy, and accountability and transparency **(SB, 2nd review**). The lack of an independent oversight body has impacted the internal audit function's independence and effectiveness. To further enhance the quality of the financial statements the BCV will seek to adopt International Financial Reporting Standards by FY 2023.

D. Structural Reforms: Supporting Private Sector-Led Growth

31. Structural reforms will aim at improving the business environment, addressing labor market inefficiencies, and increasing access to finance (MEFP ¶39-41). The authorities are developing a new five-year development strategy based on the recently completed long-term development plan (*Cabo Verde Ambition 2030*). Key priority areas include (i) completing SOE reforms, including through privatization and improving the efficiency of public enterprises; (ii) facilitating access to finance, particularly for small and medium-sized enterprises; and (iii) improving the business environment. Other reforms include climate change adaptation and mitigation measures, including progress towards achieving the 50 percent renewable energy target by 2030. In addition, the development of technology parks will also support efforts to enhance digitalization –another key priority for the government.

32. The program will also emphasize support for vulnerable groups and will seek to strengthen social safety nets. In this regard, additional resources have been allocated for the expansion of the social safety net to help mitigate the impact of higher prices on the most vulnerable groups (MEFP ¶42-43). Staff will also work closely with the World Bank and the African Development Bank (AfDB) to advise the authorities on further reforms to enhance social protection.

FINANCING AND PROGRAM MODALITIES

33. **The Extended Credit Facility (ECF) will help address protracted BOP needs stemming from the impact of the pandemic and, more recently, the war in Ukraine**. The effect of these shocks on the BOP are projected to persist with tourism expected to return to the pre-pandemic level at the end of the medium term, generating persistent downward pressure on reserves. The ECF arrangement provides financing to bolster reserves, help close the fiscal financing gap and support reforms under the authorities' development strategy. Reform implementation will also be supported by well-targeted capacity development from the IMF (Annex VI) and other donors.

Text Table 5. Cabo Verde: Impact of the Ukraine War on the Balance of Payments
(Millions of Euros, unless otherwise indicated)

	2022			
			Difference	
	Pre-war	War		percent of GDP
Current Account	-177	-273	-96	-4.9
Trade Balance	-615	-716	-101	-5.2
Services	192	169	-23	-1.2
Of which tourism	237	226	-11	-0.6
Primary Income	-74	-48	26	1.4
Secondary Income	320	323	3	0.1
Capital and Financial account	-192	-172	20	1.0
Overall balance	15	-100	-115	-5.9
Change in reserves (increase:-)	-15	100	115	5.9
of which IMF/ECF expected financing		28		1.5
Residual financing gap		0		0

Sources: Bank of Cabo Verde; IMF staff projections

34. **Funding under the ECF will help close the financing gap and support a financing mix with greater reliance on concessional external financing (Text table 6**). In the absence of the Fund program, high levels of domestic financing could lead to crowding out of the private sector, increase debt servicing costs to levels that could compromise medium-term sustainability, and leave the economy with insufficient reserve buffers to manage BOP challenges.[7] In this regard, the remaining external financing gap for the 2022 budget will be filled mostly with concessional loans from multilateral institutions including the World Bank, AfDB, and other bilateral partners and a drawdown of the recent SDR allocation (about 1 percent of GDP) (MEFP¶8).

35. **Staff considers access of SDR 45.03 million (190 percent of quota; around USD 63.37 million) (Table 10) under the 36-month ECF to be appropriate**. The program will provide a policy anchor to the authorities' fiscal reform plan, including achieving a primary surplus that helps place debt on a sustained downward path, while addressing Cabo Verde's financing needs associated with the significant increase in the price of imports. The program will also support the gradual economic recovery from the COVID-19 and Ukraine war shock. Access is proposed to be frontloaded (some 95 percent of access in 2022, followed by equal purchases) to help buffer against the headwinds associated with the war in Ukraine, which are expected to be of greater magnitude during the first year of the program.

[7]The fiscal rule limiting domestic financing to 3 percent of GDP has been suspended by Parliament for 2022.

Text Table 6. Cabo Verde: Sources of Financing for 2022-25

	2022		2023		2024		2025	
	Millions of Escudos	Percent of GDP	Millions of Escudos	Percent of GDP	Millions of Escudos	Percent of GDP	Millions of Escudos	Percent of GDP
Total financing needs	15,010	7.0	14,233	6.2	10,372	4.2	6,242	2.3
Financing sources	15,010	7.0	14,233	6.2	10,372	4.2	6,242	2.3
Domestic Financing (Net)--Issuance of treasury securities 1/	7,501	3.5	6,911	3.0	3,204	1.3	1,675	0.6
External financing (Net)	7,509	3.5	7,322	3.2	7,169	2.9	4,567	1.7
Disbursements	16,672	7.8	17,072	7.4	15,570	6.3	13,060	4.9
Of which budget support	8,130	3.8	6,466	2.8	6,743	2.7	6,232	2.3
IMF	3,105	1.5	1,238	0.5	1,233	0.5	615	0.2
World Bank	2,820	1.3	3,023	1.3	3,305	1.3	3,411	1.3
African Development Bank	2,205	1.0	2,205	1.0	2,205	0.9	2,205	0.8
Program and project loans	6,203	2.9	8,854	3.9	8,284	3.3	6,251	2.3
JICA	1,051	0.5	1,998	0.9	2,124	0.9	2,419	0.9
OFID	821	0.4	1,899	0.8				
World Bank	2,721	1.3	2,806	1.2	3,807	1.5	3,248	1.2
BADEA	1,301	0.6	1,161	0.5	97	0.0	470	0.2
SDR	1,948	0.9						
Other	309	0.1	990	0.4	2,256	0.9	114	0.0
Onlending loans	2,339	1.1	1,752	0.8	543	0.2	635	0.2
African Development Bank	964	0.5						
Amortization	9,163	4.3	9,750	4.2	8,401	3.4	8,500	3.2

Sources: Cabo Verdean authorities and IMF staff projections.

1/ In 2023 net domestic financing includes SDR's converted to domestic deposits amounting about 0.6 percent of GDP.

36. **The 36-month ECF would be used as budget support and cover 2022 through 2025 as the fiscal and balance of payments shocks are of a similar magnitude**. A 36-month arrangement is appropriate given the period required to lower debt to more moderate levels and significant scarring from the pandemic and Ukraine war. The financing from the Fund will help keep reserves within the targeted range of 5 to 5½ months of imports in 2022 and over the medium term. This level of reserves would provide sufficient support to the peg in an environment of heightened global risk and uncertainty and enable implementation of a more desirable fiscal adjustment path that would prevent the need for sharper expenditure cuts.

37. **Program conditionality, and monitoring**.

- ***Performance criteria (PC) (Table 8)***. Program performance will be monitored by the following PCs:[8] (i) floor on tax revenues; (ii) floor on primary balance; (iii) ceiling on net other liabilities (on lending and capitalization); (iv) non-accumulation of domestic and external arrears (continuous); (v) 3 percent of GDP annual ceiling on net domestic financing; (vi) ceiling on the PV of new concessional public and publicly guaranteed external debt; (vii) zero ceiling on contracting or guaranteeing non-concessional external debt with maturity of more than one year (continuous); and (viii) floor on gross international reserves. The program will also include a floor on social spending as an indicative target. The standard continuous targets will also be part of the PCs.

- ***Reviews (Table 10)***. The program will be monitored through semi-annual reviews. Reviews will include PCs for end-June and end-December, as well as indicative targets for end-March and end-September.

- ***Structural benchmarks (SBs)***. The SBs under the program are calibrated and phased in line with the authorities' plans and implementation capacity, in collaboration with other development partners.

[8] PCs are cumulative from the beginning of the year.

- ***Financing assurances***. The program is fully financed for the first 12 months, with good prospects of full financing for the remainder of the arrangement. In addition to Fund support, financing in the first year of the ECF will be provided through budget support from development partners and multinational development institutions, including the World Bank and the African Development Bank.

38. Cabo Verde's capacity to repay the Fund is assessed as adequate and enhanced safeguard rules are applied given the proposed access levels (Table 6, Annex VII). By 2025, Cabo Verde's Fund credit outstanding will be at 280 percent of quota (above the top quartile of past UCT-quality arrangements for LICs). Credit outstanding during the program would peak at about 3.6 percent of GDP, 10 percent of exports, 13.8 percent of gross international reserves and 14.5 percent of revenue (excluding grants). At the same time, annual repayments to the Fund would peak at 0.6 percent of exports, 0.9 percent of reserves, and almost 6.1 percent of PPG external debt service. Risks are mitigated by the authorities' strong track record of servicing their debt obligations to the Fund, and policy measures envisaged in the program, including fiscal consolidation. The return of tourists to the country is also likely to generate significant repayment capacity through increased export receipts.

39. Risks to the program are assessed as moderate, conditional on the successful implementation of the reform agenda and a significant reduction of the debt stock going forward. The worsened global outlook and ongoing effects of the spillovers from the Ukraine war on Cabo Verde increase risks to the program. Also, the high risk of overall debt distress remains a concern. Mitigating factors to the worsened outlook are the authorities' strong track record under the recently completed PCI, and strong program ownership. Nonetheless, risks to the medium-term outlook will be closely monitored as they could impact program performance. However, program reviews and continued dialogue with the authorities will help mitigate these risks.

STAFF APPRAISAL

40. Cabo Verde's economy is facing significant economic challenges associated with the impacts of the pandemic, as well as the spillover effects of the war in Ukraine. Climate change is also creating additional difficulties after a fourth consecutive drought year. As a result, growth is expected to weaken, inflation will rise substantially, and fiscal and external pressures will intensify. Strong commitment to implement a balanced mix of corrective policies that reduces the risk of overall debt distress, protects vulnerable groups, and supports growth is needed.

41. The government is committed to implementing reforms to reduce vulnerabilities, increase growth and support the most vulnerable. The authorities are requesting support under an Extended Credit Facility (ECF) to help address the BOP gap and fiscal financing needs stemming from the impact of the pandemic and, more recently, the war in Ukraine. The program would also help anchor the authorities' medium term economic strategy and support the implementation of reforms to achieve sustained growth and poverty reduction.

42. Fiscal consolidation is needed to contain debt vulnerabilities, but it needs to be implemented gradually and taking into account the need to safeguard growth and protect vulnerable groups. In this regard, the primary fiscal deficit would gradually decline during the program and help place public debt on a sustained downward path. The program will also support the fiscal reform agenda, which includes a focus on domestic revenue mobilization and efforts to advance SOE reforms to contain fiscal risks.

43. A steady path of debt reduction is important to increase economic resilience and rebuild buffers. External public debt is at a moderate rate of debt distress, but overall public debt is at high risk of distress due to high levels of domestic borrowing in recent years. The authorities' plan to bring the primary balance deficit of 5.1 percent of GDP in 2021 to a surplus of about 1 percent of GDP over the medium term will help reduce the risk of overall debt distress.

44. Reinforcing the social safety net will be essential to achieve the authorities' objective of making growth more inclusive and equitable. The higher allocation of resources for social spending will help mitigate the impact of rising prices on the most vulnerable. In addition, further improvements in the targeting and coverage of existing programs will also increase the efficiency of public spending and support the authorities' plans to eradicate extreme poverty. These efforts should be combined with a vigorous implementation of the graduation strategy to enhance skills and other labor market policies seeking to generate jobs so that citizens are increasingly less dependent on social support programs.

45. Monetary policy should continue to focus on safeguarding the peg and strengthening the monetary policy framework. This will be needed to maintain reserves in the range of 5 to 5½ months of imports and make progress in enhancing analytical capacity of the central bank. The BCV should continue with the gradual unwinding of the COVID-related moratorium and liquidity support measures given the continued excess liquidity in the banking system. The BCV should also work toward strengthening the AML/CFT component of its prudential supervision.

46. The banking system appears resilient but continuous vigilance will be required to ensure that financial risks are contained. In this regard, the BCV should continue to monitor risks in the banking sector, especially given the fact that the end of the credit moratorium in June 2022, is likely to result in a spike in NPLs and an erosion in banks' asset quality. The BCV's intention to carry out a comprehensive study of loan losses and provisions at the expiration of the credit moratorium, facilitate prudent restructuring of loans, and provide guidance on the prudential treatment of moratoria and NPL management strategies would help contain these risks.

47. Raising Cabo Verde's medium term growth potential will require steadfast implementation of the authorities' medium term development plan. Completing SOE reforms, including through privatization and improving the efficiency of public enterprises, will support efforts to improve long-term productivity. Steps in climate change adaptation including efforts to reach the goal of 50 percent renewable energy supply by 2030 would also increase the resilience of the economy and help increase growth potential.

48. **Staff support the authorities' request for a 36-month arrangement under the ECF with access equivalent to 190 percent of quota (SDR 45.03 million)**. This support is based on the balance of payments and fiscal financing needs, the country's positive track record of reform implementation, as well as the authorities' policy credibility, and home-grown ownership of their reform program.

Text Table 7. Cabo Verde: External Financing Gap 2020-25

(Millions of Euros, unless otherwise specified)

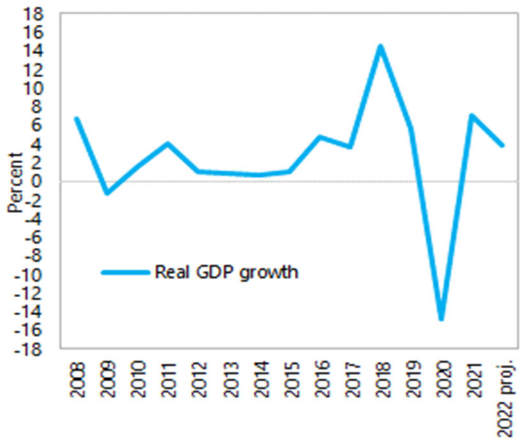
	2020	2021	2022	2023	2024	2025
Current account balance	-246.1	-201.2	-272.6	-128.2	-132.5	-113.4
Balance of goods and services	-512.9	-464.0	-547.8	-425.6	-426.6	-426.9
Exports of goods	113.3	166.7	178.0	282.3	313.5	352.0
Imports of goods	692.2	775.7	894.5	947.8	997.3	1041.8
Exports of services	258.2	350.9	397.6	480.8	533.4	576.6
Imports of services	192.3	206.0	228.8	241.0	276.2	313.6
Balance on primary income	-35.9	-59.3	-47.7	-53.7	-63.4	-66.3
Balance on secondary income	302.8	322.1	322.8	351.1	357.6	379.7
Financing						
Capital account	21.6	27.6	37.9	29.8	37.6	37.7
Financial account, net[1]	-229.4	-173.5	-234.7	-98.4	-94.9	-75.7
Direct investment, net	-55	-62	-74	-111	-89	-106
Portfolio investment, net	0	0	0	0	0	0
Other investment, net	-100	-95	-61	-41	-40	-15
Overall balance	-75	-17	-100	53	33	46
Change in reserves (increase:+)	-75	-17	-100	53	33	46
Financing gap			28	11	11	6
percent of GDP			1.5	0.5	0.5	0.2
ECF			28	11	11	6
percent of GDP			1.5	0.5	0.5	0.2
Memorandum Items:						
Targeted reserves path as months of prospective imports	7.1	6.3	5.0	5.1	5.1	5.1

Source: Authorities and IMF staff estimates.

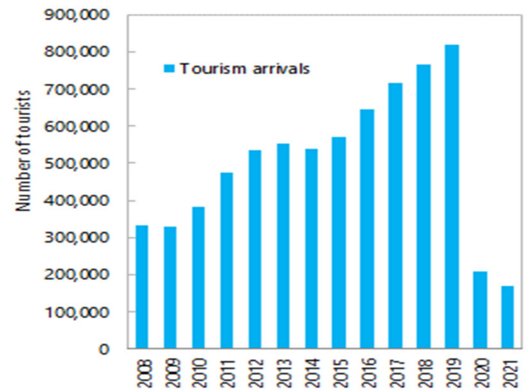
1/Includes reserves and exceptional financing

Figure 1. Cabo Verde: Recent Economic Developments

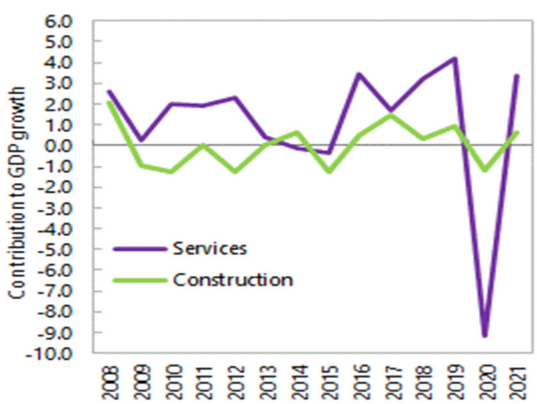
Economic growth is estimated to have increased in 2021…



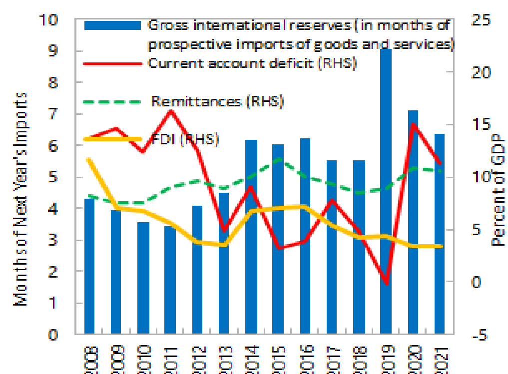
…due to the gradual recovery of the tourism sector during the second half of the year…



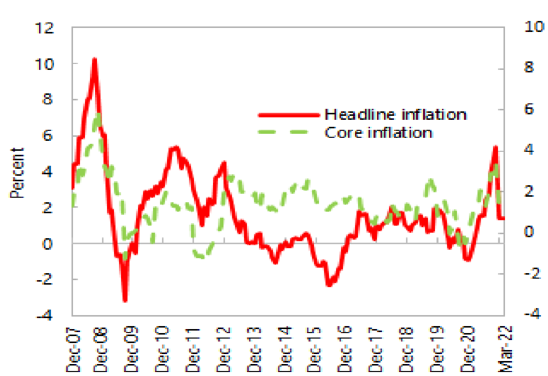
… and that of construction and other services.



International reserves remained comfortable reflecting increased FDI and higher remittances.



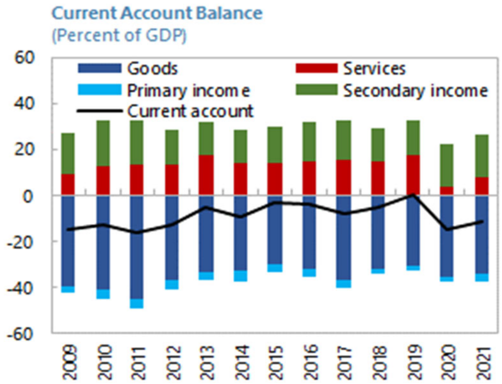
Headline inflation increased due to higher food, clothing, and transportation costs.



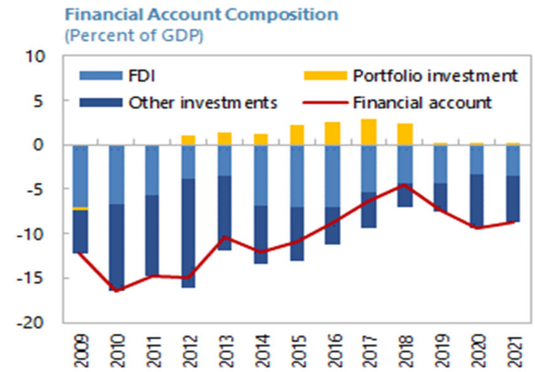
Sources: Cabo Verdean authorities; and IMF staff estimates.

Figure 2. Cabo Verde: External Sector Developments

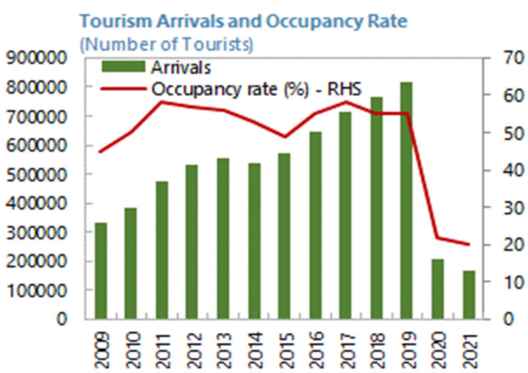
The current account deficit improves in 2021 in line with tourism recovery.



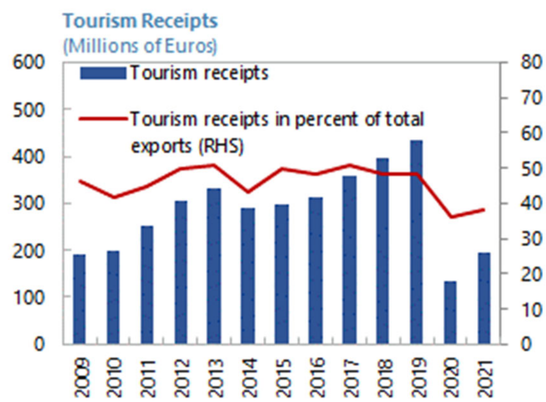
The financial account improved reflecting increased FDI.



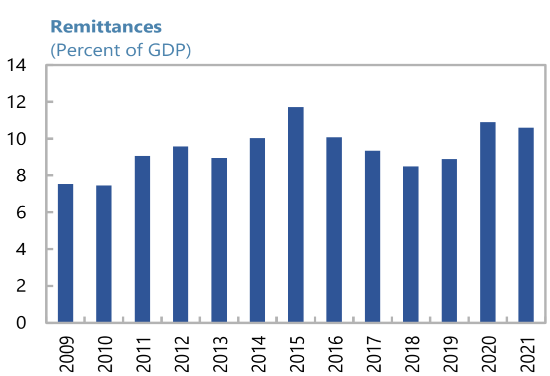
Tourism arrivals increased but remain well below pre pandemic levels.



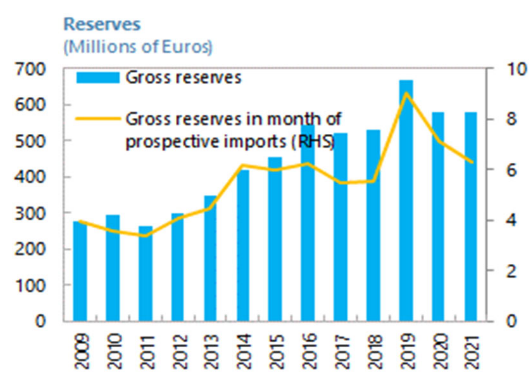
As a result, tourism receipts have only been increasing modestly.



Remittances declined slightly in 2021 compared to 2020 levels and remain an important source of foreign currency…



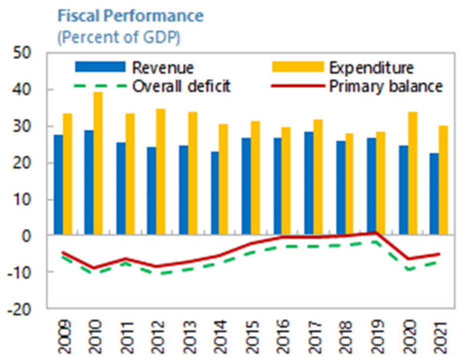
… supporting the country's strong reserve position.



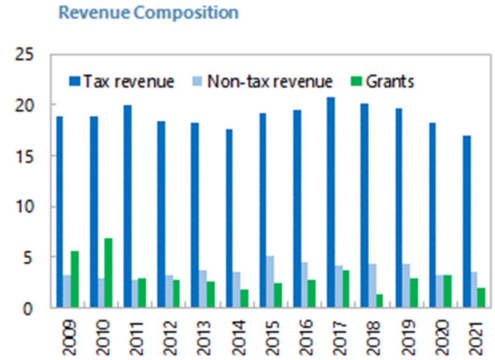
Sources: Cabo Verdean authorities; and IMF staff estimates.

Figure 3. Cabo Verde: Fiscal Sector Developments

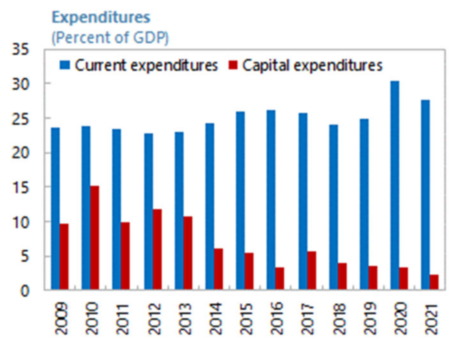
Fiscal performance improved in 2021 …



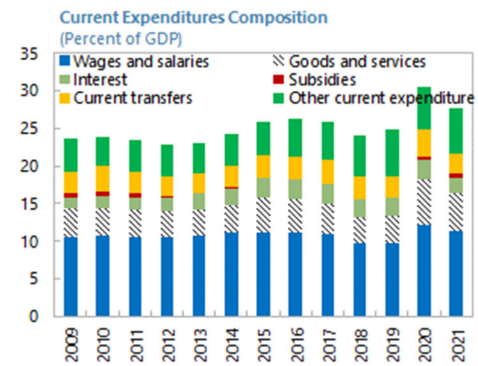
…Despite the decline in tax revenues reflecting the economic weakness. However, non-tax revenues increased reflecting the high sale of goods and services in line with the reopening of the economy.



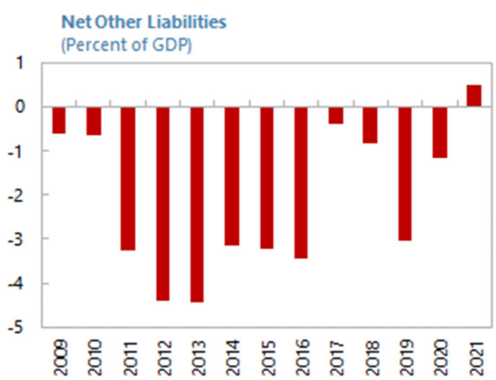
Expenditures declined due to the under execution of the public investment program.



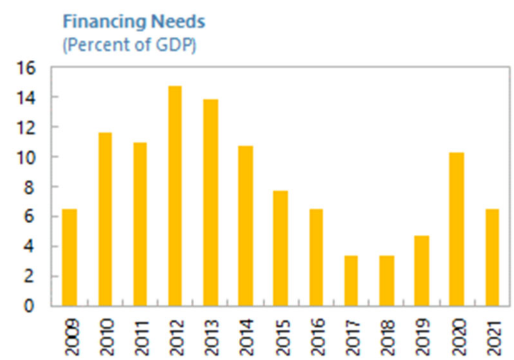
…and current expenditure restraint on account of slow wage growth and a decline in spending on goods and services.



Net other liabilities declined in 2021 reflecting higher government deposits and on lending repayments.



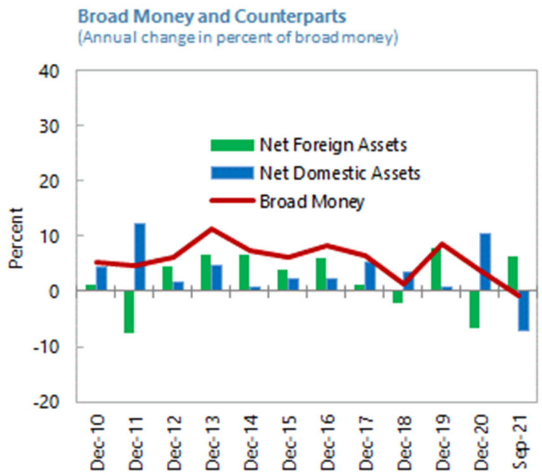
…Financing needs decreased due to lower capitalization and higher nontax revenues.



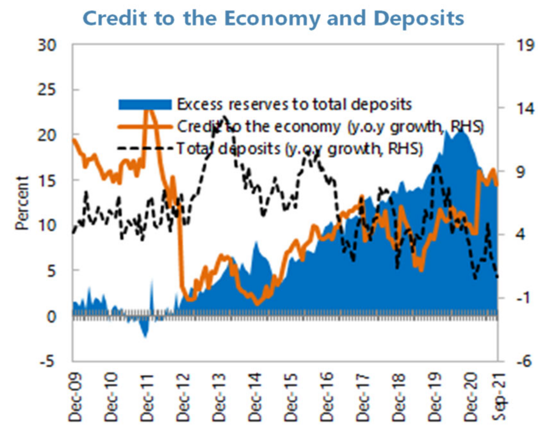
Sources: Cabo Verdean authorities; and IMF staff estimates.

Figure 4. Cabo Verde: Monetary Developments

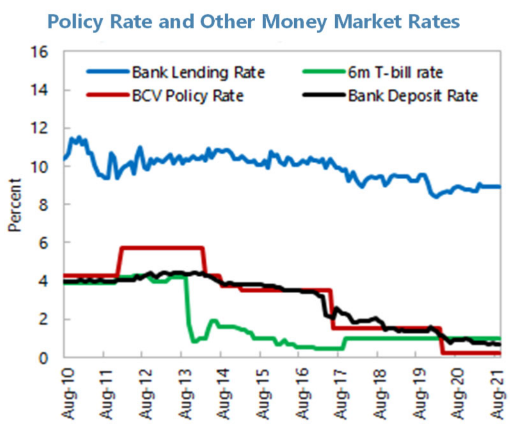
At end September 2021 broad money declined reflecting the decline in foreign currency reserves…



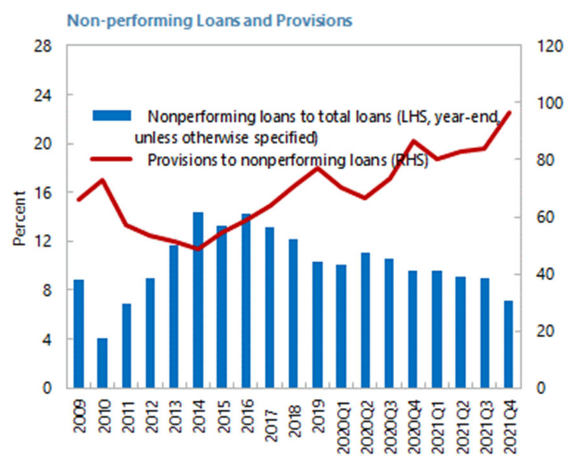
…credit to the economy increased reflecting the continued impact of COVID-19 relief measures.



The central bank lowered the policy rate in response to the COVID-19 pandemic.



Nonperforming loans have remained elevated.



Sources: Cabo Verdean authorities; and IMF staff estimates.

Table 1. Cabo Verde: Selected Economic Indicators, 2019–27

	2019	2020	2021	2022	2023	2024	2025	2026	2027
				Proj.	Proj.	Proj.	Proj.	Proj.	Proj.
	(Annual percent change)								
National accounts and prices 1/									
Real GDP	5.7	-14.8	7.0	4.0	4.8	5.7	5.5	5.0	4.5
GDP deflator	0.6	-0.9	1.8	4.5	2.6	2.0	2.0	2.0	2.0
Consumer price index (annual average)	1.1	0.6	1.9	6.5	3.5	2.0	2.0	2.0	2.0
Consumer price index (end of period)	1.9	-0.9	5.4	6.5	3.5	2.0	2.0	2.0	2.0
External sector									
Exports of goods and services	10.2	-58.7	39.3	11.2	32.6	11.0	9.6	9.0	9.3
Of which: tourism	9.4	-69.1	48.4	14.2	22.2	18.7	11.8	8.7	5.5
Imports of goods and services	1.6	-23.2	11.0	14.4	5.8	7.1	6.4	7.3	6.4
	(Change in percent of broad money, 12 months earlier)								
Money and credit									
Net foreign assets	7.8	-6.6	6.0	-10.6	2.7	1.6	2.1	2.3	1.3
Net domestic assets	0.6	10.3	-4.0	12.2	5.0	5.3	4.6	4.3	4.3
Net claims on the central government	-4.8	-1.3	0.6	1.8	1.6	0.7	0.3	-0.1	-0.4
Credit to the economy	2.3	2.9	1.8	5.1	1.3	2.7	2.1	4.3	3.2
Broad money (M2)	8.4	3.8	2.0	1.6	7.7	6.8	6.7	6.6	5.6
	(Percent of GDP, unless otherwise indicated)								
Savings and investment									
Domestic savings	37.3	20.7	31.0	30.0	35.2	33.9	35.3	34.7	34.7
Government	0.1	-7.4	-4.5	-2.6	-1.8	-0.1	1.7	2.9	2.5
Private	37.2	28.1	35.5	32.6	37.0	34.1	33.6	31.8	32.3
National investment	37.1	35.7	42.3	44.1	41.4	39.8	39.9	39.3	39.0
Government	3.6	3.3	2.2	3.4	3.1	3.1	3.0	3.0	3.0
Private	33.6	32.4	40.1	40.7	38.2	36.7	36.9	36.3	36.0
Savings-investment balance	0.2	-15.0	-11.3	-14.1	-6.2	-5.9	-4.7	-4.6	-4.2
Government	-3.4	-10.7	-6.7	-5.9	-4.9	-3.2	-1.3	-0.1	-0.5
Private	3.6	-4.3	-4.5	-8.1	-1.3	-2.7	-3.4	-4.5	-3.7
External sector									
External current account (including official transfers)	0.2	-15.0	-11.3	-14.1	-6.2	-5.9	-4.7	-4.6	-4.2
External current account (excluding official transfers)	-2.5	-17.6	-14.2	-16.1	-8.1	-7.2	-5.7	-5.6	-5.2
Overall balance of payments	6.8	-4.6	-1.0	-5.2	2.6	1.5	1.9	2.1	1.2
Gross international reserves (months of prospective imports of goods and services)	9.0	7.1	6.3	5.0	5.1	5.1	5.1	5.2	5.2
Government finance									
Revenue	26.8	24.7	22.6	25.4	24.8	25.5	25.9	26.3	26.5
Tax and nontax revenue	23.9	21.4	20.6	23.5	23.6	24.4	24.9	25.4	25.7
Grants	2.9	3.2	2.0	1.9	1.2	1.1	1.0	0.9	0.8
Expenditure	28.5	33.8	29.9	31.7	30.4	29.5	28.1	27.3	27.3
Primary balance	0.7	-6.4	-5.1	-3.6	-2.6	-1.3	0.0	1.0	1.0
Overall balance (incl. grants)	-1.7	-9.1	-7.3	-6.3	-5.6	-4.0	-2.1	-0.9	-0.8
Net other liabilities (incl. onlending)	-3.0	-1.2	0.9	-0.7	-0.5	-0.2	-0.2	-0.2	0.0
Total financing (incl. onlending and capitalization)	4.6	14.0	6.4	7.0	6.2	4.2	2.3	1.1	1.2
Net domestic credit	1.3	2.8	1.6	3.5	3.0	1.3	0.6	-0.3	-0.8
Net external financing	3.3	11.2	4.8	3.5	3.2	2.9	1.7	1.4	1.6
Public debt stock and service									
Total nominal government debt	114.0	142.6	143.0	145.9	139.7	132.5	124.0	116.2	109.6
External government debt	82.6	103.1	101.5	103.6	97.7	93.1	88.4	83.7	79.6
Domestic government debt	31.4	39.5	41.5	42.3	42.0	39.4	35.5	32.4	30.0
External debt service (percent of exports of goods and services)	5.4	14.8	13.4	17.7	14.7	11.0	10.3	9.5	9.0
Present value of PPG external debt									
Percent of GDP (risk threshold: 55%)	55.8	70.3	60.3	55.9	53.4	51.4	49.3	47.3	45.6
Percent of exports (risk threshold: 240%)	119.9	335.9	208.1	188.4	145.8	136.3	128.4	121.0	113.7
Present value of total debt									
Percent of GDP (benchmark: 70%)	92.4	105.4	104.7	97.9	95.0	90.5	84.7	79.7	75.5
Memorandum items:									
Nominal GDP (billions of Cabo Verde escudos)	213.9	180.7	196.8	213.8	229.8	247.7	266.6	285.5	304.2
Gross international reserves (€ millions, end of period)	666.1	582.4	591.3	491.0	544.3	577.6	623.3	677.5	710.3

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

1/ The Cabo Verdean exchange rate has been pegged to the Euro since 1999, at a rate of 110.265 CVE/€.

Table 2. Cabo Verde: Balance of Payments, 2018–27

(Millions of Euros; unless otherwise indicated)

	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027
					Proj.	Proj.	Proj.	Proj.	Proj.	Proj.
Current account	-89	4	-246	-201	-273	-128	-132	-113	-119	-117
Trade balance	-582	-595	-579	-609	-716	-665	-684	-690	-686	-680
Exports, f.o.b.	232	237	113	167	178	282	313	352	406	471
Imports, f.o.b.	814	833	692	776	895	948	997	1042	1092	1151
Consumer goods	278	297	256	239	270	294	312	322	323	327
Intermediate goods	158	168	159	131	145	159	172	183	199	223
Capital goods	99	92	93	72	83	96	102	108	120	128
Others (including fuel)	279	276	185	334	397	399	411	429	450	473
Fuel	82	83	62	77	100	85	81	83	88	91
Services (net)	264	343	66	145	169	240	257	263	243	238
Receipt	584	662	258	351	398	481	533	577	606	635
Of which: tourism	395	432	133	198	226	276	328	367	399	421
Payment	320	319	192	206	229	241	276	314	363	397
Primary Income (net)	-40	-38	-36	-59	-48	-54	-63	-66	-69	-73
Of which: interest on public debt	-17	-17	-15	-30	-19	-24	-17	-19	-20	-22
Secondary Income (net)	268	294	303	322	323	351	358	380	393	398
General Government	46	53	43	52	40	40	28	25	26	26
Other Sectors	223	241	260	270	283	311	329	354	367	372
Of which: remittances	155	172	178	189	195	214	223	237	249	252
Capital account	15	11	22	28	38	30	38	38	38	22
Of which: Grants	11	6	10	16	25	17	25	25	26	9
Financial account 1/	-74	-12	-229	-174	-235	-98	-95	-76	-81	-95
Foreign direct investment	-78	-84	-55	-62	-74	-111	-89	-106	-109	-87
Portfolio investment	44	1	0	0	0	0	0	0	0	0
Other investment	-50	-62	-100	-95	-61	-41	-40	-15	-27	-41
Net acquisition of financial assets	-53	4	-18	-39	-8	5	5	6	6	6
Net incurrence of liabilities	-3	65	82	56	52	46	44	21	33	47
Monetary authority	-2	0	-1	1	0	0	0	0	0	0
Central government	32	64	101	72	73	66	65	41	31	45
Disbursements	64	96	128	111	156	155	141	119	107	122
of which RCF			29							
Prospective ECF Financing					28.16	11.22	11.17	5.59		
Amortization	-32	-32	-41	-39	-83	-88	-76	-77	-77	-77
Exceptional financing 2/	0	0	14	40	0	0	0	0	0	0
Commercial banks	4	4	4	5	5	5	5	5	5	5
Non-bank flows	-37	-3	-21	-21	-26	-26	-26	-26	-3	-3
Reserve assets (+ accumulation)	10	132	-75	-17	-100	53	33	46	54	33
Errors and omissions 3/	0	-28	-5	0	0	0	0	0	0	0
Overall balance	10	132	-75	-17	-100	53	33	46	54	33
Memorandum items:										
Current account (incl. official transfers, percent of GDP)	-4.9	0.2	-15.0	-11.3	-14.1	-6.2	-5.9	-4.7	-4.6	-4.2
Current account (excl. official transfers, percent of GDP)	-7.4	-2.5	-17.6	-14.2	-16.1	-8.1	-7.2	-5.7	-5.6	-5.2
Overall balance (percent of GDP)	0.5	6.8	-4.6	-1.0	-5.2	2.6	1.5	1.9	2.1	1.2
Gross international reserves	531.9	666.1	582.4	591.3	491.0	544.3	577.6	623.3	677.5	710.3
Months of current year's imports of goods and services	5.6	6.9	7.9	7.2	5.2	5.5	5.4	5.5	5.6	5.5
Months of next year's imports of goods and services	5.5	9.0	7.1	6.3	5.0	5.1	5.1	5.1	5.3	5.2
External public debt	1822	1900	2003	2147	2371	2426	2508	2582	2617	2649
External aid (grants and loans, percent of GDP)	6.6	8.0	11.1	10.0	11.4	10.2	8.7	7.0	6.1	5.7
Nominal GDP	1826	1940	1639	1785	1939	2084	2246	2418	2589	2759

Sources: Bank of Cabo Verde; and IMF staff estimates and projections.

1/ Including international reserves and exceptional financing.

2/ Debt service suspension under the G-20 Initiative.

3/ Including banks' delays on trade credit reporting.

Table 3a. Cabo Verde: Statement of Operations of the Central Government, 2018–27[1]

(Millions of Cabo Verde Escudos)

	2018	2019	2020	2021	2022		2023	2024	2025	2026	2027
					Budget	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.
Revenue	51,857	57,389	44,626	44,530	58,196	54,270	56,964	63,139	69,159	75,220	80,506
Tax	40,657	42,013	32,900	33,542	41,184	38,215	43,273	48,854	53,870	59,328	63,876
Taxes on income and profit	12,253	12,672	9,990	9,149	11,879	9,716	11,176	11,978	13,551	15,015	16,397
Personal income tax	6,877	7,201	6,581	6,048	6,799	6,232	6,766	7,512	8,407	9,230	10,034
Corporate income tax	5,376	5,471	3,410	2,728	4,431	3,084	3,947	4,467	5,143	5,785	6,363
Taxes on goods and services	19,887	20,658	15,632	15,824	20,129	18,799	21,413	24,503	26,779	29,226	32,137
Of which: customs VAT (IVA DGA)	7,801	8,260	6,670	8,319	8,934	8,738	9,673	10,635	11,560	12,282	13,385
Of which: domestic VAT (IVA DGCI)	8,422	8,476	6,371	4,674	6,892	6,109	7,129	8,798	9,563	10,443	11,326
Taxes on international trade	7,733	8,011	6,593	7,894	8,407	8,973	9,856	11,481	12,580	13,978	14,160
Other taxes	784	672	684	675	769	727	828	893	961	1,110	1,183
Grants	2,575	6,238	5,866	3,985	3,982	3,982	2,788	2,705	2,711	2,604	2,474
Other revenue	8,625	9,137	5,861	7,002	13,031	12,073	10,904	11,580	12,577	13,287	14,156
Fees and penalties	433	408	220	166	342	357	383	413	445	476	486
Property Income	1,828	2,301	1,135	1,215	5,444	5,218	3,583	3,733	4,108	4,190	4,274
Sale of Goods and Services	5,732	5,991	3,719	4,245	5,957	5,212	5,602	6,014	6,472	6,933	7,071
Other (inc. social contributions)	633	438	787	1,376	1,288	1,286	1,335	1,419	1,552	1,688	2,325
Expenditure	56,726	60,974	61,052	58,898	72,330	67,825	69,942	73,113	74,817	77,867	83,071
Expense 2/	48,587	53,343	55,119	54,544	62,112	60,639	62,748	65,449	66,820	69,302	73,945
Compensation of employees	19,425	20,595	21,842	22,144	24,326	23,262	23,727	24,914	25,786	26,619	28,360
Use of goods and services	7,185	8,001	11,110	9,982	12,390	11,296	11,030	11,642	12,029	12,184	12,981
Interest	4,726	4,991	4,829	4,256	5,541	5,805	6,998	6,847	5,562	5,616	5,669
Domestic	2,811	3,083	3,156	3,236	3,413	3,646	4,102	4,835	3,397	3,318	3,279
External	1,822	1,867	1,614	942	2,052	2,063	2,800	1,916	2,069	2,201	2,390
Other Charges	93	41	58	78	76	97	97	97	97	97	0
Subsidies	153	160	630	816	1,008	1,409	1,459	1,488	1,518	1,548	1,579
Current transfers	6,283	6,015	6,482	5,536	6,097	6,097	6,205	6,688	6,997	7,345	7,825
Social benefits	6,237	7,270	8,268	9,267	8,316	8,901	9,422	10,156	10,929	11,707	12,472
Other expense (incl. capital transfer)	4,577	6,310	1,959	2,543	4,433	3,868	3,907	3,715	3,999	4,283	5,060
Net acquisition of nonfinancial assets	8,140	7,631	5,933	4,354	10,217	7,186	7,194	7,664	7,997	8,566	9,126
Purchase of assets	8,194	7,971	6,033	5,037	10,625	7,834	7,905	8,369	8,468	9,037	9,126
Sales of assets (-)	-54	-339	-100	-683	-408	-648	-711	-705	-471	-471	0
Primary balance	-143	1,406	-11,598	-10,112	-8,592	-7,750	-5,979	-3,127	-96	2,968	3,104
Overall balance	-4,869	-3,585	-16,426	-14,368	-14,133	-13,555	-12,977	-9,974	-5,658	-2,648	-2,565
Net other liabilities	-1,903	-6,393	-2,104	1,691	-4,363	-1,455	-1,256	-399	-584	-625	0
Onlending to SOEs for investment purpose	-1,541	-1,531	-1,650	-1,220	-2,513	-2,910	-1,752	-543	-584	-625	0
Other onlending (net)	3,606	-563	307	2,401	120	120	144	144	0	0	0
Disbursement	0	-2,299	0	0	0	0	0	0	0	0	0
Repayment	3,606	1,736	307	2,401	120	120	144	144	0	0	0
Capitalization	-3,968	-4,425	-767	-838	-2,651	-2,151	-1,000	0	0	0	0
Other	0	124	7	1,348	681	3,124	1,352	0	0	0	0
Financing needs	6,772	9,978	18,530	12,677	18,497	15,010	14,233	10,372	6,242	3,273	2,565
Total financing	5,239	9,926	25,250	12,677	18,497	15,010	14,233	10,372	6,242	3,273	2,565
Net domestic financing	2,517	2,816	5,080	3,142	11,412	7,501	6,911	3,204	1,675	-736	-2,376
Net external financing	2,723	7,110	20,169	9,536	7,085	7,509	7,322	7,169	4,567	4,009	4,941
Disbursement	6,202	11,277	16,024	14,499	16,089	16,672	17,072	15,570	13,066	12,447	13,472
Budget Loans	2,205	6,148	9,125	4,223	3,105	8,130	6,466	6,743	6,232	5,732	6,029
Of which RCF disbursement			3,213								
Prospective ECF Financing						3,105	1,238	1,233	615		
Project and Program Loans	2,456	3,599	4,025	6,801	6,785	6,203	8,854	8,284	6,251	6,090	7,443
Loans to on lend to SOEs 3/	1,541	1,531	1,377	1,220	2,513	2,339	1,752	543	584	625	0
Amortization	3,479	4,167	-4,145	4,964	9,005	9,163	9,750	8,401	8,500	8,438	8,531
Unidentified external financing						0					
Exceptional financing (DSSI)			1,498	2,255							
Net errors and omissions (+ overfinancing)	-1,533	-52	6,719	0	0	0	0	0	0	0	0
Memorandum items:											
Social Spending	14,008	14,996	20,050	18,300	15,800	15,800	16,982	18,305	19,700	21,101	22,480
Total Public Investment	9,735	9,501	7,410	6,257	13,139	10,173	9,657	8,912	9,052	9,662	9,126
of which: public investment done by SOEs	1,541	1,531	1,377	1,220	2,513	2,339	1,752	543	584	625	0

Sources: Cabo Verdean authorities; and IMF staff estimates and projections.
1/ Includes budgetary central government (BCG) and extra budgetary central government (ECG), but excludes social security funds.
2/ Higher expenditures on compensation of employees and on goods and services for 2020 partly reflect the broadening of the fiscal coverge.
3/ On lend to SOEs for public investment execution.

Table 3b. Cabo Verde: Statement of Operations of the Central Government, 2018–27[1]

(Percent of GDP)

	2018	2019	2020	2021	2022		2023	2024	2025	2026	2027
					Budget	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.
Revenue	25.8	26.8	24.7	22.6	27.2	25.4	24.8	25.5	25.9	26.3	26.5
Taxes	20.2	19.6	18.2	17.0	19.3	17.9	18.8	19.7	20.2	20.8	21.0
Taxes on income and profit	6.1	5.9	5.5	4.6	5.6	4.5	4.9	4.8	5.1	5.3	5.4
Taxes on goods and services	9.9	9.7	8.6	8.0	9.4	8.8	9.3	9.9	10.0	10.2	10.6
Taxes on international trade	3.8	3.7	3.6	4.0	3.9	4.2	4.3	4.6	4.7	4.9	4.7
Other taxes	0.4	0.3	0.4	0.3	0.4	0.3	0.4	0.4	0.4	0.4	0.4
Grants	1.3	2.9	3.2	2.0	1.9	1.9	1.2	1.1	1.0	0.9	0.8
Other revenue	4.3	4.3	3.2	3.6	6.1	5.6	4.7	4.7	4.7	4.7	4.7
Fees and penalties	0.2	0.2	0.1	0.1	0.2	0.2	0.2	0.2	0.2	0.2	0.2
Property Income	0.9	1.1	0.6	0.6	2.5	2.4	1.6	1.5	1.5	1.5	1.4
Sale of Goods and Services	2.8	2.8	2.1	2.2	2.8	2.4	2.4	2.4	2.4	2.4	2.3
Other (inc. social contributions)	0.3	0.2	0.4	0.7	0.6	0.6	0.6	0.6	0.6	0.6	0.8
Expenditure	28.2	28.5	33.8	29.9	33.8	31.7	30.4	29.5	28.1	27.3	27.3
Expense 2/	24.1	24.9	30.5	27.7	29.1	28.4	27.3	26.4	25.1	24.3	24.3
Compensation of employees	9.6	9.6	12.1	11.3	11.4	10.9	10.3	10.1	9.7	9.3	9.3
Use of goods and services	3.6	3.7	6.1	5.1	5.8	5.3	4.8	4.7	4.5	4.3	4.3
Interest	2.3	2.3	2.7	2.2	2.6	2.7	3.0	2.8	2.1	2.0	1.9
Domestic	1.4	1.4	1.7	1.6	1.6	1.7	1.8	2.0	1.3	1.2	1.1
External	0.9	0.9	0.9	0.5	1.0	1.0	1.2	0.8	0.8	0.8	0.8
Other Charges	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Subsidies	0.1	0.1	0.3	0.4	0.5	0.7	0.6	0.6	0.6	0.5	0.5
Current transfers	3.1	2.8	3.6	2.8	2.9	2.9	2.7	2.7	2.6	2.6	2.6
Social benefits	3.1	3.4	4.6	4.7	3.9	4.2	4.1	4.1	4.1	4.1	4.1
Other expense (incl. capital transfer)	2.3	2.9	1.1	1.3	2.1	1.8	1.7	1.5	1.5	1.5	1.7
Net acquisition of nonfinancial assets	4.0	3.6	3.3	2.2	4.8	3.4	3.1	3.1	3.0	3.0	3.0
Purchase of assets	4.1	3.7	3.3	2.6	5.0	3.7	3.4	3.4	3.2	3.2	3.0
Sales of assets (-)	0.0	-0.2	-0.1	-0.3	-0.2	-0.3	-0.3	-0.3	-0.2	-0.2	0.0
Primary balance	-0.1	0.7	-6.4	-5.1	-4.0	-3.6	-2.6	-1.3	0.0	1.0	1.0
Overall balance	-2.4	-1.7	-9.1	-7.3	-6.6	-6.3	-5.6	-4.0	-2.1	-0.9	-0.8
Net other liabilities	-0.9	-3.0	-1.2	0.9	-2.0	-0.7	-0.5	-0.2	-0.2	-0.2	0.0
Onlending to SOEs for investment purpose	-0.8	-0.7	-0.9	-0.6	-1.2	-1.4	-0.8	-0.2	-0.2	-0.2	0.0
Other onlending (net)	1.8	-0.3	0.2	1.2	0.1	0.1	0.1	0.1	0.0	0.0	0.0
Disbursement	0.0	-1.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Repayment	1.8	0.8	0.2	1.2	0.1	0.1	0.1	0.1	0.0	0.0	0.0
Capitalization	-2.0	-2.1	-0.4	-0.4	-1.2	-1.0	-0.4	0.0	0.0	0.0	0.0
Other	0.0	0.1	0.0	0.7	0.3	1.5	0.6	0.0	0.0	0.0	0.0
Financing Needs	3.4	4.7	10.3	6.4	8.7	7.0	6.2	4.2	2.3	1.1	0.8
Total financing	2.6	4.6	14.0	6.4	8.7	7.0	6.2	4.2	2.3	1.1	0.8
Net domestic financing	1.3	1.3	2.8	1.6	5.3	3.5	3.0	1.3	0.6	-0.3	-0.8
Net external financing	1.4	3.3	11.2	4.8	3.3	3.5	3.2	2.9	1.7	1.4	1.6
Disbursement	3.1	5.3	8.9	7.4	7.5	7.8	7.4	6.3	4.9	4.4	4.4
Budget Loans	1.1	2.9	5.0	2.1	1.5	3.8	2.8	2.7	2.3	2.0	2.0
Of which RCF disbursement			1.8								
Prospective ECF Financing						1.5	0.5	0.5	0.2		
Project and Program Loans	1.2	1.7	2.2	3.5	3.2	2.9	3.9	3.3	2.3	2.1	2.4
Loans to on lend to SOEs 3/	0.8	0.7	0.8	0.6	1.2	1.1	0.8	0.2	0.2	0.2	0.0
Amortization	1.7	1.9	-2.3	2.5	4.2	4.3	4.2	3.4	3.2	3.0	2.8
Unidentified Financing (Financing Gap)						0.0					
Exceptional financing (DSSI)			0.8	1.1							
Net errors and omissions (+ overfinancing)	-0.8	0.0	3.7	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items:											
Social Spending	7.0	7.0	11.1	9.3	7.4	7.4	7.4	7.4	7.4	7.4	7.4
Total Public Investment	4.8	4.4	4.1	3.2	6.1	4.8	4.2	3.6	3.4	3.4	3.0
Of which: public investment done by SOEs	0.8	0.7	0.8	0.6	1.2	1.1	0.8	0.2	0.2	0.2	0.0
GDP at current market prices (billions of CVEsc)	201.3	213.9	180.7	196.8	213.8	213.8	229.8	247.7	266.6	285.5	304.2

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

1/ Includes budgetary central government (BCG) and extra budgetary central government (ECG), but excludes social security funds.

2/ Higher expenditures on compensation of employees and on goods and services for 2020 partly reflect the broadening of the fiscal coverge.

3/ On lend to SOEs for public investment execution.

Table 4. Cabo Verde: Monetary Survey, 2018–27
(Millions of Cabo Verde escudos, unless otherwise indicated)

	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027
					Proj.	Proj.	Proj.	Proj.	Proj.	Proj.
Net foreign assets	56,396	70,782	57,716	70,058	47,634	53,475	57,108	62,206	68,248	71,936
Foreign assets	83,533	98,658	91,373	91,271	79,296	85,680	89,868	95,532	102,150	106,427
Of which: gross international reserves	58,649	73,453	64,213	65,197	54,135	60,016	63,690	68,726	74,701	78,319
Foreign liabilities	-27,233	-27,876	-33,658	-31,129	-31,662	-32,206	-32,760	-33,326	-33,903	-34,491
Net domestic assets	127,234	128,361	148,917	140,664	166,457	177,153	189,314	200,646	211,872	223,975
Net domestic credit	156,614	152,510	146,433	156,817	159,005	165,230	172,979	178,921	190,147	198,122
Net claims on general government (net)	40,284	31,929	20,036	14,516	18,242	21,642	23,215	24,031	23,899	22,940
Investment in TCMFs 1/	11,070	11,112	6,433	0	0	0	0	0	0	0
Net claims on the central government	32,659	23,909	21,380	22,545	26,296	29,751	31,353	32,191	31,823	30,635
Credit to central government	46,866	41,943	44,681	45,846	49,596	53,052	54,654	55,491	55,123	53,935
Deposits of central government	-14,207	-18,034	-23,300	-23,300	-23,300	-23,300	-23,300	-23,300	-23,300	-23,300
Of which: project deposits	-56	-68	-80	-80	-80	-80	-80	-80	-80	-80
Net claims on local government and other agencies 2/	-3,446	-3,093	-7,777	-8,029	-8,054	-8,109	-8,138	-8,159	-7,924	-7,695
Credit to the economy	116,330	120,581	126,396	130,062	140,764	143,588	149,764	154,890	166,248	175,182
Other items (net)	-29,380	-24,148	2,484	497	7,452	11,923	16,335	21,725	21,725	25,853
Broad money (M2)	183,630	199,143	206,632	210,723	214,092	230,628	246,421	262,853	280,120	295,910
Narrow money (M1)	86,806	97,273	104,469	90,318	104,575	112,652	120,366	128,393	136,827	144,540
Currency outside banks	9,571	9,980	11,115	10,475	10,729	11,558	12,350	13,173	14,039	14,830
Demand deposits	77,235	87,293	93,354	79,843	93,845	101,094	108,017	115,219	122,788	129,710
Quasi-money	91,862	96,444	97,565	102,050	103,682	111,690	119,339	127,296	135,658	143,306
Foreign currency deposits	4,963	5,428	4,599	5,743	5,835	6,286	6,716	7,164	7,635	8,065
(Change in percent of broad money, 12 months earlier)										
Net foreign assets	-2.1	7.8	-6.6	6.0	-10.6	2.7	1.6	2.1	2.3	1.3
Net domestic assets	3.5	0.6	10.3	-4.0	12.2	5.0	5.3	4.6	4.3	4.3
Net domestic credit	5.9	-2.2	-3.1	5.0	1.0	2.9	3.4	2.4	4.3	2.8
Net claims on the central government	4.3	-4.8	-1.3	0.6	1.8	1.6	0.7	0.3	-0.1	-0.4
Credit to the economy	1.9	2.3	2.9	1.8	5.1	1.3	2.7	2.1	4.3	3.2
Other items (net)	-2.4	2.8	13.4	-1.0	3.3	2.1	1.9	2.2	0.0	1.5
Broad money (M2)	1.4	8.4	3.8	2.0	1.6	7.7	6.8	6.7	6.6	5.6
Memorandum items:										
Emigrant deposits	63,869	65,365	66,422	108,032	118,448	127,597	136,334	145,425	154,978	163,714
Emigrant deposits/total deposits (percent)	36.7	34.6	34.0	53.9	58.2	58.2	58.2	58.2	58.2	58.2
Excess reserves/total deposits (percent)	13.4	16.7	...	...	...	...	...	...	...	...
Money multiplier (M2/M0)	3.2	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9
Money velocity (Nominal GDP/M2)	1.1	1.1	0.9	0.9	1.0	1.0	1.0	1.0	1.0	1.0
Credit to the economy (percent change) 3/	3.1	3.7	4.8	2.9	8.2	2.0	4.3	3.4	7.3	5.4
Broad money (M2 in percent of GDP)	91.2	93.1	114.3	107.1	100.1	100.4	99.5	98.6	98.1	97.3

Sources: Bank of Cabo Verde; and IMF staff estimates and projections.

1/ TCMFs (Títulos Consolidados de Mobilização Financeira) are bonds in CVE, backed by an offshore account managed by Banco de Portugal. They matured in late 2018; and in 2019 the authorities decided to redeem a portion of them and to replace the balance with new bonds.

2/ Includes Cabo Verde's National Pension Institute (INPS).

3/ Percent change, year over year.

Table 5. Cabo Verde: Financial Soundness Indicators of the Banking Sector, 2018–21Q4

(End-year; percent unless otherwise indicated)

	2018	2019	2020Q1	2020Q2	2020Q3	2020Q4	2021Q1	2021Q2	2021Q3	2021Q4
Capital adequacy										
Regulatory capital to risk-weighted assets	16.2	17.7	18.1	18.3	18.6	19.4	19.6	20.0	20.9	21.1
Regulatory Tier 1 capital to risk-weighted assets	16.1	18.2	18.6	18.8	19.0	19.8	20.1	20.5	20.9	21.0
Asset quality 1/										
Nonperforming loans to total loans	12.2	10.4	10.1	11.0	10.5	9.5	9.5	9.1	9.0	7.2
Nonperforming loans net of provisions to capital	26.0	15.0	20.4	23.9	16.6	7.1	10.9	8.5	7.6	1.2
Provisions to nonperforming loans	71.0	77.0	70.1	66.5	73.3	86.4	80.0	83.0	84.1	96.7
Earnings and profitability										
Return on assets	0.3	1.3	0.4	0.6	1.0	1.3	0.4	0.8	1.2	1.5
Return on equity	4.8	17.8	5.3	7.9	12.7	15.4	4.9	9.1	12.7	15.9
Interest margin to gross income	79.6	81.1	78.2	85.8	86.7	85.7	84.8	83.1	83.5	81.3
Noninterest expenses to gross income	69.6	49.4	46.4	49.3	48.9	48.9	45.5	45.3	45.4	46.0
Liquidity 2/										
Liquid assets to total assets	21.4	24.3	23.8	25.4	25.9	25.1	23.0	21.7	22.6	24.3
Liquid assets to short-term liabilities	25.5	28.3	27.8	30.0	30.8	29.9	27.5	26.1	28.0	30.5
Additional indicators										
Government deposits over total deposits	18.3	19.1	19.6	19.1	19.7	19.6	19.0	18.0	17.7	16.0
Demand deposits over total deposits	50.5	50.9	51.8	51.6	51.7	51.1	51.6	51.4	50.9	51.8
Total credit over total deposits	55.2	52.9	52.9	53.2	53.6	54.7	55.5	56.1	57.8	56.9
Personnel cost over cost of operations	66.6	56.6	59.2	57.8	57.7	58.0	60.4	59.7	58.4	58.0

Source: Bank of Cabo Verde.
1/ Based on IAS/IFRS definition.
2/ Liquid assets include cash in vault and marketable securities. Short-term liabilities include demand deposits.

Table 6. Cabo Verde: Indicators of Capacity to Repay the Fund, 2020-35

	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032	2033	2034	2035
Fund obligations based on existing credit (millions of SDRs)																
Principal	0.0	0.0	0.0	0.0	0.0	2.4	4.7	4.7	4.7	4.7	2.4	0.0	0.0	0.0	0.0	0.0
Charges and interest	0.0	0.0	0.1	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2
Total	0.0	0.0	0.1	0.2	0.2	2.5	4.9	4.9	4.9	4.9	2.5	0.2	0.2	0.2	0.2	0.2
Fund obligations based on existing and prospective credit (millions of SDRs)																
Principal	0.0	0.0	0.0	0.0	0.0	2.4	4.7	5.9	9.7	11.5	10.9	9.0	7.9	4.1	2.3	0.5
Charges and interest	0.0	0.0	0.1	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2
Total	0.0	0.0	0.1	0.2	0.2	2.5	4.9	6.0	9.9	11.7	11.1	9.2	8.0	4.2	2.4	0.6
Total obligations based on existing and prospective credit																
Millions of SDRs	0.0	0.0	0.1	0.2	0.2	2.5	4.9	6.0	9.9	11.7	11.1	9.2	8.0	4.2	2.4	0.6
Millions of U.S. dollars	0.0	0.0	0.1	0.2	0.2	3.6	7.1	8.7	14.3	16.9	16.1	13.3	11.6	6.1	0.0	0.0
Percent of exports of goods and services	0.0	0.0	0.0	0.0	0.0	0.3	0.6	0.7	1.0	1.1	1.0	0.7	0.6	0.3	0.0	0.0
Percent of debt service	0.2	0.0	0.1	0.1	0.1	2.5	4.8	5.8	9.3	10.5	9.5	7.4	6.1	3.0	0.0	0.0
Percent of quota	0.0	0.0	0.3	0.7	0.7	10.7	20.7	25.4	41.6	49.2	46.8	38.7	33.9	17.8	10.2	2.6
Percent of gross international reserves	0.0	0.0	0.0	0.0	0.0	0.5	0.9	1.1	1.6	1.8	1.6	1.2	1.0	0.5	0.0	0.0
Percent of GDP	0.0	0.0	0.0	0.0	0.0	0.1	0.2	0.3	0.4	0.5	0.4	0.3	0.3	0.1	0.0	0.0
Outstanding Fund credit																
Millions of SDRs	23.7	23.7	46.2	55.2	64.2	66.4	61.6	55.8	46.1	34.6	23.6	14.6	6.8	2.7	0.5	0.0
Millions of U.S. dollars	33.0	33.8	64.4	77.8	91.3	95.1	88.8	80.7	66.7	50.1	34.2	21.2	9.8	3.9	0.0	0.0
Percent of exports of goods and services	7.8	5.5	10.0	9.0	9.4	8.9	7.5	6.2	4.8	3.3	2.0	1.2	0.5	0.2	0.0	0.0
Percent of debt service	466.6	34.1	42.6	45.3	57.7	64.5	59.9	53.6	43.7	31.3	20.2	11.8	5.1	1.9	0.0	0.0
Percent of quota	100	100	195	233	271	280	260	235	194	146	100	62	29	11	2	0
Percent of gross international reserves	5.0	4.8	11.8	12.7	13.8	13.2	11.3	9.7	7.5	5.5	3.5	2.0	0.8	0.3	0.0	0.0
Percent of GDP	1.8	1.6	3.0	3.3	3.5	3.4	2.9	2.5	1.9	1.4	0.9	0.5	0.2	0.1	0.0	0.0
Net Use of Fund Credit (millions of SDRs)	23.7	0.0	22.5	9.0	9.0	2.1	-4.7	-5.9	-9.7	-11.5	-10.9	-9.0	-7.9	-4.1	-2.3	-0.5
Disbursements	23.7	0.0	22.5	9.0	9.0	4.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Repayments	0.0	0.0	0.0	0.0	0.0	2.4	4.7	5.9	9.7	11.5	10.9	9.0	7.9	4.1	2.3	0.5
Memorandum items:																
Exports of goods and services (millions of U.S. dollars)	424.1	612.7	641.5	862.6	970.4	1073.9	1178.6	1292.9	1396.6	1504.3	1674.3	1810.3	1964.3	2111.4	2272.1	2461.8
Debt service (millions of U.S. dollars)	7.1	99.0	151.3	171.7	158.4	147.5	148.4	150.5	152.7	160.1	169.7	179.6	191.9	206.4	226.7	242.4
Quota (millions of SDRs)	23.7	23.7	23.7	23.7	23.7	23.7	23.7	23.7	23.7	23.7	23.7	23.7	23.7	23.7	23.7	23.7
Gross international reserves	664.6	699.8	547.2	615.2	661.8	720.8	788.7	830.1	885.5	914.2	990.7	1082.1	1180.7	1310.1	1450.0	1583.9
GDP (millions of U.S. dollars)	1870.7	2112.3	2160.9	2355.7	2573.9	2795.8	3014.6	3224.2	3435.7	3663.4	3908.7	4170.3	4447.0	4742.0	5056.5	5391.9

Sources: IMF staff estimates and projections.

Table 7. Cabo Verde: Decomposition of Public Debt and Debt Service by Creditor, 2021-23[1]

	Debt Stock (end of period)			Debt Service					
	2021			2021	2022	2023	2021	2022	2023
	(In US$)	*(Percent total debt)*	*(Percent GDP)*		*(In US$)*			*(Percent GDP)*	
Total	2885.2	100.0	143.0	174.5	204.8	210.7	8.6	9.4	8.9
External	2048.0	71.0	101.5	81.0	107.7	113.9	4.0	5.0	4.8
Multilateral creditors[2]	1109.4	38.5	55.0	36.5	56.9	61.8	1.8	2.6	2.6
IMF	67.5	2.3	3.3	0.0	0.2	0.2	0.0	0.0	0.0
World Bank	523.4	18.1	25.9	5.9	12.1	12.3	0.3	0.6	0.5
African Development Bank Fund	263.2	9.1	13.0	14.6	26.4	28.4	0.7	1.2	1.2
European Investment Bank(incl.EEC)	36.6	1.3	1.8	4.4	0.9	0.8	0.2	0.0	0.0
Other Multilaterals	218.8	7.6	10.8	11.6	17.3	20.0	0.6	0.8	0.8
BADEA	42.4	1.5	2.1	3.3	9.4	11.7	0.2	0.4	0.5
CEDEAO	15.8	0.5	0.8	1.2	0.0	0.0	0.1	0.0	0.0
FAD	112.1	3.9	5.6	4.1	6.3	6.6	0.2	0.3	0.3
Bilateral Creditors	418.9	14.5	20.8	24.4	16.5	19.2	1.2	0.8	0.8
Paris Club	228.7	7.9	11.3	10.1	13.1	14.2	0.5	0.6	0.6
France	57.9	2.0	2.9	3.0	4.4	4.4	0.1	0.2	0.2
Japan	90.5	3.1	4.5	1.7	2.9	3.3	0.1	0.1	0.1
Other (Spa, Belg, Aus, Swed)	80.2	2.8	4.0	5.4	5.8	6.4	0.3	0.3	0.3
Non-Paris Club	188.3	6.5	9.3	14.3	3.4	5.1	0.7	0.2	0.2
Portugal	139.6	4.8	6.9	9.8	0.9	2.5	0.5	0.0	0.1
China	33.0	1.1	1.6	2.8	0.1	0.1	0.1	0.0	0.0
Kuwait	15.7	0.5	0.8	1.7	2.5	2.5	0.1	0.1	0.1
Bonds	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Commercial creditors	522.7	18.1	25.9	20.1	34.3	32.9	1.0	1.6	1.4
BPI	88.5	3.1	4.4	1.6	5.7	5.2	0.1	0.3	0.2
Caixa Geral Déposito (CGD)	427.9	14.8	21.2	18.0	28.5	27.6	0.9	1.3	1.2
Other international creditors	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Domestic	837.2	29.0	41.5	93.5	97.1	96.8	4.6	4.5	4.1
T-Bills	5.1	0.2	0.3	0.0	0.1	0.0	0.0	0.0	0.0
Bonds	821.5	28.5	40.7	0.0	31.6	0.0	0.0	1.5	0.0
Loans	10.5	0.4	0.5	0.0	0.0	0.0	0.0	0.0	0.0

1/ As reported by Country authorities according to their classification of creditors, including by official and commercial. Debt coverage is the same as the DSA.
2/Multilateral creditors" are simply institutions with more than one official shareholder and may not necessarily align with creditor classification under other IMF policies (e.g. Lending Into Arrea
3/Debt is collateralized when the creditor has rights over an asset or revenue stream that would allow it, if the borrower defaults on its payment obligations, to rely on the asset or revenue secure repayment of the debt. Collateralization entails a borrower granting liens over specific existing assets or future receivables to a lender as security against repayment of the loan.
"unrelated" when it has no relationship to a project financed by the loan. An example would be borrowing to finance the budget deficit, collateralized by oil revenue receipts.
See the joint IMF-World Bank note for the G20 "Collateralized Transactions: Key Considerations for Public Lenders and Borrowers" for a discussion of issues raised by collateral.
4/Includes other-one off guarantees not included in publicly guaranteed debt (e.g. credit lines) and other explicit contingent liabilities not elsewhere classified (e.g. potential legal claims, payments resulting from PPP arrangements).

Table 8. Cabo Verde: Quantitative Performance Criteria and Indicative Targets Under the ECF, June 2022-June 2023[1]

(Millions of Escudos, unless otherwise indicated)

	2021		2022			2023
	end-December	end-June	end-September	end-December	end-March	end-June
	Actual	Performance Criteria (PC)	Indicative Targets (IT)	Performance Criteria (PC)	Indicative Targets (IT)	Performance Criteria (PC)
		Cumulative from the beginning of the calendar year				
Quantitative performance criteria						
Primary balance, floor [2]	-10,112	-4,635	-7,500	-7,750	-2,612.0	-4,141.0
Tax revenue, floor	33,542	16,916	27,161	38,215	9,550.1	19,095.0
Net other liabilities, ceiling [3]	-1,691	742	358	1,455	501.5	625.3
Net domestic financing, ceiling	3,142	6,388	7,100	7,501	5,651	5,886
Nonaccumulation of domestic arrears [4]	0	0	0	0	0	0
Non-accumulation of external payment arrears [4]	0	0	0	0	0	0
PV of new external debt, ceiling (in millions of US Dollars)	109	61	84	94	46	60
Nominal level of new nonconcessional external debt of central government, ceiling[4]	0	0	0	0	0	0
Gross international reserves (in millions of euros), floor [2]	591	560	557	491	554	572
Indicative Targets						
Social spending, floor	18,300	5,750 0	8,928	15,800	2,923	6,180
Non-quantitative continuous PCs						
Non-imposition or intensification of restrictions on the making of payments and transfers for current international transactions						
Non-introduction or modification of multiple currency practices						
Non-imposition or intensification of import restrictions for balance of payments reasons						
Non-conclusion of bilateral payments agreements that are inconsistent with Article VIII						
Memorandum items:						
Net onlending	1,181	515	1,530	2,790	4.9	101
Capitalization	838	1,363	1,763	2,151	300.0	765.3
Program assumptions						
Project and budget support grants	3,985	675	890	3,982	181.9	623.3
External debt service	5,906	5,665	9,281	11,226	3,664.8	6,445.4
Sales of assets	683	351	431	648	142.2	516.6
Project and budget support loans	11,024	4,125	10,188	14,333	913.9	5,887.7

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

[1] Expressed in local currency and millions unless otherwise indicated. Foreign currency amounts will be converted at current exchange rates.

[2] Stock of reserves in millions of Euros.The ceiling or floor will be adjusted as specified in the TMU.

[3] Net other liabilites includes net onlending, capitalization, and other assets.

[4] Continuous.

Table 9. Cabo Verde: Structural Benchmarks Under the ECF for 2022-23

Actions	Target date	Objective
Fiscal reforms		
Invoice electronically at least 50 percent of tax payers for VAT	End-December 2022	Improve revenue collection
is in line with commitments under the program.	End December 2022	Support fiscal and debt sustainability
Compile and publish historical series of government financial statistics for general	End-March 2023	Improve fiscal transparency
Publish annual budget execution reports for the general government.	End-September 2023	Improve fiscal transparency
SOEs reforms		
Conduct quarterly analysis of fiscal risk assessment using the IMF SOEs health check tool.	End-September 2022	Improve fiscal reporting and educe fiscal risks
Introduce a quarterly monitoring report on SOEs budget execution.	End-September 2022	Improve fiscal reporting and reduce fiscal risks
Improve the annual SOEs report to include comparison of execution to initial budget projection, evaluation of performance against medium term plan, data on government relations (transfers and liabilities).	End-July 2023	Improve fiscal reporting and educe fiscal risks
Monetary policy reforms		
Preannounce a schedule for TIM and TRM auctions.	End-June 2022	Support the development of the money market
Introduce a composite indicators of economic activity.	End-June 2023	Support monetary policy analysis
Financial sector reforms		
Submit draft amendments to the BCV Law, in line with IMF recommendations, to the Ministry of Finance with a view to (i) establishing an independent oversight process that is separate from executive management, (ii) strengthening the BCV's personal and financial autonomy, and (iii) enhancing transparency and accountability mechanisms	End-December 2022	Strengthen BCV institutional framework
Carry out a comprenhensive study of loan losses and provisions at the expiration of the credit moratorium.	End-December 2022	Strengthen financial stability
Develop a common framework for the resolution of crisis related NPLs.	End-December 2022	Strengthen financial stability

Table 10. Cabo Verde: Proposed Schedule of Reviews Under the ECF, 2022-25

Date Available	Amount (SDR millions)	% of Quota	Conditions Necessary for Purchase
15-Jun-22	11.26	47.50	Executive Board approval of ECF
15-Oct-22	11.26	47.50	Observance of end-June 2022 performance criteria and completion of the first review under under the arrangement
15-Mar-23	4.50	19.00	Observance of end-Dec 2022 performance criteria and completion of the second review under under the arrangement
15-Oct-23	4.50	19.00	Observance of end-June 2023 performance criteria and completion of the third review under under the arrangement
15-Mar-24	4.50	19.00	Observance of end-December 2023 performance criteria and completion of the fourth review under under the arrangement
15-Oct-24	4.50	19.00	Observance of end-June 2024 performance criteria and completion of the fifth review under under the arrangement
15-Mar-25	4.51	19.00	Observance of end-December 2024 performance criteria and completion of the sixth review under under the arrangement
Total	45.03	190.00	

Source: IMF staff estimates.

Note: Quota is SDR 23.70 million

Annex I. Performance Under the 2019 Policy Coordination Instrument

1. **Cabo Verde completed a three-year Policy Coordination Instrument in March 2021**. Macroeconomic performance under the program and prior to the outbreak of the global pandemic was strong. Real GDP growth reached 5.7 percent in 2019 with low and stable inflation. The growth momentum was supported by strong growth in tourism, transport, construction, and other services sectors. The Government's fiscal position improved with the overall fiscal deficit declining from 3 percent of GDP in 2016 to 1.8 percent of GDP in 2019. Fiscal consolidation, combined with sustained real GDP growth, helped reduce the public debt-to-GDP ratio modestly from 127.8 percent in 2016 to 125 percent in 2019. The external position strengthened substantially, with the current account deficit narrowing from 5.1 percent of GDP in 2016 to 0.4 percent of GDP in 2019, helping increase international reserves from €541 million in 2016 to €666.1 million in 2019.

2. **Performance over 2020-21 was challenging due to the effects of the pandemic (see discussion above), though the authorities took decisive action to protect lives and livelihoods**. In particular, all quantitative targets were met, except for the floor on tax revenues that was missed in the first and second reviews due to the sharp slowdown in economic activity. The primary balance target was met with a wide margin during the program primarily due to lower execution rate of public investment projects. All non-quantitative continuous targets were met throughout the entire program.

3. **Good progress was made in the area of structural reforms with most reform targets under the PCI met ahead of schedule**. In the area of fiscal reforms, the government enhanced the monitoring of the financial performance of public enterprises through the compilation of financial information on the cash flow performance and quarterly monitoring of actual performance of the six largest SOEs. Steps were also taken to streamline tax exemptions on customs duties, excises, and VAT to enhance revenue performance. In the area of monetary policy, the BCV strengthened the monetary policy transmission mechanism by narrowing the interest rate corridor, linking the policy rate to key interest rates, and enhancing monetary policy communication. The target on the installation of the software system to revamp the public credit registry was completed under the program, which will support the government's efforts to promote access to finance.

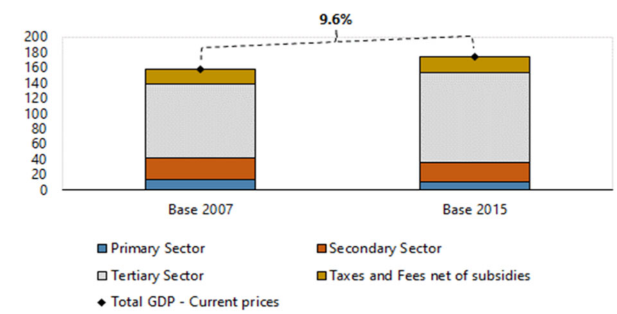
4. **The government's broader reform agenda under the strategic plan for sustainable development (PEDS) progressed well during the program period**. Key measures were introduced during June 2019-January 2021 aimed at (i) improving budgetary processes; (ii) restructuring SOEs to support growth and limit fiscal risks; (iii) improving the business environment; (iv) strengthening the anti-money laundering and combating the financing of terrorism (AML/CFT) framework; and (v) supporting financial sector development.

Annex II. GDP Rebasing

1. **In 2021 the National Statistical System (SEN) completed the benchmarking and rebasing of Cabo Verde's national accounts statistics (GDP)**. This involved changing the base year from 2007 to 2015 and the updated accounts were published in March 2022. The SEN started collecting data from new sources of information in 2015 that allowed for the shifting of the base year, which included:

- The General Census of Agriculture (V RGA), allowing an update on the sampling base of agricultural holdings and the agrarian structure.
- The III Survey on Households Expenses and Income (III IDRF), which allowed for the estimation of household final consumption, and provided data to update the consumer price index (CPI).
- The II Informal Sector Survey.
- Other short-term indicators such as: monthly foreign trade price index, quarterly indicator of service sector activity, and tourism prices index.

Figure 1. Cabo Verde: 2015 Output – Sector Share and Percent Change
(CVE billions)



2. **The benchmarking and rebasing led to an upward revision of GDP by 9.6 percent**. GDP increased to 173,911 million Cape Verdean escudos (CVE) in 2015—an increase of 15,212 million CVE, compared to the 2007 base. The primary and the secondary sectors shank by -2,721 million CVE (-19.6 percent) and -3,340 million CVE (-11.6 percent), respectively, whereas the tertiary sector increased by 20,743 million CVE (21.6 percent) (Figure 1). As a result, the tertiary sector which accounted for 13.1 percent of the upward revision now represents 67.2 percent of output. The decline in the contributions of the primary (1.7 percent) and secondary sector (2.1 percent), resulted in a decline in their weight in GDP to 6.4 percent and 14.6 percent respectively. The weight of taxes net of subsidies on products stood at 11.8 percent and contributed of 0.3 percent in the rebased GDP.

3. **Final consumer expenditure increased by 7.7 percent relative to the 2007 base and contributed 6.5 percent to the rebased level of GDP**. It moved from CVE 133,410 million in the 2007 base to CVE 143,704 million under the 2015 base. However, the weight of final consumer expenditure in GDP decreased from 84.1 percent in the 2007 base to 82.6 percent in the 2015 base.

4. **Gross fixed capital formation (GFCF) increased by 0.8 percent and contributed 0.2 percent to the rebased GDP**. However, the investment rate declined from 30.2 percent in the 2007 base to 29.1 percent in the 2015 base. Imports declined 2.1 percent and exports increased by 0.4 percent, resulting in an improved external balance which contributed 1.4 percent to the increase in GDP.

Annex III. Risk Assessment Matrix[1]

(Scale—high, medium, or low)

Source of Risks	Relative Likelihood[1]	Impact if Realized	Policy Response
Outbreaks of lethal and highly contagious COVID-19 variants	**Medium** Rapidly increasing hospitalizations and deaths due to low vaccine protection or vaccine-resistant variants force more social distancing and/or new lockdowns. This results in extended supply chain disruptions and a reassessment of growth prospects, triggering capital outflows, financial tightening, currency depreciations, and debt distress in some EMDEs.	**High** New variant outbreaks could disrupt the recovery in tourism and economic activity, with a negative impact on economic growth and the external and fiscal position.	• Enhance and optimize vaccination roll-out, focusing on high-risk population and critical areas. • Prioritize spending towards health sector. • Slow down planned unwinding of policy support while ensuring that recovery is well entrenched.
Geopolitical tensions, other disruptions and deglobalization.	**High** Intensified geopolitical tensions, war in Ukraine leads to escalation of sanctions, security risks, conflicts, and wars cause economic and political disruptions, refugee migration, fragmentation of the international monetary system, production reshoring, a decline in global trade, and lower investor confidence.	**High** The economy would be hit by disruptions in the supply chain, terms of trade and the tourism sector deteriorate resulting in the balance of payments problems and capital volatility, increase inflation leading to food insecurity and poverty.	• Create fiscal space through spending review and tax mobilization for new policies to mitigate supply shocks in the economy. • Prioritize and target public spending towards the most vulnerable people. • Diversify the economy. • Allocate additional grants and concessional loans to cover external needs.
De-anchoring of inflation expectations in the U.S. leads to rising core yields and risk premia	**Medium** A fast recovery in demand (supported by excess private savings and stimulus policies), combined with COVID-19-related supply constraints, leads to sustained above-target inflation readings and a de-anchoring of expectations. The Fed reacts by signaling a need to tighten earlier than expected. The resulting repositioning by market participants leads to a front-loaded tightening of financial conditions and higher risk premia, including for credit, equities, and emerging and frontier market currencies.	**Medium** Rising core yields and risk premia will increase the cost of new debt and add pressure foreign reserves and financial account due to a "Fly-to-quality" effect. Rising yields could also reduce the flow of migrant deposits.	• Take concessional debt with Bilateral and/or Multilateral creditors during high yield period. • Maintain a relatively large liquidity buffer and measures to keep domestic markets liquid. • Stand ready to tighten monetary policy.

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

Source of Risks	Relative Likelihood[1]	Impact if Realized	Policy Response
Rising and volatile food and energy prices	**High** Commodity prices are volatile and trend up amid supply constraints, the war in Ukraine, export restrictions, and currency depreciations. This leads to short-run disruptions in the green transition, bouts of price and real sector volatility, food insecurity, social unrest, and acute food and energy crises (especially in EMDEs with lack of fiscal space).	**High** Worsening of the current account, generating balance of payments problems. Commodity prices increase, especially in oil and food, joint with supply disruptions, leads to a higher inflation	• Build external buffers and resilience to shocks. • Diversification of energy usage (renewable energies transition), to mitigate oil price shocks.
Cyber attacks	**Medium** Cyber-attacks on critical infrastructure, institutions, and financial systems trigger systemic financial instability or widespread disruptions in socio-economic activities and remote work arrangements.	**Medium** Cyber-attacks could generate weaker confidence, cause instability in the financial system and disrupt domestic activity	• Strengthen information security particularly in the government sector. Improve financial regulation and supervision to enhance the resilience of the financial system.
Higher frequency and severity of natural disasters related to climate change.	**Medium** Higher frequency and severity of natural disasters cause severe economic damage to smaller economies susceptible to disruptions and accelerate emigration from these economies.	**Medium/High** Prolonged drought or other climate-related shocks would undermine agricultural production with negative impact on GDP growth and inflation.	• Build resilience to weather-related shocks and accelerate growth-enhancing reforms.
Faltering fiscal consolidation efforts.	**Medium/High** Less ambitious and slower fiscal consolidation efforts and delayed SOEs reforms after the health crisis.	**High** Delayed resumption of fiscal consolidation efforts and SOEs reforms after COVID-19 would undermine macroeconomic stability and hinder the return to pre-COVID medium-term fiscal and debt sustainability trajectory.	• Ensure that relief measures taken to address the impact of COVID-19 are temporary and, as soon as the health crisis abates, advance revenue-enhancing reforms, improve capital expenditure management, reduce fiscal risks, notably linked to SOEs, and contain non-priority spending.
Delays in implementing measures to increase productivity and restructure SOEs.	**Medium** Delays in structural reforms implementation, particularly in the public enterprises sector.	**Medium** Delays in advancing the structural reform agenda after COVID-19 would hinder competitiveness, potential GDP growth and employment.	• Follow through with SOEs reform plans and accelerate other structural reforms as soon as the epidemic subsides, to improve the business environment, reduce the State's role in productive activities and enhance growth potential.

[1]In case the baseline does not materialize.

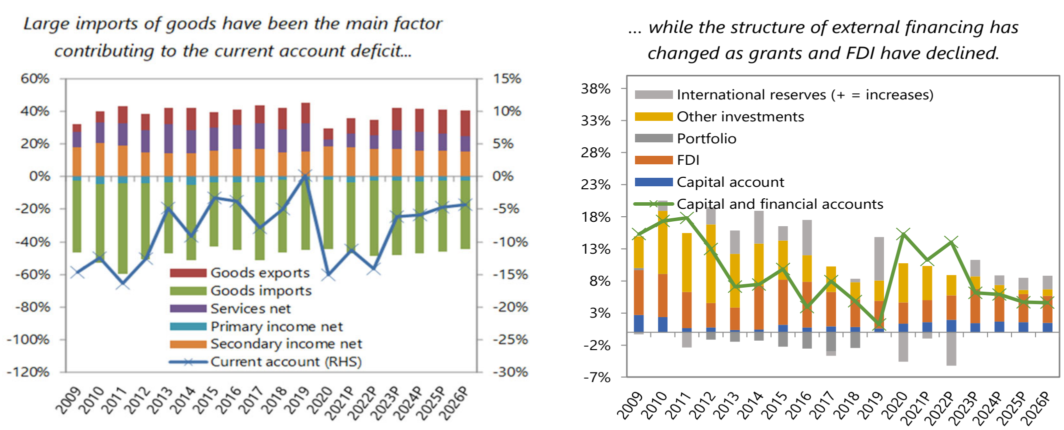
Annex IV. External Sector Assessment

Cabo Verde's external position in 2021 is assessed as substantially stronger than the level implied by fundamentals and desirable policy settings, which points to an undervaluation of the exchange rate. The high and negative net international investment position is a source of vulnerability, but the risks that it poses are partly contained by the structure of Cabo Verde's external liabilities, largely composed of FDI and long-term debt. Reserve adequacy is assessed as satisfactory, with actual reserve levels (6.3 months of imports) comfortably above the IMF LIC/MIC framework optimal level (about 3.7 months). Cabo Verde's business environment has improved in recent years, but continued structural reforms remain critical to enhance competitiveness.

A. Current Account

1. Background. The negative effects of the COVID-19 pandemic resulted in the current account deficit widening from 0.4 per cent in 2019 to 15.0 percent of GDP in 2020 (Text Figure 1). This reflected a large contraction in the exports of goods and services, largely driven by a 69.1 percent decline in tourism receipts. The large contraction in the exports of goods and services growth more than offset the 23.2 percent fall in imports of goods and services. Financial flows covered the largest share of the current account deficit in 2020. The current account deficit is estimated to have narrowed to 11.3 percent of GDP in 2021 (as export growth, tourism and remittances recover) but widens in 2022 as the war in Ukraine reverses the earlier gains. It is, however, projected to narrow and improve to 4.2 percent of GDP by 2027 supported by the expansion of tourism and the implementation of the fiscal consolidation program.

Text Figure 1. Cabo Verde: Balance of Payments, 2009–26
(Percent of GDP)



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

2. Assessment. The EBA-lite methodology is based on the current account (CA) model from a panel regression of the current account which generates an estimated "norm" consistent with medium-term fundamentals and desirable policies. The CA model shows that the cyclically adjusted current account balance is estimated at -6.0 percent of GDP in 2021 and the multilaterally consistent cyclically adjusted current account norm is -11.3 percent of GDP (Text Table 1). This suggests a current account gap of 5.8 percent of GDP. Using the estimated current account elasticities, this implies an undervaluation of the real effective exchange rate (REER) of about 16.3 percent. Nonetheless, the CA model does not fully capture Cabo Verde's need to save externally to guard against the country's vulnerability to natural disasters and is not robust to shocks of the magnitude experienced by Cabo Verde due to the COVID-19 pandemic.

B. Real Effective Exchange Rate

3. Background. Cabo Verde's REER has been relatively stable over the past decade and depreciated slightly by 1.2 percent in 2021 compared with an appreciation of 1.3 percent in 2020.

4. Assessment. The EBA-lite methodology is based on a REER panel regression model that generates an estimated "norm" consistent with medium-term fundamentals and desirable policies. The REER model suggests an undervaluation of the REER of about 7.3 percent (Text Table 1).

Text Table 1. Cabo Verde: Results from EBA-lite Assessment
(Percent of GDP)

	CA model	REER
CA-Actual	**-11.3**	
Cyclical contributions (from model) (-)	1.2	
COVID-19 adjustor (+) 1/	6.8	
Additional temporary/statistical factors (+)	0.0	
Natural disasters and conflicts (-)	-0.1	
Adjusted CA	**-6.0**	
CA Norm (from model) 2/	**-11.8**	
Adjustments to the norm (+)	0.0	
Adjusted CA Norm	**-11.8**	
CA Gap	**5.8**	**2.6**
o/w Relative policy gap	1.6	
Elasticity	-0.36	
REER Gap (in percent)	**-16.3**	**-7.3**

1/ Additional cyclical adjustment to account for the temporary impact of the tourism (6.8 percent of GDP).
2/ Cyclically adjusted, including multilateral consistency adjustments.

C. Capital and Financial Flows

5. Background. Private capital flows remained robust in 2021 at levels comparable to those recorded in 2020. The increase in 2021 reflected higher other foreign investments. The net financial account balance declined marginally from 15.3 percent of GDP in 2020 to 11.5 percent in 2021 on account of a slight decrease in net official borrowing.

6. Assessment. Net capital and financial flows are expected to slow down over the medium term and stabilize around 3 percent of GDP. The overall balance of payments is projected to record surpluses starting in 2022 in line with the projected improvement in the current account.

D. Reserve Adequacy

7. Background. The COVID-19 pandemic reversed the gains in gross international reserves recorded in 2019. Gross international reserves declined by €82.2 million to €582.4 million in 2020 as exports receipts and private capital flows declined due to the economic impact of COVID-19. Gross international reserves recovered to €591.3 million in 2021, bringing the coverage of prospective imports of goods and services to 6.3 months of prospective imports. Over the medium term, the coverage of prospective imports of goods and services is projected to remain stable between 5 and 5.2 months.

8. Assessment. The results from the Fund's LIC/MIC framework suggests that the optimal level of reserves for Cabo Verde is about 3.7 months of prospective cover of imports of goods and services. But the fragilities due to the small size of the economy, lack of export diversification, and vulnerability to exogenous shocks call for a higher level of reserves.[1] The staff's medium-term projections indicate a level of reserves of about 5 months of prospective cover of imports of goods and services, in the medium term.

E. External Balance Sheet

9. Background. Cabo Verde's net international investment position (NIIP, excluding short-term migrants' deposits) increased in 2021 to reach -201 percent of GDP. Gross external assets and liabilities stood at 90 percent of GDP and 291 percent of GDP, respectively. This persistently large negative external position is a significant source of external vulnerability.

10. Assessment. The external sustainability approach (ES) calculates the REER adjustment required to satisfy the inter-temporal budget constraint as a measure of the external adjustment required to restore external sustainability. The ES approach suggests that the NIIP does not deteriorate in net present value terms. This implies that no change in the REER is needed. However, this definition of sustainability is narrow and does not take into considerations all the vulnerabilities associated with the current level of the NIIP or the composition of the NIIP. Cabo Verde's high and negative NIIP position is a source of vulnerability particularly given its exposure to external shocks. Therefore, policies to reduce the level indebtedness are important to reduce overall external vulnerability.

F. Non-Price Competitiveness

11. Background. Cabo Verde's business environment has improved in recent years. However, there are several areas in which competitiveness could be further strengthened. Based on the World Economic Forum index,[2] Cabo Verde's overall score for global competitiveness increased to 50.8 in 2019 because of gains in human capital, particularly for health, labor markets and innovation capability. The country lost ground in ICT adaptation, product market and infrastructure (Text Table 2).

12. Assessment. Despite the achievements, decisive structural reforms aimed at improving the business environment and attracting private investment remain critical to boost competitiveness in Cabo Verde. Key areas in need of improvement include reliable power supply, access to finance, protecting minority investors, paying taxes and trading across borders.

[1] IMF Country Report No. 19/255.

[2] The World Economic Forum's Global Competitiveness Index combines both official data and survey responses from business executives on several dimensions of competitiveness.

Text Table 2. Cabo Verde: Global Competitive Indicators, 2019
0–100 (best)

	2018	2019	Change[1]
Overall score	50.2	50.8	0.6
Enabling environment component	55.8	54.9	-0.9
Institutions	51.5	51.2	-0.3
Infrastructure	54.7	53.7	-1.0
ICT adoption	48.1	44.7	-3.4
Macroeconomic stability	68.9	70.0	1.1
Human capital component	62.8	67.0	4.2
Health	75.6	80.8	5.2
Skills	53.3	53.2	-0.1
Markets components	46.2	46.9	0.7
Product market	52.8	50.1	-2.7
Labour market	57.6	61.4	3.8
Financial system	57.3	58.5	1.2
Market size	17.1	17.5	0.4
Innovation ecosystem component	32.7	34.4	1.7
Business dynamism	44.0	44.0	0.0
Innovation capability	21.4	24.8	3.4

Sources: World Economic Forum, Global Competitiveness Index.
[1]Negative sign indicates decrease in score.

G. Overall Assessment and Recommendations

13. **Results from staff's assessment of Cabo Verde's external position in 2021 suggest that the exchange rate might be slightly undervalued**. The three methodologies used: the external sustainability approach, the EBA-lite methodology based on the current account model and, the REER model point to an undervaluation of the real effective exchange rate. Nevertheless, the results should be interpreted with care as the degree of undervaluation is relatively modest and the country has large external liabilities that suggest the external position remains highly vulnerable to shocks.

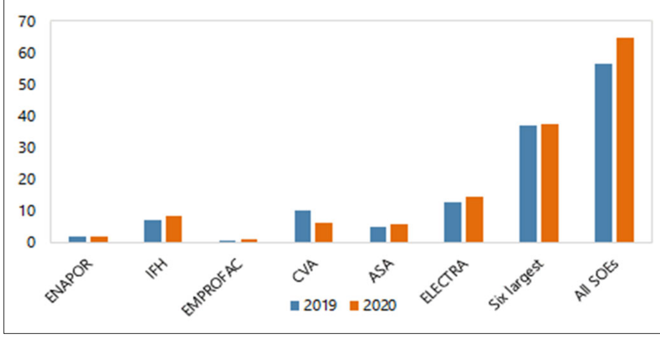
14. **Sustained medium-term fiscal consolidation and structural reforms are needed to support improvements in the external position**. Fiscal adjustment is expected to help lower external liabilities and support medium-term external sustainability. Continued implementation of structural reforms is also needed to reduce transaction costs, increase labor market flexibility, boost productivity, and support private sector development. Although the current level of reserves is assessed as adequate based on results from the application of the IMF LIC/MIC framework, building strong external buffers is critical given existing vulnerabilities, and the need to protect the peg.

Annex V. Public Enterprises Reforms: Progress and Next Steps

1. **Cabo Verde has several State-Owned Enterprises (SOEs) that have been facing important challenges in recent years**. These SOEs operate in a number of sectors, including transportation, utilities, housing, and pharmaceuticals. Performance challenges over the years have generated a need for government transfers to finance part of their operations. Financial support to SOEs has taken a variety of forms, including onlending, subsidies, and capitalization. This assistance to SOEs has been a major contributor to the rapid accumulation of public debt. Prior to 2018, fiscal risks were concentrated in the national airline (TACV), the real estate and housing company (IFH), and the electricity and water (ELECTRA) companies, which account for the largest share of SOEs' total liabilities.

2. **The government initiated the SOEs reform program in 2018 to restructure these companies and reduce support from the budget**. Key steps included: (i) the sale of majority shares in the national airline (TACV) to a strategic partner; (ii) the introduction of greater private sector participation in maritime inter-island transportation; (iii) the restructuring of ELECTRA to reduce its high commercial losses and prepare the company for privatization; (iv) the restructuring of the housing program managed by the IFH to minimize losses and increase transparency; and (v) the privatization of other SOEs.

Figure 1. Cabo Verde: Liabilities of SOEs, 2019-2022
(Percent of GDP)



3. **Key achievements on the privatization and restructuring fronts include**:

- The privatization of TACV was completed in March 2019 with the sale of 51 percent of the company's shares to a subsidiary of Icelandair, with costs for the government budget in terms of equity (1.3 percent of GDP), and debt service obligations. An additional 10 percent of shares was sold to employees and the Cabo Verde diaspora. In July 2021, the authorities reversed the privatization of CVA on the grounds of fiscal irresponsibility on the part of Iceland Air, following the exceptionally high financial uncertainty of the company.

- Public operation to sell 2.1 percent of the authorized capital that the government holds in ENACOL (oil and gas company), through the Cabo Verde Stock Exchange.

- The completion of the restructuring of the housing program managed by the housing company (IFH) in 2019 with the transfer of low-income houses (class A) to the municipalities. The granting of the concession for inter-island maritime transportation was also completed.

4. **The government also strengthened the monitoring of the six largest SOEs and the governance framework for the SOEs sector, including**:

- The compilation of financial information on cashflow performance of the six largest SOEs and the implementation of quarterly monitoring of actual performance of the six largest SOEs against their approved budgets.

- The design and implementation of a platform for monitoring the public enterprise sector, generating more and more accurate data on enterprises in the public enterprise sector to facilitate access by portfolio managers and the various stakeholders in the sector.

- The establishment of *PARPÚBLICA* as the company managing the state's corporate investments and *IMOPÚBLICA*, as the company managing the state's immovable property.

5. Going forward, the COVID-19 pandemic has weakened the momentum of the reform program, but the government has reasserted its intention to resume the restructuring and privatization of the major SOEs. These reforms are needed to support growth prospects, mitigate fiscal risks, and support debt sustainability. In this regard, the government intends to complete most of the operations in 2022-23. A new business plan is being developed for the national airline to guide its restructuring and the preparation of the company for privatization. The reform program also includes the granting of a concession for airports management (CV Handling) and licensing of port services (ENAPOR); the completion of the privatization of ELECTRA; the sale of the recently acquired state's shares in Caixa Económica; and the privatization and sale of shares in two companies in the pharmaceutical sector: INPHARMA and EMPROFAC.

6. Financial reporting and governance of the SOEs sector will be further enhanced through the implementation of a number of measures: (i) the adoption of the IMF's SOE Health Check Tool to streamline, strengthen the SOEs unit's (UASE) analysis and the assessment of fiscal risks stemming from SOEs; (ii) the provision of consolidated information on financial transactions between the government, individual SOEs and the sector in general, to strengthen transparency and facilitate fiscal risk analysis; (iii) enhancing the current annual reports on contingent liabilities, annual SOE performance and the initiation of the dissemination of quarterly reports on SOEs' performance, and (iv) adopting and publishing a comprehensive ownership policy to help further improve the ownership and oversight of the portfolio of SOEs.

7. These steps are important to set clear policy objectives guiding the management of each company and help contain fiscal risks. Staff will emphasize the importance of pursuing reform objectives without delay and will note that there are risks that delaying the restructuring process could undermine the implementation of the authorities' development strategy, compromise fiscal sustainability, and damage the business environment and the authorities' credibility to pursue robust policies that can help achieve higher and more sustainable growth.

Annex VI. Capacity Development Strategy

1. Capacity Development (CD) priority areas are aligned with the authorities' reform agenda under their medium-term development strategy (PEDS). Policies under the PEDS aim to raise broad-based growth, enhance the economy's resilience to shocks and support macroeconomic stability. CD activities focus on strengthening revenue mobilization, increasing efficiency in public expenditure, reducing fiscal risks, strengthening the monetary policy transmission mechanism, and improving the collection and dissemination of macroeconomic and financial statistics. The authorities' commitment to the implementation of CD recommendations is good, though hampered by limited administrative capacity and staffing constraints. The CD strategy aims to ensure adequate integration of CD recommendations with policy advice in the context of surveillance and program design. It also seeks to avoid the overlap of CD activities through enhanced coordination with IMF CD departments, AFRITAC West 2, and other CD providers.

2. Policy advice and reform targets under the new program build on some of the CD recommendations to support the authorities' engagement with development partners. The main CD priorities and objectives are summarized in the table below.

Priorities	Objectives	Challenges
Revenue administration	Improve custom administration core functions; strengthen management and governance arrangements at customs; enhance compliance with tax obligations; improve the quality of tax audits and inspections in the tax administration.	Staffing; lack of structured coordination between agencies.
Public Financial Management	Improve the integration of the asset and liability management framework; improve the coverage and quality of fiscal reporting; improve budget execution and control; strengthen identification, monitoring and management of fiscal risks; increase efficiency in public investment management (PIM), enhance public expenditure management (PFM).	Staffing constraints
Real Sector Statistics	Strengthen the compilation and dissemination of macroeconomic and financial data; complete the GDP rebasing.	Staffing constraints
Debt Management	Enhance analysis and management of public debt.	Staffing constraints
Central Bank Operations	Improve economic analysis and forecasting capacity; improve reserves management; enhance the effectiveness of monetary policy implementation.	Staffing constraints

Annex VII. Enhanced Safeguards for Cabo Verde

1. One of the main objectives of Cabo Verde's request for a Fund-supported program is to reduce debt vulnerabilities, including those stemming from the pandemic and the ongoing Ukraine war. Cabo Verde is assessed to be at a high risk of overall debt distress but moderate risk of external debt distress. The high risk of overall debt distress is largely due to the high stock of debt; however, the debt is on highly concessional terms with low average interest rates of about 1 percent and favorable maturity structure. The high risk of debt distress is due to persistent but progressively smaller breaches of the PV of total debt to GDP ratio during the program period (Annex VII, Figure 1 and 2), however, the deviation from the threshold narrows by a large margin during the program period. Debt vulnerabilities will be reduced under the program, as indicated by the downward path of the PV of total debt to GDP ratio over the course of the program, underpinned by fiscal adjustments (revenue and expenditure measures), and limits on non-concessional debt and, reforms of SOEs along with the prospective economic benefits from the expected recovery of the tourism sector, which is projected expected to support robust medium-term growth. The baseline overall debt-to-GDP indicator remains above the DSA threshold until the late 2020s, reflecting the initial high stock of debt, lingering effects of the pandemic and the effects of the Ukraine war. The external debt service indicators (relative to exports and revenues) are projected to remain comfortably below the DSA thresholds over the medium term and on a persistent downward trajectory during the medium term. To further reduce the stock of public debt, the authorities are in intense discussions with a bilateral creditor (Portugal) that could result in debt relief on a voluntary basis of up to 15 percent of GDP.

2. The size of Cabo Verde's de facto senior debt plus other multilateral and collateralized debt as a share of total external debt is above 50 percent at program initiation. It is projected to remain broadly stable at about 53 percent over the medium term under the baseline projection (Text Table 1). These ratios are below the mean and median for PRGT programs and indicate a significant buffer of restructurable debt. At program initiation, debt held by International Financial Institutions (IFIs) with global membership —the IMF, World Bank, and AfDB—accounts for 41.6 percent of external debt; adding debt held by other multilaterals and collateralized debt brings the total to 54.2 percent. The combined share of such debt is projected to remain at about 53 percent of external debt by 2025. Total multilateral plus collateralized debt as a share of GDP is projected to decline significantly under the program, from 55 to 44.9 percent.

3. Cabo Verde's capacity to repay the Fund is assessed to be adequate (Figure 1). By 2025, Cabo Verde's Fund credit outstanding will be at 280 percent of quota (above the top quartile of past UCT-quality arrangements for LICs). Credit outstanding during the program would peak at about 3.6 percent of GDP, 10 percent of exports, 13.8 of gross international reserves and 14.5 percent of revenue (excluding grants). At the same time, annual repayments to the Fund would peak at 0.6 percent of exports, 0.9 percent of reserves, and almost 6.1 percent of PPG external debt service. Risks are mitigated by the authorities' strong track record of servicing their debt obligations to the Fund, and policy measures envisaged in the program, including envisaged fiscal consolidation. The return of tourists to the country is also likely to generate significant repayment capacity through increased export receipts.

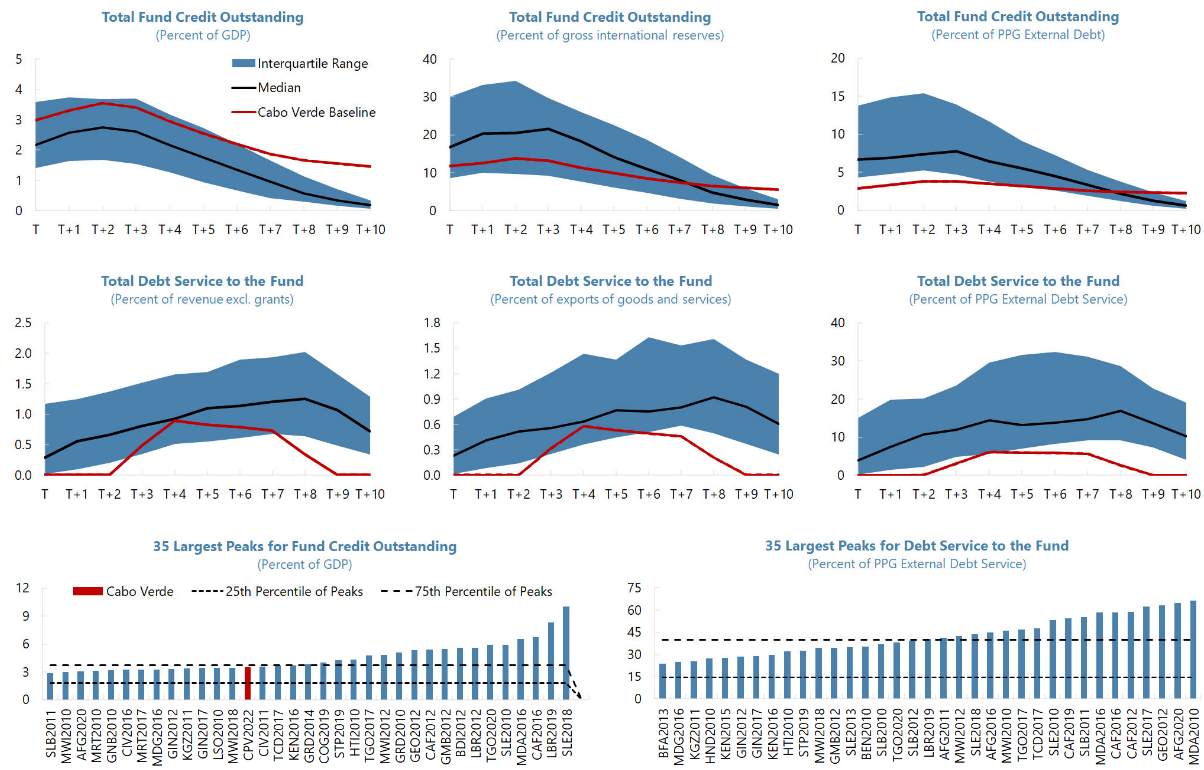
Text Table 1. Cabo Verde: Debt Composition 2021-25
(Millions of USD, unless otherwise specified)

	Actual	*Projections*			
Creditor Profile	2021	2022	2023	2024	2025
Total debt /1	2885.2	3167.1	3312.5	3423.6	3477.8
External debt	2048.0	2290.9	2392.6	2482.7	2566.8
Multilateral creditors	1109.4	1194.1	1258.5	1313.7	1355.2
o/w IMF and WB	590.8	650.0	697.4	745.2	782.1
o/w IMF	67.5	98.2	111.6	125.1	128.9
o/w AfDB	263.2	246.1	245.0	223.7	203.3
o/w Other Multilaterals	255.4	298.0	316.0	344.8	369.8
Bilateral creditors	418.9	448.6	492.4	540.6	587.9
o/w Paris Club	228.7	250.3	298.7	352.1	404.4
o/w Non-Paris Club	188.3	198.3	193.6	188.6	183.5
Private creditors	522.7	520.8	518.6	516.4	514.3
o/w Bonds	88.5	94.5	94.1	93.7	93.3
o/w Loans	427.9	426.3	424.5	422.8	421.0
Domestic Debt	837.2	876.1	919.9	940.9	911.1
Nominal GDP (USD billions)	2.0	2.4	2.6	2.8	3.0
Multilateral and collateralized debt					
Multilateral debt /2	1109.4	1194.1	1258.5	1313.7	1355.2
Percent of external debt	54.2	52.1	52.6	52.9	52.8
Percent of GDP	55.0	50.3	48.7	46.8	44.9
o/w IMF and WB	590.8	650.0	697.4	745.2	782.1
Percent of external debt	28.8	28.4	29.1	30.0	30.5
Percent of GDP	29.3	27.4	27.0	26.6	25.9
o/w AfDB/ADB/IADB	263.2	246.1	245.0	223.7	203.3
Percent of external debt	12.8	10.7	10.2	9.0	7.9
Percent of GDP	13.0	10.4	9.5	8.0	6.7
o/w Other Multilateral	255.4	298.0	316.0	344.8	369.8
Percent of external debt	12.5	13.0	13.2	13.9	14.4
Percent of GDP	12.7	12.6	12.2	12.3	12.2

1/ Data should be derived from the Debt Holder Profile table as reported by country authorities (see Table 1 in DLP GN), while the projections should be based on the LIC-DSA analyses.
2/ Teams may decide to aggregate at the level of multilaterals for the projection period and decide when to stop filling out the projections. When there are concerns with the quality of projections, teams do not need to provide data for the following four lines: ADB/AfDB/IADB, other multilaterals, Paris Club and non-Paris Club; and in cases where the team cannot project WB credit, that may also be left blank.

Figure 1. Cabo Verde: Capacity to Repay Indicators Compared to UCT Arrangements for PRGT Countries

(Percent of the indicated variable



Notes:

1) T = date of arrangement approval. PPG = public and publicly guaranteed.

2) Red lines/bars indicate the CtR indicator for the arrangement of interest.

3) The median, interquartile range, and comparator bars reflect all UCT arrangements (including blends) approved for PRGT countries between 2010 and 2020.

4) PRGT countries in the control group with multiple arrangements are entered as separate events in the database.

Appendix I. Letter of Intent

Praia
June 02, 2022

Madame Kristalina Georgieva
Managing Director
International Monetary Fund
Washington, D.C., 20431
U.S.A

Madame Managing Director:

We would like to thank you and the IMF for your support during the global health crisis. The timely approval of the disbursement under the Rapid Credit Facility in April 2020, and the active role the IMF played in facilitating relief under the G-20 Debt Service Suspension Initiative (DSSI), provided much needed emergency financing to bolster Cabo Verde's response to the global pandemic. More recently, the new SDR allocation provided additional funding for critical health, education, and infrastructure priorities for the recovery of the economy.

Prior to the global pandemic, considerable achievements under the Government's ambitious reform agenda reduced our country's vulnerabilities and improved its prospects for sustainable, inclusive, and private sector-led growth. In fact, economic growth was robust, fiscal deficits and public debt were on a clear downward trend, the external position improved, and international reserves were comfortable.

The global pandemic reversed some of these gains and delayed the implementation of planned reforms as the Government had to focus its attention on fighting the health and economic consequences of the pandemic. Reflecting travel restrictions and other COVID-19 containment measures, activity in the crucial tourism and transportation sectors was significantly affected. The fiscal and external positions weakened due to revenue losses, the need for pandemic-related financial support to businesses and households, and lower tourism receipts. The public debt-to-GDP ratio, which declined steadily until 2019, rose by more than 20 percentage points (to 143 percent in 2020) because of higher fiscal deficits and lower GDP.

In response to the global pandemic, a series of fiscal and monetary policy measures were introduced in Cabo Verde to preserve lives and sustain livelihoods. In addition, one of the most successful vaccination programs in sub-Saharan Africa was launched with over 95 percent of the adult population having received one dose and about 85 percent fully vaccinated having received two doses of the vaccine. These actions have set the stage for the ongoing recovery in economic activity and paved the way for an acceleration of reforms.

However, Cabo Verde's robust recovery, which started in 2021, is under threat due to the spillover effects of the war in Ukraine. The steep increase in international energy and food prices and weakened growth outlook for the world economy, including the euro area, is expected to affect Cabo Verde's near-term growth prospects, and weaken our fiscal and external positions. As a result, international reserves will come under pressure and challenge the pegged exchange rate regime that has served the country well.

To maintain economic and financial stability while anchoring the Government's reforms and cushioning the effects of the war in Ukraine, we request IMF support for the implementation of our economic and structural reform program under the Extended Credit Facility (ECF) for the period June 2022–June 2025 in the amount of SDR 45.03 million (190 percent of quota). The attached memorandum of economic and financial policies (MEFP) and supporting technical memorandum of understanding (TMU) outline the program's objectives and presents the policies that the Government and the Central Bank of Cabo Verde intend to implement to reach those objectives.

The ECF-supported program will provide a framework for the implementation of reforms set forth in the Government's Sustainable Development Strategy 2022-2026 (PEDS), which seeks to develop inclusive tourism, benefitting all the islands; transform Cabo Verde into an air transportation hub and international business center; create an international finance platform; develop a digital platform for technological innovation; create a special economic zone for the maritime economy (blue economy); development of wave energy and desalination technologies and support investment opportunities developed locally or by the diaspora.

Our economic and reform program also aims at preserving public debt sustainability and strengthening public finances; modernize, enhance and strengthen the monetary policy framework and maintaining an adequate level of international reserves; enhancing further the resilience of our financial system; accelerating state-owned enterprise reforms; enhancing existing mechanisms to protect the most vulnerable; and broadening the foundations for improved resilience to climate change, natural disasters, and other exogenous shocks.

The implementation of the ECF-supported program will be monitored through performance criteria, indicative targets, and structural benchmarks, as described in the MEFP and TMU. There will be semi-annual reviews of the program by the IMF to assess progress in program implementation. We believe that the policies set forth in the MEFP are adequate to achieve the objectives of the ECF-supported program. Nonetheless, we stand ready to take any additional measures that may prove necessary to reach the expected results. We will provide the IMF with all information requested to assess progress in the implementation of the program.

We stand ready to take additional measures, as appropriate, to achieve the objectives of the program. We will consult with IMF staff before adopting such measures, or in advance of revisions to the policies contained in this MEFP, or before adopting new measures that would deviate from program goals, consistent with IMF policies on such consultations

We authorize the publication of this letter of intent and the attached MEFP and TMU, as well as the forthcoming staff report for the request for a program under the ECF. We will also post these documents, including their Portuguese versions, on the Government's official webpage.

Sincerely,

/s/	/s/
Olavo Correia	Óscar Santos
Vice Prime Minister and Minister of Finance and Business Development	Governor of the Banco de Cabo Verde

Attachments: Memorandum of Economic and Financial Policies
Technical Memorandum of Understanding

Attachment I. Memorandum of Economic and Financial Policies for 2022–2025

This memorandum sets forth our economic and financial policy commitments to support the request for a 36-month arrangement under the Extended Credit Facility (ECF) of the International Monetary Fund. The program will be geared towards maintaining economic and financial stability, reducing vulnerabilities to external shocks, and strengthening the prospects for higher, sustainable, and inclusive growth. The main objectives of the program include: (i) strengthening public finances to increase fiscal space for promoting investment in catalytic sectors, as well as promoting social inclusion and reduce fiscal risks from public enterprises by strengthening their financial management and transparency; (ii) modernization of the monetary policy framework and strengthening the financial system, and (iii) raising growth potential and building resilience to shocks including climate related events.

BACKGROUND AND RECENT ECONOMIC DEVELOPMENTS

1. **Cabo Verde has emerged as a strong reformer and is a top performer on governance in Sub-Saharan Africa**. Cabo Verde's strong track record was enhanced during the PCI arrangement which was concluded in 2021. The PCI program which aimed to enhance macroeconomic stability helped support our medium-term objectives for fiscal and debt sustainability as well as a broader reform agenda under our Strategic Plan for Sustainable Development (PEDS). Significant progress was made prior to the COVID-19 pandemic on the reform agenda particularly in improvements of budgetary and regulatory processes, digitalization and enhancement of the business environment.

2. **Cabo Verde achieved high rates of economic growth during the pre-pandemic period, fiscal policy was sound, the external position was strong, and inflation was moderate**. Led by the fast-growing tourism sector, with the implementation of the PEDS, annual average growth of about 4.7 percent was recorded during the period 2016-2019. Sound fiscal policies, supported by reforms, resulted in a gradual improvement in the fiscal position and debt was placed on a downward path. The balance of payments improved, as FDI into the tourism sector increased, tourism receipts improved, and remittances emerged as a stable source of foreign exchange. As a result, gross official reserves increased to 9.0 months of prospective imports cover by end 2019.

3. **This impressive economic performance was adversely impacted by the pandemic which severely weakened economic activity**. Output contracted by about 15 percent in 2020, the largest contraction in Cabo Verde's post-colonial history. Stringent travel restrictions and other COVID-19 containment measures reduced activity in the critical tourism and transportation sectors and generated negative spillovers to other domestic sectors. This was accompanied by a large

deterioration in the fiscal account partly due to increased spending in response to the pandemic, form a deficit of 1.7 percent of GDP in 2019 to 9.1 percent of GDP in 2020 and public debt rose to 142.6 percent of GDP in 2020—an increase of over 20 percentage points relative to the previous year—although a very significant share of it is at highly favorable concessional terms. The external current account weakened sharply to a deficit of 15 percent of GDP in 2020, despite the decline in imports and stable remittances, on account of a very steep, unprecedented contraction in tourism receipts.

4. **Our strong policy buffers allowed for a swift and comprehensive response to mitigate the impact of the global pandemic through the implementation of a series of fiscal and monetary policy measures**. In that regard, our 2020 budget was revised, to expand expenditures on health and social protection programs. The Government also provided support to businesses that were heavily impacted by the pandemic through: loan guarantees amounting to CVE 4 billion; a moratorium on the payment of corporate income tax and the VAT; a temporary reduction in the VAT rate for the tourism sector to 10 percent; and the cancellation of contributions to the pension fund. The central bank also played a major role and implemented measures to maintain liquidity in the banking system and support credit extension while safeguarding financial stability. Key policy measures included: lowering of the policy rate; reduced minimum reserve requirements; lowering of the overnight deposit rate and permanent lending rate; establishment of a long-term financing facility for banks and a targeted moratorium on loan repayments. The fiscal and monetary policy interventions were initially intended to expire at the end of 2020, however, due to the duration of the pandemic, some of the measures were extended to June 2022.

5. **Our policy interventions along with a highly successful vaccination program helped mitigate the adverse impact of the pandemic and paved the way for a strong recovery**. As a result, economic growth rebounded to 7 percent in 2021. The recovery in output reflected the base effect associated with the re-opening of the economy and improvements in the tourism sector, particularly during the fourth quarter, which was aided by one of the fastest COVID-19 vaccine rollouts in sub-Saharan Africa. About 98 percent of the adult population have received at least one vaccine dose with vaccination rates close to 100 percent in some of the tourism islands, and 84.5 percent are already fully vaccinated. The rebound in economic activity was broad based as all sectors recorded an uptick in activity, with construction rebounding strongly on account of continued FDI into the tourism sector and continued implementation of the public investment program. Inflation accelerated in 2021 to 5.4 percent (y/y) in December due to higher food and energy prices but was below the inflation rate recorded in many countries, including some advanced economies.

6. **The external position improved in 2021 as exports rebounded**. The external current account deficit is estimated to have narrowed from 15 percent of GDP in 2020 to 11.3 percent of

GDP in 2021 as exports increased and recovered from the contraction recorded in 2020. The strong rebound in exports more than offset the 10 percent increase in the imports of goods and services that supported the economic rebound. Gross international reserves increased from €582.4 million in 2020 to €591.3 million in 2021 (about 6.3 months of prospected imports) supported by the SDR allocation, external loan disbursements, and financial flows associated with the recovery in tourism receipts.

7. Fiscal performance in 2021 was better than anticipated. Total revenues decreased by 0.2 percent as the pandemic continued to impact consumption and corporate incomes. However, prudent execution of the public investment program and current expenditure restraint ensured a better-than-projected improvement in the overall fiscal balance. Capital expenditure remained relatively stable at about 2.6 percent of GDP; 3.7 percent of GDP lower than budgeted as the Government focused on the implementation of high priority projects. Current expenditure restraint (mainly on goods and services and wages) reflected in part the start of the unwinding of COVID-19 related expenditures. As a result, the overall fiscal deficit is estimated at 7.3 percent of GDP in 2021 compared to 9.1 percent of GDP in 2020, and about [0.8] percent of GDP below the 2021 budget. The deficit was financed through a combination of external disbursements (about 70 percent) and the domestic financial system (about 30 percent). The stock of public debt stood at 143 percent of GDP at end 2021.

8. The execution of COVID-19 related expenditures has strictly followed the Government's transparency and accountability practices. The Government has published on a daily basis the execution of COVID-19 related expenditures on the official website of the Ministry of Finance (MOF) (www.mf.gov.cv/web/dnocp). In addition, in line with public financial management guidelines, all expenditures related to fighting the pandemic have been audited by the Court of accounts. We have also prepared a policy paper guiding the use of the recent SDR allocation. A number of projects that represent a substantial part of Cabo Verde's development plans (Cabo Verde Ambition 2030) have been selected for financing from SDR resources in 2022 and 2023. The projects are in the broad areas of health; agriculture and environment; education and culture; and infrastructure, land use planning, and housing with a total value of CVE 3 billion (about 1.7 percent of GDP). The transfer of the SDR resources from the BCV to the government was completed in 2021 and the amount has already been included in public debt. A memorandum of Understanding (MoU) detailing the framework for the use of the SDRs was signed between the Ministry of Finance and the Banco de Cabo Verde (BCV).

9. Developments in the monetary sector have been positive. Credit to the economy grew by 5.8 percent in 2021. This increase reflected the impact of the moratorium and the emerging growth in credit to the private sector, in particular tourism and construction, as the recovery gained momentum. In 2021, migrant deposits rose compared with 2020, as the Cabo Verdean diaspora has continued to display confidence in the financial system.

10. Monetary policy has been accommodative since the onset of the COVID-19 pandemic. Following the reduction in 2020 in the policy rate to 0.25 percent, minimum reserve requirement to 10 percent, the overnight deposit rate to 0.05 percent, and the permanent lending rending rate to 0.05 percent, the Central Bank of Cabo Verde (BCV) has maintained these rates through to June 2022 in part to help support the recovery. Interest rates on deposits, including migrant deposits, declined to 0.7 percent at end 2021 (1.9 percent at end 2020), while lending rates remained broadly stable at just under 9 percent.

11. The financial system has remained resilient. Data for end 2021 suggest that the financial system is highly liquid, profitable, and well capitalized. The banking sector entered the pandemic with strong capital buffers and improving profitability that helped contain risks. Regulatory capital to risk weighted assets (CAR) was 21.1 percent at end-December 2021, well-above the regulatory minimum of 12 percent; and the return on assets was at 1.5 percent. Non-performing loans (NPLs) declined from 9.5 percent at end 2020 to 7.2 percent of total loans at end December 2021 reflecting the moratorium on loan repayments and write-off of legacy loans.

MACROECONOMIC OUTLOOK

12. The economy was well poised to sustain the recovery momentum into 2022 but global economic uncertainty due to the war in Ukraine will weigh heavily on the economic outlook. Real GDP growth, which was expected to remain robust at 6 percent in 2022, has been revised downwards to 4 percent. This reflects the effects of the war in Ukraine and related sanctions on Russia, that have resulted in a sharp increase in international energy and food prices, and lowered growth prospects in the world, including in the euro area. These developments are expected to dampen somewhat the recovery in the tourism sector, and higher prices are likely to weaken domestic demand. However, over the medium-term growth is expected to return to robust levels supported by the continued recovery of the tourism sector towards the pre-pandemic levels and an increase in hotel room capacity. In addition, the successful implementation of key programs under the PEDS (2022-2026), and other structural reforms, particularly of the state-owned enterprise (SOE) sector, would raise growth potential for Cabo Verde. Over the long-term, GDP growth is projected at about 4½ percent, broadly in line with potential growth potential. Annual inflation is projected at about 2 percent, on average, after 2023, broadly in line with the euro area average.

13. The primary fiscal balance would improve by about 1 percent of GDP per year during 2023-2026, reflecting both revenue mobilization efforts and expenditure rationalization. The planned fiscal consolidation, a successful restructuring of the major SOEs, and other structural reforms are expected to lead to faster growth of credit to the private sector, boost investor confidence, accelerate medium-term growth, and place public debt on a sustained downward path. The external current account deficit is projected to narrow to about 4.2 percent of GDP in the medium-term supported by fiscal consolidation, strong tourism performance, and higher remittances reflecting labor market improvements in advanced economies. Supported by Fund financing, improved tourism receipts and remittance inflows international reserves will remain at about 5 months of prospective imports.

ECONOMIC POLICIES AND STRUCTURAL REFORMS UNDER THE PROGRAM

A. Strengthening Public Finances: Preserving Public Debt Sustainability, Expanding Social Safety Nets and Strengthening the Fiscal Framework

14. One of the keystones of our fiscal program is a significant frontloaded adjustment in 2022 followed by a more gradual but sustained consolidation effort over the medium term. This will be instrumental to place public debt on a sustained downward path, preserve debt sustainability and reduce the risk of debt distress. Other components of the strategy include strengthening the fiscal framework, and accelerating reforms in the SOE sector. Overall, these policies would result in an improvement in the primary fiscal balance from a deficit of 5.1 percent of GDP in 2021 to a surplus of about 1 percent of GDP in 2027; the overall fiscal deficit would decline from 7.3 percent of GDP in 2021 to about 1 percent of GDP over the same period. A large component of the adjustment in 2022 is based on the implementation of a carefully selected set of revenue measures. The implementation of the fiscal consolidation plan would be associated with a reduction in public debt levels, with the debt-to-GDP ratio declining from 143 percent in 2021 to 109.6 percent in 2027.

15. The 2022 budget was initially designed to be consistent with a reduction in the primary fiscal deficit from 5.1 percent of GDP in 2021 to 4 percent of GDP in 2022. This adjustment would be achieved through a combination of higher revenue and lower expenditures. However, with the change in the near-term economic outlook and a more conservative assumption on the likely intake from other revenues, the overall projected revenue intake has been revised to 25.4 percent of GDP, still 3 percent of GDP higher than in 2021 but 1.8 percent of GDP below the budgeted amount. Relative to the 2021 outturn, strong gains are expected on taxes on goods and services and on income and profits. Current expenditures, which were budgeted to increase by about 1.3 percent of GDP, are now projected to increase by 0.7 percent of GDP. Wages are projected to decrease while spending on existing social programs will be augmented by 0.3 percent of GDP to help mitigate the impact of higher prices on the most vulnerable. Capital expenditure was budgeted at 5 percent of GDP, about 2.4 percent of GDP above the outcome for 2021, but in line with a stricter prioritization of capital spending and implementation capacity it is now projected to increase to 3.7 percent of GDP. As a result of these changes, the primary fiscal deficit is now projected to improve to 3.6 percent of GDP in 2022.

16. Budgeted financing needs which were initially projected to increase in 2022 have been revised downwards. Budgeted financing needs were initially 2.3 percent of GDP higher than the outturn for 2021 but are now projected to increase by about 1.7 percent of GDP, partly due to weaker revenues and recapitalization of SOEs. Domestic funding under the 2022 budget is higher than the revised projections. The revised domestic financing requirements are above the 3 percent of GDP ceiling in light of the suspension of the fiscal rule in 2022 in line with the escape clause. External financing will be filled mostly with concessional and partially concessional loans, mainly from multilateral institutions, including the World Bank (1.3 percent of GDP), African Development Bank (1 percent of GDP), a drawdown of the recent SDR allocation (0.9 GDP), the resources provided under the ECF program, and official creditors.

B. Revenue Measures

17. We will introduce a set of carefully selected revenue policy and administration measures which is expected to yield about 1 percent of GDP in 2022. Key tax policy measures include (i) the introduction of electronic invoicing which is expected to yield 0.2 percent of GDP; (ii) the imposition of a 5 percent import duty on previously exempted goods such as business furniture and equipment, which should also generate a gain of 0.2 percent of GDP; and (iii) the increase in the excise tax on tobacco by 75 percent, with revenue gains of 0.2 percent of GDP. Furthermore, revenue administration improvements are expected to yield an additional 0.4 percent in revenues, mainly through collection of tax arrears and heightened supervision.

18. In the near- and medium-term, we will continue our efforts to enhance the efficiency of the tax system through revenue administration improvements. We will focus our efforts on the collection of VAT, as well as personal and corporate income tax arrears. These efforts will be based on the complete digitalization of all the revenue administration and collection processes and could potentially result in very significant gains in efficiency. The ongoing initiative towards completion of the electronic invoicing system is due to be completed by end 2023. In this regard, by end 2022 we will have in place an electronic invoicing system covering at least 50 percent of taxpayers for VAT **(Structural Benchmark)**. The integrated safety system which alerts of non-compliance of VAT and income tax was suspended during the pandemic but will now resume and be extended to other taxes. These reforms, including through improved compliance, is expected to yield an additional 2 percent of GDP over the medium term. The implementation of the ECOWAS common external tariff is expected to yield about 1 percent of GDP in additional revenues. The government will submit to parliament the budget for 2023 that will be in line with commitments under the program **(Structural Benchmark)**.

C. Expenditure Policies

19. We will continue to rationalize current expenditure and improve the delivery of investment spending. In the near-term, current spending will remain broadly stable but, over the medium-term, we will continue to seek efficiency gains while reducing spending on wages and interest payments, resulting in a gradual decline in current expenditures as a share of GDP. To support the recovery and the development needs of Cabo Verde, the public investment program is projected to increase as a share of GDP. However, capital expenditure will be strictly prioritized.

20. We will review and streamline social welfare programs to ensure adequate coverage particularly in the context of rising prices which disproportionately affect the most vulnerable. The sharp increase in international energy and food prices which has spilled over to domestic inflation will have a disproportionate impact on the vulnerable. To protect the poor and vulnerable, the Government will augment funding for social programs by 0.2 percent of GDP as a way of decreasing extreme poverty.

21. We recognize that to achieve our medium-term fiscal objectives additional policy measures will be required. As a result, the Government will continue to implement measures to improve revenue mobilization and public expenditure management, as well as continued SOE reforms to maintain medium-term debt sustainability. However, the downward adjustment of expenditure as a share of GDP over the medium term would not be associated with a decline in service delivery as the Government plans to focus its efforts on improving the efficiency of public spending. Our aim is to return to the pre-pandemic levels of spending in the medium term.

D. Fiscal Reforms

22. The Government is committed to improving the efficiency of the public investment framework. Public investment is a key component of our development plan and will play a critical role in supporting the recovery. In line with recent IMF technical assistance (TA) recommendations, we will develop a plan to bring about better projects in the near- to medium-term which would be both feasible and practical. This would involve the following four steps: (i) redefining the existing thresholds to reduce the number of projects qualifying for more detailed appraisal in line with available capacity; (ii) developing and implementing an enhanced pre-screening system (pre-screening+), a single-entry point for all project ideas regardless of size or source of financing; (iii) developing and implementing multi-criteria analysis (MCA) techniques and matrices for prioritization and selection; and (iv) developing and implementing a pre-implementation checklist.

23. We will build on the recent improvements in cash flow management that helped the Ministry of Finance to manage the challenges posed by COVID-19. In recent years, we have developed a Treasury Single Account (TSA) in line with sound international practices, that benefited from our early and successful adoption of a modern financial management information system (SIGOF). Despite the gains that have been achieved, other steps will be taken to enhance cash flow management, including continuing the process of bringing in all central government accounts into the TSA; and institute a cash coordination committee to systematically review forecasts.

24. We will advance plans towards broadening the fiscal coverage to allow for the preparation of accounts at the level of the general government. This includes the compilation and publication of the historical series of government financial statistics for the general government **(Structural Benchmark)**; publication of annual budget execution reports for the general government **(Structural Benchmark)**.

25. We will intensify efforts to reduce SOE related fiscal risks. In this regard, special focus will be placed on reinvigorating SOE reforms, including improving the framework for monitoring the financial performance of SOEs to reduce fiscal risks and thus support medium-term debt sustainability. Quarterly analysis of fiscal risk assessments using the IMF SOE's health check tool will be prepared, as well as quarterly monitoring report of SOEs' budget execution **(Structural Benchmark)**. These reforms would also include publication of quarterly consolidated transaction and financial flows between the government and SOEs on an individual and aggregate basis to help identify indirect support from the government to SOEs. Furthermore, the annual SOEs' report will be improved to include comparison of execution relative to the initial budget projection, evaluation of performance against medium-term plans, and data on government relations **(Structural Benchmark)**.

26. Cabo Verde Airlines (CVA) is a key priority, and the Government intends to complete the reorganization of CVA and resume its privatization efforts. The CVA privatization process, which commenced in 2019, was aborted due to concerns with the strategic partner, which resulted in the Government having to take over ownership of the airline. The Government is in the process of reorganizing the airline and is in negotiations with potential partners. Under the new plan, CVA will start operations with two aircrafts in 2022, with the number of airplanes in operation increasing to three in 2023. The airline will fly to [four international cities] which would be sufficient (based on our projections) to achieve breakeven by March 2023. The Government will provide financing during the reorganization process to cover the projected financing gap in the amount of €30 million (about 1.7 percent of GDP). We will seek Cabinet approval of (i) the least cost structure for CVA; and (ii) the long-term strategy that lays out the options for CVA, in consultation with the World Bank.

E. Public Debt

27. We will continue our efforts to ease Cabo Verde's public debt burden. We have already reached an agreement with Portugal to continue receiving debt service relief in line with the DSSI treatment during the year 2022, and we will continue conversations with other creditor partners.

28. We will update key aspects of the debt law, institute the guarantee fund, and enhance debt reporting and analysis. The debt legislation will be updated in line with the 2018 review, which provided guidance on the type of analysis and reporting which should be produced; and steps will be taken to clearly identify the required reports. The requirement in the debt management strategy for conducting internal debt sustainability analysis (DSA) will be implemented. Officers in the Ministry of Finance have already received the relevant training and the ministry intends to conduct the first internal DSA by January 2023. This would help inform the 2023 budget. Furthermore, the Government will undertake a review of the laws regulating guarantees. The guarantees law provides for the establishment of a fund to be financed by the beneficiaries of guarantees, which would provide a cushion in the event of noncompliance with the terms of the guarantee. During 2022 this fund will be activated and the regulations for its operations will be established.

F. Macroeconomic Stabilization Fund

29. As part of the broader strategy of strengthening the fiscal framework we will establish a macroeconomic stabilization fund. Cabo Verde is a small open economy and is highly susceptible to external shocks. We have had to contend with an ongoing drought from 2017, the devastating economic impact of the pandemic and the spillover effects from the Ukraine war. These events highlight the need for us to build buffers to help mitigate the effect of external shocks including from the impact of climate change, which usually worsens the fiscal position. The creation of the Macroeconomic Stabilization Fund establishes a platform on which we will start to build buffers to help mitigate the impact of exogenous shocks on the economy and public finances.

30. Cape Verde is highly vulnerable to floods, droughts, earthquakes, and volcanic eruptions, which imposes significant cost on the economy. The average economic damage from natural disasters, particularly floods was estimated to cost US $18 million (I percent of GDP) per year by the World Bank. Higher levels of damages are likely in the future due to the impact of climate change, which would be magnified by the fact that Cabo Verde consist of several islands.

31. The range and magnitude of global shocks has severely impacted Cabo Verde. In that regard we will redouble our efforts to implement reforms to improve our resilience and secure long-term sustainability. In order to achieve this, we will ensure that there is strategic alignment, institutional cooperation, and operational coordination at an intersectoral, multidisciplinary level, by the public entities involved in the process.

G. National Accounts Rebasing

32. The National Statistics Institute (INE) has completed the major task of rebasing the national accounts. With IMF TA, INE has finalized the rebasing of the national accounts statistics to 2015, from 2007. The published data indicate nominal GDP about 10 percent higher than previous estimates, which reflects mainly a more accurate measurement of the services sector. The rebased national accounts will enhance policy making with the availability of a more accurate representation of Cabo Verde's economy.

H. Monetary Policy and Financial Stability

33. The conventional fixed peg exchange regime continues to provide a stable anchor for monetary policy. Monetary policy will continue to focus on safeguarding the peg and strengthening the monetary policy framework. In the wake of the new external shock due to the war in Ukraine, international reserves are projected to decline sharply in 2022. In the near-term, the BCV will closely monitor economic developments in the euro area and stand ready to take corrective measures, if pressures on reserves become excessive. The BCV was in the process of unwinding the COVID-19 related monetary policy stimulus as the recovery strengthens given continued excess liquidity in the banking system and the recent positive evolution of the pandemic. However, the geopolitical shock warrants a more cautious approach. Over the medium-term, to support the peg, the BCV will target international reserves in the range of 5 to 5½ months of prospective imports.

34. We will continue to take steps to further strengthen the monetary policy transmission mechanism and to enhance our analytical capacity to track developments in the economy. The central bank will take actions to support the development of the money market, including pre-announcing a schedule for auctions of Monetary Intervention Securities (TIMs) and Monetary Regularization Securities (TRMs) **(Structural Benchmark)**. Policy analysis will be reinforced, including through the introduction of composite indicators of economic activity and strengthening near-term forecasting **(Structural Benchmark)**. The central bank will also develop a framework to guide the provision of emergency liquidity assistance. The BCV and the Ministry of Finance have sought World Bank TA to undertake a digital economy assessment and formulate a national fintech strategy, that would set the necessary pillars for the use of financial technologies which embrace innovation and competition, and lower transaction costs.

35. The BCV will closely monitor emerging risks to the banking sector. Available indicators indicate that the banking sector is well placed to withstand the effects of the projected increase in NPLs associated with the end of the credit moratorium in June 2022. However, the BCV will undertake a comprehensive study of loan losses and provisions at the expiration of the credit moratorium in June 2022 **(Structural Benchmark)**, encourage and facilitate prudent restructuring of loans, and proactively provide guidance on the prudential treatment of moratoria and NPLs management strategies and develop a common framework for bank resolution. In addition, it will encourage the development of detailed reporting templates for restructured and rescheduled loans and for monitoring the impact of the COVID-19 related measures on the asset quality of banks. In support of these efforts, the BCV will develop a common framework for the resolution of crisis related NPLs **(Structural Benchmark)**. Recent improvements in the AML/CFT framework, including the establishment of a national AML/CFT committee and Cabo Verde's recent exit from the EU list of non-cooperative jurisdictions for tax purposes have helped preserve correspondent banking relationships.

36. As part of the Financial Sector Development Plan, our efforts will be focused on the ongoing modernization of the financial system. We will enhance the regulatory and supervisory frameworks with the aim of deepening the financial sector, including to support inclusive and sustainable growth, while preserving financial stability. We remain committed to ensuring a stable and well-capitalized banking system that can continue to support the recovery by effectively monitoring and supervising the health of the financial system. To ensure effectiveness of the supervisory process, we will increase the frequency of stress testing to at least two times a year from 2023. In addition, the stress testing methodology will be revamped to include detailed banking data and cyber security risk assessment. The recent IMF safeguards assessment mission recommended amending the BCV Law to strengthen the decision-making structure, autonomy, accountability and transparency of the central bank. Supported by technical assistance from the IMF we will submit draft amendments to the BCV Law, to the Ministry of Finance which will address the gaps identified **(Structural Benchmark)**.

37. We will accelerate work towards the adaption of Basel II Pillar 1. During the first half of 2023 an evaluation will be undertaken of the implementation of the Basel principles through the BCP Self-Assessment (more details to be provided by BCV).

38. We continue to improve on the accuracy of our monetary and financial sector statistics. Over the past year, we have eliminated discrepancies between the monetary and financial sector survey disseminated by the BCV in its publications and data sent to the IMF, by adopting the methodology of the central bank survey compiled for the IMF, which is based on international statistical standards (IMF's 2016 Monetary and Financial Statistics Manual and Compilation Guide (MFSMCG)). This new compilation system allows for correcting discrepancies between the other deposit corporations (ODC) survey disseminated by the BCV in its publications and the data sent to the IMF. Further improvements will continue this year with the enhancement of data on credit by economic activity using INE's economic activity classification.

I. Structural Reforms: Supporting Private Sector-Led Growth

39. Structural reforms will aim to improve the business environment, addressing labor market inefficiencies by revising certain provisions of the labor code, and increasing access to finance. The new five-year strategy (PEDS) is based on the recently completed long-term development plan (Cabo Verde Ambition 2030). Key priority areas include: (i) completing SOE reforms, including through privatization and improving the efficiency of SOEs; (ii) reducing informality, (iii) facilitating access to finance, particularly for small and medium-sized enterprises, and (iv) improving the business environment. In support of our business environment reforms, we will examine possible changes to the labor code with a view to increasing incentives to make the labor market more dynamic. Climate change adaptation and mitigation including achieving the 30 percent renewable energy target by 2026 and 50 percent by 2030, and digitalization including the development of technology parks are also two key priorities of the government (Table 3).

40. We will continue to make efforts to diversify our economy. Diversification efforts are being pursued through two channels. Firstly, within the main tourism sector we are actively moving towards more integrated resort projects heralded by the presence and emergence of top hotel brands. Secondly, we are actively promoting alternative sectors, such as the blue economy, digital economy, industry integrated into the regional and global value chains, and modernization of the agriculture sector using desalinated water.

41. Legal procedures for businesses will be made easier, through a reduction in waiting time by improving the link between businesses and judicial processes. One area of focus will be on land titling, where issues often arise because of unclear ownership due to incomplete information that can cause delays in investment decisions. In this regard, the government will digitalize the relevant information to facilitate ease of access to all parties, which will facilitate more timely settlement of disputes.

42. The Government will enhance support to vulnerable groups by strengthening social safety nets. Even though Cabo Verde performs very well on social indicators, poverty and unemployment remain high particularly in the rural areas and these trends have worsened due to the pandemic and are likely to be negatively impacted by the rising price level. Social safety nets will be strengthened through improved targeting of social spending. In partnership with our external partners, we will continue to work towards better targeting of social programs and will sign a pact for poverty reduction, with the goal of eliminating extreme poverty by 2026. The government will also take the opportunity during the program period to reform the national social security system to ensure that it evolves in alignment with best practices and the changing needs of the country.

43. In that regard, policies under the program will help safeguard spending on social safety nets and help increase our capacity to expand on these interventions. We have made important investments in the delivery systems for social protection, particularly the social registry and the [RSI] cash transfer program. These gains will be protected during the IMF supported ECF as support for the most vulnerable and helping lift households out of poverty are key objectives of our strategy and will be monitored in part through an indicative target on social spending. Through a program of productive inclusion, the government guarantees empowerment for the most vulnerable families, as well as the transfer of money to some of the most vulnerable families in Cabo Verde. Our method of supporting the most vulnerable through cash transfers is an important and efficient way of investing in the people; contribute towards strengthening their resilience and enhances their human capital in several ways, including through ensuring food security and enabling expenses related to education and health for children in these households, as well as training for inclusion in the job market.

J. Risks and Contingencies

44. The uncertainty about the trajectory of the COVID-19 pandemic and the evolution of the spillover impact of the Ukraine war will continue to weigh on the economic outlook. If COVID-19 developments were to deteriorate or the negative impact of the Ukraine were to worsen compared to our baseline, economic outcomes would worsen. However, we believe that our strong commitment to implementing reforms along with the policies under our Fund-supported ECF program and continued support from development partners provides a strong platform to manage these challenges. However, if the macroeconomic outlook deteriorates, we commit to take additional measures in consultation with the IMF.

K. Financing and Program Monitoring

45. The program will be closely monitored through quantitative performance criteria, indicative targets, and structural benchmarks. The Technical Memorandum of Understanding describes the definitions as well as data provision requirements. The first and second program reviews are scheduled to be completed by November 2022 and May 2023 (based on end-June and end-December 2022 test dates, respectively). Thereafter, the program will continue with monitoring on a semi-annual basis by the IMF Executive Board.

Table 1. Cabo Verde: Structural Benchmarks for 2022-23 under the ECF

Actions	Target date	Objective
Fiscal reforms		
Invoice electronically at least 50 percent of tax payers for VAT	End-December 2022	Improve revenue collection
Submit to parliament the budget for 2023 that is in line with commitments under the program.	End December 2022	Support fiscal and debt sustainability
Compile and publish historical series of government financial statistics for general	End-March 2023	Improve fiscal transparency
Publish annual budget execution reports for the general government.	End-September 2023	Improve fiscal transparency
SOEs reforms		
Conduct quarterly analysis of fiscal risk assessment using the IMF SOEs health check tool.	End-September 2022	Improve fiscal reporting and educe fiscal risks
Introduce a quarterly monitoring report on SOEs budget execution.	End-September 2022	Improve fiscal reporting and reduce fiscal risks
Improve the annual SOEs report to include comparison of execution to initial budget projection, evaluation of performance against medium term plan, data on government relations	End-July 2023	Improve fiscal reporting and educe fiscal risks
Monetary policy reforms		
Preannounce a schedule for TIM and TRM auctions.	End-June 2022	Support the development of the money market
Introduce a composite indicators of economic activity.	End-June 2023	Support monetary policy analysis
Financial sector reforms		
Submit draft amendments to the BCV Law, in line with IMF recommendations, to the Ministry of Finance with a view to (i) establishing an independent oversight process that is separate from executive management, (ii) strengthening the BCV's personal and financial autonomy, and (iii) enhancing transparency and accountability mechanisms	End-December 2022	Strengthen BCV institutional framework
Carry out a comprenhensive study of loan losses and provisions at the expiration of the credit moratorium.	End-December 2022	Strengthen financial stability
Develop a common framework for the resolution of crisis related NPLs.	End-December 2022	Strengthen financial stability

Table 2. Cabo Verde: Quantitative Performance Criteria and Indicative Targets under the ECF, June 2022-June 2023[1]

(Millions of Escudos, unless otherwise indicated)

	2021	2022			2023	
	end-December	end-June	end-September	end-December	end-March	end-June
	Actual	Performance Criteria (PC)	Indicative Targets (IT)	Performance Criteria (PC)	Indicative Targets (IT)	Performance Criteria (PC)
		Cumulative from the beginning of the calendar year				
Quantitative performance criteria						
Primary balance, floor [2]	-10,112	-4,635	-7,500	-7,750	-2,612.0	-4,141.0
Tax revenue, floor	33,542	16,916	27,161	38,215	9,550.1	19,095.0
Net other liabilities, ceiling [3]	-1,691	742	358	1,455	501.5	625.3
Net domestic financing, ceiling	3,142	6,388	7,100	7,501	5,651	5,886
Nonaccumulation of domestic arrears [4]	0	0	0	0	0	0
Non-accumulation of external payment arrears [4]	0	0	0	0	0	0
PV of new external debt, ceiling (in millions of US Dollars)	109	61	84	94	46	60
Nominal level of new nonconcessional external debt of central government, ceiling[4]	0	0	0	0	0	0
Gross international reserves (in millions of euros), floor [2]	591	560	557	491	554	572
Indicative Targets						
Social spending, floor	18,300	5,750 0	8,928	15,800	2,923	6,180
Non-quantitative continuous PCs						
Non-imposition or intensification of restrictions on the making of payments and transfers for current international transactions						
Non-introduction or modification of multiple currency practices						
Non-imposition or intensification of import restrictions for balance of payments reasons						
Non-conclusion of bilateral payments agreements that are inconsistent with Article VIII						
Memorandum items:						
Net onlending	1,181	515	1,530	2,790	4.9	101
Capitalization	838	1,363	1,763	2,151	300.0	765.3
Program assumptions						
Project and budget support grants	3,985	675	890	3,982	181.9	623.3
External debt service	5,906	5,665	9,281	11,226	3,664.8	6,445.4
Sales of assets	683	351	431	648	142.2	516.6
Project and budget support loans	11,024	4,125	10,188	14,333	913.9	5,887.7

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

[1] Expressed in local currency and millions unless otherwise indicated. Foreign currency amounts will be converted at current exchange rates.

[2] Stock of reserves in millions of Euros.The ceiling or floor will be adjusted as specified in the TMU.

[3] Net other liabilites includes net onlending, capitalization, and other assets.

[4] Continuous.

Table 3. Cabo Verde: Other Reforms Under the ECF, 2022-2025

Fiscal reforms
1. Compile and publish financial balance sheet for the general government.
2. Digitalization of all the revenue administration and collection processes.
3. Redefine the existing thresholds to reduce the number of projects qualifying for more detailed appraisal in line with available capacity.
4. Develop and implement an enhanced pre-screening system (pre-screening+), a single-entry point for all project ideas regardless of size or source of financing.
5. Develop and implement multi-criteria analysis (MCA) techniques and matrices for prioritization and selection of capital projects.
SOEs reforms
6. Automatic Digital Platform for Monitoring the SOEs and automating the model for analyzing the financial health of SOEs.
7. Resumption of privatization of SOEs. Completion of the privatization process, namely of ASA, Cvhandling, Emprofac,Inpharma, TACV, Electra, Enapor; Cabvane, CASHIER and, CVTelecom.
Monetary policy reforms
8. Conduct a study on the implication of central bank digital currency (CBDC) for monetary policy and develop a legal framework for CBDC.
9. Develop a framework guiding the provision of emergency liquidity assistance.
Financial sector reforms
10. Increase the frequency of stress testing to at least two times a year.
11. Implement a revamped stress testing methodology incorporating detailed banking data and cyber security risk assessment.
12. Undertake an evaluation of the implementation of the Basel principles through the BCP Self-Assessment during the first half of 2023.
Public sector investment and digital reforms
13. Public Key Infrastructure (PKI) - Issue digital certificates to people and entities and leverage the digital economy
14. Digital Mobile Key of Cape Verde (CMDCV) - Modernize the system for issuing, and managing the life cycle of identification documents, reinforcing security levels.
15. Consular Portal, to facilitate relations with the Cape Verdean diaspora and relations with those seeking Cape Verde.
16. Digital Certificate – Nha Card & Blockchain Platform Design Unique Business Creation Platform that will allow the creation of a business both in person and through online channels,using a digital signature and digital authentication mechanism.
17. External Investment Platform – One-Stop-Shop for Investors, for registration and authorization of their investments.
18. SIMPLE- Integrated Municipal Platform, a robust Information System with all the necessary functionalities and covering all Municipal Management and Action Areas.
19. Digitalization of Nacional Health Care System (e-Health), with electronic medical records, electronic prescribing,Telehealth and Telemedicine.
20. Digital transformation in the Justice System (e-Justice). Restructuring, Adaptation and streamlining the operationalization of the current Justice Information System (SIJ).
21. Implementation of the National Investment System.
22. Implementation of a new Monitoring and Evaluation framework.
23. Approval of the action plan for digital governance.
Legal framework reforms
24. Submission to Parliament of the Public Employment Law.
25. Review and implementation of the SOEs and ERI's legal framework and governance policies.

Attachment II. Technical Memorandum of Understanding

This memorandum sets out the understandings between the Cabo Verdean authorities and the IMF staff regarding the definitions of variables included in the quantitative targets and continuous targets set out in the Memorandum of Economic and Financial Policies (MEFP), the key assumptions, and the reporting requirement of the Government and the Central Bank of Cabo Verde for the three-year Extended Credit Facility (ECF).

PROGRAM EXCHANGE RATES

1. **Program exchange rates are used for formulating and monitoring quantitative performance criteria**. All assets and liabilities denominated in U.S. dollars (USD) will be converted into escudos at a program exchange rate of CVE 98.8 per one USD. Assets and liabilities denominated in SDRs and in foreign currencies not in USD will be converted into USD at the exchange rates reported in the Table 1:

Table 1. Cabo Verde: Program Exchange Rates

Currency	Program Exchnage Rates
Escudos/US Dollars	98.8
Escudos/Euros	110.3
US Dollar / U.K. pound	1.34
US Dollar/Euro	1.11
US Dollar/ Japanese yen	0.01
SDR/US Dollar	0.72

Source: WEO April period average exchange rates

QUANTITATIVE AND CONTINUOUS TARGETS

A. Floor on the Primary Balance of the Central Government

2. **The central government includes all units of budgetary central government**. It does not include local government (municipalities), extrabudgetary units, social security funds and public corporations.

3. **The central government primary balance is defined as total tax and non-tax revenues and grants minus primary expenditure** and covers non-interest government activities as specified in the budget. The central government primary balance will be measured as cumulative flow over the calendar year.

- Revenues are recorded when the funds are transferred to a government revenue account. Tax revenues are recorded as net of tax refunds.

- Central government primary expenditure is recorded on a cash basis and covers recurrent expenditures and capital expenditure.

4. The floor of the primary balance will be adjusted upward (downward) by the surplus (shortfall) in disbursements of grants relative to the baseline projection.

Table 2. Cabo Verde: Grants Projected Under the Program (GIR)

Date	Grants projected under the program, cumulative from the beginning of the year (in million CV Escudos)
30-Jun-22	675
30-Sep-22	890
31-Dec-22	3,982
31-Mar-23	182
30-Jun-23	623

Source: Cabo Verdean Authorities: IMF Staff estimates

5. For program monitoring, data will be provided to the Fund by the Directorate National of Planning (DNP) of the Ministry of Finance monthly with a lag of no more than six weeks from the end of-period.

B. Cumulative Floor on Central Government Tax Revenue

6. Tax revenues refer to revenues from tax collection. It excludes all revenues from asset sales, grants, and non-tax revenues. To gauge the impact of tax policy reforms and improvements in tax administration, the program will have a floor on central government tax revenues. The revenue target is calculated as the cumulative flow from the beginning of the calendar year.

7. For program monitoring, data will be provided to the Fund by the DNP of the Ministry of Finance monthly with a lag of no more than six weeks from the end of-period.

C. Ceiling on Net Other Liabilities

8. Net Other Liabilities is defined as the sum of central government deposits, loans to state-owned enterprises (SOEs) and municipalities (onlending), capitalization, and other assets. The ceiling of central government net other liabilities will be measured as cumulative over the calendar year. Deposits are all claims, represented by evidence of deposit, on the deposit-taking corporations (including the central bank). Onlending is defined as domestic and external loans contracted by the central government from another institution and then onlending the proceeds to SOEs. Net onlending is defined as disbursement of these loans minus repayment of previous loans by SOEs to the central government. Capitalization is defined as capital injection or equity participation made by the central government into corporations when some financial support is provided to capitalize or recapitalize these corporations. Other assets comprise of other accounts receivable/payable such as of trade credit and advances and miscellaneous other items due to be paid or received.

9. **For program monitoring, data will be provided to the Fund by the DNP of the Ministry of Finance** monthly with a lag of no more than six weeks from the end of-period.

D. Non-accumulation of Domestic Payments Arrears

10. **As part of the program, the government will not accumulate any new domestic payments arrears.** This will be monitored through the monthly execution of the cash-flow plan and the corresponding release of budget appropriations. For programming purposes, a domestic payment obligation to suppliers is deemed to be in arrears if it has not been paid within the normal grace period of 60 days (30 days for government salaries and debt service) or such other period either specified by the budget law or contractually agreed with the supplier after the verified delivery of the concerned goods and services, unless the amount or the timing of the payment is subject to good faith negotiations between the government and the creditor.

11. **Reporting requirements**. The DNP of the Ministry of Finance will submit on a quarterly basis a detailed table of the stock of domestic payments arrears, including the accumulation, payment, rescheduling and write-off of domestic payments arrears during the quarter. The data are to be provided within six weeks after the end of the quarter.

E. Ceiling on the PV of New External Concessional Debt of the Central Government

12. **Under the program a ceiling applies to the PV of new external debt, contracted or guaranteed by the public sector with original maturities of one year or more**. The ceiling applies to debt contracted or guaranteed for which value has not yet been received, including private debt for which official guarantees have been extended. An adjustor of up to 5 percent of the external debt ceiling set in PV terms applies to this ceiling, in case deviations from the performance criterion on the PV of new external debt are prompted by a change in the financing terms (interest, maturity, grace period, payment schedule, upfront commissions, management fees) of a debt or

debts. The adjustor cannot be applied when deviations are prompted by an increase in the nominal amount of total debt contracted or guaranteed.

13. External public debt (long-term, medium-term, and short-term) is defined as debt to nonresidents contracted or guaranteed by the central government. The external public debt comprises the external debt of the central government and the external debt of the official sector entities and SOEs guaranteed by the central government.

14. The definition of debt is set out in Point 8(a) of the Guidelines on Public Debt Conditionality in Fund Arrangements attached to Executive Board Decision No. 15688-(14/107), adopted December 5, 2014.

(a) The term "debt" will be understood to mean a current, i.e., not contingent, liability, created under a contractual arrangement through the provision of value in the form of assets (including currency) or services, and which requires the obligor to make one or more payments in the form of assets (including currency) or services, at some future point(s) in time; these payments will discharge the principal and/or interest liabilities incurred under the contract. Debts can take a number of forms, the primary ones being as follows:

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

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

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

(b) Under the definition of debt set out in this paragraph, arrears, penalties, and judicially awarded damages arising from the failure to make payment under a contractual obligation that constitutes debt are debt. Failure to make payment on an obligation that is not considered debt under this definition (e.g., payment on delivery) will not give rise to debt.

15. **Under the program, ceilings on medium and long-term, as well as on short-term, concessional external debt constitute quantitative targets**. The coverage of the ceiling on concessional external debt includes budget loans, projects and program loans, and on-lending loans to SOEs in line with the fiscal program. For program purpose, a debt is concessional if it includes a grant element of at least 35 percent, calculated as follows: the grant element of a debt is the difference between the present value (PV) of debt and its nominal value, expressed as a percentage of the nominal value of the debt. The PV of debt at the time of its contracting is calculated by discounting the future stream of payments of debt service due on this debt.[1] For debts with a grant element equal or below zero, the PV will be set equal to the nominal value of the debt. The discount rate used for this purpose is the unified discount rate of 5 percent set forth in Executive Board Decision No. 15248-(13/97). Debt rescheduling, and debt reorganization are excluded from the limits on concessional external debt. New concessional external debt excludes normal short-term (less than one year) import-related financing.

16. **For debts carrying a variable interest rate in the form of a benchmark interest rate plus a fixed spread, the PV of the debt would be calculated using a program reference rate plus the fixed spread (in basis points) specified in the debt contract**. The program reference rate for the six-month USD LIBOR is 2.699 percent and will remain fixed for the duration of the program. The spread of six-month Euro LIBOR over six-month USD LIBOR is -168 basis points. The spread of six-month GBP LIBOR over six-month USD LIBOR is -80 basis points. For interest rates on currencies other than Euro, JPY, and GBP, the spread over six-month USD LIBOR is 100 basis points. Where the variable rate is linked to a benchmark interest rate other than the six-month USD LIBOR, a spread reflecting the difference between the benchmark rate and the six-month USD LIBOR (rounded to the nearest 50 bps) will be added. Given the anticipated global transition away from LIBOR, this TMU can be updated to reflect the relevant benchmark replacements (U.S. Secured Overnight Financing Rate (SOFR); U.K. Sterling Overnight Index Average (SONIA); EURIBOR; and Tokyo Overnight Average Rate (TONAR)) prior to the complete phase out, once operationally feasible.

17. **Reporting requirements**. The government of Cabo Verde will consult with Fund staff before assuming any liabilities in circumstances where they are uncertain whether the instrument in question falls under the quantitative target. Details of all new external debt (including government guarantees), indicating terms of debt and creditors, will be provided on a quarterly basis within six weeks of the end of each quarter.

[1] The calculation of concessionality take into account all aspects of the debt agreement, including maturity, grace period, payment schedule, upfront commissions, and management fees.

F. Non-Concessional External Debt Contracted or Guaranteed by the Central Government

18. **Under the program, ceilings on medium- and long-term, as well as on short-term, non-concessional external debt constitute quantitative target**. The zero ceiling on non-concessional external debt is on a continuous basis. For program purpose, a debt is non-concessional if it includes a grant element of less than 35 percent, calculated as follows: the grant element of a debt is the difference between the present value (PV) of debt and its nominal value, expressed as a percentage of the nominal value of the debt. The PV of debt at the time of its contracting is calculated by discounting the future stream of payments of debt service due on this debt.[1] For debts with a grant element equal or below zero, the PV will be set equal to the nominal value of the debt. The discount rate used for this purpose is the unified discount rate of 5 percent set forth in Executive Board Decision No. 15248-(13/97). Debt rescheduling, and debt reorganization are excluded from the limits on non-concessional external debt. The quantitative target on new non-concessional external debt contracted or guaranteed by the central government, excluding borrowing from the Fund. Non-concessional external debt excludes normal short-term (less than one year) import-related financing. The Portuguese government's precautionary credit line (the "Portuguese credit line") in support of the exchange rate peg is also excluded from the definition of non-concessional external debt (continuous PC target).

19. **Reporting requirements**. The government of Cabo Verde will consult with Fund staff before assuming any liabilities in circumstances where they are uncertain whether the instrument in question falls under the quantitative targets. Details of all new external debt (including government guarantees), indicating terms of debt and creditors, will be provided on a quarterly basis within six weeks of the end of each quarter.

G. Gross International Reserves of the Central Bank

20. **The floor on the stock of gross international reserves (GIR) of the BCV constitutes a quantitative target under the program**. The GIR of the BCV are defined as gross international reserves of the BCV which include assets that are readily available (i.e., liquid and marketable and free of any pledges or encumbrances), controlled by the BCV and held for the purposes of meeting balance of payments needs and intervening in foreign exchange markets. They include gold, holdings of SDRs, the reserve position at the IMF, holdings of foreign exchange and traveler's checks, demand and short-term deposits at foreign banks abroad, fixed-term deposits abroad that can be liquidated without penalty, and any holdings of investment-grade securities. The program floors for the GIR will be adjusted downward by:

- The cumulative upward deviations in external debt service relative to program assumptions.
- The cumulative downward deviations in external financial assistance, and project and budget loans relative to program assumptions. For purposes of calculating the adjusters, these flows will be valued at current exchange rates.

21. Reporting requirements. A table on the GIR prepared by the BCV will be transmitted on a monthly basis, with a maximum delay of four weeks.

Table 3. Cabo Verde: External Debt Service Projected under the Program (GIR)

Date	External debt service projected under the program, cumulative from the beginning of the year (in million CV Escudos)
30-Jun-22	5,665
30-Sep-22	9,281
31-Dec-22	11,226
31-Mar-23	3,665
30-Jun-23	6,445

Source: Cabo Verdean Authorities: IMF Staff estimates

Table 4. Cabo Verde: External Financial Assistance and Project and Budget Loans Projected under the Program

Date	External financial assistance and project and budget loans projected under the program, cumulative from the beginning of the year (in million CV Escudos)
30-Jun-22	4,800
30-Sep-22	11,078
31-Dec-22	18,315
31-Mar-23	1,096
30-Jun-23	6,511

Source: Cabo Verdean Authorities: IMF Staff estimates

H. Non-Accumulation of External Payments Arrears

22. **As part of the program, the government will not accumulate any new external payments arrears**. This will be a continuous target under the program. This will be monitored through the monthly execution of the cash-flow plan and the corresponding release of budget appropriations.

23. **External payments arrears for program monitoring purposes are defined as the amount of external debt service due and not paid within the contractually agreed period**, subject to any applicable grace period, including contractual and late interests. Arrears resulting from the nonpayment of debt service for which a clearance framework has been agreed or a rescheduling agreement is sought are excluded from this definition.

24. **Reporting requirements**. Data on (i) debt-service payments; and (ii) external arrears accumulation and payments will be transmitted on a quarterly basis by the DNP of the Ministry of Finance, within six weeks of the end of each quarter. In addition, the government will inform the Fund staff immediately of any accumulation of external arrears.

I. Floor on Central Government Social Spending

25. **The floor on social spending of the central government is an indicative target under the program**. This will apply only to expenditures incurred by the central government on the following plans and programs that are intended to have a positive impact on education, health, and social protection, excluding the wages and salaries component.

26. **For program monitoring, the data will be measured as cumulative over the fiscal year** and it will be reported by the DNP on a quarterly basis, with a lag of no more than six weeks from the end-of-period.

OTHER DATA REQUIREMENTS AND THE ASSESSMENT OF THE ACVIEVEMENT OF REFORM TARGETS

27. **Data on exports and imports, including volume and prices and compiled by the Director of Customs and the BCV**, will be transmitted on a quarterly basis within five weeks after the end of each quarter. A preliminary quarterly balance of payments, compiled by the BCV, will be forwarded within six weeks after the end of each quarter.

28. **The Statement of Other Economic Flows as defined in the IMF Manual GFSM2001 or GFSM2014** relative to holding gains/losses of the previous year with ASA, Electra, EMPROFAC,

ENAPOR, and IFH will be transmitted on an annual basis within three months after the end of the following year (15 months after the closing date).

29. The consolidated balance sheet of ASA, Electra, EMPROFAC, ENAPOR, and IFH relative to the previous year will be transmitted on an annual basis within three months after the end of the following year (15 months after the closing date).

30. Pre-announce a schedule for TIM and TRM auctions reform target. This reform target will be assessed as achieved when the pre-announcements are posted on the central bank website.

31. Introduce a composite indicator of economic activity reform target. This reform target will be assess as achieved when the central bank has released the composite indicator.

32. Carry out a comprehensive study of loan losses and provisions at the expiration of the credit moratorium in June 2022 reform. This reform target will be assessed as achieved when the study is completed and released.

33. Develop a common framework for the resolution of the crisis related NPLs. This reform target will be assessed as achieved when the common framework is complete and released. The common framework is being developed jointly by the BCV and the World Bank.

INTERNATIONAL MONETARY FUND

CABO VERDE

REQUEST FOR AN ARRANGEMENT UNDER THE EXTENDED CREDIT FACILITY—DEBT SUSTAINABILITY ANALYSIS

June 3, 2022

Approved By
Costas Christou (AFR), Johannes Wiegand (SPR), and Marcello Estevão and Abebe Adugna (IDA)

Prepared by the Staff of the International Monetary Fund and the International Development Association

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

Cabo Verde's risk of overall debt distress remains high, unchanged from the joint WB/IMF Debt Sustainability Analysis (DSA) of October 2020[1]. The risk of external debt distress, on the other hand, is assessed at moderate, upgraded from the last DSA. The present value (PV) of public and publicly guaranteed (PPG) external debt-to-GDP ratio breaches its threshold only in 2022 under the baseline, and protractedly under stress test scenarios. The breach under the baseline is of shorter duration compared to the last DSA due to the GDP rebasing. Liquidity indicators (debt service to revenue and to export ratios) remain firmly below their respective thresholds under the baseline, reflecting the high concessional nature of Cabo Verde's external debt. The PV of total public debt-to-GDP ratio is projected to breach the threshold during 2022–28 under the baseline scenario and stress test; at the same time, The external and overall debt outlook is assessed to be sustainable and is predicated on several assumptions, including continued recovery of economic activity in 2022, a return to the pre-pandemic fiscal consolidation path as well as resumption of structural reforms, notably to restructure State-Owned Enterprises (SOEs) to reduce fiscal risks (including from contingent liabilities) and improve the business environment. Prudent borrowing policies through sourcing mainly concessional external loans and strengthened debt management, as well as measures to enhance the functioning of the government securities market are critical to sustainable debt dynamics over time. In view of Cabo Verde's vulnerability to exogenous shocks, continuous progress in export and output diversification are also needed for long-term debt sustainability.

[1]Cabo Verde's debt-carrying capacity is assessed as "strong" as in the previous DSA with a composite index score of 3.23, which is based on the October 2021 WEO and the 2020 CPIA.

PUBLIC DEBT COVERAGE

1. **Coverage of the public sector is in line with the previous DSA (Table 1)**. Consistent with the fiscal accounts, social security funds 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 on-lending and capitalization. Government guarantees to SOEs' external borrowing are included in the baseline stock of debt, but publicly guaranteed domestic debt and non-guaranteed debt by SOEs are not included. Efforts to broaden the coverage of public sector debt are ongoing, including under a World Bank project focused on SOEs.[2] External debt is defined on a residency basis.

2. **Recent efforts to strengthen the quality and coverage of public debt data have shown results**. As part of the Fund supported program, the authorities introduced a new system of recording and monitoring debt which resulted in more accurate and timely dissemination of information on public debt. This should help improve the quality and timeliness of data available to the authorities for planning and debt management purposes.

3. **The contingent liability tailored stress test is amended to reflect gaps in the debt coverage discussed above (Table 1)**. First, the default shock of 0 percent of GDP for the components of general government not captured in the baseline stock of debt is raised to 0.2 percent of GDP to account for the size of publicly guaranteed domestic debt of local governments. The social security fund (INPS) financial position is strong, with minimal fiscal risk and the contingent liability stress test does not require adjustments for its exclusion. Second, the default shock of 2 percent of GDP for SOEs' debt is raised to 26.4 percent of GDP to reflect vulnerabilities associated with[3] publicly guaranteed domestic borrowing by ELECTRA, TACV, IFH, ENAPOR, NEWCO, CERMI amounting to CVE 20.8 billion at end-2021 (10.4 percent of GDP); and (ii) non-guaranteed domestic debt of loss-making SOEs totaling CVE 34.3 billion (about 16 percent of GDP).[4] Third, the default shock of 1.1 percent of GDP is kept for public private partnerships (PPPs). Fourth, 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.

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[2]Efforts to expand debt coverage are supported by the World Bank through the Policy and Performance Action under the Sustainable Development Financing Framework. Specifically, the coverage of the quarterly public debt bulletin will be broadened to include debt of SOEs, the social pension fund, and guaranteed debt from municipalities.

[3]Government-guaranteed domestic borrowing of municipalities from the banking system stood at CVE 359 million at end-December 2021 (see Text Table 2 for more details).

[4]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). Data for 2020 and 2021 is not yet available.

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

	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		
		Default	**Used for the analysis**	**Reasons for deviations from the default settings**
2	Other elements of the general government not captured in 1.	0 percent of GDP	0.2	
3	SoE's debt (guaranteed and not guaranteed by the government) 1/	2 percent of GDP	26.4	To reflect vulnerabilities associated with guaranteed and non-guaranteed domestic 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)		32.7	

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%.

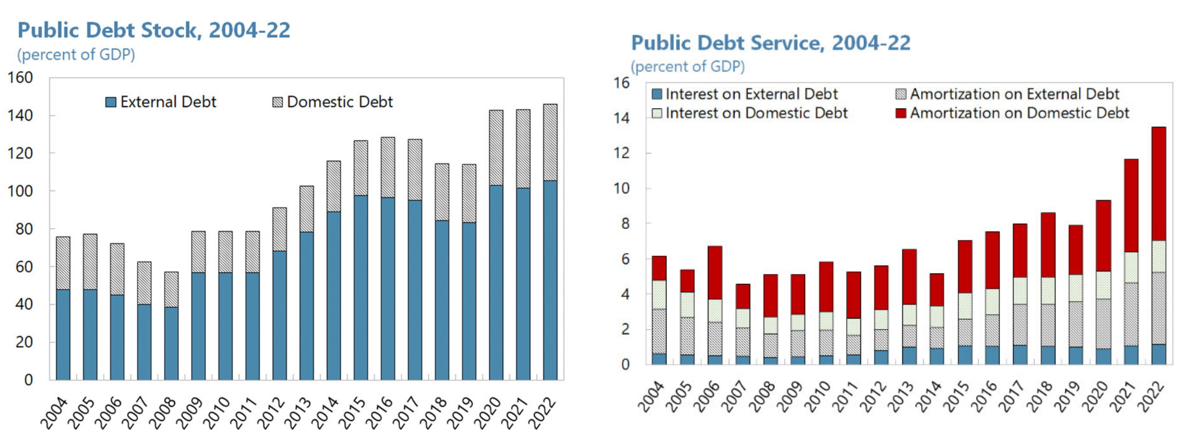
BACKGROUND

A. Evolution and Composition of Public Debt

4. **Prior to the COVID-19 crisis, Cabo Verde experienced robust growth driven by a thriving tourism sector and benefited from structural reforms, particularly in the SOE sector**. Between 2016 and 2019, growth averaged 4.7 percent (3.4 in per capita terms). Favorable global conditions coupled with important structural reforms, mainly impacting the SOE sector, supported growth. The privatization efforts of the government helped support investor and consumer confidence. Public debt had decreased from its peak of 128.4 percent of GDP in 2016 to 115 percent in 2019. The poverty rate in 2019 was 10.2 percent (using US$3.2 per cay PPP in 2011).

5. **The COVID-19 pandemic contributed to a substantial increase in external and overall public sector debt levels**. Total public sector debt reached 143 percent of GDP at end-2021 up from 114 percent in 2019 (Text Figure 1). The large increase in the debt ratio reflected the substantial decline in output level and a higher public sector deficit of 7.3 percent of GDP, financed largely through increased external concessional borrowing mainly from multilateral institutions to cushion the economic effects of the pandemic. Recognizing the severe impact posed by the crisis, and despite limited policy buffers, the authorities rapidly implemented measures to contain and mitigate the impact of the pandemic, including a comprehensive vaccination campaign. As of April 2022, the country has one of the highest vaccination rates in Africa.[5] The rebound in economic activity in 2021 resulted in a reduction in the poverty rate to 12.3 percent.

Text Figure 1. Cabo Verde: Profile of Public Debt and Debt Service, 2004–22



Sources: Cabo Verdien authorities and IMF staff estimates.
Note: External debt includes publicly-guaranteed SOE debt from 2015.

[5] Around 74 percent of the eligible adult population has received two doses, about 77 percent of eligible teenagers has received at least one dose, and boosters has been applied to 15.8 percent of eligible adults.

6. Cabo Verde's public external debt is highly concessional (Text Table 1). Multilateral Institutions are the main creditors with the World Bank and the African Development Bank accounting for about 27.3 percent of external public debt, while Portugal is the most significant bilateral creditor.[6] The cost of servicing the debt is modest with an average interest rate of about 1 percent and average maturity of about 30 years. The exchange rate risk is low thanks to the peg with the external assessment pointing to undervaluation and the comfortable foreign currency reserve position.

Text Table1. Cabo Verde: External Debt Profile by Type of Creditors, 2021

	Percent of GDP	Percent of external debt	Average maturity (in years)	Average interest rate
Multilateral	55	54.2	27.9	0.94%
Bilateral	20.8	20.5	18.9	1.01%
Commercial	25.9	25.3	20.0	1.59%

Source: Cabo Verdean authorities and IMF staff estimates.

7. Domestic debt consists mostly of medium and long-term Treasury securities. At end-2021, domestic debt accounted for 29 percent of total public debt (Text Figure 1), comprising mainly Treasury bonds (98 percent); with an average maturity and interest rate of about 7 years, and 4.5 percent respectively. Commercial banks hold 53.6 percent of domestic government securities, with non-banks holding 46.4 percent of which the national social security fund accounts for 22 percent.

8. External and total public debt service appears manageable. The ratio of public external debt service to exports reached 18.6 percent in 2021, reflecting the decline in exports due to the COVID-19 shock. The ratio is estimated to increase 2022 and decline thereafter in line with the recovery in economic activity. The ratio of public external debt service to revenue rose to 16 percent in 2020 and increased further to 22 percent in 2021 and is projected to average about 18 percent over the medium term and decline thereafter. Total public debt service absorbed about 41 percent of revenue and grants in 2022 and is projected to climb to about 49 percent in 2024 and steadily decline thereafter.

9. Publicly guaranteed debt stood at CVE 23.3 billion (11.9 percent of GDP) at end-2021 (Text Table 2). The State guarantee is mainly issued for SOEs' domestic debt. For 2021, the stock of publicly guaranteed domestic debt consists primarily of liabilities of ELECTRA, ENAPOR, IFH, TACV, NEWCO and CERMI to the domestic banking system; and borrowing by a few municipalities.[7] TACV and NEWCO are the larger recipients of guarantees after 2019.[8]

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

[7]The issuance and management of State guarantee is regulated by Decree-Law 42 of June 29, 2018, which clarified the entities that could benefit from guarantees and under which conditions. It also cut red tape by empowering the Ministry of Finance and Planning in authorizing up to CVE 50 million of guarantees per project.

[8]Annual financing needs of TACV, after its nationalization in July 2021, are estimated at 1 percent of GDP and has been financed through direct capitalization and central government guaranteed domestic loans.

Text Table 2. Cabo Verde: Publicly-Guaranteed Debt, 2018–2021

	2018			2019			2020			2021		
	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)	**1,674**	**0.8**	**100.0**	**395**	**0.2**	**100.0**	**1,913**	**1.1**	**100.0**	**2,502**	**1.3**	**100.0**
contracted by SOEs	1,674	0.8	100.0	395	0.2	100.0	1,913	1.1	100.0	2,502	1.3	100.0
contracted by private entities	0	0.0	0.0	0	0.0	0.0	0	0.0	0.0	0	0	0.0
Domestic Debt (B)	**11,077**	**5.5**	**100.0**	**13,843**	**6.5**	**100.0**	**15,369**	**8.5**	**100.0**	**20,832.4**	**10.6**	**100.0**
contracted by local governments	396	0.2	3.6	363	0.2	2.6	356	0.2	2.3	359	0.2	1.7
contracted by SOEs	10,681	5.3	96.4	13,473	6.3	97.3	15,004	8.3	97.6	20,474	10.4	98.3
contracted by private entities	0	0.0	0.0	8	0.0	0.1	9	0.0	0.1	0	0.0	0.0
Total Publicly-Guaranteed Debt (A+B)	**12,751**	**6.3**		**14,238**	**6.7**		**17,283**	**9.6**		**23,335**	**11.9**	

Source: Cabo Verdean authorities and IMF staff calculations.

10. Historical series of private external debt derived from international investment position (IIP) data indicate a stock of about 15.3 percent of GDP at end-2021. Private debt includes both bank and non-bank external debt.

11. Cabo Verde participated in the G-20 Debt Service Suspension Initiative (DSSI). The DSSI is a net-present-value (NPV) neutral exercise intended to provide eligible countries with liquidity relief from May 2020 -December 2021 to allow them to redirect resources in response to the COVID-19 pandemic. The DSSI provided around US$15.4 million in debt service relief, including US$2.9 million in interest in 2020. The G-20 extended the DSSI initiative until the end of 2021, which provided an additional US$45.9 million in debt service relief. Portugal has agreed to provide additional debt service relief in 2022 of US$1.3m. The debt service relief from the DSSI is captured in the baseline. Repayments to ensure NPV-neutrality will occur over 2022–25 and average about US$15 million per year.

B. Outlook and Key Macroeconomic Assumptions

12. Compared to the last DSA (October 2020) the macroeconomic assumptions underlying the projections have been adjusted to reflect the lingering effects of the pandemic and the impact of the Ukraine-Russia crisis. The Ukraine war has increased inflationary pressures and reduced growth prospects in 2022, highlighting the structural vulnerability of the country to external shocks. The main transmission channels are higher international oil and food prices, as Cabo Verde imports about 80 percent of consumption products, domestic prices have increased in line with international developments. The authorities have announced a package of measures to help mitigate the impact of rising fuel and food prices on the most vulnerable. The package of measures includes the reduction of VAT on electricity from 15 to 8 percent and an increase in the energy subsidy to poor households from 30 to 50 percent.

13. The level of GDP has been revised in line with the completion of the of the rebasing of the national account statistics to 2015 from 2007. The published data indicate nominal GDP about 10 percent higher than previous estimates, which reflected a more accurate measure of the services sector.

14. The projected medium and long-term real GDP growth is expected to be lower compared to the last published DSA (IMF Country Report No. 20/297) (Text table 3). Real GDP growth contracted by 14.8 percent in 2020 due to the impact of the COVID19 pandemic. Economic growth is estimated to have rebounded to 7 percent in 2021. It is projected to increase by 4 percent in 2022 (revised downwards from 6 percent due to the impact of the Ukraine war) and thereafter gradually stabilize around potential to reflect the more gradual recovery of lost output from the pandemic (Text Table 3). Relatively subdued near term economic growth is expected to be followed by more robust economic activity over the medium term supported by recovery of the tourism sector as the impact of the pandemic gradually wanes; and as the vaccine coverage provides confidence of Cabo Verde's ability to exit the pandemic.

15. Medium- and long-term growth will be supported by the successful implementation of structural reforms aimed at improving public sector efficiency, the business environment, and increasing access to finance. The authorities are developing a new five-year development strategy based on the recently completed long-term development plan (Cabo Verde Ambition 2030). Priority areas include (i) completing SOE reforms, including through privatization and improving the efficiency of public enterprises; (ii) promoting diversification by leveraging the potential of the blue economy; (iii) reducing informality; and (iv) facilitating access to finance, particularly for small and medium-sized enterprises. The implementation of key reforms will be supported through TA and investment from the World Bank and under the new ECF arrangement.

Text Table 3. Cabo Verde: Assumptions for Key Economic Indicators, 2022–42

	2022 Proj.	2023 Proj.	2024 Proj.	2025 Proj.	2026 Proj.	2027 - 31 Proj.	2032 - 42 Proj.
Real GDP growth							
Current DSA	4.0	4.8	5.7	5.5	5.0	4.5	4.5
2020 2nd PCI Review	4.8	5.7	6.0	6.2	5.5	5.5	5.5
GDP Deflator							
Current DSA	4.5	2.6	2.0	2.0	2.0	2.0	2.0
2020 2nd PCI Review	1.4	1.5	1.6	1.7	1.8	1.8	2.0
Fiscal balance (including grants)							
Current DSA	-6.3	-5.6	-4.0	-2.1	-0.9	-1.1	-2.9
2020 2nd PCI Review	-3.7	-1.8	-0.8	0.0	-0.2	0.1	0.3
Overall financing needs (including onlending)							
Current DSA	-7.0	-6.1	-4.1	-2.3	-1.1	-1.1	-2.9
2020 2nd PCI Review	-3.9	-2.0	-1.0	-0.2	-0.2	0.1	0.3
Current account balance (including grants)							
Current DSA	-14.1	-6.2	-5.9	-4.7	-4.6	-3.8	-3.4
2020 2nd PCI Review	-6.4	-4.1	-2.1	-1.8	-1.4	-0.9	-0.9
Total Debt/GDP Ratio							
Current DSA	145.9	139.7	132.5	124.0	116.2	98.9	76.1
2020 2nd PCI Review	130.0	122.8	114.9	106.3	98.9	79.4	46.1
Cv$/USD exchange rate (e-o-y)							
Current DSA	98.5	96.9	95.8	95.0	94.5	94.2	94.2
2020 2nd PCI Review	93.1	93.0	93.0	93.1	93.1	93.1	93.1

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

- *Real GDP growth*. Cabo Verde's real GDP growth rate is projected at 4 percent in 2022 and 4.8 percent in 2023. Real output is projected to converge to the pre pandemic level in 2024 and the growth rate is projected to decline to about 5 percent through 2027. Over the long run, real GDP growth is projected to stabilize at 4.5 percent.[9]

- *Tourism services*. The framework assumes an initial gradual rebound of the tourism sector to reach the pre pandemic level by 2029. The impact of the Russia Ukraine crisis is likely to dent the pace of the near term rebound. However, recent increases in hotel capacity linked to the opening of new hotels will support a sustained increase in tourism arrivals over the medium to longer term.

- *Inflation*. Inflation is projected to increase to 6.5 percent in 2022 in line with the recent uptick in fuel and commodity prices, due to the impact of the Russia-Ukraine crisis. For the remainder of the projection period, inflation is expected to gradually decline to reach 2 percent by 2024 in line with euro area forecast.

- *Public sector deficit*. The current framework is predicated on a slightly more delayed but still ambitious and steadfast fiscal consolidation path. The overall fiscal deficit is estimated to have improved slightly from 9.1 percent of GDP in 2020 to 7.3 percent of GDP in 2021 and is projected to improve further to 6.3 percent of GDP in 2022. The fiscal position is projected to gradually improve to a surplus of about 1 percent of GDP in 2027. The fiscal effort in the near and medium term is assumed to be underpinned by strengthened domestic revenue mobilization and expenditure restraint with an unwinding of COVID-19 related expenditures. Several revenue measures, such as invoicing electronically at least 50 percent of taxpayers for VAT, the increase in tobacco tax, and the concession of the airport management company, are expected to bolster revenue collections. Fiscal adjustment will be implemented with safeguards to protect and broaden support for the vulnerable. The projected improvement in the primary balance from a deficit of -5.1 percent of GDP in 2021 to a surplus of about 1 percent of GDP by 2026, combined with a reduction in government financial support to SOEs reflecting continuous reform efforts would bring total financing to about 1.2 percent of GDP by 2026.

- *Current account deficit*. Compared to the previous DSA, the external current account deficit is projected to be above 3 percent of GDP from 2022-2026. The baseline scenario assumes a current account deficit of 14.1 percent in 2022 and 6.2 percent in 2023. This reflects the protracted impact of the pandemic, the impact of higher fuel and commodity prices, as well as the significant ongoing investments in the tourism sector. The current account deficit is projected to decline to about 4.2 percent of GDP in 2027 supported by continued strong recovery in the tourism sector and steady growth in remittances. Strong export performance and increased remittances, together with higher FDI inflows and IMF financing under ECF would help sustain international reserves at about 5 months of prospective imports.

[9] The long term historical average growth rate (1980-2000) was 4.7 percent and 5.2 percent if 2020 is excluded, while the five-year pre-pandemic average growth rate stood at 4 percent.

16. The DSA assumes a financing mix consistent with a prudent borrowing strategy, emphasizing external financing on concessional terms, in the near term with the share of domestic debt remaining broadly stable at about 30 percent. Financing for the revised 2022 budget will be filled mostly with grants and concessional and semi-concessional loans, mainly from multilateral institutions including the World Bank, African Development Bank, other bilateral partners, and draw-down of the recent SDR allocation. Multilateral and bilateral funding for budget support of US$43.8 million 2.2 percent of GDP is expected to be provided during 2022. The DSA is premised on continued concessional foreign support in the short and medium term but assumes a very gradual move toward lower concessional resources in the long term, including semi-concessional loans (with a grant element of less than 35 percent) and limited non-concessional borrowing, consistent with Cabo Verde's middle-income status. The domestic debt profile assumes bonds issuance with maturities of at least 4 years that would account for 96 percent of the stock in the medium term, in line with the profile of domestic debt portfolio at end-2021. 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. These projections are subject to risks associated with a tightening of monetary policy to contain inflationary pressures that could affect the entire yield curve. Finally, the authorities have drawn down the US$32 million (1.5 percent of GDP) of the recent SDR allocations to finance the 2022 and 2023 budget.

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

- The realism tools indicate that the fiscal adjustment path is ambitious, but staff are of the view that it is achievable through a combination of measures including strengthening of domestic revenue mobilization, expenditure restraint and the unwinding of COVID-19 related expenditures from 1.8 percent of GDP in 2021 to 1.6 percent of GDP in 2022. The proposed primary balance adjustment path of about 3.6 percent of GDP over 2022-2024 is in the top quartile of the historical distribution for LICs. However, the authorities have identified several policy measures which they estimate could increase revenue collections by close to 1 percent of GDP (detailed in the ECF request). The frontloading of policy measures provides a strong basis for the central government to achieve its goal of reducing the fiscal deficit to 4 percent of GDP by 2024. The adjustment will be supported by relatively robust near-term growth that are above the pre-pandemic historical average as the framework anticipates a steady and strong rebound from the COVID-19 pandemic. The DSA's realism tools do not signal any other signs of over-optimism in terms of large changes to investment or contributions to growth compared to previous DSAs (Figure 4). Tools for assessing the realism of the baseline scenario do not flag significant and systematic deviations from historical experience.

- Drivers of debt dynamics (Figure 3). The contributions of past and projected debt-creating flows to PPG external and overall debt dynamics differ. Interest rates are expected to contribute positively to PPG external debt accumulation, consistent with the historical experience, while price and exchange rate changes are projected to exert downward pressure on debt accumulation also in line with the historical experience. For total public debt, the projected contribution of real GDP growth to public debt reduction is significantly higher compared to the historical five-year change, reflecting higher forecasted near- term growth rebound from the effects of COIVD-19. Continued fiscal consolidation efforts and restructuring of SOEs will limit the contribution of the primary deficit to public debt accumulation relative to what the past five years would suggest. Unexpected changes in the current account/prices and exchange rates were the main drivers of past forecast errors of debt dynamics.

- Consistency between fiscal adjustment and growth (Figure 4). The projected growth path for 2022 and 2023 is in line with the multiplier-based projections. The realism of the expected adjustment is predicated on the authorities' commitment to further fiscal consolidation and restructuring of SOEs. It is also underpinned by initial strong rebound in economic activity from the effects of the pandemic, on account of strong activity in the tourism and transportation sectors. In addition, additional growth impetus is expected from reforms aimed at transforming Cabo Verde into an air and maritime transportation hub in the medium term, under the strategic plan for sustainable development (PEDS).

- 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 in line with the substantial import content of capital spending. Public investment is expected to hover around 4 percent of GDP in the medium term broadly similar to the previous DSA, while private investment is expected to remain at about 40 percent of GDP on average over 2022-26.

C. Country Classification and Determination of Stress Test Scenarios

18. Cabo Verde's debt-carrying capacity is assessed as "strong" as in the October 2020 DSA for second review of the PCI (Text Table 4). The debt-carrying capacity is determined by the composite indicator (CI) combining the World Bank Country Policy and Institutional Assessment (CPIA), external conditions captured by world economic growth and country-specific factors. The methodology is based on the data from the October 2021 World Economic Outlook (WEO) vintage and the 2020 CPIA, the CI score for Cabo Verde stands at 3.23, which is slightly above the threshold of 3.05 applicable for a "strong" rating. The CI score reflects positive contributions from the CPIA (45 percent), international reserves (32 percent), world growth (13 percent), remittances (7 percent) and country real growth rate (3 percent) that are all broadly in line with the last DSA. Debt burden thresholds associated with the strong debt carrying capacity under the framework are summarized in Text Table 5.

Text Table 4. 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	3.776	1.45	45%
Real growth rate (in percent)	2.719	4.119	0.11	3%
Import coverage of reserves (in percent)	4.052	53.614	2.17	67%
Import coverage of reserves^2 (in percent)	-3.990	28.745	-1.15	-35%
Remittances (in percent)	2.022	10.705	0.22	7%
World economic growth (in percent)	13.520	3.137	0.42	13%
CI Score			3.23	100%
CI rating			Strong	

Text Table 5. 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

DEBT SUSTAINABILITY ANALYSIS

19. **The debt sustainability analysis relies, in addition to the baseline projections 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 incomplete coverage of public sector debt as explained in paragraph 2. None of the tailored stress tests is triggered for Cabo Verde.

A. External Public Debt

20. **Under the baseline scenario, the PV of PPG external debt-to-GDP ratio breaches its threshold only in 2022 and lies below the threshold for the rest of projection period (Figure 1, Tables 2 and 4)**. The breach under the baseline is of shorter duration compared to the last DSA due to the GDP rebasing. The risk of external debt is assessed as moderate, an improvement relative to the last DSA which was assessed as high risk of external debt distress. The other external debt burden indicators remain comfortably below their prescribed thresholds under the baseline scenario throughout the DSA horizon. The PV of PPG external debt ratios to GDP and exports are expected to steadily decrease over time. Both debt service-to-exports and debt service-to-revenue ratios display similar patterns, peaking in 2022 for the former and 2023 for the latter as Cabo Verde commence

repayment of the principal on loans from the Portuguese bank Caixa Geral de Depósitos (CGD), and decreasing gradually thereafter.

21. The PV of PPG external debt-to-GDP ratio also breaches its threshold for an extended period under the stress test scenarios (Figure 1, Tables 2 and 4). Under the most extreme shock, to exports, it rises to just under 80 percent in 2024 before gradually decreasing but remains above the threshold of 55 percent of GDP up to 2032. The threshold is also breached under the remaining five standardized bound tests, albeit to different extents, and under the tailored combined contingent liabilities test from 2022-2031.

22. The PV of PPG external debt-to-exports ratio and debt service to export ratio exceeds the respective thresholds from 2023-2032 under the export stress test. The projected trajectories of PPG external debt burden indicators appear vulnerable to export and growth shocks and to a one-time depreciation shock, highlighting the potential adverse impact of Cabo Verde's exposure to adverse shocks due to the high concentration of economic and export activity in the tourism sector.

B. Total Public Debt

23. The PV of total public debt-to-GDP ratio exceeds the 70 percent benchmark through 2028 under the baseline scenario (Figure 2, Tables 3 and 5). The prescribed benchmark is also breached up to 2029 under the six standardized bound tests and the tailored combined contingent liabilities test, with the combined contingent liabilities shock being the most severe. Furthermore, the debt outlook, as shown by the other public DSA indicators, is particularly vulnerable to growth shocks and to contingent liabilities associated with SOEs' debt which emerge as the most extreme shock.

C. Risk Ratings and Vulnerabilities

24. Cabo Verde's DSA is classified at "moderate" risk of external debt distress. The PV of PPG external debt-to-GDP ratio breaches its threshold in 2022 under the baseline scenario, thereby signaling a moderate risk of external debt distress and is particularly sensitive to export and growth shocks. However, it is projected to decline below the 55 percent threshold from 2023 onwards. The external debt service to revenue indicator is sensitive to a one-time depreciation that would result in an initial spike in the ratio.

25. Cabo Verde's overall public debt is sustainable but remains at high risk of debt distress. The present value of public debt to GDP remains above its threshold under the baseline scenario through to 2028, suggesting a high risk of debt distress. Debt service is projected to average about 43 percent of revenues over the next five years, which represents a large share of future fiscal revenues. Stress tests indicate that Cabo Verde is most vulnerable to a growth shock. Under such a shock, all three public debt indicators would be set on an explosive path. The risk of debt distress is partly mitigated by support from Portugal, the main bilateral creditor.

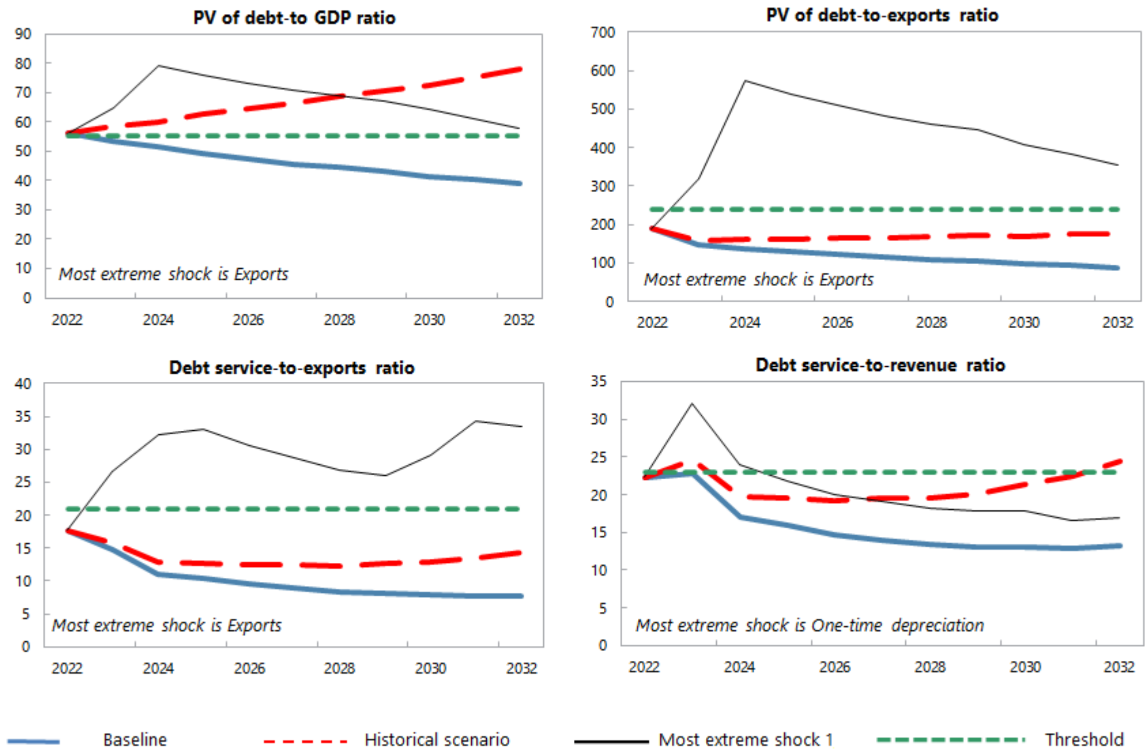
26. Heightened uncertainty over the global economic outlook suggests the need for a prudent approach that emphasizes macroeconomic stability, particularly fiscal discipline. High debt levels reduce the space for public expenditures in support of a robust and inclusive economic recovery. The authorities should prioritize further efforts to mobilize additional revenues and continue the strategy of only incurring concessional borrowing.

27. There are significant risks to the assessment. The outlook depends primarily on how quickly the COVID-19 pandemic is contained domestically and globally and Cabo Verde's ability to withstand the effects of the Ukraine war. Likewise, higher oil prices and continued supply chain disruptions could hinder the economic recovery. However, Cabo Verde's impressive and strong commitment to good governance and transparency, coupled with a very successful vaccination campaign, should allow a gradual resumption of activity in the tourism sector. Medium to long-term debt sustainability would be supported by focused implementation of growth-enhancing structural reforms, particularly actions to reduce fiscal risk from SOEs and address critical infrastructure gaps. Measures to develop the government securities market and lower the costs of domestic borrowing will be also crucial going forward.

D. Authorities' Views

28. The authorities agreed with the results of the DSA, and highlighted the challenges associated with reducing the debt stock given the frequency and magnitude of external shocks. The COVID-19 pandemic severely disrupted the planned fiscal consolidation path which would have resulted in a sharp decline in the debt stock. The pandemic exposed the structural challenges facing the economy, including heavy dependence on tourism, and vulnerability to exogenous shocks, which has been further magnified by the spillover effects of the Ukraine war and the ongoing drought. They indicated that the already limited fiscal space was exhausted by the health crisis, with the need to introduce measures to support the economy. They highlighted the impact of the recent increases in food and fuel prices triggered by the war in Ukraine on the vulnerable and which requires further interventions to mitigate the impact. The authorities however, reaffirmed their continued commitment to fiscal consolidation to preserve debt sustainability and reduce the risk of overall debt distress. In that regard they noted that the policies agreed under the new Extended Credit Facility and continued support from other developments partners, notably the World Bank is critical for the success of the economic reform agenda. They highlighted the high uncertainties of macroeconomic assumptions particularly with the Ukraine war and welcome more direct Fund engagement on the available policy options. 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 over the long term.

Figure 1. Cabo Verde: Indicators of Public and Publicly Guaranteed External Debt under Alternatives Scenarios, 2022–32



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	1.9%	1.9%
USD Discount rate	5.0%	5.0%
Avg. maturity (incl. grace period)	21	21
Avg. grace period	6	6

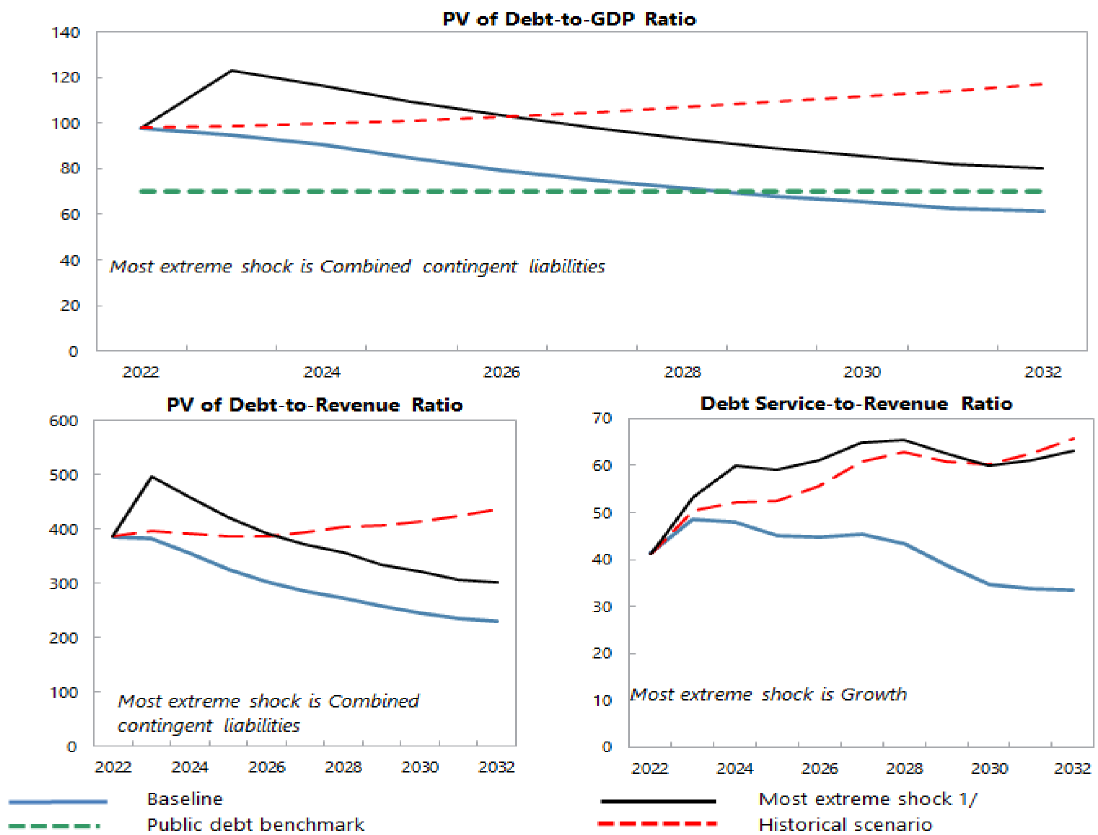
* Note: All the additional financing needs generated by the shocks under the stress tests are assumed to be covered by PPG external MLT debt in the external DSA. Default terms of marginal debt are based on baseline 10-year projections.

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 2032. 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, 2022–32



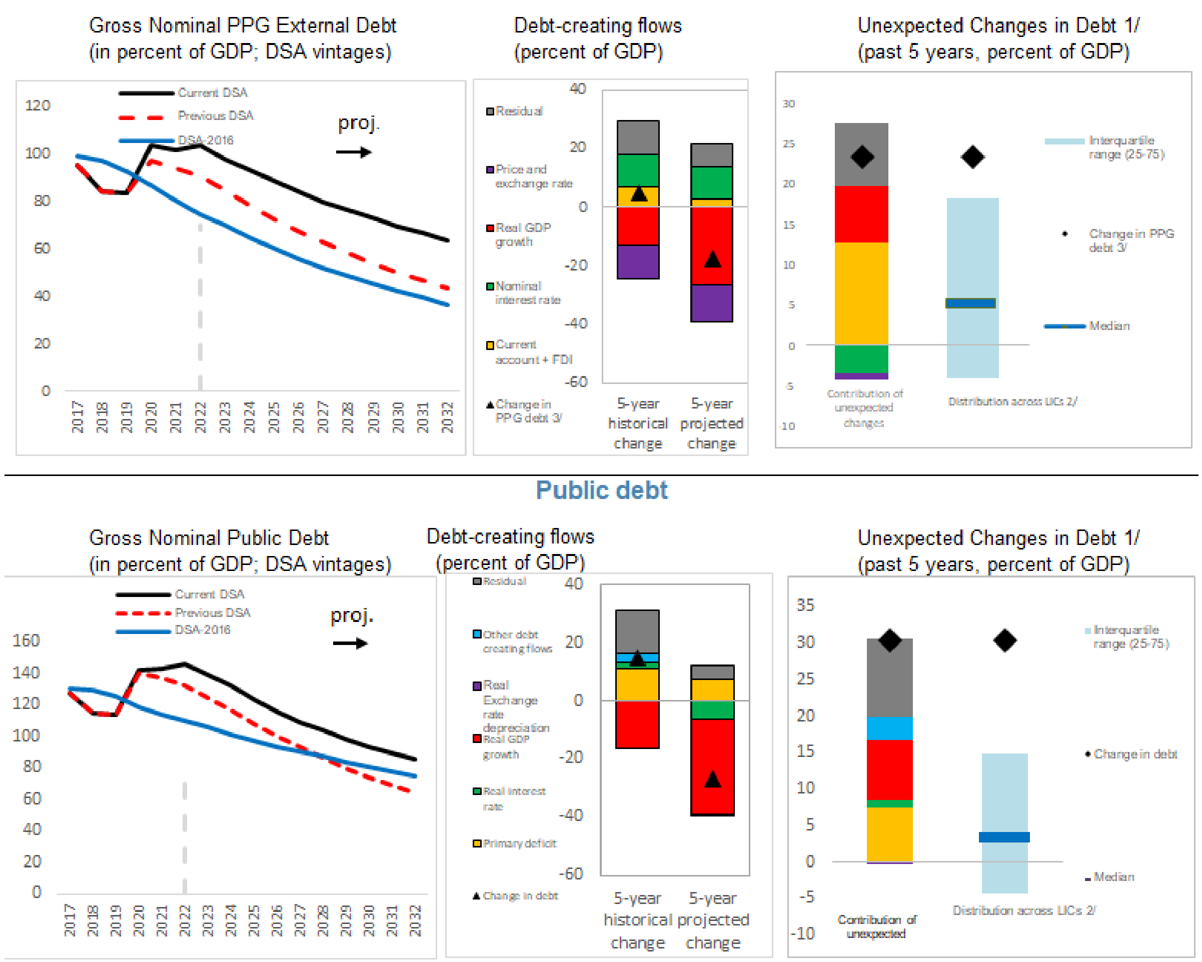
Borrowing Assumptions for Stress Tests*	Default	User defined
Shares of marginal debt		
External PPG medium and long-term	44%	44%
Domestic medium and long-term	55%	55%
Domestic short-term	1%	1%
Terms of marginal debt		
External MLT debt		
Avg. nominal interest rate on new borrowing in USD	1.9%	1.9%
Avg. maturity (incl. grace period)	21	21
Avg. grace period	6	6
Domestic MLT debt		
Avg. real interest rate on new borrowing	2.9%	2.9%
Avg. maturity (incl. grace period)	6	6
Avg. grace period	0	0
Domestic short-term debt		
Avg. real interest rate	-1%	-1.0%

* 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 2032. 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.

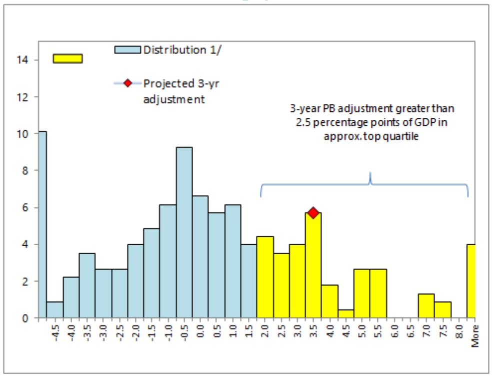
1/ Difference between anticipated and actual contributions on debt ratios.

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.

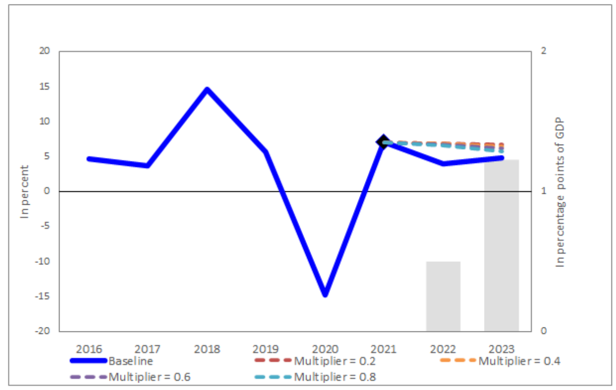
Figure 4. Cabo Verde: Realism Tools

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



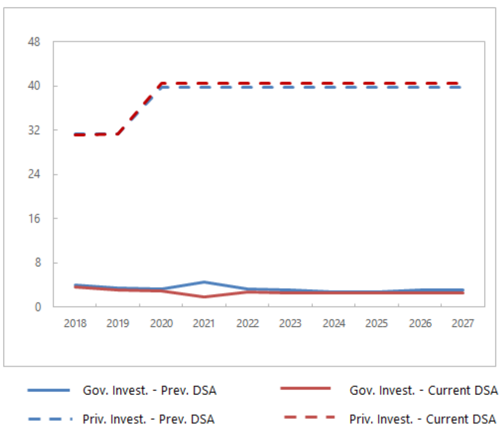
1/ Data cover Fund-supported programs for LICs (excluding emergency financing) approved since 1990. The size of 3-year adjustment from program inception is found on the horizontal axis; the percent of sample is found on the vertical axis.

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)



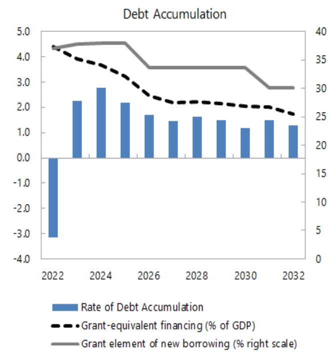
Contribution to Real GDP growth
(percent, 5-year average)

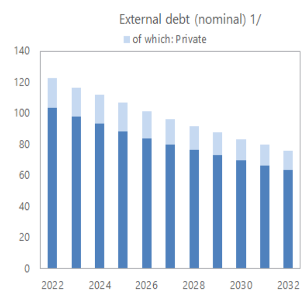
Table 2. Cabo Verde: External Debt Sustainability Framework, Baseline Scenario, 2021–42

(Percent of GDP, unless otherwise indicated)

	Actual	Projections								Average 8/	
	2021	2022	2023	2024	2025	2026	2027	2032	2042	Historical	Projections
External debt (nominal) 1/	119.4	122.4	116.6	111.7	106.8	101.1	96.0	75.7	40.5	103.9	97.5
of which: public and publicly guaranteed (PPG)	101.5	103.6	97.7	93.1	88.4	83.7	79.6	63.5	40.5	89.7	81.3
Change in external debt	-4.0	2.9	-5.8	-4.8	-4.9	-5.7	-5.1	-3.8	-3.3		
Identified net debt-creating flows	-6.3	5.6	-4.5	-4.1	-5.4	-4.5	-3.1	-3.2	0.1	1.0	-2.9
Non-interest current account deficit	8.8	11.7	3.6	3.8	2.6	2.6	2.2	1.3	2.8	4.9	3.2
Deficit in balance of goods and services	26.0	28.3	20.4	19.0	17.7	17.1	16.0	12.7	11.9	19.9	17.1
Exports	29.0	29.7	36.6	37.7	38.4	39.1	40.1	44.2	50.8		
Imports	55.0	57.9	57.0	56.7	56.1	56.2	56.1	56.9	62.7		
Net current transfers (negative = inflow)	-18.0	-16.6	-16.8	-15.9	-15.7	-15.2	-14.4	-11.9	-9.5	-16.0	-14.4
of which: official	-2.9	-2.1	-1.9	-1.3	-1.1	-1.0	-0.9	-0.7	0.0		
Other current account flows (negative = net inflow)	0.9	0.1	0.0	0.7	0.7	0.6	0.6	0.5	0.3	1.0	0.5
Net FDI (negative = inflow)	-3.5	-3.8	-5.3	-3.9	-4.4	-4.1	-3.1	-3.0	-2.3	-4.9	-3.6
Endogenous debt dynamics 2/	-11.7	-2.3	-2.8	-4.0	-3.6	-2.9	-2.2	-1.5	-0.3		
Contribution from nominal interest rate	2.4	2.4	2.5	2.1	2.1	2.0	2.0	1.9	1.5		
Contribution from real GDP growth	-7.7	-4.7	-5.3	-6.1	-5.7	-5.0	-4.3	-3.4	-1.9		
Contribution from price and exchange rate changes	-6.5	...	...	...	...	...	...	...	...		
Residual 3/	2.3	-2.6	-1.3	-0.7	0.5	-1.3	-1.9	-0.6	-3.4	4.1	-1.1
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	60.3	55.9	53.4	51.4	49.3	47.3	45.6	38.9	25.7		
PV of PPG external debt-to-exports ratio	208.1	188.4	145.7	136.3	128.4	121.0	113.7	88.1	50.6		
PPG debt service-to-exports ratio	13.4	17.7	14.7	11.0	10.3	9.5	8.9	7.8	5.5		
PPG debt service-to-revenue ratio	18.9	22.3	22.9	17.1	15.9	14.6	14.0	13.2	10.4		
Gross external financing need (Million of U.S. dollars)	227.7	314.1	119.5	137.4	97.1	103.8	127.1	125.1	348.3		
Key macroeconomic assumptions											
Real GDP growth (in percent)	7.0	4.0	4.8	5.7	5.5	5.0	4.5	4.5	4.5	2.4	4.7
GDP deflator in US dollar terms (change in percent)	5.5	-1.6	4.1	3.4	3.0	2.7	2.3	2.0	1.9	-0.7	2.2
Effective interest rate (percent) 4/	2.2	2.0	2.3	2.0	2.0	2.1	2.1	2.5	3.7	2.5	2.2
Growth of exports of G&S (US dollar terms, in percent)	44.5	4.7	34.5	12.5	10.7	9.8	9.7	8.5	8.6	1.9	11.4
Growth of imports of G&S (US dollar terms, in percent)	15.1	7.8	7.3	8.6	7.4	8.1	6.8	7.6	7.7	-0.5	7.3
Grant element of new public sector borrowing (in percent)	...	37.1	37.8	37.9	37.9	33.6	33.6	30.0	30.1	...	34.4
Government revenues (excluding grants, in percent of GDP)	20.6	23.5	23.6	24.4	24.9	25.4	25.7	26.0	26.9	22.8	25.1
Aid flows (in Million of US dollars) 5/	174.2	188.9	197.9	204.3	191.0	151.2	144.6	161.9	274.5		
Grant-equivalent financing (in percent of GDP) 6/	...	4.4	3.9	3.7	3.2	2.4	2.2	1.7	1.6	...	2.7
Grant-equivalent financing (in percent of external financing) 6/	...	50.5	46.7	46.5	47.1	44.7	44.7	39.2	40.3	...	45.1
Nominal GDP (Million of US dollars)	2,112	2,161	2,356	2,574	2,796	3,015	3,224	4,447	8,424		
Nominal dollar GDP growth	12.9	2.3	9.0	9.3	8.6	7.8	7.0	6.6	6.4	1.8	7.0
Memorandum items:											
PV of external debt 7/	78.3	74.7	72.2	70.0	67.7	64.7	62.1	51.2	25.7		
In percent of exports	269.9	251.6	197.1	185.7	176.3	165.4	154.8	115.8	50.6		
Total external debt service-to-exports ratio	18.6	22.4	18.5	14.6	13.7	12.8	12.1	10.2	7.2		
PV of PPG external debt (in Million of US dollars)	1274.7	1208.5	1257.2	1322.3	1378.6	1426.6	1470.1	1729.8	2168.9		
(PVt-PVt-1)/GDPt-1 (in percent)		-3.1	2.3	2.8	2.2	1.7	1.4	1.3	-0.9		
Non-interest current account deficit that stabilizes debt ratio	12.9	8.8	9.4	8.6	7.5	8.3	7.2	5.1	6.1		

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.

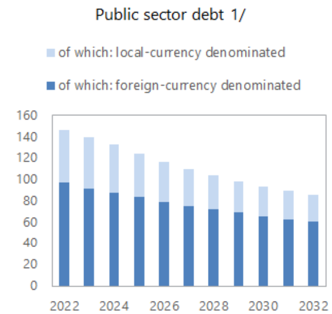
8/ Historical averages are generally derived over the past 10 years, subject to data availability, whereas projections averages are over the first year of projection and the next 10 years.

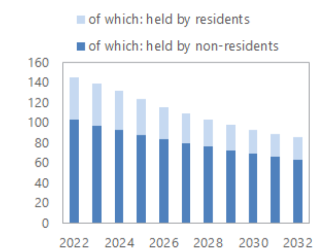
Table 3. Cabo Verde: Public Sector Debt Sustainability Framework, Baseline Scenario, 2021–42

(Percent of GDP, unless otherwise indicated)

	Actual	Projections								Average 6/	
	2021	2022	2023	2024	2025	2026	2027	2032	2042	Historical	Projections
Public sector debt 1/	**143.0**	**145.9**	**139.7**	**132.5**	**124.0**	**116.2**	**109.5**	**86.0**	**66.1**	**120.6**	**112.6**
of which: external debt	**101.5**	**103.6**	**97.7**	**93.1**	**88.4**	**83.7**	**79.6**	**63.5**	**40.5**	**89.7**	**81.3**
Change in public sector debt	0.4	2.9	-6.1	-7.2	-8.5	-7.8	-6.6	-3.2	-2.7		
Identified debt-creating flows	**2.3**	**-3.6**	**-5.4**	**-6.9**	**-8.3**	**-7.6**	**-6.5**	**-3.0**	**-0.9**	**4.8**	**-5.5**
Primary deficit	**4.8**	**4.3**	**3.1**	**1.2**	**-0.5**	**-1.0**	**-1.0**	**0.8**	**1.6**	**3.6**	**0.5**
Revenue and grants	22.6	25.4	24.8	25.5	25.9	26.3	26.5	26.5	27.5	**25.4**	**26.1**
of which: grants	2.0	1.9	1.2	1.1	1.0	0.9	0.8	0.6	0.6		
Primary (noninterest) expenditure	27.5	29.7	27.9	26.7	25.5	25.3	25.5	27.3	29.1	**29.0**	**26.6**
Automatic debt dynamics	**-1.7**	**-8.0**	**-8.5**	**-8.1**	**-7.9**	**-6.6**	**-5.4**	**-3.8**	**-2.5**		
Contribution from interest rate/growth differential	-11.2	-10.7	-7.4	-7.5	-7.2	-6.1	-5.2	-3.8	-2.5		
of which: contribution from average real interest rate	-1.9	-5.2	-0.8	0.0	-0.3	-0.2	-0.2	0.1	0.4		
of which: contribution from real GDP growth	-9.3	-5.5	-6.6	-7.5	-6.9	-5.9	-5.0	-3.8	-3.0		
Contribution from real exchange rate depreciation	9.5	...	...	...	...	...	...	...	...		
Other identified debt-creating flows	**-0.9**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.7**	**0.0**
Privatization receipts (negative)	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		
Debt relief (HIPC and other)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Other debt creating or reducing flow (please specify)	-0.9	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Residual	**-1.9**	**9.2**	**-1.9**	**-0.9**	**-0.9**	**-0.6**	**-0.5**	**-0.2**	**-1.8**	**1.7**	**0.3**
Sustainability indicators											
PV of public debt-to-GDP ratio 2/	**104.7**	**97.9**	**95.0**	**90.5**	**84.7**	**79.6**	**75.5**	**61.4**	**51.3**		
PV of public debt-to-revenue and grants ratio	**462.6**	**385.8**	**383.2**	**355.1**	**326.4**	**302.3**	**285.1**	**231.4**	**186.3**		
Debt service-to-revenue and grants ratio 3/	**41.0**	**41.3**	**48.5**	**48.0**	**45.1**	**44.6**	**45.5**	**33.5**	**32.2**		
Gross financing need 4/	14.1	14.6	14.7	13.4	11.2	10.7	11.0	9.6	10.5		
Key macroeconomic and fiscal assumptions											
Real GDP growth (in percent)	7.0	4.0	4.8	5.7	5.5	5.0	4.5	4.5	4.5	**2.4**	**4.7**
Average nominal interest rate on external debt (in percent)	1.0	1.0	1.2	0.9	0.9	0.9	1.0	1.2	1.6	**1.2**	**1.1**
Average real interest rate on domestic debt (in percent)	2.8	-0.4	1.9	3.0	1.4	1.5	1.6	2.0	2.3	**4.5**	**1.7**
Real exchange rate depreciation (in percent, + indicates depreciation)	10.2	...	...	...	...	...	...	...	...	**2.8**	**...**
Inflation rate (GDP deflator, in percent)	1.8	4.5	2.6	2.0	2.0	2.0	2.0	2.0	1.9	**0.7**	**2.3**
Growth of real primary spending (deflated by GDP deflator, in percent	-5.2	12.5	-1.7	1.1	0.8	4.3	5.1	7.4	3.0	**0.9**	**4.7**
Primary deficit that stabilizes the debt-to-GDP ratio 5/	4.5	1.5	9.3	8.4	8.1	6.8	5.6	4.0	4.3	**-5.9**	**5.6**
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		

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/ 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 4. Cabo Verde: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt 2022–32

(Percent)

	Projections										
	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032
PV of debt-to GDP ratio											
Baseline	56	53	51	49	47	46	44	43	41	40	39
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2022-2042 1/	56	58	60	63	65	66	69	70	73	75	78
B. Bound Tests											
B1. Real GDP growth	56	59	63	60	58	56	54	53	51	49	48
B2. Primary balance	56	55	55	53	51	50	49	47	46	45	43
B3. Exports	56	65	79	76	73	71	69	67	64	61	58
B4. Other flows 2/	56	56	56	54	51	50	48	47	45	43	42
B6. One-time 30 percent nominal depreciation	56	75	67	64	61	59	57	56	54	52	51
B6. Combination of B1-B5	56	69	71	69	66	64	62	60	57	55	53
C. Tailored Tests											
C1. Combined contingent liabilities	56	64	62	61	60	59	58	58	56	55	54
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	188	146	136	128	121	114	109	105	97	93	88
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2022-2042 1/	188	159	159	163	166	165	169	171	169	174	176
B. Bound Tests											
B1. Real GDP growth	188	146	136	128	121	114	109	105	97	93	88
B2. Primary balance	188	149	145	137	130	123	119	116	107	103	98
B3. Exports	188	320	572	539	509	480	462	445	408	382	355
B4. Other flows 2/	188	154	148	139	132	124	119	114	105	100	95
B6. One-time 30 percent nominal depreciation	188	146	126	119	112	105	101	97	89	86	82
B6. Combination of B1-B5	188	271	167	306	289	272	261	251	229	217	204
C. Tailored Tests											
C1. Combined contingent liabilities	188	174	165	158	152	146	143	141	132	128	123
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	18	15	11	10	10	9	8	8	8	8	8
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2022-2042 1/	18	16	13	13	13	12	12	13	13	13	14
B. Bound Tests											
B1. Real GDP growth	18	15	11	10	10	9	8	8	8	8	8
B2. Primary balance	18	15	11	11	10	9	9	8	8	8	8
B3. Exports	18	27	32	33	31	29	27	26	29	34	33
B4. Other flows 2/	18	15	11	11	10	9	9	8	8	8	8
B6. One-time 30 percent nominal depreciation	18	15	11	10	9	9	8	8	8	7	7
B6. Combination of B1-B5	18	22	23	21	20	19	17	17	19	19	19
C. Tailored Tests											
C1. Combined contingent liabilities	18	15	12	11	10	10	9	9	9	9	9
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	22	23	17	16	15	14	13	13	13	13	13
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2022-2042 1/	22	25	20	20	19	19	20	20	21	22	24
B. Bound Tests											
B1. Real GDP growth	22	25	21	19	18	17	16	16	16	16	16
B2. Primary balance	22	23	17	16	15	14	14	13	14	14	14
B3. Exports	22	23	18	19	17	16	16	15	18	21	21
B4. Other flows 2/	22	23	17	16	15	14	14	13	14	14	14
B6. One-time 30 percent nominal depreciation	22	32	24	22	20	19	18	18	18	17	17
B6. Combination of B1-B5	22	24	21	19	18	17	16	16	19	18	19
C. Tailored Tests											
C1. Combined contingent liabilities	22	23	18	17	16	15	15	14	14	14	15
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 5. Cabo Verde: Sensitivity Analysis for Key Indicators of Public Debt, 2022-32
(Percent)

	Projections										
	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032
PV of Debt-to-GDP Ratio											
Baseline	**98**	**95**	**91**	**85**	**80**	**75**	**72**	68	66	63	61
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2022-2042 1/	**98**	**99**	**100**	**101**	**103**	**105**	**107**	**109**	**112**	**114**	**117**
B. Bound Tests											
B1. Real GDP growth	**98**	**106**	**117**	**115**	**113**	**112**	**112**	**111**	**112**	**113**	**114**
B2. Primary balance	**98**	**98**	**98**	**92**	**86**	**82**	**78**	**74**	**71**	68	66
B3. Exports	**98**	**106**	**118**	**111**	**105**	**100**	**96**	**92**	**88**	**84**	**80**
B4. Other flows 2/	**98**	**98**	**95**	**89**	**84**	**79**	**76**	**72**	69	66	64
B6. One-time 30 percent nominal depreciation	**98**	**118**	**111**	**103**	**97**	**92**	**87**	**83**	**79**	**76**	**74**
B6. Combination of B1-B5	**98**	**102**	**106**	**100**	**96**	**93**	**90**	**87**	**85**	**82**	**81**
C. Tailored Tests											
C1. Combined contingent liabilities	**98**	**123**	**117**	**110**	**103**	**98**	**93**	**89**	**86**	**82**	**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	386	383	355	326	302	285	273	257	246	235	231
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2022-2042 1/	386	397	391	387	388	393	404	408	415	423	437
B. Bound Tests											
B1. Real GDP growth	386	427	456	438	425	420	422	416	417	419	429
B2. Primary balance	386	395	385	353	327	309	296	278	266	254	250
B3. Exports	386	429	463	428	400	380	366	347	331	313	302
B4. Other flows 2/	386	396	372	343	318	300	288	271	259	248	242
B6. One-time 30 percent nominal depreciation	386	476	435	397	367	346	331	311	297	284	279
B6. Combination of B1-B5	386	412	412	385	364	349	341	326	316	307	306
C. Tailored Tests											
C1. Combined contingent liabilities	386	496	458	422	392	371	356	335	321	308	302
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	41	49	48	45	45	45	43	39	35	34	33
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2022-2042 1/	41	51	52	52	56	61	63	61	60	63	66
B. Bound Tests											
B1. Real GDP growth	41	53	60	59	61	65	66	62	60	61	63
B2. Primary balance	41	49	50	50	49	50	49	44	39	38	37
B3. Exports	41	49	49	48	47	48	46	41	39	42	41
B4. Other flows 2/	41	49	48	46	45	46	44	39	36	35	35
B6. One-time 30 percent nominal depreciation	41	54	56	54	54	55	54	50	46	46	47
B6. Combination of B1-B5	41	51	54	53	54	56	56	52	49	49	49
C. Tailored Tests											
C1. Combined contingent liabilities	41	49	65	61	60	61	60	55	44	43	42
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 Mr. Afonso Bevilaqua, Executive Director for Cabo Verde|
and Mr. Ricardo Velloso and Ms. Carla Cruz,
Advisors to the Executive Director**

June 15, 2022

On behalf of our Cabo Verdean authorities, we thank the staff team lead by Mr. Segura-Ubiergo for the comprehensive and insightful report. The authorities are also very appreciative of staff's dedication and tireless efforts during these challenging times through both virtual and in-person interactions. The mission conducted in the country's capital, Praia, contributed to building an even closer and more constructive policy dialogue, benefiting from the proximity to the reality on the ground and the additional availability of Government officials and other stakeholders.

Despite the well-recognized success of the Government in fighting the pandemic, the country remains vulnerable to external shocks. Global uncertainties associated with the pandemic and its scars, amplified by the effects of the war in Ukraine, particularly on food and fuel prices, are weighing on the risks to the outlook of Cabo Verde, a small and open economy that is highly dependent on tourism and imports.

Against this background, the authorities seek support of the Executive Board for approval of a three-year Extended Credit Facility (ECF) arrangement in the amount of SDR 45.03 million (190 percent of quota). This arrangement will be instrumental in helping preserve macroeconomic and financial stability, maintain debt sustainability, and support the steadfast implementation of the country's structural reform agenda envisaged in the Government's Sustainable Development Strategic Plan (PEDS 2022-2026). The authorities are grateful for the successful conclusion of the program discussions with staff and timely consideration by the Executive Board of the ECF program request.

Background

Cabo Verde had engineered an impressive period of sustainable and inclusive growth prior to the onset of the pandemic crisis. The Government that took office in 2016 established an ambitious development program for the period 2017-2021, with the main objective of making Cabo Verde a hub economy in the mid-Atlantic. In 2019, the country celebrated the successful review of the Government's Sustainable Development Strategic Plan (PEDS 2017-2021). The economy was growing fast: at 5.7 percent in 2019 and close to 5 percent annual average in the period of 2016-2019. That strong performance was sustained by favorable macroeconomic conditions upheld by adequate monetary and financial policies that continued protecting the exchange rate peg to the euro and maintaining inflation low and stable, and a strong fiscal policy framework. Robust growth and fiscal consolidation implemented during that period put the public debt-to-GDP ratio on a clear declining trend.

Also, a comprehensive set of structural reforms were implemented, strengthening the investment climate, and improving economic diversification and inclusiveness with job creation and strong social outcomes.

In 2019, the authorities reinforced its engagement with the IMF by requesting an 18-month program under the Policy Coordination Instrument (PCI). At that time, there was no current or prospective balance of payments needs and, therefore, the PCI was the ideal instrument to strengthen the policy framework, signal the commitment to prudent policies and structural reforms, and catalyze external financing from other bilateral and multilateral development partners.

In 2020, however, the global pandemic hit particularly hard small island economies like Cabo Verde, interrupting the Government's ambitious reform agenda given the need to focus on protecting lives and livelihoods upended by the pandemic. The Government's COVID-19 response prioritized boosting the health system and protecting the most affected by the economic dislocation triggered by the global pandemic. Notwithstanding the Government's swift actions, the economy experienced a historical contraction by almost 15 percent in 2020.

The global pandemic created significant balance of payments needs, requiring the authorities to request in April 2020 financial support under the Rapid Credit Facility (RCF). This timely support, in the amount of SDR 23.7 million (100 percent of quota), was instrumental in helping the authorities to implement its COVID-19 response plan and reduce fiscal and external financing gaps. It also helped to catalyze additional financial support, including from the World Bank, the African Development Bank, and other development partners of Cabo Verde. It is important to highlight that the execution of COVID-19 related spending has strictly followed the Government's transparency and accountability practices. These include the daily publication on the Ministry of Finance website of all expenditures related to the pandemic fighting and, adhering to the public financial management guidelines, these expenditures are timely audited by the Court of Accounts.

A revised budget was approved in 2021 to better align spending priorities with the evolution of the pandemic and accelerate the vaccination campaign. As a result of the latter, as of May 22, 2022, approximately 98 percent of the target population were vaccinated with the first dose of the vaccine and 85 percent with two doses. Vaccines were mobilized with the support of several development partners, and a well-organized logistic system was put in place, allowing access to vaccines, including in the most remote areas given the archipelago geography of the country. The vaccination program in Cabo Verde is considered one of the most notable in sub-Saharan Africa.

Recent Economic Developments and Outlook

Thanks in no small part to the authorities' assertive pandemic response, a robust recovery is underway. According to the National Institute of Statistics (INE), real GDP increased by 13.2 percent in the fourth quarter of 2021 (compared to the same quarter of 2020) and 7 percent on average in 2021 mainly due to a rebound in consumption and exports. This recovery reflects the positive impact of the well-implemented vaccination program, which helped to boost confidence in Cabo Verde as a safe tourist destination. This is reflected in the sharp increase in tourist arrivals, particularly in the last months of last year, as well as the resumption of FDI in constructions related to the tourism sector. Also, strategic public investments have contributed to the recovery, namely in key areas such as digital (technologic parks), transport, and in the agriculture, water, and energy sectors to mitigate the impact of the prolonged droughts.

The war in Ukraine, however, poses additional risks to this otherwise positive outlook. On top of the uncertainties related to new variants of COVID-19, the war in Ukraine has amplified global inflationary pressures due to higher food and fuel prices. Given that Cabo Verde is highly dependent on imports of commodities and the recovery in tourism may be adversely affected by the global economy slowdown, the real GDP growth projection for Cabo Verde in 2022 was cautiously revised downward, from 6 percent to 4 percent.

Fiscal Policy

Fiscal performance in 2021 was better than expected and the authorities are firmly committed to gradual fiscal consolidation going forward. Public spending prioritization based on the focused execution of key selected public investment projects and rationalization of current expenditures contributed to improving the fiscal position last year. The performance of revenue collections, however, was still affected by the continued impact of the pandemic on consumption and corporate income. Also, support to taxpayers included tax deferrals, which eased their tax burden amid weak economic activity. However, with the recovery taking hold, the Government will implement revenue mobilization measures which, combined with further public spending rationalization, should contribute to steady primary fiscal balance improvements over time. Revenue measures include tax and customs administration improvements as well as the introduction of electronic invoicing, imposition of import duties on previously exempted goods, increasing excise taxes, and the implementation of the ECOWAS common external tariff.

Preserving public debt sustainability is one of the authorities' main priorities. The recent national account rebasing completed by INE, with IMF TA, pointed to an increase in nominal GDP by about 10 percent compared to previous estimates, leading to an important reduction in debt-to-GDP ratios. The authorities, nevertheless, recognize that Cabo Verde's debt remains elevated, contributing to the perception that the risk of debt distress is high. However, liquidity indicators remain comfortably below their respective sustainability thresholds under the baseline scenario, reflecting the high level of concessionality of external debt, as shown in the updated DSA. To continue ensuring public debt sustainability, the authorities will improve further the efficiency of the public investment framework and implement prudent borrowing policies, preferentially through concessional external financing. Also, strengthened debt management practices, including to enhance the government securities market, and discussions with selected creditors on voluntary debt service relief (such as debt conversions into catalytic investment projects) will be undertaken. In addition, the Government will continue to mitigate SOE related fiscal risks. In this regard, the privatization agenda should be resumed in the near-term, with the Cabo Verde Airlines (CVA) privatization process as priority.

Monetary and Financial Policies

Monetary policy will continue to support macroeconomic stability. An accommodative monetary policy stance in the context of the pandemic was needed to put a floor on the downturn and foster the recovery while protecting the peg of the Cabo Verdean escudo to the euro. While some support measures have been extended until June 2022 due to the external shock triggered by the war in Ukraine, the authorities are committed to phasing out these measures. The Central Bank of Cabo Verde (BCV) will monitor closely global and domestic developments and, if needed, corrective measures will be considered to further strengthen the monetary policy transmission mechanism. Despite the projected reduction in international reserves in 2022, they should remain in the recommended range of 5 months of prospective imports over the medium-term.

The BCV will remain vigilant to emerging risks to the banking sector while taking steps to modernize the financial system. With the expected end of the debt service moratorium in June 2022, the BCV is preparing to provide comprehensive guidance on the prudential treatment of the moratorium and NPL management strategies, also developing a framework for the resolution of health crisis related NPLs. The BCV continues to be committed to strengthening the regulatory and supervisory frameworks and ensuring a stable and well-capitalized banking system to safeguard financial stability. Additional measures include amending the BCV Law to strengthen the central bank's autonomy, accountability, and transparency, moving ahead with Basel II implementation, and improving monetary and financial sector statistics with help from IMF TA.

Structural Reforms

The authorities are engaged in a comprehensive agenda of structural reforms in support of faster, sustainable, and inclusive growth. Key priority areas and policies for the development of the country are identified in PEDS 2022-2026, which is aligned with "Cabo Verde Ambitions 2030" and the country's Sustainable Development Goals (SDGs). A key objective is to support business environment reforms by facilitating access to finance to micro, small, and medium-sized enterprises, improving the functioning of the labor market, easing legal procedures, cutting red tape, and expediting judicial processes. Attracting private sector investment not only to the already well-established tourism and transport sectors but also to other sectors of the digital, green, and blue economies, water and sanitation, and renewable energy is key to the future of Cabo Verde.

The Government also intends to create a macroeconomic stabilization fund considering Cabo Verde's high vulnerability and exposure to shocks. In addition to the severe impact of the pandemic and the war in Ukraine, Cabo Verde has been continuously affected by droughts since 2017. Building buffers to mitigate the effects of external and weather shocks, which are becoming more frequent due to climate change, will help to improve the resilience of the economy.

Social safety nets will be strengthened through improved targeting of social spending. Cabo Verde has an excellent track record of positive social outcomes, especially when compared with regional peers. However, poverty and unemployment remain high and will likely deteriorate with the rising price of essential goods and pandemic related scarring. Therefore, to protect the most vulnerable, the Government will strengthen and better target social programs, including the national income for inclusion program (RNI). In addition to reforming the national social security system, the Government will sign a pact for poverty reduction, which should be established with the partnership of key institutions and development partners, aiming to eliminate extreme poverty by 2026.

Conclusion

The authorities are fully committed to the IMF-supported program. They are confident that Fund support through the three-year ECF arrangement will help Cabo Verde to cover part of its financing needs, ensuring the continuation of the gradual economic recovery from the global pandemic despite the new external shock triggered by war in Ukraine, while preserving macroeconomic and financial stability and protecting the most vulnerable. The Fund program is also expected to provide support to the authorities' fiscal consolidation plan and debt sustainability goals, as well as the implementation of their structural reform agenda as envisaged in PEDS 2022-2026.